Japanese Manufacturing Affiliates in Europe and Turkey
- 2009 Survey -

March 2010

Japan External Trade Organization
(JETRO)

Preface

The survey on the "Japanese manufacturing affiliates in Europe and Turkey" has been conducted 25 times since 1983*. The latest survey conducted from May 2009 to July 2009 focused on research and analyzed the business situation of Japanese manufacturing affiliates operating in Europe and Turkey and the activities (outlook of operating profit, managerial issues, procurement of parts and materials, sales and production setups, impact of the FTAs under negotiation between the EU and other Asian countries, etc.).

We would like to express our great appreciation to the affiliates for their kind cooperation for our survey, which, over the years, has enabled us to constantly improve both the survey itself and report on the results. We hope that this report helps the affiliates and the other parties understand business development in Europe and Turkey

March 2010

Europe Division
Middle East and Africa Division
Overseas Research Department
JETRO centers/offices in Europe and Turkey
Japan External Trade Organization (JETRO)

* Countries in Central and Eastern Europe and Turkey were included in the survey from 1998 and 1999 respectively.

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Overview of the Survey

This is the 25th of a series of surveys that has been conducted annually since 1983 by the JETRO centers and offices based in Europe and Turkey.

1. Purpose of the Survey

This survey analyzes the activities of Japanese manufacturing affiliates operating in Europe and Turkey (operating profit forecasts of each company, managerial issues, procurement of parts and materials, sales and production setups, impact of the FTAs under negotiation between the EU and other Asian countries, etc.) for the purpose of assisting the implementation of strategic business planning and business activities at the Japanese enterprises.

2. Targets of the Survey

The survey targeted manufacturing companies in Turkey, 16 countries in Western Europe* and 10 countries in Central and Eastern Europe** where Japanese manufacturing affiliates are located. The targeted companies derive 10% or more of their investment from Japanese companies, both directly and indirectly. Survey also included companies (subsidiaries) set up by the Japanese affiliates already operating in Europe and other regions as well as companies that have completed local corporate registration but have not yet started operations.

* 16 countries in Western Europe (Ireland, The Netherlands, Belgium, Luxembourg, Portugal, Finland, Sweden, Denmark, UK, Germany, France, Italy, Spain, Greece, Austria, and Switzerland)

**10 countries in Central and Eastern Europe (Lithuania, Poland, Czech Republic, Slovakia, Hungary, Romania, Bulgaria, Slovenia, Serbia, and Montenegro)

3. Method of Conducting the Survey

The survey was conducted by sending an e-mail containing an Internet link (URL) to the online questionnaire form to the respondents and asking them to reply directly on line. As exceptions, some of questionnaire sheets were sent by mail or facsimile. The answers to the surveys sent by mail and facsimile have also been included in the tabulated results.

As this survey covered a number of companies operating overseas in various countries and industries, we endeavored to learn to the extent possible the exact number of Japanese affiliates that have entered into (or withdrawn from) the surveyed regions since the previous (24th) survey. In the process, we added or deleted Japanese affiliates established or withdrawn in the regions before 2007 but that we had been unable to access at the time of the previous survey.

4. Period of the Survey

May through July 2009

5. Response Status

Of the 1,028 Japanese manufacturing enterprises indentified as active in Europe or Turkey, we sent questionnaires to the 557 enterprises that agreed to cooperate in the survey. Of those, we received responses from 389 companies (response rate of 69.8%).

6. Notes on the Survey Results

(1) The number of Japanese manufacturing affiliates was totaled using information sources that can be considered reliable by the JETRO offices in Europe and Turkey and through the cooperation of each company. However, we do not guarantee the accuracy and comprehensiveness of the information.

(2) Not all the respondents answered every question. The percentages in this report were calculated using the number of respondents who actually answered the specific question (rounded to two decimal places). The percentages do not necessarily add up to 100.0%.

Europe

I. Overview of Japanese Manufacturing Affiliates in Europe

[Number of Japanese manufacturing affiliates in Europe]

- The latest survey shows that there were 1,011 Japanese manufacturing affiliates in Europe at the end of 2008, 766 in Western Europe, and 245 in Central and Eastern Europe. A total of 18 new Japanese manufacturing affiliates were established in Europe in 2008, 11 in Western Europe, and 7 in Central and Eastern Europe.

[Country overview]

- The UK was the home to the largest number of Japanese companies, with 197, followed by Germany with 151 and France with 117. These three countries accounted for 46.0% of the total number of Japanese manufacturing affiliates in Europe.
- The Czech Republic, which has the greatest number of Japanese manufacturing affiliates (87 companies) among Central and Eastern European Countries, has become the 4th largest manufacturing base for Japan among all European countries, followed by Poland, which has became the 5th largest European manufacturing base for Japan since 2006, with 72 companies.

[Industry overview]

- The transportation machinery parts industry accounts for the largest number of Japanese manufacturing affiliates with 206 (20.4% of the total), followed by the general machinery industry (including parts, molds and machinery tools) with 144 (14.2%), the chemical/petrochemical products industry with 89 (8.8%), and the electric and electronic parts industry with 88 affiliates (8.7 %).
- Among the 18 newly established Japanese manufacturing affiliates in Europe in 2008, the greatest number of affiliates belonged to the general machinery industry with 4 companies (22.2% of the total number of Japanese manufacturing affiliates newly established), followed by the transportation machinery parts industry with 3 companies (16.7%).

[Number of R&D and design centers]

- At the end of 2008, 425 Japanese manufacturing affiliates operated R&D and design centers in Europe, of which 150 companies operated independent R&D and design centers.

1. Two of the top five European manufacturing bases for Japanese manufacturing affiliates are in Central and Eastern Europe

The latest survey shows that there were 1,011 Japanese manufacturing affiliates in Europe at the end of 2008, 766 in Western Europe, and 245 in Central and Eastern Europe. By country, the UK was the home to the largest number of Japanese companies with 197 affiliates, followed by Germany (151) and France (117). These three countries accounted for 46.0% of the total number of Japanese manufacturing affiliates in all of Europe and 75.8% of the total in Western Europe.

The Czech Republic was the 4th largest European manufacturing base for Japan with 87 companies,

followed by Poland with 72 companies, making these two countries become two of the top five areas of investment in Europe, showing the growing presence of Central and Eastern European countries as centers for the Japanese manufacturing industry.

The industry with the largest number of Japanese manufacturing affiliates was the transportation machinery parts (automobiles, motorcycles) with 206 companies (20.4% of the total), followed by the general machinery (including parts, molds and machinery tools) with 144 companies (14.2%), the chemical/petrochemical products with 89 (8.8%), and the electric and electronic parts with 88 (8.7%). Together, these four industries accounted for 52.1% of the total.

There are some dominant industries particular to certain countries/regions. In Western Europe, the dominant industries are the general machinery (including parts, molds and machinery tools), the transportation machinery parts (automobiles, motorcycles) and the chemical/petrochemical products . In the U.K., the transportation machinery parts (automobiles, motorcycles), the general machinery (including parts, molds and machinery tools), and the electric and electronic machinery take the top spots. Meanwhile, in France, the transportation machinery parts (automobiles, motorcycles), the food products, agricultural and fisheries product processing, and the general machinery (including parts, molds and machinery tools) are dominant. However, in Germany, the general machinery (including parts, molds and machinery tools), other manufacturing, and the electric and electronic parts are dominant. In Central and Eastern Europe, Japanese manufacturing bases are highly concentrated in the transportation machinery parts (automobiles motorcycles) with 88 companies, which accounted for 35.9% of the total number of Japanese manufacturing affiliates in Central and Eastern Europe, followed by the electric and electronic parts with 39 companies (15.9% of the total).

Diagram 1: Top Five Industries by Countries/Regions

	1st	2nd	3rd	4th	5th
Europe [1011]	Transportation machinery parts (automobiles, motorcycles) 206 (20.4%)	General machinery (including parts, molds and machinery tools) 144 (14.2%)	Chemical/petrochemical products 89 (8.8%)	Electric and electronic parts 88 (8.7%)	Electric and electronic machinery 84 (8.3%)
Western Europe [766]	General machinery (including parts, molds and machinery tools) 121 (15.8%)	Transportation machinery parts (automobiles, motorcycles) 118 (15.4%)	Chemical/petrochemical products 83 (10.8%)	Other manufacturing 67 (8.7%)	Electric and electronic machinery 61 (8.0%)
UK [197]	Transportation machinery parts (automobiles, motorcycles) 44 (22.3%)	General machinery (including parts, molds and machinery tools) 37 (18.8%)	Electric and electronic machinery 21 (10.7%)	Other manufacturing 17 (8.6%)	Chemical/petrochemical products 15 (7.6%)
France [117]	Transportation machinery parts (automobiles, motorcycles) 20 (17.1%)	Food products, agricultural and fisheries product processing 18 (15.4%)	General machinery (including parts, molds and machinery tools) 18 (15.4%)	Chemical/petrochemical products 11 (9.4%)	Electric and electronic machinery 10 (8.5%)
Germany [151]	General machinery (including parts, molds and machinery tools) 27 (17.9%)	Other manufacturing 22 (14.6%)	Electric and electronic parts 18 (11.9%)	Chemical/petrochemical products 17 (11.3%)	Precision machinery and optical devices 14 (9.3%)
Central and Eastern Europe [245]	Transportation machinery parts (automobiles, motorcycles) 88 (35.9%)	Electric and electronic parts 39 (15.9%)	General machinery (including parts, molds and machinery tools) 23 (9.4%)	Electric and electronic machinery 23 (9.4%)	Ceramics, soil and stone 13 (5.3%)
Czech Republic [87]	Transportation machinery parts (automobiles, motorcycles) 33 (37.9%)	Electric and electronic parts 18 (20.7%)	Ceramics, soil and stone 8 (9.2%)	General machinery (including parts, molds and machinery tools) 8 (9.2%)	Electric and electronic machinery 8 (9.2%)
Poland [72]	Transportation machinery parts (automobiles, motorcycles) 20 (27.8%)	General machinery (including parts, molds and machinery tools) 10 (13.9%)	Electric and electronic machinery 9 (12.5%)	Other manufacturing 7 (9.7%)	Electric and electronic parts 6 (8.3%)

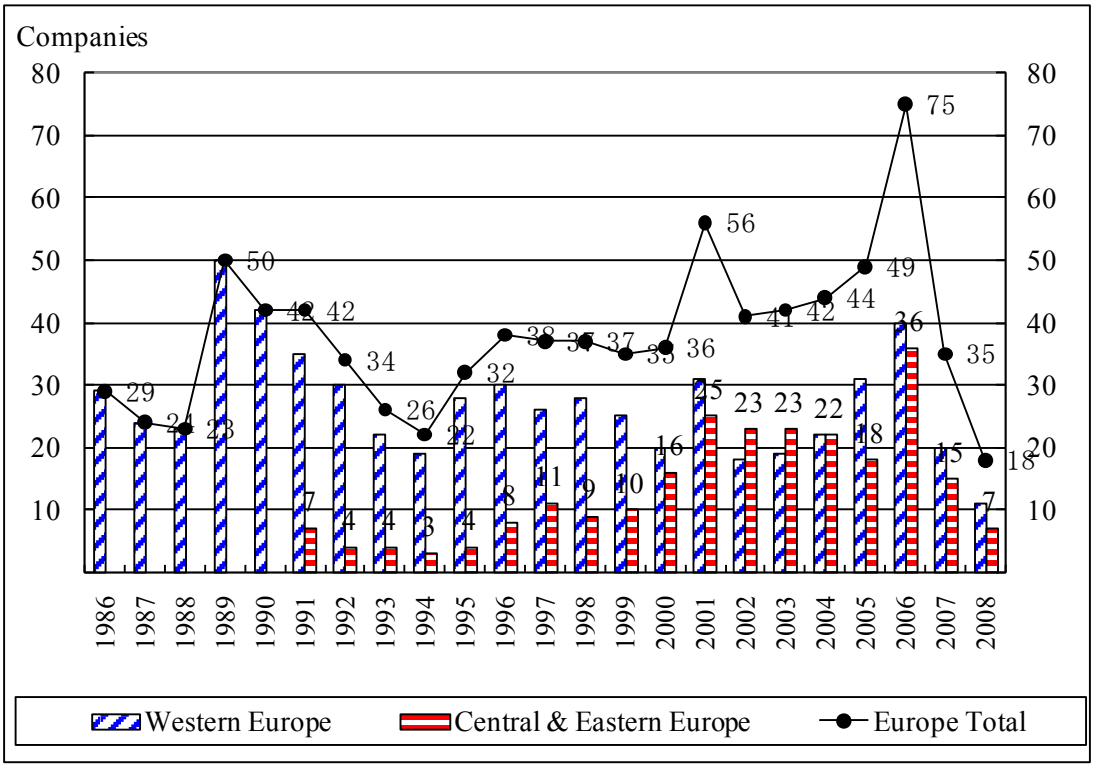
Source: JETRO Survey, Japan External Trade Organization

2. Only 18 new affiliates established in 2008—the lowest in history

During 2008, 18 Japanese manufacturing affiliates were established in Europe (11 in Western Europe and seven in Central and Eastern Europe), which was only half of the 35 affiliates established in 2007 (20 in Western Europe and 15 in Central and Eastern Europe). By country, the largest number of affiliates was established in Germany with six companies, followed by Czech Republic with three, and Denmark and Poland both with two. Thus, it seems the growing trend of operating affiliates in Central and Eastern Europe since the end of the 1990s has now reached a turning point. By industry, four general machinery manufacturing affiliates and three transportation machinery parts affiliates were established.

On the other hand, 13 Japanese manufacturing affiliates were closed in 2008, three in both the UK and Germany, and two both in Ireland and France. By industry, two affiliates in the area of chemical/petrochemical products, electric and electronic machinery, and transportation machinery parts each withdrew from business.

Diagram 2: Changes in the Number of Japanese Manufacturing Affiliates Established in Europe

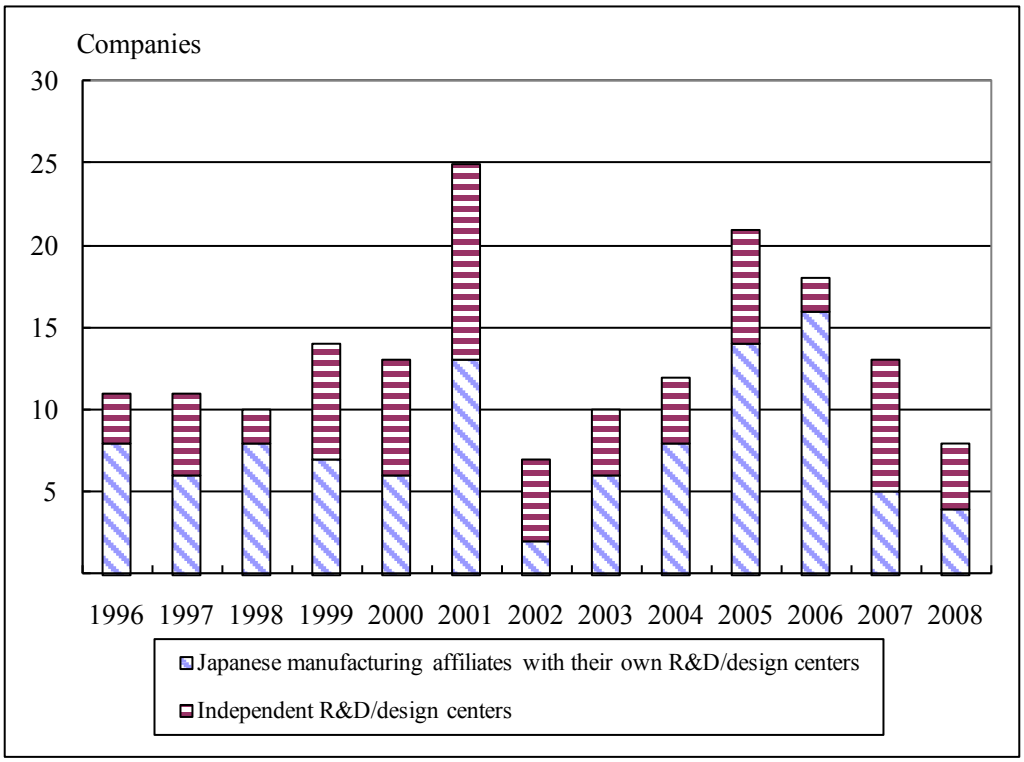


Source: JETRO Survey, Japan External Trade Organization

3. Concentration of R&D and design centers in Western Europe

At the end of 2008, 425 Japanese manufacturing affiliates in Europe had R&D and design centers, out of which 150 operated independent R&D and design centers. Out of these 425 companies, 409 affiliates, or 96.2%, had established R&D and design centers in Western Europe, and only 16, or 3.8%, had established such facilities in Central and Eastern Europe. By country, Germany had the most facilities with 128, followed by the UK (126) and France (39). In 2008, eight R&D and design centers were established in Europe, with the majority of them in Germany (with five facilities).

Diagram 3: Number of R&D and Design Centers Established by Year



Source: JETRO Survey, Japan External Trade Organization

II. Business Conditions and Prospects of Japanese Manufacturing Affiliates in Europe

[2008 operating profit]

- Of the Japanese manufacturing affiliates in Europe, 57.1% recorded operating "profit" for 2008, while 34.9% recorded operating "loss". For Japanese manufacturing affiliates in Western Europe, 59.8% recorded operating "profit" with 33.4% recording operating "loss". As for those in Central and Eastern Europe, 46.8% recorded "profit", while 40.3% recorded "loss".

[Operating profit forecast in 2009 and 2010]

- For 2009, 34.0% of the Japanese manufacturing affiliates in Europe forecasted "profit" and 43.2% predicted "loss", while in Western Europe, 33.8% of the Japanese manufacturing affiliates forecasted "profit", while 41.9% forecasting "loss". For those in Central and Eastern Europe, 35.1% projected "profit" and 48.1% projected "loss". Both in Western and Central/Eastern Europe, more affiliates are projecting "loss" and fewer seem to expect "profit", continuing the trend of the previous year.
- For 2010, 55.9% of the Japanese manufacturing affiliates in Europe forecasted "profit" and 10.4% predicted "loss", while in Western Europe, 55.7% of the Japanese manufacturing affiliates forecasted "profit", while 10.0% forecasted "loss". For those in Central and Eastern Europe, 56.6% forecasted "profit" and 11.8% predicted "loss", i.e., both in Western and Central/Eastern Europe, the affiliates are predicting dramatic recovery in 2010.

[Year-on-year comparison—operating profit in 2008]

- For all of Europe in 2008, 23.4% of the companies answered that their operating profit had "improved" as compared to the previous year (2007), while 61.8% said it had "declined". The major reasons that operating profit in 2008 had "improved" were: "increased sales in overseas markets", "increased sales in domestic market" and "improvements in productivity"; while the main reasons it "declined" were: "global economic downturn stemming from financial crisis", "decreased sales in overseas markets" and "decreased sales in domestic market".

[Year-on-year comparison—operating profit in 2009]

- For 2009, 25.8% predicted that their operating profit will "improve", while 55.1% predicted a "decline". The major reasons for the improvement were a "reduction in personnel costs", "reduction in administrative and utility costs" and "improvements in productivity", while the main reasons for the "decline" were "global economic downturn stemming from financial crisis", "decreased sales in domestic market" and "decreased sales in overseas markets".

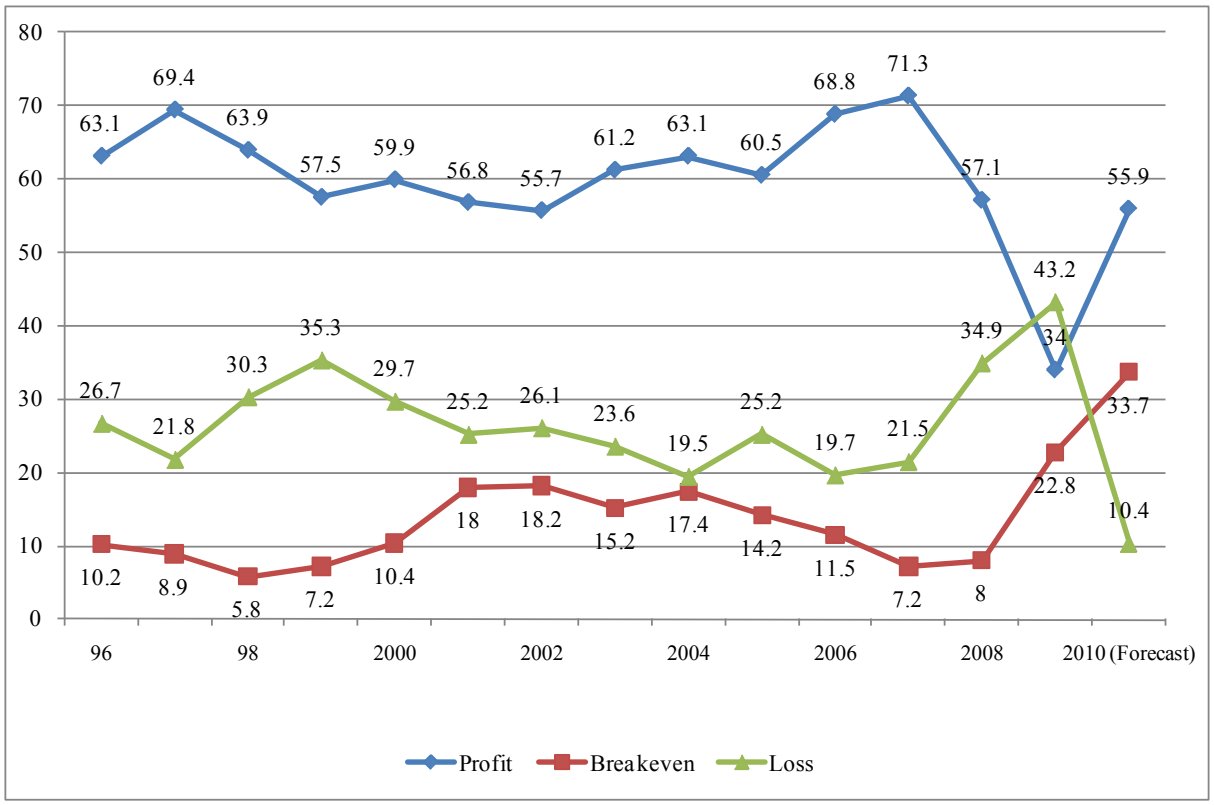
1. Operating "profit" projected by 57.1%, "loss" by 34.9% for 2008

With regard to inquiries about operating profit for 2008, 57.1% of the Japanese manufacturing affiliates in Europe replied that they recorded "profit" (up 14.2 percentage points from the previous year), while 8.0% replied "breakeven" (up 0.8 points) and 34.9% replied that they recorded "loss" (up 13.4 percentage points). For 2008, the number of companies recording profit dramatically declined, while the companies running loss increased significantly, due to such reasons as the spike in energy prices at the beginning of the year and the global economic downturn triggered by the financial crisis in September.

Also for the survey this time, in addition to the forecast of the operating profit of the next year, 2009, where business performance is expected to deteriorate due to the economic downturn caused by the financial crisis, inquiries were also made for forecasts concerning the operating profit for 2010, in order to measure the future prospects of the Japanese manufacturing affiliates in Europe regarding the economic slowdown. The result shows that the impact of the economic downturn is still predicted to be substantial in 2009 (34.0% of the companies forecasted "profit" in 2009, while 22.8% replied "breakeven" and 43.2% predicted "loss"). On the other hand, concerning 2010, 55.9% forecasted "profit", 33.7% replied "breakeven" and only 10.4% predicted "loss". The number of companies reporting "profit" is actually expected to increase to the 2008 level, after the slump seen in 2009 (see Diagram 4).

Diagram 4: Operating Profit for Japanese Manufacturing Affiliates in Europe

(%)

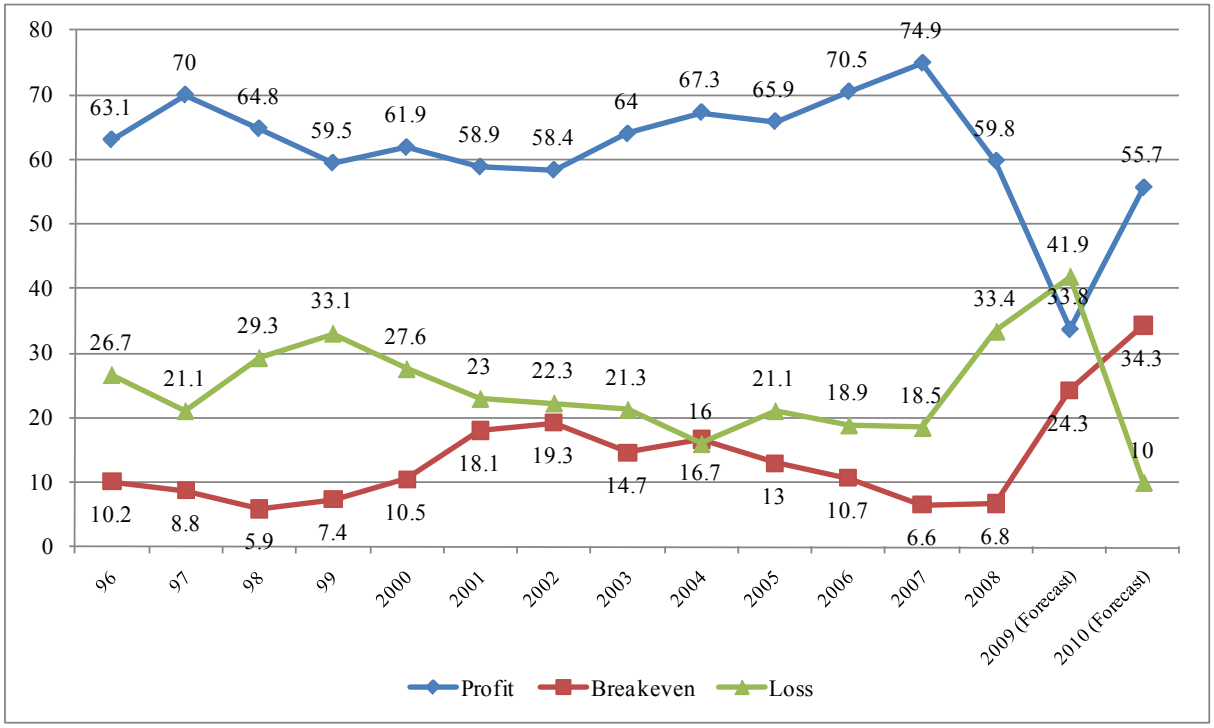


Source: JETRO Survey, Japan External Trade Organization

The trend concerning the forecast of operating profit is more or less the same throughout Europe. For the

Japanese manufacturing affiliates in Western Europe, 59.8% replied “profit” (down 15.1 percentage points from the previous year), 6.8% replied “breakeven” (up 0.2 percentage points) and 33.4% replied “loss” (up 14.9 percentage points), i.e., the trend of the reduction rate of profitable companies and increase rate of loss-reporting companies is the same as that for all of Europe. With regard to predictions for operating profit in 2009, 33.8% replied “profit”, 24.3% cited “breakeven” and 41.9% replied “loss”; however, companies are expecting recovery in 2010, as shown by the answers that 55.7% predicted “profit”, 34.3% replied “breakeven” and 10.0% answered “loss” (see Diagram 5).

Diagram 5: Operating Profit for Japanese Manufacturing Affiliates in Western Europe



Source: JETRO Survey, Japan External Trade Organization

A country-by-country breakdown in Western Europe shows that a large portion of companies recorded profit in the Netherlands, Belgium and Finland (in the order of the percentage of companies that replied “profit”) in 2008; while for the “loss”, Austria, Sweden and Demark were dominant (in the order of the percentage of companies that replied “loss”) (see Diagram 6).

Diagram 6: Operating Profit by Country in Western Europe (2008)

Countries with the most "profit" answers (%)

	Profit	Loss
Netherlands	80.0	16.0
Belgium	68.0	25.0
Finland	66.7	33.3

Countries with the most "loss" answers (%)

	Profit	Loss
Austria	25.0	75.0
Sweden	25.0	75.0
Denmark	28.6	71.4

Source: JETRO Survey, Japan External Trade Organization

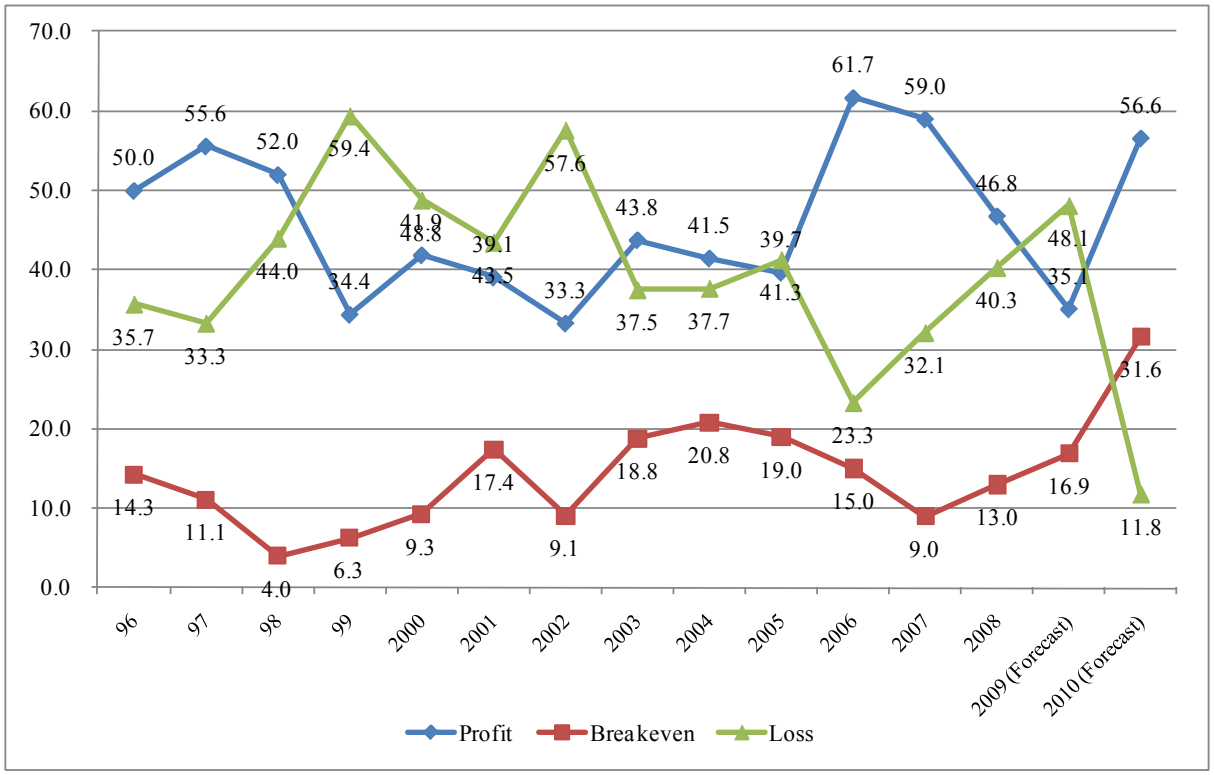
As for the industry breakdown, the top three industries where Japanese manufacturing affiliates are dominant in this area are transportation machinery parts (profit: 48.1%; loss: 40.7%), general machinery (profit: 68.1%; loss: 23.4%), and chemical/petrochemical products (profit 78.8%; loss: 18.2%).

On the other hand, as for the operating profit forecast for 2008 by the Japanese manufacturing affiliates in Central and Eastern Europe, 46.8% replied "profit" (down 12.2 percentage points from the previous year), 13.0% replied "breakeven" (up 4.0 percentage points) and 40.3% replied "loss" (up 8.2 percentage points). While the margins of the decline in "profit" and the increase in "loss" are smaller than those of Western Europe, the percentage of the affiliates that replied "profit" was lower than that in Western Europe by 13.0 percentage points, and the percentage of affiliates that replied "loss" was larger than that in Western Europe by 6.9 percentage points. As for the operating forecasts for 2009, 35.1% replied "profit", 16.9% replied "breakeven" and 48.1% predicted "loss", reflecting their gloomy business prospects affected by the continuing economic downturn, which was also witnessed by companies in Western Europe. On the other hand, in 2010, the companies expect recovery that will be better than that of their Western counterparts, which they actually expect to be much better than 2008, as shown by the data that 56.6% of the respondents replied "profit", 31.6% replied "breakeven" and 11.8% predicted "loss". The companies that replied profit increased by 9.8 percentage points from 2008, while those that replied "loss" decreased by 28.5 percentage points (see Diagram 7).

A country-by-country breakdown in Central and Eastern Europe shows that the largest portion of companies recorded "profit" in the Czech Republic for 2008 (profit: 57.9%; loss: 36.8%), while the largest percentage of companies replied "loss" in Romania (profit: 37.5%; loss: 50.0%).

As for the industry breakdown, the top three industries where Japanese manufacturing affiliates are dominant in this area are transportation machinery parts (profit: 56.3%; loss: 31.3%), electric and electronic parts (profit: 44.4%; loss: 44.4%), and electric and electronic machinery (profit: 33.3%; loss: 0.0%).

Diagram 7: Operating Profit for Japanese Manufacturing Affiliates in Central and Eastern Europe



Source: JETRO Survey, Japan External Trade Organization

2. Companies reporting "declined" operating profit for 2008 due to the "global financial crisis" increased dramatically

The companies replying that their operating profit "improved" in 2008 compared to the previous year (2007) accounted for 23.4% for all of Europe, which was a significant decline (down 27.7 percentage points) from the previous survey where 2007 operating profit was compared to 2006. The companies that replied "remained the same" was 14.8% (down 6.2 percentage points from the previous survey), and the companies that replied "declined" significantly increased to 61.8% (up 33.9 percentage points)

By industry in all of Europe, a large portion of companies replied that their operating profit "improved" in the area of timber/wood products (excluding furniture and interior goods), pharmaceutical products, food products, and agricultural and fisheries product processing—industries not easily affected by economic slowdown. On the other hand, responses mentioning "declined" were conspicuous in the areas of ceramics, soil and stone, rubber products, nonferrous metal, and electric and electronic parts.

Diagram 8: Industries Where "Improved" or "Declined" Replies Concerning Operating Profit Were Dominant (Europe Total, 2008)

Industries with the most "improved" answers (%)

	Improved	Declined
Timber/wood products	60.0	40.0
Pharmaceutical products	58.3	16.7
Food products, agricultural and fisheries product processing	33.3	47.6

Industries with the most "declined" answers (

	Improved	Declined
Ceramics, soil and stone	0.0	100.0
Rubber products	9.1	81.8
Nonferrous metal	20.0	80.0

Source: JETRO Survey, Japan External Trade Organization

For the "improved" replies of operating profit in 2008 (multiple answers allowed), the biggest reason was "increased sales in overseas markets" (54.0%), followed by "increased sales in domestic market" (40.2%) and "improvements in productivity" (35.6%). Responses of an "increase in sales prices" were also considerable (32.2%).

On the other hand, reasons for mentioning "declined" (multiple answers allows) included: the "global economic downturn stemming from financial crisis" (76.5%), which was the most frequently cited answer, followed by "decreased sales in overseas markets" (57.0%) and "decreased sales in domestic market" (52.2%). This indicates that the global economic slowdown triggered by the financial crisis in September 2008 and its resulting decline in demand and consumption, both in domestic and overseas markets, caused a drop in sales, which negatively impacted overall operating profit.

By region, the percentage of the Japanese manufacturing affiliates in Western Europe that answered that their operating profit in 2008 had "improved" from the previous year was 25.0%, which was a significant decrease from the previous survey by 29.2 percentage points. The margin of drop was larger than that of all of Europe. The companies that answered "remained the same" was 14.2%, down 5.0 percentage points from the previous survey, and those that replied "declined" increased dramatically to 60.8%, up 34.2 percentage points from the previous year. The margin of increase was also larger than that of all of Europe (see Diagram 10).

The country-by-county breakdown shows that Austria, Switzerland and Denmark were the top three countries where the percentage of the companies that replied "improved" was high. On the other hand, the top three answering "declined" were Portugal, France and the UK.

By industry, a large portion of companies replied that their operating profit had "improved" in the area of timber/wood products (excluding furniture and interior goods), pharmaceutical products and precision machinery—the result was similar to that of all of Europe. On the other hand, the "declined" responses were conspicuous in the areas of ceramics, soil and stone, nonferrous metal, electric and electronic parts, and plastic products.

Diagram 9: Countries/Industries Where "Improved" or "Declined" Replies Concerning Operating Profit Were Dominant (Western Europe, 2008)

Countries with the most "improved" answers (%)

	Improved	Declined
Austria	75.0	25.0
Switzerland	60.0	20.0
Denmark	57.1	14.3

Countries with the most "declined" answers (%)

	Improved	Declined
Portugal	0.0	87.5
France	13.2	67.9
UK	20.3	65.6

Industries with the most "improved" answers (%)

	Improved	Declined
Timber/wood products	60.0	40.0
Pharmaceutical products	58.3	16.7
Precision machinery	44.4	22.2

Industries with the most "declined" answers (%)

	Improved	Declined
Ceramics, soil and stone	0.0	100.0
Nonferrous metal	20.0	80.0
Electric and electronic parts	15.8	78.9

Source: JETRO Survey, Japan External Trade Organization

As a reason for "improved" operating profit in 2008, the affiliates in Western Europe most frequently mentioned "increased sales in overseas markets" (54.1%), followed by "increased sales in domestic market" (39.2%), which are also the No. 1 and 2 reasons for all of Europe. The third reason was an "increase in sales prices" (35.1%). The top three reasons for a "declined" operating profit are also the same as those in all of Europe, which consisted of: "global economic downturn stemming from financial crisis" (79.4%), "decreased sales in domestic market" (58.9%) and "decreased sales in overseas markets" (55.0%) (multiple answers allowed) (see Diagram 9).

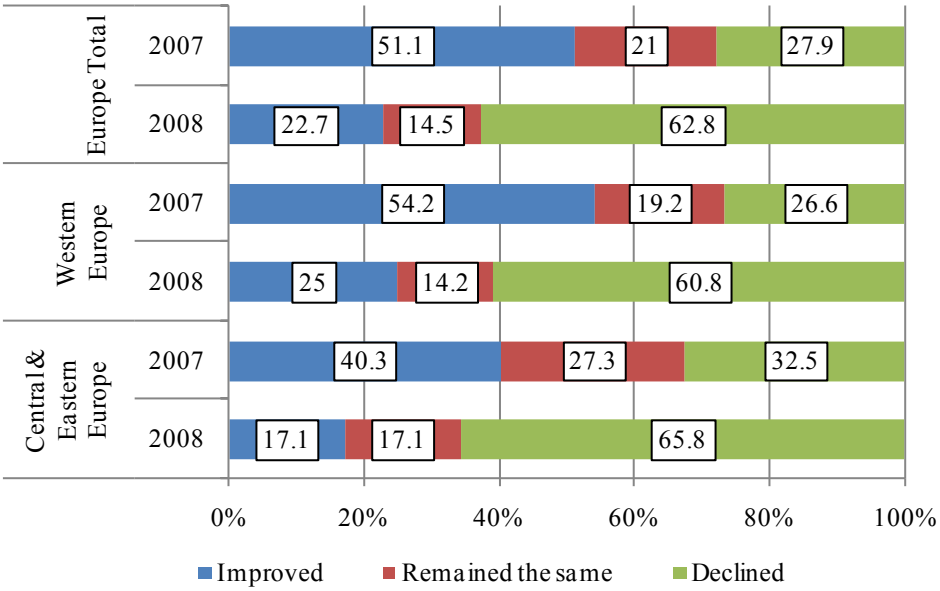
For Japanese manufacturing affiliates in Central and Eastern Europe, 17.1% said that their operating profit had "improved" in 2008, compared to the previous year (2007), which is 23.2 percentage points down from the previous survey, showing a smaller drop as compared to counterparts in Western Europe and all of Europe, including Western Europe. Replies consisting of "remained the same" were at 17.1% (down 10.2 percentage points from the previous year), while 65.8% replied "declined", which is a significant increase of 35.0 percentage points since the previous year, showing a larger increase than what was seen in all of Europe, again including Western Europe (see Diagram 10).

As for the country-by-country breakdown, many companies in the Czech Republic answered that their operating profit had "declined" (improved: 10.5%; declined: 78.9%), and the same can be said for Hungary (improved: 20.0%; declined: 73.3%) and Poland (improved: 13.0%; declined: 69.6%). The data also shows that some countries, such as Lithuania and Hungary, are heavily affected by the financial crisis.

As for the top three industry bases for Japanese manufacturing affiliates in Central and Eastern Europe, 19.4% replied improved and 71.0% cited declined for transportation machinery parts (automobiles, motorcycles), 0.0% replied improved and 77.8% cited declined for electric and electronic parts, and 20.0% replied improved and 60.0% said declined for general machinery. In the area of electric and electronic parts, while investment and sales in the area of LCD televisions have dramatically increased in recent years, with the transition to digital broadcasting, which had already started in parts of Europe, the operating profit of such industry is expected to drop in 2009 after TV set replacement reaches the saturation point.

The main reasons for the "improved" operating profit of the Japanese manufacturing affiliates in Central and Eastern Europe in 2008 were "improvements in productivity" and "increased sales in overseas markets" (58.3% respectively) (multiple answers allowed), which were followed by "increased sales in domestic market" (46.2%). On the other hand, the main reasons for stating "declined" were "global economic downturn stemming from financial crisis" (66.0%), "decreased sales in overseas markets" (64.0%) and "foreign exchange losses" (58.0%), which were the same in Western Europe. It is also noteworthy that the fourth reason for the decline in this area was an "increase in personnel costs" (32.0%). Personnel costs also increased in Central and Eastern Europe, along with all of Europe as a whole, and the trend seems to be continuing even now (see Diagram 11).

Diagram 10: Operating Results for Japanese Manufacturing Affiliates in Europe (Compared to the Previous Year)



Source: JETRO Survey, Japan External Trade Organization

Diagram 11: Top Reasons for Improvement (Decline) in Operating Profit in 2008

(Multiple Answers Allowed)

Reasons for "Improvement" of Operating Profit in 2008
(Multiple responses allowed)

Japanese Manufacturing Affiliates in Western Europe

Reason	No. of responses	%
Increased sales in overseas markets	40	54.1
Increased sales in domestic market	29	39.2
Increase in sales prices	26	35.1
Improvements in productivity	24	32.4
Reduction in personnel costs, Foreign exchange gains (same score)	16	21.6

Reasons for "Decline" of Operating Profit in 2008
(Multiple responses allowed)

Japanese Manufacturing Affiliates in Western Europe

Reason	No. of responses	%
Global economic downturn stemming from financial crisis	143	79.4
Decreased sales in domestic market	106	58.9
Decreased sales in overseas markets	99	55.0
Foreign exchange losses	70	38.9
Fall in sales prices	43	26.7

Japanese Manufacturing Affiliates in Central and Eastern Europe

Reason	No. of responses	%
Increased sales in overseas markets, Improvements in productivity (same score)	7	53.8
Increased sales in domestic market	6	46.2
Reduction in personnel costs	4	30.8
Reduction in importing procurement costs, Foreign exchange gains (same score)	3	23.1

Japanese Manufacturing Affiliates in Central and Eastern Europe

Reason	No. of responses	%
Global economic downturn stemming from financial crisis	33	66.0
Decreased sales in overseas markets	32	64.0
Foreign exchange losses	29	58.0
Increase in personnel costs	16	32.0

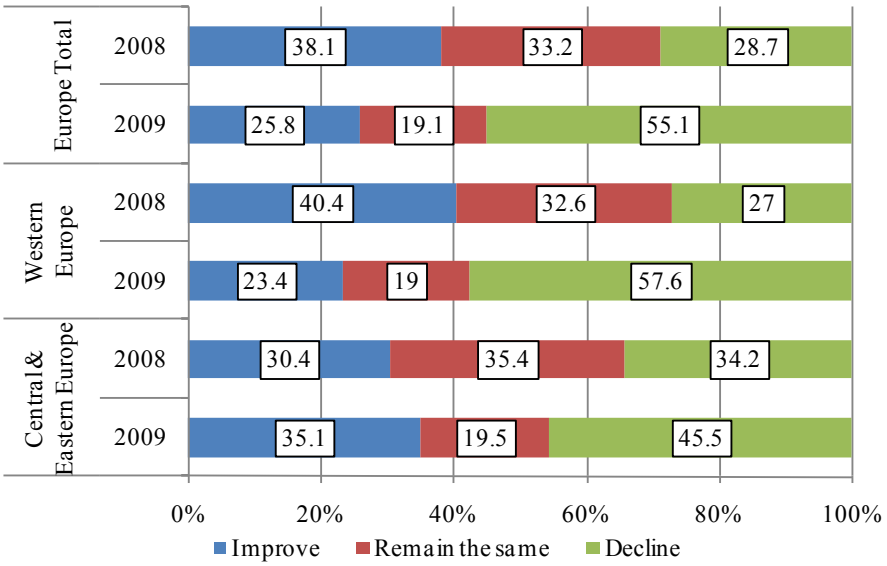
Source: JETRO Survey, Japan External Trade Organization

3. Further decline predicted for 2009, yet recovery expected for 2010

To inquiries pertaining to the outlook for operating profit in 2009 as compared to 2008, 25.8% of the Japanese manufacturing affiliates answered that it would “improve”, while 55.1% answered that it would “decline”. Breaking it down into Western and Central/Eastern Europe shows that, in Western Europe, an improvement was projected by 23.4%, while a decline was projected by 57.6%. In Central and Eastern Europe, improvement was projected by 35.1%, while a decline was projected by 45.5%.

As a ground for the prospect that operating profit would “improve” in 2009, the top three reasons were the same for Western Europe, Central and Eastern Europe and for all of Europe itself, consisting of: “reduction in personnel costs”, “reduction in administrative and utility costs” and “improvements in productivity”. This indicates that companies are expecting improvements to their business performance by changing their internal environment for the better, in the midst of the tough external situations that are predicted to continue next year. On the other hand, in Western Europe and Central/Eastern Europe, as well as in all of Europe itself, the top three reasons cited for a “decline” were “global economic downturn stemming from financial crisis”, “decreased sales in domestic market” and “decreased sales in overseas markets” (see Diagram 13). In 2009, companies predict further declines in operating profit due to the continued sales slump, both in domestic and overseas markets, caused by the global financial crisis.

Diagram 12: Operating Profit Forecast for Japanese Manufacturing Affiliates in Europe (Compared to the Previous Year)



Source: JETRO Survey, Japan External Trade Organization

Diagram 13: Top Reasons for Improvement (Decline) in Operating Profit in 2009 (Multiple Answers Allowed)

Reasons for "Improvement" of Operating Profit in 2009 (Multiple Answers Allowed)

Japanese Manufacturing Affiliates in Western Europe

Reason	No. of responses	%
Increased sales in overseas markets	40	54.1
Increased sales in domestic market	29	39.2
Increase in sales prices	26	35.1
Improvements in productivity	24	32.4
Reduction in personnel costs, Foreign exchange gains (same score)	16	21.6

Reasons for "Decline" of Operating Profit in 2009 (Multiple Answers Allowed)

Japanese Manufacturing Affiliates in Western Europe

Reason	No. of responses	%
Global economic downturn stemming from financial crisis	143	79.4
Decreased sales in domestic market	106	58.9
Decreased sales in overseas markets	99	55.0
Foreign exchange losses	70	38.9
Fall in sales prices	43	26.7

Japanese Manufacturing Affiliates in Central and Eastern Europe

Reason	No. of responses	%
Improvements in productivity	20	74.1
Reduction in personnel costs	15	55.6
Reduction in administrative and utility costs	13	48.1
Increased sales in overseas markets, Foreign exchange gains (same score)	9	33.3

Japanese Manufacturing Affiliates in Central and Eastern Europe

Reason	No. of responses	%
Global economic downturn stemming from financial crisis	26	74.3
Decreased sales in overseas markets	25	71.4
Decreased sales in domestic market, Fall in sales prices (same score)	15	42.9
Increase in procurement costs (for imports)	9	25.7

Source: JETRO Survey, Japan External Trade Organization

On the other hand, as for the forecast of the operating profit for 2010 (as compared to 2009), 64.6% of the companies replied that it would “improve”, while 3.6% answered “decline”. By region, 65.6% replied improve and 3.5% said decline in Western Europe, while 60.5% replied improve and 3.9% said decline in Central and Eastern Europe. The companies expect dramatic recovery of operating profit in 2010, after the economy bottoms out in 2009.

III. Procurement, Sales and Production

1. Procurement source of parts and materials and procurement policy

- The number of Japanese manufacturing affiliates in Western Europe that purchase parts and materials in Europe has been increasing. While the number of Japanese manufacturing affiliates in "Central and Eastern Europe" that are sourcing locally (in Central and Eastern Europe) is steadily increasing, the number of companies that procure parts and materials from Japan significantly decreased.
- "China" (45.8%) was the most targeted region to "expand/reinforce" among current procurement sources for Japanese manufacturing affiliates in Western Europe (50 or more companies responded to this inquiry), followed by "Central and Eastern Europe" (45.2%) and "ASEAN" (44.2%) by a small margin. For the Japanese manufacturing affiliates in Central and Eastern Europe, the most targeted region for expansion/reinforcement of future procurement is "Central and Eastern Europe" (71.4%). On the other hand, more than 40% of the respondents answered that they would plan to "decrease" procurement from "Japan".
- Expectations are continuously high for "China" and "Central and Eastern Europe" as future procurement sources (the same trend as the previous survey).

(1) Current procurement sources

The major sources of procurement for parts and materials by Japanese manufacturing affiliates in Western Europe are: "Western Europe" (cited by 85.2%), "Japan" (59.6%), "China" (27.9%), "Central and Eastern Europe" (20.9%), and "ASEAN" (17.5%). There was no change in the above ranking from the previous year (see Diagram 14).

As compared to the previous year, the number of Japanese manufacturing affiliates that procure parts and materials from "Central and Eastern Europe" has increased (up 3.2 percentage points compared to the previous year). While there was no major change for procurement from "ASEAN" (up 0.6 percentage points) and "Western Europe" (up 0.2 points), procurement from "China" (down 1.4 points) and "Japan" (down 2.1 points) has slightly decreased.

Country-by-country characteristics concerning procurement sources are as follows:

U.K.: The ratio of the Japanese manufacturing affiliates that procure parts and materials from "China" is significantly high at 38.5%, similar to the previous year at 42.7%.

Germany: The ratio of companies that procure parts and materials from "Central and Eastern Europe" is large at 37.9%, up by 11.9 percentage points from the previous year (26.0%).

France: The ratio of procurement from "Japan" decreased from 62.5% of the previous year to 45.3%, down by 17.2 percentage points.

Spain: The procurement ratio from "ASEAN" countries (40.7%) is large, up from 28.0% of the previous year by 12.7 percentage points.

The Netherlands: The ratio of procurement from "Western Europe" is significantly high at 96.0%, similar to the previous year at 94.7%.

Major procurement sources by industry are as follows (numbers within parentheses indicate the number of companies that replied [i.e., companies that chose the relevant option] and the percentage of replies [percentage of such choices]):

Transportation machinery parts: Western Europe (48 companies, 88.9%), Japan (34 companies, 63.0%) and China (13 companies, 24.1%).

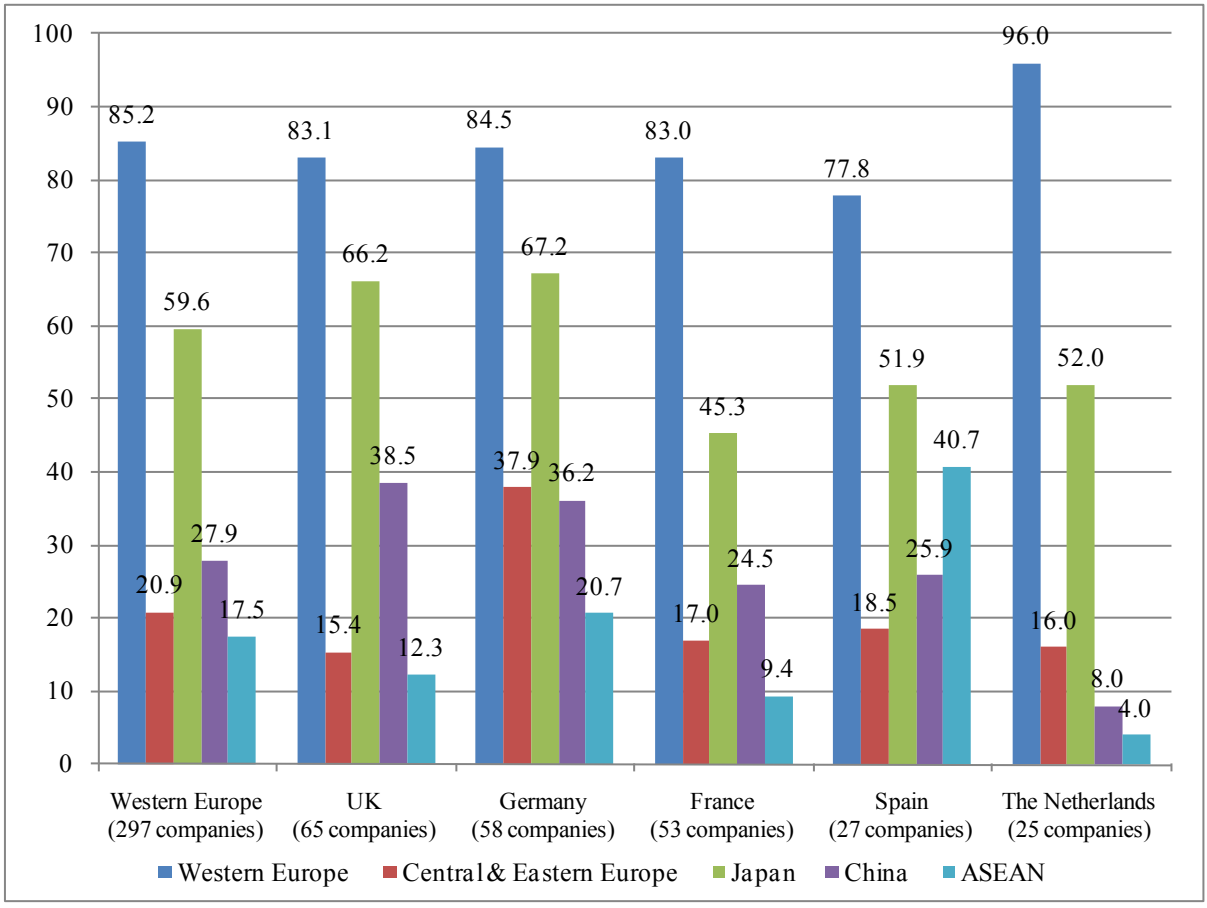
General machinery: Western Europe (39 companies, 83.0%), Japan (29 companies, 61.7%), and Central and Eastern Europe (17 companies, 36.2%).

Chemical/petrochemical products: Western Europe (26 companies, 78.8%), Japan (20 companies, 60.6%) and China (11 companies, 33.3%).

Electric and electronic parts: Western Europe (16 companies, 84.2%), Japan (14 companies, 73.7%) and China (9 companies, 47.4%).

Electric and electronic machinery: Western Europe (14 companies, 73.7%), Japan (12 companies, 63.2%) and China (8 companies, 42.1%).

Diagram 14: Major Procurement Sources of Japanese Manufacturing Affiliates in Western Europe (By Countries/Regions) (Multiple Answers Allowed)



Source: JETRO Survey, Japan External Trade Organization

The major procurement sources of parts and materials for Japanese manufacturing affiliates in Central and Eastern Europe, on the other hand, are: “Western Europe” (cited by 70.1%), “Japan” (64.9%), “Central

and Eastern Europe" (63.6%), and "ASEAN" (27.3%). Only 18.2% of the companies replied that they were sourcing parts and materials from "China" (see Diagram 15). The Japanese manufacturing affiliates that are sourcing locally (in" Central and Eastern Europe") have increased again from the previous year by 2.1 percentage points, after the significant growth (up by 17.4 percentage point) discovered by the previous survey—more and more companies are sourcing locally. On the other hand, Japan, which received the biggest number of responses (78.2%) in the last survey, reduced the responses by 13.3 percentage points, giving its No. 1 place to Western Europe.

Country-by-country characteristics concerning procurement sources are as follows:

Poland: Many companies (39.1%) source parts and materials from "ASEAN" countries, up 12.8 percentage points from the previous year's 26.3%.

Czech Republic: Many companies (78.9%) source parts and materials from "Central and Eastern Europe", up 7.5 percentage points from the previous year's 71.4%; the number of companies that procure parts and materials from Japan decreased by 12.6 percentage points from the previous year.

Hungary: Parts and materials are often sourced from "China", with 31.3% of the companies doing so, which is 10.2 percentage points up from the previous year (21.1%).

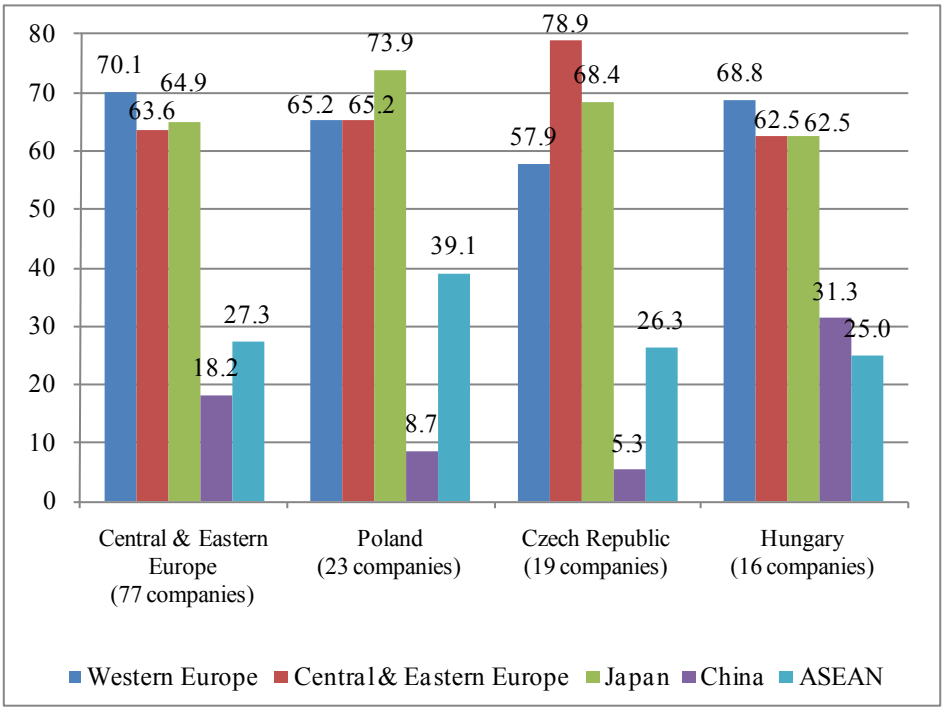
Major procurement sources by industry are as follows (numbers within parentheses indicate the number of companies that replied [i.e., companies that chose the relevant option] and the percentage of replies [percentage of such choices]). As compared to the previous survey, it shows that the number of companies that source from Japan is declining.

Transportation machinery parts: Western Europe (78.1%), Central and Eastern Europe (71.9%) and Japan (71.9%).

Electric and electronic parts: Japan (66.7%), Western Europe (55.6%), and Central and Eastern Europe (55.6%).

Electric and electronic machinery: Central and Eastern Europe (100%), ASEAN (83.3%), and Western Europe and Japan (50.0%, respectively).

Diagram 15: Major Procurement Sources of Japanese Manufacturing Affiliates in Central and Eastern Europe (By Countries/Regions) (Multiple Answers Allowed)



Source: JETRO Survey, Japan External Trade Organization

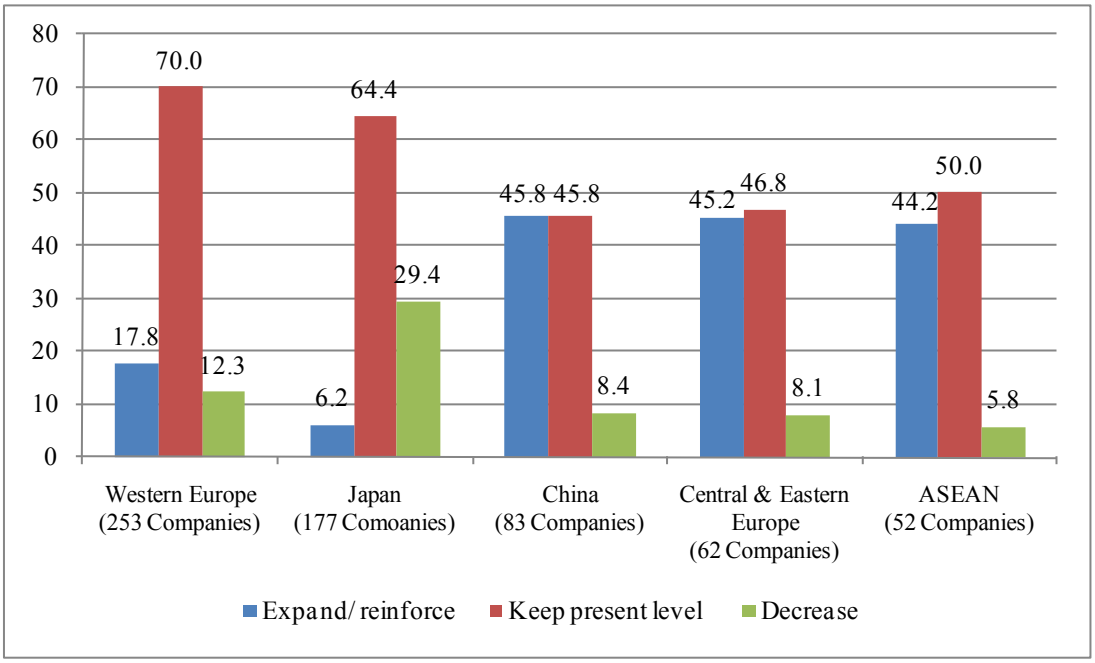
(2) Future procurement policy

Regarding future procurement policy, “China” (45.8%), “Central and Eastern Europe” (45.2%) and “ASEAN” (44.2%) top the list of countries/regions where Japanese manufacturing affiliates operating in Western Europe plan to “expand/reinforce” procurement (50 or more companies responded to this inquiry). “China” has been promoted from the previous third place to the first, although the margin was very small.

With regard to the industries of companies that selected “China”, the transportation machinery parts manufacturers were conspicuous (11 companies, 84.6%). Czech Republic (70.4%) and Poland (48.1%) were the top two countries for “Central and Eastern Europe”.

On the other hand, 29.4% of the companies replied that they will “decrease” procurement from “Japan”. By industry, rubber products (three companies, 100%) and plastic products (four companies, 66.7%) are among the top of the list (see Diagram 16).

Diagram 16: Future Procurement Policies of Japanese Manufacturing Affiliates in Western Europe for Current Major Procurement Sources (Multiple Answers Allowed)



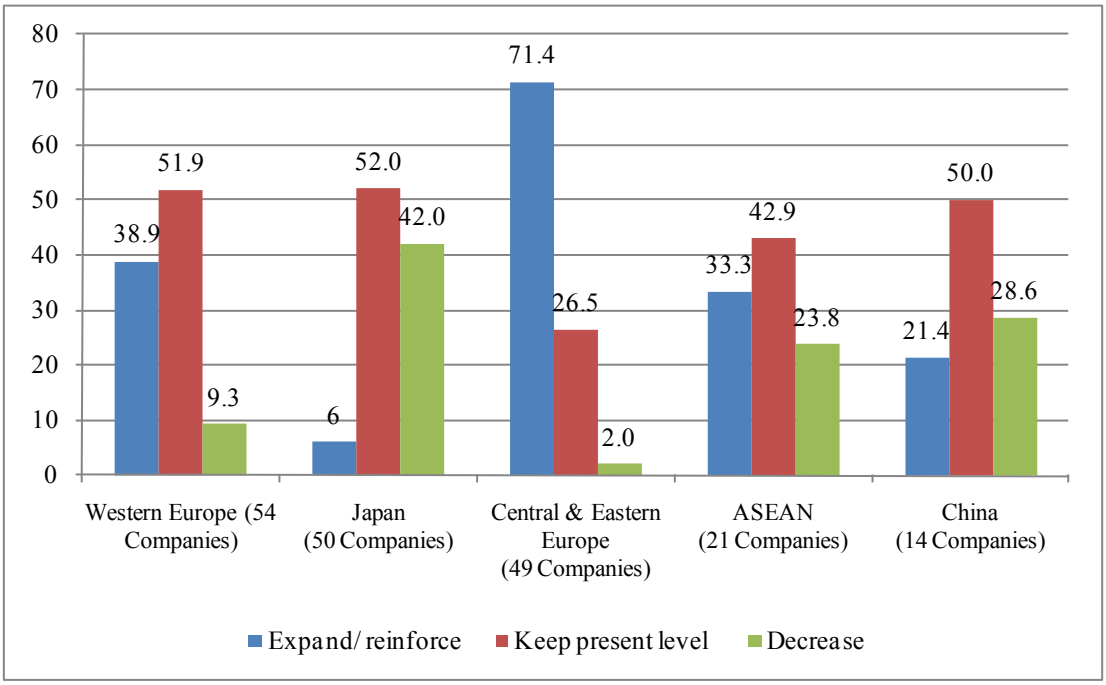
Source: JETRO Survey, Japan External Trade Organization

Regarding future procurement policies from current procurement sources, “Central and Eastern Europe” (71.4%), “Western Europe” (38.9%) and “ASEAN” (33.3%) top the list of countries/regions where Japanese manufacturing affiliates in Central and Eastern Europe plan to “expand/reinforce” procurement. Procurement from “Central and Eastern Europe” is expected to further increase. By industry, the transportation machinery parts manufacturers were conspicuous (17 companies, 73.9%). Meanwhile, the ratio of the companies considering the expansion of procurement from “Western Europe” was 38.9%, although it was only 17.8% among the Japanese manufacturing affiliates in Western Europe. It seems that more affiliates in Central and Eastern Europe plan to promote sourcing within Europe, including procurement from their home area (Central and Eastern Europe).

This makes a contrast with Japanese manufacturing affiliates in Western Europe that are sourcing more and more from “China”. It seems that the procurement sources of parts and materials shifted to Central and Eastern Europe, where related industries are concentrated to specific regions.

With regard to procurement from “Japan”, 6.0% have plans to “expand/reinforce” 52.0% plan to” keep present level” and 42.0% plan to “decrease” a reduction. By industry, transportation machinery parts manufacturers are conspicuous (12 companies, 52.2%) among the companies that replied “decrease”, supporting the above-mentioned fact that the procurement sources of the Japanese manufacturing affiliates in Central and Eastern Europe are shifting toward Europe (see Diagram 17).

Diagram 17: Future Procurement Policies of Japanese Manufacturing Affiliates in Central & Eastern Europe for Current Major Procurement Sources (Multiple Answers Allowed)



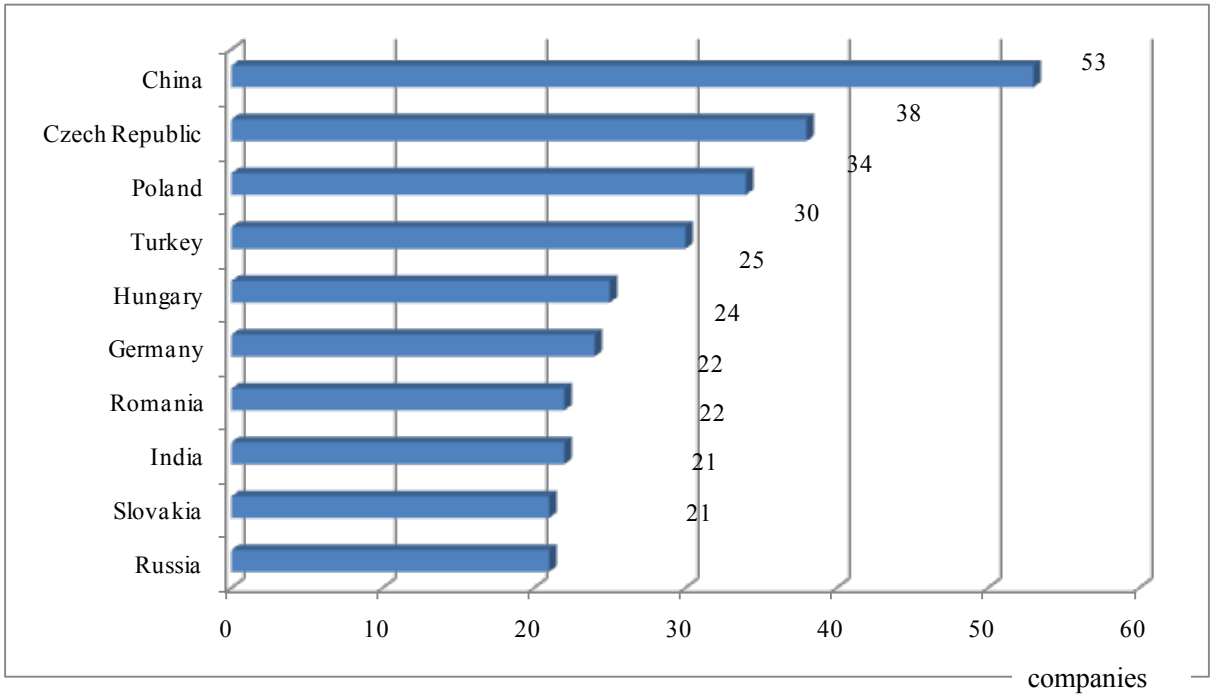
Source: JETRO Survey, Japan External Trade Organization

(3) Future procurement sources

For the countries/regions being considered by Japanese manufacturing affiliates in Europe as future procurement sources (among the countries from where the companies are not currently procuring parts and materials), “China” tops the list with 53 replies, followed by “Czech Republic” with 38, “Poland” with 34, “Turkey” with 30, “Hungary” with 25 and “Germany” with 24 (see Diagram 18).

This result implies that China, as well as Central and Eastern Europe, where concentration of the manufacturing of transportation machinery (automobiles) and related parts, electric and electronic machinery, and electric and electronic parts is progressing, are highly expected to be future procurement sources.

Diagram 18: Countries Considered by Japanese Manufacturing Affiliates in Europe as Candidates for Future Procurement Sources



Source: JETRO Survey, Japan External Trade Organization

2. Sales destinations and sales policies

- While the market of the products made by Japanese manufacturing affiliates in Western Europe is mainly "Western Europe", the manufacturers in Central and Eastern Europe focus on the markets in "Central and Eastern Europe", as well as "Western Europe".
- Japanese manufacturing affiliates in Europe are planning to "expand/reinforce" their sales in "Russia and CIS countries", as well as in "Central and Eastern Europe" and "Turkey". Also at the top of the list are: "India", "China" and "North Africa", although the number of companies that cited these countries/regions were not very large.
- While many Japanese manufacturing affiliates in Western Europe selected the emerging markets, such as "Russia and CIS countries", "Central and Eastern Europe" and "North Africa" as the target to expand/reinforce their sales, those in Central and Eastern Europe selected the answer to "expand/reinforce" for almost all markets of the major countries/regions, including "Western Europe".
- Russia has been the number one target for the future market for three consecutive years.

(1) Current sales destinations

Currently, Western Europe (cited by 93.3%) was the most cited answer by Japanese manufacturing affiliates in Western Europe as a sales market, followed by "Central and Eastern Europe" (39.1%), "Russia and CIS countries" (24.6%), "Turkey" (18.2%), "North America" (18.2%) and "Japan" (17.2%). There was no major change in the ranking from the previous year.

For Japanese manufacturing affiliates in Central and Eastern Europe, most of the sales are to "Western Europe" (75.3%), "Central and Eastern Europe" (67.5%), "Russia and CIS countries" (14.3%) and "Turkey" (14.3%). The ranking was the same as that of the previous year.

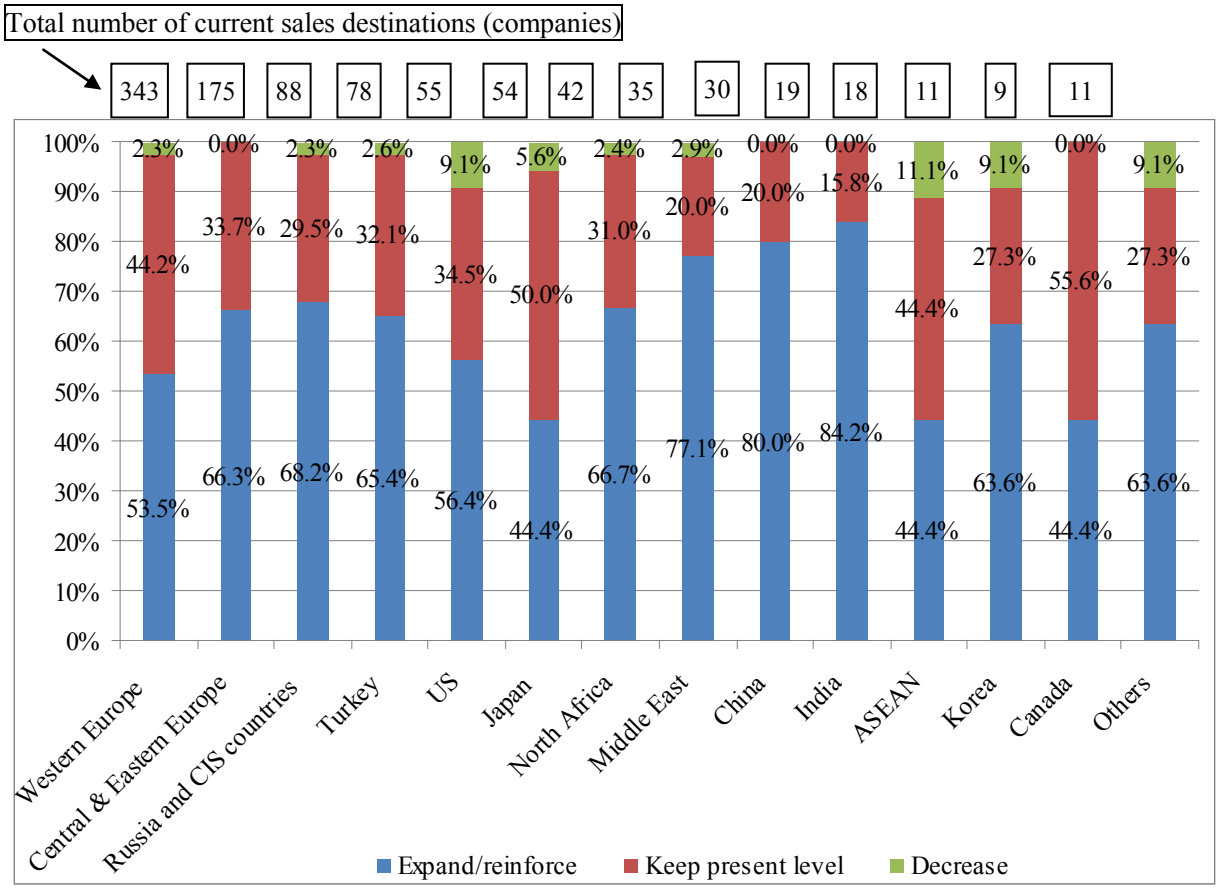
(2) Future sales policies

With regard to future sales policies for the current sales destinations, many Japanese manufacturing affiliates in Europe plan to "expand/reinforce" their sales in "Russia and CIS countries" (cited by 57 companies or 67.9%), followed by "Central and Eastern Europe" (113 companies, 67.3%) and "Turkey" (40 companies, 61.5%). Although the number of companies was not very large, the response rate was high for "India" (16 companies, 84.2%), "China" (24 companies, 80.0%), the "Middle East" (25 companies, 75.8%) and "North Africa" (25 companies, 65.8%) (see Diagram 19).

For the Japanese manufacturing affiliates in Western Europe, many answered that they will "expand/reinforce" sales in emerging markets, such as "Russia and CIS countries" (49 companies, 67.1%), "Central and Eastern Europe" (77 companies, 66.4%), "North Africa" (22 companies, 64.7%) and "Turkey" (32 companies, 59.3%). Although many Japanese manufacturing affiliates in Western Europe have strong interest to expand/reinforce their sales in Central and Eastern Europe, as well as Russia and CIS countries, only less than half (49.5%) plan to expand/reinforce their sales in the market in Western Europe. By industry, the companies in the "chemical/petrochemical products", "electric and electronic machinery", and "electric and electronic parts" industries are active in their sales to "expand/reinforce".

On the other hand, for Central and Eastern Europe overall, a high percentage of companies consider to "expand/reinforce" their sales to major markets including "Western Europe" (75.9%), "North Africa" (75.0%), "Russia and CIS countries", "Turkey" (72.7%), and "Central and Eastern Europe" (69.2%). This indicates that Japanese manufacturing affiliates in Central and Eastern Europe are aggressive to "expand/reinforce" their existing sales channels. The by-industry data also shows the generally high interest to "expand/reinforce" their sales activities.

Diagram 19: Future Sales Policies of Japanese Manufacturing Affiliates in Western Europe for Current Major Sales Destinations (Multiple Answers Allowed)



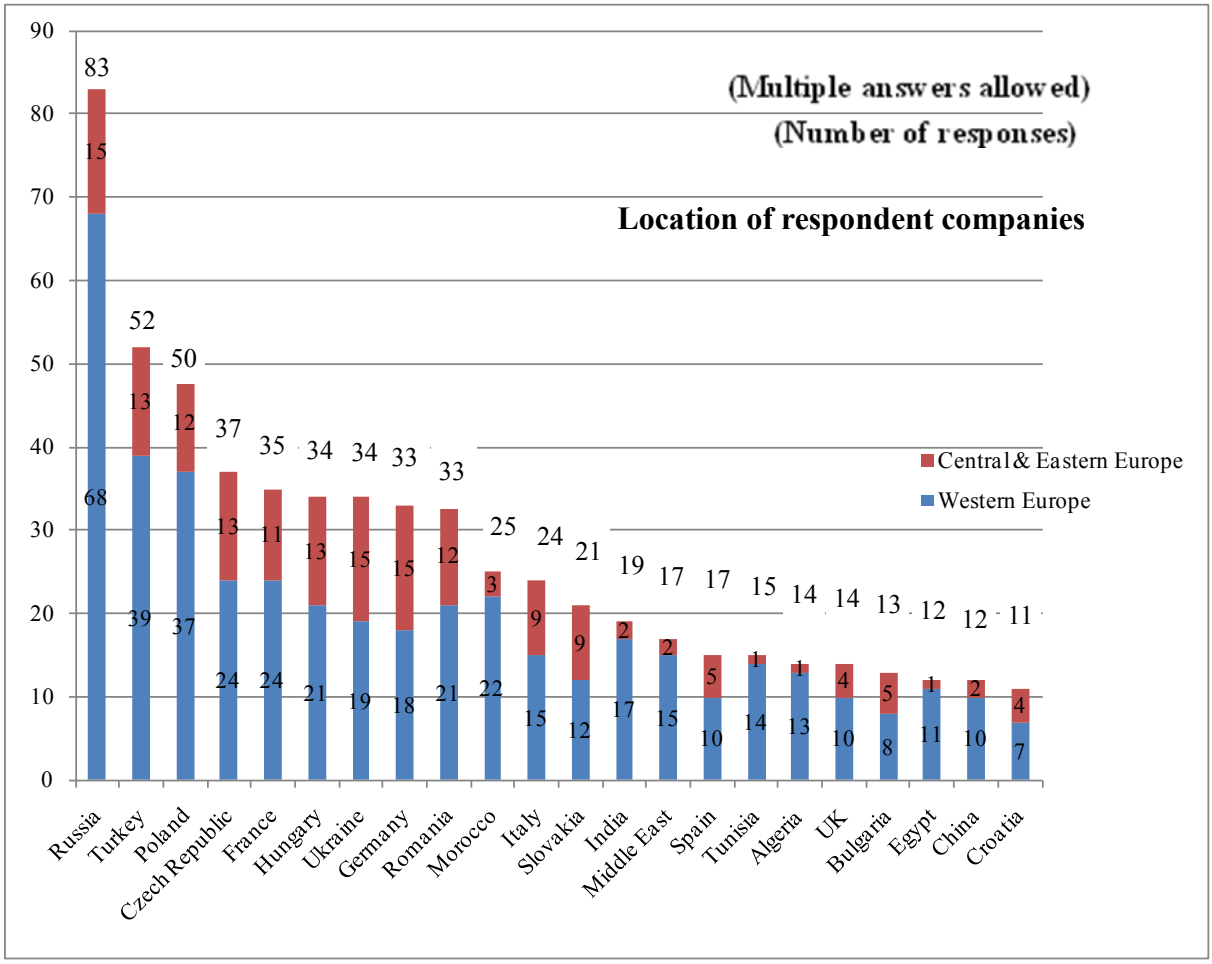
Source: JETRO Survey, Japan External Trade Organization

(3) Future sales destinations

As for the countries/regions that are currently not included in sales destinations but that are being considered for future sales destinations, Russia came first (83 companies, 39.2%) for three consecutive years, followed by Turkey (52 companies, 24.5%), Poland (50 companies, 23.1%), the Czech Republic (37 companies, 17.5%), France (35 companies, 16.5%), Hungary (34 companies, 16.0%), Romania and Germany (33 companies and 15.6%, respectively), Morocco (25 companies, 11.8%) and Italy (24 companies, 11.3%). By industry, transportation machinery parts (21 companies), general machinery (11 companies), plastic products (7 companies), and electric and electronic machinery (7 companies) are

among the top of the list (see Diagram 20).

Diagram 20: Countries/Regions Being Considered for Future Sales Destinations



Source: JETRO Survey, Japan External Trade Organization

Responses to the questions concerning "(2) Future sales policy (for the established sales destinations)" and "(3) (Countries/regions being considered as candidates for) future sales destinations" mentioned above clearly indicate that Japanese manufacturing affiliates in Europe, as was the case last year, have high expectations for sales in the rapidly growing Russian market. It was also confirmed that Japanese manufacturing affiliates in Europe are exploring the possibilities of expanding/reinforcing sales in neighboring emerging markets of Central and Eastern Europe, Turkey and North Africa.

3. Production

- For attractions/advantages as production bases in which the company operates, while many Japanese manufacturing affiliates in Western Europe cited “public safety and social conditions”, “high quality of workforce” and “widespread use of English language”, their counterparts in Central and Eastern Europe selected “low labor costs” and “offers strategic location” as top items.
- 28.2% of Japanese manufacturing affiliates in Western Europe and 46.8% of Japanese manufacturing affiliates in Central and Eastern Europe plan “expansion” of their operations in the next 1–2 years. The numbers were lower than those of the previous survey.
- The specific policies/plans for “expansion” by Western and Central/ Eastern Europe include the curtailment of additional investment in the midst of declined demand caused by the financial crisis and the operational expansion through the “expansion/diversification of product lines”.
- Promising production bases in the mid- to long-term (5–10 years) are Russia, Poland and the Czech Republic, which were also mentioned in the previous year’s survey.

(1) Attractions/advantages of the country in which Japanese manufacturing affiliates operate

For the attractions/advantages of the country (production base) in which Japanese manufacturing affiliates in Western Europe operate , the largest number of companies selected “public safety and social conditions” (44.9%), followed by “high quality of workforce” (35.8%), “widespread use of English language” (32.8%), “political conditions” (30.6%) and “offers strategic location” (28.7%).

On the other hand, the highest number of Japanese manufacturing affiliates in Central and Eastern Europe selected “low labor costs” (46.6%), followed by “offers strategic location” (42.5%), “high quality of workforce” (32.9%), “public safety and social conditions” (31.5%) and the “ease in securing factory workers” (27.4%).

Although 15 items received 20% or more responses among the Japanese manufacturing affiliates in Western Europe, only five were selected by 20% or more affiliates in Central and Eastern Europe. This shows that, while the requirements for the host country (production base) of Japanese manufacturing affiliates in Western Europe are diversified, the attractions/advantages of the above-mentioned five items are much more focused than others in Central and East European countries (see Diagram 21).

Diagram 21: Attractions/Advantages of Production Bases

Attractions/Advantage of the Production Bases (Western Europe) (n=265)

Category	Attractions/Advantage	Responses	%
Political, economic and social conditions	Public safety and social conditions	119	44.9 %
Labor-related	High quality of workforce	95	35.8 %
Others	Widespread use of English language	87	32.8 %
Political, economic and social conditions	Political conditions	81	30.6 %
Others	Offers strategic location	76	28.7 %
Procurement of parts and materials	Quality	71	26.8 %
Investment legislation/procedures	Stable administration of related laws	67	25.3 %
Infrastructure	Port facilities	66	24.9 %
Others	Living environment for foreigners	66	24.9 %
Infrastructure	Airports	62	23.4 %
Others	Well-developed industrial and technological infrastructure	62	23.4 %
Labor-related	Ease in securing multilingual staff	61	23.0 %
Others	Quality of end products	55	20.8 %
Infrastructure	Industrial parks	54	20.4 %
Others	High level of education	54	20.4 %
Labor-related	Ease in securing factory workers	51	19.2 %
Others	Market size	50	18.9 %
Tax systems/procedures	Stable administration of related laws	49	18.5 %
Labor-related	High labor productivity	46	17.4 %
Labor-related	Ease in securing engineers	44	16.6 %
Tax systems/procedures	Corporate tax rates	41	15.5 %
Political, economic and social conditions	Economic conditions	40	15.1 %
Investment legislation/procedures	Easily accessible investment incentive schemes	37	14.0 %
Investment legislation/procedures	Efficient administrative procedures	35	13.2 %
Labor-related	Flexible employment systems	32	12.1 %
Investment legislation/procedures	Visa/work permits easily acquired	31	11.7 %
Procurement of parts and materials	Delivery dates are strictly kept	27	10.2 %
Procurement of parts and materials	Abundant procurement sources	27	10.2 %
Finance	Stable exchange rate	25	9.4 %
Labor-related	Low labor costs	24	9.1 %
Labor-related	Ease in securing managerial personnel	23	8.7 %
Labor-related	Ease in securing clerical workers	23	8.7 %
Utility rates	Electricity	23	8.7 %
Others	Measures taken to promote industry by local government	23	8.7 %
Others	Business practices	18	6.8 %
Procurement of parts and materials	Procurement costs	16	6.0 %
Tax systems/procedures	Efficient administrative procedures	14	5.3 %
Tax systems/procedures	Easy-to-use tax system	13	4.9 %
Finance	Availability of credit	13	4.9 %
Utility rates	Water	13	4.9 %
Finance	Depreciating local currency	12	4.5 %
Finance	Appreciating local currency	11	4.2 %
Utility rates	Gas	10	3.8 %
Others	Funding capacity of business partners	9	3.4 %
Others	Sales capacity of business partners	9	3.4 %
Infrastructure	Others	7	2.6 %
Others	Others	7	2.6 %
Labor-related	Others	6	2.3 %
Investment legislation/procedures	Others	5	1.9 %
Labor-related	Low social security burden	5	1.9 %
Tax systems/procedures	Others	3	1.1 %
Procurement of parts and materials	Others	3	1.1 %
Finance	Others	1	0.4 %
Utility rates	Others	1	0.4 %
Labor-related	Low personal income tax rates	0	0.0 %

Attractions/Advantage of the Production Bases (Central & Eastern Europe) (n=73)

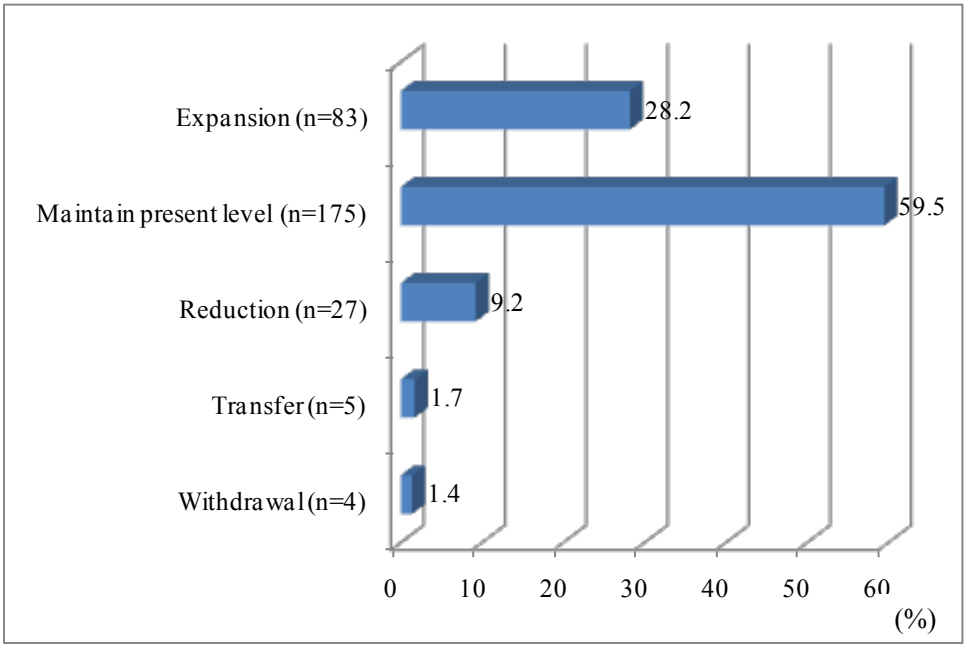
Category	Attractions/Advantage	Responses	%
Labor-related	Low labor costs	34	46.6 %
Others	Offers strategic location	31	42.5 %
Labor-related	High quality of workforce	24	32.9 %
Political, economic and social conditions	Public safety and social conditions	23	31.5 %
Labor-related	Ease in securing factory workers	20	27.4 %
Tax systems/procedures	Corporate tax rates	12	16.4 %
Investment legislation/procedures	Easily accessible investment incentive schemes	11	15.1 %
Procurement of parts and materials	Procurement costs	9	12.3 %
Infrastructure	Industrial parks	9	12.3 %
Political, economic and social conditions	Political conditions	9	12.3 %
Others	High level of education	9	12.3 %
Labor-related	Ease in securing multilingual staff	8	11.0 %
Labor-related	High labor productivity	8	11.0 %
Others	Living environment for foreigners	8	11.0 %
Investment legislation/procedures	Visa/work permits easily acquired	7	9.6 %
Finance	Depreciating local currency	7	9.6 %
Procurement of parts and materials	Quality	7	9.6 %
Infrastructure	Airports	7	9.6 %
Others	Quality of end products	7	9.6 %
Finance	Availability of credit	6	8.2 %
Procurement of parts and materials	Delivery dates are strictly kept	6	8.2 %
Others	Well-developed industrial and technological infrastructure	6	8.2 %
Others	Widespread use of English language	6	8.2 %
Investment legislation/procedures	Stable administration of related laws	5	6.8 %
Labor-related	Ease in securing engineers	5	6.8 %
Labor-related	Flexible employment systems	5	6.8 %
Tax systems/procedures	Easy-to-use tax system	4	5.5 %
Procurement of parts and materials	Abundant procurement sources	4	5.5 %
Infrastructure	Others	4	5.5 %
Utility rates	Electricity	4	5.5 %
Political, economic and social conditions	Economic conditions	4	5.5 %
Others	Measures taken to promote industry by local government	4	5.5 %
Others	Market size	4	5.5 %
Tax systems/procedures	Stable administration of related laws	3	4.1 %
Labor-related	Low personal income tax rates	3	4.1 %
Others	Sales capacity of business partners	3	4.1 %
Others	Others	3	4.1 %
Labor-related	Ease in securing clerical workers	2	2.7 %
Finance	Stable exchange rate	2	2.7 %
Finance	Others	2	2.7 %
Procurement of parts and materials	Others	2	2.7 %
Utility rates	Water	2	2.7 %
Utility rates	Gas	2	2.7 %
Utility rates	Others	2	2.7 %
Investment legislation/procedures	Efficient administrative procedures	1	1.4 %
Tax systems/procedures	Others	1	1.4 %
Labor-related	Low social security burden	1	1.4 %
Labor-related	Ease in securing managerial personnel	1	1.4 %
Labor-related	Others	1	1.4 %
Infrastructure	Port facilities	1	1.4 %
Investment legislation/procedures	Others	0	0.0 %
Tax systems/procedures	Efficient administrative procedures	0	0.0 %
Finance	Appreciating local currency	0	0.0 %
Others	Business practices	0	0.0 %
Others	Funding capacity of business partners	0	0.0 %

Source: JETRO Survey, Japan External Trade Organization

(2) Business development in the next 1–2 years

With regard to business development in the next 1–2 years, 28.2% of Japanese affiliates in Western Europe plan an “expansion” of their operations, 59.5% plan to “maintain present level” of production, 9.2% plan a “reduction” of their production, 1.7% plan to “transfer” production bases and 1.4% plan to “withdrawal”. The percentage of companies planning to expand their business declined significantly from the previous survey (45.4%), while “maintain present level”(45.4%) and “reduction” (5.2%) increased(see Diagram 22).

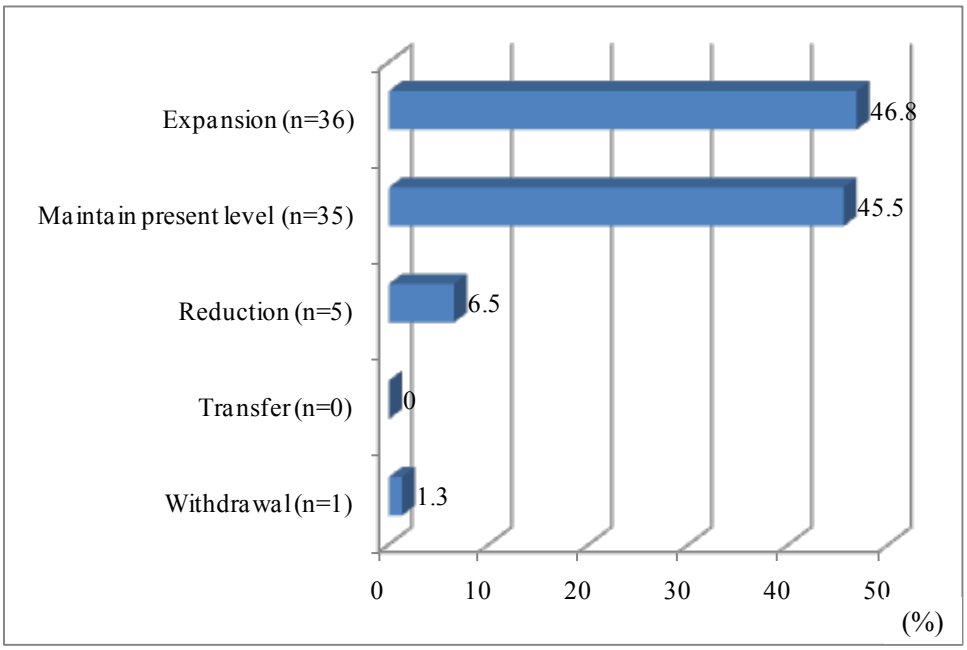
Diagram 22: Direction of Business Development by Japanese Manufacturing Affiliates in Western Europe in the Next 1–2 Years



Source: JETRO Survey, Japan External Trade Organization

With regards to business development plans in the next 1–2 years for Japanese affiliates in Central and Eastern Europe, 46.8% plan an “expansion” of their operations, 45.5% plan to “maintain present level” of production and 6.5% plan a “reduction” of production, while 0% plan to “transfer” production bases and 1.3% plan to “withdrawal”. While the percentage of companies planning an “expansion” has been decreasing since the second last survey (75.4%, and it was 55.7% in the last survey), those planning to “maintain present level” of production (21.3% in the second last survey and 40.5% in the last survey) and for “reduction” increased (1.6% in the second last survey and 2.5% in the last survey) (see Diagram 23).

Diagram 23: Direction of Business Development by Japanese Manufacturing Affiliates in Central and Eastern Europe in the Next 1–2 Years

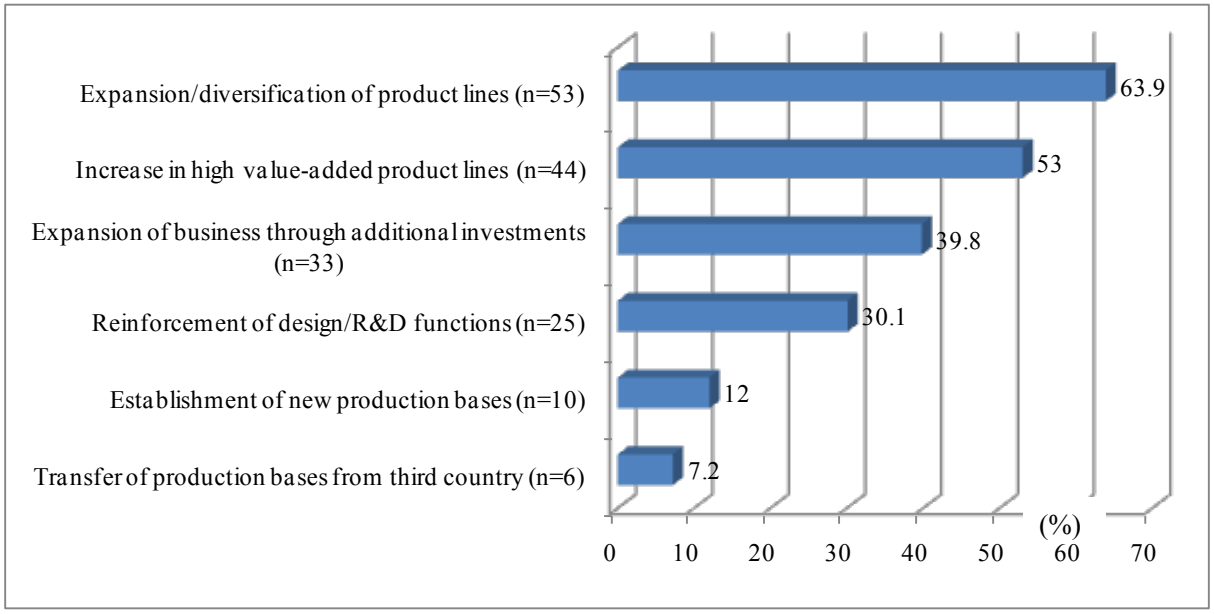


Source: JETRO Survey, Japan External Trade Organization

(3) Specific policies of the companies that think of "expansion" of their business activities

When the Japanese manufacturing affiliates in Western Europe that are considering the "expansion" of their business activities were asked specific plans and policies, the "expansion/diversification of product lines" (63.9%) was the most frequently cited reply, followed by an "increase in high value-added product lines" (53.0%). Meanwhile, the ratio of companies that cited the "expansion/diversification of product lines", which significantly increased by almost 40% from the previous survey, and the "expansion of business through additional investments"—both the most frequently cited policies in the previous survey—reduced dramatically from 63.9% to 39.8% (see Diagram 24).

Diagram 24: Specific Policies of Business Expansion by Japanese Manufacturing Affiliates in Western Europe

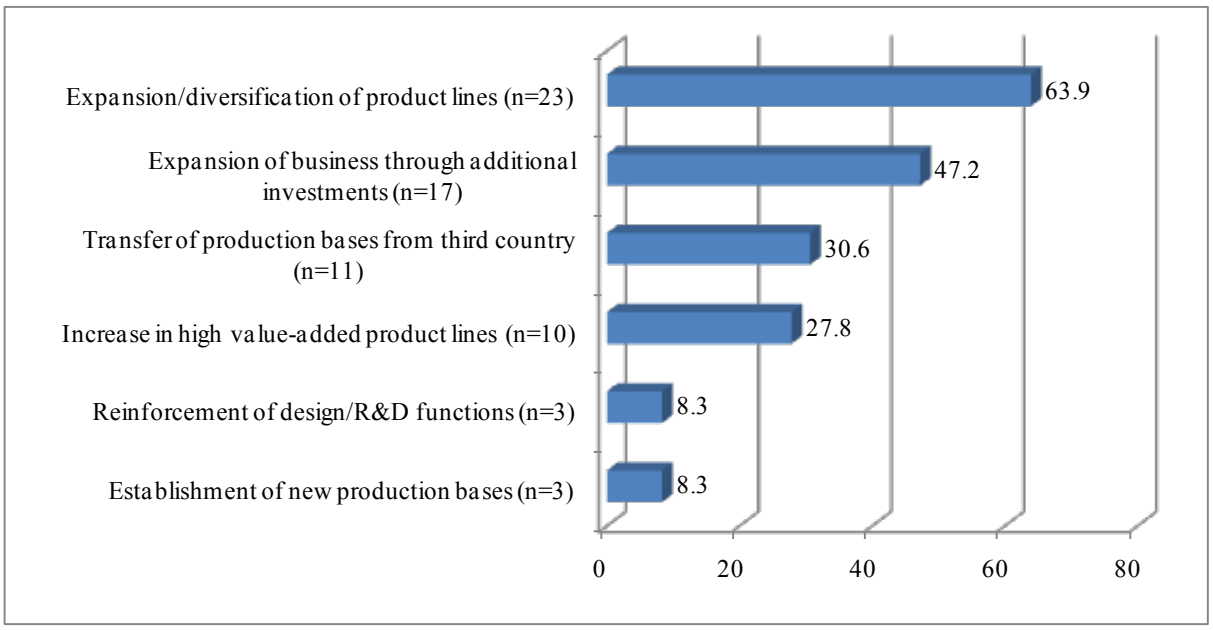


Source: JETRO Survey, Japan External Trade Organization

On the other hand, concrete business expansion policies of Japanese manufacturing affiliates in Central and Eastern Europe consist of: “expansion/diversification of product lines” (63.9%), “expansion of business through additional investments” (47.2%) and “transfer of production bases from third country” (30.6%). While the “expansion/diversification of product lines”, which was selected by 50.0% of the respondents in the previous survey, increased by more than 10 percentage points, the most cited reply of the previous survey, “expansion of business through additional investments”, reduced significantly from the previous survey (77.3%) (see Diagram 25).

Both in Western and Central/Eastern Europe, there is a trend occurring where companies curtail additional investment with weak demand in the midst of the financial crisis, while trying to expand business with enhanced/diversified product lines.

Diagram 25: Specific Policies of Business Expansion by Japanese Manufacturing Affiliates in Central and Eastern Europe



Source: JETRO Survey, Japan External Trade Organization

(4) Specific policies of the companies that plan "reduction", "transfer" or "withdrawal" of their business activities

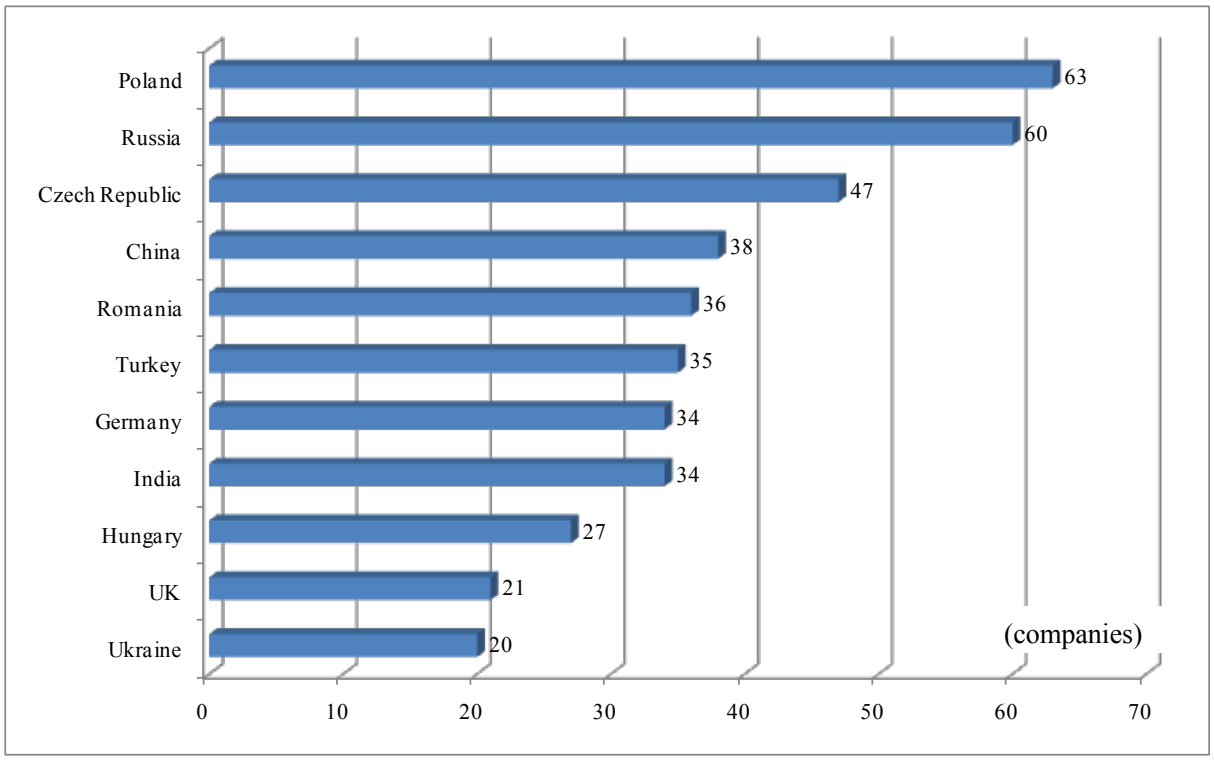
There were 42 Japanese manufacturing affiliates (36 in Western Europe and 6 in Central and Eastern Europe) that indicated they plan for "reduction" , "transfer" or "withdrawal" about their business activities in the next 1–2 years. The number significantly increased from the 28 companies in the previous year, and the most frequently cited policies of such companies were: "transfer production of certain product lines to third country" (15 companies), "transfer production bases to third country" (14 companies) and "cease production of certain product lines" (11 companies).

(5) Countries/regions being considered promising locations for production

The country/region most frequently cited as a promising production base over the mid- to long-term (5–10 years) was Poland (63 companies), a dramatic increase from the previous year (44 companies). Similar to last year, many companies answered Russia (60 companies), which was also cited by more companies than the previous year (51 companies). This indicates that the focus on Russia as a promising area for production—not just as a market—has been increasing.

Other countries among the top of the list are the Czech Republic (47 companies), China (38 companies) and Turkey (35 companies). Continued from the previous year, many companies focused on countries in Central and Eastern Europe and China, while Turkey (increased from 31 companies in the previous survey to 35 this time) and Germany (23 to 34) also received more votes (see Diagram 26).

Diagram 26: Countries/Regions Considered Promising Production Bases over the Mid- to Long-Term (5–10 Years)



Source: JETRO Survey, Japan External Trade Organization

IV. Management problems

- Managerial issues common to Japanese manufacturing affiliates in Western Europe, as well as Central and Eastern Europe, are: “global economic downturn stemming from financial crisis”, “volatile exchange rate fluctuations”, “domestic economic conditions” and “visa/work permits”.
- Major issues for Japanese manufacturing affiliates located in Western Europe are generally related to labor costs, such as “high labor costs”, “stringent dismissal laws” and “heavy social security burdens”. These issues are caused by the extensive protection of workers and high costs associated with that.
- For companies located in Central and Eastern Europe, “volatile exchange rate fluctuations” is the most serious issue, cited by three out of four companies. Also among the major issues are labor problems such as: “high labor cost growth rate” and “difficulty in securing engineers”, and that which is related to insufficient infrastructure, such as “general road conditions”.

1. Management problems common to Japanese manufacturing affiliates in Western Europe and in Central and Eastern Europe

Among the managerial issues faced by Japanese manufacturing affiliates in Europe, “global economic downturn stemming from financial crisis”, “volatile exchange rate fluctuations”, “domestic economic conditions”, and “visa/work permits” are the most common issues encountered by Japanese manufacturing affiliates in Western Europe, as well as those in Central and Eastern Europe (see Diagram 27)

Diagram 27: Management Problems for Japanese Manufacturing Affiliates in Europe (Multiple Answers Allowed)

Japanese Manufacturing Affiliates Operating in Western Europe (Multiple Answers allowed) (n=288)

Category	Problem	Responses	Percentage
Political, economic, and social conditions	Global economic downturn stemming from financial crisis	195	67.7 %
Labor issues	High labor costs	170	59.0 %
Finance	Volatile exchange rate fluctuations	121	42.0 %
Environmental regulations	REACH	110	38.2 %
Labor issues	Stringent dismissal laws	108	37.5 %
Labor issues	Heavy social security burdens	100	34.7 %
Parts and materials procurement	Procurement costs	96	33.3 %
Political, economic, and social conditions	Domestic economic conditions	83	28.8 %
Labor issues	Quality of workforce	72	25.0 %
Tax systems/procedures	Transfer pricing taxation	68	23.6 %
Investment legislation/procedures	Visa/work permits	64	22.2 %
Labor issues	Union activities/strikes	57	19.8 %
Labor issues	Difficulty in securing managerial personnel	56	19.4 %
Labor issues	High labor cost growth rate	54	18.8 %
Labor issues	Difficulty in securing engineers	54	18.8 %
Standards, certifications and regulations	High costs of acquiring CE mark	51	17.7 %
Parts and materials procurement	Quality	50	17.4 %
Parts and materials procurement	Deliveries	50	17.4 %
Parts and materials procurement	Shortage of domestic procurement sources	43	14.9 %
Standards, certifications and regulations	Different inspection standards for each country	41	14.2 %
Finance	Collection of receivables	38	13.2 %
Tax systems/procedures	Non-uniform taxation among EU countries	37	12.8 %
Labor issues	High personal income tax rates	36	12.5 %
Finance	Depreciating local currency	35	12.2 %
Tax systems/procedures	High corporate tax rates	32	11.1 %
Others	Extent of English language use	29	10.1 %
Environmental regulations	RoHS	28	9.7 %
Trade legislation/procedures	High tariff rates	27	9.4 %
Investment legislation/procedures	Complicated administrative procedures and/or lack of transparency	27	9.4 %
Finance	Difficulty in obtaining credit	27	9.4 %
Finance	Appreciating local currency	26	9.0 %
Tax systems/procedures	Complicated administrative procedures and/or lack of transparency	23	8.0 %
Others	EU competition law	23	8.0 %
Trade legislation/procedures	Complicated administrative procedures and/or lack of transparency	22	7.6 %
Trade legislation/procedures	Customs clearance issues	21	7.3 %
Insufficient infrastructure	Communications	18	6.3 %
Others	Living environment for foreigners	17	5.9 %
Others	Business practices	17	5.9 %
Standards, certifications and regulations	Others	16	5.6 %
Labor issues	Difficulty in securing clerical workers	16	5.6 %
Others	Inflow of counterfeit goods	16	5.6 %
Political, economic, and social conditions	Public safety and social conditions	15	5.2 %
Finance	Fluctuating interest rates	14	4.9 %
Investment legislation/procedures	Frequent legislation revisions	13	4.5 %
Investment legislation/procedures	Lack of transparency in investment incentive schemes	13	4.5 %
Environmental regulations	European regulation on new car CO2 emissions	13	4.5 %
Trade legislation/procedures	Rule-of-origin	12	4.2 %
Tax systems/procedures	Double taxation (in both Japan and the country where operations are located)	12	4.2 %
Tax systems/procedures	Others	12	4.2 %
Labor issues	Double social security payments	12	4.2 %
Labor issues	Difficulty in securing factory workers	12	4.2 %
Insufficient infrastructure	Power supply	12	4.2 %
Insufficient infrastructure	General road conditions	11	3.8 %
Political, economic, and social conditions	Concerns for measures against new strains of influenza	11	3.8 %
Trade legislation/procedures	Tariff classification	10	3.5 %
Political, economic, and social conditions	Political conditions	10	3.5 %
Trade legislation/procedures	Others	9	3.1 %
Parts and materials procurement	Others	9	3.1 %
Environmental regulations	WEEE	9	3.1 %
Environmental regulations	Others	9	3.1 %
Finance	Others	8	2.8 %
Insufficient infrastructure	Others	8	2.8 %
Investment legislation/procedures	Others	6	2.1 %
Labor issues	Others	6	2.1 %
Insufficient infrastructure	Highways	6	2.1 %
Environmental regulations	ELV	6	2.1 %
Trade legislation/procedures	Anti-dumping measures	5	1.7 %
Others	Insufficient protection of intellectual property rights	5	1.7 %
Others	Others	5	1.7 %
Environmental regulations	Euro5	4	1.4 %
Insufficient infrastructure	Port facilities	3	1.0 %
Insufficient infrastructure	Railways	2	0.7 %
Insufficient infrastructure	Gas	1	0.3 %
Insufficient infrastructure	Water	0	0.0 %
Environmental regulations	EuP, ErP (Eco-design)	0	0.0 %

Japanese Manufacturing Affiliates Operating in Central & Eastern Europe (Multiple Answers Allowed) (n=77)

Category	Problem	Responses	Percentage
Finance	Volatile exchange rate fluctuations	58	75.3 %
Political, economic, and social conditions	Global economic downturn stemming from financial crisis	56	72.7 %
Labor issues	High labor cost growth rate	35	45.5 %
Labor issues	Difficulty in securing engineers	35	45.5 %
Insufficient infrastructure	General road conditions	31	40.3 %
Labor issues	Difficulty in securing managerial personnel	30	39.0 %
Parts and materials procurement	Shortage of domestic procurement sources	29	37.7 %
Insufficient infrastructure	Highways	28	36.4 %
Environmental regulations	REACH	27	35.1 %
Investment legislation/procedures	Visa/work permits	26	33.8 %
Political, economic, and social conditions	Domestic economic conditions	25	32.5 %
Standards, certifications and regulations	High costs of acquiring CE mark	23	29.9 %
Parts and materials procurement	Procurement costs	22	28.6 %
Labor issues	Heavy social security burdens	21	27.3 %
Labor issues	Quality of workforce	20	26.0 %
Tax systems/procedures	Transfer pricing taxation	18	23.4 %
Parts and materials procurement	Deliveries	17	22.1 %
Others	Living environment for foreigners	17	22.1 %
Others	Extent of English language use	17	22.1 %
Investment legislation/procedures	Frequent legislation revisions	16	20.8 %
Investment legislation/procedures	Complicated administrative procedures and/or lack of transparency	15	19.5 %
Trade legislation/procedures	Complicated administrative procedures and/or lack of transparency	14	18.2 %
Parts and materials procurement	Quality	14	18.2 %
Labor issues	High personal income tax rates	13	16.9 %
Labor issues	Stringent dismissal laws	13	16.9 %
Finance	Depreciating local currency	13	16.9 %
Political, economic, and social conditions	Political conditions	12	15.6 %
Tax systems/procedures	Complicated administrative procedures and/or lack of transparency	11	14.3 %
Labor issues	High labor costs	11	14.3 %
Environmental regulations	RoHS	11	14.3 %
Insufficient infrastructure	Power supply	10	13.0 %
Tax systems/procedures	Non-uniform taxation among EU countries	9	11.7 %
Labor issues	Union activities/strikes	9	11.7 %
Trade legislation/procedures	Customs clearance issues	8	10.4 %
Investment legislation/procedures	Lack of transparency in investment incentive schemes	8	10.4 %
Labor issues	Difficulty in securing factory workers	8	10.4 %
Labor issues	Difficulty in securing clerical workers	8	10.4 %
Labor issues	Others	8	10.4 %
Others	Business practices	8	10.4 %
Standards, certifications and regulations	Different inspection standards for each country	7	9.1 %
Insufficient infrastructure	Railways	7	9.1 %
Insufficient infrastructure	Communications	7	9.1 %
Tax systems/procedures	Double taxation (in both Japan and the country where operations are located)	6	7.8 %
Labor issues	Double social security payments	6	7.8 %
Environmental regulations	ELV	6	7.8 %
Trade legislation/procedures	High tariff rates	5	6.5 %
Trade legislation/procedures	Others	5	6.5 %
Tax systems/procedures	High corporate tax rates	5	6.5 %
Tax systems/procedures	Others	5	6.5 %
Finance	Collection of receivables	5	6.5 %
Political, economic, and social conditions	Public safety and social conditions	5	6.5 %
Political, economic, and social conditions	Concerns for measures against new strains of influenza	5	6.5 %
Finance	Difficulty in obtaining credit	4	5.2 %
Trade legislation/procedures	Tariff classification	3	3.9 %
Trade legislation/procedures	Rule-of-origin	3	3.9 %
Standards, certifications and regulations	Others	3	3.9 %
Finance	Appreciating local currency	3	3.9 %
Finance	Fluctuating interest rates	3	3.9 %
Parts and materials procurement	Others	3	3.9 %
Environmental regulations	European regulation on new car CO2 emissions	3	3.9 %
Trade legislation/procedures	Anti-dumping measures	2	2.6 %
Insufficient infrastructure	Port facilities	2	2.6 %
Insufficient infrastructure	Water	2	2.6 %
Insufficient infrastructure	Gas	2	2.6 %
Environmental regulations	WEEE	2	2.6 %
Environmental regulations	Euro5	2	2.6 %
Environmental regulations	Others	2	2.6 %
Others	EU competition law	2	2.6 %
Investment legislation/procedures	Others	1	1.3 %
Finance	Others	1	1.3 %
Insufficient infrastructure	Others	1	1.3 %
Environmental regulations	EuP, ErP (Eco-design)	1	1.3 %
Others	Insufficient protection of intellectual property rights	1	1.3 %
Others	Inflow of counterfeit goods	1	1.3 %
Others	Others	0	0.0 %

Source: JETRO Survey, Japan External Trade Organization

2. Management problems encountered by Japanese manufacturing affiliates in Western Europe

The major difference between the Japanese manufacturing affiliates in Western Europe and their counterparts in Central and Eastern Europe is that, in Central and Eastern Europe, as many as 20 items out of 70 received 20% or more replies, showing that their managerial issues are diversified in regard to the areas of finance, labor, and infrastructure, and to the housing and living environment and penetration of the English language. On the other hand, for Western Europe, the items with 20% or more responses were 11, almost the half of those of Central and Eastern Europe, which seems to be the proof that they have a more mature environment for investment (see Diagram 27).

When looking at the answers from Japanese manufacturing affiliates in Western Europe, the most cited problem among all of them was: “global economic downturn stemming from financial crisis” with 67.7% responses, followed by “high labor costs” (59.0%), “volatile exchange rate fluctuations” (42.0%), “REACH” (38.2%), “stringent dismissal laws” (37.5%) “heavy social security burdens” (34.7%) and “procurement costs” (33.3%).

“High labor costs” was the most cited issue in the 2008 survey ranked second this time, although the difference with the most frequently cited issue discovered in this survey, “global economic downturn stemming from financial crisis”, was small. The companies that selected “high labor costs” as a management problem increased from 54.7% in 2008 by 4.3 percentage points, showing that high labor costs are still heavily affecting business management in the midst of the economic slump.

42.0% of the companies cited “volatile exchange rate fluctuations” as a management issue, which was almost the same response rate from the 2008 survey (40.0%). Country-by-country comparison shows this was the most cited issue (68.3%) in the UK, which is outside the Euro zone, and the numbers were also high in European countries such as France (38.5%), Spain (33.3%) and Germany (29.6%). The reason for this seems to be the sudden depreciation of the pound and euro at the end of 2008, which hovered high against the yen and the dollar for a long time before that (see Diagram 28).

“Stringent dismissal laws”, which is a new item added to the survey this year, was cited as a managerial issue by many companies in various countries (France: 57.7%, Spain: 48.1%, the Netherlands: 40.0%, and Germany: 40.7%), showing that non-flexible labor laws and regulations have become a heavy burden for the management of companies. Although some countries’ governments have introduced a system to compensate the amount of worker salaries reduced by corporations, such as the enhanced support for shorter operation hours in Germany and partial unemployment insurance in the Netherlands, they have yet to provide a substantial solution for the issue. The “heavy social security burdens”, another new item that appeared this year, has been selected by many companies in France (55.8%), Germany (38.9%) and the Netherlands (32.0%), showing that high worker protection is increasing the burden of corporations.

Compared to the survey conducted in January and February 2004, “volatile exchange rate fluctuations”

(64.6% in 2004) and "high labor costs" (56.6% in 2004), which recorded a high response rate at that time, were still pointed out by many companies in this survey, indicating that these issues continued to be a management problem for Japanese manufacturing affiliates in Western Europe. On the other hand, "quality of workforce" (39.2% in 2004) and the "difficulty in securing human resources" (38.9% in 2004) reduced to less than 30% and less than 20%, respectively—showing that these problems have been solved to some extent.

Diagram 28: Management Problems Encountered by Japanese Manufacturing Affiliates in Western Europe, in Descending Order (UK, Germany, France and Spain)

(Multiple Answers Allowed)

UK (Respondent companies: 63)	Germany (Respondent companies: 54)	France (Respondent companies: 52)	Spain (Respondent companies: 27)
Volatile exchange rate fluctuations 68.3%	Global economic downturn stemming from financial crisis 72.2%	Global economic downturn stemming from financial crisis 67.3%	Global economic downturn stemming from financial crisis 70.4%
Global economic downturn stemming from financial crisis 66.7%	High labor costs 64.8%	Stringent dismissal laws 57.7%	Visa/work permits 51.9%
High labor costs 58.7%	Stringent dismissal laws 40.7%	Heavy social security burdens 55.8%	High labor costs 51.9%
Procurement costs 44.4%	REACH 40.7%	High labor costs 50.0%	Stringent dismissal laws 48.1%
REACH 41.3%	Domestic economic conditions 40.7%	Union activities/strikes 44.2%	Procurement costs 48.1%
Domestic economic conditions 36.5%	Transfer pricing taxation 38.9%	Volatile exchange rate fluctuations 38.5%	High labor cost growth rate 44.4%
Quality of workforce 31.7%	Heavy social security burdens 38.9%	REACH 30.8%	Union activities/strikes 37.0%
Visa/work permits 28.6%	Volatile exchange rate fluctuations 29.6%	Quality of workforce 28.8%	REACH 37.0%
Depreciating local currency 27.0%	Procurement costs 29.6%	Procurement costs 28.8%	Domestic economic conditions 37.0%
High costs of acquiring CE mark 25.4%	Difficulty in securing managerial personnel 22.2%	Visa/work permits 25.0%	Extent of English language use 37.0%
Heavy social security burdens 25.4%	Difficulty in securing engineers 18.5%	Transfer pricing taxation 25.0%	Transfer pricing taxation 33.3%
Difficulty in securing engineers 25.4%	High labor cost growth rate 16.7%	High costs of acquiring CE mark 23.1%	Quality of workforce 33.3%
Difficulty in securing managerial personnel 23.8%	Union activities/strikes 16.7%	Deliveries (of parts and materials) 21.2%	Volatile exchange rate fluctuations 33.3%
Shortage of domestic procurement sources 23.8%	Quality (of parts and materials) 16.7%	High corporate tax rates 19.2%	Quality (of parts and materials) 29.6%
RoHS 19.0%	High tariff rates 14.8%	Different inspection standards for each country 19.2%	Complicated administrative procedures and/or lack of transparency (Investment legislation/procedures) 18.5%
Quality (of parts and materials) 17.5%	Quality of workforce 14.8%	Domestic economic conditions 19.2%	High costs of acquiring CE mark 18.5%
Different inspection standards for each country 15.9%	Appreciating local currency 14.8%	Non-uniform taxation among EU countries 17.3%	Heavy social security burdens 18.5%

Source: JETRO Survey, Japan External Trade Organization

3. Management problems encountered by Japanese manufacturing affiliates in Central and Eastern Europe

The most cited managerial problem of Japanese manufacturing affiliates in Central and Eastern Europe was "volatile exchange rate fluctuations" (75.3%), and this percentage was higher than "global economic downturn stemming from financial crisis" (72.7%). Although the responses for "volatile exchange rate fluctuations" have been decreasing in recent years, it increased again this time (71.1% in 2004, 66.7% in 2005, 53.8% in 2006, 47.5% in 2007 and 57.0% in 2008). Local currencies, such as the koruna (Czech Republic), forint (Hungary) and zloty (Poland) have depreciated by 20–30% respectively after marking a record high rate against the euro in July (see Diagram 27).

A "High labor costs growth rate", which was the most cited issue in the 2008 survey, ranked third this time, and the response rate declined from 84.8% to 45.5%. On the other hand, only 14.3% selected "high labor costs", which was selected by many companies in Western Europe, indicating that companies still do not feel that the level of labor costs is actually very high.

Many companies pointed out human resource shortages as a problem, which continued from the 2008 survey. Out of the total, concerning managerial problems, 45.5% replied that they had "difficulty in securing engineers", and 39.0% replied that they experienced "difficulty in securing managerial personnel", which is significantly higher than Western Europe (18.8% for "difficulty in securing engineers" and 1.4% for "difficulty in securing managerial personnel").

Many companies also pointed out insufficient infrastructure as an important managerial issue. Of the total, 40.3% selected "general road conditions", and 36.4% selected "highways" as an issue (in Western Europe, 3.8% and 2.1% also considered them a problem, respectively). These two items were also selected by many companies in Poland in particular—17 out of 23 companies (73.9%) selected "general road conditions" and 16 companies (69.6%) selected "highways" as troublesome issues (see Diagram 29). As many general roads in Poland are unpaved and have only one lane for each direction, local logistics are heavily affected, for example, when precision machinery or parts are transported. Also concerning "highways", while they are well developed in the Czech Republic and Hungary, in Poland, only parts of the industrial areas in the southern and central portions of the country have highways, and these roadways are not well connected to neighboring countries. This is considered to be the main reason for the high response rate for this item.

Compared to the survey conducted in January and February 2004, "volatile exchange rate fluctuations" remained at the top this time (the response rate was as high as 71.1% in 2004). On the other hand, "visa/work permits", which ranked first in 2004 at the same percentage as "volatile exchange rate fluctuations", reduced its percentage to 33.8%, suggesting that obtaining work permits has become easier as the countries in Central and Eastern Europe continue to develop. Additionally, "administrative procedures"

in trade, investment and tax systems were all reduced to less than 20%, although they were all above 40% in 2004. This indicates that the time spent on various administrative procedures has been reduced.

Diagram 29: Management Problems Reported by Japanese Manufacturing Affiliates in Central and Eastern Europe (Poland, the Czech Republic and Hungary), in Descending Order (Multiple Answers Allowed)

Czech Republic (Respondent companies: 19)	Hungary (Respondent companies: 16)	Poland (Respondent companies: 23)
Volatile exchange rate fluctuations 84.2%	Difficulty in securing managerial personnel 68.8%	Volatile exchange rate fluctuations 82.6%
Global economic downturn stemming from financial crisis 84.2%	Volatile exchange rate fluctuations 68.8%	Global economic downturn stemming from financial crisis 78.3%
Difficulty in securing engineers 57.9%	Global economic downturn stemming from financial crisis 68.8%	General road conditions 73.9%
REACH 57.9%	Heavy social security burdens 62.5%	Highways 69.6%
Shortage of domestic procurement sources 47.4%	Domestic economic conditions 62.5%	High labor cost growth rate 47.8%
Procurement costs 42.1%	High personal income tax rates 43.8%	Visa/work permits 43.5%
Visa/work permits 36.8%	Difficulty in securing engineers 43.8%	Difficulty in securing engineers 43.5%
High costs of acquiring CE mark 36.8%	Shortage of domestic procurement sources 43.8%	Shortage of domestic procurement sources 43.5%
High labor cost growth rate 36.8%	Political Conditions 43.8%	High costs of acquiring CE mark 34.8%
Difficulty in securing managerial personnel 36.8%	Extent of English language use 43.8%	Complicated administrative procedures and/or lack of transparency (Investment legislation/procedures) 30.4%
Domestic economic conditions 36.8%	High costs of acquiring CE mark 37.5%	Transfer pricing taxation 30.4%
Difficulty in securing factory workers 26.3%	Transfer pricing taxation 31.3%	Deliveries (of parts and materials) 30.4%
Heavy social security burdens 21.1%	High labor cost growth rate 31.3%	REACH 30.4%
High personal income tax rates 21.1%	Depreciating local currency 31.3%	Complicated administrative procedures and/or lack of transparency (Trade legislation/procedures) 26.1%
Quality of workforce 21.1%	Procurement costs 31.3%	Difficulty in securing managerial personnel 26.1%
General road conditions 21.1%	REACH 31.3%	Stringent dismissal laws 26.1%
Living environment for foreigners 21.1%	Frequent legislation revisions (Investment legislation/procedures) 25.0%	Quality (of parts and materials) 26.1%

Source: JETRO Survey, Japan External Trade Organization

V. Compliance with EU Environmental Regulations and Environmental Incentives

[Compliance with EU Environmental Regulations]

- Slightly less than 70% of the respondent companies are subject to "REACH", and approximately 40% must comply with "RoHS".
- With regard to "RoHS", more than 80% of the subject companies have completed compliance with regulations. On the other hand, approximately 50% have complied with "REACH", and only approximately 30% have complied with "Euro5" and "European regulations on new car CO_2 emissions", for which companies have some moratorium before full compliance.
- Many companies answered that the biggest problem involved in compliance with regulations is "increasing costs due to compliance" for all relevant regulations. For "REACH" and "WEEE", many pointed out the non-transparency and unpredictability of the administration of the rules as problems.

[Impact of environmental incentives and/or economic stimulus measures in environmental areas]

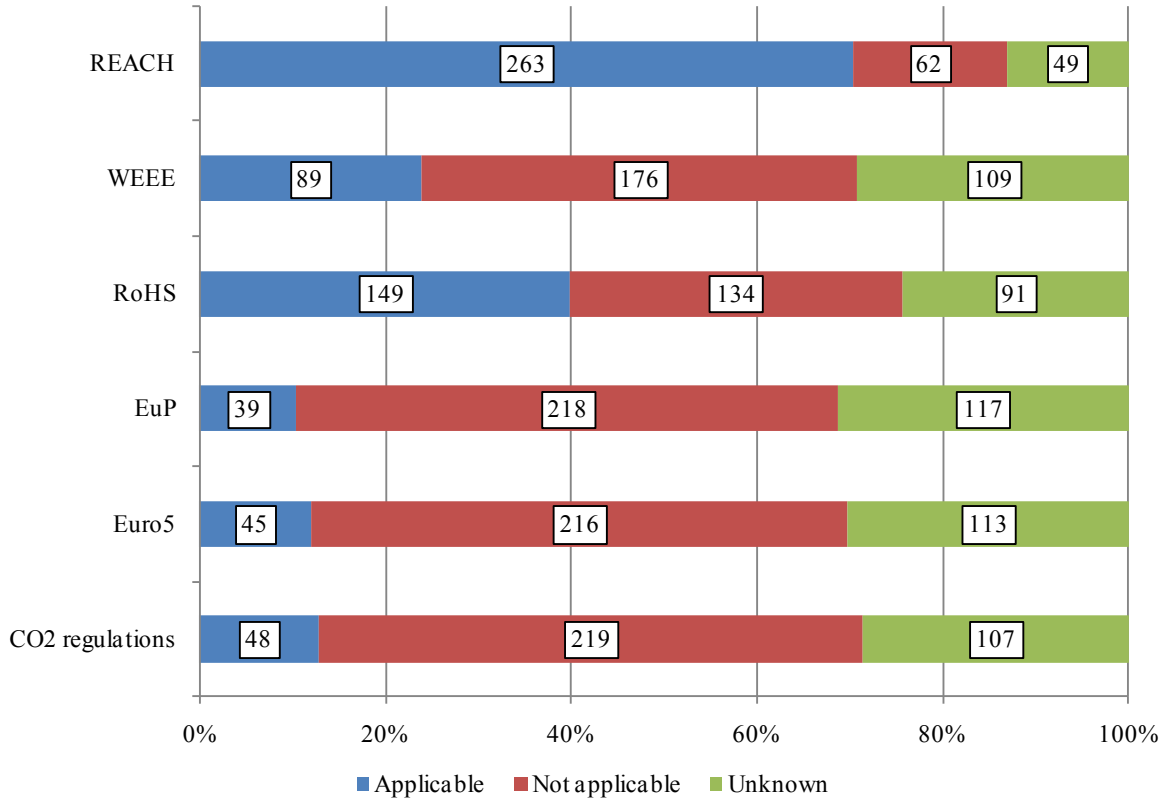
- While many companies provided positive answers regarding policies, such as the "expansion of environment-related business opportunities", many also answered "tougher competition" and "increased costs".

1. Impact of and compliance with EU environmental regulations

Recently, more and more companies point out EU environmental regulations as managerial issues. In this survey, inquiries were made about the compliance situation of Japanese manufacturing affiliates in Europe and issues involved in complying with the regulations, with regard to the EU environmental regulations, such as the "directive on Waste Electrical and Electronic Equipment" (WEEE, effective from August 2003), the "directive on Restriction of Hazardous Substances" (RoHS, effective from July 2006), and the regulations concerning the "Registration, Evaluation, Authorization and restriction of CHemicals" (REACH, effective from June 2007) (multiple answers allowed).

Among the EU environmental regulations that apply to the products of Japanese manufacturing affiliates in Europe, REACH was the number one "applicable" regulation—almost 70% (263 companies out of 374 respondents) answered that their product(s) are subject to this regulation. The second most "applicable" regulation was RoHS, with 149 companies (approximately 40% of the total respondents), followed by WEEE (89 companies), European regulations on new car CO_2 emissions (48 companies), Euro5 emission regulations (45 companies) and product eco-design regulations (EuP/ErP) (39 companies) (see Diagram 30). By industry, companies in 19 industries (82.6% of the total 23 industries) stated that their product(s) are subject to REACH, followed by RoHS (16 industries), WEEE (13 industries), European regulations on new car CO_2 emission (13 industries), EuP/ErP (12 industries) and Euro5 (10 industries). This indicates that, compared to European regulations on new car CO_2 emissions and Euro5, the impact of which is almost limited to the auto parts industry, and WEEE and RoHS, in which the target is mostly the electric and electronic parts industry, REACH covers much wider areas and has a greater impact on various industries.

Diagram 30: Applicability of EU Environmental Regulations

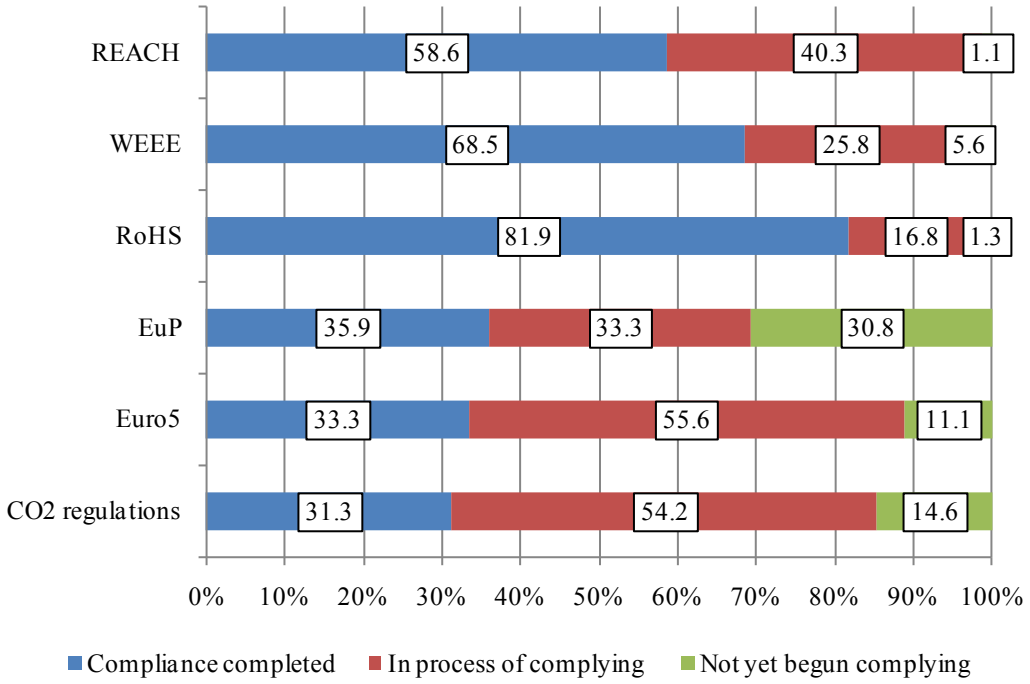


Source: JETRO Survey, Japan External Trade Organization

As for the status of compliance with each regulation, RoHS recorded the highest compliance rate (81.9% of the companies that answered that their product(s) are subject to the regulation) after six years since it took effect in February 2003. On the other hand, only 58.6% of the subject companies said they have complied with REACH, for which the registration of the chemical products started in July 2008. For Euro5, which that took effect in 2008 and imposes stricter restrictions on the emission of nitrogen oxide (NOx), carbon hydride (HC), carbon monoxide (CO) and particulate matter (PM) from every automobile from 2011, and for the European regulations on new car CO_2 emissions that regulates an average CO_2 emission of 65% for automobiles on sale to 130 g per kilometer by 2012 and 100% of the automobiles by 2015 (that have some moratorium before full implementation), the compliance rate was only 33.3 % and 31.3%, respectively. Meanwhile, more than 50% of the subject companies for each regulation said they have begun activities required for compliance.

With regard to EuP/ErP, which require environmentally friendly product design, only 35.9% of the respondent companies said that they have completed compliance, as many of the 19 product categories designated as the possible subject of the regulation are still undergoing research, and an implementation order has not yet been announced, although the framework directives took effect in 2005 (see Diagram 31).

Diagram 31: Compliance Status with EU Environmental Regulations

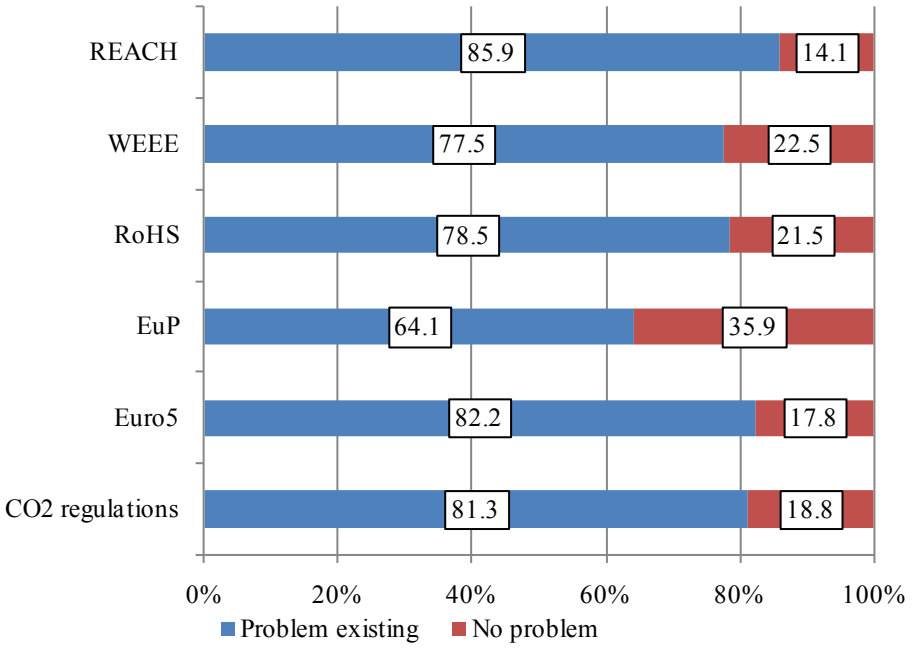


Source: JETRO Survey, Japan External Trade Organization

For questions regarding the situation of compliance with environmental regulations (multiple answers allowed), 60%–80% of the companies subject to each regulation said they have "encountered problems" (see Diagram 32). Concerning REACH, for which 85.9% of the respondents answered "encountered problems", as many as 116 companies out of the total 182 respondents that stated specific problems replied that they have experienced "increasing costs due to compliance", while many also pointed out specific issues concerning REACH, such as "inadequate information sharing along supply-chain" (60 companies), as problems. Some companies mentioned that the administration of the regulation itself is problematic, such as "substances to be registered/notified are unclear" (67 companies) and "responses by ECHA and the helpdesks of each country" (8 companies). Additionally, some mentioned "pre-registration incomplete" (11 companies), indicating that there is not just a small number of companies that are required to make official registration after failing to make pre-registration in the determined period.

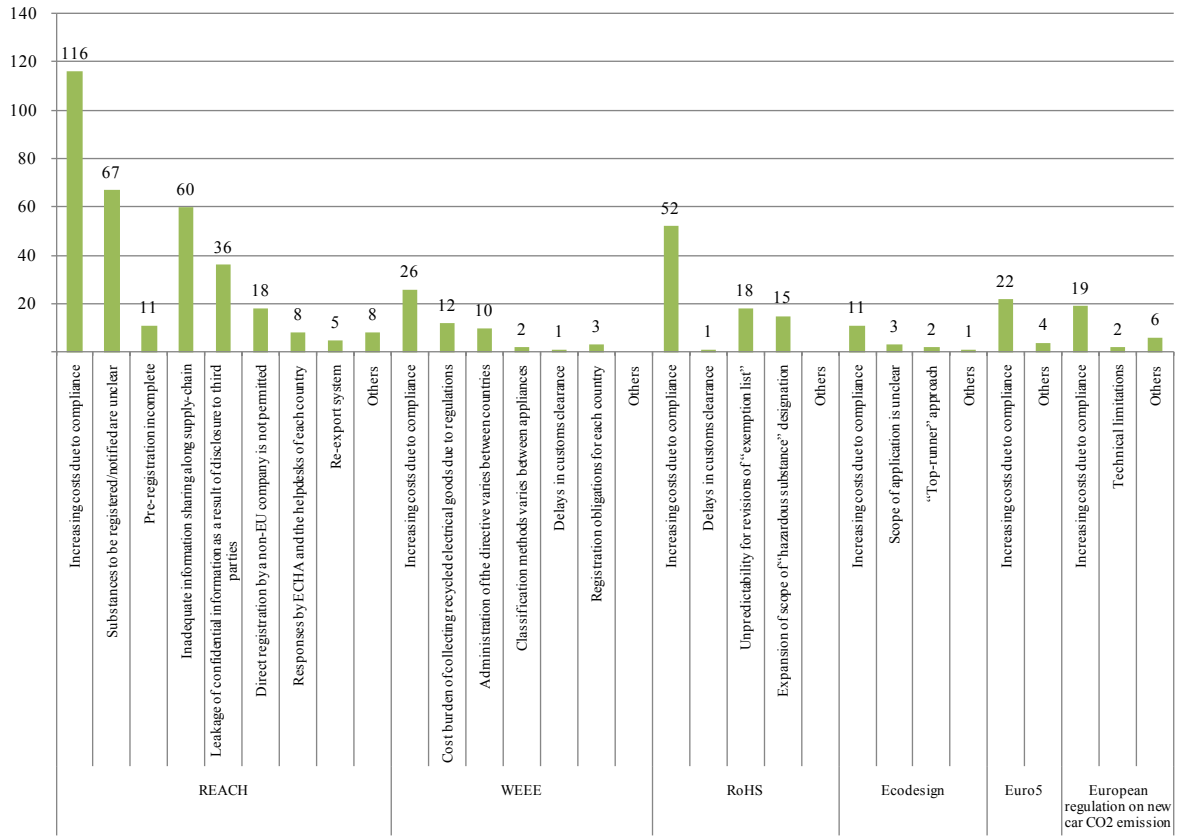
As for WEEE, the most cited problem was "increasing costs due to compliance", selected by 26 companies. There were also many companies that pointed out that the actual administration of the regulation is the problem, such as the "cost burden of collecting recycled electrical goods due to regulations" (12 companies) and the "administration of the directive varies between countries" (10 companies). For RoHS, many companies pointed out the problems related to the future development of the regulations, such as the "unpredictability for revisions of 'exemption list'" (18 companies) and the "expansion of scope of 'hazardous substance' designation" (15 companies). In December 2008, an RoHS amendment plan was announced, and discussion will be made by the European Commission hereafter (see Diagram 33).

Diagram 32: Existence of Problems in Complying with EU Environmental Regulations



Source: JETRO Survey, Japan External Trade Organization

Diagram 33: Specific Issues in Complying with EU Environmental Regulations



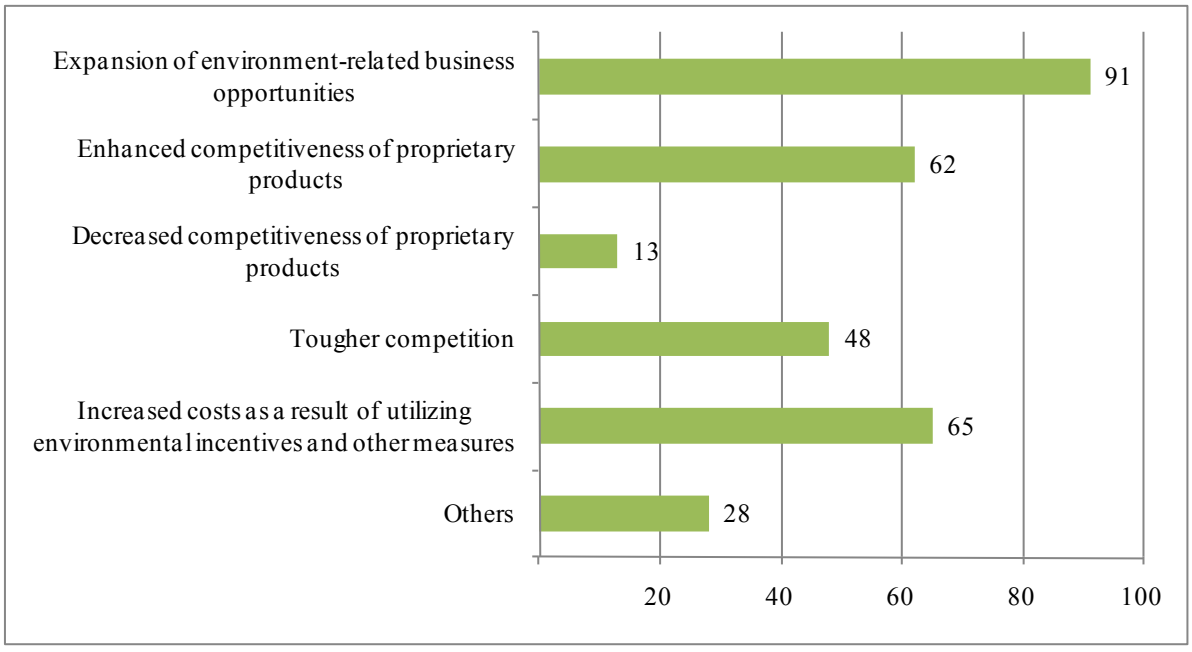
Source: JETRO Survey, Japan External Trade Organization

2. Impact of environmental incentives and/or economic stimulus measures in environmental areas

In Europe, some countries have introduced incentives for the purchase and installment of environmentally friendly products, such as energy-efficient products, through such measures as the provision of subsidies, tax relief and tax refunds. Additionally, as part of economic stimulus measures against the global economic downturn triggered by the financial crisis, countries such as Germany have introduced environment-related economic stimulus measures, such as the "Environmental Premium" system, under which the government provides subsidies to people who replace their car (after a certain duration of use) with a new car that satisfies certain environmental regulations (Euro5/Euro6). In this regard, in the survey this time, we asked the Japanese manufacturing affiliates in Europe about the impact of the environmental incentives and environment-related economic stimulus measures implemented by the government of each country (multiple answers allowed).

According to the survey result, 91 out of 238 respondent companies selected the "expansion of environment-related business opportunities" and 62 replied "enhanced competitiveness of proprietary products"; i.e., many companies take the government's incentives positively. On the other hand, many provided negative answers, such as "increased costs as a result of utilizing environmental incentives and other measures" (65 companies) and "tougher competition" (48 companies). The result of the survey indicates that the environmental incentives and economic stimulus measures by the government do not always work favorably for the Japanese manufacturers that have advanced technology in environmental areas (see Diagram 34).

Diagram 34: Impact of Environmental Incentives and/or Economic Stimulus Measures in Environmental Areas



Source: JETRO Survey, Japan External Trade Organization

VI. FTAs between the EU and Other Countries

[Impacts of the EU FTA]

- The EU-South Korea FTA is expected to be a "substantial disadvantage" for high-tariff industries, because the elimination of tariffs will lead to a decline in relative competitiveness.
- The EU-ASEAN FTA is expected to be a "substantial advantage", due to the reduction of the procurement cost of parts.
- More than 40% of the respondent companies said that the EU-Japan FTA is a "substantial advantage". However, some companies show concern that having a local plant may become less meaningful and worry about tougher competition among Japanese affiliates.
- Many companies answered "no impact", except for the EU-Japan FTA. However, there is a possibility that they are only evaluating the current impact of the removal of tariffs. Other impacts need to be considered as well.

In October 2006, the EU announced the "Global Europe: Competing in the World", a strategy that defines new external trade and sets out a policy of actively pursuing bilateral FTAs with countries that can satisfy certain requirements. Based on this strategy, the EU began negotiations for FTAs with ASEAN and South Korea in May 2007 and with India in June 2007. Further, the EU also began negotiations with Ukraine in February 2008 and Canada in May 2009. With regard to the EU-South Korea FTA, negotiations were completed at the South Korea-Sweden Summit in July 2009, and it was confirmed that the nations plan to sign the treaty by the end of the year.

If FTAs are established between the EU and these countries/regions, the deregulation and liberalization of trade and investments, such as the elimination of tariffs, may bring both advantages and disadvantages to Japanese manufacturing affiliates in Europe. Thus, inquiries were made regarding the expected impact.

1. The EU-South Korea FTA

In terms of advantages and disadvantages, the answers varied depending on the participants of the FTA. With respect to the EU-South Korea FTA, which reached an agreement on general matters in July 2009, and as far as impact on Japanese affiliates is concerned, 58.4% of the companies (out of 180 respondent companies) said that they expected "no impact". However, the companies that answered that they expected a "substantial disadvantage" (11% or 34 companies) exceeded those that answered "substantial advantage" (6.5% or 20 companies), indicating that relatively more companies think the FTA will have more negative impact than other FTAs. This trend is more obvious in Central and Eastern Europe, where 17.6% answered "substantial disadvantage", while 11.8% cited "substantial advantage". On the other hand, in Western Europe, 9.2% cited "substantial disadvantage" and 5.0% replied "substantial advantage".

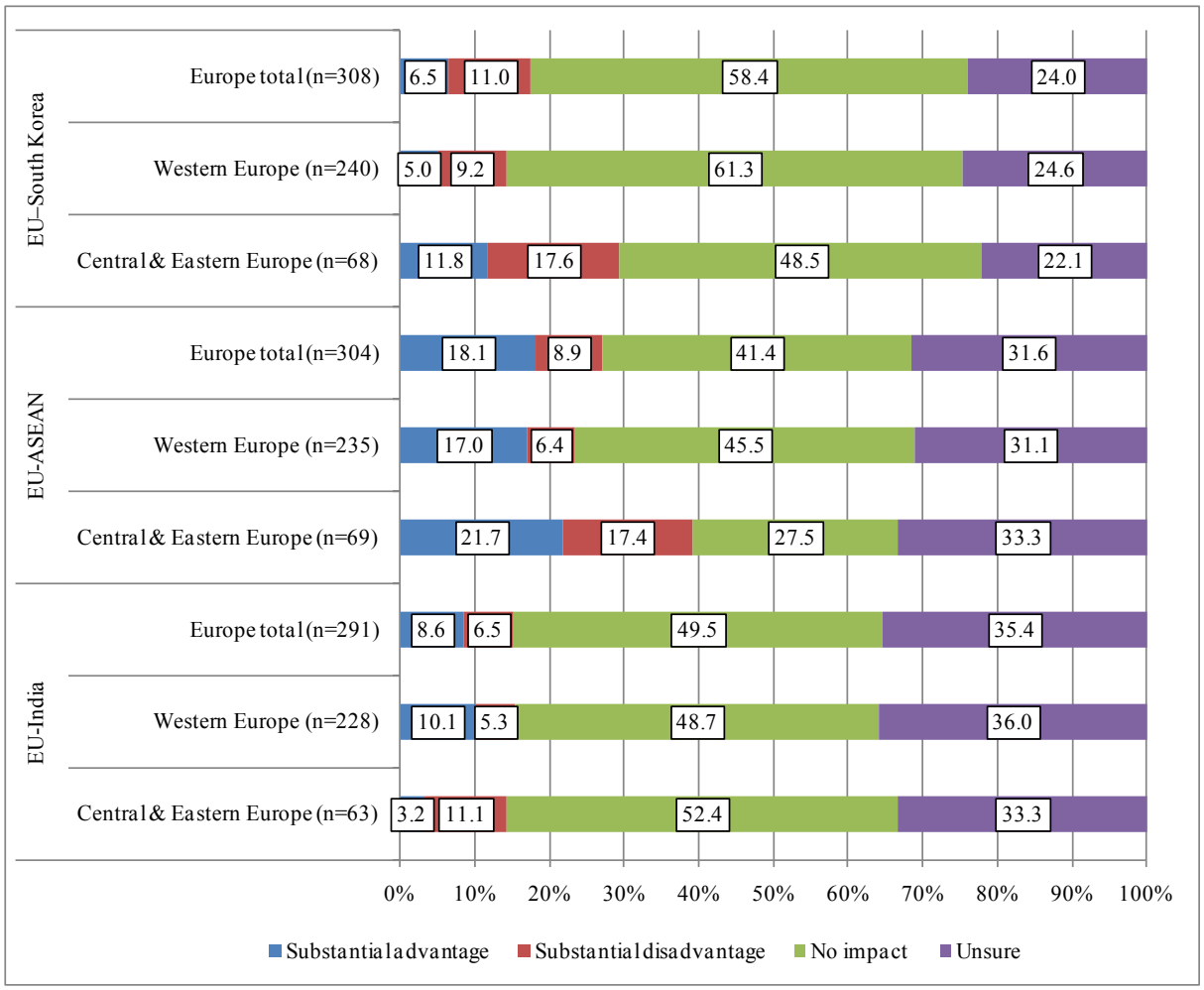
Most of the reasons for expected "substantial disadvantage" related to concerns about tougher competition due to the inflow of South Korean products—the influx of cheaper products, in particular. On

the other hand, some mentioned advantages, although the number of companies were small, by pointing out the reduction of parts procurement costs and better opportunities for market entry due to the removal of tariffs as favorable factors.

By industry, many companies in the automobile or TV-related industries, where high tariffs are imposed, expected a "substantial disadvantage". Almost half of those in transportation machinery (automobiles, motorcycles), 11.1% of those in transportation machinery parts (automobiles, motorcycles), and 23.8% of those in electric and electronic machinery said the FTA provides a "substantial disadvantage", totaling nearly half of the companies that answered "substantial disadvantage". The EU imposes high tariffs on automobile bodies, ranging from 10% (passenger cars, etc.) (MFN base; the same hereinafter) to 22% (for trucks). Tariffs on some electric and electronic machinery are also high; 12.5% is imposed on video cameras and recorders, 14% on LCD monitors (suspended until the end of 2010, as a tentative measure) and 14% on TVs.

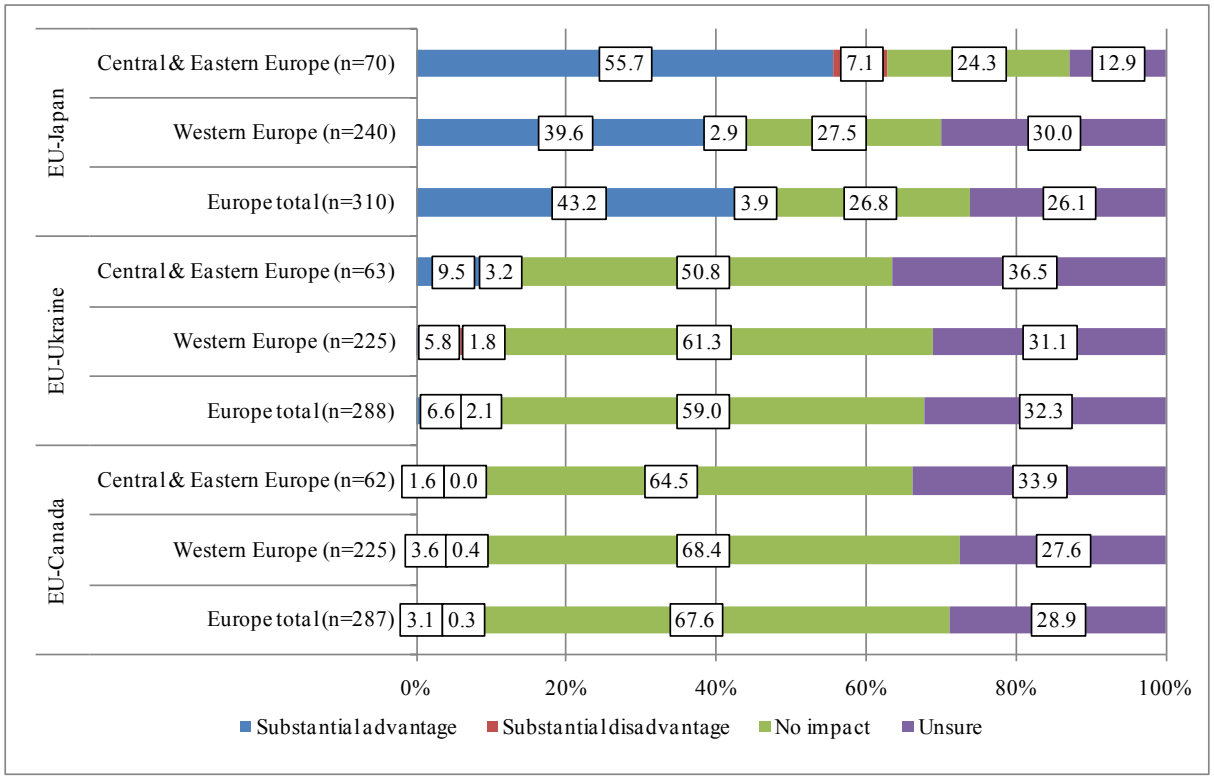
These concerns are supported by the anxieties that the Japanese manufacturers' relative competitiveness against South Korean counterparts in the European markets may be lowered if the EU-South Korea FTA is established and tariffs are removed. Additionally, for LCD monitors and TV parts, tariffs are currently and tentatively suspended voluntarily by the EU; however, the EU has the discretion to re-introduce these at any time. On the other hand, South Korean companies do not have to worry about the revival of high tariffs once they are removed by the EU-South Korea FTA. In other words, even if the competitive conditions faced by two countries with regard to tariffs are currently the same, Japan has more risks and uncertainties for the future, as it does not have any FTA with the EU. Further, Korean companies that are now free from anxieties about high tariffs, thanks to the FTA, may solicit the EU for the revival of tariffs to maximize the benefit of the FTA.

Diagram 35: Impact of FTAs between EU and Asian Countries (Global Europe)



Source: JETRO Survey, Japan External Trade Organization

Diagram 36: Impact of FTAs between EU and Non-Asian Countries



Source: JETRO Survey, Japan External Trade Organization

2. The EU-ASEAN FTA

On the other hand, concerning the EU-ASEAN FTA, the percentage of companies that expect a "substantial advantage" was 18.1% (55 respondent companies)—much higher than the percentage of companies that expect a "substantial disadvantage", which was 8.9% (27 companies). By region, the number of companies that expect this "substantial advantage" was 17% (40 companies) in Western Europe and 21.7% (15 companies) in Central and Eastern Europe—these percentages are higher than the companies that answered that they expect a "substantial disadvantage" in both regions, although 17.4% or 12 companies in Central and Eastern Europe expected a "substantial disadvantage". Further breakdown into industry in Central and Eastern Europe shows that 25.0% of the transportation machinery parts (automobiles, motorcycles) manufacturers expect a "substantial advantage", while 17.9% expect a "substantial disadvantage". The difference between positive and negative responses is not significant. On the other hand, in Western Europe, 21.7% of the transportation machinery parts (automobiles, motorcycles) manufacturers expect a "substantial advantage", while 6.5% mentioned that they expect a "substantial disadvantage"—the positive answers exceeded the negative ones by a large margin.

Concerning specific reasons for these answers, while some companies expect a "substantial advantage", as they can reduce procurement costs mainly for parts, others cited a "substantial disadvantage" as local production may no longer be required due to tougher competition from cheaper ASEAN products or the switch to ASEAN as a supplier of parts.

The above survey results indicate that benefits can be expected from the EU-ASEAN FTA, in terms of the procurement of some parts; however, it depends on the company's current procurement model or how their proprietary products are positioned into the entire manufacturing process (upstream or downstream), in terms of whether they realize an advantage or disadvantage from the FTA. In other words, the companies that expect advantages to come from the EU-ASEAN FTA are considered to have a business model in which the company sources parts from ASEAN countries (or their affiliate plant does, in some cases), assembles them in Central or Eastern Europe and provides the assembled product to Western Europe. In this kind of business case, for the companies that are involved in the middle process in Central or Eastern Europe and the downstream process in Western Europe, the EU-ASEAN FTA provides an advantage (the reduction of the parts procurement cost). On the other hand, for plants in Central or Eastern Europe that manufacture upstream parts, sourcing parts from ASEAN countries may make their existence less meaningful.

3. The EU-India FTA

For the EU-India FTA, those companies that expected a "substantial advantage" (8.6%, 25 companies) exceeded those fearing a "substantial disadvantage" (6.5%, 19 companies). While the most frequently replied answer was "no impact" (49.5%, 144 companies), responses of "unsure" (35.4%, 103 companies) were relatively higher than that of other FTAs. This might be due to the fact that negotiation over the EU-India FTA has made virtually no progress since it started in June 2007, and there is no clear prospect of the FTA coverage.

By region, while "substantial advantage" (10.1%, 23 companies) exceeded "substantial disadvantage" (5.3%, 12 companies) in Western Europe, "substantial disadvantage" (11.1%, 7 companies)" was higher than "substantial advantage" (3.2%, 2 companies) in Central and Eastern Europe. By industry, it is noteworthy that 16.3% (7 companies) answered "substantial advantage" for transportation machinery parts (automobiles, motorcycles) in Western Europe.

4. The EU-Canada FTA

Most companies answered that they expected "no impact" concerning the EU-Canada FTA (67.6%, 194 companies). Although negotiations recently started just in May 2009, and since it's not clear what shape the FTA will take, there were not many companies that answered "unsure" (28.9%, 83 companies). As there are not many companies that directly compete with Canadian companies, it must be safe to consider that there is not much direct impact from this FTA on Japanese manufacturing affiliates. However, as it is the first FTA for EU to conclude with one of the G8 countries, it shows the change of their previous stance of not concluding FTAs with industrialized nations: therefore, it is expected to still have an indirect impact. Additionally, even without direct impact, Japanese companies need to follow the progress of the development of this FTA and its contents carefully, as it can be referred to and studied when EU possibly concludes FTAs with Japan in the future.

5. The EU-Ukraine FTA

For the EU-Ukraine FTA, the largest number of companies answered "no impact" (59.0%, 170 companies). The percentage of the companies that answered "substantial advantage" was slightly higher in Central and Eastern Europe (9.5%, 6companies) than in Western Europe (5.8%, 13 companies). While the reason for such "substantial advantage" included the enhancement of procurement sources and reduction of procurement costs, more answers were related to the creation of opportunities of entry into the Ukraine market. In European business, there seems to be a limited number of companies that have established supply chains including the Ukraine. However, if the EU-Ukraine FTA is established and the regulation reform is implemented in Ukraine, a more attractive environment will be provided, and the country may be reconsidered as a procurement source/provider of parts and finished products.

6. The EU-Japan FTA

As expected, the percentage of companies that answered that the EU-Japan FTA would be a "substantial advantage" was 43.2% (134 companies), much higher than other FTAs. Of the total, 39.6% of the Japanese manufacturing affiliates in Western Europe (95 companies) and 55.7% of the affiliates in Central and Eastern Europe (39 companies) answered that the EU-Japan FTA would provide a "substantial advantage".

On the other hand, it is noteworthy that 7.1% of the Japanese manufacturing affiliates (5 companies) in Central and Eastern Europe answered "substantial disadvantage". The reason for this is considered to be that the significance of manufacturing products in Central and Eastern Europe locally may be reduced due to the elimination of tariff costs, which may mean a disadvantage for the manufacturers that have production bases in the concerned area.

Furthermore, of the total, 26.8% (83 companies) selected "no impact". The reason for this choice is considered to be that, if the company has already established a supply chain in Europe, the sourced parts may already be free from tariffs even if they are procured in Japan. Additionally, the reason for 26.1% (81 companies) answering "unsure" may be because the contents of the treaty are uncertain as the negotiation for this has yet to even start, and the possibility that, not only their own company, but also their Japanese competitors might enter the market if such entry into the local market by Japanese companies becomes easier.

7. Conclusion

Out of the total, "No impact" was the most frequently selected answer for every FTA except for the EU-Japan FTA. However, when delving further into the reason why companies answered "substantial advantage" or "substantial disadvantage", it becomes evident that the respondent companies are really only evaluating the impact of the removal of tariffs and are not considering the other impacts of the treaty. It is certainly difficult to predict the impact of an FTA, other than tariffs, in particular, when negotiations for the treaty haven't even begun or agreements have not yet been made, and when the content of the treaty is unclear. Still, FTAs certainly cover more areas than just tariffs, such as the removal of non-tariff barriers, the opening of the service industry or government procurement areas, and the establishment of dispute settlement mechanisms. It must be noted by the companies answered "no impact" that they will not be free

from the indirect impact of these FTAs.

Turkey

I. Overview of Japanese Manufacturing Affiliates in Turkey

Most of the 17 Japanese manufacturing affiliates in Turkey belong to automotive and related industries.

The latest survey revealed that 17 Japanese manufacturing affiliates are operating in Turkey, as of the end of June 2009. By industry, three out of the 17 affiliates are based in the "transportation machinery" sector and 10 are based in the "transportation machinery parts" sector, which indicates, if two companies in the "rubber products" sector are included, 15 companies are involved in automobile related operations. The remaining two affiliates are each involved in the "food products, agricultural and fisheries production processing" industries, along with "other manufacturing" industries.

In Turkey, auto manufacturers almost completed their production base establishment in the early 1990s, followed by auto parts manufacturers, which came into the market by early 2000. The original sales destination of their products was the domestic market. However, mainly due to the decline in domestic sales at the time of the economic crisis from the middle of the 1990s to the early 2000s, Turkey transformed into a "production and export base for the EU" for Japanese manufacturers.

II. Business Conditions and Prospects of Japanese Manufacturing Affiliates in Turkey

- For financial results in 2008, the same number of companies recorded operating "profit" and "loss". Business performance was worse than the previous year overall.
- For 2009, more than half of the companies expected a "loss". While more than 80% of the companies think their financial performance would decline in 2009.
- Also for the operating results of 2010, conservative prospects have been spreading.

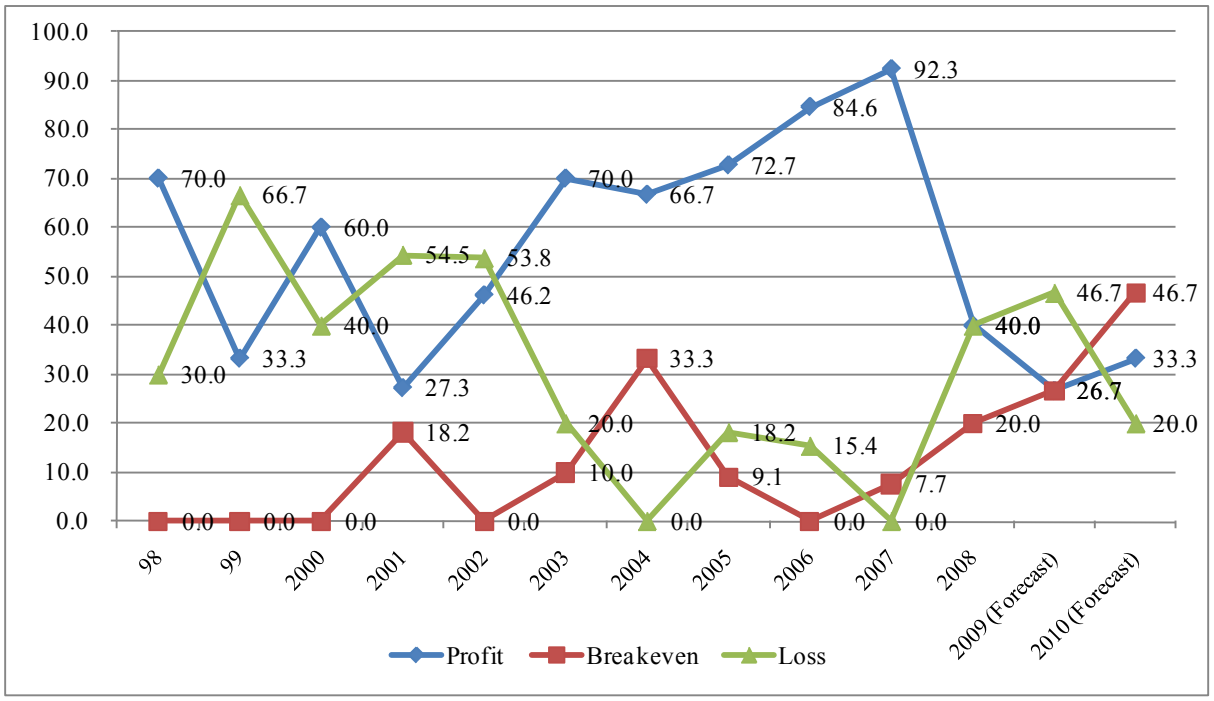
1. Operating "profit" and "loss" recorded by the same number of companies in 2008; business performance worse than the previous year

For 2008, among the 15 respondent companies, six companies each answered that they recorded operating "profit" and "loss", while the remaining three companies said they would "breakeven". In the previous year's survey, approximately 70% of the respondent companies expected "profit" for 2008, but some seem to have been forced to make a downward revision of financial performance, due to the global financial crisis seen at the end of the year (see Diagram 1).

Compared with the operating profit of 2007, operating profit for 2008 has "declined" by almost all respondent (13 companies). The most dominant reason among those respondents was "global economic downturn stemming from financial crisis" (11 companies), "decreased sales in overseas markets" (nine companies) and "decreased sales in domestic market" (eight companies).

According to the Automotive Manufacturers Association (OSD) in Turkey, domestic automobile production in 2008 (excluding tractors) was 1,147,000 units (up 4.3% from the previous year), while the number of exported cars increased to 910,000 units (up 11.2% from the previous year), rising the export ratio to 79.3% (up two consecutive years from 75.5% in 2007 and 69.7% in 2006).

Diagram 1: Operating Profit for Japanese Manufacturing Affiliates in Turkey



Source: JETRO Survey, Japan External Trade Organization

2. 2009 forecast shows "loss" is expected by many companies; 80% predict decline in business performance

For the 2009 forecast, the largest number of the companies (seven companies out of 15 respondent companies, or 46.7%) expected "loss". However, four companies expected "profit" and "breakeven", respectively.

Compared with the operating profit of 2008, many companies predicted a "decline" (12 companies or 80.0%) for 2009. Meanwhile, two companies said things would "remain the same", and one answered that things would "improve" (see Diagram 2).

The most dominant reason among the respondents that projected a "decline" (multiple answers allowed) was "decreased sales in overseas markets" (11 companies), "decreased sales in domestic market" (10 companies) and "global economic downturn stemming from financial crisis" (10 companies). The companies expect that the economic slowdown from the end of 2008 will continue.

In Turkey, the business performance of export-oriented industry (such as automobiles) has continued to be sluggish, due to the economic slowdown in Europe. The government expects the real GDP growth rate to decline from 1.1% in 2008 to -3.6% in 2009.

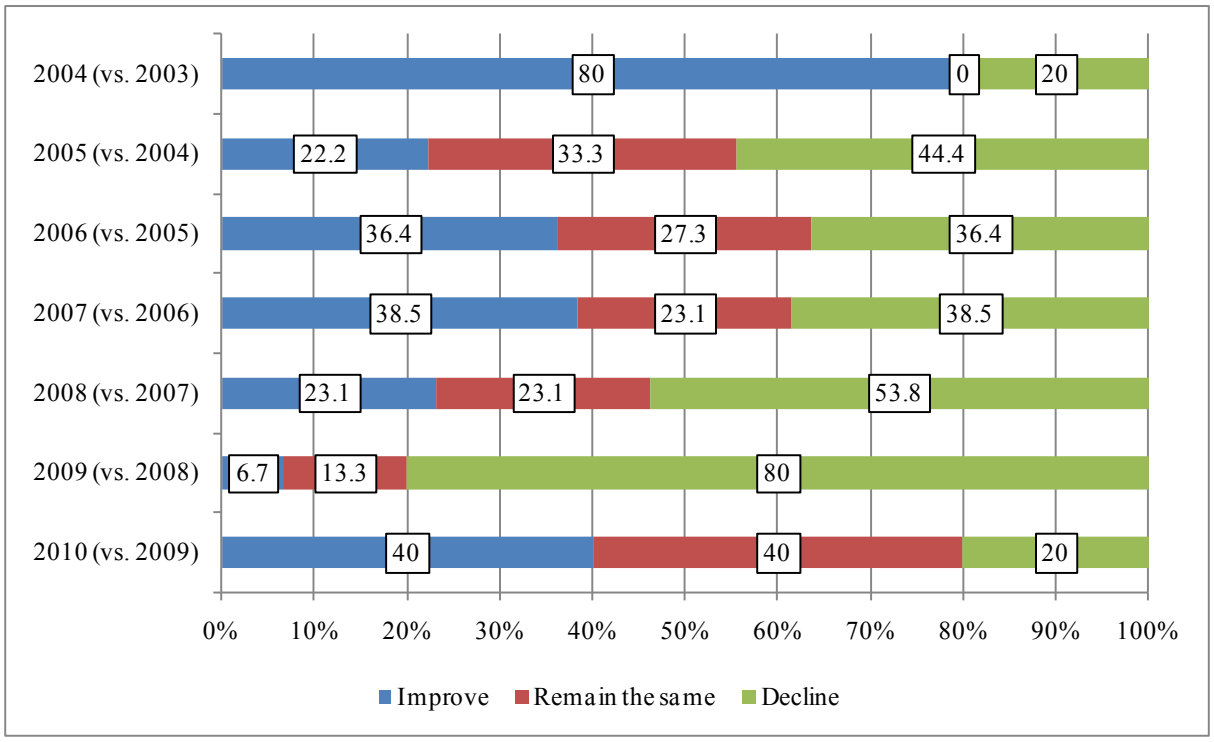
As part of economic stimulus measures, the temporary special consumption tax (SCT) on automobiles and home electronics introduced in March 2009 contributed to the tentative boost in demand. The number of automobiles sold in Turkey from January to June in 2009 (cumulative) was 282,000 units, up 1% compared to the same period in the previous year. There was a sign of improvement, as it was a 5% year-on-year reduction from January to May. However, the cumulative number from January to July was

again lower than the same period last year, showing that the impact of the tax relief is getting weaker. Additionally, the number of automobiles manufactured in the period from January to June 2009 was 394,000, which is a significant (45%) decrease from the same period last year. Manufacturers operating in Turkey are still waiting for the recovery of demand in other areas, such as Europe.

3. Conservative 2010 forecast for operating profit

Concerning 2010 operating profit (15 companies), five companies expected a "profit" (33.3%), seven expected to "breakeven" (46.7%) and three predicted that they would see a "loss" (20%). Compared to companies in Western and Central/Eastern Europe, the percentages of the companies that expected to "breakeven" and experience a "loss" were higher. Also for the comparison with the 2009 forecast (15 companies), six companies expected to "improve" (40.0%), six said they would "remain the same" (40.0%) and three said things would "decline" (20.0%). Although at least 80% of the companies expect that financial performance will bottom out, the percentages of the companies that answered "remain the same" and "decline" were once again higher than the Japanese manufacturing affiliates in Western and Central/Eastern Europe. In 2009, company attitudes turned conservative, in general, and some companies have even frozen the production enhancement plan—this is reflected in the conservative predictions and forecasts made by companies on the whole.

Diagram 2: Operating Profit Forecast for Japanese Manufacturing Affiliates in Turkey



Source: JETRO Survey, Japan External Trade Organization

III. Procurement, Sales and Production

1. Procurement of parts and materials (excluding parts for production equipment used in the production process)

- Procurement from domestic sources in Turkey is to be "expanded/reinforced", while that from Western Europe is to be" kept present level". Procurement from Japan will be "decreased".
- Among the current procurement sources of parts and materials, Japanese manufacturing affiliates in Turkey are planning to "expand/reinforce" purchase with domestic sources. While the companies are to "keep present level", procurement from Japan will be expected to "decrease".
- More and more companies are shifting toward Asia and neighboring areas of Europe for future procurement sources.

(1) Present procurement sources and procurement policy: Procurement from domestic sources (Turkey) is to be enhanced, while sourcing from Japan is to be reduced.

The country or region named most often by Japanese manufacturing affiliates in Turkey (15 respondent companies) as a major procurement source of parts and materials (multiple answers allowed) was "Japan", which was named by 12 companies, followed by "Turkey" (11) and "Western Europe" (11)—the top three countries/regions were the same as the previous year (see Diagram 3).

When questioned about their future procurement policies regarding current sources, the percentage mentioning "expand/reinforce" was the highest for Turkey (seven companies or 63.6%), continuing from the previous year. Among the affiliates that procure from sources in Western Europe, eight companies, the largest number, answered that they plan to "keep present level" of procurement (three for Germany, three for Italy and two for France), with three answering that they plan to "expand/reinforce" procurement. Among the affiliates that procure sources in Japan, seven companies (58.3%) plan to "decrease" their procurement from Japan. The response rate was high (see Diagram 4).

For other countries/regions, five companies said they are currently sourcing from ASEAN, four from Central and Eastern Europe, three from North America, two from China and one from South Korea, Russia and CIS countries and North Africa. With regard to future policy, three companies selected "expand/reinforce" for ASEAN (two for Indonesia, one for Malaysia and one for Thailand [including multiple answers]), and one company each also said that they would "expand/reinforce" procurement from Central/Eastern Europe (Czech Republic), North America, China, South Korea, Russia and CIS countries and North Africa (Egypt). No companies expected a "decrease" for these countries/regions.

(2) Future promising procurement sources: the shift to Asia and regions neighboring Europe becoming obvious

When asked about future procurement sources (10 companies, multiple answers allowed), the companies mentioned Turkey (five companies), Central and Eastern Europe (four companies—two for Poland and two for Bulgaria), Western Europe (three companies—one each for Germany, France and Italy), ASEAN (three companies—one each for Indonesia, Malaysia and the Philippines), Russia and CIS countries (two companies—one each for Russia and the Ukraine), China (two companies), North Africa (one company for Egypt), India (one) and Japan (one).

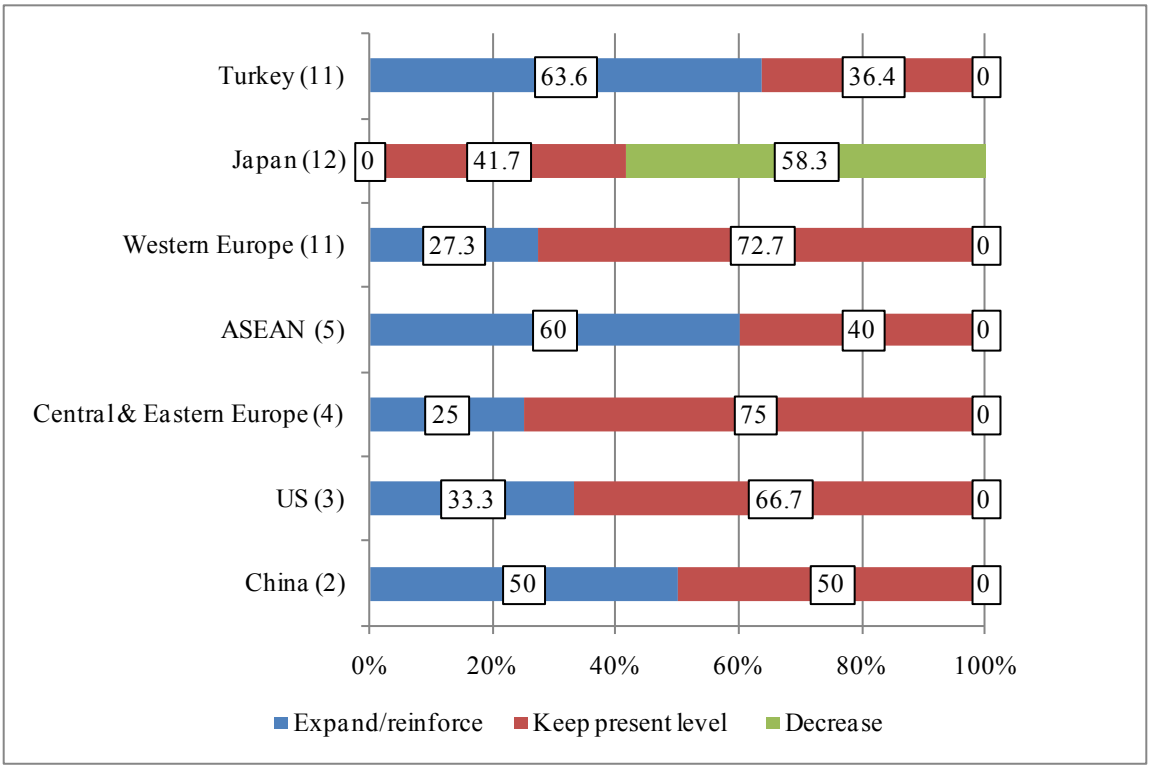
Turkey was mentioned as a current major procurement source, as well as a target of future procurement expansion. Additionally, Russia and CIS countries and North Africa, which did not receive any responses in the previous survey, were locations that companies expected to "expand/reinforce" as a present procurement policy, with some companies even starting to consider them as future prospective procurement sources. This shows that the target of optimum procurement for companies in Turkey has been expanding to neighboring southeastern areas.

Diagram 3: Status of Major Procurement Sources (Countries/Regions)
(Multiple Answers Allowed)

Japan	Western Europe	Turkey	ASEAN	Central and Eastern Europe	Total number of companies responded
12	11	11	5	4	15

Source: JETRO Survey, Japan External Trade Organization

Diagram 4: Future Procurement Policies of Japanese Manufacturing Affiliates in Turkey Regarding Current Procurement Sources



Source: JETRO Survey, Japan External Trade Organization

2. Sales destinations and policies

- The principal sales destinations are “Turkey”, “Western Europe” and “Central and Eastern Europe”.
- The affiliates plan to expand and reinforce sales in “Turkey”, “Western Europe” and “Russia and CIS countries”.

(1) Present sales destinations: neighboring countries

Regarding sales destinations for Japanese manufacturing affiliates in Turkey (15 companies, multiple answers allowed), “Turkey” was named by the largest number of companies (13 companies), followed by “Western Europe” (nine companies), “Central and Eastern Europe” (seven), “Russia and CIS countries” (four), “North Africa” (four) and the “Middle East” (two) (see Diagram 5). Compared to the previous year, the affiliates naming Turkey and North Africa as their sales destinations increased in number by two companies each.

Diagram 5: Sales Destinations (Countries/ Regions) (Multiple Answers Allowed)

Turkey	Western Europe	Central and Eastern Europe	Russia & CIS	North Africa	Total number of companies responded
13	9	7	4	4	15

Source: JETRO Survey, Japan External Trade Organization

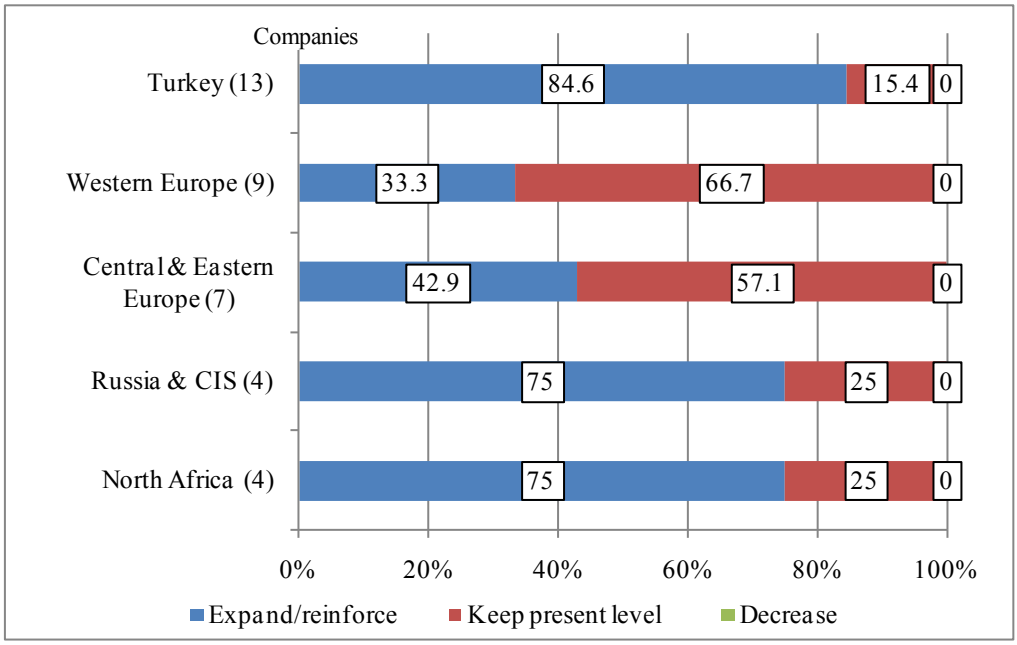
(2) Future sales policies: Companies plan to "expand/reinforce" sales in "Turkey", "Western Europe" and "Russia and CIS countries"

Eleven out of the 13 affiliates (84.6%) selling products intended for the domestic market in "Turkey" and three out of the nine affiliates selling products intended for the "Western Europe" market replied that they planned to "expand/reinforce" sales in the future (in France and the UK, three companies each, and others; multiple answers allowed). For Western Europe, in particular, seven out of 10 companies said they would "expand/reinforce" sales there, but the current sluggish economic situation shows that companies cannot continue to rely on sales in Europe.

The seven affiliates selling products intended for the "Central and Eastern Europe" market were divided, with three companies planning to "expand/reinforce" sales (the Czech Republic, Slovakia, Romania and Bulgaria), and four companies planning to "keep present level". Three companies each said they would expand or reinforce sales in "Russia and CIS countries" and "North Africa" (three for Russia, and one for Morocco, Algeria and Egypt each, and others), and two companies (all of the respondents) said they planned to "expand/reinforce" sales in the "Middle East" (see Diagram 6).

Among the leading potential "future sales destinations", Italy, Spain, Turkey and Russia were named by three affiliates respectively, followed by Tunisia and Egypt (two companies each).

Diagram 6: Future Sales Policies for Present Sales Destinations



Source: JETRO Survey, Japan External Trade Organization

3. Production

- For the next 1–2 years, more companies than in the previous survey say they will "maintain present level", which seems to reflect the current economic situation.
- Specifically, many of the affiliates that plan "expansion" of their production aim for the "Expansion of business through additional investments" and the "Expansion/diversification of product lines".
- In the medium to long term, "Turkey" and "Russia" are rated highest by Japanese affiliates in Turkey as promising production bases for their products.

(1) Business development over the next 1–2 years: more companies than the previous survey say they will "maintain present level", reflecting the current economic situation

Out of the 15 Japanese manufacturing affiliates in Turkey that responded to this survey, five companies answered that they were looking for their business "expansion" in the next one or two years, and eight companies answered that they would "maintain present level", while two companies said that they planned for "reduction". The number of companies that replied "expansion" decreased, while the number stating that they would "maintain present level" increased. Additionally, two companies selected "reduction", which had not been selected by any company in the previous survey. No company stated either transfer or withdrawal on their production.

When the companies that said that they planned to expand their business activities were asked about specific policies (multiple answers allowed), out of the five companies that responded, four answered that

they planned the “expansion/diversification of product lines”, while three said that they planned the “expansion of business through additional investments”. The rate of the companies that selected these two items exceeds the average ratios of Western Europe, as well as that of Central and Eastern Europe. Additionally, “increase in high value-added product lines”, “reinforcement of design/R&D functions” and “establishment of new production bases” were cited by one company. On the other hand, the specific policy for reduction was “cease production of certain product lines”.

(2) Countries/regions considered promising mid- to long-term (5–10 years) locations for production: “Turkey” and “Russia” highly evaluated

When Japanese manufacturing affiliates in Turkey were questioned about the countries/ regions that they consider to be “promising production bases for their company’s products”, responses were received from 11 companies, and 22 countries were mentioned.

“Russia” and “Turkey” were selected by five companies respectively, which were at the top of the poll, followed by “China” (three companies), “India” and “North Africa (Egypt)”, each selected by two companies.

IV. Management Problems & Attractions/Advantages as Production Bases

- The attractions/advantages of Turkey being a production base are its "high quality of workforce" and "ease in securing factory workers".
- As managerial issues, companies are concerned about impacts on cost, such as "volatile exchange rate fluctuations" and a "high labor cost growth rate".

1. The attractions/advantages: evaluating the "high quality of workforce" and "ease in securing factory workers"

Concerning the attractions/advantages of having a production base in Turkey, 12 out of 15 respondent companies (80%) cited the "high quality of workforce", while 10 companies (66.7%) mentioned the "ease in securing factory workers".

As shown in the above survey result, the high quality of the workforce has been well evaluated by people concerned with manufacturers operating in Turkey, and the Turkish workers are famous for their diligence and are often "not overly concerned with working overtime". According to data for the average working hours per week for the manufacturing industry (for February 2009), announced by the International Labor Organization (ILO) in August 2009, the average working hours of Turkish people is reported to be 52.0 hours. For neighboring nations, it was 41.5 hours in Poland, 40.3 hours in the Czech Republic, 40.6 hours in Slovenia, 41.2 hours in Bulgaria, 41.0 hours in Romania and 42.2 hours in Greece. This data shows how hardworking the Turkish people are. Additionally, according to the Investment Support and Promotion Agency of Turkey (ISPAT), their low absentee rate must be an "appealing" point, as it pairs well with their ability to work longer hours.

The "ease in securing factory workers" is mainly due to the fact that the labor force in Turkey is extremely broad in terms of age—Turkey has a large young labor pool to draw from. According to estimates by the United Nations, the median age of the workforce in Turkey is 28.3 years in 2010, almost 10 years younger compared to Western Europe (42.2), Eastern Europe (38.5), and even Russia (38.1) and the Ukraine (39.5). Additionally, the population growth rate from 2010 to 2015 was 1.10%, which is expected to be higher than Western Europe (0.13%) and Eastern Europe (-0.34%). Incidentally, the labor pool in Turkey (as of May 2009) was 24,840,000.

The above two factors were highly evaluated by the majority of respondent companies, and other than that, six companies (40.0%) referred to "low labor costs" and "offers strategic location" as advantages. Additionally, five companies (33.3%) mentioned "high labor productivity" and the "quality of end products" as advantages. While the number of the companies that responded as such was relatively small, some companies pointed out the attractiveness of "quality", "procurement costs" and "delivery dates are strictly kept", in the category of "procurement of parts and materials" (three companies each, or 20.0%).

Some companies also mentioned that the people in Turkey are "friendly with Japanese people, and Japanese language is widely accepted in the country".

Such high evaluation of overall labor matters is considered to have resulted in the "satisfaction level of the product quality".

2. Management problems: company concerns regarding impacts on cost, such as "volatile exchange rate fluctuations" and the "high labor cost growth rate"

In the latest survey, the top managerial issue was "global economic downturn stemming from financial crisis", cited by 13 out of 15 respondent companies (86.7%), followed by "finance: volatile exchange rate fluctuations" (12 companies or 80.0%) and "labor issues: high labor cost growth rate" (11 companies or 73.3%) (see Diagrams 7 and 8).

Diagram 7: Management Problems (2008)

(n=13)

Category	Problem	Responses	Percentage
Labor Issues	High labor cost growth rate	12	92.3 %
Finance	Volatile exchange rate fluctuations	10	76.9 %
Others	Others	8	61.5 %
Standards, certifications and regulations	High costs of acquiring CE mark	7	53.8 %
Parts and materials procurement	Procurement costs	6	46.2 %
Political, economic, and social conditions	Political conditions	6	46.2 %
Others	Others	6	46.2 %
Political, economic, and social conditions	Public safety and social conditions	6	46.2 %
Trade legislation/procedures	Complicated administrative procedures and/or lack of transparency	5	38.5 %
Investment legislation/procedures	Visa/work permits	4	30.8 %
Labor Issues	Difficulty in securing engineers	4	30.8 %
Parts and materials procurement	Quality	4	30.8 %
Insufficient infrastructure	Power supply	4	30.8 %
Others	Others	4	30.8 %
Investment legislation/procedures	Frequent legislation revisions	3	23.1 %
Investment legislation/procedures	Complicated administrative procedures and/or lack of transparency	3	23.1 %
Labor Issues	High labor costs	3	23.1 %
Finance	Difficulty in obtaining credit	3	23.1 %
Insufficient infrastructure	General road conditions	3	23.1 %
Insufficient infrastructure	Communications	3	23.1 %
Trade legislation/procedures	High tariff rates	2	15.4 %
Tax systems/procedures	High corporate tax rates	2	15.4 %
Tax systems/procedures	Others	2	15.4 %
Labor Issues	Quality of workforce	2	15.4 %
Parts and materials procurement	Deliveries	2	15.4 %
Environmental regulations	REACH	2	15.4 %
Others	Living environment for foreigners	2	15.4 %
Trade legislation/procedures	Rule-of-origin	1	7.7 %
Trade legislation/procedures	Others	1	7.7 %
Investment legislation/procedures	Lack of transparency in investment incentive schemes	1	7.7 %
Investment legislation/procedures	Others	1	7.7 %
Tax systems/procedures	Complicated administrative procedures and/or lack of transparency	1	7.7 %
Labor Issues	Difficulty in securing managerial personnel	1	7.7 %
Labor Issues	Difficulty in securing clerical workers	1	7.7 %
Labor Issues	Union activities/strikes	1	7.7 %
Labor Issues	Others	1	7.7 %
Finance	Collection of receivables	1	7.7 %
Parts and materials procurement	Others	1	7.7 %
Insufficient infrastructure	Port facilities	1	7.7 %
Insufficient infrastructure	Others	1	7.7 %
Insufficient infrastructure	Water	1	7.7 %
Insufficient infrastructure	Others	1	7.7 %
Environmental regulations	RoHS	1	7.7 %
Environmental regulations	ELV	1	7.7 %
Trade legislation/procedures	Anti-dumping measures	0	0.0 %
Trade legislation/procedures	Others	0	0.0 %
Tax systems/procedures	Double taxation (in both Japan and the country where operations are located)	0	0.0 %
Standards, certifications and regulations	Others	0	0.0 %
Standards, certifications and regulations	Others	0	0.0 %
Labor Issues	Difficulty in securing factory workers	0	0.0 %
Labor Issues	Others	0	0.0 %
Finance	Others	0	0.0 %
Environmental regulations	WEEE	0	0.0 %
Environmental regulations	EuP, ErP (Eco-design)	0	0.0 %
Environmental regulations	Euro5	0	0.0 %
Environmental regulations	Others	0	0.0 %
Others	EU competition law	0	0.0 %
Others	Insufficient protection of intellectual property rights	0	0.0 %
Others	Others	0	0.0 %

Diagram 8: Management Problems (2009)

(n=15)

Category	Problem	Responses	Percentage
Political, economic, and social conditions	Global economic downturn stemming from financial crisis	13	86.7 %
Finance	Volatile exchange rate fluctuations	12	80.0 %
Labor Issues	High labor cost growth rate	11	73.3 %
Standards, certifications and regulations	High costs of acquiring CE mark	8	53.3 %
Parts and materials procurement	Shortage of domestic procurement sources	7	46.7 %
Insufficient infrastructure	Power supply	7	46.7 %
Political, economic, and social conditions	Domestic economic conditions	7	46.7 %
Trade legislation/procedures	Complicated administrative procedures and/or lack of transparency	6	40.0 %
Investment legislation/procedures	Frequent legislation revisions	6	40.0 %
Investment legislation/procedures	Visa/work permits	6	40.0 %
Insufficient infrastructure	Communications	6	40.0 %
Trade legislation/procedures	Customs clearance issues	5	33.3 %
Tax systems/procedures	Transfer pricing taxation	5	33.3 %
Parts and materials procurement	Procurement costs	5	33.3 %
Insufficient infrastructure	General road conditions	5	33.3 %
Environmental regulations	REACH	5	33.3 %
Political, economic, and social conditions	Public safety and social conditions	5	33.3 %
Parts and materials procurement	Quality	4	26.7 %
Political, economic, and social conditions	Political conditions	4	26.7 %
Others	Extent of English language use	4	26.7 %
Investment legislation/procedures	Complicated administrative procedures and/or lack of transparency	3	20.0 %
Tax systems/procedures	Complicated administrative procedures and/or lack of transparency	3	20.0 %
Labor Issues	High labor costs	3	20.0 %
Labor Issues	Difficulty in securing engineers	3	20.0 %
Labor Issues	Union activities/strikes	3	20.0 %
Finance	Collection of receivables	3	20.0 %
Insufficient infrastructure	Highways	3	20.0 %
Insufficient infrastructure	Water	3	20.0 %
Environmental regulations	RoHS	3	20.0 %
Environmental regulations	ELV	3	20.0 %
Others	Inflow of counterfeit goods	3	20.0 %
Others	Living environment for foreigners	3	20.0 %
Others	Business practices	3	20.0 %
Trade legislation/procedures	Tariff classification	2	13.3 %
Trade legislation/procedures	Anti-dumping measures	2	13.3 %
Investment legislation/procedures	Lack of transparency in investment incentive schemes	2	13.3 %
Tax systems/procedures	High corporate tax rates	2	13.3 %
Labor Issues	Stringent dismissal laws	2	13.3 %
Finance	Depreciating local currency	2	13.3 %
Parts and materials procurement	Deliveries	2	13.3 %
Insufficient infrastructure	Railways	2	13.3 %
Environmental regulations	European regulation on new car CO2 emissions	2	13.3 %
Environmental regulations	Others	2	13.3 %
Political, economic, and social conditions	Concerns for measures against new strains of influenza	2	13.3 %
Others	Insufficient protection of intellectual property rights	2	13.3 %
Trade legislation/procedures	Rule-of-origin	1	6.7 %
Tax systems/procedures	Double taxation (in both Japan and the country where operations are located)	1	6.7 %
Standards, certifications and regulations	Others	1	6.7 %
Labor Issues	Heavy social security burdens	1	6.7 %
Labor Issues	Difficulty in securing factory workers	1	6.7 %
Labor Issues	Difficulty in securing managerial personnel	1	6.7 %
Labor Issues	Quality of workforce	1	6.7 %
Finance	Fluctuating interest rates	1	6.7 %
Insufficient infrastructure	Port facilities	1	6.7 %
Insufficient infrastructure	Gas	1	6.7 %
Environmental regulations	Euro5	1	6.7 %
Others	EU competition law	1	6.7 %
Trade legislation/procedures	High tariff rates	0	0.0 %
Trade legislation/procedures	Others	0	0.0 %
Investment legislation/procedures	Others	0	0.0 %
Tax systems/procedures	Non-uniform taxation among EU countries	0	0.0 %
Tax systems/procedures	Others	0	0.0 %
Standards, certifications and regulations	Different inspection standards for each country	0	0.0 %
Labor Issues	Double social security payments	0	0.0 %
Labor Issues	High personal income tax rates	0	0.0 %
Labor Issues	Difficulty in securing clerical workers	0	0.0 %
Labor Issues	Others	0	0.0 %
Finance	Appreciating local currency	0	0.0 %
Finance	Difficulty in obtaining credit	0	0.0 %
Finance	Others	0	0.0 %
Parts and materials procurement	Others	0	0.0 %
Insufficient infrastructure	Others	0	0.0 %
Environmental regulations	WEEE	0	0.0 %
Environmental regulations	EuP, ErP (Eco-design)	0	0.0 %
Others	Others	0	0.0 %

Source: JETRO Survey, Japan External Trade Organization

With regard to the foreign exchange situation, the Turkish lira temporarily depreciated significantly against the euro and U.S. dollar, affected by concerns about the currencies of emerging nations, after the financial crisis triggered by the economic turmoil in the U.S. toward the end of 2008. This seems to be the reason for the said concerns.

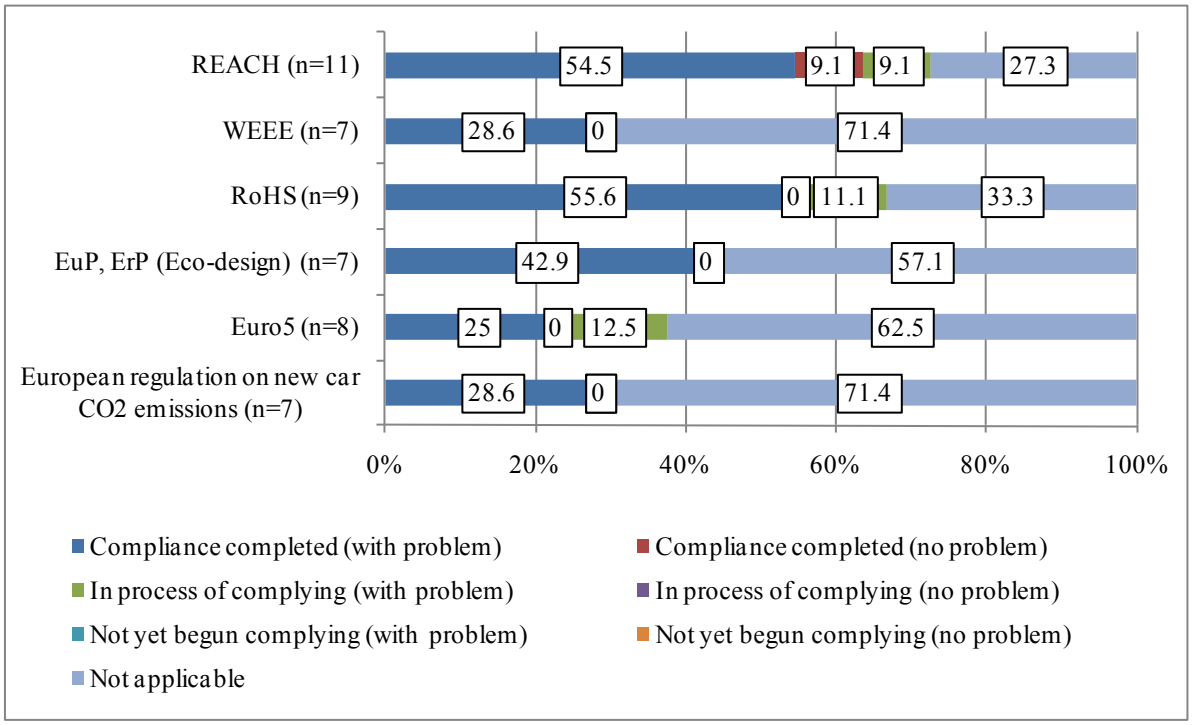
Other noteworthy answers were: “high costs of acquiring CE mark” (eight companies or 53.3%), the “shortage of domestic procurement sources”, “domestic economic conditions”, “insufficient infrastructure: power supply” (seven companies or 46.7%, respectively), “insufficient infrastructure: communications”, “trade legislation/procedures: complicated administrative procedures and/or lack of transparency” and “investment legislation/procedures: frequent legislation revisions, visa/work permits, lack of transparency in investment incentive schemes” (six companies or 40.0%, respectively). There were no changes in these top items from the previous survey.

V. Compliance with EU Environmental Regulations

- "RoHS" is the most frequently applicable EU environmental regulation to Japanese manufacturing affiliates in Turkey, and compliance with the regulation is making good progress.
- Six out of seven respondent companies answered that compliance has "impact on cost".

With regard to compliance status with EU environmental regulations by Japanese manufacturing affiliates in Turkey, seven companies are working on "REACH" (compliance completed by six companies and in progress for one company), six company is working on "RoHS" (compliance completed by five companies and in progress for one company), three companies completed compliance with "EuP/ErP "(Eco-design), and two companies completed compliance with "WEEE", "Euro5" and "European regulation on new car CO_2 emission", respectively. As can be seen in the data, the largest numbers of companies are making responses to "REACH "(see Diagram 9).

Diagram 9: Compliance Status with EU Environmental Regulations and Problems in Complying with Regulations (by Japanese Manufacturing Affiliates in Turkey)



Source: JETRO Survey, Japan External Trade Organization

As for the problems involved in compliance with EU environmental regulations, problems were clearly identified with "REACH", where the largest number of companies (seven, including one in process) is involved. Encountered problems in complying with EU environmental regulations were, "substances to be registered/notified are unclear" (three companies), "inadequate information sharing along supply-chain"

(one company) and “leakage of confidential information as a result of disclosure to third parties” (one company).

For the impact on product costs by compliance with EU environmental regulations, two companies referred to “increasing costs due to compliance” for “RoHS”, “EuP/ErP” (eco-design), and “Euro5”, respectively; there were many comments stating the impact of the compliance cost.

VI. Alignment with European Union Law (*acquis communautaire)*

- The existing laws/legal systems, as well as the standards/certifications procedures, may be revised to harmonize Turkey's domestic laws with those of European Union law.
- Only a quarter of the respondent companies are taking countermeasures against such revisions, with specific solutions.

The "screening" (an examination of how Turkey's domestic laws comply with European Union law, in preparation for the introduction and enforcement of European Union law) has been gradually implemented in the 35 areas of negotiation, as part of Turkey's EU accession negotiations and was finally completed on October 13, 2006. Formal negotiations in the area of "science and technology" were also completed in June 2006. Additionally, negotiations were initiated in the area of "business and industrial policies" in March 2007, in the areas of "financial controls" and "statistics" in June 2007, in the areas of "trans-European networks", as well as "consumer and health protection" in December 2007, and in the areas of "business law" and" intellectual property law "in June 2008.

Although the EU Foreign Affairs Council concluded to freeze eight chapters in the accession negotiation agenda while allowing negotiations in the remaining 26 chapters to be initiated but not completed (unless Turkey signs a customs agreement with Cyprus), at the meeting held at the end of 2006, the negotiations resumed in the areas mentioned above after the temporary interruption.

The Turkish government still maintains the policy of bringing the country's laws in line with European Union law (acquis communautaire), and it is possible that the existing laws/legal systems, as well as standards/certifications procedures, may be drastically revised. When asked about their responses to the process of the legislative compliance based on this situation, only four out of the 15 companies answered that "countermeasures are being taken" to deal with the situation, and the remaining 10 companies answered that "countermeasures are not being taken". The number of companies increased by one from the previous survey in both categories (the action of one company is unknown). Regarding the specific countermeasures (multiple answers allowed), four companies referred to "gathering information", one company referred to "re-examining production structures, including cutting back on costs" and one company referred to "others" (see Diagram 10).

The EU progress report issued in November 2008 commended the developments made on the part of Turkey in the aforementioned areas that were already in negotiation, but also commented that the country's compliance with the Copenhagen criteria (which ask for the protection of human rights and democratization) is limited, especially in the area of political reform (although it mentioned the legislation developed concerning freedom of expression). No major improvement has been seen as of August 2009.

Diagram 10: Countermeasures to the Process of Legislative Compliance

Countermeasures are being taken	Countermeasures are not being taken	Total number of companies responded
4	10	15
26.7	66.7	100.0

Upper row: Number of respondent companies
Lower row: Component ratio (%)

Source: JETRO Survey, Japan External Trade Organization

VII. FTA Impacts

- Japanese manufacturing affiliates in Turkey are most concerned and cautious about the EU-South Korea FTA, among the FTAs between EU and countries/regions outside the EU.
- **Companies are considering a transformation from being an EU-oriented production and export base for Europe, to focusing on the new market,** by effectively using FTAs between Turkey and neighboring countries.
- Many said that there was a "high cost advantage" to a Japan-Turkey FTA.

1. Japanese manufacturing affiliates in Turkey most concerned and cautious about conclusion and effectuation of an EU-South Korea FTA, among FTAs between EU and third-party countries.

In this survey, with regard to the FTA between the EU and the countries/regions outside the EU, questions were asked about the impact on the Japanese manufacturing affiliates in Turkey when they are agreed to and when they take effect.

The survey results shows that for the EU-South Korea FTA, six out of 14 respondent companies (42.9%) said that the FTA was expected to be a "substantial disadvantage" for them, while no company said it gave them any advantage (three companies said "no impact"). For the EU-ASEAN FTA, three companies said it would provide them with "substantial disadvantage", and four responded as "no impact", while for the EU-India FTA, two mentioned it would give them "substantial disadvantage", with four responding "no impact".

It was only the EU-South Korea FTA for which the percentage of companies that answered "substantial disadvantage" exceeded "substantial advantage" or "no impact". Japanese companies have been highly cautious about South Korean products that they consider are competing with their own, and the progress of the negotiations is to be carefully monitored regarding the FTA between South Korea and the EU, which is Japan's major sales market. As for specific comments, companies replies that an "increased import of competitive products" is expected by "enhanced competitiveness", which leads to the concern about "tougher competition" and "(resulting) decreased sales".

Incidentally, for the EU-Japan FTA, five companies (35.7%) replied that they would experience "substantial advantage", while one company each said "substantial disadvantage" and "no impact".

2. Companies are considering a transformation from being an EU-oriented production and export base for Europe, to focusing on the new market, by effectively using FTAs between Turkey and neighboring countries

At present, Turkey has agreed on and implemented free trade agreements (FTA) with Israel, Macedonia, Bosnia-Herzegovina, Croatia, Morocco, Tunisia, Syria, Egypt, Albania and Georgia. Preferential tariff treatment and other measures are being accorded by some of the countries with which Turkey has an FTA. When asked about the influence Turkey's FTA strategy may have on their business activities, responses were received from 15 Japanese manufacturing affiliates in Turkey (see Diagram 11).

While four companies stated, "we are currently utilizing the FTA framework in our business" and three companies replied, "we are currently considering utilizing the FTA framework in our business in the future", the remaining eight companies said, "we currently do not have any plans for utilizing the FTA framework".

When the four companies that stated, "we are currently utilizing the FTA framework in our business" were asked about their use in specific terms, three companies answered that they used it for the "expansion of export market". They named Morocco (four companies), Egypt (three companies), Israel (two companies), Macedonia and Syria as trade partners. The three companies that answered "we are currently considering utilizing the FTA framework in our business in the future" also intended to use the framework for the "expansion of export market" (two companies) and "parts procurement" (one company). "Israel", "Morocco" and "Egypt" were cited as their trade partners.

Compared with the previous survey (three companies were utilizing FTAs in their business, and one was considering using them), the utilization rate of FTAs is increasing. Additionally, Turkey is expanding their export markets in areas other than the EU.

Diagram 11: Influence of Turkey's FTA Strategy on Business Activities

We are currently utilizing the FTA framework in our business	We are currently considering utilizing the FTA framework in our business in the future	We currently do not have any plans for utilizing the FTA framework	Respondents
4	3	8	15
26.7	20.0	53.3	100.0

Upper row: Number of respondent companies
Lower row: Component ratio (%)

Source: JETRO Survey, Japan External Trade Organization

3. The Japan-Turkey FTA is considered to have a "substantial cost advantage"

Fifteen companies responded to questions concerning the business impact of the Japan-Turkey FTA, if it is negotiated, if agreement is reached, and if it takes effect.

The result shows a large number of the companies consider the Japan-Turkey FTA to be beneficial, with 10 companies replying "substantial advantage", one replying "substantial disadvantage" and four

answering “unsure”. For specific benefits, the companies said that “the option of procurement sources will be enhanced”, due to “materials procurement cost reduction with preferential tariff treatment”, and the “competitiveness of the products exported to Japan will be enhanced”—such companies are taking into consideration exporting from Turkey to Japan. On the other hand, the reason for disadvantages included the “significance of local production in Turkey partly disappears” (due to lower tariffs).

Ⅷ. Concerning the status of competition with Chinese and South Korean Products

- The products of the Japanese manufacturing affiliates in Turkey are exposed to tough competition from South Korean products.
- The solution for both "vs. South Korean" and "vs. Chinese" products is "differentiation through introduction of high valued-added products".

1. Impact stemming from the influx of Chinese and South Korean products in the Turkish market

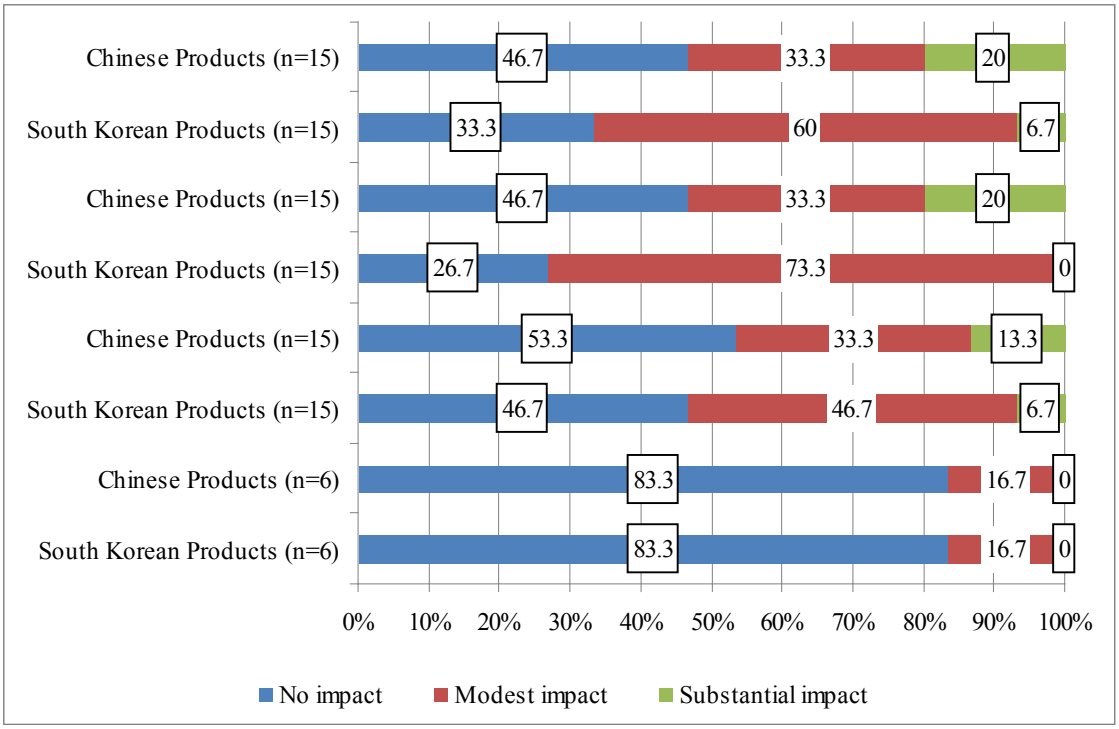
According to the State Institute of Statistics in Turkey, China ranks the third in by-country import values (15.6 billion dollars) in 2008, while South Korea ranked the 12th with 4.1 billion dollars (Japan was the 13th with 4.0 billion dollars). According to the export-side countries' survey for the first half of 2009, China has exported 3.6 billion dollars of products (down 34.0 % compared to the same period of the previous year), South Korea exported 1.2 billion dollars of products (down 40.1% year-on-year) and Japan exported 0.7 billion dollars (down 60.0% year-on-year), showing an across-the-board decline, due to the global economic crisis.

Drops in the exports of transportation machinery, such as automobiles, were large in particular, resulting in a small drop for "from China to Turkey" exports, as the percentage of transportation machinery against the total export portfolio was small.

With this background, the companies were asked about the impact from the influx of Chinese and South Korean products in the Turkish market (15 companies) (see Diagram 12). For the "fall in sales prices" caused by the influx of Chinese products, five companies selected "modest impact", and three said "substantial impact" (there were seven companies that said "no impact"). With regard to Korean products, the highest percentage of companies (nine companies) answered "modest impact".

For "declining sales due to increased competition", seven out of 15 respondent companies said "no impact" with regard to Chinese products, and 11 companies said "modest impact" with regard to Korean products, which illustrates the competition status with Japanese products. Incidentally, for the question of "procurement of inexpensive parts and materials made possible", which takes the Chinese and South Korean products positively, the total of "substantial impact" and "modest impact" were selected by seven companies for Chinese products and eight companies for South Korean products, which presented no major difference (15 companies).

Diagram 12: Impact from the Influx from Chinese and South Korean Products

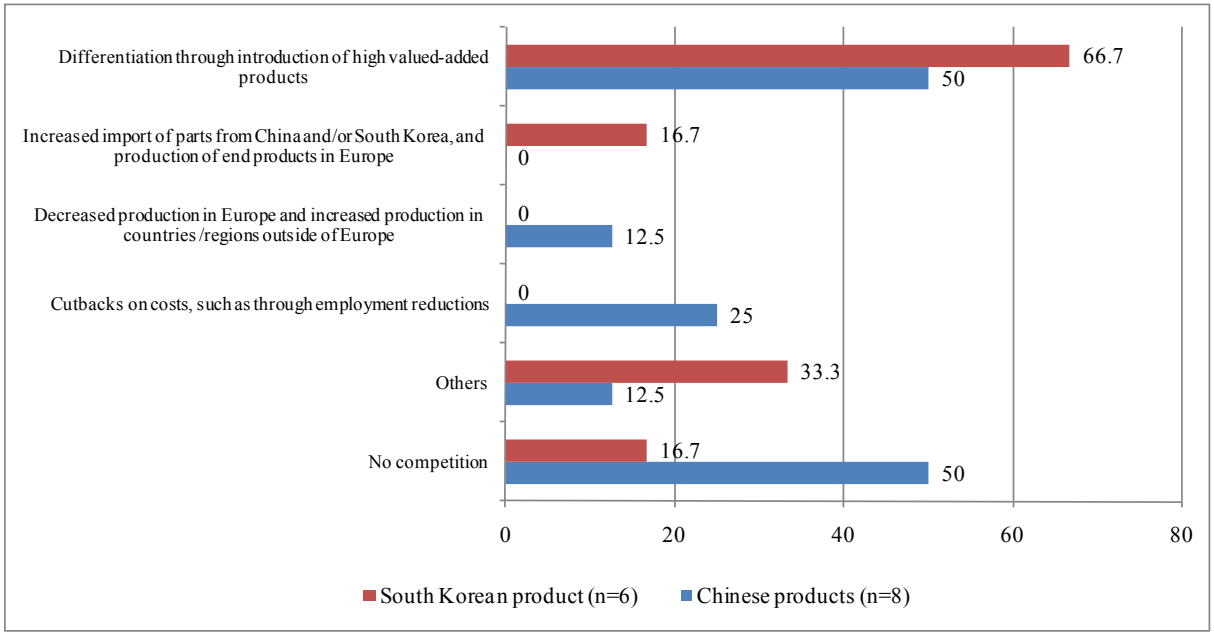


Source: JETRO Survey, Japan External Trade Organization

2. Responses to the influx of Chinese and South Korean products

For solutions to the influx of the products from these countries (multiple answers allowed), "differentiation through introduction of high valued-added products" received the biggest votes (four companies each) both for Chinese products (eight companies) and South Korean products (six companies). Additionally, four companies selected "no competition" with Chinese products, and one selected this choice for Korean products.

Diagram 13: Responses to the Influx of Chinese and South Korean Products



Source: JETRO Survey, Japan External Trade Organization