

Investing in JAPAN

FINANCIAL TIMES SPECIAL REPORT | Friday February 25 2011

Not lost in translation

Universities are trying to be more outward looking in a country where foreigners are a rare breed
Page 3



www.ft.com/invest-japan-2011 | twitter.com/ftreports

Need to tap fresh sources of dynamism

The country has an ageing population and its competitiveness is weakening, writes **Michiyo Nakamoto**

At HP's Ogikubo office, in western Tokyo, Naoyuki Shimizu points proudly to a row of PCs, labelled "Made in Tokyo". The sticker is a sign of the confidence the US computer group has in its locally made PCs and has been a useful tool to reassure users of the products' high quality.

"It has a certain impact" as a status symbol, explains Mr Shimizu, director of the company's supply chain operations.

Defying conventional logic that it does not pay to manufacture in Japan, HP makes almost all its desktop PCs and workstations sold in the country at its site in Akishima on the edge of Tokyo.

HP's ability to manufacture PCs profitably in Japan is a rare example of success at a time when foreign interest and investment in the country remain weak. With anaemic growth and a shrinking market because of its ageing population, the vitality of a country once described as an economic animal is on the wane.

Japan's share of global gross domestic product dropped from 14.3 per cent in 1990 to 8.9 per cent in 2008, according to the International Monetary Fund's World Economic Outlook database.

Between 2000 and 2008, Japan also tumbled from third place to 23rd in the IMF rankings of per capita GDP.

The country's international competitiveness has plunged from first place in 1990 to 27th last year, according to the IMD World Competitiveness Yearbook.

Japan's declining attractiveness as a place to invest is even driving its own companies overseas. In a survey conducted by the Ministry of Economy, Trade and Industry (Meti), more than half of respondents said they would shift some or all of their manufacturing facilities abroad.

Nissan, for example, shifted production of its March range of mid-sized vehicles to Thailand, while Sunstar, a healthcare products maker, moved its headquarters to Switzerland.

The situation has spurred the country into action. The Democratic party-led government is pursuing a campaign to attract more foreign investment as part of its growth strategy. Last year, it agreed to reduce the corporate tax rate for foreign companies for five years, if they set up a new regional HQ or research operations in Japan.

The strategy, combined with a general corporate tax cut, will bring the corporate rate for qualifying companies down to 28.5 per cent compared with about 40 per cent at present.

The government is also busy marketing the idea that, despite its own slow growth, Japan can be an attractive base for foreign companies' Asian operations, given its sophisticated infrastructure, cultural and gastronomic attractions and overall safety.

"Asia is becoming a pillar of the world economy [and] Japan should be a main player in that market," says



Get up and go: with anaemic growth and a shrinking market because of its ageing population, the vitality of a country once described as an economic animal is on the wane

Getty

Shozo Azuma, vice-minister for financial services.

Until recently, the government had been encouraging companies to invest on the basis that Japan was a big market. But it has become one-third, rather than half, of Asian GDP, says Tadayuki Nagashima, director-general of the Invest Japan department at

the Japan External Trade Organisation (Jetro).

While "it is no longer attractive enough to say Japan is a good place to invest on its own, Japan could be a base for Asian growth", says Mr Nagashima.

What is more, even though Japan has been overtaken by China as the world's second-largest economy, it still has many things in its favour, Mr Azuma says. Many Japanese companies are active all over the world and Japan has the second highest number of companies in Forbes Magazine's Global 2000 rankings, after the US, he says. "So, in the real economy, Japan is still very, very strong."

Japanese companies have expertise in advanced areas, such as digital, solar and other green and automotive technologies and the country ranks first for scientific research expenditure as a percentage of GDP and the number of researchers per 10,000 people, according to statistics from the Organisation for Economic Co-operation and Development.

"If the future is digital and if the future is ecological, Japan is starting from a tremendous position from which to grow," says Stephen Bird, chief executive officer of Citi Asia Pacific.

Many Asian companies, in particular, recognise that Japan has useful technologies for them and are seeking tie-ups or direct investments.

"Companies say that if it is about growth, they will go to China," says Masaru Nishiura, deputy director of trade and investment facilitation at Meti. But Japanese companies have expertise in advanced areas such as solar batteries, electric vehicles and low carbon products.

Japan is also a trendsetter in sectors, from fashion to digital products. "To sell to Asia, you have to be accepted in Japan first," Jetro's Mr Nagashima says.

"If you can be successful in this market, you can be successful anywhere in the world," says Darren Buckley, Citi's chief executive officer in Japan.

Citigroup discovered how useful the

Inside this issue

Dividend debate The concept of shareholder returns is finally gaining acceptance, writes Kenji Hall **Page 2**

Corporate funds Fund managers see an ageing population as providing good opportunities, writes Michiyo Nakamoto **Page 2**

Global education Students need access to a more international environment, says Lindsay Whipp **Page 3**

Medicine Government-dictated price cuts have made it difficult for drugmakers to recoup investments on innovative products **Page 3**

Resorts A grim environment for a country with a declining population holds attractions for foreigners **Page 4**

Haneda airport Jonathan Soble reports on a new lease of life for the Tokyo hub **Page 4**

Kyushu The southern island is attracting manufacturing and its population is growing **Page 4**



Michiyo Nakamoto



Jonathan Soble

The price that must be paid for revolving door leadership

Political risk

Mure Dickie looks at the long-term consequences of party infighting

It is a measure of the general dissatisfaction with the state of Japanese politics that one of the nation's biggest newspapers last month featured a front page column comparing recent Diet debate with flatulence.

As Diet members shouted at each other, parliamentary wisdom was "evaporating", complained the "Vox Populi, Vox Dei" column in the Asahi Shimbun, a left-of-centre broadsheet with a morning circulation of 8m.

The public would judge politicians by the quality of their debates, "not the loudness of their farts", the column warned.



Riven by division: protest against prime minister Naoto Kan

brutal 2008-2009 downturn. Gross government debt is soaring to more than 200 per cent of gross domestic product.

And China's usurpation of the long-treasured title of world's second-largest economy has highlighted the challenge posed by shifting patterns of global influence.

But rather than mapping out solutions, political discussion has been dominated in recent months by opposition groups' efforts to topple the Democratic party-

led government and by feuding within the DPJ itself.

It is a long way from the optimism with which the DPJ took power in September 2009, after a landslide victory that ended half a century of near-continuous rule by the centre-right Liberal Democratic party.

While the DPJ has made progress toward some of its goals - including the introduction of hefty child allowances intended to help shore up a perilously low

national birth rate - the party's novice ministers have often failed to present a coherent or unified face on issues ranging from tax to highway management.

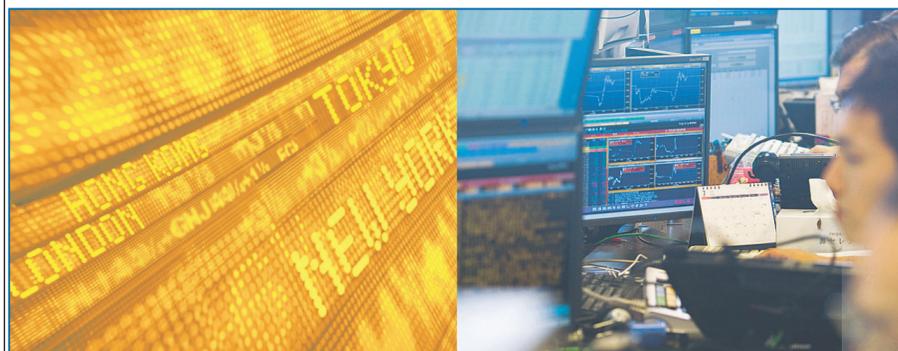
The departure of the party's disastrous first prime minister, the famously fickle Yukio Hatoyama, has done little to repair the DPJ fortunes.

The party is riven by divisions between supporters of Naoto Kan, who succeeded Mr Hatoyama, and Ichiro Ozawa, the scandal-plagued party powerbroker. Mr Hatoyama has himself reversed a pledge to retire from politics and is seeking to undermine Mr Kan at almost every turn.

Meanwhile, opposition groups, including the once-mighty LDP, which last summer won control of the Diet's less powerful upper house, are piling on the pressure by threatening to block passage of legislation needed to implement the budget for the year from April.

Japan's budget can be enacted only with approval

Continued on Page 2



Daiwa Capital Markets

Sales & Trading • Research • Capital Markets • M&A • IPOs

Centred on Asia. Serving the world.

At Daiwa Capital Markets, we are passionate about Asia, with an ambition to become the region's top investment bank. Our experienced professionals provide clients with insight and commitment across asset classes for all their Asian initiatives, backed by comprehensive investment banking services linking Asia and other major markets worldwide.

www.daiwacm.com



Passion for the Best

Daiwa Capital Markets is the global brand name of Daiwa Securities Capital Markets Co. Ltd. (Tokyo) and its subsidiaries worldwide that are authorised to do business within their respective jurisdictions. These include: Daiwa Capital Markets Hong Kong Ltd. (Hong Kong), regulated by the Hong Kong Securities and Futures Commission, Daiwa Capital Markets Europe Limited (London), regulated by the Financial Services Authority and a member of the London Stock Exchange, and Daiwa Capital Markets America Inc. (New York), a U.S. broker-dealer registered with the U.S. Securities and Exchange Commission, a futures commission merchant regulated by the U.S. Commodity Futures Trading Commission, and a primary dealer in U.S. government securities. Daiwa Capital Markets America Inc. is a member of the Securities Investor Protection Corporation (SIPC).

Investing in Japan

The concept of shareholder returns gains acceptance

Corporate profile
JSR CorpKenji Hall reports on
a change of attitude

A little over a decade ago, executives at JSR Corp were locked in an intense debate. The Tokyo-based materials maker had been receiving feedback from global investors who felt it could do more to boost shareholder returns.

However, JSR officials had reservations. "We worried that if we raised our dividends we wouldn't be able to lower them when earnings declined," says Tsugio Haruki, JSR's executive managing director and head of investor relations.

JSR no longer thinks that way. The company, which

makes synthetic rubber for tyres, films for flat-panel displays and semiconductor materials, and has about \$3.3bn in annual revenues, is now a favourite among analysts.

Goldman Sachs, JPMorgan and Macquarie Securities, recommend the stock, and many others applaud the company for regularly buying back its own shares and raising dividend payments.

Its transformation and other cases like it offer evidence that the concept of shareholder returns is finally gaining acceptance among Japanese companies.

"Companies that want to expand globally realise they must think about shareholder value," says Fumiya Takahashi, equity strategist at Barclays Capital Japan.

In recent weeks, a number of companies whose earnings are

rising have unexpectedly announced share buy-backs.

This month, Yamaha unveiled a plan to purchase up to 1m shares, for an estimated ¥1.2bn (\$14m). Nidec says it expects to spend ¥25bn for 3m of its own shares. Others, including Rohm, Unicharm and Daito Trust Construction, have made similar announcements.

Deutsche Securities predicts buy-backs will reach ¥4,000bn this year, from less than ¥1,000bn last year, and that dividends will top ¥6,000bn, up from ¥5,500bn last year. Those trends coincide with renewed interest in Japanese equities. Global investors now account for 65 per cent of the value of all trades on the Tokyo Stock Exchange's first section, according to Barclays Capital Japan's estimates.

In Canada, the US and Mexico, pensions funds that

used not to touch Japanese stocks are giving the market a serious look, analysts say.

On some measures, Japanese stocks look a bargain. More than a third of companies in the Tokyo Stock Price Index, or Topix, have a price-to-book ratio of less than 1.0.



JSR Corp, which makes synthetic rubber for tyres, is a favourite among analysts

Meanwhile, the average return on equity has rebounded to about 7 per cent from near zero just a year ago, according to Barclays Capital Japan. The Topix's average dividend yield of 1.86 per cent is now higher than the S&P 500's, which is 1.8 per cent.

Still, plenty of global investors remain wary of Japanese companies' reputation for hoarding cash, owning shares in groups they do business with and being stingy with dividends and buy-backs.

Steel Partners, a US private equity fund, spent six years lobbying the management of Sapporo Holdings and Bull-Dog Sauce for higher dividends and better governance before cashing out last December.

The UK-based hedge fund, Children's Investment Fund, also tried forceful tactics with J-Power, Japan's largest electricity wholesaler, but gave up and sold its stockholdings at a loss in 2008.

For JSR, the catalyst was a sixfold rise in net profit from 2000. The company soon

attracted global investors who raised their stake from 5 per cent in the late 1990s to more than 30 per cent.

In 2001, annual dividends were a miserly 6 yen per share, and share buy-backs were rare. JSR's priority was investing its cash in research and development.

But there was another reason for keeping dividends low. Like many Japanese companies, JSR wanted to avoid having to cut dividends if earnings soured. Doing so was considered a betrayal of shareholders' trust.

Talks with global investors persuaded company executives to change. JSR started increasing dividends in 2003 as earnings soared. It adopted informal targets, aiming to return up to half its net earnings per share to investors in the form of dividends and buy-backs.

"We became comfortable with rewarding shareholders in good times and asking for their tolerance in bad," says Mr Haruki.

In the fiscal year to March 2009, dividends were 32 yen a share, and the company bought ¥8.6bn of its shares. A critical test came last year when, after a dip in earnings caused by the financial crisis, the company lowered its dividend for the first time ever and froze share buy-backs. "We worried about a backlash, but there was none," says Mr Haruki.

This year, JSR expects net profits to rebound, nearly doubling to ¥26bn on a 9.6 per cent rise in sales to ¥340bn from the previous year. Anticipating stronger earnings, the company forecasts a rise in the dividend to 32 yen a share and has announced ¥1.3bn in share repurchases.

Contributors

Michiyo Nakamoto
Deputy Tokyo Bureau Chief

Mure Dickie
Tokyo Bureau Chief

Kenji Hall
FT Contributor

Jonathan Soble
Tokyo Correspondent

Lindsay Whipp
Tokyo Investment Reporter

Stephanie Gray
Commissioning Editor

Steven Bird
Designer

Andy Mears
Picture Editor

For advertising, contact:
Michiko Hayashi on:
tel: +813 3581 2097;
e-mail:
michiko.hayashi@ft.com
All FT Reports are
available on FT.com.
Go to:
www.ft.com/reports
Follow us on twitter at
www.twitter.com/ft.reports

Patient investors can
enjoy hidden jewels

Corporate funds

Despite the risky market, there are sectors worth considering, says Michiyo Nakamoto

When Steel Partners, the US activist fund, pulled out of Sapporo Holdings last year, it provided sceptics with further proof that activist investing is a risky business in Japan.

Steel Partners had been one of the most determined and vocal activist investors in the country, so its retreat after years of trying to per-

suaide the poorly performing beer group to increase shareholder value and improve returns sent a bleak message about the prospects for change.

Nevertheless, many funds emphasise that, with the right approach, Japan can provide stable and attractive returns. While the economy as a whole is not growing as fast as neighbouring China or India, there are sectors that are still expanding, they say.

TPG Newbridge, the US private equity fund, believes the increasing number of older people provides a significant opportunity.

"One area that we like a lot is the ageing population. They will be big spenders," says Jun Tsusaka, managing director of

TPG Newbridge in Tokyo.

TPG last year acquired Avon Japan, the cosmetics group, which has long catered to the 45-plus generation. ParkwayLife Reit, a Singapore-listed real estate fund, has invested in 29 nursing homes.

Generic medicine is another area where growth is expected, as the government steps up efforts to bring down medical costs.

"People think there is no growth in Japan, but in fact there are hidden jewels. What is important is to find a catalyst. As soon as there is a catalyst, there will be a unique alpha opportunity," says Yasunori Nakagami, president of Asuka Corporate Advisory.

Fund managers say the key is to look for companies

that have good business models but lack expertise or resources to expand their company or maximise its value.

The managing director of one fund says: "There is a huge portion of corporate Japan that isn't at the revitalisation stage, but needs third parties to help them reach the next level."

Many of these companies are in the small- to medium-sized sector, which are better targets than large companies, because there is more room for improvement, fund managers say.

"There are many companies that are not as efficient as they could be, so you can improve their efficiencies and help them go global," says Mr Tsusaka.

Many companies, including medium-sized ones, are facing a pressing need to globalise their operations. But, other than the large multinationals, few have experience of how to internationalise, analysts say.

While large companies can get advice from investment banks, and very small companies may be receiving funds and guidance from venture capital, advisory services for mid-cap companies are non-existent, says Mr Nakagami.

"I think there is real vision and logic to Japanese companies looking to partner with private equity funds to expand overseas, taking advantage of the well-developed global reach of the funds' existing portfolio companies," says Steven Thomas, head of Japan M&A at UBS in Tokyo.

Another factor that favours small- to medium-sized companies is that they "tend to be controlled by people who can make decisions," says Mr Tsusaka.

Large companies and their subsidiaries are usually bogged down by bureaucracy and a reluctance to change, analysts say.

On the other hand, "with family-owned companies in particular, as long as the top management makes a decision, they can move quickly", says Kazushige



Going grey: ParkwayLife Reit, a Singapore fund, has invested in 29 nursing homes

Kobayashi, managing director of Capital Dynamics, a fund-of-funds based in Switzerland. What is important, when working with smaller companies, is to have a strong relationship with the top management, he says.

"You're trying to be the counsellor, the guy who is there to help in a non-threatening way. Because every company has internal issues, an outside set of eyes and ears is useful," says one fund manager.

A common mistake of many activist hedge funds, is to try to enforce an Anglo-Saxon style of shareholder capitalism on Japanese management. It is also important for investors to work in a spirit of collaboration and to take a long-term view of that relationship, many fund managers point out. "What tends to put the spanner in the works is impatience," says

Mr Thomas. Japan has watched activist funds engage with companies for more than a decade, sometimes with horror, but in many cases with admiration.

When funds make mistakes, and antagonise management, the word gets around, raising nervousness about working with outside investors, fund managers say. But by the same token, good relationships bring dividends in the form of references that could provide investment opportunities.

What Japan needs are more success stories that demonstrate that funds can help Japanese companies thrive, fund managers say. Once that is demonstrated, "then the companies will open up", Mr Tsusaka says. "We need tangible evidence that it is a good thing [for Japan]."

"When funds make mistakes, and antagonise management, the word gets around"

Price to be paid for lack of leadership

Continued from Page 1

of the Diet's lower house, where the DPJ has a majority. But to issue the bonds needed to finance spending and to implement measures such as changes to the child allowances, the government needs either upper house approval or two-thirds majority support in the lower chamber.

Takao Tshikawa, a political analyst, says Mr Kan's increasing isolation is making it almost impossible for him to win the necessary co-operation from either the LDP, the smaller New Komeito party or the Social Democratic party, an estranged DPJ ally.

The result of this "severe confrontation", Mr Tshikawa says, is likely to be Mr Kan's resignation about the end of March.

Mr Kan and his senior party colleagues deny that there is any chance of him stepping down, but such speculation can only fur-

ther reduce his already dwindling stock of political capital.

A period of political turmoil need not be serious short-term problem for international investors. As Nomura analyst Kenichi Kawasaki notes, even failure to pass the budget-related legislation by the March end of this fiscal year would have only limited immediate impact.

"The instability of the political situation in Japan is nothing new," Mr Kawasaki wrote in a recent research report. "We think the markets have already priced in a certain amount of political noise and its impact."

Still, yet another spin of Japan's revolving door premiership – all four prime ministers before Mr Kan lasted a year or less in office – could have long-term implications.

At the least, it would delay progress on the issues Mr Kan has identified as his

top priorities: creating a cross-party consensus to address Japan's fiscal woes, laying out a plan to revive the agricultural sector and paving the way for entry to an emerging Asia-Pacific free trade zone.

While domestic investors remain happy to hold low-yielding government bonds, concern about longer term fiscal sustainability is growing.



Naoto Kan, the prime minister, is described as increasingly isolated

– as illustrated by Standard & Poor's January decision to cut Japan's sovereign debt rating for the first time since 2002.

Focusing their efforts on ousting Mr Kan could also prove costly for opposition groups, particularly the LDP. The party's refusal to accept the prime minister's

appeals for discussion on welfare and tax reform throw into question its own commitment to fiscal responsibility.

And while support for Mr Kan and the DPJ has slumped, voters are hardly enthusiastic about the alternatives. Just 21 per cent of respondents to an opinion poll by Kyodo news agency in mid-February supported the DPJ – but the LDP was backed by an only marginally more impressive 24 per cent.

The poll also found that 80 per cent of voters believed opposition parties should accept Mr Kan's invitation to cross-party talks on tax and welfare.

The prime minister's foes may yet decide that their interests lie in ignoring such popular desire for a more constructive approach to politics.

But if they do, they can expect to be the subject of plenty more malodorous metaphors in the future.

'TORAY'
Innovation by Chemistry

Innovation by Chemistry



Travel light with Toray carbon fiber.

Light, strong, corrosion-resistant Toray carbon fiber composite materials are expanding the horizons for next-generation wind power generators, automobiles, ships and aircraft like the Boeing 787 and Airbus A380. The world leader in carbon fiber composite materials, Toray continues to develop mold-breaking technologies to meet the global energy challenge and bring new value to life. **The right chemistry, the right answers.**

Campaign to open door to greater creativity

Global education

Lindsay Whipp on a programme aimed at internationalisation

Upon arrival at Osaka National University, the security guard calls to inform the vice-president's secretary of this reporter's arrival. "A foreigner has just arrived here," he says in a friendly voice.

Placing someone's foreignness first and foremost when identifying them is widespread in Japan, and the guard's choice of word was not meant offensively.

However, it is just one example of many demonstrating that, in spite of Japan being one of the largest trading nations in the world, foreigners are a still rare enough breed to generate this sort of description, even in universities such as Osaka, where there is a push to give an international education more prominence.

There is good reason for this internationalisation. Japanese companies, even the most domestic ones, are employing an increasingly international staff as a falling population at home means limited market opportu-

nities. Many professors also argue that a more diverse student base will lead to more creativity.

It should also help Japanese students gain access to a more international environment, one that many are missing out on, as the numbers studying abroad decline. "We want to become one of the leading institutions in the world and to be in this group we have to be internationalised," says Prof Kiichiro Tsuji, the bilingual vice-president of Osaka University, and a keen promoter of the institution's globalisation.

"As the Japanese market shrinks, we need global human resources," he says. "[Also] when our students come back from studying abroad they are different, their eyes sparkle and they're energetic."

Figures suggest that this transition towards more international campuses is slowly happening. The number of foreign students hit an all-time high of 141,774 last May, according to the Japan Students Services Organisation.

This means Japan is now a substantial net importer of students, as the numbers of those studying overseas slowed to 66,833 at the end of 2008, according to education ministry fig-

ures.

The ministry has established a programme aimed at doubling the number of foreign students to 300,000 by 2020. The government has picked 13 universities as the focus, providing funds to recruit professors who can offer courses in English, to set up international branches of the universities and to improve credit transfer programmes between them and overseas

"There are going to be more and more people from Asian countries who are going to want to study technology, economics and sociology in Japan"

institutions. They are also shifting focus to encourage Japanese students to take courses offered in English.

These universities differ from some of the smaller private ones that have struggled to maintain their student numbers as the university-age population starts to decline. Some of them have aggressive international recruitment drives that arguably do

not focus on the quality of students.

Peter Matanle, a lecturer at the University of Sheffield's School of East Asian Studies, says that, over the long term, Japan's top universities could reach a level of international recognition to rival European institutions, if not the top ones in the US.

"Japan's economic, social, cultural and political relationship is changing a lot with China and with other Asian countries as well," Mr Matanle says. "There are going to be more and more people from Asian countries who are going to want to study technology, economics and sociology in Japan."

Waseda University says its double degree programmes with other top Asian universities help attract top students. The main focus of Waseda's globalisation is its International School of Liberal Studies and its graduate school of Asia-Pacific studies.

It has a relatively long tradition of foreign participation, with about 25 per cent of students in its early history being Chinese. It also benefits from funding from prominent alumni, such as the founder of Samsung and other large Asian companies.



Going places: double degree programmes with other Asian universities help attract top students

Alamy

The push to internationalise Osaka, a prominent science, engineering and medical school, is much more recent. Its focus is on its "frontier" programme, one of a few it set up in 2008 for foreign students to spend up to a year researching

in the university's laboratories. Prof Tsuji says exchange programmes in the region that allow for students to spend a year at another European university – similar to Erasmus in Europe – would help encourage more student exchange, as well

as more transparency in education levels to facilitate broader credit transfer between universities.

Prof Tsuji sees the spread of foreign students to the traditional degree programmes as crucial to internationalisation.

Drugmakers find it hard to do business

Medicine patents

Kenji Hall explains why the system is likely to change

Among pharmaceutical industry insiders, it is known as the patent cliff.

Over the next two years, patents for many blockbuster brand-name drugs sold in Japan are set to expire. Astellas Pharma's patent on Lipitor, a cholesterol lowering drug licensed from Pfizer, runs out in 2011, while that of AstraZeneca's Arimidex, for breast cancer, is up the following year.

With patent protections gone, it is likely to throw the field wide open for companies that make generic, or copycat, drugs. Those companies could significantly build on their limited share of Japan's \$80bn pharmaceutical market, the world's second-largest, analysts say. "We expect the market to accelerate," says

'No doctor or pharmacist has ever recommended generics to me.. There's a lack of awareness about generics here'

Alan Thomas, of IMS Japan, a pharmaceutical market research company.

The biggest of Japan's generics makers could prosper. Morgan Stanley M&A predicts that net profits for Nichi-Iko Pharmaceutical, the largest generics producer, will nearly double between 2011 and 2015, while Osaka-based Towa Pharmaceutical's net profits will jump 47 per cent. Credit Suisse sees net profits for Osaka-based Sawai Pharmaceutical, the second-biggest generics maker, gaining 25 per cent in the next two years.

It is not just the domestic groups that are well positioned. Swiss company Novartis' generics unit Sandoz was among the early wave of entrants. So was Indian drug maker Lupin, which acquired a majority stake in Japanese generic drug maker Kyowa Pharmaceutical Industry in 2007.

Last year, Teva, the world's top generic drug maker, formally stepped in through a tie-up with Japan's Kowa, and aims for 10 per cent of the market by 2015. France's Sanofi-Aventis opted to partner Nichi-Iko last year.

Japan's Daichi Sankyo, Mitsubishi Tanabe Pharma and Fujifilm have also said they will enter the fray. Credit Suisse predicts groups such as these will have between 100 and 150 generic products by early 2013, allowing them to com-

pete with homegrown generic drug makers.

Japan has not been an easy place for drugmakers to do business. Every other year, the government dictates price cuts to keep its medical costs in check.

These cuts have made it harder for some drugmakers to recoup investments on innovative products. They have also worked against the spread of generics: brands win out over generics when there is little difference in price.

In June 2010, generic drugs were 22.4 per cent of the market by volume, according to the Japan Generic Medicines Association. The figure is low compared with the US, where generics account for more than 70 per cent by volume.

The health ministry has set a target of 30 per cent market share by volume in March 2013. Wider generics use could help lower overall spending on drugs, something the government is keen to do as the population ages, says Ludwig Kanzler, a partner at consultancy McKinsey in Tokyo.

The National Institute of Population and Social Security Research has forecast the number of people under 65 will nearly halve by 2055, leaving fewer workers to pay taxes.

Few think the ministry will reach its target. "We aren't optimistic," says Shuhei Hosokawa, of the Japan Society of Generic Medicines, an industry group.

Persuading doctors and patients could also take time. "I have never asked for a generic drug and no doctor or pharmacist has ever recommended generics to me," says Haruo Hatakeyama, a 55-year-old Tokyo resident. "There's a lack of awareness about generics here."

New rules were designed to bring change. Last April, the government opted to leave prices unchanged for some drugs still protected by patent, while cutting prices for generics.

At the same time, more hospitals are shifting towards a flat-fee system, known as Diagnosis Procedure Combination, or DPC. The transition attempts to do away with the system in which doctors and hospitals are reimbursed for every procedure they perform and drug they dispense.

To educate patients, the health ministry has printed posters and pamphlets, hosted public seminars, and posted videos online that explain the benefits of generics.

Japan's national health insurance agency has issued cards with "generic drugs, please" on them so patients can ask for generics without having to challenge the authority of doctors. "You will see higher penetration of generics as the government becomes more assertive," says McKinsey's Mr Kanzler.

INVEST JAPAN | Your Destination to New Growth

Experience the Rebirth of Japan



Japan is back. The past is giving way to a new era of innovation and global growth. Already, Japan holds the top position as a producer of green technologies, and boasts the world's most robust ICT infrastructure. To spur this transformation further onward, the Government of Japan is instituting a program of new incentives to attract investors and businesses from around the world. The Government of Japan is now providing generous subsidies for firms establishing regional headquarters or R&D centers here.

In addition, beginning before this summer, new initiatives will be introduced for certified international firms allowing them to receive a significantly lowered corporate tax rate and for their executives to be granted a personal tax deferral for stock options. These firms will also enjoy a reduction in fees for patent applications, and expedited visa processing for expat staff. And throughout Japan, a nationwide internationalization movement beginning this summer will create a working and living environment that welcomes people from all countries.

For more information, visit:



www.investjapan.org



Investing in Japan

Overseas groups take on a series of distressed projects

Resorts

Michiyo Nakamoto reports on a sector struggling in the face of weak corporate and consumer spending

On the outskirts of the southern city of Miyazaki, on a stretch of forest that is just a stone's throw from the beach, a large dome has stood unused for the past three years.

The Seagaia Ocean Dome, once the world's largest indoor water park, and sporting a man-made ocean and a beach, has become a symbol of the grim environment for resort developments in a country with a declining population.

Seagaia, which was acquired by Ripplewood, the US private

equity fund, in 2001, is now part of RHJ International, the holding company that was spun out of Ripplewood and listed in Belgium.

Although the resort, which has two golf courses, three hotels, a spa and bowling alley, among other amenities, made a pre-tax profit last year, RHJI is considering all options for exiting an investment that has been a long-term problem.

Last year, it offered to donate the Ocean Dome to the prefecture, but was rejected. "It costs money just to keep it open [and] it costs money to pull it down," says Sono Uchiyama, a project manager at RHJI.

Many resorts have suffered a similar, though less sudden, downturn, in the face of weak corporate and consumer spending and changes in the way people spend their free time. However, the plight of resorts such

as Seagaia has not dented interest in such developments among overseas investors.

In particular, foreign capital has descended on Hokkaido, in the north, which has become a popular destination for skiers and holidaymakers from the Asia-Pacific region.

YTL, a Malaysian group, last year acquired Niseko Village, a huge resort encompassing 462 hectares with two hotels, two championship golf courses, ski slopes, several hot springs (or *onsen*) and an equestrian centre.

"My family and I have been visiting Niseko over the years, and we have always enjoyed skiing [there]," says Francis Yeoh Sock Ping, managing director of YTL.

Nearby, Pacific Century Group of Hong Kong is developing the Hanazono resort. The rush of foreign investment in Hokkaido has triggered con-

cerns about foreign ownership of vast tracts of forests and woods.

But it is not just Niseko, with its famous powder snow, that is attracting interest from overseas. Asian investors have picked up a range of distressed



'In the spring you have two to three kilometres of cherry blossoms'

resorts, from golf courses, which are popular among Koreans, and hotels with views of Mr Fuji, which cater to Chinese and other Asian tourists who enjoy soaking in a hot spring and gazing at the famous mountain.

Many are relying on an increase in tourists from other parts of Asia, which the govern-

ment is keen to encourage. The Park Hotel Group, a Singapore-based hotel group, acquired a hotel in Otaru, a remote city in Hokkaido, popular for its quaint streets, canals and glass blowing industry and wants to buy further properties.

The tourism agency reported last month that, despite the strong yen, a record 8.6m foreigners visited Japan last year, a year-on-year increase of 27 per cent. The government hopes that Japanese hospitality will lure Asian tourists in particular, and is expecting a strong rise in visitors to 25m a year by 2020.

After Hotel Palm Spring in Fukushima was acquired by a Korean investor, the hot spring resort, which had not had Korean guests before, saw an increase in the number of Korean visitors, according to the Japan External Trade Organisation.

In a reflection of keen Korean interest in golf courses, Kitagoh, a smaller hotel and golf course complex near Seagaia, was also acquired from RHJI by a Korean investor.

By contrast, Payson Cha, chairman of Mingly Group, the Hong Kong-based financial advisory and investment group, hopes Chikuseno, a hot spring hotel in the Zao National Park, can remain "a Japanese hotel to be enjoyed by Japanese people. A Japanese *onsen* without any Japanese is not a Japanese *onsen*", he says.

Mr Cha had been visiting Chikuseno since 1992, ever since he was introduced to the northern prefecture of Miyagi by a business school classmate. He was so enamoured of the hotel, he has come back many times and tried to buy it.

"In the spring, you have two to three kilometres of cherry

blossoms. In the summer, you live in the middle of the forest, the streams flowing icy cold with trout, and in the autumn, the leaves change colour. Every season, this place transforms itself into a different environment," he says.

It was only when Chikuseno's parent company collapsed that Mr Cha could realise his ambition and buy the hotel.

Chikuseno was renovated at huge cost both so it could retain its Japanese charm and to "transform it into the first international hot spring and spa resort in the area", as Mingly notes on its website.

Still, even in the difficult economic environment, Mr Cha hopes to continue attracting Japanese clientele, who make up about 90 per cent of its guests. "It's like working towards the perfect cherry blossom," he says.

New terminal restores role as global gateway

Haneda airport

International travellers can now arrive closer to central Tokyo, says Jonathan Soble

When a new international terminal opened at Tokyo's Haneda airport in October, it represented a step forward for language as much as for air travel.

For three decades, Haneda – officially Tokyo International Airport – was one of the most misleadingly named places in Japan. Limited almost exclusively to domestic flights since the opening of rival Narita in 1978, it kept

its name but lost its role as a global gateway.

Now, it is beginning to take it back, to the benefit of business travellers in particular. The bright, efficient new terminal hosts a still modest 370 international flights a week, but Haruhiko Shimoda, president of Tokyo International Air Terminal Corporation, expects volume to double in a couple of years.

"We are convinced that the number of flights will increase in the near future," he says.

Since Haneda can be reached from central Tokyo in about half an hour – compared with 60-90 minutes for Narita – industry executives reckon it will be popular with busy professionals.

That will be especially true for those travelling to nearby destinations in Asia,

since shorter flights mean getting to and from airports accounts for a larger portion of overall travel time. Flying from Tokyo to Shanghai, for instance, involves less than three hours in the air, so an extra 30 to 60 minutes on the ground is significant.

"In theory, you can go to Hong Kong for the weekend without missing a beat of work," says an employee at an international bank in Tokyo who has used Haneda to fly to the Chinese territory, about five hours away, since the airport started limited charter flights several years ago.

A two-day weekend in Hong Kong requires stamina: a flight on All Nippon Airways leaves at 8:30pm and reaches Hong Kong just after midnight; the return flight leaves at 12:35am and arrives at 5:45am.



Happy landing: for three decades, the airport has been limited to domestic flights since the opening of Narita in 1978

Bloomberg

The less hardy may still appreciate Haneda for working trips. A sales manager in Shanghai can leave his or her home city just before 9am on China Eastern Airlines and land at Haneda at 12:30pm, leaving plenty of time for meetings before dinner.

Even long-haul carriers are being drawn to Haneda. British Airways, American Airlines and Delta began flying from the airport on February 20, with services to London, New York, Los Angeles and Detroit. "We believe it will be a popular choice with our premium customers," says Jamie Cassidy, Asia-Pacific general manager at BA.

Haneda's smaller international capacity means the carriers will still operate

most flights out of Narita. Mr Cassidy says the two airports will serve different kinds of customers, with Narita remaining a hub for connections to the rest of Asia – already a big part of its business – and Haneda taking an increasing share of dedicated traffic to and from Japan.

Narita's operators are reportedly considering lowering the airport's landing fees and adding new facilities for discount carriers, a breed of airline that has been largely absent from Japan until now, because of high operating costs and a lack of slots near Tokyo for new entrants.

Haneda's re-internationalisation remains a work in progress. Long-haul flights are limited to the small

hours between 11pm and 7am, meaning blurry-eyed arrivals and departures.

The problem is compounded by a lack of train services to the city centre between about midnight and 5am. Expensive taxis or patchy shuttle-bus services are the only options in the middle of the night.

Mr Shimoda acknowledges that "the biggest issue is whether we are doing enough for customers arriving late at night or early in the morning."

He says that he is negotiating with bus operators to increase services as Haneda adds more international flights.

The government hopes that increased access to Tokyo will lure more foreign tourists and business

people, especially as Asian neighbours become richer. The number of visitors to Japan rose 60 per cent to more than 8m between 2002 and 2008, in spite of the fact that many foreign carriers were shut out of Narita for lack of space.

According to a report by the Nippon Foundation, a think-tank, the combined demand at Narita and Haneda could grow from 100m passengers a year to 170m in 2030.

International traffic is projected to account for 110m of the total, three times the present level.

That means Haneda – with only 10 main gates in the new international terminal – is likely to come under pressure to expand again soon.

MIZUHO Channel to Discovery

Mizuho Corporate Bank supports industries involved in the development of advanced railway systems by offering specialized, sophisticated financial solutions.

Changing Lives. Unchanging Values.

Our lives are ever changing but at Mizuho Corporate Bank our mission remains unchanged: to support the growth of our customers while contributing to the prosperity of the global economy and the people of the world. A mission achieved through our expertise in developing innovative financial solutions.

This is our commitment. This is why you can continue to rely on us as "Your Global Financial Partner."

The Banker
Bank of the year 2010 in JAPAN
a member of the Mizuho Financial Group

Mizuho Corporate Bank
mizuhocbk.co.jp/english

Kyushu: car production starts to move in a southerly direction

On the first floor of a warehouse in Kitakyushu, a gritty industrial city on Japan's westerly Kyushu island, uniformed workers assemble steel pipes and gears into the skeletons of automobile seats.

The operation was set up in a rented space four years ago by Imasen, a mid-sized auto parts supplier based in Aichi prefecture. It is one of about 200 industrial ventures established in Kitakyushu between 2006 and 2010 by companies from outside the city.

"As Japanese regions go, Kyushu is doing well," says Tomoyuki Tani, the factory's boss. Production is back above pre-financial crisis levels, and Mr Tani hopes to stop renting soon and build a factory of his own.

Like many newcomers, Imasen was drawn to the area by the expansion of the automobile industry beyond labour-short Aichi, headquarters of Toyota, 700km away in central Honshu, Japan's main island.

Just as the southern US has pulled car factories away from Detroit, Japan's automakers have also moved south. Kyushu now accounts for about a sixth of production.

Fukuoka prefecture, the wider administrative area that is home to Kitakyushu and the glitzier Fukuoka city nearby, is one of the few places outside Tokyo where the population is growing.

Fukuoka attracts about 8,000 residents a year from Kyushu's six other, more rural prefectures, according to local data. After Imasen's seat-frames have been upholstered at another company down the road, they will be shipped to a nearby Nissan factory for installation in the automakers' Sentra compacts and other vehicles.

Next door to Imasen's operation is a Toyota plant that builds hybrid drive systems for the Prius and other petrol-electric cars. Toyota also operates a standard engine factory in the area and an assembly plant that manufactures high-end Lexus models.

Together with the Nissan assembly site and a Daihatsu minicar plant, the area in and around Kitakyushu is



Cars being assembled in Fukuoka

capable of churning out about 1.5m vehicles a year.

A big part of Kitakyushu's attraction is location. Coal deposits under nearby hills attracted miners in the 19th century, who were followed by steelmakers. The Yawata steelworks, today run by Nippon Steel, produced half Japan's steel until the second world war, using local coal and iron ore imported from China.

"We are geographically blessed," says Susumu Murata of Yaskawa Electric, a local company founded in 1915 by a Kyushu coal baron. Established to make conveyor belts and other machinery for the mines, Yaskawa expanded into electric motors, motor-controllers and eventually industrial robots, and today supplies welding and painting robots to carmakers.

Kitakyushu's car-based prosperity may not last. Between 70 and 80 per cent of the region's vehicle output is exported – a big problem when the yen is trading near a 15-year high against the US dollar. The domestic car market is shrinking and automakers are shifting more production overseas.

Nobuo Tomitaka, the official in charge of attracting businesses to the area, says the relative youth of Kyushu's automobile industry should

protect it from big cuts in the sector. "Carmakers' newest and most efficient factories are here. If they close plants, they will start with older ones elsewhere," he reasons.

Still, the city is aware of the dangers of complacency. It offers subsidies of up to 5 per cent of capital investment, aid that is roughly matched by Fukuoka prefecture.

The seaport has been refurbished, a new airport opened in 2007 and Kyushu University moved to a high-tech campus in 2009.

Mr Tomitaka says he wants to turn Kitakyushu into a freight and logistics hub. It is as close to Shanghai as it is to Tokyo. Companies such as Amazon, for example, could benefit by combining Japanese efficiency and stability with the dynamic growth of the rest of Asia, he says.

Authorities are also trying to encourage new manufacturing industries, particularly "green tech" ones such as alternative energy. Kyushu University's new campus is home to a big hydrogen fuel cell research centre and a corner of Kitakyushu's docklands has been transformed into an experimental coal gasification plant operated by J-Power, a utility, which is testing the effectiveness of carbon capture technologies to trap and store greenhouse gases.

Local companies also see opportunities. Yaskawa is developing electric motors for battery-powered vehicles and selling inverters to the industry to regulate the flow of electricity to machine motors and cut down on power consumption. It hopes to earn ¥1.5bn from sales of green technology by 2012, up from little more than zero now, Mr Murata says.

"The idea is to gather a certain amount of knowhow in Kitakyushu, then eventually sell [clean technology] overseas to places such as China," he says. "Manufacturing has always been the watchword for this area, and now we are trying to add environmentalism as well."

Jonathan Soble