When Small is Big

Why do investors pick London ahead of New York and Tokyo? Solid corporate governance? Low costs? It's certainly not the weather. In fact, there are many reasons the British capital, time and again, tops global polls as a preferred financial hub. The latest one is the array of new Shariah-friendly products offered to tap oil-rich nations' funds.

Now, our cover story on this politically charged issue says Tokyo has also stolen a march on the U.S. by feting such investors in a quest to become Asia's most attractive financial center.

Indeed, identifying and exploiting that elusive, lucrative niche market is a fundamental pursuit for many successful businesses, especially startups. Achievement in a market dominated by a handful of long-established and powerful global players deserves a closer look. On page 34, our Case Study by an acclaimed international motor reviewer reveals how a Nagoya automaker has patiently built up a specialist SME, and is now ready to crack Western markets. During a two-day visit to the Mitsuoka Motors factory, he found that the company had garnered such industry-wide respect for its business acumen that "rivals" happily supply engines and other parts for a fleet of unique and rather eccentric sports cars and hearses. The *ACCJ Journal* plans to feature more successful SME models in 2008, to show how entrepreneurial flair can overcome the many perceived obstacles in a strong corporate culture.

In this special Corporate Social Responsibility issue, we welcome another new writer who offers an academic's take on how to secure the best partner to complement your CSR efforts in Japan (page 42). She explores in depth the problems and obstacles facing successful CSR efforts here in a report that could save others much time, cost and effort.

Logistics gets generous coverage this month, too, with an ACCJ Roundtable on page 26, and an Opinion Leader (page 40) by a very senior airline association official who speaks bluntly on the issues facing a fast-expanding business.

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CSR Benefits People, Environment and Business

One of the ACCJ's three themes for its 60th year is Corporate Social Responsibility. CSR is a carryover as an ACCJ priority from prior years. A good question is why we should continue to highlight this topic instead of just concentrating on our newer initiatives this year. The reason is that ACCJ members have made a significant and valuable contribution to Japanese society during the ACCJ's 60-year history and the focus on CSR is a good way to emphasize that. In Japan, CSR is often identified with charitable contributions but our companies have shown that CSR can be a part of our everyday businesses and contribute to the profitability of our businesses. For example, from the ACCJ's earliest days, corporate members have been leaders in gender and age equality and cultural and ethnic diversity in their employment practices. While our companies have benefited from the ability to hire from a larger pool of candidates and select and promote employees based on their capacity to contribute, they have also served as an example to domestic employers of the advantages of more open employment practices.

This is just one example of how CSR is just good business practice. There are other examples as well. Recently, many American companies have focused on reducing their emissions of greenhouse gases, not just because a smaller carbon footprint is good for the environment, but also because of the potential to save money on energy costs in the long run. My own company, when it built a new call center in Nagasaki, included a large day-care center for employees' small children. This benefit has allowed us to attract more better-qualified employees. Surveys of Japanese women indicate that the lack of such facilities is one factor in Japan's low birth rate. Employer-sponsored day-care can help in meeting Japan's demographic challenges.

The public has a heightened awareness of environmental issues, food safety, healthy lifestyles and healthcare, which creates marketing opportunities for products that contribute to improvements in those areas. Companies seeking profitability in creative and thoughtful ways can contribute to society. Many of our member companies in consumer goods, financial services, pharmaceuticals and medical devices, for example, are actively trying, often in the face of entrenched regulatory practices and opposition from domestic competitors, to introduce products that will be beneficial to Japan's aging population.

Companies can also improve their bottom lines by changing the way that they approach compliance with laws and regulations. Rather than being a burden and purely additional cost, superior compliance is an investment in the business. A run-in with a regulator and the resulting damage to a company's reputation can take years to overcome or even do permanent damage. Most laws and regulations are intended to protect consumers. Those companies that go beyond the bare minimum required by the regulations and actively seek their customers' welfare through good compliance practices can promote their superior record and customer satisfaction and they will be rewarded in the marketplace.

In the coming months, the ACCJ will be sponsoring a number of events and programs to help companies better understand and implement CSR. Please be on the lookout for those and participate. CSR is not just good, it is good for our businesses too.

asmith@accj.or.jp
Allan D. Smith is ACCJ President.

Faith in Finance

Japan, Europe, Asia woo Islamic and sovereign wealth as post sub-prime U.S. shows caution.

Tokyo is seeking to establish itself as a global hub for Islamic investment as Shariah-compliant financial products are taken seriously by some Western institutions. A series of initiatives, including the proposed launch of a groundbreaking Islamic bond, or *sukuk*, by the government-owned Japan Bank for International Cooperation (JBIC) could further strengthen Tokyo's bid to become Asia's financial center in a market estimated to be worth $100 billion and growing rapidly.

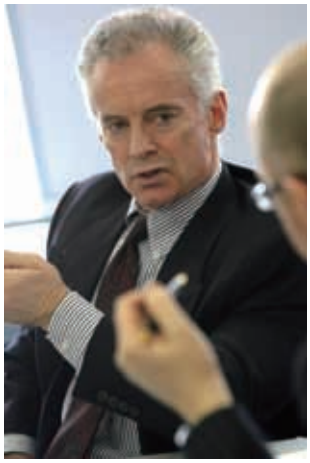
One reason Islamic finance—under Shariah (Islamic Law), interest payment is forbidden in financial transactions—is thriving as conventional financing systems reel from the sub-prime mortgage crisis is that it is based upon real economic transactions. This, argue some analysts, makes it immune from the massive leveraging that occurs in Western systems when debts are securitized and parceled out among myriad investors, divorcing lenders from the original transaction.

One certainty is that Islamic finance is expanding very rapidly, drawing huge volumes of petro-dollars from the Middle East and elsewhere as oil prices soar. The Malaysian capital Kuala Lumpur has until now been the acknowledged Asian hub of Islamic financing, but Singapore and Hong Kong are competing strongly while London is becoming a leading spot for such products, ahead of New York for now.

Tokyo began to take serious notice of Islamic finance in 2007 when the government decided that Japan needed to bolster its financial services industry. The Tokyo Stock Exchange and credit rating agency Standard & Poor's (S&P) launched a new stock index for Islamic investors in large-cap Japanese stocks. Daiwa Asset Management and Societe Generale Asset Management (Japan) have introduced Islamic exchange-traded funds, while Nomura Asset Management is planning to launch products aimed at Islamic institutional investors.

Meanwhile, Boubyan Bank, of Kuwait, has bought three Tokyo office buildings for ¥4.38 billion, leasing them back to the previous owners. The properties become part of a global, open-ended real estate fund that could serve as underlying assets for future Islamic transactions. The deal creates a useful precedent for Japanese institutions to follow as

Geographically speaking, Japan is great; politically, it's off the map.



Philip C. Jones, Managing Director, Morgen, Evan & Company, Inc.

Nathan Paine, Vice President, Transactions and Business Development, AMB Property Japan, Inc.

Scott A. Smalley, General Manager, Contract Logistics, Kuehne and Nagel Ltd.

Tom Wilken, President, Wallem Shipping Limited

Smalley: You have to consider the costs: fuel, expressway tolls, etc., which are passed on to the consumers. To take one example, there isn't much rail infrastructure here for cargo, compared to North America. Only about 20% of cargo travels by rail.
Wilken: And there's a coastal element as well, with ships running from Japanese port to Japanese port. This is done at extremely high costs. The costs stem from such things as the legal requirement that ships must be Japanese flagged and, thereby, by Japanese convention are crewed by Japanese crews, whose pay, internationally speaking, is very high.

So the Japanese domestic shipping scene is protected and extremely costly.

So I wonder whether "efficiency" should merely be a measure of time, convenience—and a happy smile.
Paine: Restaurants are a good analogy. We've all been to Japanese restaurants, and they're all great at giving you what's on the menu. But if you deviate from the menu, the system breaks down.

How important is Japan as an international transshipment hub? After all, this island country lies between the continental U.S. and the Asian mainland. It appears to be very well positioned, geographically, for such a role.

Jones: If you're talking about ocean cargo, that opportunity has passed.
Wilken: Japan was such a hub, back in the '80s, but it's been lost. Kobe would be a perfect hub, given Northern China's lack of adequate ports. But it hasn't happened because of the relative high costs, which have never come down since the 1980s. Pusan [South Korea], by contrast, is a huge hub for Northern Asia. And now it's even a reverse hub, with a lot of Japanese cargo moving over to Pusan.
Paine: It's literally a case of "Japan passing." Ships nowadays are so big that you can leave China and head straight to the U.S., without having to stop over in Japan.

Geographically speaking, Japan is great; politically, it's off the map.

But a number of seaports in Japan's provincial regions are promoting themselves, making pitches to foreign investors. So isn't there at least the will to try to turn things around?
Jones: I've got one experience that may shed light on that question.

Every prefecture says it wants greenfield construction and more jobs, and so on.

Well, myself and a client, a global operator of port infrastructure, made a detailed proposal to the

… there doesn't seem to be much of a consumer lobby or user lobby shouting, "We want lower costs!"

Perfect for key ocean-cargo business, but Kobe's Rokko island is restrained by costs and competition.

City of Kobe not too long ago, whereby my client would spend ¥18 billion to build and then operate a state-of-the-art, ship-handling and container terminal. Most folks in the industry don't know this, but Kobe had an approved plan, prior to the earthquake, to build a new terminal area, called "New Rokko Island," on reclaimed land. My client was willing to lease 1,000 meters or more of the planned 2,000 meters of wharf length, and nearby yard area, thereby giving the city a base client for more than half of the island. We saw it as win/win: a chance for my client to gain an access point to the Japan market and a chance for Kobe to re-establish its leadership in ocean-cargo handling in general and to recapture some of the North Pacific transit cargo.

But we never got anywhere. The city authorities thought the plan—having one company to manage the gantry cranes, the container yard, the truck-transfer area, a break-bulk area, etc., all on a tightly integrated basis—was just too disruptive. They told us, off the record, to find local partners and work within the system. So, in the end, they wanted something incremental, not something that would upset a very carefully choreographed business environment.

Smalley: Kobe officials have gone to Singapore a multitude of times to look at what the Singaporeans have done. The Singaporeans, it should be pointed out, have automated nearly all their facilities, adapting technology to reduce their carrying and transfer costs within their port.

Kobe, however, has organized labor and there's pressure to remain how they've always remained. And so they just can't be competitive.

But do Japanese officials—in the central and local government and bureaucratic ranks—have the wherewithal to make the necessary reforms to make Japanese seaports competitive again?

Wilken: Yes. It can be done. But you need to take that first step – the will to make it happen. Things are happening, but terribly slowly. I'm not sure exactly why. Maybe one reason is that there doesn't seem to be much of a consumer lobby or user lobby shouting, "We want lower costs!"

Smalley: I think it's leadership as well. Junichiro Koizumi [former Japanese prime minister] got a lot done in the time he was around. Why? Because he was willing to tell the country, "This is what we need." But now things seem to be reverting.

Paine: You also have a lot of cannibalization here. For instance, the Kobe government wants to have an airport and a port, and you have [nearby] Osaka that wants to have *two* airports and a port. There's only so much of the pie. And all the regional governments are grabbing for it. Since the 1990s,

The real competition in this market comes from the 60-year-old company president who won't sell his or her assets, or who won't do what needs to be done for the business.

In the wake of 9/11, Japan, like other industrialized countries, ramped up its security procedures at airports and seaports. How would you rate the Japanese authorities' approach?

Smalley: The port security issue was the U.S. government insisting that Japanese ports be more secure. And it was under this pressure that the Japanese went around and did things like put barbwire around the port areas. Before, security was very limited.

Wilken: The security measures [at seaports] have been done efficiently, as far as I can see. There have been no impediments.

Outsourcing to third-party logistics [3PL] providers has been less common in Japan than in other big markets, but it is predicted to grow by leaps and bounds in the years ahead. How big of a piece of this market do you think foreign 3PL providers stand to grab?

Smalley: I think this "leaps and bounds" will really take the form of consolidation within the industry, by not just foreign companies, but Japanese ones as well. I know that all our major competitors are looking for opportunities to merge or acquire the smaller warehousing and transportation companies.

There isn't much new business taking place; in fact, I suspect, the business is actually shrinking.

In retail, you're going to see a lot more companies shift their stocks offshore, to mainland China, and then make direct shipments here. So a store in, say, Hachioji, will carry products slapped with stickers and prices done in China.

Paine: The reason the contract logistics market is so fragmented is its very nature—it doesn't lend itself so well to consolidation. That's because companies—Japanese ones are no exception—have a lot of ingrained historical practices. Then they try to outsource their logistics to someone else. But an important way that a 3PL makes its money is to integrate the newly acquired business into a larger platform with multiple customers.

So I think it's going to take a long time for any one company to take a large position here.

Logistics is a relatively new industry, and in Japan much of it continues to be done in-house, by subsidiaries on behalf of the parent companies. What challenges does that pose for you?

Paine: The real competition in this market comes from the 60-year-old company president who won't sell his or her assets, or who won't do what needs to be done for the business. One primary challenge for exclusively domestic and some of the subsidiary logistics companies is overcoming the inertia within the executive ranks.

Many of these executives have never operated in a truly competitive environment, as they have always maintained a captive customer in their manufacturing parent. Their management expertise has been developed in a cost-center operating environment, versus a profit-center operating environment. These types of companies frequently operate with legacy management, systems, facilities and staffing. As a consequence, their most senior management have little incentive to alienate themselves by making the tough decisions, such as upgrading their information technology, automating or mechanizing their distribution centers, attracting and training a young workforce to sustain the business, or monetizing assets to access valuable capital from their own balance sheets—which is necessary to restructure their businesses to be more cost-efficient and competitive globally.

The day I look forward to is when a Japanese company will look at the logistic provider in the same way they look at a lawyer—that they don't second-guess the provider's recommendation. I mean, you don't second-guess a lawyer's recommendation, do you?

Wilken: I wonder if that's because the transportation-distribution process is very often viewed in Japan as well down the food chain. It's not seen as intellectual as, say, marketing.

But, in fact, there is science involved. It's not about moving stuff; really; it's about managing assets.

Geoff Botting is a freelance writer based in Tokyo.

On the Spot

Toshiyuki Shiga

Chief Operating Officer, Nissan Motor Co., Ltd.

It's not easy being an automaker today—even a Japanese one. Most players in the industry count their blessings with profit margins as slim as 3%. Even those thin returns don't start flowing until hundreds of thousands of cars have been sold in each new mass-market model.

Still, you may not make a profit if you slip up in any of a million parts and processes, or if raw material costs spike, or if fickle fashions turn against you. And what if consumers simply decide to take the train instead? With new-car sales in Japan declining steadily over several years, could that be what's happening domestically? What does this portend for the future of Japan's auto industry?

Sales of new cars in Japan seem to be declining every year. How far has the market dropped? Will sales ever rebound?

Overall, unit sales declined by 4% over 10 years through fiscal year 2006 (ending March 2007). But over that period, sales of minicars (vehicles with engine displacement less than 660cc that enjoy special tax breaks in Japan) rose by 22% and sales of conventional cars dropped by 15% to less than 3.6 million [units]—about the level we saw 30 years ago.

As a manufacturer, the only thing we can do to counter this is to develop more attractive products and look for new ways to deliver value to our customers.

Toyota has had a 40-50% share of the Japanese market for many years, leaving Nissan, Honda and five other domestic makers to fight over the rest. With such intense competition, do any of the Japanese brands—even Toyota—make profits at home? Or is the struggle for market share just about saving face?

NISSAN MOTOR CO., LTD.

Well, I really can't comment on the profitability of other companies. But I can tell you for Nissan that our priority is not market share. What's important is that we meet the goals of our own business plan, reaching profit targets on sales objectives that we set for ourselves.

With our domestic dealer network, we have made substantial improvements in the context of intense competition as demand declines. On one hand, we've reduced fixed costs, and on the other we've increased revenue and profitability by introducing attractive new products and pursuing opportunities with used vehicles and services.

Even when domestic sales were booming, relative to the size of the population, didn't every automaker have many more sales outlets in Japan than in the U.S.? Now that the local market is clearly shrinking, is Nissan going to consolidate its dealer network?

PHOTOS JEREMY SUTTON-HIBBERT

The flagship Orochi is Mitsuoka's first motorcar built entirely in-house.

SME Case Study

Automaker a lesson in entrepreneurship.

Abroad, Mitsuoka Motors is barely known. But in Japan, the niche manufacturer turns heads and its popularity is spreading in Asia. Mitsuoka Motors Co., Ltd. invited the *ACCJ Journal* to its factory as it readies for the U.S. market.

OK. Perhaps it *is* hilarious. The Jaguar Mk2—that stately 1960s saloon decked out in chrome, timber and leather, with six beefy cylinders purring under the bonnet—*that* car cannot be confused with Nissan Motor Co., Ltd.'s Micra. For the latter is a modern supermini—round and compact, ergonomic and economic. Still, though, Mitsuoka has seen a chance to mix the two to create an all-new oddball—the Mitsuoka Viewt. Though technically very much a Micra, it unmistakably wears the Jaguar's tweed jacket. Unlikely, it might seem; but stranger things happen in Mitsuoka's Toyama Prefecture HQ.

How about the Mitsuoka Galue? A car based on Infinity's M35, with a front that recalls classic Rolls-Royces and Bentleys with its grille, is like a Greek temple in chrome. There's the similarly retro-styled Nouera, based on Honda Motor Co., Ltd.'s Accord; and there's the new top-model Mitsuoka Orochi—the first Mitsuoka that is built entirely in-house, only borrowing Toyota Motor Corporation's 3.3 liter V6-engine. In the 10 years that Mitsuoka has been in business, it has built and sold over 9,000 Viewts alone, and there is a club with thousands of members. Mitsuoka is a rising star in Japan's automotive market. It might be the smallest motor manufacturer; it definitely is the most eccentric one. But it works—and with fresh plans to start exporting.

Toyama, about 300 miles north of Tokyo, is home to 300,000. Its modern city center has straight, wide lanes lined by tall buildings. Akio Mitsuoka started importing European cars here in the late 1970s by specializing in the top segment— such as Lamborghini and Saab. It was a good choice, and Mitsuoka was able slowly but surely to start working on his biggest dream: his own car manufacturing plant. The first Mitsuoka car, called the Zero, came out in 1995. It was a basic two-seater sportscar with

Okay, the Viewt might not be fast, powerful, and not too civilized. Nevertheless, it has a charm all its own. You can definitely have fun in it, as long as you are not in too much of a hurry.

Handmade is what sets apart Mitsuoka from the bigger and better-known brands.

In front of the factory gates, a burgundy-colored Viewt is parked. Although the car might seem to have just been driven off the lot of a well-known UK detective TV series, you won't be fooled once the door is opened. The inside of the Viewt is very much 2008. It hasn't changed a bit from the Micra and—as this car is the base model—that means simple seats with no-nonsense fabric and a rather dull dashboard in grey plastic. Varnished walnut veneer, chrome clocks and bakelite switches are nowhere to be found. This cockpit forms an ergonomic workplace; speedo and other gauges are bright and big, and are all housed in one cluster behind the thick steering wheel—airbag included. In the console you will find plastic switches to control audio, heater and air-conditioning—under it, the gearlever for the automatic four-speed gearbox, as all Viewts are automatics. Apart from the Mitsuoka logo on the steering wheel, nothing differentiates the inside of this car from the ordinary Micra.

The Viewt's 1.2-liter engine runs smoothly and quietly. Mitsuoka offers a more powerful 1.4- and 1.5-liter variant, but our burgundy Viewt with 80 bhp will have to do. Steering is very light and the same goes for the throttle, as well as the brakes. Acceleration is not spectacular, to say the least. The 1.2-liter engine might not be the fastest—the added brightwork and bodywork that make this car what it is have made it put on weight. I can feel those extra 90kg now, as I go uphill and the Viewt very much needs its kickdown.

I have pointed the car toward the Tateyama range, not far from Toyama City. The roads are scattered with cars and trucks, but no one seems to take notice of our little Viewt. People in Toyama know Mitsuoka well and are used to its cars being driven around here. The view outside gets better and better the further behind we leave Toyama City, with scenic woodlands and rice plantations along the road.

But the car is struggling to reach the top of the hill. When the road turns into double lanes, even trucks take over. The kickdown takes huge steps back to keep the car in motion. We reach the top screaming. Okay, the Viewt might not be fast, powerful, and not too civilized. Nevertheless, it has a charm all its own. You can definitely have fun in it, as long as you are not in too much of a hurry. This car has a character of days long gone by, while it's modern, too. The Japanese obviously love it.

The tires squeak when we reach Mitsuoka head-quarters again. Getting from the top to the bottom

"We used to import hearses from the U.S., but the quality of these cars was poor. That's the reason why we started building them ourselves, using Infinity models as a base."

Takanori Aoki, designer of the Orochi.

of the mountain went a little quicker than the ascent! An enormous truck that carries several new Mitsuoka cars is just about to leave from here. Between two Mitsuoka Galues, there's a stately black hearse. According to Takazawa, this is something quite new to Mitsuoka.

"We used to import hearses from the U.S., but the quality of these cars was poor. That's the reason why we started building them ourselves, using Infinity models as a base. In the meantime we sell them [Mitsuoka hearses] throughout Japan. There is a huge market for vehicles like these, as Japanese hearses always were styled traditionally," Takazawa says. "Now that traditional Japanese funerals are decreasing, demand for our hearses is increasing rapidly. We produce three to four cars like this every month."

Such is Mitsuoka: always looking for a new niche. In one of the factory halls we can actually see the craftsmen work on a brand new hearse—quite a project. Cars in several stages of building can be found here, but everywhere is clean and tidy. Workmen are dressed in white overcoats and it's clear they all have their own task.

"By now, we are becoming well known in the Japanese automotive industry," says Takazawa, "which means it's getting easier to attract good people."

Yushi Naruyama is one of them. "It's so much nicer to work for Mitsuoka than for one of the big manufacturers," he says. "Here, you can build a car; with Honda, Mazda or Nissan, you can only build a part of the wheel suspension or the gearbox."

That is also exactly the kind of atmosphere Akio Mitsuoka likes in his dream factory.

"Mr. Mitsuoka himself can be found regularly in the factory, working on the floor on the cars," says Takazawa. "He loves it and he couldn't do without it."

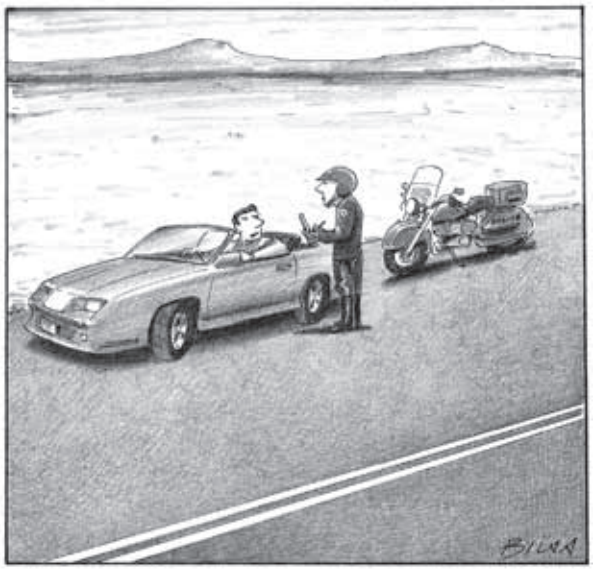
But how about the future? What's the new model going to look like?

"Only last year we started production of the Orochi and have just launched our new Galue. There are no plans for new models in the near future, as we will focus on exporting now," says Takazawa. "We do have lots of customers asking for a Mitsuoka SUV, though, but Mr. Mitsuoka doesn't like the idea. The classic appearance he is so keen on doesn't fit the style of a modern SUV."

Mitsuoka does it his own way.

"My way" happens to be exactly what "Galue" means in Japanese. But you might have guessed that.

Jeroen Booij writes for the international motoring press and is based in Amsterdam.



"Do I know how fast I was going? Isn't that your job?"

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Air Industry Needs Common Vision

Since 2001, airlines have done an impressive job of rebuilding their business. This includes a 64% improvement in labor productivity, a 25% reduction in sales and marketing unit costs, and a 16% cut in non-fuel unit costs. Not many industries can show this kind of performance.

Within the industry, we're starting to see some meaningful consolidation. Airlines are like any other business. We need the same commercial freedoms that other industries take for granted to sell our products where markets exist and to merge or consolidate where it makes business sense. But we're the only case in history where, to sell a product, we need an international treaty.

The growing challenges that airlines will face in 2008 reinforce the need for change. In December, we predicted a $5 billion profit for 2008 with important uncertainties in the calculation. Oil prices would remain high. Even with an optimistic average price of $78 per barrel, the bill will grow by $14 billion to $149 billion. The fallout from the U.S. credit crunch is widening and revenues will be hit. In December, U.S. traffic dropped 3.4%.

Already, it's clear that 2008 will be difficult for the global industry. Japan will not have much of a buffer, with its heavy reliance on oil imports and the U.S. consuming 22% of its exports.

But the good news for Japan is that it's well positioned to play a leadership role on our most important issues in safety, security, efficiency, infrastructure and environment.

Our top priority is safety. In this regard, Japan's record is excellent. It has been nearly a quarter of a century since the last fatal accident here.

Security is a sister priority to safety. The industry is much more secure than in 2001. But the system remains an uncoordinated mess that costs airlines and their passengers $5.9 billion a year. For that price, we deserve better service. People who travel frequently will see some improvement with the common approach to liquids and gels. But that's not enough. Every airport has its own process. Shoes on or off? Laptop in our out? How can passengers have confidence in the system when the answers are different each time?

I have just experienced Japan's new facilitation procedures—the fingerprinting of all foreign nationals on entry. I say congratulations to both industry and government for working together on such a smooth implementation.

One of our leading issues is efficiency—simplifying the business. This means using technology more effectively to make travel and shopping more convenient. Narita terminal 1 is a model for check-in procedures, with over 160 common-use kiosks.

We are now working with Japan's three biggest airports to improve the country's airport infrastructure. Our needs are not rocket science. We require

Views expressed in the Opinion Leader column are those of the author and do not necessarily represent the views or policies of the ACCJ.

ILLUSTRATION FOR THE *ACCJ JOURNAL* BY DARREN THOMPSON