

# Foreign Affiliates

## Key Players in Revitalizing Local Economies

By Naoyuki Haraoka



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### Introduction

Under globalization, foreign direct investment (FDI) plays a pivotal role in the economic prosperity of a nation. In 2010, the percentage of FDI stock in Japan to total GDP was 3.9%, the lowest among the major economies. In Germany, it was 20.6% and in the United States it was 20.8% (Table). This means, however, that Japan has an enormous potential for increasing its economic growth by raising this percentage. In particular, its local economies, less populated and less industrialized, should see a larger impact from such internal FDI than urban areas.

A Ministry of Economy Trade and Industry (METI) statistical survey on foreign affiliates' business activities in 2014 showed an increasing trend in all business indicators among foreign affiliates in Japan, such as the number of permanent employees, sales amount, profits, and private investment, and the majority are planning to expand their business in the future.

According to the Japan External Trade Organization (JETRO), which is strongly promoting internal FDI, 1,365 foreign affiliates among 2,432 in total surveyed have their offices, production bases, distribution facilities or R&D bases only in Tokyo. Only 1,067 foreign affiliates have any of these facilities in areas other than Tokyo. Even among those, many have their facilities in urban areas like Osaka, Kanagawa and Aichi. So local economies will have much greater growth potential from an increase in internal FDI than urban economies.

TABLE

### Percentages of internal FDI stock to total GDP among major countries

	1990	1995	2000	2005	2010
Japan	0.3%	0.6%	1.1%	2.2%	3.9%
Germany	7.0%	6.6%	14.4%	17.2%	20.6%
South Korea	2.0%	1.8%	8.2%	12.4%	12.5%
UK	20.1%	17.3%	29.7%	36.9%	48.3%
France	7.9%	12.2%	29.4%	41.6%	39.4%
Euro zone excluding Germany	3.2%	3.0%	6.6%	7.9%	9.5%
US	9.3%	13.6%	28.0%	22.3%	20.8%
China	5.1%	13.3%	16.2%	11.9%	9.9%

Sources: Institute for International Trade and Investment (ITI); OECD.Stat

### Foreign Affiliates' Contributions

More specifically, besides boosting economic growth through production or sales, how can foreign affiliates contribute to the economy of the host country? Employment is the economic indicator that would best highlight the positive impact of internal FDI. In 2014, the number of permanent workers employed by foreign affiliates in Japan increased by 610,000, some 14.1% over the previous year, according to METI's survey. The survey also showed that foreign affiliates increasingly thought about expanding recruitment in the following year.

Exports would be another indicator of their contribution to the host country's economy. In 2013, foreign affiliates' exports from Japan totaled 5.25 trillion yen, an increase of 20.9% over the previous year. Their private investment, another key factor in economic performance, reached almost 1 trillion yen in 2014, having risen by 42.3% over the previous year.

This overview tells us that today foreign affiliates' activities in the Japanese economy are in good shape and could be a supplementary engine of growth in Japan.

It is also noteworthy that today many overseas companies are interested in starting business alliances with Japanese companies (Chart).

By sector, the wholesale business accounted for 40.7% of all foreign affiliates in Japan at the end of March 2014, followed by the services and information & telecommunication sectors.

Manufacturing accounted for only 17.6% of the total, and non-manufacturing 82.4%.

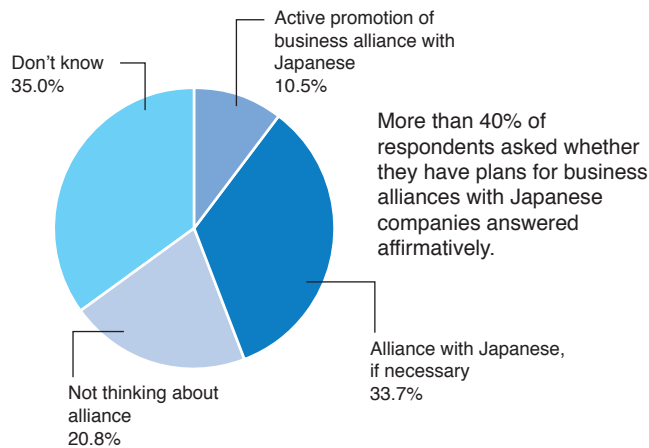
By region, European affiliates made up 44.4% of the total, American ones 26.8% and Asian ones 22.2%.

### Best Practices at Local Level

Although there are not so many foreign affiliates operating yet in local Japanese economies, there have been some notable success stories that demonstrate their contributions. The potential growth and prosperity of a local economy stimulated by an increase in internal FDI can be predicted by

CHART

## Plans for alliances with Japanese businesses in the future



Sources: METI, JETRO

considering the best practices of some of these foreign affiliates. JETRO has provided an overview of these.

First of all, there are some foreign affiliates significantly contributing to an increase in jobs in local economies and thereby to their revitalization. Notable among these are service businesses such as IKEA, a Swedish furniture retailing company that started operating in local areas in Japan in 2006, and LUSH, a British soap and cosmetics retailer that opened its first shop in Japan in 1999 and has since expanded nationwide. Manufacturing companies such as Bosch, a German auto components firm that established its first factory in Japan in 1912, and Valeo, a French auto parts company that entered in 2010, have contributed to the growth of business with their subcontractors in local economies, with spillover effects such as technology transfers and job creation. These companies now have offices, shops or factories all over Japan, not just in specific local areas.

Some foreign affiliates have established R&D bases in local Japanese regions. Cabot Microelectronics, an American company engaged in grinding-precision and polishing for semiconductors, located their R&D center in Mie Prefecture in the middle of Japan and started work there in 2013 on a new product to be exported to emerging Asian nations. It has been successful in promoting innovation and the internationalization of their partner companies, as well as creating jobs for highly-skilled professionals in the local economy.

Umicore, a Belgian non-ferrous metal producing company, set up a joint venture with Japanese chemical maker Nippon Shokubai and founded an R&D center in 2013 in Aichi Prefecture, also in the middle of Japan, to meet the various needs of its client companies, mostly Japanese automakers.

Development of renewable energy sources is another field that is vital for Japan to survive in the wake of the nuclear crisis in the

country. Ciel Terre Japan, a French company specializing in floating solar power generation, established a solar power station in Saitama Prefecture, close to Tokyo, in 2013 and is now promoting projects in other Japanese regions. Solar Power Network, a Canadian company specializing in generating solar power on roofs, has also started many projects all over the country. These companies contribute to loosening the energy supply constraints in Japan by providing local energy resources. Local companies are also the beneficiaries of these projects as they get part of the revenue from power generation in lieu of rent on the land they own that is used for such solar power generation. Of course, these projects also contribute to a reduction in CO2 and other environmental pollutants in local economies.

Tourism is another key industry that could possibly produce enormous benefits for local economies in the future in Japan. With the growth in the number of foreign tourists, sales and employment in local tourism, hotels and other services will increase and help to revitalize the regions. Asian airline companies are now attracting large numbers of tourists visiting the more local areas of Japan. Lion Travel, the largest travel agency in Taiwan, and other large Asian travel agencies are providing clients with a variety of tour plans for visiting local spots in Japan, and the high consumption of such wealthy Asian visitors is starting to have effects on some of the local economies. We can expect a further expansion in this field towards the Tokyo Olympics and Paralympics in 2020.

Lastly, it is noteworthy that there are some foreign affiliates exporting indigenous Japanese products from specific local areas and thus contributing to boosting exports of such products, in many cases agricultural products. This also contributes to attracting tourists or businessmen from around the world to these local Japanese places.

Taiwanese trading company Laimex, mainly dealing with agricultural products, has a subsidiary in Japan and in close collaboration with Japanese prefectural governments like Shimane and others in the northern Tohoku region they export Japanese rice, tea and other local produce overseas.

A Dutch buyer is exporting high-quality and expensive Japanese carp reared in local places such as Ojiya city in Niigata Prefecture to more than 10 countries around the world, while Hokkaido Bussan Trading, a subsidiary of Taiwanese trading company Jan Fruit set up in 2014, is trying to diversify its exports of agricultural products from Hokkaido to other Asian destinations as well as North America. People in the local governments and agricultural associations in Hokkaido are all hoping for an expansion in these exports.

Foreign affiliates could play a wide range of contributing roles in revitalizing local Japanese economies. We discussed these issues with the top management of one of these foreign affiliates in the interviews that follow this introductory article. **JS**

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