Grant Thornton

Japan

International Business Report 2008 – Country focus

The Grant Thornton IBR 2008 reveals that privately held businesses (PHBs) in most economies remain optimistic about economic prospects for the year ahead. For the fifth consecutive year, India tops the league table as the most optimistic economy with an optimism/pessimism balance[1] of +95 per cent with the Philippines joining them at the top for the first time (also +95 per cent). Japan is still at the bottom this year with a balance of -49 per cent.

Optimism amongst businesses in East Asia[2] is in line with the global average, although overall optimism has fallen from 2007. This year +39 per cent of all East Asian businesses are positive about their economy compared to a balance of +54 per cent in 2007. East Asia continues to present a very mixed picture however, with optimism/ pessimism balances ranging from +95 per cent in the Philippines to -49 per cent in Japan.

The Japanese economy

The Japanese economy bounced back strongly in the second half of 2007, expanding by 0.9 per cent in the fourth quarter after a more modest growth of 0.3 per cent in the third. Exports are still the main driver of growth. But the household sector has lost momentum, with spending growing by just 0.1 per cent and 0.2 per cent in the third and fourth quarters respectively. Residential investment remained a strong drag on growth, owing to regulatory changes that have seen the housing market plummet. Business investment bounced back after contracting in the second quarter, but growth in year-on-year terms has decelerated significantly.

Even with the respectable performance in the second half of 2007, sentiment indicators are deteriorating sharply. Consumer outlook is gloomy, and business sentiment is tanking, despite some signs that conditions are at least stabilising after hitting a ten-year low in September. The Bank of Japan's quarterly Tankan survey showed a sharp fall in sentiment, although large and medium-sized enterprises' assessments of business conditions still remain on average 'favourable'. This may reflect assumptions that are too optimistic, especially regarding the yen and future profit growth.

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1 the balance is the proportion of businesses reporting they are optimistic less those reporting they are pessimistic.
2 for the purposes of IBR, the term 'East Asia' refers to those East Asian economies covered by our survey – mainland China, Hong Kong, Japan, Malaysia, the Philippines, Singapore, Taiwan, Thailand and Vietnam.

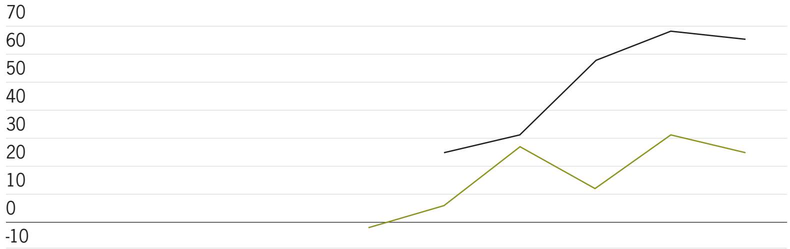
Business expectations/revenue

- PHBs in Japan are less optimistic about their revenue prospects in 2008 (+24 per cent) than they were in 2007 (+31 per cent).
- Their level of optimism regarding revenue performance is well below both the East Asia (+65 per cent) and global (+63 per cent) averages.
- Their level of optimism regarding exports is just +5 per cent. This actually represents a +1 per cent increase from 2007 but is marginally below the East Asian average of +6 per cent.

Employment

- Expected employment growth in Japan has risen from +18 per cent in 2007 to +24 per cent in 2008.
- Conversely a balance of +20 per cent of PHBs in East Asia as a whole expect employment to grow, compared with +44 per cent in 2007.
- Actual reported employment growth in Japan (+29 per cent) was higher than expected in 2007.

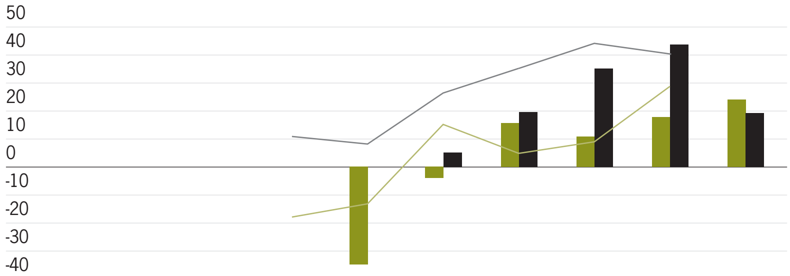
Figure 1: Revenue expectations for Japan and the East Asian average 2003-2008
Percentage balance of businesses indicating optimism against those indicating pessimism



	2003*	2004	2005	2006	2007	2008
Japan	-2	6	27	12	31	24
East Asia	–	24	31	58	68	65

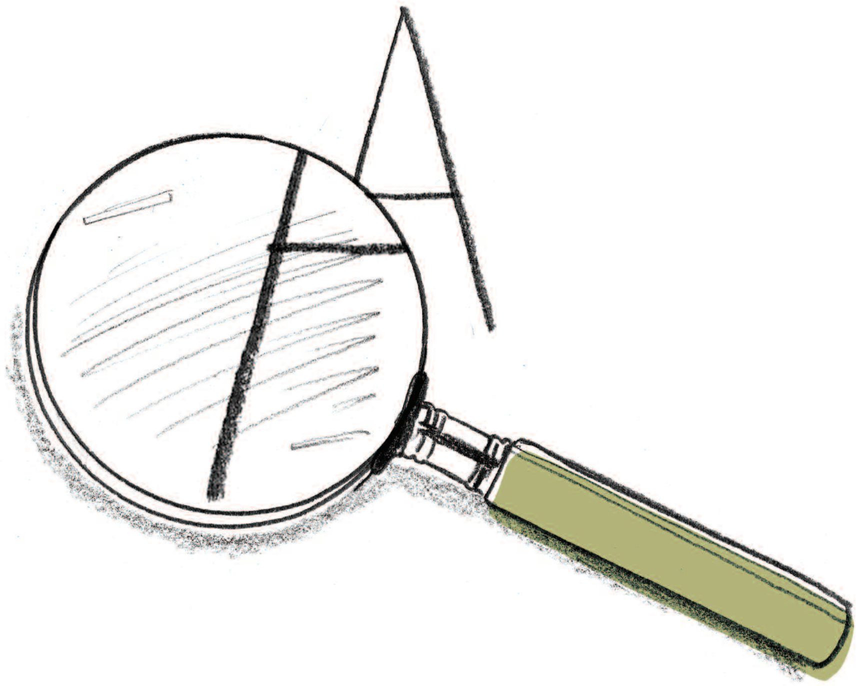
*data not available for East Asia
Source: Grant Thornton IBR 2008

Figure 2: Employment history of Japan and the East Asian average 2002-2008
Percentage balance of businesses indicating optimism against those indicating pessimism



	2002*	2003*	2004	2005	2006	2007	2008**
Expected Japan	–	-36	-4	16	11	18	24
Expected East Asia	–	–	5	20	35	44	20
Actual Japan	-18	-13	15	5	9	29	–
Actual East Asia	11	8	26	35	44	40	–

*data not available
**2008 data will be documented in IBR 2009
Source: Grant Thornton IBR 2008



Constraints

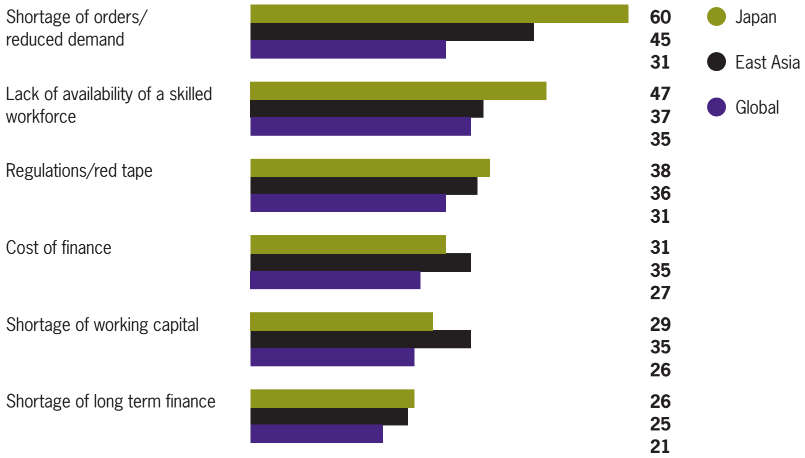
- Shortage of orders/reduced demand is the constraint restricting expansion cited most by businesses in Japan (60 per cent).
- The availability of a skilled workforce is cited by almost half of PHBs in Japan, compared to around one third of businesses globally.
- PHBs in Japan rate every constraint higher than the global business average.

Emerging markets

- The most important factor for PHBs in Japan when determining whether to invest internationally, as is true of businesses globally, is market size and growth potential (48 per cent).
- The number of Japanese businesses which export (15 per cent) is up from seven per cent in 2007, but is still well below the East Asia average (39 per cent).
- 23 per cent of PHBs in Japan import, which is below the global average of 39 per cent.
- PHBs in Japan see their main sources of competition coming from very similar areas to businesses globally.

Figure 3: Largest constraints on growth for Japanese businesses compared to the East Asian and the global average

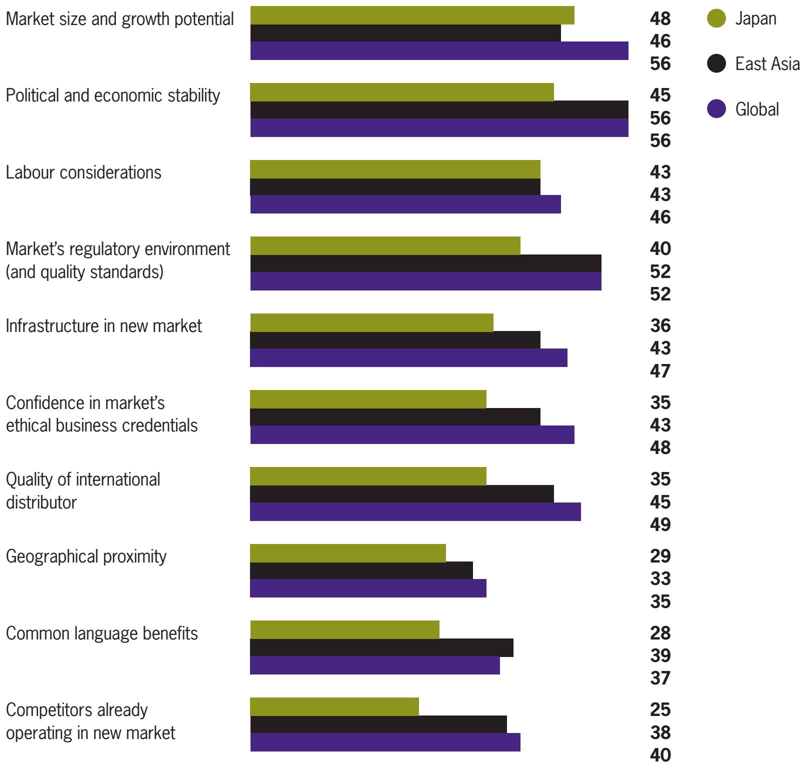
Percentage of businesses rating constraint 4 or 5 on a scale of 1 to 5 where 1 is not a constraint and 5 is a major constraint



Source: Grant Thornton IBR 2008

Figure 4: Importance of factors determining foreign investment

Percentage of businesses rating level 4 or 5 on a scale of 1 to 5 where 1 is a low priority and 5 is a high priority



Source: Grant Thornton IBR 2008

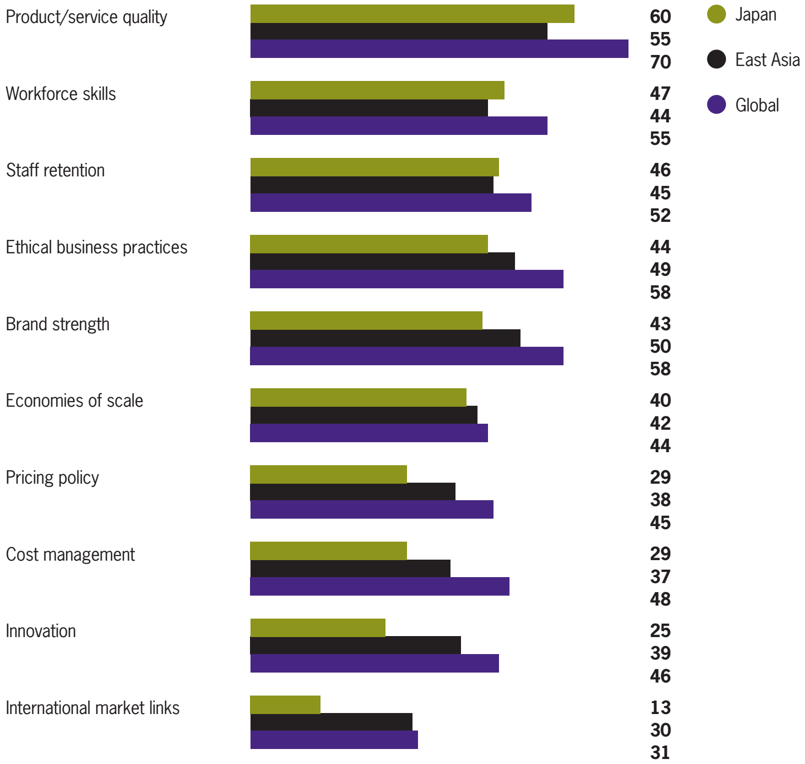
Competitiveness

- Similarly to businesses globally, PHBs in Japan see their greatest source of competitive advantage as product/service quality (60 per cent).
- 47 per cent of PHBs in Japan see workforce skills as a source of competitive advantage, compared to 55 per cent of all businesses.
- Just 13 per cent of PHBs in Japan cite international market links, compared with almost one third of businesses in East Asia and globally.

Corporate social responsibility (CSR)

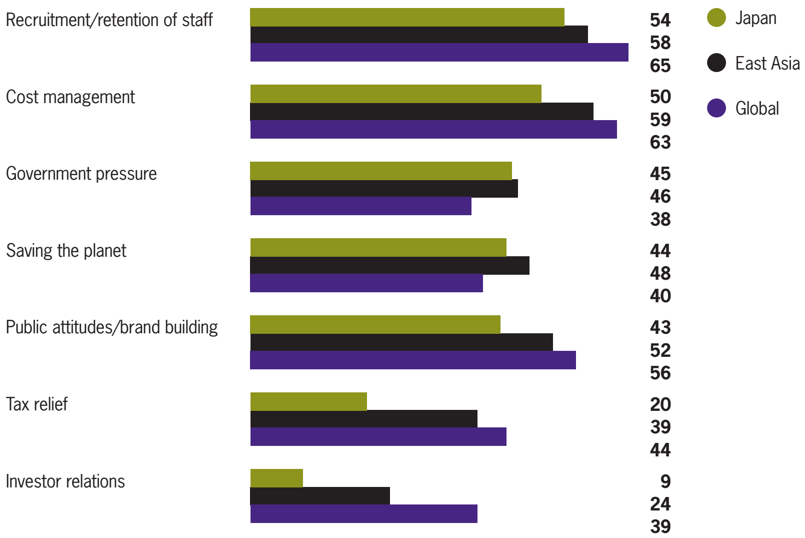
- Recruitment/retention of staff is viewed as the biggest driver towards more ethical practices by PHBs in Japan (54 per cent) and by businesses globally (65 per cent).
- 53 per cent of PHBs in Japan actively promoted workforce health and well being in the past year, compared to 65 per cent of all businesses in East Asia.
- 40 per cent of Japanese businesses have incorporated their policies in to a written CSR document. This is below the East Asia average of 61 per cent.

Figure 5: Main sources of competitive advantage for Japanese businesses compared to the East Asian and the global average
Percentage of businesses rating strength of the advantage 4 or 5 on a scale of 1 to 5 where 1 is not very strong and 5 is very strong



Source: Grant Thornton IBR 2008

Figure 6: Importance of drivers to more ethical practices for Japanese businesses compared to the East Asian and the global average
Percentage of businesses rating the importance 4 or 5 on a scale of 1 to 5 where 1 is not very important and 5 is very important



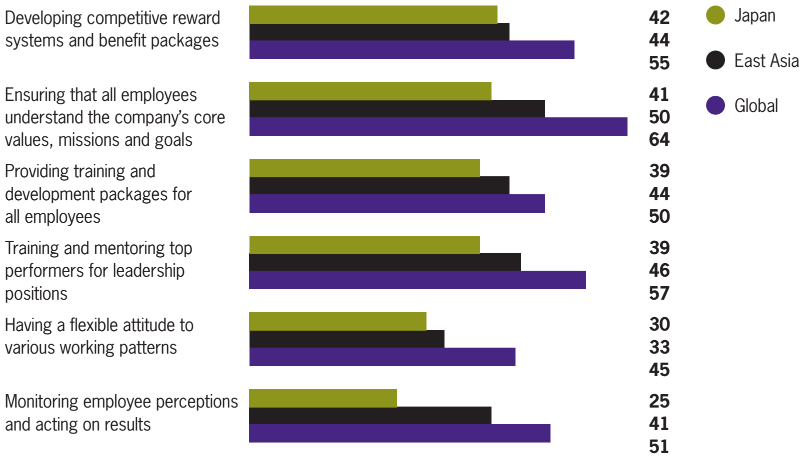
Source: Grant Thornton IBR 2008

Recruitment and retention

- The balance of PHBs in Japan more focused on retention than one year ago is +3 per cent. This is well below both the East Asian business (58 per cent) and global business (59 per cent) averages, and represents a 38 per cent fall since 2005.
- 42 per cent of Japanese businesses develop competitive reward systems and benefit packages to aid recruitment/retention.
- Cited by 52 per cent of Japanese businesses, a fall in product quality standards is viewed as the major problem staff retention issues have caused.
- It is costing 17 per cent of PHBs in Japan businesses significantly more to pay their staff than it was 12 months ago. This is below both the East Asian (68 per cent) and global (63 per cent) averages.

Figure 7: Usage of recruitment and retention tools for Japanese businesses compared to the East Asian and global average

Percentage of businesses rating the level 4 or 5 on a scale of 1 to 5 where 1 is not at all and 5 is a great deal



Source: Grant Thornton IBR 2008

Outlook for the Japanese economy

With external demand in the global economy softening, exports will not be the boost to growth that they have been in the past. Furthermore, industry surveys show most firms plan to cut back on capital expenditures. Sustaining real GDP growth at current levels will thus rest increasingly on the shoulders of consumers. However, they look likely to stay on the sidelines in 2008 with some sentiment indicators having hit all-time lows. Even with residential investment likely to recover strongly, real GDP growth may slow to one per cent in 2008.

In 2009 growth should pick up as the global credit crunch comes to an end and exporters and consumers look ahead to better times. But mainland China's economy is expected to slow further and 2009 has the potential to be a worse year for Asia than 2008. With export growth remaining slow, and rising consumer demand boosting imports, the external sector's net contribution to headline growth will wane considerably.

The outlook depends heavily on a comparatively smooth end to the global credit crunch followed by a recovery in the United States. However, sub-prime woes in the United States could depress US consumer spending which would have severe implications for the Japanese economy.

The Grant Thornton International Business Report (IBR) 2008 examines the attitudes, plans and trends of 7,800 privately held businesses in 34 economies across six continents. The Grant Thornton IBR builds on data collected in previous surveys and boasts 16-year trend data for European Union (EU) countries and six year trend data for international economies.

To find out more about the Grant Thornton IBR and to obtain copies of reports, including focuses on emerging markets, corporate social responsibility and recruitment and retention, please visit www.internationalbusinessreport.com.

Focus reports are also available for each of the 34 participating economies, as well as regional and global summaries. You can also complete the questionnaire online and benchmark your answers against PHBs around the world by industry, size and geographical location.

Participating economies

Argentina
Armenia
Australia
Belgium
Botswana
Brazil
Canada
Mainland China
Denmark
France
Germany
Greece
Hong Kong
India
Ireland
Italy
Japan
Malaysia
Mexico
Netherlands
New Zealand
Philippines
Poland
Russia
Singapore
South Africa
Spain
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