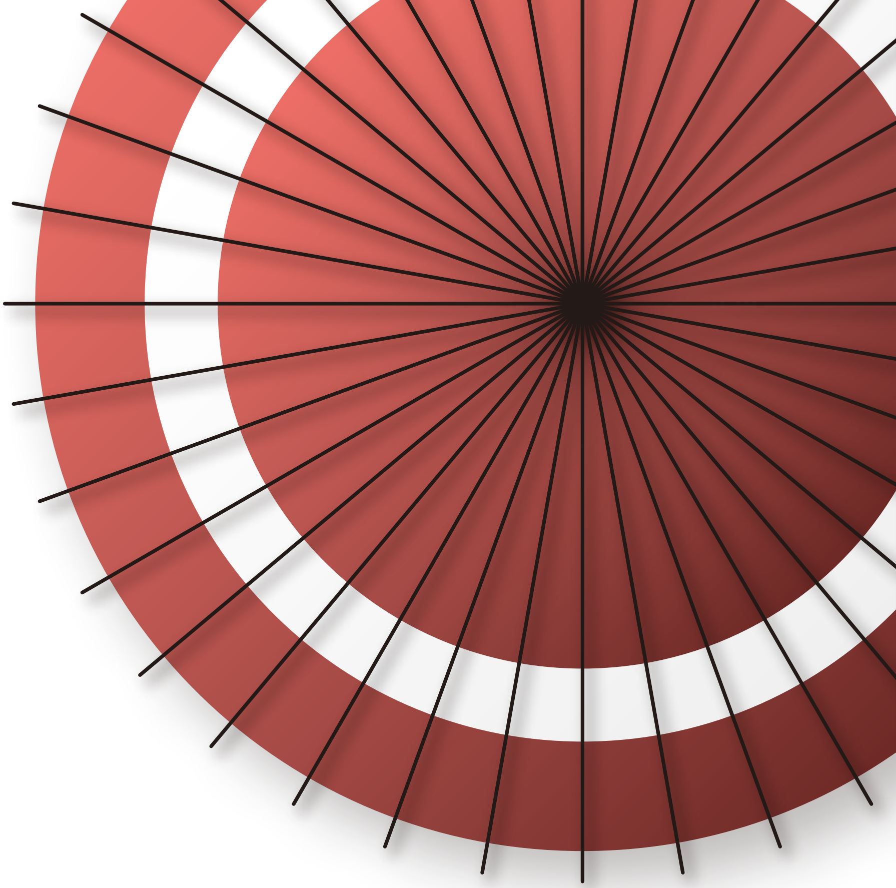
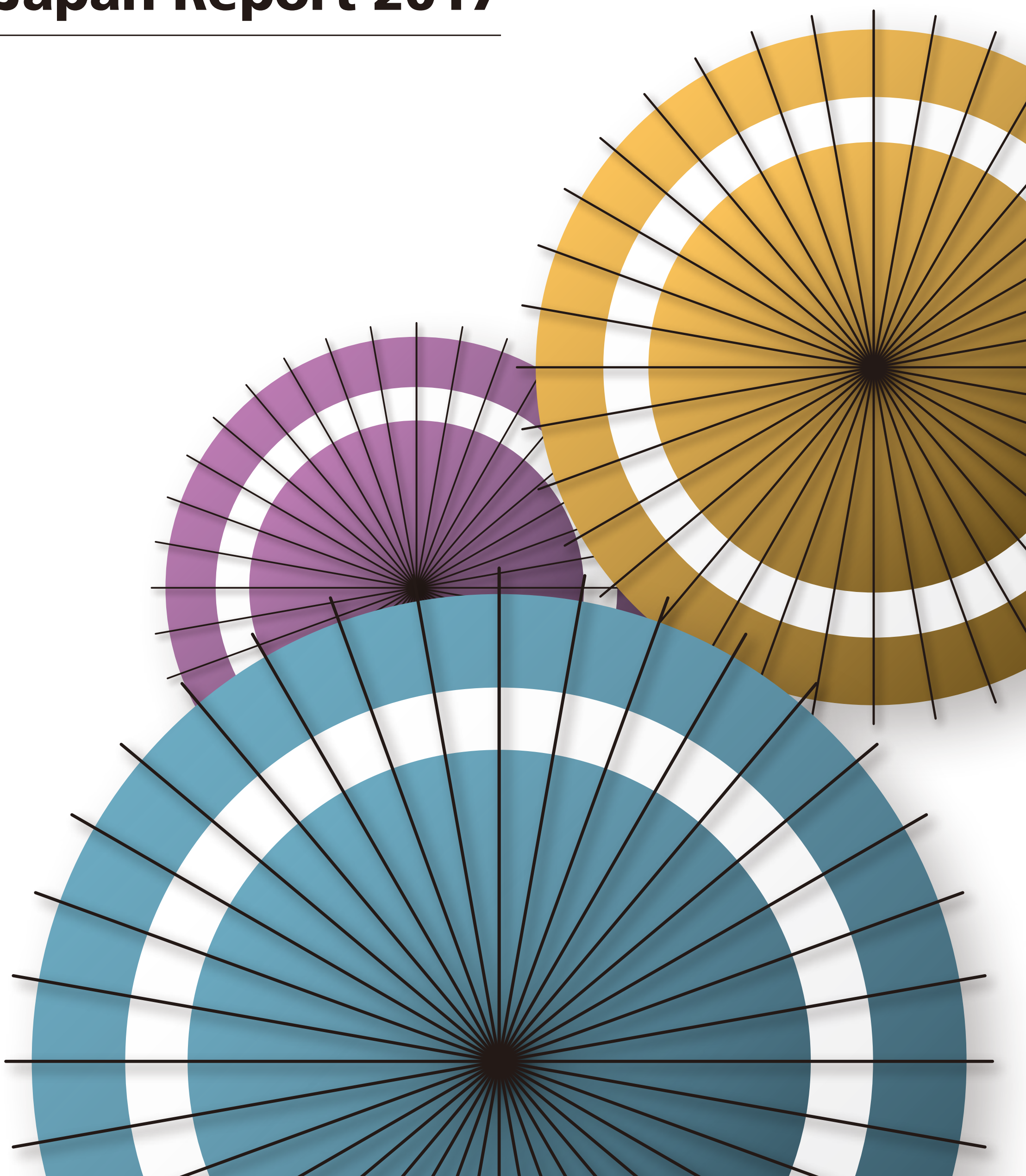


# JETRO Invest Japan Report 2017



JETRO

INVEST JAPAN

# Message from the Chairman

Hiroyuki Ishige
Chairman and CEO
Japan External Trade Organization

With the goal of creating employment and innovation by attracting excellent human resources and technologies to Japan, the government has announced its target of increasing inward foreign direct investment (FDI) stock to 35 trillion yen by 2020. In 2014, inward FDI stock exceeded the 20-trillion-yen mark for the first time, and by the end of 2016 it had achieved a historical high for the third consecutive year with 27.8 trillion yen, increasing by 12.4% year-on-year. The policy target, which was once thought too ambitious, has now become feasible.

FDI in Japan is experiencing a number of qualitative changes today. Some trends which are gaining momentum include: (1) the establishment of research and development centers, (2) expansion of investment from Asia and (3) a focus on the tourism business in response to the rapid increase in visitors to Japan. In addition, there are new moves to contribute to solutions of problems that Japan, which is called a "frontrunner in overcoming global challenges," is facing, through use of the Internet of Things, artificial intelligence and cutting-edge technologies of the so-called Fourth Industrial Revolution. With the expansion of e-commerce, there has also been investment in establishing procurement bases in Japan, which is also expected to help in the development of overseas markets by Japanese companies.

In order to expand, as well as accelerate, FDI into Japan, the country must continue to be an attractive market. "Business friendliness" is one important factor. In recent years, the government has realized various reforms—including of "bedrock regulations." It has also lowered the corporate tax rate and encouraged the strengthening of corporate governance. Furthermore, in the Growth Strategy 2017 (decided by the Cabinet on June 9, 2017), the government announced a new reform policy meant to break free from existing frameworks and made from the viewpoint of enterprises. It includes a "regulatory sandbox" system to encourage development of business models through trial and error in order to foster new innovative businesses and a 20% reduction in cost for administrative procedures. With the success of Abenomics, both the investment environment and major economic indicators in Japan are steadily improving. Foreign-affiliated companies doing business in the country have become aware of these changes and many of them are actually planning to increase investment in Japan.

However, one of the greatest obstacles for these foreign-affiliated companies is the difficulty in securing human resources. The "Japanese Green Card for Highly-Skilled Foreign Professionals" established this spring is a bold measure by the government to address this by making it easier for qualified professionals from overseas to settle in Japan. JETRO is also contributing to solving this problem by calling the attention of international students in Japan to foreign-affiliated companies as potential places of employment.

Since the start of the "Invest Japan" campaign in 2003, JETRO, as Japan's central organization for attracting inward FDI, has provided support for more than 16,000 projects aimed at entering the Japanese market, and helped in the successful establishment of over 1,600 companies. Experienced staff members and specialists in industry, law, accounting and other fields cooperate to address the challenges faced by foreign companies starting up in Japan, including those related to language, business practices, rules and regulations. This year, we introduced the "Personal Advisors System for Foreign Companies" in which our staff members serve as "attendants" to about 1,000 companies in order to provide enhanced consultation and solve individual problems. We are working to realize more projects by providing customized and highly-reliable services in cooperation with the central and local governments.

This report, which is in its third publication, is a compilation of information on recent trends, statistics on Japan's inward FDI, the activities of foreign-affiliates and their perception of the Japanese business environment, related policies of the central and local governments and JETRO's own activities. We hope it will be a useful resource for anyone considering starting business in Japan or supporting foreign investment into Japan.

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# KEY FIGURES

**27.8 trillion yen**

Japan's inward FDI stock at the end of 2016 reached a record high for the third consecutive year

**3.8 trillion yen**

The net inflow of FDI in Japan in 2016 marked a record high.

**10 times**

Inward FDI stock from Asia at the end of 2016 (compared to the year 2000)

**72%**

The ratio of the foreign-affiliated companies which answered "We will expand our business" within the next 5 years

**66%**

The ratio of the candidate prefectures other than Tokyo for foreign-affiliated companies' secondary investment

**70%**

The ratio of the foreign-affiliated companies which answered "The number of employees will increase" within the next 5 years

**-7%**

The reduction rate of the effective corporate tax rates (FY 2003 → 2016)

**-20%**

The reduction rate of administrative costs which the government has set as a numerical target (by March of 2020)

**1 trillion yen**

The amount of China's cross-border EC purchase from Japan (in 2016)

**200 staff members**

The number of JETRO's staff members working to attract foreign investment

**1,600 projects**

Successful startups & business expansion by foreign/foreign-affiliated companies supported by JETRO (FY 2003-2016)

**1,000 companies**

The number of companies JETRO supports in the "Personal Advisors System for Foreign Companies"

# KEY WORDS

## The Fourth Industrial Revolution

Commercial opportunities in Japan, a frontrunner in overcoming global challenges
— Contributing to solutions of various problems through IoT and AI

## Cross-Border EC

New trend of investment in Japan helping Japanese companies cultivate overseas markets

## “Regulatory sandbox” system

Demonstration experiments to foster new innovative businesses

## Japanese Green Card for Highly- Skilled Foreign Professionals

Greatly shortening the residence period for an application for permission of permanent residence

## Productivity enhancement & work-style reform

Efforts by foreign-affiliated companies may indicate solutions for Japanese companies to pursue "productivity enhancement" and “work-style reform.”

## Japanese market & stability of nation and society

First- and second-ranking appeal for foreign-affiliated companies doing business in Japan

## Engineers who can communicate in foreign languages

Human resources which foreign-affiliated companies are particularly struggling to secure

## Exchange Students/Global Talent & Foreign-affiliated Company Networking Event

Providing matching opportunity to foreign-affiliated companies having difficulty in recruiting global talent

## Regional revitalization by attracting foreign-affiliated companies

Creating jobs and introducing cutting-edge technologies and innovative business management know-how
— Local governments' various efforts to attract FDI

## Making Japan the most business-friendly country

— To create a more international and open business environment in Japan

# I Solid Growth in Japan's Inward FDI

Inward foreign direct investment (FDI) in Japan was vigorous in 2016, as its stock achieved the record high at the end of the year, while the full-year investment amount (net, flow) largely increased to about six times that of the previous year. Investment was especially active in the field of pharmaceutical and auto parts from Europe and in electric/electronics field from Asia. Large-scale deals include acquisition of long-term management rights of the Kansai International Airport and the Osaka International Airport (Itami Airport) by a consortium participated by French company VINCI Airports and acquisition of Sharp by the Hon Hai Group from Taiwan.

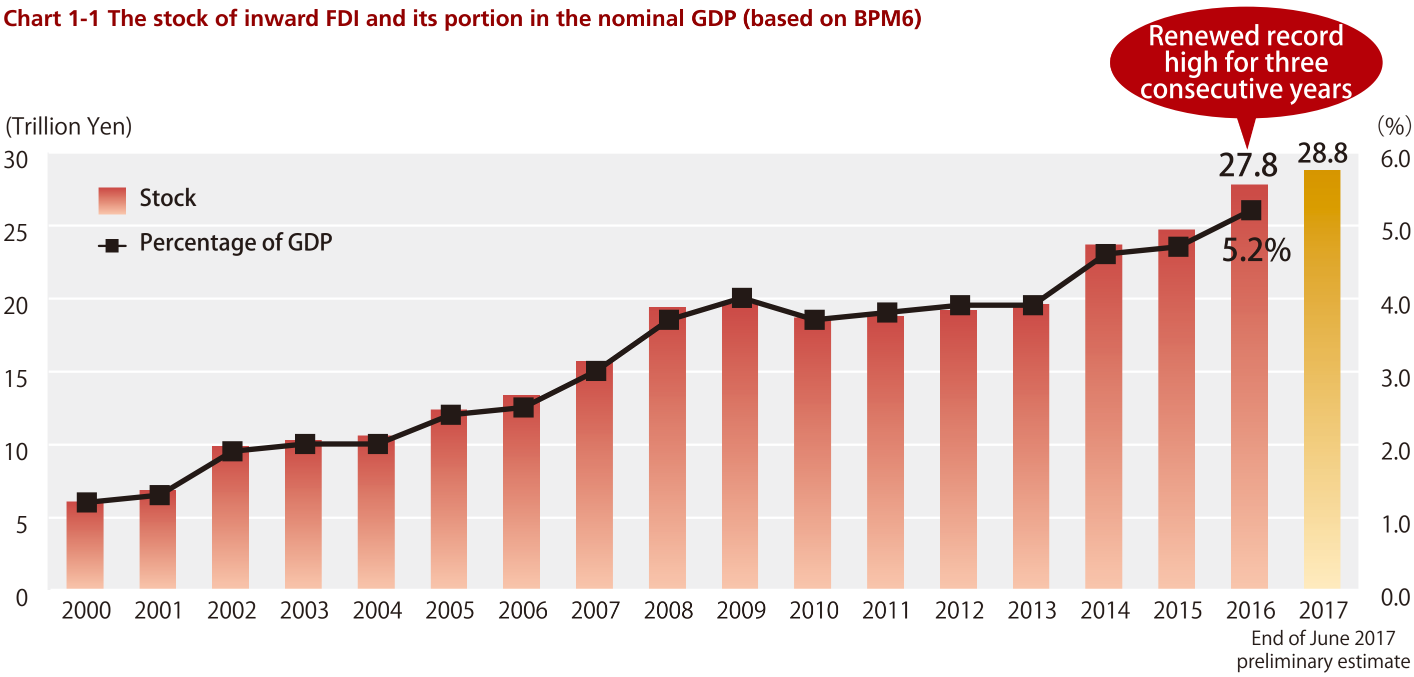
## 1. Inward FDI stock marked record highs and the inward FDI's ratio in nominal GDP was also a record high at over 5%

Japan's inward FDI stock at the end of 2016 was 27.84 trillion yen, marking 3.07 trillion yen growth from 24.77 trillion yen (value revised on May 26, 2017) at the end of 2015 and reached a record high for the third consecutive year (Chart 1-1).

By breakdown of the stock, "equity capital" which indicates stock acquisitions of and capital contributions to Japanese companies and subsidiaries in Japan by foreign companies (with over 10% voting rights) was 16.1 trillion yen. "Reinvestment of earnings," which is equivalent to the share of foreign companies according to the investment ratio in the undistributed earnings (retained earnings) of Japanese companies with contribution by foreign companies and subsidiaries in Japan was 6.3 trillion yen. "Debt instruments" that indicate debits and credits of fund transfers between parties involved in direct investment such as foreign companies and its subsidiary in Japan, and acquisition/disposal of debt was 5.4 trillion yen.

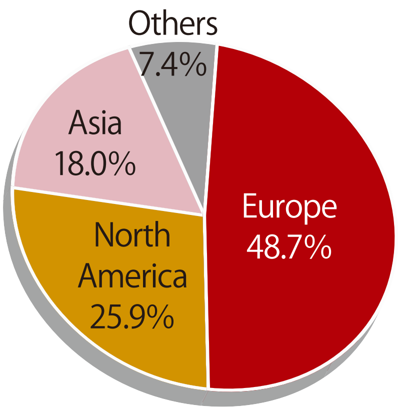
As a result of the increase in Japan's inward FDI stock, the ratio against its nominal GDP rose from 4.7% in 2015 to 5.2% in 2016, exceeding 5% mark for the first time. Comparing inward and outward FDI stock, outward FDI stock (159.2 trillion yen) was 5.7 times that of the inward FDI stock, still maintaining in an imbalanced state, as it has been in previous years.

**Chart 1-1 The stock of inward FDI and its portion in the nominal GDP (based on BPM6)**




[Source] "International Investment Position of Japan" (Ministry of Finance), "National Accounts of Japan" (Japan Cabinet Office)

#### Chart 1-2 Share of inward FDI stock in Japan by region (as of the end of 2016)




[Source] "International Investment Position of Japan" (Ministry of Finance)

## 2. The largest investor is Europe - Vigorous investment activities in the fields of pharmaceutical and auto parts

By region, Europe has the largest FDI stock in Japan reaching 13.6 trillion yen (the share of 48.7%), followed by North America (7.2 trillion yen, 25.9%) and Asia (5.0 trillion yen, 18.0%) (Chart 1-2).

By country, the US ranks first with 7.0 trillion yen (the share of 25.2%), followed by the Netherlands (3.8 trillion yen, 13.6%) and France (3.4 trillion yen, 12.0%). The ranking of the top ten remained the same from the ranking at the end of the previous year (Chart 1-3).

Stock by industry is the largest for finance and insurance reaching 7.8 trillion yen (the share of 35.0%) followed by electric machinery manufacturing by 3.1 trillion yen (14.1%) and transportation equipment manufacturing by 3.0 trillion yen (13.6%) (Chart 1-4).

Manufacturing accounts for about 70% of the FDI stock from Europe that is the largest investor by region. In 2016, investment in Japan by pharmaceutical and auto parts companies stood out. In the pharmaceutical field, LEO Pharma of Denmark acquired the overseas dermatology business of Astellas Pharma for 675.0 million EURO (about 89.1 billion yen). AstraZeneca of UK that positions treatment of respiratory diseases as one of its strategic businesses acquired the respiratory medicine business of Takeda Pharmaceutical for 575.0 million US dollars (about 69.9 billion yen). These companies narrow down priority fields and pursue improvement of business efficiency through selection and concentration.

#### Chart 1-3 Inward FDI stock in Japan by country and region (as of the end of 2016) TOP 10

| | Country/region | Stock (billion¥) | Ratio (%) |
|---|---|---|---|
| 1 | US | 7,010 | 25.2 |
| 2 | Netherlands | 3,800 | 13.6 |
| 3 | France | 3,351 | 12.0 |
| 4 | UK | 2,262 | 8.1 |
| 5 | Singapore | 2,210 | 7.9 |
| 6 | Switzerland | 1,294 | 4.6 |
| 7 | Cayman Islands | 1,199 | 4.3 |
| 8 | Hong Kong | 1,099 | 3.9 |
| 9 | Luxembourg | 868 | 3.1 |
| 10 | Germany | 850 | 3.1 |

[Source] "International Investment Position of Japan" (Ministry of Finance)

#### Chart 1-4 Inward FDI stock in Japan by industry (as of the end of 2016) TOP 10

| | Industry | Stock (billion¥) | Ratio (%) |
|---|---|---|---|
| 1 | Finance and insurance | 7,791 | 35.0 |
| 2 | Electric machinery | 3,127 | 14.1 |
| 3 | Transportation equipment | 3,019 | 13.6 |
| 4 | Chemicals and pharmaceuticals | 1,393 | 6.3 |
| 5 | Services | 1,179 | 5.3 |
| 6 | Communications | 859 | 3.9 |
| 7 | Wholesale and retail | 842 | 3.8 |
| 8 | General machinery | 595 | 2.7 |
| 9 | Real estate | 407 | 1.8 |
| 10 | Transportation | 327 | 1.5 |

[Note] In the statistics of the inward FDI stock by industry, the investment made by a subsidiary to the parent company is counted as the withdrawal of investment by the parent company (Directional Principle). Therefore, the calculation method differs from that of the statistics for inward FDI stock by region and investment type.
[Source] "International Investment Position of Japan" (Ministry of Finance)

In the field of auto parts, Autoliv (Sweden), the world's largest air bag company, and Nissin Kogyo (Nagano Prefecture), Japan's leading brake manufacturer, established a joint company by making 51% investment and 49% investment respectively. They started joint development, production and sales of parts involved in brakes and control of four-wheeled vehicles with an eye to automatic driving. Valeo, a leading vehicle parts company of France, made Ichikoh Industries (Kanagawa Prefecture), a manufacturer of automobile lamps, its consolidated subsidiary through TOB (take-over bid). They will advance optimization of their R&D and production bases.

As the auto makers of the world are scrambling to develop automatic driving technologies, European auto parts suppliers are expanding their R&D functions in Japan. In 2016, Valeo, mentioned above, set up a test area for automatic driving in its Tsukuba Techno Center. The company announced that it will increase the number of employees to strengthen its R&D system for automatic driving and driving aid. Bosch of Germany, positioning Japan as an important development center following Germany and the US, started testing of automatic driving on public roads in Japan and set up a new system development department. Continental, another leading auto parts company of Germany, opened a test course for automatic driving in Mombetsu, Hokkaido.

## 3. Asia continues to increase its share

Inward FDI stock from Asia at the end of 2016 has rapidly increased to 971% above 2000 levels (Chart 1-5). It is the fastest growing investor region in recent years.

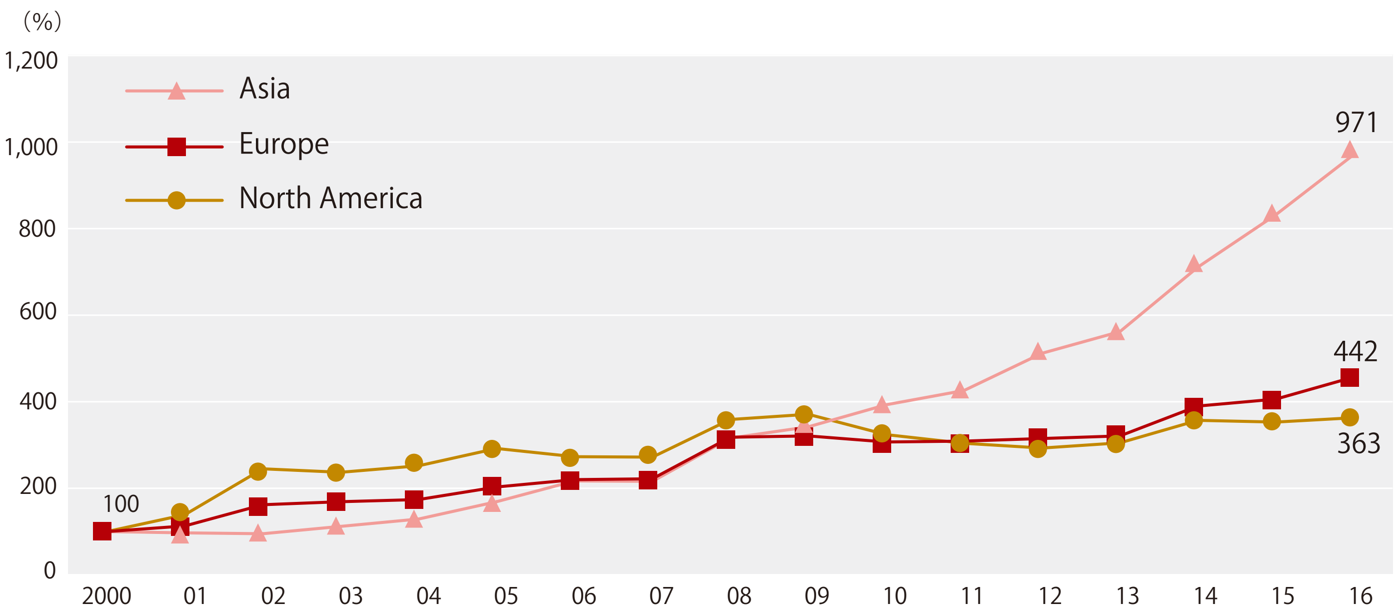
FDI stock increase is especially significant from Taiwan (764.4 billion yen, a 44.7% increase from the end of the previous year), Singapore (2.2 trillion yen, a 22.2% increase) and Thailand (217.9 billion yen, a 33.5% increase), among Asia.

From Taiwan, there was a large-scale M&A, acquisition of Sharp by the world's leading electronic manufacturing service (EMS) Hon Hai Precision Industry Group (for 388.8 billion yen). Hon Hai proposed a big contribution to Sharp that was reconstructing its business and completed the contribution in August 2016. As a result, Hon Hai became the biggest shareholder with about 66% of the voting power of Sharp.

About 90% of FDI stock from Singapore is in the non-manufacturing field. In recent years, with the expansion of 3PL (acronym for third-party logistics, a service to take care of logistics as a third party separately from shippers and carriers) and e-commerce, development of and investment in physical distribution facilities are vigorous. In other services, ASCOT of serviced apartments, Bee Cheng Hiang of pork jerky, Kwanpen of high-class bags, concierge shopper honestbee and others made their first entrance into Tokyo. The Singapore brand started to appeal to Japanese consumers. From Thailand, entry into the photovoltaic market is active in the last few years. In 2016, leading private power company Gunkul Engineering acquired GK Utsunomiya operating photovoltaic power plants for 24 billion yen, and BCPG Japan, a subsidiary of Bangchak Petroleum, built photovoltaic power plants in Akita and Okayama Prefectures.

80% of the FDI stock from the US, the largest investor country, is in the non-manufacturing industry. Finance and insurance, retail, telecommunications and services account for a large part of the stock. In recent years, private equity (PE) funds such as Kohlberg Kravis Roberts (KKR), Bain Capital and Carlyle have been making conspicuous M&A investments in Japan. Looking at M&A in Japan from the US by industry sector in the past three to four years, there have been more M&A in the high-tech sector including software and semiconductors.

**Chart 1-5 Changes in Inward FDI stock in Japan by region (growth ratio when the stock as of year 2000 is 100)**




[Note] The stocks for 2014 and after are calculated based on BPM6. The stocks before 2013 were recalculated from being BPM5-based to BPM6-based by JETRO.
[Source] "International Investment Position of Japan" (Ministry of Finance)

## 4. Inflow greatly exceeded in 2016

The net inflow of inward FDI in Japan in 2016 marked 3.8 trillion yen, about six times that of the previous year (667.5 billion yen) and a record high since 1996 when comparisons could be made. By investment type, debt instruments were 1.9 trillion yen, reinvestment of earnings was 1.4 trillion yen and equity capital was 522.2 billion yen.

By region, flow was 2.0 trillion yen from Europe, 903.7 billion yen from Asia and 629.8 billion yen from North America. Inflow exceeded outflow for all three regions (Chart 1-6).

By industry type, the amount was largest in electric machinery at 493.0 billion yen where Taiwan (208.2 billion yen) accounted for the largest part. This is thought to be an effect of the acquisition of Sharp by Hon Hai mentioned above.

The net flow of inward FDI in Japan in January to September term of 2017 (provisional) was down from a year earlier but maintained a positive inflow of 1.24 trillion yen (Chart 1-7).

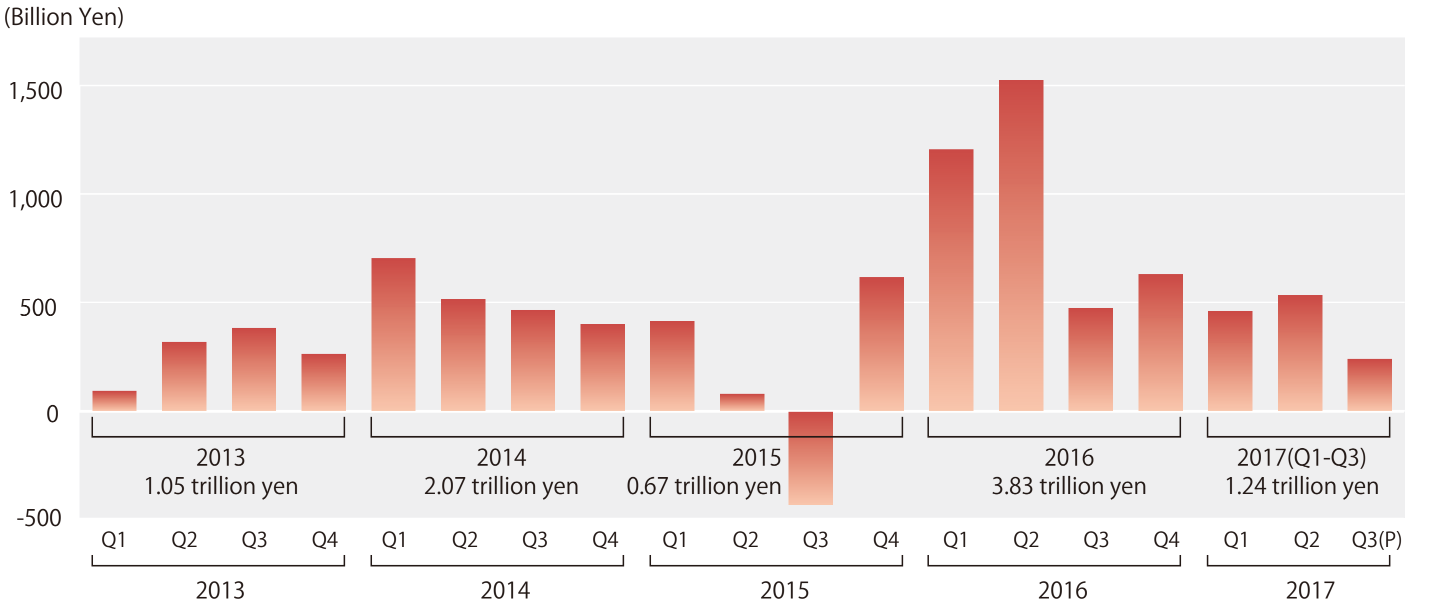
**Chart 1-6 Changes in the flow (net) of inward FDI into Japan by country/region**

(Billion Yen)

| | 2014 | 2015 | 2016 | 2017 Jan.-Sep. (P) | Year-on-year growth (%) |
|---|---|---|---|---|---|
| Asia | 678.2 | 673.7 | 903.7 | 524.7 | -39.9 |
| China | 80.2 | 77.8 | -15.1 | 64.7 | 34.5 |
| Hong Kong | 227.9 | 117.8 | 145.8 | -35.4 | - |
| Taiwan | 126.4 | 87.6 | 258.9 | 56.5 | -77.2 |
| Korea | 69.9 | 114.0 | 61.2 | 71.3 | 55.0 |
| ASEAN | 173.6 | 274.8 | 453.9 | 367.3 | -9.2 |
| Singapore | 144.0 | 222.9 | 383.0 | 389.5 | 23.4 |
| North America | 758.6 | 629.7 | 629.8 | 440.1 | -18.0 |
| US | 757.6 | 631.2 | 632.3 | 450.0 | -16.1 |
| Latin America | 72.9 | -248.4 | 180.8 | 159.4 | 6.8 |
| Oceania | 61.8 | -75.9 | 90.8 | -2.0 | - |
| Europe | 440.9 | -339.0 | 2,012.7 | 111.1 | -92.9 |
| EU | 375.8 | -314.5 | 1,896.3 | 57.9 | -96.1 |
| World | 2,074.5 | 667.5 | 3,830.7 | 1,237.0 | -61.4 |

[Note] The data for 2017 is provisional.
[Source] "Balance of Payments" (Ministry of Finance)

**Chart 1-7 Changes in the quarterly flow (net) of inward FDI into Japan**




[Note] Q1(Jan. ～ Mar.), Q2(Apr. ～ Jun.), Q3(Jul. ～ Sep.), Q4(Oct. ～ Dec.)
[Source] "Balance of Payments" (Ministry of Finance)

## 5. Acquisition of the management rights of Kansai International Airport and Osaka International Airport was the largest M&A in Japan

According to Thomson Reuters database, the largest M&A (completed) in Japan in 2016 was the acquisition of 44-year management rights of the Kansai International Airport and Osaka International Airport (Itami Airport) by a consortium led by VINCI Airports of France and ORIX (total value is about 2.2 trillion yen). This project is structured using a scheme called "concession," that is a scheme for infrastructure development where the national or local government sells long-term management rights of public facilities to a private company while keeping their ownership. In other countries, the concession scheme has been introduced into areas such as airports, roads and water services. The project by the consortium above became the first large-scale concession project in Japan. Another concession project by a foreign-affiliated company in Japan is acquisition of the management rights of sewage treatment service of Hamamatsu City, Shizuoka Prefecture by a consortium including Veolia of France, JFE Engineering, ORIX and others (for 2.5 billion yen, announced by Hamamatsu City in March 2017).

Other major M&A deals in Japan in 2016 include investment by Asian companies in the electric/electronic field. In addition to the acquisition of Sharp by Hon Hai, Chinese home appliance manufacturer Midea Group acquired 80.1% (about 51.4 billion yen) of the share of Toshiba Lifestyle, a company manufacturing and selling home appliances under the umbrella of Toshiba. Investments by European pharmaceutical companies include acquisition of specific businesses by Leo Pharma and AstraZeneca as described above.

M&A by foreign investment funds is spreading from manufacturing to services in recent years. A US investment fund Kohlberg Kravis Roberts (KKR) acquired Calsonic Kansei, the largest auto parts manufacturer under the Nissan group for 498.2 billion yen, and Hitachi Koki, one of the major subsidiaries of Hitachi, through TOB. Other M&A deals include acquisition of Hasegawa Holdings offering house cleaning and nursing-care services by UK investment fund CVC Capital Partners (35.0 billion yen), and acquisition of shares of Joyful Honda operating home improvement centers by Baring Private (Equity) Asia, an investment fund based in Hong Kong (38.9 billion yen) (Chart 1-8).

**Chart 1-8 Major inward M&A deals in Japan (2016 to the first half of 2017)**

| Date effective | | Target | | Acquirer | | | Value (Billion¥) |
|---|---|---|---|---|---|---|---|
| | | | Industry | | Parent country/region | Industry | |
| 2016 | Apr. | New Kansai Intl-Op Concession | Transportation & infrastructure | an SPV formed by ORIX-VINCI Airports consortium | - | Transportation & infrastructure | 2,205.0 |
| | Aug. | Sharp | Electronics | Hon Hai Precision Industry | Taiwan | Electronics | 388.8 |
| | Feb. | One M Logistics 2 | Real estate | LaSalle LOGIPORT REIT | US | Real estate investment trust | 161.4 |
| | Apr. | Astellas Pharma-Dermatology | Pharmaceuticals | LEO Pharma | Denmark | Pharmaceutical | 89.1 (675 million Euro) |
| | May | Takeda Pharm-Respiratory | Pharmaceuticals | AstraZeneca | UK | Pharmaceutical | 69.9 (575 million USD) |
| | Jun. | Toshiba Lifestyle Products & Services | Consumer electronics | Midea International | China | Consumer electronics | 51.4 |
| 2017 | May | Calsonic Kansei | Autoparts | Kohlberg Kravis Roberts (KKR) | US | Investment firm | 498.2 |
| | Apr. | USJ | Leisure | Comcast NBCUniversal | US | Media | 254.8 |
| | Mar. | Accordia Golf | Leisure | MBK Partners | Korea | Investment firm | 149.0 |
| | Jul. | Hitachi Koki | Machinery | Kohlberg Kravis Roberts (KKR) | US | Investment firm | 79.3 |

[Note] 1) As of September 2017. 2) Ranking according to single transaction amount. 3) "Acquirer" is the final acquirer (including corporate group)
[Source] Thomson Reuters

## FDI and geographical/historical proximity

column

Flow of FDI from one country to another may be characterized by geographical/historical proximity of the two countries. To take an example of the Inward FDI stock of Germany and France by country and region, investment in the two countries from EU countries account for about 70% (Chart 1-9).

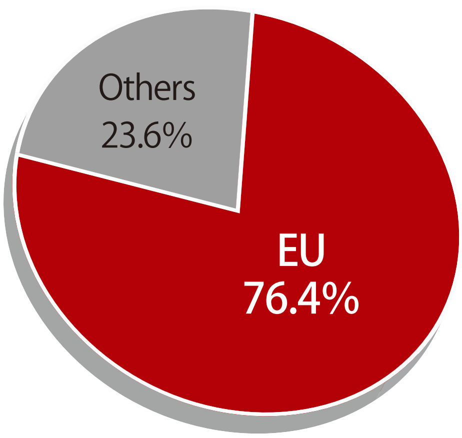
You can see that EU enterprises are vigorously making investments within the EU that gathers countries sharing the common currency Euro and close historical and cultural ties.

A similar trend is seen also in North America. Investments from the neighboring US account for about half of the inward FDI into Mexico and Canada. For Mexico, Spain is the second largest investor following the US, due to the historical background. Canada, another member of NAFTA (North American Free Trade Agreement), is also Mexico's major investor.

On the other hand, currently the US and Europe have the large share of FDI stock in Japan but the amount of investment from Asian countries is greatly increasing. Geographical/historical proximity means ease of mutual visits, availability of information, and acceptability of culture, which are big advantages for business activities by enterprises. The role of Asia in investment in Japan will further increase in importance.

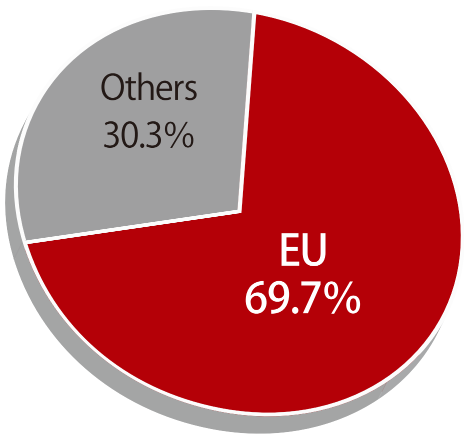
**Chart 1-9 Inward FDI into each country by country and region**

International investment position of Germany, liabilities (stock, 2015)



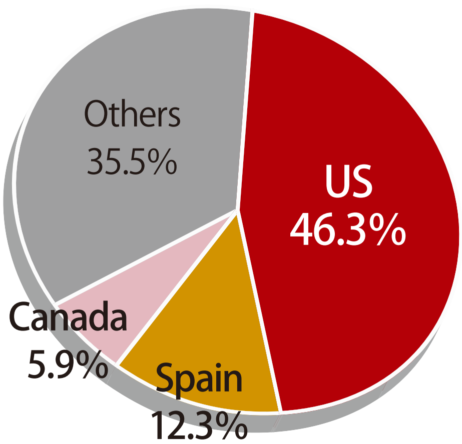

[Source] German Federal Bank

International investment position of France, liabilities (stock, 2015)



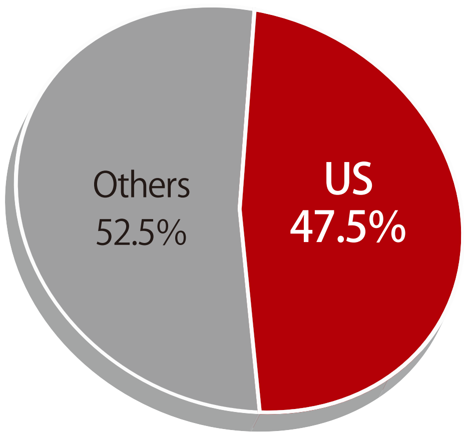

[Source] Bank of France

Inward FDI into Mexico (Cumulative, 1999-2016, net, flow)




[Source] Secretariat of Economy, Mexico

International investment position of Canada, liabilities (stock, 2016)




[Source] Statistics Canada