The EU and Japan Accelerate Mutual FDI

Shinichi Ishii

Overview

Foreign Direct Investment (FDI) around the world has increased remarkably since the late 1990 s with both inward and outward investment dominated by the major industrialized countries. The yearly average from 1995 through 1999 was 54. 15 billion dollars- 19 times as much as in the 1970 s. JETRO—the Japan External Trade Organization—in its 2001 report says that in 1999, Britain ranked first in outward investment at 20. 21 billion dollars, followed by the United States, France, Germany, and the Netherlands. For inward investment, the U. S. has placed first for two straight years with 28. 25 billion dollars, followed by Britain, Sweden, Germany and France.

Cross-border mergers and acquisitions sparked by globalization and the intensification of IT are two main reasons why the industrialized countries are the major investors. There is a widespread understanding in the industrial community that, in this swiftly changing business climate, M&A enables cross-border firms to acquire production-line, technology and expertise, personnel, and marketing and distribution channels. This is regarded as an effective way to avoid running the risks of new investment and survive the fierce competition.

JETRO's 2001 report says that in 1999, reflecting the spread of cross-border M&A, the EU's overseas investment in the United States increased by 48. 5 percent to 22. 81 billion dollars compared to 1998, while its inward investment doubled to 23. 79 billion dollars, excluding Greece. As a result, the EU's investment in the U. S together with internal investment among members accounted for about a half of the world's total investment in 1999, showing how EU's very active EU investment has been across the globe.

Behind this EU trend, several factors can be identified. Firstly the launch of the single integrated market in 1993 touched off cut-throat competition among regional business firms, leading to mergers, takeovers, and alliances. Secondly, the free flow of capital, services, information and personnel in the course of globalization have naturally activated business consolidation outside the region too. Deregulation and privatization policies could be counted as the third reason. I also regard the introduction of the euro as another incentive for M&A as the euro has made it possible to issue EU-denominated bonds, thereby strengthening fund-raising abilities.

We can see typical examples in the electronics and telecommunications industry. British Vodafone Group PLC took over AirTouch Communications of the U. S. in June 1999. Germany's Mannesmann AG purchased British Orange PLC in 1999. This was followed by the purchase of Mannesmann AG by Vodafone AirTouch PLC. Change in cross-border consolidation among business enterprises is and will continue to be

very intense as the wave of industrial restructuring sweeps all regions of the world.

FDI in and out of Japan

Now we turn our gaze to investment in and out of Japan. According to the JETRO report, Japan's investment in the EU increased by 81. 9 percent from the previous year to 25. 19 billion dollars in 1999. This was the largest overseas investment quantity from Japan, marking a two-digit increase for the third year in a row. By country, Britain came first and the Netherlands placed second, with Japan's investment in these two countries accounting for about 90 percent of the total.

Regarding Britain, Japanese banks and security houses accelerated their capital investment in financial institutions to improve and support their own deteriorating financial situation caused by the rise in Japan premiums. Some increase in investment in the Netherlands stems from the growth of new holding companies aimed at making the most of the taxation benefits. Holding companies are exempt from taxation when receiving profits, for example, and this leads to intensive business activity through those companies.

Inward investment in Japan hit an all-time high of 21. 51 billion dollars, an increase of 105. 5 percent. Investment in manufacturing industry marked a sharprise of 257. 8 percent from 1998 to 8. 78 billion dollars in 1999. Investment in machinery formed an 88. 3 percent share in this, particularly contributing to the increase. Of the investment in machinery, three-quarters came from European industry, among which the French automaker Renault SA's capital injection to the debt-laden Nissan Motor Company was a leading example.

Investment in non-manufacturing industry, too, rose by 58. 5 percent to 12. 72 billion dollars in 1999, with the financial and insurance sectors expanding for three years in a row. In the financial sector, the investment environment is changing rapidly and capital-related reorganization has been very active.

On the country basis, countries from the EU have emerged as new and major partners. France ranked first, replacing the U. S. – the largest investor since 1991 – for the first time. The Netherlands followed next though some big deals, such as GM Canada, are included in the statistics for the Netherlands, the JETRO report says.

As a whole, inward investment from the EU increased five-fold, by 505. 8 percent to 12. 32 billion dollars. The EU's share in the total investment also climbed to 57. 3 percent from 19. 4 percent in 1998.

Renault's Capital Injection into Nissan

This growth of investment in Japan largely reflects large-scale M&A deals in the machinery, financial and insurance sectors. In the machinery sector, the most notable inroads are seen in automobiles, where Renault SA struck a broad alliance with Nissan Motor. By providing capital of 54. 11 billion dollars, Renault acquired a 36. 8 percent equity stake in Nissan Motor and also a 22. 5 percent equity stake in Nissan Diesel. In the financial and insurance industry, France's life insurance firm Axa purchased Nihon Dantai Life Insurance for 19. 54 billion dollars.

This large auto deal came when Nissan Motor, saddled with a huge sum of interest bearing liabilities, opted for financial restructuring through a business tie-up with a global automaker. Financial support from a single main bank has become ever harder to obtain due to the bank's

own need to write off the bad loans accumulated since the economic bubble burst. On the other hand, it was not unnatural for Renault to be looking for an influential partner to generate synergy gains through the pooling of the local production line, engineering and distribution channels.

Renault's then Executive-Vice President, Carlos Ghon, who took up the post of Chief Operation Officer, unveiled the revival plan in October 1999. This aimed to streamline management by slashing the purchasing costs by 20 percent over the next two years. Mr. Ghon sold the majority stakes in the keiretsu business group, such as those in parts and components subsidiaries, and this forced the keiretsu's parts and components subsidiaries to seek consolidation. In April 2000, a member of the Nissan parts and components group, Ichimitsu Kogyou, received capital from a French components supplier, Valeo, and others also sought alliances with foreign capital.

Foreign components suppliers' alliances with or purchases of Japanese counterparts are said to be intended to beef up their own business activities in Asia, with Japan at the core. At the same time, in a swiftly changing business climate, components makers and suppliers are under pressure to develop the parts and components which can keep up with the automakers' strategy in procurement and, the setting-up of global networks for parts and components supply.

It is, therefore, believed that many European components makers have a strategy of expanding sales in Asia, taking advantage of transactions with Japanese automakers. As Japanese components makers have established a foothold in Asia, the extensive use of Japanese production-lines, and distribution networks, together with the joint development of products and engineering, will help them to make inroads in Asian markets.

French Industry's Inroads in Japan

Here in brief, we review the history of French technology transfer to Japan. Japan's first silk mill was built in 1870 and first military plane in 1919 with the aid of French technology. France was the first foreign country to transfer technology to Japan after the San Francisco Peace Treaty was concluded in 1951. In 1953, the state-run Renault company gave permission to Hino Diesel to assemble 4 CV type Renault passenger cars.

France's investment in Japan grew remarkably in 1998, which also happened to be the cultural 'French Year in Japan'. Besides Renault's capital investment in Japan, the world's second largest retailer, Carrefour, announced the opening of large superstores in Japan in May 1999. A number of other French firms also announced their entry to Japan and opened branches or offices in this country one after another. This was followed by the opening of the first store on the busy Ginza shopping street in Tokyo by France's largest cosmetics firm, Sephora.

This trend continued into 2000. The world's second largest tire maker, Michelin, announced a tie-up with Toyo Rubber Industry. Europe's largest steel maker, Usinor, struck up an alliance with Nippon Steel Corp. in January 2001. French industrial branches or offices in Japan numbered 450 as of October 2000.

An official responsible for economic and commercial affairs at the French Embassy in Tokyo cited several attractions for French corporate investment in Japan, as follows : (1)-Fierce competition among business enterprises, resulting from the advance of globalization and information technology, facilitates entry into big markets like Japan. (2)-The decline of real estate

prices since the bursting of the bubble has made it easier for foreign investors to buy real estate. (3)–The advance into Japan was also prompted by deregulation and liberalization. (4) –The protracted economic slump has been driving Japanese firms to restructure and seek alliances with foreign firms, in order to survive the cut-throat competition. The official also cited the long-established traditional cultures of France and Japan as an impetus for French firms to take an interest in the Japanese market, even though the details of Oriental culture differ from the culture of the West.

It goes without saying, however, that there have been several obstacles on the Japanese side, including high commodity prices, the difficulty of finding business persons competent to conduct their duties in English, and the slowness of internationalization of the business environment.

The EBU Calls for Easier Access to the Japanese Market

A JETRO survey conducted in October 2000 reports that foreign investors have high regard for the improvements in the business environment in certain areas such as the decline in land prices, but notes that foreign investors still want further improvements. 71.4 percent of respondents requested the compulsory disclosure of corporate information in accordance with international accounting standards. 45.8 percent requested the introduction of a consolidated tax payment system as a necessary step for the globalization. About 70 percent of respondents also requested the launch of a system to provide the comprehensive information necessary to facilitate decisions on market entry. The single door inward investment organization of Britain is an example of what they want.

The European Business Community, comprised of foreign firms in Japan, issues an annual report as a paper for the EU-Japan Business Dialogue Roundtable–where issues arising between Japan and the EU are discussed. In its 2000 report on 'Issues for the New Millennium', the European Business Community applauded the Japanese government's embarkation on an ambitious program to lower regulatory barriers, improve market access, strengthen competition and promote inward investment. It said that as a result, barriers to trade and investment are slowly falling, and opportunities increasing for European companies in Japan.

The report further said, however, that filing and licensing requirements in such diverse sectors as health sciences, cosmetics, telecom, civil aviation, and shipping not only present a major barrier to product innovation and service delivery, but also often fail in their original purpose of protecting consumers and society.

The report went on to say that the government's apparent commitment to bringing the Japanese tax regime in line with international practice was encouraging and welcome reductions in the overall effective corporate tax rate and the planned introduction of a system for taxing groups of companies.

Regarding the quest for easier access to the Japanese market, however, recommended that an appropriate land transaction disclosure mechanism should be introduced to make it easier for companies to acquire information and make informed decisions on real estate transactions. The EBC urged the Japanese government to bring financial disclosure and accounting standards in line with international practice by requiring adequate disclosure of current assets and liabilities at market-based prices. It stressed that access to accurate financial information remained critical to firms wanting to pursue M&A.

Case Study I –Toyota's Plant in France Activates the Economy

As an example of the striking increase in automotive investment abroad in 1999, Toyota began building an auto-manufacturing plant and recruiting engineers, managers and maintenance teams in Valenciennes, northern France (near Brussels). Toyota Tsusho also opened a distribution base for auto parts and components there. I believe the French government's own call for Toyota to invest had some influence on Toyota's decision to locate its second plant in Europe.

Here, I shall look at how the location of this large-scale 4 billion franc (80 billion yen) auto assembly plant has been activating the local economy, including with regard to job creation.

Toyota's new European plant began production of the one-litre Yaris in January 2001. It employs 1,600 local people as of January 2001 and this number will increase to 2,100 when the production capacity reaches 150,000 units in mid-2002.

Of 1,600 line-operators, 43.5 percent were job seekers, students or former national service personnel, 29 percent temporary, short-term contract workers and 27.5 percent part-and full-time salaried workers. 80 percent of the total came from Nord prefecture, where Valencienne is located, 13 percent from Pas-de-Calais region, and the remaining 7 percent from other areas.

Toyota says that since its launch of the Toyota Valencienne-Onnaing project at the end of 1997, the project has generated business opportunities for numerous firms in the region. More than 300 companies in the region have benefited. 283 companies were involved in building the factory and installing the manufacturing equipment. 223 of these were French. 511 companies have provided Toyota Motor Manufacturing France with goods and services. 120 European car parts suppliers, of which 37 percent are French, have provided parts and components.

Environmental conservation is another feature of the Toyota plant in France. 26 hectares of the total 200 hectare site is planted with over 22,000 plants of different species as a Regional Nature Park. Flower meadows cover 80 hectares and there is also a 51 hectare mowed meadow.

Buildings are constructed in a discreet, low-rise manner. The best suited materials have been selected to minimize waste at source, as an environmentally-friendly waste disposal management measure. Waste is separated in order to achieve the maximum re-use of plastic parts and packaging and recycling of paper, wood and metal.

Parts imported from Japan are transported by waterways from Dunkirk to a nearby location. The Yaris cars produced there are exported by railway. Toyota says this eco-friendly production system is consistent with the Toyota production corporate principle of throughly eliminating waste on production sites.

The First Plant in Europe Built in England

Toyota plant in Valencienne was its second vehicle production unit in Europe. The first production plant was built in Burnaston, Derbyshire, England in 1989. Toyota's inroads into Britain were prompted by British enthusiasm to invite foreign capital to revitalize regional economies. The British government had long been promoting deregulation and liberalization, and Thatcherism intensified the effort to attract foreign firms by enhancing the incentives to invest, including through reductions in corporate tax and the provision of a highly skilled work-force.

Britain had experienced serious unemployment when the key industries of coal and shipbuilding declined, and tried hard to invite inward investment in order to create jobs. Seeking to attract foreign capital, it established a single door inward investment organization which funnels the necessary information and facilitates decision-making on whether to enter the market. In Britain, where authority is decentralized, Scotland, Wales and Northern Ireland each has its own single door office to invite foreign capital in cooperation with the central government.

I would like to relate the example of a visit I made in 1998 to the industrial zone of Silicon Glen in Scotland-a 160 kilometer electronics and biotechnology corridor extending from Glasgow to Edinburgh. Looking around at the concentration of the semiconductor industry, I could find affordable land, water, utilities, and a skilled labor force all at a relatively low cost, and a low corporate tax rate. They are good incentives for attracting foreign capital. JETRO says, however, the strong pound and week euro have adversely affected corporate profits, forcing some businesses to shift some manufacturing units to Central and Eastern Europe or even leave Britain entirely. It is likely that the British domination of FDI will be undermined by that fact of remaining outside the euro zone. The issue of whether Britain joins the euro or not may have a substantial effect on inward investment in Britain in the future.

Case Study Ⅱ –Sony Europe

Here I would also like to introduce how one of Japan's global companies has developed its business strategy in the cross-border market. Sony Europe GmbH, which holds 15 manufacturing and engineering units on the Eurasian continent, moved its headquarters from Cologne to Berlin in October 1999. In the Federal Republic of Germany, states have decisive authority in areas other than diplomacy, defense and other federal matters. The state of Nordrhein-Westfalen in the midwest with Dusseldorf as its capital, has about 550 Japanese business branches, offices and factories. In this state, the banks file for investment on behalf of foreign companies and this is widely known as a measure that promotes inward investment.

Sony Europe's head office is said to have selected Berlin as the site for its headquarters in Europe for the following three reasons. (1)–Germany is the largest sales market for Sony in Europe. (2)–Berlin's social and information infrastructure is sufficient to support a headquarters at a time when Germany's political and economic role is growing, especially in view of the EU's enlargement towards Central and Eastern European countries. (3)–Berlin is centrally situated between Western Europe, with its population of 380 million people, and Central and Eastern Europe and Central Asia, with their population of about 400 million people. This location is considered favorable for promoting Sony's growth and strategic competitiveness.

In terms of corporate advantages from the standpoint of business activities in Europe, Sony Europe GmbH is the center of an organically combined network of functions, such as engineering, manufacturing, marketing and distribution and other services dispersed in various regions. Sony says that instead of excessive concentration of business activities in certain areas, dispersion of those activities is necessary to meet the challenges of cross-border transactions. The marketing functions of electronics products for daily use are set up near to the Netherlands' Schiphol airport–a hub airport of Europe. London is chosen as the center of fi-

nancial services and entertainment goods, such as PlayStation and AIBO. The possible future shift of manufacturing units to Central and Eastern Europe and also the potential growth of these former communist states may be counted as another business advantages of Berlin.

Sony believes that the countries of the former East Europe will develop into attractive markets with promising economic growth. It also evaluates this region highly as a treasury of highly educated manpower resources. Thus, Sony Europe has the intention to break new business ground there with respect to its global market. I also would like to draw attention to the fact that programs for training local business managers, and the transfer of management authority to local staff, are said to have been adopted at a meeting of Sony's European managers in June 2001 in line with the global localization policy.

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