

4 Perception of the Business Environment in Japan among Foreign-affiliated Companies

From May to June 2018, JETRO conducted the “Survey on Japan’s Investment Climate,” designed to collect data on the perception of the business environment in Japan among foreign-affiliated companies and develop a more attractive investment environment for foreign-affiliated companies through the analysis of the resulting data.

The questionnaire was sent out to approximately 1,700 companies, with a focus on foreign-affiliated companies supported by JETRO in their entry into the Japanese market, and 266 companies responded.

The results of the survey show that foreign-affiliated companies perceive Japan as a highly profitable market. In addition, the results also highlighted the fact that, although companies felt that Japan’s greatest appeal lies in the large scale of its market, at the same time, they are also focusing on mid- to long-term growth in their business sectors, as well as business opportunities resulting from the fact that Japan is a frontrunner in addressing global challenges. Companies on the whole are keen to expand investment and increase the number of employees in Japan in the future, and are positive about the open innovation with Japanese companies, universities, etc.

1. Greatest appeal lies in the Japanese market, with high profitability also seen as a major selling point

Japan’s attractiveness as seen from the perspective of foreign-affiliated companies is a vital element in gaining a comprehensive grasp of Japan’s business environment. In this survey, in regard to the perceived attractiveness of doing business in Japan among foreign-affiliated companies, the top three answers given by companies are as follows: “Japanese market,” “Existence of suitable partners (companies, universities, etc.) with outstanding technology or products,” and “Stability of country and society” (Chart 4-5).

Japan has an established reputation as a huge sophisticated market. In addition, Japan’s macroeconomic situation is picking up steadily, as shown by the fact that in September 2017, it recorded the second longest period of economic recovery in the postwar era, a factor which may have helped the Japanese market gain a favorable rating. Furthermore, the results of the survey may reflect the fact that Japan has been reevaluated for its stability

[Survey on Japan’s Investment Climate: Overview]

Objective of the survey and summary of operation

The survey is designed for present data analysis to develop a more attractive investment environment for foreign/foreign-affiliated companies and make policy recommendations for this purpose. Companies were asked about attractiveness of the investment environment in Japan, obstacles for doing business in Japan and other questions in the form of questionnaire. This survey was initiated in 2015 and has been conducted every year since then.

Survey period: from May 15 to June 6, 2018

Target companies

About 1,700 foreign-affiliated companies supported by JETRO in their entry into the Japanese market and member companies of foreign chambers of commerce in Japan.

Response: valid response from 266 companies

Profile of the responding companies

Chart 4-1 Country/region of the parent companies

Country/region	No. of Companies	Country/region	No. of Companies
US	61	Spain	3
Germany	51	Vietnam	3
China	30	Belgium	3
Korea	15	UAE	2
France	13	Australia	2
India	10	Thailand	2
UK	10	Denmark	2
Taiwan	10	Philippines	2
Canada	9	Israel	1
Italy	8	Czech Republic	1
Netherlands	5	Finland	1
Switzerland	4	Malaysia	1
Hong Kong	4	Myanmar	1
Austria	3	Mexico	1
Singapore	3	Luxembourg	1
Sweden	3	Russia	1
		Total (Valid response)	266

in contrast to the uncertainty surrounding the political and economic situation in some Western countries.

In addition, looking at a breakdown of the “Japanese market,” which comes top in this survey every year, in regard to those areas of the Japanese economy that companies felt were especially attractive, a considerable number of companies, mainly in the communications, IT and software fields, answered “Mid- to long-term growth potential of our business field,” while a considerable number of companies, mainly in the life sciences field, answered “Opportunities for innovation due to Japan’s status as a frontrunner in addressing global challenges” (Chart 4-6).

These answers differ to the perception in which Japan is seen merely as a readily available huge sophisticated market, and are significant in the sense that these answers indicate that companies are forming their perceptions and appraisals of the Japanese market from a mid- to long-term perspective. Japan’s market scale is predicted to shrink in the future due to such factors as a population decrease resulting from its low birth rate and increasingly aging population. What is noteworthy here is that, despite this, a considerable number of foreign-affiliated companies are still seeing business opportunities in Japan, and are observing the potential for mid- to long-term growth, mainly in the communications, IT and software fields, which are deeply connected with the Fourth Industrial Revolution.

Furthermore, for the first time in this survey, companies were asked to evaluate the Japanese market from the perspective of profitability. The results show that over 70% of companies answered “Profitability is high” or “Profitability is somewhat high” (Chart 4-7). When looking at these figures

by industry, what stands out most is the fact that a considerable number of companies in the communications, IT and software fields answered “Profitability is high,” and that the opposite tendency was witnessed in the fields of trading, wholesale and retail.

According to “FDI in Figures” in an OECD report (April 2016), among 22 countries, Japan’s rates of return on inward FDI is 3rd overall and 1st in the service industry, thus demonstrating a high degree of profitability.

As to the reason for this, there is the perception that it is because highly profitable and resilient foreign-affiliated companies have long been making inroads into the Japanese market. On the other hand, the fact that many foreign-affiliated companies appraise Japan as a “lucrative market” sends out an important message to those foreign companies seeking to expand into the Japanese market in the future. (see p.7 Column, “Rate of return on inward FDI into Japan”)

Chart 4-2 Country/region of the parent companies (by region)

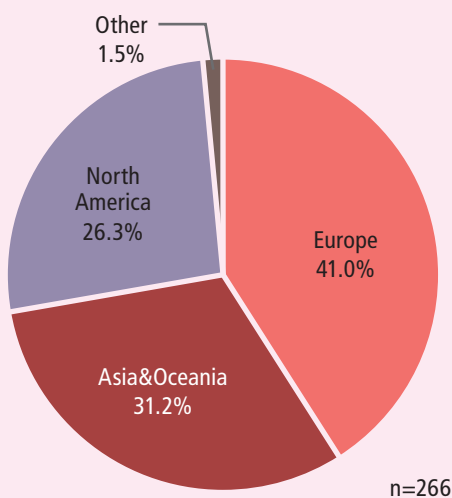


Chart 4-3 Number of years since establishment in Japan

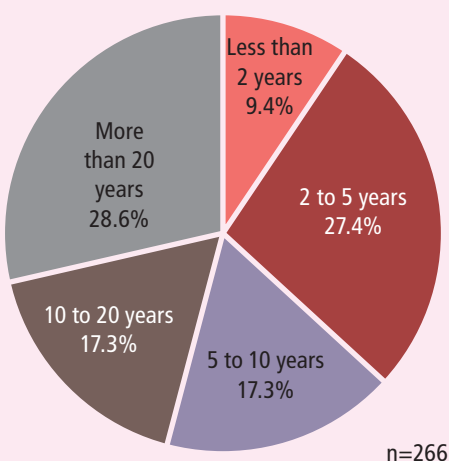


Chart 4-4 Type of industry

Type of industry	Rate
Communications/IT/software	14.7%
Life science (including pharmaceuticals, medical services, medical equipment, cosmetics)	11.7%
Electrical devices/electronics/precision machinery/ ICT equipment	10.9%
Trade/wholesale/retail	10.2%
Transport machinery/vehicles and parts	8.3%
Transportation/tourism (including hotel and entertainment services)	6.8%
Chemicals	5.6%
Professional services (consulting, legal, etc.)	5.6%
Finance/insurance	4.5%
Other services	4.5%
General machinery	3.4%
Energy and infrastructure (electricity, gas, water, petroleum, etc.)	2.6%
Textiles/apparel	2.3%
Other manufacturing (furniture, plastic supplies, printing, glass, etc.)	2.3%
Food and beverages	1.9%
Iron/nonferrous metals	1.5%
Construction	1.5%
Agriculture/forestry/fisheries	0.4%
Other	1.5%

n=266

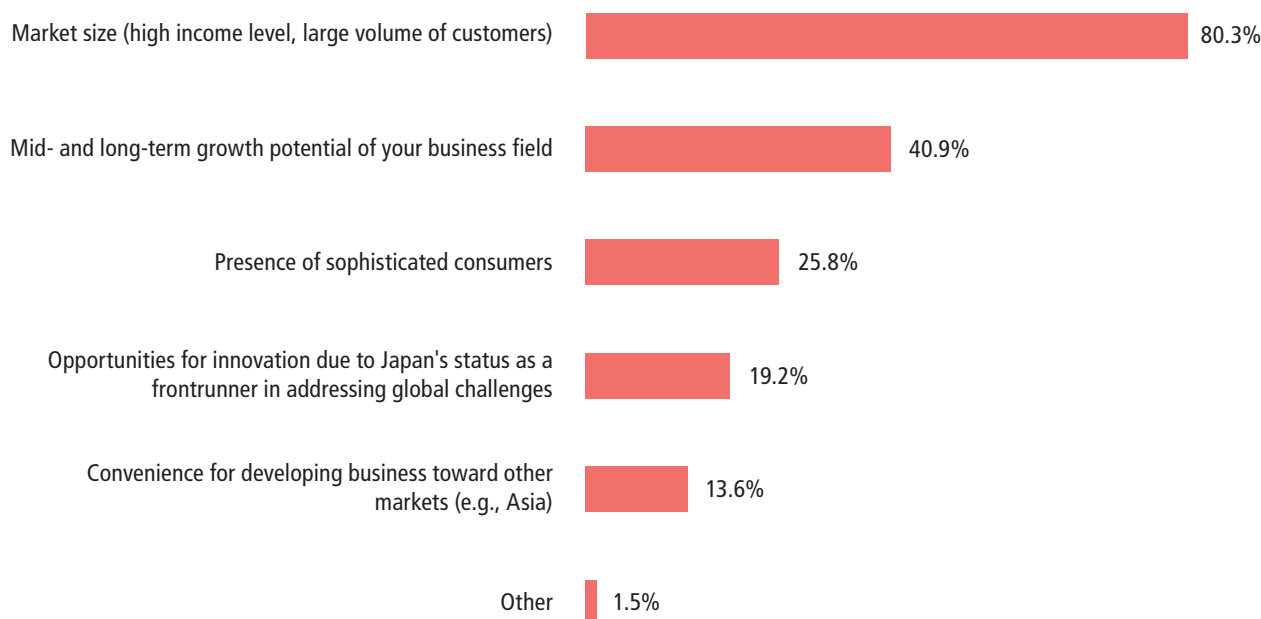
Chart 4-5 Attractiveness of doing business in Japan (select each from 1st to 3rd position)

Rank	Answer	Votes			Points
		1st	2nd	3rd	
1	Japanese market	158	20	20	534
2	Existence of suitable partners (companies, universities, etc.) with outstanding technology or products	25	50	29	204
3	Stability of country and society	16	43	60	194
4	High quality of R&D	19	38	15	148
4	Existence of renown global companies	24	26	24	148
6	Infrastructure (traffic, logistics, ICT, energy, etc.)	4	39	30	120
7	Potential for securing talented human resources	4	14	19	59
8	Well-maintained living environment	4	7	23	49
9	Japan's location (e.g. position as a gateway to Asia, advantage as a base for regional headquarters, etc.)	3	12	14	47
9	Expected increase in demand and sales toward the 2020 Tokyo Olympics	3	9	20	47
11	Well-structured legislation regarding intellectual property	2	6	5	23
	Other	4	2	7	23

[Note] In regard to the 1st, 2nd and 3rd place answer selected by respondents, each is awarded points as follows: 1st = 3 points, 2nd = 2 points, 3rd = 1 point, and are listed in order of answer with the highest points total.

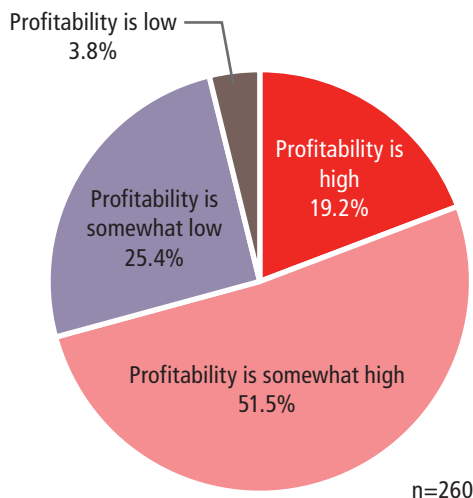
n=266

Chart 4-6 What is particularly appealing to you about the Japanese market? (top 2 options)



n=198

Chart 4-7 How do you evaluate the Japanese market in terms of profitability?



2. High level of business confidence among foreign-affiliated companies and a positive outlook on the future

Just under 50% of foreign-affiliated companies rated their current business conditions in Japan as “Improving,” which rose to over 60% in terms of their future outlook for the next 1 – 2 years (Charts 4-8 and 4-9). Compared to the previous year, this represents an increase of 5.1 points and 8.9 points, respectively. When looking at these figures by industry, many companies that answered “Improving” are connected with the communications, IT and software fields.

The Diffusion Index, the value obtained when subtracting the percentage of companies that answered “Declining” from the percentage of companies that answered “Improving,” is 39.2 for current business conditions and 61.0 for future outlook. These figures greatly exceed the value for the business outlook in the Bank of Japan’s Short-term Economic Survey of Enterprises in Japan (TANKAN) (in this survey in June 2018, the total for all industries and all sizes is 16 for “Recent” and 13 for “Future”). While it is important to bear in mind that TANKAN contains many SMEs, nevertheless business confidence among foreign-affiliated companies still remains high.

Chart 4-8 Current business conditions in Japan

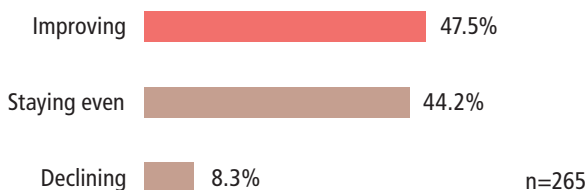
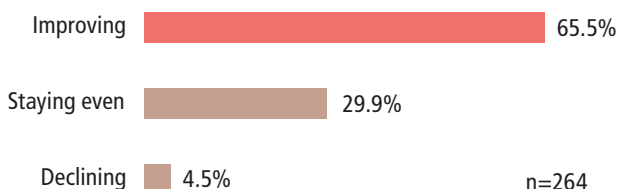


Chart 4-9 Outlook of the business conditions in Japan (over the next one or two year)



3. 70% of foreign-affiliated companies plan to expand their business operations and employment

Regarding their investment plans within the next five years, around 70% of companies answered, “Expand business” (Chart 4-10). While this represents a drop in 2 points compared with the previous year, taking into consideration the comparatively high level of business confidence among foreign-affiliated companies as Japan’s macroeconomic situation continues to pick up steadily, coupled with their perception of Japan as a highly profitable market, the fact that such a high percentage of foreign-affiliated companies answered affirmatively suggests that they remain eager to expand their investments in the future. In terms of employment, more than 70% of companies answered, “The number of employees will increase” within the next five years, around the same level as the previous year (Chart 4-11).

Chart 4-10 Investment plans within the next 5 years

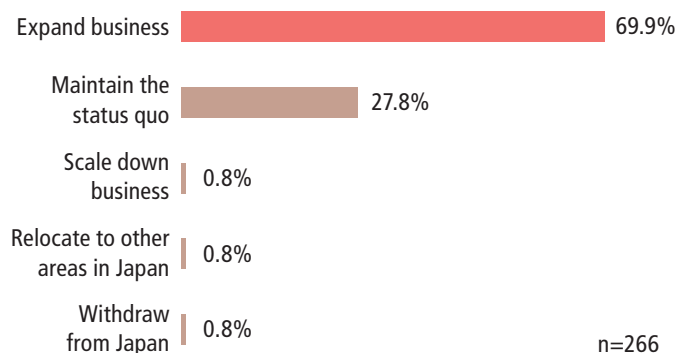


Chart 4-11 Projected number of employees in Japan (within the next 5 years)

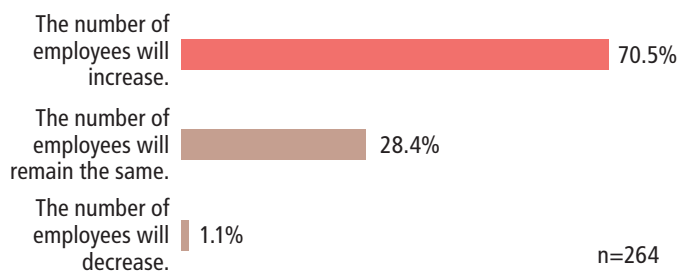
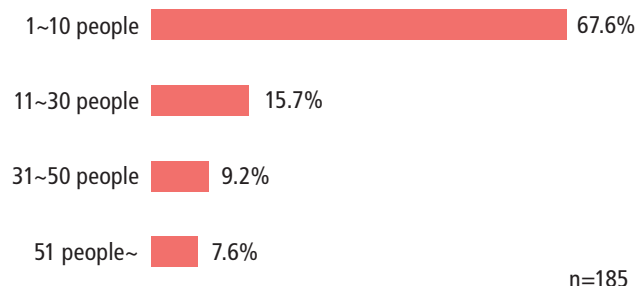


Chart 4-12 Number of increase



While M&A is one method of expanding business operations, in Japan the smooth succession of businesses is a major issue, given that many SME proprietors are reaching their senior years along with the fact that there is a lack of successors to take over their companies. Among those companies that are eager to expand their investments, over 50% expressed an interest in M&A deals with Japanese companies (Chart 4-13).

Chart 4-14 and Chart 4-15 set out specific locations (prefectures) for expanding investments, functions and reasons for selecting these locations. Over 60% of considered locations are outside of Tokyo, with the top locations being Osaka Prefecture, Kanagawa Prefecture, Aichi Prefecture, Fukuoka Prefecture, etc., largely the same as in previous years.

For the first time in this survey, foreign-affiliated companies were asked to state their reasons for selecting their locations. "Proximity to customers"

and the "Presence of relevant industrial clusters" were common answers for many regions. In addition, Tokyo and Kyoto Prefecture rose to the top positions for "Ease of securing human resources." This reflects a major need among foreign-affiliated companies for students who majored in sciences at universities or international students, as well as recent issues in expanding businesses in Japan (see p.30). In the case of Hyogo Prefecture, "Preferential treatment and services by local government" was seen in top three reasons.

Chart 4-13 Are you interested in secondary investment through M&A with a Japanese company?

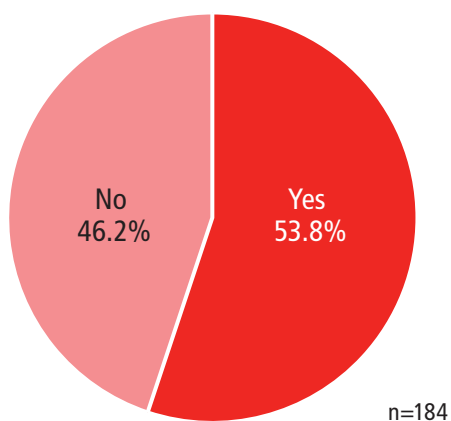


Chart 4-14 Where to make secondary investment (top 2 options)

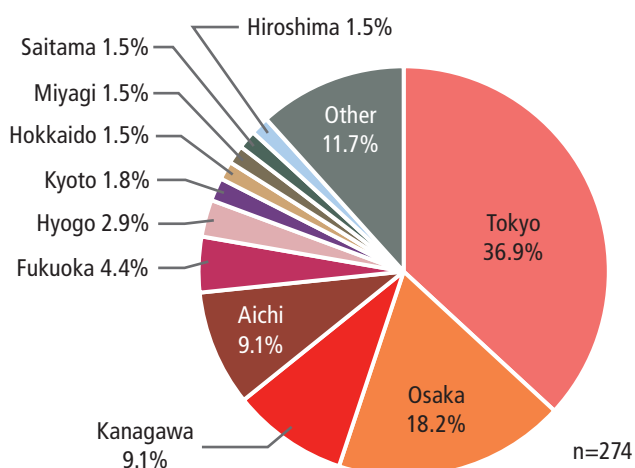


Chart 4-15 Where to make secondary investment (prefecture), the type of business and the reasons (top 3 options)

Rank	Prefecture	No. of projects	Type of business (top 3)	Reason (top3)
1	Tokyo	101	Sales/customer service	Proximity to customers
			R&D	Market size
			Manufacturing, Logistics	Development of infrastructure (transportation, logistics, information communication, energy, etc.), Ease of securing human resources
2	Osaka	50	Sales/customer service	Market size
			R&D	Proximity to customers
			Manufacturing, Logistics	Positioning compared to other bases in Japan
3	Kanagawa	25	Sales/customer service	Proximity to customers
			R&D	Positioning compared to other bases in Japan
			Manufacturing	Presence of relevant industrial clusters
3	Aichi	25	Sales/customer service	Proximity to customers
			R&D	Market size
			Manufacturing	Presence of relevant industrial clusters
5	Fukuoka	12	Sales/customer service	Market size
			Manufacturing, Logistics	Presence of relevant industrial clusters
			-	Proximity to customers
6	Hyogo	8	Sales/customer service	Proximity to customers
			R&D, Logistics	Presence of relevant industrial clusters
			-	Preferential treatment and services by local government
7	Kyoto	5	R&D	Ease of securing human resources
			Sales/customer service	Market size, Positioning compared to other bases in Japan
			-	-
	Other	48		

4. Focus on Japan's SMEs as partners for open innovation

This survey asked for the first time about the status of foreign-affiliated companies' initiatives concerning open innovation with Japanese companies, universities, etc. Around 70% of companies answered that "Efforts have already been implemented, and will continue/expand in the future" or "Efforts have not yet been implemented, but we are interested" (Chart 4-16). When looking at these figures by industry, interest tended to be high in the field of life sciences.

As global competition surrounding innovation continues to intensify, throughout the world, great importance is increasingly being attached on open innovation rather than closed innovation. In addition, Japan enjoys a largely high rating overseas as a center of research and development, and in recent years an increasing number of foreign-affiliated companies have been making moves to incorporate Japan's outstanding technologies and know-how into their own business operations. The current situation, therefore, suggests that foreign-affiliated companies are interested in open innovation with Japanese companies.

In regard to specific partners for open innovation, interest in "Small and medium-sized Japanese enterprises" came out highest along with "Universities/research institutes" (Chart 4-17). Also, as mentioned previously, the "Existence of suitable partners (companies, universities, etc.) with outstanding technology or products" was the second most popular answer concerning the perceived attractiveness of doing business in Japan among foreign-affiliated companies. These results suggest that "suitable Japanese companies" in this case does not necessarily indicate major companies. Rather than Japan's major companies, foreign-affiliated companies are more interested in Japan's SMEs, who possess outstanding technologies etc., as candidate partners for the creation of innovation.

In addition, foreign-affiliated companies were asked a new question related to the creation of innovation in Japan, concerning the "Regulatory Sandbox" system (see p.8). Here, over 60% of companies expressed an interest, mainly in the field of life sciences (Chart 4-18). Therefore, it is conceivable that foreign-affiliated companies are most interested in this system, which could be described as the Japan's government's centerpiece set of measures designed to boost the creation of innovation in Japan.

Chart 4-17 Please select the kinds of partners you are interested in (multiple answers)

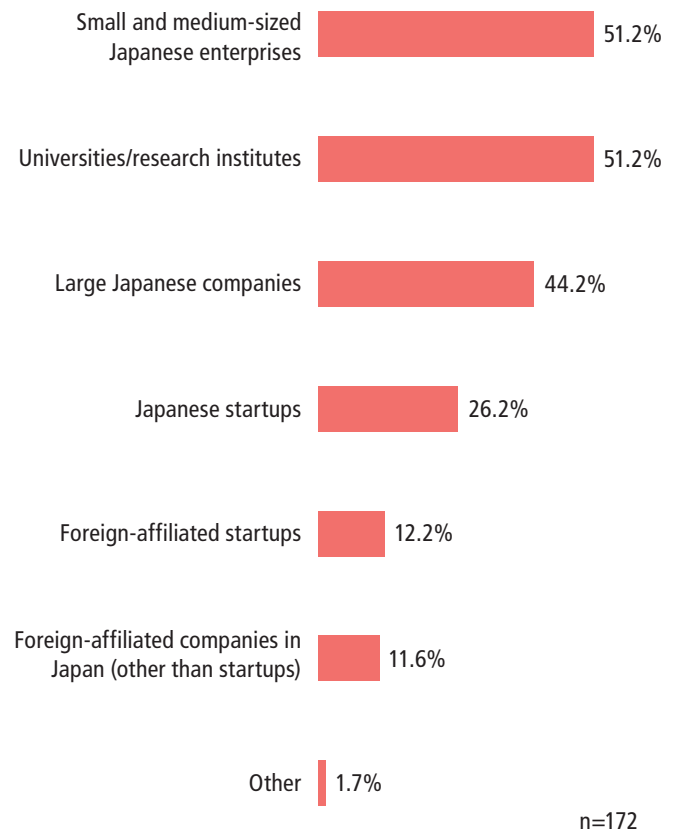


Chart 4-16 Please tell us about your efforts regarding open innovation with Japanese companies/universities, etc.

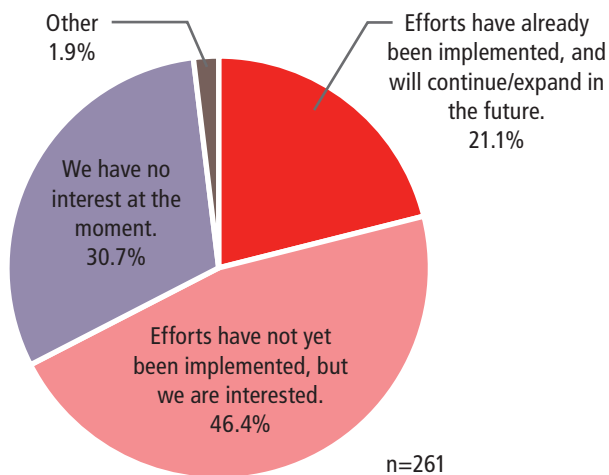
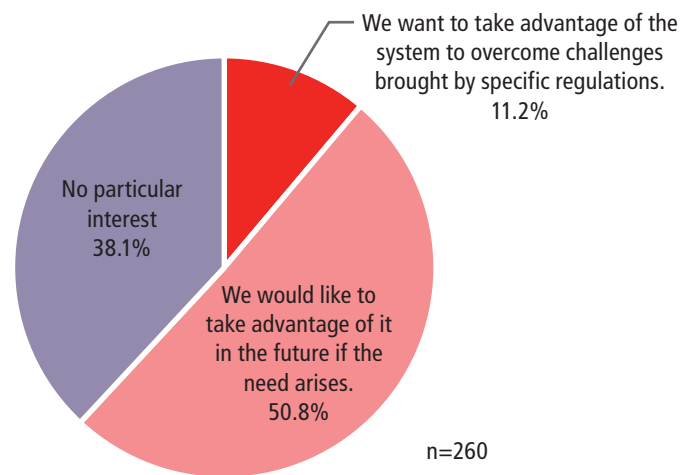


Chart 4-18 Please tell us about your interest in the "Regulatory Sandbox" system



5. The biggest obstacle to doing business in Japan is difficulty in finding human resources

The results of this survey show that the biggest obstacle to doing business in Japan is “Difficulty in finding human resources,” something that represents a serious business challenge (Chart 4-19). Over 30% of companies cited difficulty in finding human resources as the top obstacle to doing business in Japan, and around 60% of companies cited this as one of the top three obstacles.

When asked about particularly troublesome issues in connection with “Difficulty in finding human resources,” a majority answered “Lack of human resources with foreign language ability” followed by “Difficulty in finding experts” (Chart 4-20). When looking at these figures by category of job, the most difficult to fill is “Engineering” (Chart 4-21). These results are the same as in the previous year. Looking at the categories of industry of companies that answered “Engineering,” it is apparent that many are in the fields of “Chemistry” and “Electrical devices, electronics, precision machinery, and ICT equipment”

It is possible that the Japanese government’s current policy of accepting more highly skilled foreign professionals into the country will have a certain effect in improving this situation. In this survey, around 40% of foreign-

affiliated companies expressed high hopes that the “Japanese Green Card for Highly-Skilled Foreign Professionals” (established in April 2017) would prove effective (Chart 4-22).

In addition, the Japanese government is currently preparing to introduce a new status of residence for working in Japan, aimed at foreign professionals who already possess a certain level of expertise or technical skills and are ready to become immediate assets in the workplace (see p.11). If this measure comes to fruition, it has the potential to bring about a certain level of improvement. In light of the fact that around 60% of foreign-affiliated companies stated in last year’s survey that they would be interested in hiring international students (mainly in the sciences), JETRO has been taking steps to help solve such issues being experienced by foreign-affiliated companies, such as by holding networking events to connect international students and foreign-affiliated companies (see p.44).

In regard to “Complicated administrative procedures,” one of the top obstacles to doing business in Japan, many companies pointed to the “Excessive amount of required documents,” “Lack of English translation” and “Excessive amount of time required to complete procedures,” especially with “Tax matters,” “Labor matters” and “Matters related to status of residence (visas)” (Chart 4-23). As to why foreign-affiliated companies have given their relatively low appraisal of administrative procedures in Japan,

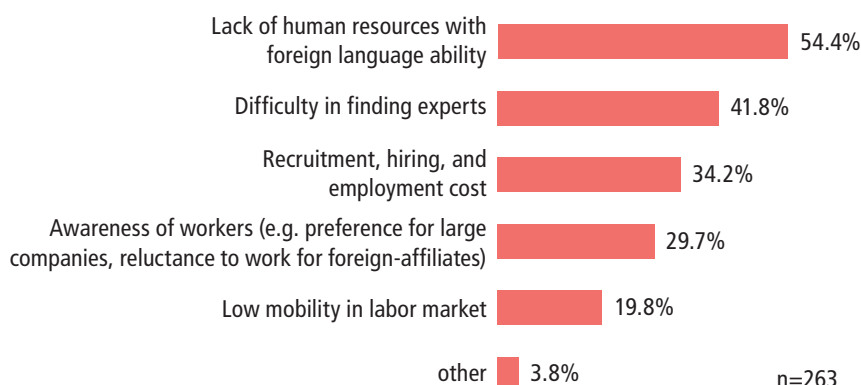
Chart 4-19 Obstacles to doing business in Japan (select each from 1st to 3rd position)

Rank	Answer	Votes			Points
		1st	2nd	3rd	
1	Difficulty in finding human resources	87	35	37	368
2	Difficulty in communicating in non-Japanese languages	54	69	31	331
3	High business costs	41	45	63	276
4	Complicated administrative procedures	36	40	39	227
5	Rigid regulations	24	32	31	167
6	Difficulty in finding business partners	11	25	15	98
7	Immigration control system	7	6	9	42
8	Difficulty in financing	0	7	12	26
9	Difficulty in living conditions for foreigners	0	2	11	15
	other	6	5	18	46

[Note] In regard to the 1st, 2nd and 3rd place answer selected by respondents, each is awarded points as follows: 1st = 3 points, 2nd = 2 points, 3rd = 1 point, and are listed in order of answer with the highest points total.

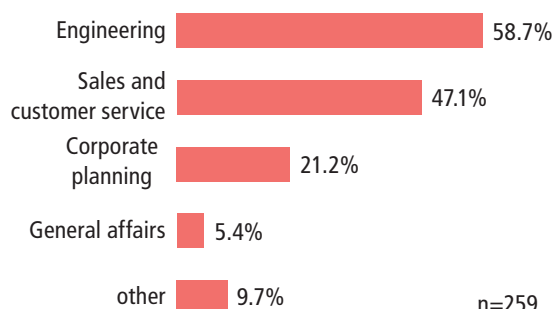
n=266

Chart 4-20 Regarding securing human resources, what difficulties in particular have you encountered? (top 2 options)



n=263

Chart 4-21 Regarding securing human resources, which categories of jobs are most difficult to fill? (multiple answers)



n=259

it is possible that they tend to base their perspective on comparisons with their own countries' systems and procedures, along with the fact that, in the 2000s, countries in Europe and North America carried out an extensive reduction in costs associated with administrative procedures along with the burden of paperwork.

In order to rectify this situation, the Japanese government set a KPI (key performance indicator) in its growth strategy to cut costs associated with administrative procedures by 20% or more in key fields by March 2020, and it is currently taking a range of measures to this end (see p.10). At any rate, moves to simplify a range of procedures and promote digital government can be expected to have a positive effect in simplifying accompanying documents during procedures and reducing the amount of time taken for procedures.

In terms of providing English language versions of documents, this continues to be a pressing concern for foreign-affiliated companies, which includes administrative procedures, and is an area in which ongoing efforts need to be made to bring about improvements. For instance, "Difficulty in communicating in non-Japanese languages" occupies the top position in the list of obstacles to doing business in Japan, and "Lack of English translation" has also risen to the top as the biggest difficulty relating to regulations in Japan (Chart 4-24).

Chart 4-22 From the perspective of securing human resources, what do you expect regarding the effectiveness of the "Japanese Green Card for Highly-Skilled Foreign Professionals"?

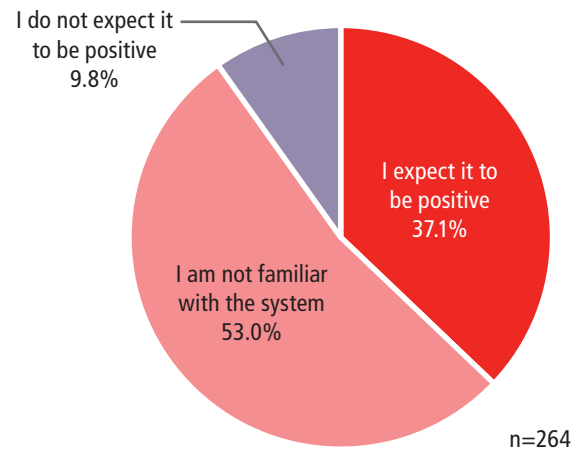


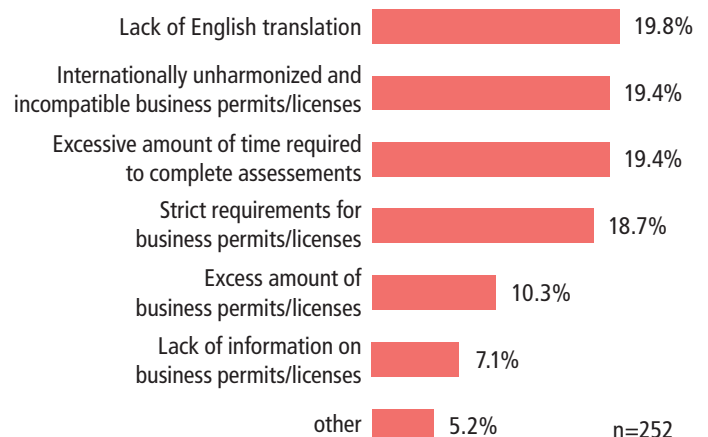
Chart 4-23 Administrative procedures felt to be in need of most improvement and specific issues currently experienced by companies

Administrative procedures that need improvement the most	Issues necessary to be improved the most								
	Excessive points of contact(lack of consolidation)	Excessive amount of required documents	Inconvenience caused by the lack of online procedures	Lack of English translation	Excessive amount of time required to complete procedures	High cost of applications and procedures	Other	Unselected	Total
Company registration	3	5	0	8	5	1	1	2	25
Tax matters	6	15	6	19	6	5	0	0	57
Social insurance	1	5	6	6	5	2	1	0	26
Labor matters	6	14	3	7	14	1	7	0	52
Matters related to status of residence (visas)	0	6	8	6	23	1	2	0	46
Intellectual property	0	1	2	3	0	0	0	0	6
Trade	1	4	0	2	4	2	0	1	14
Other	1	2	2	5	4	0	14	1	29
Unselected	0	0	0	2	1	0	0	8	11
Total	18	52	27	58	62	12	25	12	266

From the perspective of promoting inward foreign direct investment in Japan, the Japanese government has taken a number of measures, including the promise to "overcome language barriers at retailers and restaurants" along with efforts to translate Japanese laws into foreign languages, but some foreign-affiliated companies have pointed out that they face a major burden having to translate large volumes of information relating to individual regulations, and that there is no set interpretation of the content because no official English translations exist, making it difficult to report back to parent companies back in their home countries.

The provision of English language versions of documents requires time along with the development of suitable human resources, making it difficult to come up with measures that will take immediate effect. Having said this, the continuation of steady uninterrupted efforts to make improvements will be an important factor in further improving Japan's "business friendliness" in the future.

Chart 4-24 Regarding regulations in Japan, what is the most significant challenge for you?

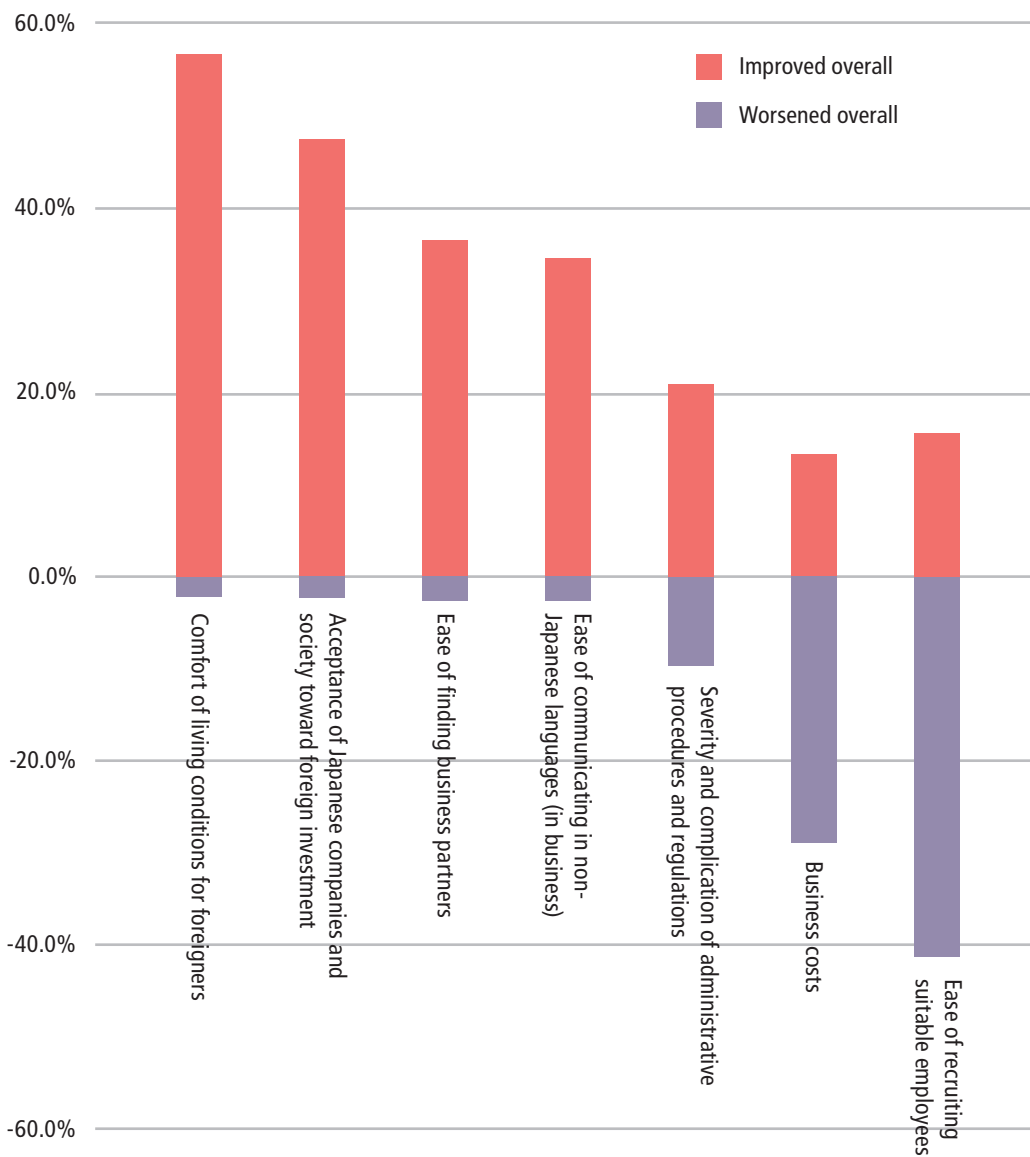


6. Japan's improving business environment

While issues still remain, foreign-affiliated companies are positive in many ways about the changes which have taken place in Japan's business environment over the past 1 – 2 years. Among the 7 items included in the survey, such as "Comfort of living conditions for foreigners," as with last year many companies felt that things are improving in 5 of the items, with the exception of "Ease of recruiting suitable employees" and "Business costs" (Chart 4-25).

In particular, in the case of "Comfort of living conditions for foreigners" and "Acceptance of Japanese companies and society toward foreign investment," a large proportion of companies feel that things are improving. With the increasing number of foreign tourists visiting Japan (28.69 million in 2017) and increasing number of foreign workers in Japan (1.28 million as of October 2017, the highest ever level) in recent years, it is possible that changes have taken place in the awareness of people in Japan as the accepting country.

Chart 4-25 Business environment in Japan - changes in comparison with past one or two years



n=266

[Note] Ratio of companies answering "Improved overall" is shown as positive, while that of answering "Worsened overall" is shown as negative. Ratio of answers "Unchanged" is not shown in the chart.

In regard to “Ease of communicating in non-Japanese languages (in business),” too, while this occupies the top position as an obstacle to doing business in Japan, the results show that companies believe things are improving in this area.

A major factor behind the conspicuous number of companies answering that the “Ease of recruiting suitable employees” has worsened is an increasingly severe labor shortage. In addition, in the case of “Business costs,” many companies feel that office rent and payroll are high (Chart 4-26), with rising wages due to recent labor shortages and rising office rents as a result of rising land prices accounting for this.

Since the start of the current administration, the Japanese government has sought to position Japan as “the most business friendly country in the world,” and as stated in Chapter 2, has worked out various policies from the perspective of businesses to achieve this. As this flow of initiatives continues to take root, Japan’s business environment is expected to improve step-by-step into the future. JETRO will continue to deliver feedback from foreign and foreign-affiliated companies to the Japanese government based on the results of its surveys, etc., and will work to help further improve Japan’s investment environment.

Chart 4-26 Regarding business costs in Japan, which is the greatest cost? (top 2 options)

