

Market Entry in Japan



Theory and Management
in a Turbulent Era

Ulrike Maria Haak and René Haak

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and

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List of Abbreviations and Acronyms

CNC	Computer Numerical Control
CPA	Certified Public Accountants
ESOP	Employee Share Ownership Program
EU	European Union
FANUC	Fujitsu Automatic Numerical Control
FDI	Foreign Direct Investment
FILP	Fiscal and Loan Program
FRI	Fujitsu Research Institute
FY	Fiscal Year
GATT	General Agreement on Tariffs and Trade
GDP	Gross Domestic Product
GNP	Gross National Product
HQ	Headquarters
HR	Human Resource
HRM	Human Resource Management
IMVP	International Motor Vehicle Program
IT	Information Technology
JETRO	Japan External Trade Organization
JMNC	Japanese Multinational Corporation
JPY	Japanese Yen
JUSE	Japanese Union of Scientists and Engineers
LDP	Liberal Democratic Party (Japan)
M&A	Mergers and Acquisitions
METI	Ministry of Economy, Trade and Industry (Japan)
MIC	Mobile Internet Centre
MIT	Massachusetts Institute of Technology
MITI	Ministry of International Trade and Industry (Japan)
MNC	Multinational Corporation
MNE	Multinational Enterprise
MOF	Ministry of Finance (Japan)
NC	Numerical Control
NGO	Non-Governmental Organization
NIE	Newly Industrializing Economy
NRI	Nomura Research Institute

OECD	Organization for Economic Cooperation and Development
OEM	Original Equipment Manufacturer
PDAC	Plan Do Check Act
POS	Point of Sales
PPP	Purchasing Power Parities
R&D	Research & Development
ROE	Return on Equity
SME	Small- and Medium-sized Enterprise
TPS	Toyota Production System
TQC	Total Quality Control
TQM	Total Quality Management
TRIM	Trade-Related Investment Measures
TRIPS	Trade-Related Aspects of Intellectual Property Rights
TSE	Tokyo Stock Exchange
UK	United Kingdom
UN	United Nations
UNCTAD	United Nations Conference on Trade and Development
US	United States
USA	United States of America
USD	US Dollar
WTO	World Trade Organization

About the Authors

Ulrike Maria Haak is an arts editor with the German television company ZDF/3sat and a journalist with special interests in the comparative study of different cultures, economics and the social sciences. She majored in Theatre, Film and Television Studies and German and Romance Studies at the Universities of Erlangen-Nuremberg, Lyon and Cologne. Since 1995, she has worked as an editor with the German television company ZDF for the culture channel 3sat, working on programmes such as “DENKmal” and “Bookmark – das Sachbuchmagazin” and is currently working in the editorial team for “Kulturzeit”. From September 1999 to October 2005 Ulrike Maria Haak worked as a foreign correspondent in Tokyo (for the newspapers *Die Zeit* and *Der Tagesspiegel* amongst others). She has produced numerous publications on intercultural and international management, particularly in the context of European–Asian relations.

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Introduction

1.1 Globalization of the markets

Globalization of the markets, of production and also of many services offers opportunities, but also presents risks to companies with international operations. Business activities became considerably more internationalized at the beginning of the 20th century; the process accelerated after the end of the Second World War resulting in a period of radical breakdown and far-reaching change in the international environment in the final two decades of the century. Business activity at the beginning of the new millennium is deeply marked by these changes (Haak and Tachiki 2004; Haak, U. and Haak, R. 2006).

Against the background of this development, it is important for international companies to develop future-proof strategies which not only safeguard the status quo of their market position and their competitiveness, but also allow them to become more competitive and penetrate new and promising markets (Perlitz 1997; Hungenberg 2002).

Consequently, no international company can now seriously afford to neglect the dynamic Asian economic region. In this respect, Japan in particular assumes a key position because the Japanese market is large and future-oriented and its consumers are wealthy and sophisticated. The Japanese market offers international companies attractive opportunities and locational benefits which play a crucial part in setting up a business or in engaging in other forms of economic activity.

1.2 Japan – the largest economy in Asia

With a gross domestic product (GDP) of 4.976.797 Mio. USD in 2008, Japan is by far the largest economy in Asia. Its share of the world market is currently around 11 per cent. This makes Japan the second largest economy in the world after the United States. Despite the high growth in other Asian countries, Japan's GDP continues to far exceed the economic power of these neighbouring countries. For example, the GDP of the Kanto region (Tokyo and the adjacent prefectures) is larger than that of the whole of China. The second most important economic region in Japan, the Kinki region with Osaka at its centre, generates a higher GDP than India (JETRO 2005a, p. 5).

Several affluent groups shape the image of Japanese consumer society. These include the "silver market" with older and free-spending consumers and young working people who, often unmarried and living at home with their parents, have considerable disposable income. There are market opportunities mainly in high-quality consumer goods and in IT and communications. However, the automotive sector and its supplying industries also present considerable opportunities in Japan. The supplier industry in this case also includes mechanical engineering, which as the key industry for many other sectors has a decisive impact on the productivity and innovative ability of an economy. Japan has a mature and modern mechanical engineering industry which is developing constantly through innovative processes.

However, other industrial nations like Germany, Italy and Switzerland also have an innovative mechanical engineering industry which can use the opportunities offered by the Japanese market. Overall, there is great growth potential for companies engaged in mechanical engineering on an international scale as the Japanese manufacturing industry is very keen on improving productivity. It is important that international companies include the Japanese market in their strategies from the point of view of not only consumer goods markets but also investment goods markets (mechanical engineering, chemistry and pharmaceuticals, raw materials) when assessing an approach to international market cultivation and penetration.

There is another important aspect of business involvement in one of the most demanding competitive environments in the Asian economic region which must also be mentioned in this context. Business

involvement in different Japanese markets not only creates growth potential for a company and therefore improves the profit situation long term; activity in a foreign and highly competitive market with sophisticated consumers and buyers also sharpens the company's own performance profile, which can then lead to exceptional performance. This improvement in performance opens up opportunities for market and technology leadership in less demanding and competitive markets.

Against the background of these various considerations, Japan deserves to be accorded special attention in the strategies of international companies which in recent years have neglected this economic heavyweight in their often blind enthusiasm for the Chinese market. The preparations for the Olympic Games and the media focus on China have boosted this development in recent years.

However, it should not be forgotten that Japan's share of global consumption amounts to around 20 per cent, with a population one-tenth that of China. Even if China and India continue to become more significant, Japan will remain in the world economy superleague. What is meant here by superleague? Japanese markets, Japanese technology and not least Japanese products and manufacturing technology set the standards in international business and its dominance of the emerging markets in the Asia-Pacific region is not insignificant.

Even though other countries in the Asia-Pacific region have followed suit and have started to close the gap very rapidly, it will be difficult for them to overtake Japan in the innovational core areas of industry. Development in many industry sectors and their key products takes evolutionary routes which cannot simply be copied and transferred. To draw level with Japan in product, process and innovation management requires more than just many years of high growth rates. It requires a tradition of innovation, which most aspiring industrial countries in Asia do not yet have. The power of an economy to innovate is rooted in its highly qualified people who are prepared to learn constantly both at and away from the workplace.

1.3 Specialists – a key role in market success

The recruitment of suitable specialist personnel plays an important part in the selection of a location in which to establish a foreign base.

Japan has a potential workforce of over 60 million. The high educational standards of the Japanese population are admired throughout the world. In 2003, the proportion of the population who had studied at university or a similar educational institution was 74.1 per cent (compare the United States with 60.4 per cent and Germany with 33.2 per cent).

At the time of the bubble economy and in the ensuing years, Japanese university graduates exhibited a clear preference to be employed by Japanese companies. As most blue- and white-collar workers remained with the same company throughout their lives, it was often difficult for foreign companies to attract suitable manpower. However, in the meantime, the situation has changed fundamentally. Pay and working conditions and not least foreign management role models like Carlos Ghosn have contributed to making non-Japanese companies more attractive as employers so that they are now also able to find highly qualified specialists and graduates to work for them.

These employees are not assembly workers, but the holders of expertise who develop their own brand concepts for the Japanese market. Localization of personnel and the consequent use of local knowledge for cultivating and penetrating the market are opportunities for international companies to combine the two aspects of "local trade" and "global thinking" which are often in opposition.

1.4 Innovative technologies

Japan's competitiveness is based largely on innovative technology and as such the Japanese government directly supports R & D. Total expenditure on R & D in Japan is around 3.2 per cent of GDP, which puts Japan ahead of every other industrial country, with many European countries lagging far behind. Even Germany together with France, Britain and Italy, the leading industrial and academic nations in Europe, cannot boast this proportion of GDP spent on R & D.

Japan also leads the world in the number of patent applications. Intellectual property enjoys long-term patent protection in Japan, which is crucial for both domestic and foreign suppliers of innovative technology. New laws are intended to ensure that in the future registration procedures for intellectual property rights are accelerated and disputes in this area are dealt with more quickly.

Japan has a dense road network, over 1000 ports, of which 133 are classified as being of particular importance for the national interest and foreign trade, and around 100 airports. The efficient rail network is famous throughout the world particularly for the high-speed *shinkansen* trains.

Because of its high gross national product, considerable spending power – Japanese GDP at USD 37 625 per capita exceeds that of the United States (2004) – and many globally first-class companies and research institutions, Japan will maintain its position as a leading economy even after the economies of other Asian nations have continued to grow.

With Japan currently in such good economic shape, we would do well to not forget that the process of modernization which formed the basis for its advancement to a world economy has only taken place over the last 160 years, after centuries of pursuing a policy of separation and isolation towards the rest of the world.

1.5 Economic boom and bust

The economic boom years up to the end of the 1980s ended with the bursting of the “bubble economy”. The prices of property and shares, which had been inflated by speculation, fell to previously unheard-of depths. In the years of recession that followed, Japanese companies, especially the complex and interwoven *keiretsu* organizations, were forced to undergo restructuring. Many of the loans that had been secured so generously with objects of speculation in the bubble years now appeared as unrepaid bad debt in account books and made a major contribution to the banking crisis in Japan.

However, since the end of the 1990s the restructuring measures have borne fruit. The *keiretsu* have become leaner and have divested themselves of most of the unprofitable branches. Many banks are in the process of writing off the bad debts and are returning to profitability. Japanese companies with high levels of debt but which are essentially competitive are being given the opportunity to function profitably again through debt-equity swaps, for example, and through the measures of the Industrial Revitalization Corporation of Japan (IRCJ), a kind of trust company which takes over their liabilities and develops rescue packages.

These structural changes have improved the chances of foreign companies gaining entry to the Japanese market or improving their market position. Investors in particular are profiting from the Japanese government's objective of increasing the amount of Foreign Direct Investment (FDI) substantially over the next few years.

As a consequence of the crisis in Asia the Japanese economy shrank in 1998 and 1999. In 2000 and 2001, Japanese GDP exhibited poor growth rates of 0.4 and 0.1 per cent; it was not until 2003 that the economy started to make a significant and lasting recovery. In the last three years, GDP growth has fluctuated between 2.5 and 3.0 per cent. Economic growth slowed in 2007.

1.6 Return to economic growth

Stock market experts are amazed by the strong dynamics of the economic recovery. The Nikkei index has climbed to astonishing heights. The stock market reveals a robust picture. A clear indication of the revival are real estate prices in Tokyo, which are picking up again after years of decline. Newly built urban complexes such as Roppongi Hills or Shiodome are attracting interest with their offices, restaurants, shops and hotels. Japanese consumers, in many areas trendsetters for global changes, are gratefully welcoming the new towns.

Consumer buying patterns – Development takes a new direction

It is now certain that Japan has succeeded in pursuing economic growth again. However, only core sectors of key industries have been included in the upturn. Nevertheless, there are unmistakeable signs of consumer buying patterns gradually changing in the Japanese markets.

In recent years, the polarization of society and the growing social divide have also become topics under discussion in Japan. Compared to countries like the United States and China, however, Japanese consumer demand is still influenced by around 100 million people with a pronounced awareness of their middle-class status. Two key trends have become apparent recently. Firstly, the proportion of quality-oriented consumers (for example, of organic products) is growing and, secondly, the number of price-conscious consumers is increasing steadily.

In other countries, it is often observed that where there is less buying power, only cheaper products are bought. In Japan it is much more the case that customer loyalty towards cheap products rises as satisfaction with the quality of the product rises. Therefore, anyone who believes that the key to the buying patterns of Japanese consumers in 2008 lies in the division of society is risking the failure of their marketing strategy.

Where the consumer group concentrating on cheap products is concerned, it should be recognized that since the mid-1990s, Japanese industry has been progressively undermined, as China and other Asian countries manufacture products for the Japanese market which are cheap but at the same time high quality. Furthermore, the range of products on offer is constantly being extended. The case of the clothing industry is particularly revealing. Since the mid-1990s, more and more Japanese companies are getting their products made in China and in other Asian countries at low wage costs. At the same time, it has been possible to do away with margins for intermediaries by building up new direct routes for distribution. The success of the Uniqlo fast retailing chain is representative of this business model which has transformed the whole industry. It is not an exaggeration to say that casual leisure clothing that previously cost over JPY 5000 is now offered by Uniqlo and other companies for less than JPY 2000.

Under the influence of the ubiquitous Uniqlo shops, the middle and upper classes, for whom up till then “cheap equalled bad”, were thought to be gradually coming round to believing “cheap but not all that bad”. However, as Japanese consumers are exceptionally demanding, they are generally not happy with this “cheap but not all that bad” view. Many of the textiles specialists aimed at the success of Uniqlo and copied its low-price strategy. This resulted in even more competition amongst these suppliers and the increasing pressure on costs did not always have a positive influence on customer loyalty.

For this reason, recent years have seen simple low-price strategies abandoned and independent brands emerge. A market survey carried out in 2007 in which consumers were questioned in group interviews revealed that Uniqlo has been able to position itself not as a cheap brand but as a brand with the best customer loyalty. The respondents belonged to the group with an annual income of JPY 7 million, that is, a class with above-average incomes.