

Shibuya's Bit Valley is the Base of Japanese Net Businesses

By Arai Takuya

The Japanese economy is now on the threshold of a full-scale self-sustainable recovery.

The April 14 stock market crash in New York is spilling over to Tokyo and other parts of Asia as well as Europe.

Uncertainty still lingers over the New York stock market with some economists expressing optimism and others pessimism. The fate of the Japanese economy, meanwhile, depends on whether the prosperity of venture businesses buoyed by the information technology (IT) revolution can sustain itself.

With pump-priming directed toward public works reaching a financial and social limit, "structural reform" is becoming the catchword for the development of a new generation.

The need for the nurturing of new industries and creation of new businesses, along with the relaxation or abolition of regulations, were urged throughout the prolonged recession that followed the burst of the bubble economy. Although there is a good chance of success, it is not all plane sailing.

Looming large against this background is a concentration of Internet-related small venture businesses in Tokyo's Shibuya, the area that is being called "Bit Valley."

These firms emerged in the mid-1990s. People in high-tech industries began to call this cluster of venture businesses Bit Valley during 1999 because of its similarity to Silicon Valley on the U.S. West Coast around San Jose and Silicon Alley in New York.

Most companies based in Bit Valley are Web-page producers and designers, Net advertisement distributors and

content providers for cellular phones. They are all new businesses, which without doubt would never have come into being without the rapid spread of the Internet and cellular phones and the upgrading of related services.

Otemachi business districts which have a conservative atmosphere.

Shibuya Mark City, a building complex that opened in Shibuya on April 7, symbolizes Bit Valley. Behind a commercial tower housing restaurants and boutiques stands a business-orientated tower where some 20 Japanese and foreign IT-related companies are based.

One is Cyber Agent, a Net advertisement distribution company, which was successfully listed in March on Mothers, a new market for venture businesses at the Tokyo Stock Exchange.

The company's dashing president, 26-year-old Fujita Susumu, cited the advantage of name recognition as a representative player of Bit Valley as the reason for basing his company in Shibuya Mark City.

A survey by Yukawa Ko, a senior researcher with Fujitsu Research Institute, shows that 1,200 Internet-related companies are located in the 23 wards of Tokyo, with most of them concentrated in five wards, including Shibuya and Minato. Half of the companies have been established since 1994.

Two factors necessitate the concentration of Internet-related companies in specific districts: they must exchange information on financing and recruitment of personnel when launching businesses, and they must look for business partners.

Hori Kazutomo, the U.S.-born president of Cybird, a content provider for cellular phone-based Internet



Shibuya Mark City, where some 20 Japanese and foreign IT-related companies are based, symbolizes Bit Valley

Although Son Masayoshi's Softbank, the quintessential Japanese venture business, is not based there, Bit Valley is full of young entrepreneurs trying to emulate Son. It is more than a coincidence that young business talent has rallied around Shibuya, a district favored by young people, whereas traditional big businesses are concentrated in the Marunouchi and

services such as NTT DoCoMo's i-Mode, explained why he launched his company in Nishiazabu, Minato ward, where Net firms are concentrated, even though he was educated at Kwansai Gakuin University in Osaka and has a house in the Kansai area centered on Osaka. "You can hardly find any opportunities in the business world unless you place yourself in the mainstream. If I had remained in Kansai, I would never have gained any business opportunities," he said.

The concentration of Net-related companies is likewise common in other large cities, such as Sapporo, Osaka and Nagoya.

Social gatherings or study meetings organized by entrepreneurs can develop into forums where people can establish contacts with large companies ready to offer money or business opportunities.

Tateishi Tomonori, who is just out of college, is busying himself with launching "Mid Valley," an organization for the interchange between Internet businessmen in Nagoya. He decided to create his own business, instead of finding a position in a company, because his operation has begun to earn profits. He attributed his success to his contacts with business people through his activities as a middleman in the establishment of Mid Valley. "I have received orders through my Mid Valley activities. Contacts with large companies also increased thanks to Mid Valley," he said.

Yet the going is not so easy for these new, aspiring Japanese Net businesses, as they have begun to be exposed to the rigors of the business world.

When Internet Research Institute Inc., a company providing Internet-related technology services, and Liquid Audio Japan, Inc., a company selling digital music systems, were listed on Mothers on December 22, their opening prices were several times higher than the subscription prices. Other companies listed on Mothers early on fetched similarly high prices.

However, the opening prices of venture firms listed on Mothers in or after March, such as Cyber Agent, were all below the subscription prices.

Even Rakuten, the Setagaya ward-based operator of a full-scale virtual shopping mall and Net auctions, regarded as one of the most promising Net firms, saw its opening price quoted more than 10 million yen below the subscription price when the company was listed on the TSE over-the-counter market on March 19.



NTT DoCoMo's i-mode has proved to be a mega-hit, especially among young people

Proceeds from initial public offerings, supported by Net stock booms, represented venture businesses' largest source of funding. A collapse of this funding structure would inevitably stymie the expansion of these companies.

Senmoto Sachio, a university professor-turned venture businessman, points out that while Net companies are constantly being established in Japan, the number of companies having enough proprietary technological strength to ensure long-term growth or sustainable marketing know-how is far below that in the U.S.

"Investors apparently place excessive expectations on some Net companies. It's nothing but a bubble phenomenon. Japanese venture businesses will not be able to take initiatives in reforming the country's industrial structure unless they become venture businesses in the

real sense of the word," says Senmoto, an engineer formerly involved in the development of the Integrated Services Digital Network (ISDN) at Nippon Telegraph and Telephone Corporation (NTT). He later served as a graduate school professor at Keio University and as an outside executive of a Silicon Valley firm, and was instrumental in launching the new telecom group DDI Corp. in conjunction with Kyocera Corp. honorary chairman Inamori Kazuo. Senmoto has just launched his own telecom venture firm, e-Access Ltd., in Tokyo's Minato Ward.

Another problem Japanese venture firms must address is contact with the criminal underworld. At the request of the Metropolitan Police Department, the Tokyo Stock Exchange has asked newly listed companies to submit a document promising they will bar people associated with organized crime groups from becoming involved in their businesses.

The TSE's action reflected the fact that a number of the promising venture firms have already been penetrated by organized crime.

An official of an influential think tank familiar with the Net industry points out that among venture businesses' weak points is their lack of information on the underworld economy, compared with large companies which have accumulated data on organized crime through their efforts to deal with corporate racketeers.

Members of organized crime groups try every possible means to contact promising new companies. Their methods include offering money or introducing influential people. Naive venture business owners always face the risk of receiving "black money" due to their lack of information.

One venture business owner said there are two important ways to discern the real nature of people who offer money: whether they retain analysts or other specialists who can correctly assess the potential of business models, or whether they are ready to make middle- and long-term investments, instead of merely aiming to earn profits through initial public offerings.

One of the other and perhaps biggest challenge facing venture businesses is from major companies which, especially since the start of the year, are attempting to regain lost ground.

Convenience store chains, such as Seven Eleven Japan, have gone in with Mitsui & Co., Mitsubishi Corp. and other major trading houses to launch full-scale electronic trading operations by taking advantage of their nationwide outlet networks.

Separately, major trading houses, including Mitsui, Mitsubishi, Itochu Corp. and Marubeni Corp., have initiated activities for starting up electronic trading sites for steel products and chemical products, among others. Electronic trading between companies is said to have more growth potential than that between companies and consumers. It is also worth noting that the IT giant NEC Corp. did the spadework for the Japanese site of E-Bay, the largest online auction site in the U.S.

These moves by major Japanese companies in a way represented their attempt to beat the "time machine" business style of Softbank's Son Masayoshi, who has continually introduced business models which first took off in the U.S.

One of the big factors which enabled midsize or small venture companies to launch Net businesses to their advantage was their ability to promptly make decisions and take action in a top-down fashion.

Major companies still remain enmeshed by their conservative tendencies. Yet it is apparent that big companies outrank venture companies in overall potential, such as the ability to gather information, hire and develop personnel, raise money and launch new businesses.

As long as the market continues to expand, big companies and venture businesses can share the Internet pie. But when the Net sector enters a zero-sum game stage, the survivors will not necessarily be venture companies.

Venture companies also face the challenge of foreign patent rights, particularly those known as "business method patents."



Seven Eleven Japan, one of the country's major convenience store chains, is developing full-scale electronic trading operations nationwide

One day in April, a large number of Japanese Internet operators received an e-mail from an unknown American company to the effect that their services may be violating the patent rights it owns in the U.S. and Japan.

Most Japanese network providers are small, regional firms and find themselves in the dark about intellectual property and other legal matters. An Internet industrial organization held an urgent seminar, in which legal specialists updated Internet providers on Internet-related patent problems.

It turned out that the American company's patent claim was groundless and that it only invented a pretext for collecting patent fees wherever there was a chance to do so. Even so, Japanese network providers were terrified by the claim at least temporarily, and with good reason. In 1998, the major American bank State Street lost a law suite to an upstart financial venture firm over the patent of a fund management method known as "Have and Spoke."

Patents rights used to be granted to the invention of high technology. Now, as the U.S. court verdict indicated, U.S.

patent authorities are apparently ready to grant patent rights even to such a net service as the one which enables Internet users to order books just by hitting an icon on a homepage.

There is a sudden increase in cases of U.S. network operators, like cyber-book store chain Amazon Dotcom, applying for patent rights in Japan. Japanese Internet operators who have just taken off increasingly face the reality of being sued by American companies for violation of their patents rights.

Since Japanese patent authorities' stance on patent rights is still unclear, a Tokyo patent agent familiar with business patent rights suggests that there is no way for venture businesses to protect themselves other than applying for a patent as soon as they hit upon a new idea. **JTI**

Arai Takuya is an economic correspondent of Kyodo News. His beat has included the Bank of Japan, the Ministry of Finance and the information industry. He will take up a post in New York in August.