Survey Report on Overseas Business Operations by Japanese Manufacturing Companies

—Results of the JBIC FY2018 Survey: Outlook for Japanese Foreign Direct Investment (30th Annual Survey)—

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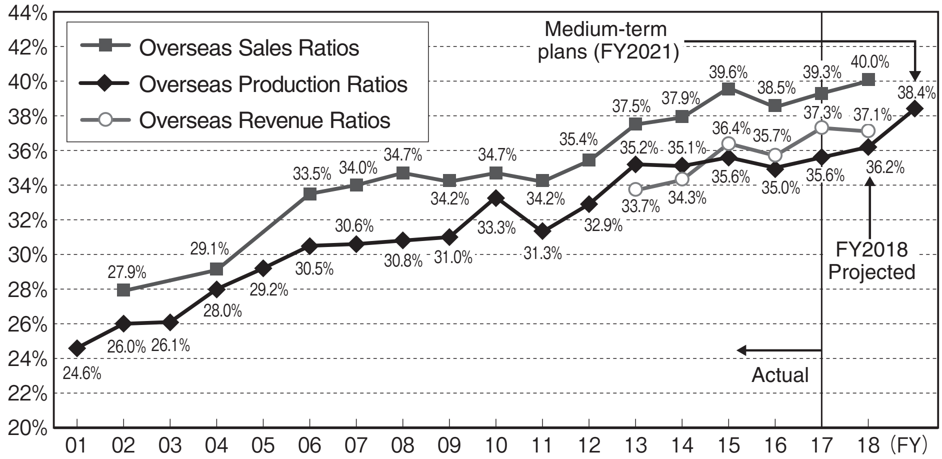
Figure 1. Overseas Production / Sales / Revenue Ratios



Note1: Calculation methods of various indicators (all consolidated basis)
• Overseas Production Ratios = (Overseas Production) / (Domestic Production + Overseas Production)
• Overseas Sales Ratios = (Overseas Sales) / (Domestic Sales + Overseas Sales)
• Overseas Revenue Ratios = (Overseas Operating Revenue)/ (Domestic Operating Revenue + Overseas Operating Revenue)
Note2: In the graph, the respective ratios were calculated by simply averaging the values the respondent companies provided.
Note 3: Overseas sales ratios were not surveyed in 2003 and 2005.

1. Introduction

The Japan Bank for International Cooperation (JBIC) has released its "Survey Report on Overseas Business Operations by Japanese Manufacturing Companies." For this year's survey, as in other years, questionnaire forms were sent out toward the end of June, and responses were collected through up to September (number of companies questionnaires were mailed: 1,012, number of valid responses: 605, response rate: 59.8%). JBIC would like to express its appreciation to the companies that cooperated with this survey.

In this year's survey, we asked the companies the survey's usual topics of "Business performance evaluation," "Overseas business prospects," and "Promising countries/regions over the medium-term," as well as individual topics of "Impact of protectionism" and "Views on environmental regulations and development of environment-related business."

2. Overseas Production / Sales / Revenue Ratios

The overseas production ratio in FY2017 reached 35.6%, marking a recovery from the temporary drop in FY2016. It is expected to increase to 38.4% in the medium term (FY2021), which indicates that the companies are still eager to expand their ability to produce overseas. The overseas sales ratio rose to 39.3%, also recovering from 38.5% in the previous year. The overseas revenue ratio marked a record high of 37.3%. The evaluation of satisfaction with business performance in FY2017 also indicates that performance was robust especially in Asia and Europe, and it appears to have propped up business performance overseas. However, overseas revenue prospects for FY2018 was 37.1%, slightly lower than that of FY2017, representing companies' concerns over factors such as global economic slowdown (Figure 1).

3. Medium-term Prospects for Overseas & Domestic Operations

440 companies (75.6%) responded "Strengthen/expand"

for overseas business over the medium-term (Figure 2). The ratio of "Strengthen/expand" for overseas business had been in a declining trend from the peak of 87.2% in FY2011, as more companies were focusing on maintaining their present business scale through actions such as consolidating factories and strengthening existing bases, but this year, the downward trend came to a halt. Ways to strengthen business include "Introducing new production facilities to meet the rising demand in Asia," "Expanding business for the upper-income market in China," "Reorganizing production/sales system in anticipation of the rise in demand of EV-related business," etc. The response rate of "Strengthen/expand" among mid-tier firms/SMEs is lower than that of large corporations, but it still increased by 8.6 points to 69.2%.

As for the medium-term prospects for domestic business, the response rate of "Strengthen/expand" increased substantially to 45.9%, recovering to the level prior to the 2008 financial crisis (Figure 3). As for ways to strengthen/expand, common responses were "Increasing value of products/improving production lines" and "Increasing sales volume, developing new customers," the background to which is companies actively investing to upgrade domestic facilities. Also, "Focusing on mass production of standardized products in overseas bases, while strengthening ability to produce wide range of value-added products in small volumes in domestic bases" was a common response.

From the time series analysis, the response rate of "Strengthen/expand" for overseas business is hovering at a high level, while that of domestic business is significantly increasing in recent years, which indicates that the companies are focusing more on domestic business (Figure 4).

4. Rankings of Promising Countries

The respondent companies were each asked to name up to five promising countries/regions for overseas business over the medium-term, and the results are shown in time series graph in Figure 5. China maintained the top spot, and its percentage share rose 6.5 points from the previous survey to 52.2%. By industry, percentage shares increased particularly in general machinery, precision machinery, etc. With capital investment increasing under the "Made in China 2025" plan, demands for foreign companies' products and technologies are increasing, resulting in strong sales of semiconductors and machine tools. Also, the rising income level in China is spurring growth of on-

Figure 2. Medium-term Prospects (next 3 years or so) for Overseas Operations

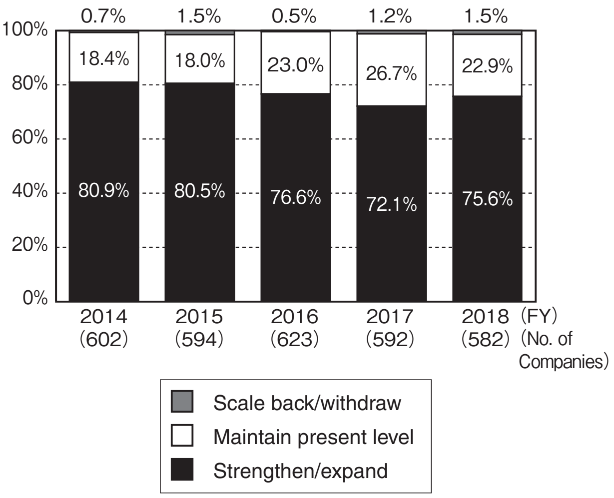


Figure 3. Medium-term Prospects (next 3 years or so) for Domestic Operations

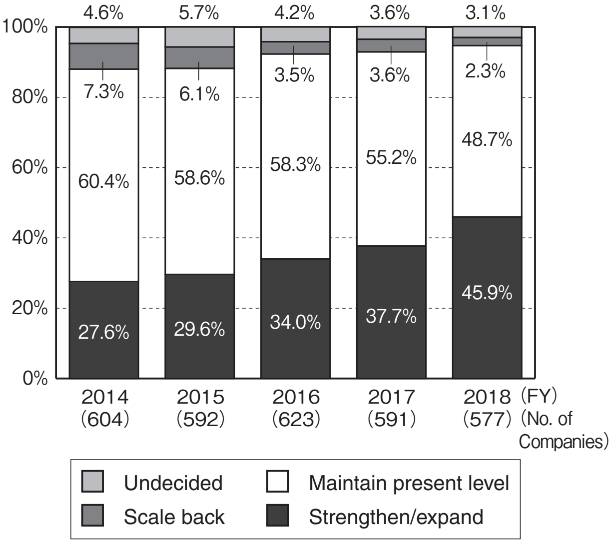
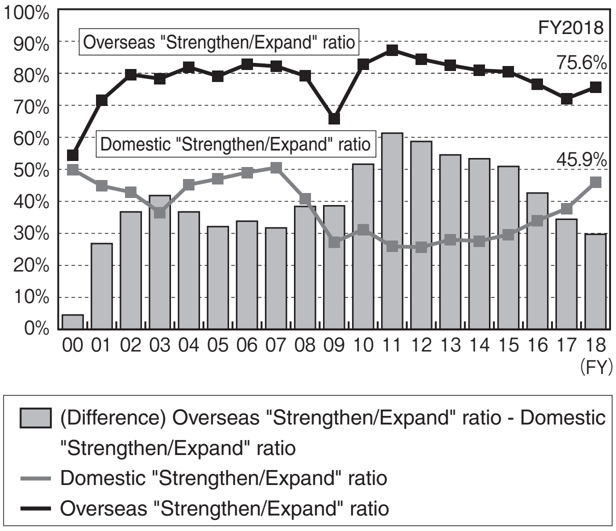


Figure 4. Shift in intentions to Strengthen/Expand Businesses (FY2000-2018)



line sales of consumer goods (health-care related products, etc.) and durable goods (passenger vehicles, etc.). Other countries in the ranking are as below.

- India fell to the second place in FY2017, but its percentage share recovered to 46.2% this year, as confusion, such as elimination of large denomination bills, has subsided.
- Thailand rose to the third place. Its share continued to increase from the previous survey supported by the votes from the automobiles industry. Economic recovery and impact of the "first-car buyer incentive" scheme by the Yingluck administration in 2011-12 (sales recovery from the slack growth following the last-minute demand, and the end of a five-year restriction on selling cars bought under the scheme, etc.) seem to have casted positive effects.
- Vietnam fell to fourth and its percentage share declined from 38.1% to 33.9%, owing to the impact of the new nontariff trade barriers under the Decree issued in Jan 2018, which forces car exporters and manufacturers to obtain Vehicle Type Approval certification by authorities in the exporting countries, etc.
- The US remained in sixth with percentage share of 28.8%, increasing by 2.7points from the previous survey. However, this year's margin of increase was relatively small compared to 6.8 points in the previous survey.
- While Mexico stayed at seventh place, its percentage share fell to 13.7%, 4.5 points down from the previous survey. Malaysia rose to tenth supported by steady exports. Germany's percentage share also increased, mainly in general machinery.

Figure 5. Change in Percentage Shares of Promising Countries/Regions over the Medium-Term

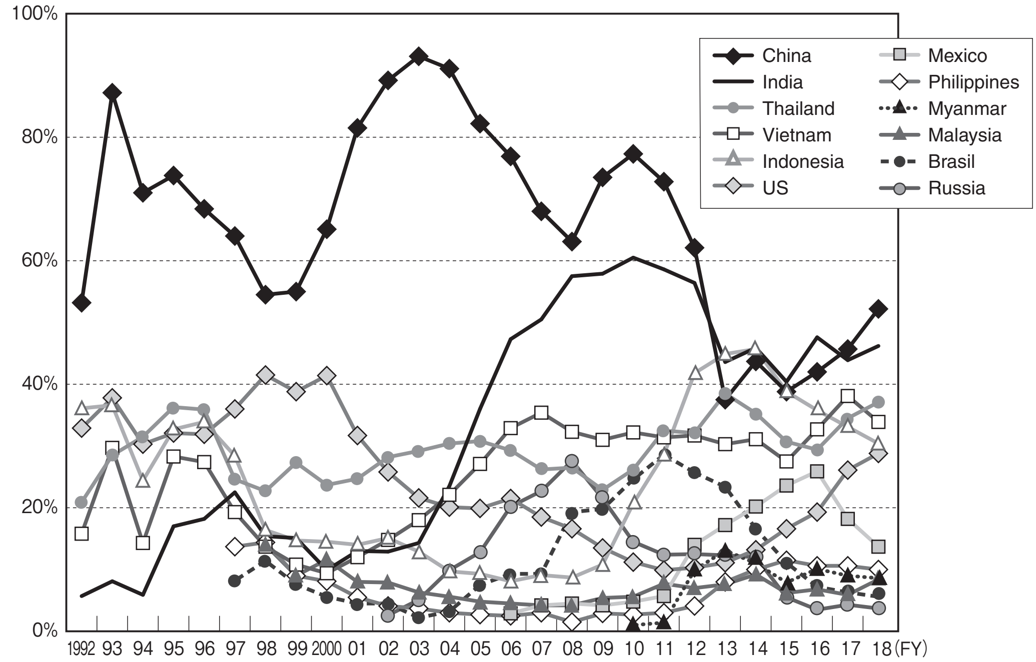
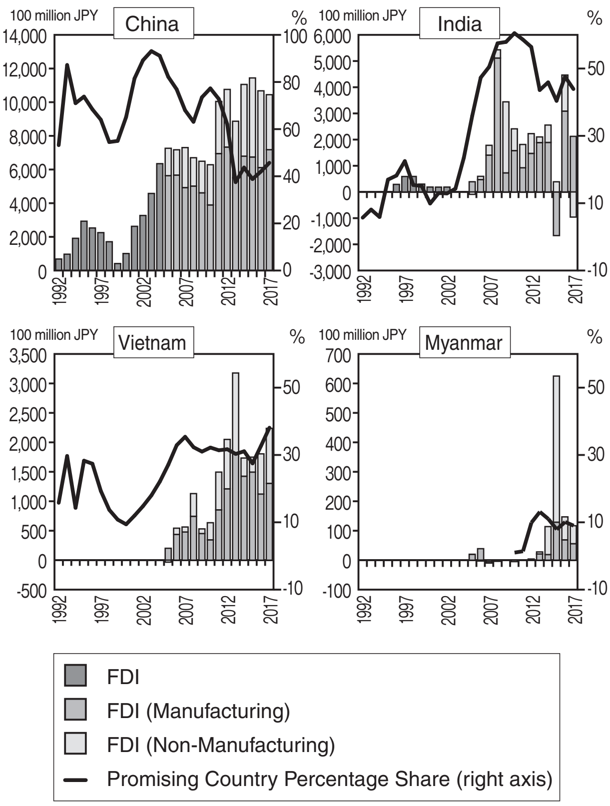


Figure 6. Percentage Share and Outward FDI of Japan (1992-2017)



Data sources: Ministry of Finance's "Monthly Finance Review (Balance of Payments Feature: Balance of Payments by Region)" (1992-2004), Bank of Japan's "Balance of Payments (Direct Investment by Industry and Region)" (2005-2014) and Bank of Japan's "Balance of Payments (Direct Investment Flow)" (2015-2017)

Note: There is no data industry based data for 2005 and before, so only the total amount is shown.

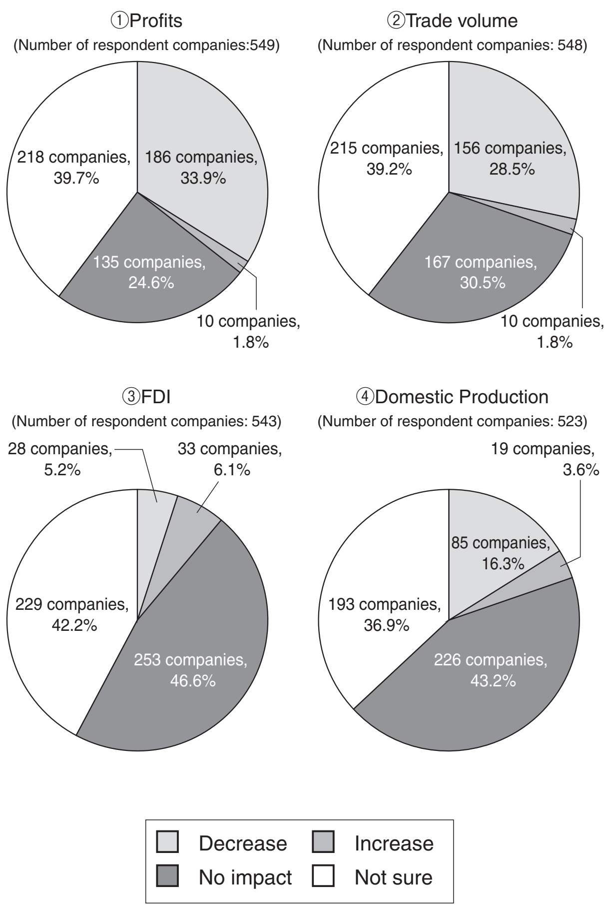
5. Correlation between percentage share and outward FDI

We conducted an analysis on the relationship between the percentage share as medium-term promising countries in our Promising Country/Region Survey and the actual amount of outward FDI from Japan, using long-term data (1992-2017). The results show some correlation between our Survey data and FDI (Figure 6). Specifically, in countries that are in the phase of receiving initial FDI from Japan, percentage shares tend to rise ahead of actual inflow of direct investment (e.g., Indonesia, India, Vietnam, Myanmar).

6. Impact of Protectionism

As for the impact of protectionism, considerable amount of companies are already expecting a decrease in "Revenue" and "Trade volume." Meanwhile, negative impacts on "Foreign direct investment" and "Domestic production" were yet to be seen, which indicates that companies are starting to acknowledge the short-term effects first. As for "Foreign direct investment" and "Domestic production," although negative effects did not appear strongly in the overall results, when we compare the preliminary results (answers up to July) and the final results (September), the latter had a slightly higher response rate of "Decrease." This suggests that prolonged protectionism will likely start to cast a negative impact on long-term investment activities (Figure 7).

Figure 7. Impact of Protectionism



As for profits, "decrease" had a high response rate of 33.9%. By industry, the response rate of "Decrease" was the highest in nonferrous metals (56.0%), followed by automobiles with 50.9% (note that half of the nonferrous metals companies handle automobile-related products). Since the possibility of an additional automobile tariff by the US government was widely reported during the survey period, this might have affected the auto-related companies to strongly expect a fall in profits. When asked how the profits will "Decrease," companies not only mentioned the negative impact of raised tariffs, but also voiced concerns over the deterioration of business environment caused by the prolongation of the US-China trade dispute, such as "Decrease in capital investment among clients that export to US/China", "Decline in demand due to the economic slowdown in China", "Slowdown of flow of business resulting in delayed market growth," and "Oversupply of goods in the Asian markets resulting from the inflow of Chinese products that were previously destined for the US."

As for the impact of protectionism on FDI, the most common response was "No impact" at 46.6%, and movements toward restructuring supply chains or withdrawing overseas bases seem to be limited, at least at this point. However, in interviews, within the companies that chose "No impact" on FDI, there were some that showed a passive desire to maintain a status quo, saying "We are holding off on investment decisions due to increasing global uncertainty."

Moreover, many responded that they were "Not sure" of the impact, suggesting that it is possible that these companies might move to cut back or withdraw FDI depending on future policy trends. For FDI, only 6.1% (33 companies) responded with "Increase," and the respondents were mainly auto-related. When asked about the reasons why they chose "Increase," some companies said "The market size of US and China is too big and is hard not to be attracted to, so we will continue to invest in these countries regardless of their trade policies," suggesting that their answers are not necessarily influenced by protectionism. Meanwhile, 28 companies (5.2%) responded with "Decrease." By country, the number of companies that chose "Increase" FDI for the US (20 companies) was larger than that of "Decrease" (13 companies). On the other hand, as for China, "Decrease" and "Increase" shared the same number (11 companies). Interestingly, as for FDI in the countries other than the US and China, "Increase" (12 companies) largely exceeded "Decrease"

(3 companies). While it needs to be noted that the number of companies that gave these answers is very small, it seems that protectionism could have an impact on FDI trends not only in the countries and regions implementing such policies, but in other countries and regions as well (Figure 8, 9).

Figure 8. Reasons for Increase in FDI
(No. of respondent companies=33)

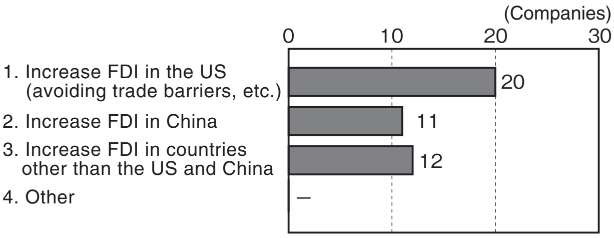
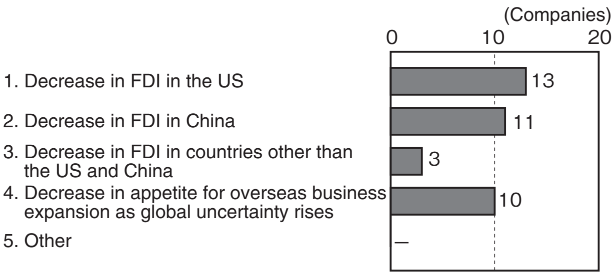


Figure 9. Reasons for Decrease in FDI
(No. of respondent companies=28)



7. Evaluation of USMCA

We conducted additional survey in early October for the companies that named Mexico and Canada as medium-term promising countries (59 target companies, 41 valid responses). When companies were asked which part of the USMCA agreement will be important to their business, the most common responses were "quantitative restrictions on auto imports" and "import ceiling for auto parts," followed by "wage clause" and "local procurement requirement," and all of them are directly connected to local production/sales. Also, 11 companies responded with "Reducing uncertainty and unpredictability of the investment environment, " and in interviews some positively said, "for a year we were taking a wait-and-see attitude for our new base in Mexico, but now we can start operating at last." (Figure 10, 11)

Figure 10. Agreement Points Important to Business

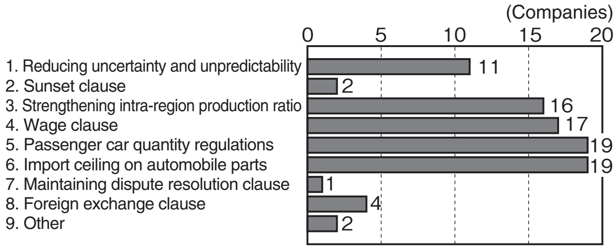
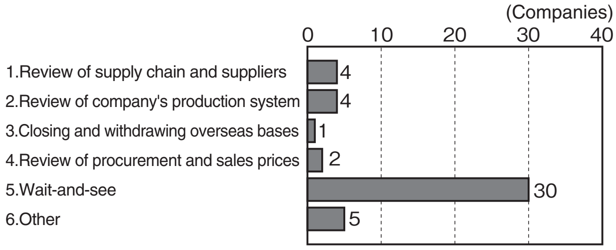


Figure 11. Business Development Based on the Agreements



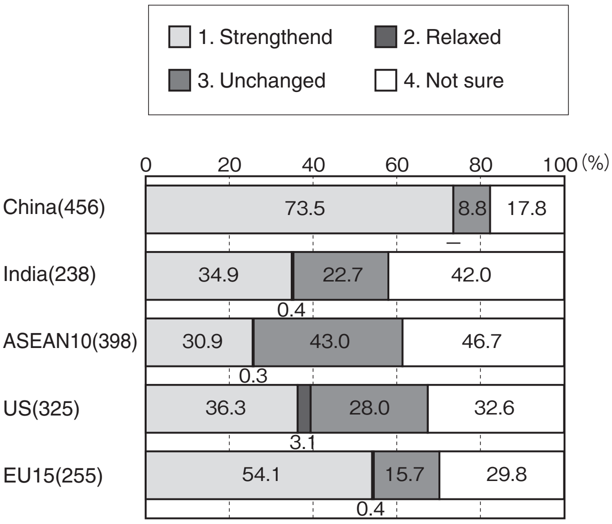
8. Environmental Regulations and Environment-related Business

Among the countries/regions Japanese companies are doing business in, China received the most responses for "Environmental regulations are being strengthened," (73.5%), followed by EU15 (54.1%), the US (36.3%), and India (34.9%) (Figure 12).

As for the effects of the tightening of environmental regulations on business, China received the most responses of "In a negative way" (51.3%), followed by ASEAN10 (41.5%). In contrast, EU15 and the US received more responses of "In a positive way" than "In a negative way," showing differences among the regions. As for "In a positive way," in almost all of the countries and regions, the majority of companies responded with "Increased demand for our environment-friendly products" (72.9%). Thus, it seems that for companies that handle environment-friendly products, areas that are tightening regulations are generating high demands. As for "In a negative way," there was no difference between advanced and developing countries, and as for specific effects, "Increase in the cost of production" received the most responses in all the countries/regions. However, in China, "Need to relocate or close our local factories" received a relatively large number of responses. In interviews, some companies, mainly those with production bases near urban areas such as Shanghai, expressed that they not only had to relocate or close their factories but also had to "find alternative suppliers due to sudden and forced shut downs of local suppliers" (Figure 13).

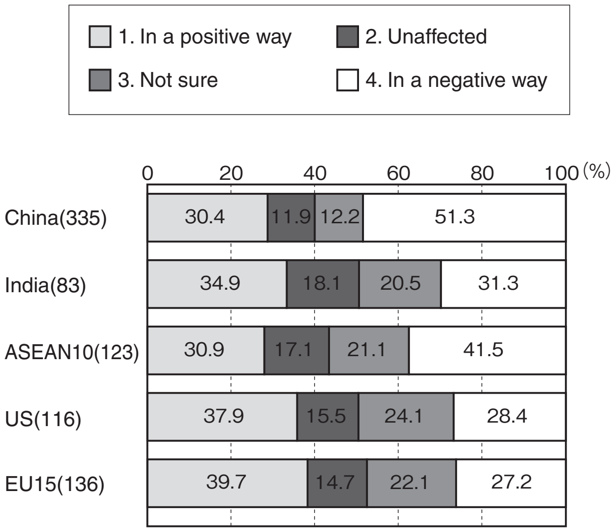
As for current and future approach to environment-related business, in the field of automobiles (EV and

Figure 12. Views on Environmental Regulations



Note: The total of the percentages may not be 100% because of multiple answers.

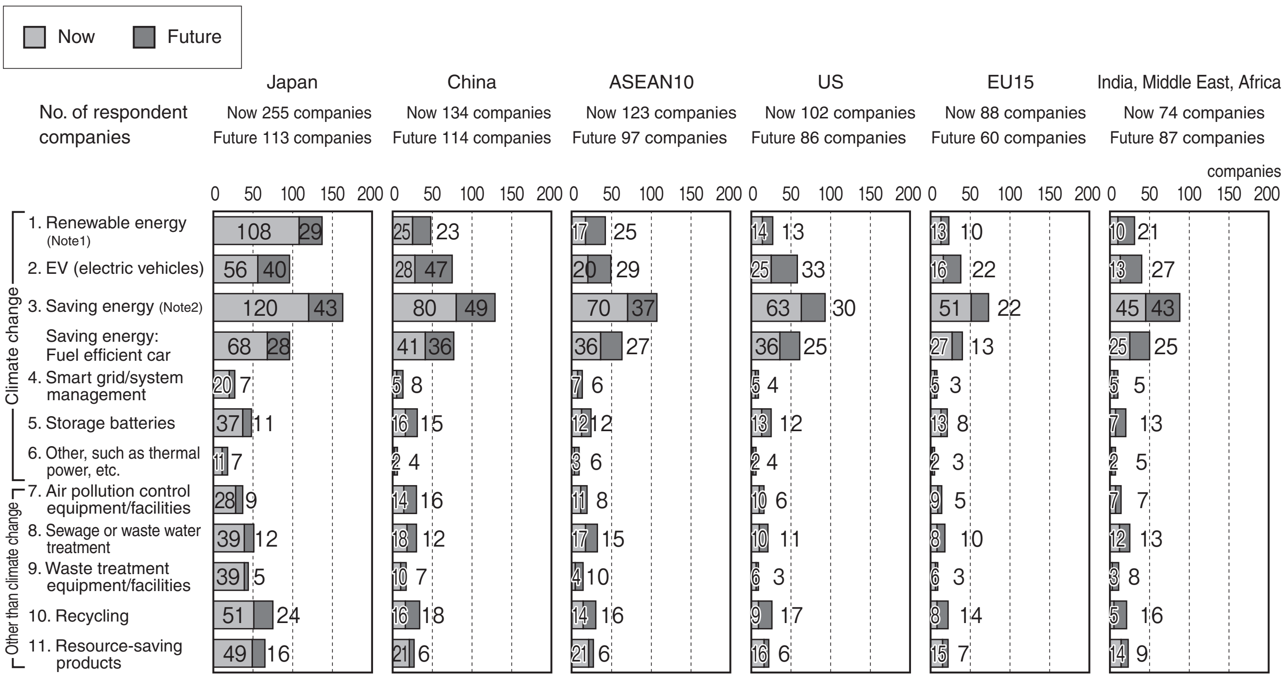
Figure 13. Effects of the Tightening of Environmental Regulation on Business



Note: The total of the percentages may not be 100% because of multiple answers.

fuel-efficient car) in China are expected to expand. Among climate-change related businesses, EV" and "Fuel-efficient car" attracted strong long-term interest, and the number of companies choosing China as their country of interest were especially high: 47 companies and 36 companies respectively. Companies that chose EV-related business as promising included not only the automobiles and electrical equipment & electronics industries but chemical companies, which suggest that a broad range of industry will enter the EV-related market in the future. As for green businesses not related to climate change, infrastructure business, especially in the field of sewage, waste water, and industrial waste treatment, are already carried out in ASEAN and India, and this trend seems to continue in the long run (Figure 14).

Figure 14. Existing Environment-related Business and Plans for the Future



Note1: Renewable energies … Solar, Geothermal, Hydro, Wind, Biomass, Other Renewable energies.
Note2: Saving energy … Steel, Cement, Electrical equipment & electronics, Automobiles, General machinery, Other Saving energy.