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Japan - Land of the Rising Sun

then an impenetrable fortress, now a land of opportunities?

Abstract

This thesis will be focused on examining the underlying reasons behind the rapid increase in interest among Swedish companies to enter the Japanese market or to further invest there.

The view of Japan has shifted from being seen as one of the world's most closed markets with a reputation as "Japan corporation", where every aspect of life is aimed at benefitting Japanese companies, often at the expense of foreign interests. Now instead people active in the market or in other way knowledgeable of it are speaking of practically endless opportunities and no special barriers to entry. This topic is interesting today as the amount of FDI in Japan is rapidly increasing, and has been doing so for approximately 10 years now, still there are no studies of what drives Swedish FDI in Japan.

This thesis explores the perceived differences between Japan before and Japan today and describes how the perception has changed. This is done in the form of a theoretical background compared to interviews, news and literature about Japan today.

The general conclusions are that Japan today is very different from Japan before and that the country is still rapidly changing. Today there is a completely different openness to influence and liberal economic forces are gaining strength. This is perceived to provide great opportunities for entry.

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Introduction

Background

The Japanese market has historically been regarded as more or less closed to foreign entry by most academics and businessmen. This situation has been created by the existence of an unusually large amount of both official and unofficial trade barriers restricting foreign firms from successfully entering Japan.

During more recent history these trade barriers have been gradually removed¹ and the level of Foreign Direct Investment (FDI) has increased dramatically since 1998. There has also been an increased interest about Japan, not only regarding business but also about the culture et cetera. In Sweden this interest has further been strengthened by major Swedish companies opening up or investing further in Japan during the last years. These investments include for example, IKEA opening their first two stores in Tokyo, H&M opening its first store in Tokyo, Volvo's acquisition of Nissan Diesel, Autoliv's acquisitions of a number of car parts manufacturers and many more. Today almost all Swedish companies have a local subsidiary or agent in Japan. For example the list of local subsidiaries to Swedish companies provided by the Swedish trade council is almost all inclusive of the larger Swedish companies.²

“Japan is such an important market; you cannot afford to not be there” Tommy Kullberg, former CEO of IKEA K.K.

This increased interest can also be seen in the now more positive attitude towards Japan and the Japanese market that is being showed by the Wallenberg group which is prominent in Sweden and this is often said to have influenced the view of other non Wallenberg companies towards Japan. The Wallenberg family has otherwise historically been prone to a negative view of Japan dating all the way back to when Gustaf Oskar Wallenberg worked as a diplomat in Japan during the beginning of the 20th century.³

The general opinion of Japan at the moment seems to be one of a market with great possibilities and opportunities, a sentiment well summarized in the following statement by the U.S Ambassador to APEC.

“Japan is now an attractive destination for foreign companies wishing to take advantage of its highly skilled labor force and reach its affluent population of potential customers.” Michael W. Michalak,

This is quite far from the earlier common view of Japan as a closed, impenetrable market and represents a fascinating change in how a country is perceived.

¹ See appendix for data on barriers to investment

² http://dbl.swedishtrade.se/list_subsiary.aspx?countryid=32

³ Interview with Atsushi Hasegawa, head of EIJS Tokyo

Purpose

This thesis will address the special circumstances that western companies face when doing business in Japan. The main focus will be on explaining the increase of western interest and investments in the Japanese market during the recent period, particularly the last ten years. It will also try to answer if the differences facing foreign companies in Japan are decreasing and if so, if the recent increase in foreign activity is due to a perceived increased similarity.

“On one hand, the MNE (Multi National Enterprises) is an agent of change, linking diverse national environments; on the other hand, the MNE must respond to national environments whose accepted patterns of behavior continually shift as they influence each other” Rosenzweig and Singh, 1991

Research questions

The researched questions in this paper are:

Why are foreign companies showing increased interest and increasing their investments in Japan during the last ten years.

Do foreign companies perceive a decreased difference and increased understanding? If they do, is this a cause of the increased FDI or a result of this?

Limitation

To limit the scope of study the essay will be focused on Swedish FDI in Japan and the interviews will be limited to Swedish companies. As of today there has not been any particular study focused at the driving factors of Swedish FDI in Japan.

Method

To address these questions I give you a theoretical background on international trade and the determinants of trade and company localization. I then present a number of Swedish companies that are active in Japan and are typical for particular categories. Finally there are some interviews with people who are or have been working for foreign companies in Japan and with persons knowledgeable about the situation and the change in Japan. The results of the studies of companies and these interviews are compared with the theory to give an explanation of what is affecting the increase of foreign investments in Japan.

Outline

The structure of the paper will be the following: Beginning with a description of the economy today, then follows a summary of FDI in Japan with a particular focus on Swedish FDI. After this there will be a theoretical summary on trade barriers and other hindrances to trade and investment and how these have changed. Finally there will be case studies and interviews followed by analysis and conclusions.

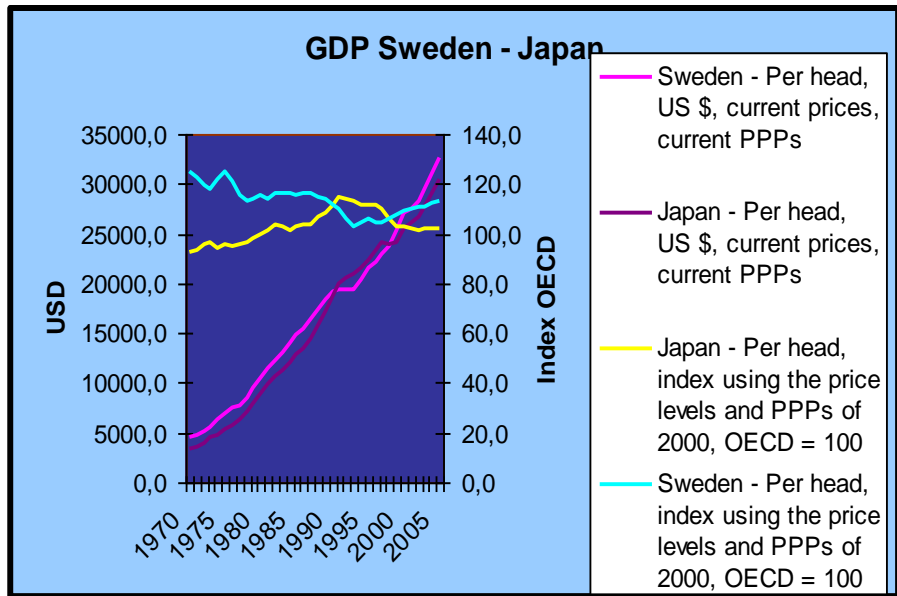
Japan

Often when you hear about Asia and the great business opportunities that are available on this vast continent with 3.9 billion inhabitants, more than 60 % of the world's population,⁴ you hear about developing countries such as China and India. These large and incredibly populous countries, that together house more than 2.4 billion people, attract more and more foreign businesses and are increasingly in the focal point of western investors.

What many do not know is that although much less populous than its large Asian neighbors, Japan has a greater total gross domestic product (GDP) than any other Asian country due to a much higher GDP per capita. The Japanese GDP per capita experienced a rapid increase after World War 2 and is today on par with the GDP per capita of western countries such as Sweden and almost 21 times greater than that of China. In fact the greater Tokyo area alone has a higher GDP than all of China.

	Japan	US	China	Sweden
GDP ex	4,567	11,712	2,234	359
GDP pc, ex	35,757	39,863	1,708	39,694
GDP PPP	3,911	11,570	9,412	271
GDP pc, PPP	30,615	39,377	7,198	29,926

The development of the Japanese GDP since 1970 can be viewed in the following diagram. It shows how the Japanese and Swedish GDP have developed on a similar level since the 1970: ies and that Japan's GDP is approximately equal to the average OECD country's GDP.⁵



⁴ <http://en.wikipedia.org/wiki/Asia>

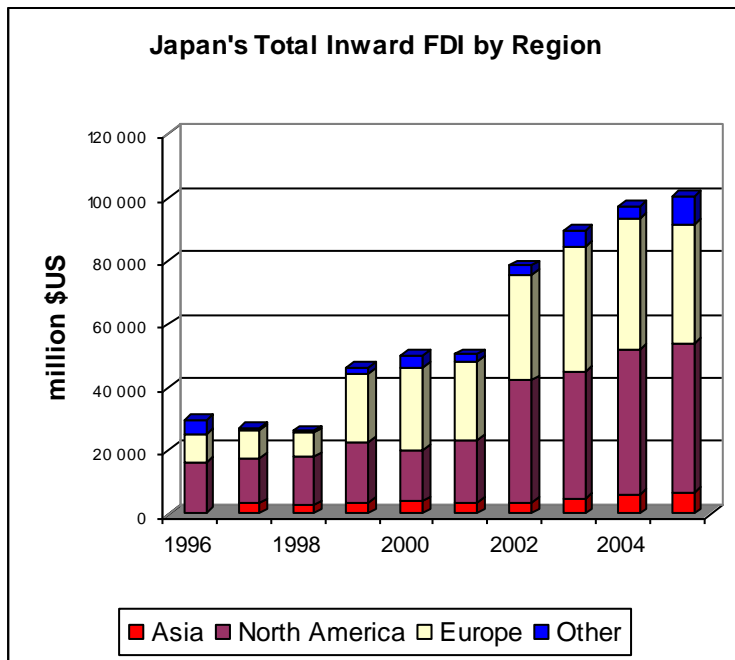
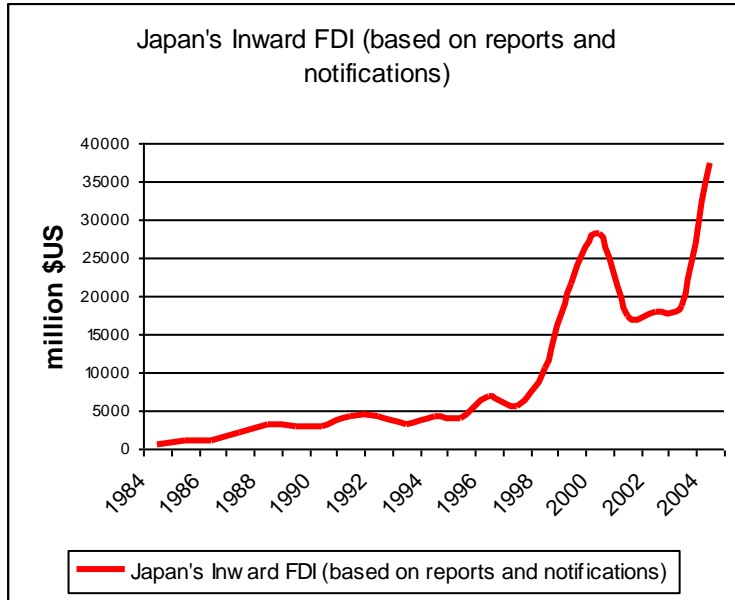
⁵ www.oecd.org

This high GDP per capita, combined with a population of 128 million,⁶ makes Japan the second largest economy in the world. Also striking figures are that the Japanese GDP comprises 60% of the total Asian GDP and that a fifth of all the services and goods produced yearly in the world are produced within Japan.⁷

Lately this huge market has become more available and interesting for outside entrants and we have seen an increasing level of Foreign Direct Investment (FDI) in Japan. This increase particularly started after 1997. FDI in Japan almost quadrupled between 1997 and 1999 and increased from 5500 million \$US in 1994 to 37500 million \$US in 2004.

This increase in FDI has primarily come from companies located in North America (47.1%) and Europe (37.6%).

Until the mid nineties the inflows into manufacturing and non-manufacturing sectors were approximately equal. The later increase in inflow of capital has primarily been focused on the non-manufacturing sectors in Japan.⁸ For a further discussion on this topic see page 44.



⁶ <http://www.stat.go.jp/data/nenkan/zuhyou/y0201b00.xls>

⁷ Swedish Trade Council

⁸ <http://www.jetro.go.jp/en/stats/statistics/>

Sweden – Japan

The large Japanese market has for a long time attracted Swedish companies. The first Swedish company to open up an office in Japan was the trading house Gadelius. They established themselves in Yokohama in 1907 and thereby commenced a hundred year old tradition of Swedish companies going to Japan.⁹

By 2004 approximately 100 Swedish companies had established subsidiaries in Japan and the total turnover of these companies equaled 37 billion SEK. Besides these official subsidiaries in Japan there are more than 1850 contracted agencies or similar arrangements between Swedish exporters and Japanese counter parties.

The result of all these contacts is a direct export from Sweden to Japan of approximately 15 billion SEK, which makes Japan, Sweden's third largest export market outside of Europe.

The Swedish export to Japan has decreased from the unusually high levels achieved in 2001. The decrease is much due to a lower level of telecommunication exports.¹⁰ However if the trade within companies also is included, the importance of the Japanese market greatly exceeds what the export figures show.¹¹

What also can be considered is the level of successfulness. As mentioned by a number of the interviewed persons and also in studies, it is not only sales that determine if a country or market is important. Measures of profitability might also be as important.

The Swedish companies today report high or very high profits in Japan which indicate that the market might be more important than what the export figures show.¹²

In the opposite direction, a large number of Japanese firms have invested in Sweden, and the Japanese investments in Sweden are actually several times larger than the Swedish investments in Japan. This is also strengthening the ties between the two economies and encouraging trade and exchange, particularly since many of the Japanese owned companies in Sweden are focused on production primarily for the Japanese market. One such example is Sweden's largest wooden house manufacturer that exports its total production to Japan.¹³

⁹ <http://www.gadelius.com/index.cfm?category=106>

¹⁰ <http://www.regeringen.se/content/1/c6/06/03/01/a4849126.pdf>

¹¹ <http://www.swedishtrade.se/japan/?objectID=564>

¹² <http://www.regeringen.se/content/1/c6/06/03/01/a4849126.pdf>

¹³ <http://www.regeringen.se/content/1/c6/06/03/01/a4849126.pdf>

Background Foreign Direct Investment theory

This part contains explanations of the basic theories, facts and statistics regarding foreign direct investment.

Factor endowments

What determines foreign direct investment? On a basic national level one can say that FDI is a result of different factor endowments. Some countries have more capital compared to labor than others. This means that capital is abundant in some economies and scarce in others. With a free flow of capital, the most mobile of the factors, the return of capital can be increased by investing in capital scarce markets.¹⁴

Capital and labor endowments for some selected economies in 1984¹⁵

Country	Capital (\$b)	Labor force (m)	Capital per worker (\$)
Switzerland	120	3	40 000
Japan	2 336	59	39 593
Canada	419	12	34 917
U.S.	3 696	116	32 421
Mexico	353	23	15 348
Rep. of Korea	204	14	14 571
India	482	254	1 898

Looking at these numbers one can compare them with the figures for FDI

Selected countries' stock of foreign direct investment in 1991¹⁶

Country	Host (\$b)	Source (\$b)	Ratio H/S
Switzerland	44.2	75.4	58.6 %
Japan	12.3	231.8	5.3 %
Canada	112.7	80.1	140.7 %
U.S.	487.0	655.3	74.3 %
Rep. of Korea	5.9	5.3	111.3 %

The trend for capital abundant economies is to be net exporters of capital, i.e. FDI.

This indicates that Japan should be a net exporter of capital. What can be observed is that there is a significantly larger difference between imported and exported capital than for other similarly developed economies. However some research indicates that the difference is over estimated in the statistical material. The most often cited research is one study done in 1988 by Julius and Thomsen that showed that foreign firms only accounted for 1 % of the sales in Japan while accounting for 10 % in the U.S. However if you study the data and the way the survey was done you will find some striking

¹⁴ Markusen, J., et al, 1995, p 12

¹⁵ Markusen, J., et al, 1995, p 100

¹⁶ Markusen, J., et al, 1995, p 13

differences in the sample data, and how the firms are classified in Japan and the U.S data. When correcting for this the result is an estimate of approximately 6 %. This number is though still 2-3 times lower than the levels experienced in other industrialized countries.

¹⁷.

This low level of foreign activity in Japan can be partly explained by historical policies to limit foreign investments, also easy access to capital resulting from one of the world's highest national savings rate has reduced the need for foreign capital. Lately, as these factors have become more normalized compared to other OECD countries, it is other more intrinsic factors such as cultural barriers, language barriers and mental distance that are likely to have kept the inflow of investment at a relatively low, although quickly increasing, level. These barriers will be further explained in the next section.

¹⁷ Weinstein, D., p. 3

Culture and institutions

One suggested reason to this low level of foreign FDI in Japan is the resistance and difficulties connected to mergers & acquisitions. This form of FDI is very common among American companies and it has often been argued that the Keiretsu structure and cross ownership of shares are large impediments to FDI in Japan. Some even argue that the Keiretsu makes takeovers impossible and that this is part of the reason for them to exist.¹⁸

Cultural differences might also be reducing the level of FDI in Japan. According to the widely accepted Uppsala-model of company internationalization, presented by Johanson and Vahlne in 1977, companies make small incremental investments in a market as their knowledge of the market increases. They also state that companies make their investments in a limited number of markets and focus on neighboring or psychologically close markets as the knowledge of these markets is greater and easier to gather.¹⁹

In the case of Japan this might have a reducing effect on FDI as Japan has no cultural close ties to any other country and constitutes its own “cultural block” unlike any other country.²⁰

Besides merging or acquiring an existing company, another way to enter a new market is Greenfield investment. Greenfield investment is when you start up a business in a country without acquiring already existing strategic assets. This kind of investments is seen as more beneficial for the host country. This is due to the fact that foreign acquisitions lead to a loss of jobs and a concentration of market power, while Greenfield investments lead to additional investments, more jobs and increased competition.²¹

Traditionally Greenfield investments dominated, especially in Asia. However the proportion of FDI through M & A (Mergers and Acquisitions) is increasing and the trend is particularly strong in the developed countries in Asia of which Japan is the most prominent.

A study made by the Swedish Research Institute of Industrial Economics found the following pattern of foreign direct investments made by Swedish companies.²²

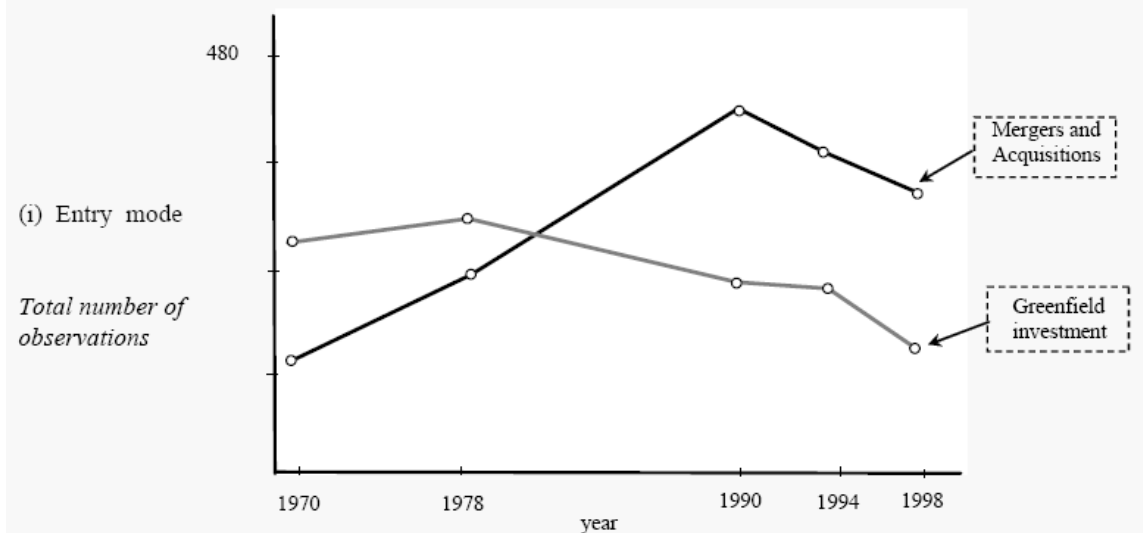
¹⁸ Weinstein, D., p. 7

¹⁹ Forsgren, M., et al, p 5

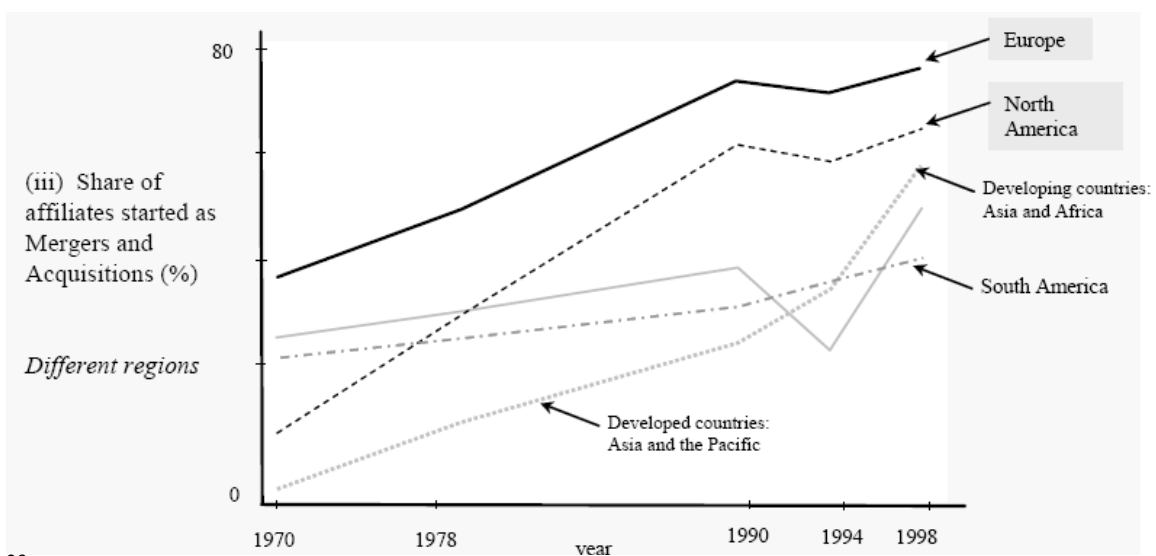
²⁰ Berkema, H., 1996, p 157

²¹ Bertrand, O., et al, 2007, p 5

²² Bertrand, O., et al, 2007, p 7



And divided by region



23

The graph “Developed countries: Asia and the Pacific” is most interesting for the purpose of this essay. We can observe a steady increase in M&A from an exceptionally low starting point in the 1970s. In connection with the financial crisis of the 1990s in Japan we can see a break of the trend and a rapid increase in M&A activity.

Further strengthening the trend of M&A as entry mode is the implementation of the 2005 Corporate Law which allows cross-border M&A using shares as payment. This change is part of an initiative started by Prime Minister Koizumi in 2001, and then reiterated in 2007 by Prime Minister Abe, to double the stock of FDI in Japan in five years.²⁴

²³ Bertrand, O., et al, 2007, p 10

²⁴ http://www.jetro.go.jp/en/invest/newsroom/newsletter/pdf/ij_16_3.pdf

Ownership, location and internationalization advantages

One popular theory concerning the determinants of individual companies' FDI is the OLI framework presented by Dunning in 1977 and 1981. The OLI framework focuses on three factors *ownership advantage*, *location advantage* and *internalization advantage*.

Ownership advantage is any sort of property right that separates the company from its competitors. This could for example be assets such as patents, products et cetera or as intangible as a reputation for quality or a trademark.

Location advantage means that the particular location has a benefit of some kind, making it more profitable to produce the product or service there instead of in the home country. This could be trade barriers, factor prices or transportation costs.

Internalization advantage is the fact that there has to be some kind of factor that makes it more profitable to invest there instead of licensing or selling the asset to a local firm. This implies that the firm has to have some kind of way to exploit the product or process more efficiently within the company than externally.²⁵

The location advantages are extra interesting as they are the part that can explain why companies choose to invest in Japan. As mentioned before, Japan is often referred to in literature when discussing trade barriers, factor prices and is located far from the other major industrialized markets.

One interesting point in the sample of companies I have chosen is that manufacturing in Japan is very limited and sold goods are almost entirely imported. This indicates that market access is seen as the primary priority.

The earlier mentioned Uppsala model commands a strong position in internationalization theory. This model, in brief, focuses on where and how firms internationalize. The emphasis is on small incremental steps, both in term of the structure of operations and in which markets the companies choose to penetrate.

Based on this an alternative interpretation is that the perceived psychic distance to Japan has decreased but that the companies often still are in an early phase of their investment and that production will be added later.

²⁵ Markusen, J., et al, 1995, p 396

Japan Before

This section contains a description of a number of areas in economic theory that historically has been associated with Japan and Japanese trade policy.

Trade theory

There are a number of different models explaining trade. They all focus on some specific factor that could possibly explain why countries engage in trade. The basic theories of trade are founded on differences between countries in: levels of endowments such as capital and labor, in taste, technology in production, increasing returns to scale or more structural issues such as imperfect competition or government policies.

The basic theories are; the comparative advantage model (technology) developed by the British economist David Ricardo during the 19th century and the Heckscher-Ohlin (H-O) model, (factor endowments). The H-O model is a further development from the Ricardian model allowing for two goods and two production factors and was developed during the beginning of the 20th century and has been the predominant trade theory during the 20th century.²⁶

These general theories of trade work well for giving an intuitive understanding of general flows of trade. However for the research and question at hand in this thesis, the more modern theories are more applicable. These theories are better suited for looking at less general questions and are more focused on specific issues driving trade and are thereby better suited to explain individual companies' behavior.

The theories that will be examined are the following:

- Government Policies as Determinants of Trade
- Imperfect Competition as a determinant of Trade
- Increasing Returns to Scale
- Tastes, Per Capita Income, and Technological Change as Determinants of Trade

All these theories have strong connections to issues raised related to Japanese trade and trade policy after World War II. The following section will explain the theories and show how they are connected to the Japanese case.

²⁶ Markusen, J. et al, 1995, p

Government Policies as Determinants of Trade

Taxes and subsidies are well known government policies that affect trade. Other examples of policies that influence trade flows are regulations and environmental policies. These factors may not have an as strong direct effect on trade as factor endowments or technology however collectively they have a profound impact on trade.

One important factor to remember in trade theory is that increased exports do not equal improved welfare. To generate exports by subsidies leads in fact in many cases to welfare reductions. By creating distortions through introducing taxes, subsidies or regulations, you shift the economy from the welfare maximizing competitive equilibrium. All taxes and regulations are not distorting. In some cases there are external distortions such as pollution or other secondary effects that means that consumers and producers are not facing the true costs when making decisions. The key fact is that all trade induced by distortions is welfare reducing.²⁷

When discussing anticompetitive practices and an active policy regarding government interventions in trade, Japan is one of the most frequently mentioned countries. Especially the United States of America-Japan bilateral trade relationship, one of the world's most consequential, is tumultuous and creating an apparently infinite stream of disputes.²⁸

One explanation for the many trade disputes is that the trade flow is “enormously lopsided” in favor of Japan. The United States have incurred constant and increasing trade deficits ever since 1965. This itself is however not an explanation to the friction and disputes as the United States also experience similar trade imbalances towards other countries such as Canada and Germany. In these cases the difference is that Germany and Canada, contrary to Japan, are perceived to have open and unregulated markets where companies compete on similar terms. As a result of this “experienced” fairness, the number of disputes is minor.

Accusations and complaints of Japan's unfair trade practices and “renegade” behavior are well documented. United States trade officials have complained that despite more than 30 bilateral trade agreements since 1980, Japan remains less open to imports than any other industrialized country. Other reports published by the office of the U.S. Trade Representative have singled out Japan as the most offensive perpetrator of barriers to competition.²⁹

Is it then so clear that Japan is using unfair trade practices to benefit at the expense of other countries? The famous economist, MIT professor and advisor to President Bush, Paul Krugman has written:

²⁷ Markusen, J., et al, 1995, p 142

²⁸ Kotabe, M., et al, p XIV

²⁹ Kotabe, M., et al, p 5

“Does Japan take unfair advantage of our open market while closing its own? Many, perhaps most, Americans believe this, though few economists would agree... Even a brief review of the evidence explodes most of the myths that continue to circulate in the U.S. discussion. While there is room to criticize Japan, the idea that that Japan is pursuing beggar-my-neighbor policies on a grand scale is essentially preposterous.”

This statement can be seen in connection to the theory previously presented, where government induced trade is seen as welfare reducing.

Studies presented in David Flath’s book, “The Japanese Economy”, also come to the conclusion that the Japanese industrial policy *“made virtually no measurable contribution to Japan’s postwar growth”*. In their studies they surveyed government transfers, tariff rates, corporate tax rates, and government loans to companies.³⁰

One peculiarity with the Japanese case is the strong presence of nontariff barriers to trade, possibly more than in any other country. These barriers can partly be seen as actions to limit access to the Japanese market for foreign companies. The American Chamber of Commerce in Japan published a report in 1993 listing “recurrent issues which represent major obstacles to fair access to the Japanese market”. In this report they listed actions taken by the Japanese government to preserve advantages for domestic companies such as:

- Incompatibility of many Japanese standards, certification procedures, and testing practices with internationally recognized criteria, and reluctance to accept internationally approved measures as applicable in Japan..
- Excessive regulation
- Lack of transparency in formation, dissemination, and enforcement of rules and regulations.
- Inadequate protection of intellectual property rights.
- Unnecessary obfuscation created by problems of classification or definition of terms
- Tariffs and quotas
- Government procurement tactics

A study done by James Harrigan in 1993 based on trade flow data from 1983 showed that Japan had the highest coverage level of nontariff barriers in the studied sample of ten developed nations. In the case of Japan 40% of all imports were covered by at least one

³⁰ Flath, D., p 211

nontariff barrier, as defined by the United Nations Commission on Trade and Development. This was substantially higher than the other countries, where France had the second highest coverage with 27%.

Other similar studies have come to varying levels of imports covered by nontariff barriers. But regardless of level, the ratio between coverage in Japan and the U.S. is always approximately twice as high in Japan.³¹

These nontariff barriers are also strongly connected to practices causing imperfect competition which will be presented later.

Imperfect Competition as a determinant of Trade

The presence of market power in one or more industries provides for a different type of distortion. In free market economies the most typical reason is scale economies in production. The high costs associated with producing small outputs of a product may limit the number of firms that can survive in a market and thereby give the remaining few firms market power.

The profit maximization rule for an economy is when producers increase production until marginal cost (MC) equals marginal return (MR). The stronger market power a company has the further apart MC and MR will be.

When a closed market is opened for trade, the number of firms competing in that market will increase and as a result the perceived price elasticity will decrease. Decreased price elasticity makes firms compete more aggressively and increase production, this reduces firm level profits but increase overall welfare.³²

The case with imperfect competition is also highly relevant when analyzing Japan. There are a number of anticompetitive practices that are particularly associated with the Japanese economy.

Typical examples of institutions, more or less designed to limit competition are:

- **The anti-monopoly laws of Japan**

Japan's anti-monopoly laws are a legacy from the U.S. occupation of Japan, following World War II, and the Fair Trade Commission of Japan monitors the laws. These are analogous to their American counterparts, but have in reality turned out to be very different. In Japan there are many businesses that are designated as in recession or in need of rationalization and therefore are exempted from the anti-monopoly laws. Also the investigative power of the Fair Trade Commission is much more restricted than the American counterpart. Furthermore the penalties for breaking the regulations are trivial in Japan.

³¹ Kotabe, M., et al, p 34

³² Markusen, J., et al, 1995, p 168

- **Long-term trading ties**
 Japanese firms rely on long term trading relations where the reputation of the partner and the long relationship is the guarantee of performance. One explanation of this is the legal culture. In America, and most other places, the threat of a lawsuit, in the case of a breach of contract, can make suppliers live up to their obligations. In Japan the likelihood of a lawsuit is small and they are often not resolved quickly. A problem is also that even in the event of damages being paid, they most often do not cover the incurred cost.
- **Regulations**
 In regulated industries the government controls variables such as entry, price, quality and quantity. Areas with strong government regulations include utilities, transports, banking, finance and telecommunications.
 The regulation in Japan is handled by the national government and different ministries have some discretion regarding the manner in which way they implement regulations. Regulations have been especially strict in the utilities, transport and finance sectors which have been strongly regulated or dominated by government enterprises.³³
- **Marketing System**
 Manufacturers, wholesalers and retailers in Japan frequently enter contractual agreement with one another regarding minimum resale prices, customer restrictions, exclusive dealing stipulations and similar clauses. Such vertical restraints are against the anti- monopoly laws in Japan but they are still pervasive.³⁴ One example of this is that consumer goods tend to cost exactly the same regardless of which store you enter or which town you go to. The product often also has the sales price printed directly on the box making intra-brand competition impossible.
- **Keiretsu**
 What is connected to the long-term trading ties is the issue of Keiretsu. Keiretsu are the Japanese business groups connected by cross ownership. These groups are seen partly as a result of outside pressure to liberalize the Japanese market. By creating these business groups it has become harder for foreign companies to enter the Japanese market especially by FDI through hostile takeovers.³⁵

Increasing Returns to Scale

It has long been recognized that economies of scale provides possibilities for gains from trade. By increasing the total market, the firms can produce larger batches of the same product which in the case of economies of scale gives lower average costs. However in many cases tariffs and barriers to trade have made firms still produce small quantities of a wide range of products. Recent research has indicated that even countries as large as the

³³ Flath, D., p. 250

³⁴ Flath, D., p. 295

³⁵ Weinstein, D., p. 1

U.S. have not completely exhausted the possible benefits of scale economy in certain industries.

Examples of industries that greatly benefit from expanded markets are cars and electronics. These industries have large fixed costs in the form of development of their products and costly production facilities. This gives great advantage to actors with access to larger markets than their competitors have.

Another benefit that was already pointed out by Adam Smith is the possibilities for specialization. For example we grow potatoes in Sweden but we do not grow bananas which we instead import. This makes our farming more efficient.³⁶

Increased diversity can also be achieved by focusing production on one variety of a product and supplying it to the whole expanded market. This is called intra-industry trade. The car market is an often used example. In Sweden we make Volvo and SAAB cars, in Japan they make Toyota, Nissan, Honda, Subaru et cetera. These are all cars, but they are not perfect substitutes to each other, as they all have slightly different characteristics. This means that some Swedes prefer Japanese cars and some Japanese prefer Swedish cars. As a result of this Sweden exports cars to Japan and vice versa.³⁷

Japan has for a long period been accused of blocking imports from other countries and closing its market for foreign firms. Particularly the Americans have vigorously complained that American firms and products are denied access to the Japanese market. Polls made in the U.S. in 1990 showed that two thirds of the Americans believed that Japan unfairly restricts sales of U.S. goods in Japan.

Also South Korea and Taiwan have argued that Japanese nontariff barriers are restricting their access to Japan and the EU have complained that Japanese firms are using high profits earned in the protected Japanese market to subsidize lower export prices in Europe.³⁸

This strategy is only logical if there are increasing returns to scale. In the case of no scale economies this strategy would simply constitute a direct subsidy of European consumers at the expense of the Japanese consumers.

From Swedish companies perspective the Japanese market offers great possibilities of scale. It is the world's second largest consumer market and provides a large concentrated homogenous consumer group. To leave this market uncontested is a strategy that historically has proven to be costly for many companies.

³⁶ Markusen, J., et al, 1995, p 174

³⁷ Markusen, J., et al, 1995, p 186

³⁸ Kotabe, M., et al, p 6

Tastes, Per Capita Income and Technological Change as Determinants of Trade.

This can be seen as a more psychological method of explaining trade but is also based on more practical issues such as patents and development of new products. One example is the product cycle. New products are developed in some advanced countries and then exported from there. When these products have reached a certain maturity the production is moved to less advanced countries with lower production costs. In the final stage the technology is widespread and the patents have expired. At this point all production shifts to low cost countries that now even export back to the country where the product originally was developed. This causes flows of trade of products in different stages of the cycle.³⁹

Swedish companies can expect to face similar costs in Japan as in Sweden. The Japanese average level of income and development is roughly equal to the Swedish levels and both countries are in the technological forefront. This would indicate that development levels are poor determinants of FDI and trade from developed countries such as Sweden to Japan.

Japan is an exception from the normal pattern of intra-industry trade between developed countries of similar GDP per capita. Japan has a significantly lower ratio of intra-industry trade compared to all other similar countries. One explanation for this could be that Japan is separated from most of the other developed countries geographically which increases transportation cost. Others claim, as earlier mentioned, that it is import barriers that cause the low import of goods to Japan.⁴⁰

The low intra-industry trade is also the outcome associated with investment liberalization and high trade costs in the General Equilibrium model of Trade and Affiliate Activity. This model was developed by Markusen and Venables in 1998 and 2000.⁴¹

Another explanation that is more likely in the case of Japan is the differences in taste. Differences in taste enforce the factors presented under increasing returns to scale and the difference in taste is a particularly important issue in trade when it comes to Japan.

In Japan a common explanation is that Japanese taste is different from the standard western taste. Also it is often said that Japanese consumers value quality higher than other consumers and that as a result of this Japanese products have superior quality compared to products from other countries.

The success of some big foreign companies such as IBM, Coca Cola etc. are shown as examples that good products can succeed in Japan. On the other hand comments such as the following show the mainstream view in Japan.

³⁹ Markusen, J., et al, 1995, p 209

⁴⁰ Markusen, J., et al, 1995, p 228

⁴¹ Markusen, J., et al, 2001, p 8

“We have to go out of our way to find American products worth buying” Takuma Yamamoto, chairman of Fujitsu

“High quality in the United States is not necessarily high quality in Japan,” Jiro Kawake, chairman of the Japan Paper Association.⁴²

“We have special lines in the factories with extra high quality requirements that only produce for the Japanese market” Bengt Jönsson, Country Manager Japan, Swedish Match⁴³

This requirement of adjusting products to Japanese “standards” makes exporting to Japan more complicated and also reduces the benefits of IRS for foreign firms, giving local Japanese firms an advantage in the Japanese market.

One interesting parallel is also drawn by Mr. Hasegawa of EIJS (European Institute of Japanese Studies) who during the interview mentions the story of the shoe company that sent two persons to Africa to investigate if there was any market for their shoes there. One reported back that there was no point of opening business there since people did not wear shoes. The other person reported huge market possibilities as there were no competitors and nobody was wearing shoes.⁴⁴ This can illustrate how different your view of the world can be due to just a small change in attitude.

The sales of soft mattresses, which will be presented later, in the interview with Mr. Kullberg is a good example of how these “preferences” and “tastes” might change quickly when presented with new alternatives and options.

Theories on firm behavior in internationalization

Starting in the 1980s researchers began to note that firm specific factors seemed to have a stronger influence on FDI flows than aggregate capital levels. For example studies showed that factors such as knowledge based and other intangible assets were better predictors of FDI than capital.⁴⁵

On the single firm level, the strategy choice is where to place the operations of the firm to achieve an optimal structure. The first models presented focused on access to markets in the case of trade friction (horizontal FDI) or access to cheaper production (vertical FDI). More recently, focus have shifted to more complex models with for example FDI in a particular country as an export platform or integrated production systems in many countries.⁴⁶

⁴² Kotabe, M., et al, p 7

⁴³ Jönsson, B., interview

⁴⁴ Hasegawa, A., interview

⁴⁵ Maskus, K., et al, 2001, p 1

⁴⁶ Blonigen, B., 2005, p 21

One concept that is common in literature is the liabilities of foreignness. This concept concerns the special difficulties that face subsidiaries of multinational enterprises (MNE) operating in foreign cultures. The main problem is to understand and adapt to the host country's environment and country specific nature of institutional norms. Even if the locally used and accepted organizational practices are identified, it is difficult to implement them successfully in a foreign entity.⁴⁷

When pursuing a multinational strategy each company has to determine how much they will adapt to local variations in their different markets. All firms want to standardize their products as much as possible to achieve benefits from scale. This has to be balanced against the desire for local adaptation in national markets. A strategy of minimal adaptation is called a global strategy while a strategy of local adaptation is called a multi-domestic approach.⁴⁸

Connecting to the research on institutional differences and the resulting difficulties is the work by P. Rosenzweig and J. Sing on dual pressure. They say that MNEs are "catalysts for reconceptualizing organization-environment relations" because they are working simultaneously in multiple nations. Doing so their local subsidiaries face dual pressures, both pressure regarding internal consistency within the company but also external pressure to comply with local standards.⁴⁹

Particularly regarding Japan the research show that Japanese companies were different from Swedish when it came to structure and control systems (Horvath, McMillan, Azumi and Hickson). When comparing with American firms Lincoln et al found that Japanese companies were embedded in a tighter institutional environment with stronger company centralization. Yoshino found in a study that Japanese firms are more uncertainty avoidant and therefore place higher requirements on subsidiary similarity and relied more heavily on expatriates, to increase the possible level of control, than the researched American firms did.⁵⁰

⁴⁷ Yadong, L., 2002, p 218

⁴⁸ Yadong, L., 2002, p 219

⁴⁹ Rozenzweig, P., et al, 1991, p 340

⁵⁰ Rozenzweig, P., et al, 1991, p 345

Japan today

This section describes Japan today and how the market has changed.

Internationalization

The mutual influence of the MNEs is one of the driving factors of the internationalization of the world that has taken place. Lately this has also started picking up pace in Japan as the country has opened up more and more.

*“On one hand, the MNE is an agent of change, linking diverse national environments; on the other hand, the MNE must respond to national environments whose accepted patterns of behavior continually shift as they influence each other”.*⁵¹

Swedish companies are active in this process and IKEA's expansion has been mentioned as globalization, the Scandinavian style. Today you can buy Swedish style furniture and food in most of the larger countries in the world. Similarly H&M and other companies are spreading Scandinavian style management, corporate culture and many other factors to more and more countries.

Japan is one of the countries where this type of interaction historically has not had a strong impact. The country was first closed almost completely for foreigners until the 1870s and the Meiji revolution and even after that the country has had few large foreign companies operating successfully in the home market. This is however changing and the number of successful large foreign firms is now rapidly increasing. Examples such as Nissan, now controlled by Renault of France, are providing good examples of how new styles of management and change in structure can improve operations. Going the opposite direction one can mention many other Japanese management and operation concepts that have become popular in other countries, such as just in time delivery or Toyota style manufacturing and many more.

The areas where one can expect the strongest inflow of FDI from foreign countries are areas where Japanese companies lack comparative advantages or even have disadvantages for sale in Japan, and areas with comparative advantages in Japan for export industries.

The history of low levels of FDI in Japan has been going on since before World War II. This has been a result of strong government restriction on investments in the country until the 1970s and after the deregulation during the 1980s there has been private barriers instead, however the inflow of capital and technology has still been important in the restructuring of the Japanese economy. These barriers, both private and public, are lately being removed in an attempt to make the Japanese market more competitive and attractive to investments. As a result, many small inefficient Japanese firms that have been too dependent on the Japanese market are being eliminated. This is rapidly changing

⁵¹ Rozenzweig, P., et al, 1991, p 355

the sectors in Japan that are open to competition, a process known as “*risutora*” which can be translated to restructuring.⁵²

This restructuring and opening up to more market liberalization has also taken place within the financial sector, which previously was one of the most regulated. In 1996 a coalition government announced what was to be called the “Tokyo Big Bang”. This deregulation plan aimed at a wide reform of the industry structure and a new institutional framework. The idea was to increase competition by allowing all firms with a financial concession to compete in all segments and allow complete freedom of capital movement. The idea was to adopt the “free market principle” to increase efficiency. The scheme was implemented starting from 1998 and progressing until 2001.⁵³

The restructuring is not only an internal process in Japan, it has also made it possible for foreign companies to enter less well performing Japanese companies as complete or part owners. Well known examples of this are the purchases of stakes in Nissan by Renault, Mazda by Ford and Mitsubishi by Mercedes-Benz. In 1998 alone, the number of foreign acquisition of companies in Japan doubled and the value six folded, and it continues to grow.⁵⁴

The regulatory and structural reforms taking place in Japan since 1992 are laying the foundation for economic growth and should, if implemented comprehensively, assist the country’s return to sustainable growth. The deregulation taking place from 1992-2002 has already in 2002 resulted in ¥14.3 trillion in economic benefits for the Japanese consumers. The deregulation is also estimated to increase Japan’s long term growth by 0.2 percentage points by 2010.⁵⁵

The reforms will restructure the economy and “*let business do what it does best*” as former Prime Minister Koizumi has said.

For Swedish companies this openness and deregulation presents a great opportunity to increase their presence on the Japanese market. Many of the interviewed persons have mentioned that Japan today is not more difficult to enter than other countries and present huge possibilities for successful entrants.

*“The ongoing reform process has led to foreign companies to a lesser degree than before suffer from discrimination compared to their Japanese counterparties. The problems faced by companies in Japan today, may they be bureaucratically or competition law related, are the same for all companies, foreign or Japanese.” Swedish embassy in Tokyo 2001*⁵⁶

⁵² Blomström, M., et al, 2000, p 20

⁵³ Nakamura, R., 2002, p 15

⁵⁴ Blomström, M., et al, 2001, p 257

⁵⁵ http://www.ustr.gov/assets/Document_Library/Reports_Publications/2004/2004_National_Trade_Estimate/2004_NTE_Report/asset_upload_file860_4776.pdf

⁵⁶ Aambs Charlotta Ozaki Macías, Swedish Embassy in Tokyo

Cases

To further give a more practical view on how companies actually perceive doing business in Japan, and not only report on theory about doing business there, I have studied a number of companies active in Japan.

The companies

Researching Swedish companies in Japan I have chosen to divide the sample into three categories. This division is based upon the companies experience in the Japanese market, primarily on the length of their operations there, but also on how these have turned out.

The categories are the following:

- Companies that are just entering Japan
- Companies that are returning to Japan
- Companies that have been in Japan for a long period

These categories are not perfect and some companies do not fit perfectly in a single one of them, however they do provide some structure and in general they convey a good understanding of in which phase of their Japanese experience they are.

Companies that are just entering Japan

Swedish Match

Swedish match is not a perfect example of a company just entering Japan since it actually has been active on the Japanese market for a very long time. The first business in Japan was conducted during the 1920s and was related to manufacturing of matches.

Since 1960 Swedish Match operated its Japanese business without any local subsidiary, however in 2003 they opened up a local subsidiary again. Today the turnover in Japan is approximately 130 million SEK. All locally sold products are imported from production facilities in other markets.

The move to open a local office is quite exceptional for Swedish Match that otherwise is selling its products on most of the markets in the world through representatives without any own local presence. This recent opening of a new office selling new products more than 40 years after closing their old office motivates the placement of Swedish Match in this category.

History and internationalization of Swedish Match

This section gives a short description of how Swedish Match was created and how it later became a global company.

The construction of the present Swedish Match is rather new, however it is created by the merger of activities with a long history. The two main components of the modern company are the former two companies Svenska Tändsticks AB and Svenska Tobaksmonopolet.

Svenska Tändsticks AB

As a result of severe competition in the decades immediately prior to the First World War, the Swedish match industry was restructured, and 20 independent factories were replaced by two large companies, one of which was Aktiebolaget Förenade Tändsticksfabriker (Förenade), headed by Ivar Kreuger.

1917-1932 | The Kreuger era - Global expansion

The Kreuger era was initiated by Ivar Kreuger's initiative for a merger with Jönköpings & Vulcan Tändsticksfabriksaktiebolag, resulting in the formation of Svenska Tändsticks Aktiebolaget (STAB). Then STAB expanded internationally at a quick pace. By 1930, STAB was the sole or dominant owner of match companies in 33 countries and had minority interests and agreements to restrict competition in a number of other markets. In all, STAB controlled 60% of the world production. Domination of the global match industry was an explicit objective for Kreuger and the most common method of expanding the market share was the acquisition of competitors.

Until 1927 expansion was primarily in the form of acquisitions, but this proved to be insufficient to eliminate competition. Instead Ivar Kreuger tried to establish match monopolies in various countries, usually in combination with offers of loans to the governments of states with shaky economies.

Following Kreuger's death in March 1932, doubts were expressed about the group's financial position and some companies in the group could not be saved and were declared bankrupt. After this a period of divesting assets began and STAB's share of match trade in the world decreased from 40 % in 1930 to about 20 % in 1938.

This marked the end of the first era of expansion, an era that had been focused on internationalization and the aim to reach global dominance by acquisitions of competitors.

1960s & 1970s | Acquisitions and new areas of operations

The second era of expansion began during the 1960s and continued until the purchase of the company, now renamed to its present name Swedish Match, by Stora in 1988.

More than 50 companies were acquired between 1968 and 1976 and subsequently match products only accounted for 20% of sales. In addition to building products such as doors, windows, flooring and board, the company had operations in the packaging and match-

making machinery industries, and was also involved in manufacturing garbage trucks, waste combustion facilities, tobacco-making machinery, and equipment for bakeries, fish processing and bowling halls et cetera.

1981 – 1985 Acquisitions of international lighter manufacturers gave Swedish Match further presence on the international markets in a new segment.

1987 Acquisition of Pegulan, a German flooring manufacturer, and Wilkinson Sword, a UK razor blade manufacturer proved to be the last acquisitions of the second era, as Swedish Match itself was acquired the following year by Stora, another company within the same Wallenberg owner sphere.⁵⁷

Parallel to this history was the development of the second leg of the present Swedish Match, the Swedish Tobacco Monopoly.

Svenska Tobaksmonopolet

1915 The Swedish Tobacco Monopoly (Tobaksmonopolet) was introduced to give the government the funds it needed to build up the country's military defense and to serve as a foundation for the new national pension system.

The funds for the defense and the pension system were to come from tobacco, and the most effective way of doing this appeared to be through the creation of a monopoly. Consequently, all of Sweden's tobacco factories were nationalised in 1915.

During the 1960s the Monopoly was abolished and the name changed to Svenska Tobaks Akitiebolaget (STA)

The internationalization of STA began after the Swedish monopoly was revoked and started with export of pipe tobacco and was soon followed by acquisitions of other tobacco companies, primarily in Europe.

A further step in the globalization of the tobacco business was taken in 1985 when STA acquired The Pinkerton Tobacco Company, the leading manufacturer of chewing tobacco, in the United States.

The parent company of STA was acquired by Volvo and the operations were in 1992 merged with the operations of Swedish Match, by then also a subsidiary of the same company. This created the “new Swedish Match”.⁵⁸

In 1996 the company was spun off from Volvo and listed on the Stockholm stock exchange and a new wave of company purchases began in countries such as, Finland,

⁵⁷ <http://www.swedishmatch.com/Eng/SvenskaTandsticksAB.asp>

⁵⁸ <http://www.swedishmatch.com/Eng/SvenskaTobaksAB.asp>

Singapore, India, Bulgaria, Turkey, Australia, Hong Kong, New Zealand, Slovenia, Poland and several companies in The United States and South Africa.⁵⁹

These waves of acquisitions have been the typical mean of internationalization in Swedish Match's history and this pattern is common in businesses with strong brands and brand affiliation. The brand loyalty of customers in these businesses make Greenfield investments very time consuming and costly, on the other hand the customer loyalty makes brand acquisitions less risky for the acquirer, as the customers propensity to switch supplier is low.

In the case of Swedish Match in Japan there would, according to the country manager, have been an interest in acquiring a local brand, if such a brand had been available. However today there are no local companies directly active in Swedish Match's segment of the market and therefore the Greenfield investment was the only available option for entering the market.

The choice to enter the Japanese market in spite of this can be seen as a demonstrator of how important this market is perceived to be. Swedish Match today has operations in 26 countries of which Japan is one of the few where there has not been any sort of acquisition.

⁵⁹ <http://www.swedishmatch.com/Eng/SwedishMatchAB.asp>

Bengt Jönsson – Country Manager Japan at Swedish Match

Why Japan?

The potential of the Japanese market is immense. Today the market for cigarettes is well penetrated with 45% of Japanese men smoking. A contrast to this is the market segment of non smoking tobacco products, where Swedish Match operates, which is completely lacking tradition and local competitors.

This large market in combination with a willingness among Japanese customers to pay for high quality products makes the Japanese market interesting.

“Everybody wants to dig gold in China, but still the GDP of China is just equal to that of the Tokyo area”.

Why now?

Today there is no tradition to consume Swedish Match type of products on the Japanese market. This is good in the way that there are no competitors in the area but it also creates problems as the consumption of non smoking tobacco products is something that has to be taught to the consumers. At the moment Swedish Match is perceiving a rapid change in consumer behavior, partly triggered by the changing laws on where you are allowed to smoke, which is making this a good time to introduce new products.

“At this moment everything is changing in Japan” ... “it is not a gold rush but step by step and with a little patience and the right attitude...”.

Is Japan a protected market?

Today three firms dominate the Japanese tobacco market and form a powerful oligopoly. One firm, Japan Tobacco, in particular is controlling the market. The competition is similar to the level in Sweden and profitability is good. Swedish Match has not experienced that it is especially difficult to obtain licenses or similar governmental approvals. There are low import barriers and as long as you are well prepared it is not more difficult than in other countries. The existing barriers are for example the requirements for warning labels on tobacco products but this is also present in many other countries, for example Sweden.

To start operations was for example in Swedish Match case easier than they had expected, once they understood how the system works. As long as you speak Japanese it is not harder than anywhere else.

“When you have contacts with authorities do not send “gaijin” (Japanese for foreigners) instead send local personnel”.

One thing that might hinder entrance is the Japanese custom of long term business relations. To start a new company or establish a new product can often take a very long time. In many cases this can take several years, as the Japanese are very brand and supplier loyal.

Difficulties in Japan

Also making the Japanese market more difficult to enter is the Japanese taste. There has been a change towards adapting more to western tastes but still the Japanese customers, in general, require a lot of changes in products, to more suit their preferences.

Demand for quality is for example higher in Japan than most other countries. Swedish Match has solved this problem by arranging special product lines that only produce extra high quality products for the Japanese market.

The major difference between business in Sweden and business in Japan is the time aspect. To make a deal in Japan can often take several years during which you have to be patient and develop the relation with your business partner. Also the personal relation part is much more important in Japan.

To adjust to the cultural differences between Japan and the western world takes time. This is something that most expatriates do not have as they are often there for a limited period. Many are not fully functional until after at least three years, then it is often time to return to the home country.

Companies that are returning to Japan

IKEA – Globalization Scandinavian-style.

IKEA is very interesting as a study object as they have entered the Japanese market before, failed or not found it ready, but are now entering again. This is a very strong indicator of change, either in the recipient market or in the company itself.

History and internationalization of IKEA

From Älmhult to Tokyo



The first period of IKEA's existence was focused on development of the IKEA concept. This development began in 1943 with the founding of IKEA in Älmhult, Sweden. The now to most people so familiar IKEA characteristics developed over the following years. The first catalog, now the world's most published printed item with 175 million yearly printed copies, was published in 1951.

The maybe most distinct and revolutionizing feature of IKEA's business model, the "flatpicks" were introduced in 1956. This is one of the core reasons of IKEA's success as it has allowed IKEA to consistently offer lower prices than regular furniture stores.

In 1958 IKEA further developed its concept and opened the first IKEA store, this store is situated in the small Swedish town of Älmhult. This marked the start of an expansion that today has made IKEA the largest furniture retailer in the world.

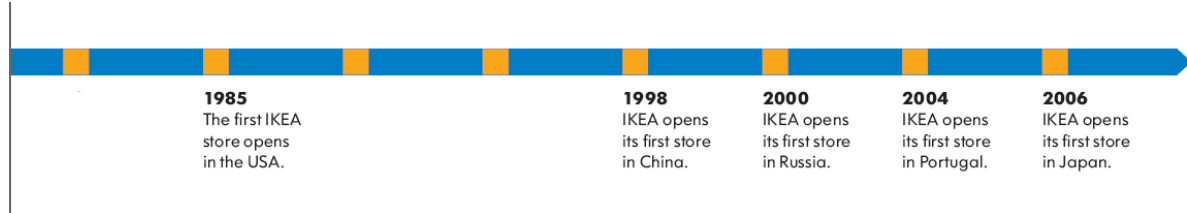
In 1965 one further step towards the IKEA of today is taken as the store in Kungenskurva, Stockholm, Sweden, introduces the self service system that now is so typical for IKEA stores. This system reduces the need of staff by letting the customer personally collect his purchases in the storage facility.

The internationalization of IKEA begins with the opening of a store in Norway in 1963. This is the first step for IKEA outside of the Swedish home market and was soon to be followed by many more.

The second level of internationalization begins in 1973 as IKEA opens the first store outside of Scandinavia. This store is situated in Switzerland, now the resident country of Ingvar Kamprad, founder of IKEA.

After this followed a period of further expansion within Europe as IKEA entered more countries and added more stores in already penetrated markets.

The third level of internationalization



In 1985 IKEA opens up its first store in the USA, this signals the beginning of the expansion outside of Europe. From here on the pace of internationalization increases dramatically and new markets are rapidly penetrated. These also include more diverse markets such as Russia, China and Japan.

This pattern of internationalization corresponds clearly to the Uppsala model. First IKEA built and developed its concept in its home market Sweden. Later they expanded in their close vicinity by opening a store in culturally similar Norway and the further expansion in Scandinavia. This was followed by opening a store in Switzerland a country with relatively low perceived cultural difference and also now home of the founder of the company.

The markets perceived to be more distant have been saved for later stages of expansion, allowing IKEA to first accumulate a vast experience of entering foreign markets which can be used to avoid many mistakes that are common for less internationally experienced companies.

The founder Ingvar Kamprad has himself said “No-one has made as many mistakes as I have”. This has however allowed IKEA to learn and further develop the way they do business, and this also includes how they enter markets.⁶⁰

Japan is an ideal example of this learning. IKEA first entered Japan in 1974, which understandably is not mentioned on their web page. This attempt was not very successful and IKEA withdrew after a short period saying that the Japanese customer was not yet ready for flat pack living and especially not convinced of assembling their own furniture.

These problems of adjustment were however later again experienced in the USA and there they forced IKEA to finally reconsider and allow some local adaptation. However anywhere in the world the assortment shows normally only a maximum of two percent adjusted products, as each adjustment increases the total cost for IKEA. The company still emphasizes its Swedish origin and culture and refuses to become “American”, “Japanese” or in other words more locally adapted.

⁶⁰ <http://www.ikea-group.ikea.com/corporate/PDF/FF2006english.pdf>

Adjustment is though not only a cost, some of the adjusted products have later proved to be big sellers back in Europe, such as for example soft couches the USA style. This time, thirty years later, IKEA is hopeful that it can seduce the Japanese, who have suffered more than a decade of recession, although now the economy is again picking up pace, and are now less convinced that they must pay high prices to obtain high-quality goods.

IKEA has opened two shops just outside Tokyo in late 2005, with plans to open eight to twelve more, employing 6000-8000 employees in the future.⁶¹

This large scale entry will demand large efforts of interaction with their Japanese customers, employees, local authorities, government and all other involved parties.

Tommy Kullberg – Former CEO of IKEA K.K, now involved in H&M’s launch in Japan.

Tommy Kullberg was first posted to Asia in 1988 to manage region-wide operations for Swedish trading firm Gadelius KK. His assignments before that included Africa, the US, and Europe. Since moving to Tokyo ... Kullberg has worked on hundreds of projects around the region, the majority of which are in Japan. In 2002, he was recruited by the IKEA Group to spearhead its entry into Japan. Kullberg also served as chairman of the Swedish Chamber of Commerce in Japan, and was formerly a commercial counselor for the Swedish Embassy in Tokyo.⁶²

Why Japan?

Japan is a very important market. It is the world’s second largest market for consumer goods. Historically Swedish companies have made rather weak efforts to penetrate this market but this will have to change and the importance of the Japanese market for Swedish firms has to increase. One problem facing Swedish companies is that they cannot imagine the true size of the market. Many firms have sales of approximately one billion SEK in Japan and feel successful when actually they rather should be selling for 10 billion SEK.

“Japan is such an important market that you cannot overlook it.”

Why now?

There is now a change in how people in Japan look on interior design and home decoration. Traditionally the average spending in IKEA’s segments’ of the market has just been equal to one quarter of the spending in Europe. This is now changing as the interest in furniture is changing from purely functional to a more design and fashion oriented interest. This change coincides well with the reestablishment of the IKEA brand in Japan and the opening of the new IKEA stores in Tokyo. Also benefiting IKEA’s entry, as a large retail store operator, is the reduced land prices that Japan is experiencing at the moment.

⁶¹ http://www.brandchannel.com/features_effect.asp?pf_id=256#more

⁶² http://www.itvjapan.com/market_acc.asp?Id=3

In Japan IKEA cannot identify any close competitors in their segment of price and quality and rather have to compare themselves with Disneyland and other all day family activities.

Lately Kullberg has experienced a shift in the view of the Japanese market in both media and the corporate establishment towards a more positive outlook. In this shift some key actors are driving the change, but it also has influence on a more general level through increased positive coverage in media.

One reason mentioned by Kullberg about why IKEA has been more successful this time than during their previous effort, is the increased awareness about Japanese culture in Sweden and the fact that they hired a number of Swedish students speaking Japanese with knowledge of the culture. This helped reduce the cultural differences, increase the understanding and helped spreading the IKEA values to the local employees.

Is Japan a protected market?

Today there are few remaining formal trade barriers. Some products are difficult to import, for example food and medicine and the licenses to start business within these sectors take very long time to acquire.

Relevant in the IKEA case is particularly the Large Scale Retail Law that requires approval by the authorities of each new IKEA store. This is according to Kullberg a reasonable restriction as a large store requires substantial investment in facilities and infrastructure. The experience in the case of IKEA is that foreign companies are not discriminated against and in fact they got their permit faster than some local companies.

Today the greatest trade barrier is the Japanese housewife. She demands high quality from all products and is spoiled with the level of service Japanese companies offer.

“The Japanese customers can choose between Japanese and American products in almost all areas. Then the choice is often simple.”

Difficulties in Japan

To do business in Japan you have to do thorough market research and find out what the customer really wants and what they are willing to pay for. IKEA has chosen not to adjust its design of the furniture but to be very selective of which products to offer. Before the launch employees of IKEA visited over 200 homes and measured apartments to see which products would fit in a standard home.

In some cases doing market research is not even enough as there are always some answers that are seen as more “politically correct” to give. For example in Japan many customers answered that of course they could not consider driving their furniture home by themselves. This kind of answers is common in the entire world and is something that you have to be wary of.

In some cases you have to challenge the present standard. IKEA for example chose to focus on soft mattresses in Japan as they do in Europe, although tradition in Japan said that they should sell hard mattresses. This choice has proven very successful and shows that some change can be achieved.

When doing business in Japan then there are no quick short cuts. It takes committed and knowledgeable personnel in place for a long time, often as long as five to seven years to start up. To be successful you have to have a long term investment perspective, the same way as the Japanese companies do.

What you should not do is adapt to certain local inefficiencies. Kullberg says that he has never worked so much as when working in Japan and gotten so little done. Not even as Japanese expatriates return, has the efficiency increased more than on the surface. This will probably change as young people in Japan will not accept the same kind of working hours and conditions as the previous generations have done.

“One common mistake when entering the Japanese market is to spread the effort on all of Japan. A better strategy would be to focus resources on a smaller area; perhaps just a few blocks of Tokyo would be big enough for a Swedish company.”

Companies that have been in Japan for a very long time

Gadelius

Gadelius has been in Japan for longer than any other Swedish company and thereby also experienced more change than any other. Today they have been there for such a long time that it is questionable if they still are Swedish more than by name. For example, of 170 employees just six are Swedish and of them four are located at the office in Sweden.

This phenomenon of foreign companies turning Japanese is widely observed and most entrants only send a few expatriates to the local office. This could be a result of local pressure to adapt and adjust and also of the difficulties for foreign employees to work effectively in the very different Japanese business culture.

On the other hand the difficulties experienced by foreign firms may, as occasionally in the case of Gadelius for example, force them to invent new strategies and approaches to deal with these problems. An example of such a strategy is that Gadelius was among the first companies in Japan to approach students before they graduated. This was necessary as already graduated students were reluctant to choose foreign firms as employers.⁶³ This has later become the standard approach applied by almost all Japanese firms.

Gadelius History

Gadelius was the first Swedish company to enter the Japanese market and establish a local office. The first office was opened in Yokohama in 1907 by company founder Knut Gadelius. Who later received a number of medals for his work in Japan from among others the Japanese emperor. Gadelius has moved on during its 100 years of operating in Japan and now has seven local offices (Tokyo, Sapporo, Nagoya, Fukuoka, Ota, Sendai and Kobe).

Gadelius' business started with importing Swedish products using technology that was not available at that time in Japan. This strategy developed as a response to Knut Gadelius identifying a possibility to contribute to the industrialization of Japan and utilizing the business opportunity this gave.

Gadelius internationalized rapidly which is rather understandable being an international trading house. After being founded in 1890 in Gothenburg, with the aim of developing the Swedish trade with the Far East, Gadelius soon began exporting Swedish goods to Asia. During the initial travels of Knut Gadelius, the founder of the company, he realized that a company with good knowledge of language, customs, culture and needs of the Asian countries would have tremendous opportunities.⁶⁴

⁶³ Bass, B., et al, 1990 p 107

⁶⁴ Bass, B., et al, 1990, p 16

The first local office opened in Asia was the Singapore office opened in 1904. This was later followed by the Yokohama office in 1907 and the first imported product to Japan was AGA lighthouse equipment. After this a number of well known Swedish products were exported to Japan through agency or licensing contracts.

In 1958 Gadelius opened offices in nearby South Korea and Taiwan but the second stage of internationalization did not really begin until 1982. This year, offices were opened in Denmark and Norway and soon after followed offices in Brunei, Thailand, Germany, the Philippines, Indonesia, and the US.⁶⁵

From starting as an importer Gadelius developed into a local producing partner that also manufactured the products locally under license from the principal. After a number of acquisitions and sales of the company, the business is today again focused on the trading of products in machinery, industrial supplies and medicine, rather than production. This development can also be seen in the number of employees that has been reduced from a peak at 1500 to today only 170 employees.

Nobuyoshi Ota - Director Human Resources at Gadelius

Why Japan

When coming to Japan, Knut Gadelius found a country that more or less completely lacked industrial structure or any visible traces of industrialization. However he found a large population of well educated, honest, clean and hardworking individuals. This convinced him that Japan had a brilliant future and influenced him to move there permanently and establish the Yokohama office.

For Swedish companies in particular it is the small home market that forces them to become international early. When looking for a larger market Japan offers the world's second largest, although fiercely competitive with an abundance of local companies. But if you have a unique product and good quality you should sell it in all markets and Japanese customers will buy if your offer is better than the rivaling Japanese firms.

⁶⁵ Bass, B., et al, 1990, p 1

Difficulties in Japan

As one of the first western companies to open in Japan, Gadelius faced tremendous difficulties in the first years, mostly regarding business differences, cultural differences and bureaucracy. Today the differences are much smaller on all accounts but still there are a number of points that differ dramatically.

Two of the most important are:

- **Mentality.** In Japan it is always the customer that comes first and you have to please the customer at almost any cost. One example is the Swedish industrial vacation that often means that many Swedish companies more or less close down operation for two months. In Japan vacation is never an acceptable reason for not being available for the customer.
- **Service/Quality.** The Japanese customers are very specific in their demands and require perfect quality. For example when printing, even flaws so small that you cannot see them without a magnifier are deemed unacceptable. These requirements are often difficult for Western companies to imagine and understand and often the only way to grasp them is to actually visit the customer in person at their facility.

What also cause problems is that it is almost mandatory to have local personnel in Japan to handle service. If you lack this resource then your customers are likely to be less understanding and less likely to buy. As a result of this Gadelius handles service in Japan for its principals.

An issue when doing business in Japan or with Japanese companies abroad is the problem of communicating. This issue is however not only limited to the lack of English speaking personnel in Japanese companies. It is in fact even a difficulty for Japanese speaking people as even communication within companies or between Japanese companies is troublesome. This is however likely even worse between individuals that lack a natural understanding of the culture.

The differences between Japanese and foreign companies are today decreasing rapidly and has been doing so for a number of years, this makes contact and interaction easier. But it also removes many business opportunities as the differences between the products of different countries also diminishes. This might in fact reduce trade and Gadelius has had to drop many products as Japanese companies have started making similar products of same or better price and quality.

Is Japan a protected market?

As an importer of foreign goods, Gadelius has 100 years of experience of protectionism in Japan. In history there has been very many different trade barriers used to protect the initial industries that sprung up after the opening of the Japanese border that took place after the Meiji revolution. What can be said is that today almost all of these official barriers have been removed and as an importer/exporter Gadelius perceives import to Japan to be as easy as to export to the European Union.

What makes it difficult are not the barriers raised by the government, as it was before, instead it is the cultural distance that cause many companies difficulties. It is more difficult when entering Japan without any previous network and with a different mindset than your customers and competitors then when you are familiar with the market. One such network that has been reduced or even removed during the last years is the keiretsu system. As main banks, traditionally the organizers of the keiretsu, are merging the new groups involve companies from several former keiretsu. These new groups becomes larger, but less tight and this has opened up for collaboration and partnerships that earlier were seen as impossible.

One thing that has to be kept in mind is that successful companies usually do not brag about their success while companies that fail often complain loudly about difficulties perceived to make success impossible. This is likely to distort the image presented in media and press and might give an impression of more severe difficulties than what actually exist.

Possibilities in Japan

Japan is rapidly changing into a more westernized culture. This change is mostly driven by the younger generations of which many have studied abroad. Another influencing factor is the spreading of internet that has given better knowledge about the rest of the world. The change in attitude can be viewed in the traditional view on managers and their age in different industries. When Gadelius sends a representative to a “traditional” industry, such as power generation, then they have to send a senior official of approximately the same age as the client. However when they are dealing with “newer” industries such as e-trade, then sending a younger official is acceptable to the client. As these “new” industries increase in importance the more western style of business might take over.

The opposite trend can also be observed as western companies study and learn from Japanese manufacturing companies. However a majority of Japanese workers are still suspicious of parts of western style capitalism and perhaps particularly hostile takeovers. A common view is that “companies should be built by hard labor, not quick purchases”

The interviews

To further explore what may influence the increase in the number of Swedish companies focusing on the Japanese market I conducted a number of interviews with people in possession of knowledge concerning Swedish companies in Japan. This knowledge comes from either working for Swedish companies in Japan today or in the past or from working with issues regarding Swedish companies in Japan.

Johan Rugfeldt – Secretary of Trade at the Swedish Trade Council in Tokyo

The Swedish trade council has today 400 employees at 50 offices in the world. Of these 21 are employed at the office in Tokyo. They work with advising Swedish companies already in Japan or planning on entering the market. The complexity of this issue can be illustrated by the fact that the office in England, which services an equally large trading partner, only employs four persons. Of the advised companies approximately 50 % are new to the market and the other half has some prior experience in Japan.

During the last two years, and particularly the last six months, the trade council has experienced an increasing interest in the Japanese market from Swedish companies, and today there are over 120 Swedish subsidiaries established in Japan and more than 1500 companies have sales there.

The general feeling among Swedish companies that are getting in contact with the trade council can be summarized as “we want to do something in Japan; we are not feeling like we are getting a part of the pie”. The most common question asked by interested companies is “is there a market for our product and how can we enter the market?”

Why Japan?

The Japanese market is today the world’s second largest market with consumption equal to the total of the rest of Asia. It is also the world’s largest homogenous market and concentrated in all aspects. The area between Tokyo and Osaka has a larger purchasing power than all of China and nowhere in the world is there any similar concentration of economic power. The GDP of this area is now also growing again.

One further interesting aspect of the Japanese market is the customers. The Japanese consumer is the most demanding in the whole world. The quality requirement in Japan are higher than anywhere else and if you can make it in Japan as a seller, then the rest of the world is available too.

Why now?

The Japanese market is perceived to be increasing in importance in the future. This is taking place after the correction that followed the inflated bubble economy. Japan today is more open, market oriented and shareholder value focused. This has led to an increased competition and openness to foreign companies, which is increasing the trade with the rest of the world. This increased openness and reduction of many “traditional Japanese” characteristics can be seen as a reaction to the economic problems that have plagued Japan and made the weaknesses of the former system visible. Japan is today Sweden’s 16th largest trading partner, a position that is expected to be strengthened in the future.

One door opener for Swedish companies expanding to foreign markets has historically been IKEA. When IKEA opens up a new market and succeeds, this signals that this market is mature enough, or in other ways available, for foreign companies to enter. One example of a company that earlier has used this tactic of following IKEA is H&M. These two leading Swedish companies are now opening up in Japan. First IKEA opened its first store in 2006 and later H&M is opening in 2008.

Is Japan a protected market?

Historically during the 1960s and 1970s Japan used or tried to use the international trade to attain benefits. Now however Japan has become a normal economy with more or less the same rules and policies as any other western country.

Almost all government regulations have been removed and today the barriers remaining are more of a private character. What still can be seen is that for certain licensed products it may take a longer period to get approval in Japan than in most other countries. This is though not particular for foreign companies. Japanese companies face the same procedures and problems getting approval. This is most noticeable in markets such as medicine, health and food.

Difficulties in Japan

The government regulations are decreasing and have in most cases been removed, but one barrier still remains, the Japanese taste. To sell a product in Japan you will most likely have to adapt it to the Japanese customers’ preferences. The Japanese standards are becoming more adapted to international standards, but the Japanese customers still prefers products adapted to Japanese style and unique Japanese requirements. However, if you perform and build relationships, then the customers are very brand and supplier loyal. They are also willing to pay for the adaptation and also for quality.

“The Americans are world champions in complaining, but if you are selling cars with the steering wheel on the wrong side, it is no wonder nobody is buying.”

Göran Edman – Board member at Gadelius, earlier at the Trade Council, Invest in Sweden Agency and companies in Japan and author of Frankly speaking Mr. Foreigner.

Göran Edman has a long experience as official at Swedish authorities in Japan, as manager of companies operating in Japan such as ASG, Skandia and Gadelius and is now sharing his experiences as an author and lecturer about doing business in Japan and the inevitable cultural clashes that follow.

Why Japan?

The profitability of the Japanese markets is high. The Japanese customers know what high quality is and they are willing to pay for it. When you buy for example a Toyota then you know what you get. If you chose something else then you get what you pay for. This in combination with the Japanese custom of long relations and strong loyalty to products and suppliers makes the Japanese customer an ideal customer.

This makes the Japanese market a great market to be successful in. The problem is building a position. The above mentioned characteristics have created a market structure where it is very hard to enter as a new firm if the customers are already customers of some other brand. Although this difficulty for newcomers to enter markets, the already existing companies keep up a strong competition in most areas of the economy.

Often the structure of the market is in the form of oligopolies and in some branches there are restrictions that limit the competition.

Why now?

Japan is now changing into a more westernized economy with more focus on efficiency. The crisis during the 1990s helped to facilitate this change as it made the problem obvious. Today for example it is acceptable with inefficient companies going bankrupted, something which before very rarely was allowed.

One example of this is the abandonment of the “Convoy system”. This was a system where strong banks bailed out weak banks that risked going bankrupted, in return for favors from the powerful ministry of finance (MOF).

Difficulties in Japan

The main problem with doing business in Japan is the time. You have to invest a lot of time building relations and waiting for acceptance. Given this you have to have a long term perspective when entering Japan.

Most Swedish companies start small scale and establish an agent in Japan to then gradually build up the scale of their activities in Japan.

Analysis

Trade theory

The trade theory background section mostly focused on how literature depict Japan as a classical case off government interventions trying to improve a country's terms of trade and to benefit from international trade at others expense. This view has primarily been presented in American trade literature and is in most cases based on historical empirical and statistical data.

This is also, according to the EU trade council and the European Business Community (EBC) representing a struggle between the old and new industries in Japan. Older industries are fighting to keep the protectionism and benefits that they were used to enjoy before while newer more innovative industries are rationalizing and improving efficiency, often by shifting production to cheaper places.⁶⁶ These new industries are becoming stronger and, as said by Mr. Ota during the interview, they are taking over an increasing share of the Japanese economy. This shift in power is making further reforms and liberalization possible as the old structures and interest groups, such as for example Keiretsu, are broken up.

During the interviews with representatives of Swedish businesses in Japan today, they have all stated that they do not perceive Japan today as more closed or difficult to enter than other markets. None of them have listed political reforms or barriers to trade as a major problem. However several of them recognize that Japan was "protectionist" before or at least was perceived to be so.

What still can be seen is that some needed approvals for certain businesses takes longer time to get than in most other countries, but it is the same for local companies. IKEA for example got the approval quicker than a local rival.

The general consent seems to be that during the rapid growth of Japan's economy in the 1960s and 1970s it is possible that Japan tried to take advantage of certain policies to keep foreign companies away from the Japanese market. Today however Japan seems to be an open economy, though some scholars argue that the attempts actually even were counterproductive, and the earlier so celebrated Ministry of Finance bureaucrats are now not as hailed anymore.

This can also be due to the shift in paradigm that has taken place, where both former Prime Minister Koizumi and his follower, the present Prime Minister Abe, are strong supporters of reforms, privatizations and liberalization.

The unusually strong support Koizumi gained in the 2005 elections also show that there is a strong public support for the new more liberal line of LDP (Liberal Democratic

⁶⁶ <http://www.exportnytt.swedishtrade.se/docfile/5866.doc>

Party) politicians against the more traditional conservative LDP politicians.⁶⁷ This support would suggest a continuation of the reforms also in the future, although the recent LDP loss of majority in the upper house might indicate some change of direction.

“Today the greatest trade barrier is the Japanese housewife. She demands high quality from all products and is spoiled with the level of service Japanese companies offers.”
Tommy Kullberg, Former CEO IKEA K.K.

Also frequently mentioned is the need for adaptation to the demand of the local Japanese customer. What is high quality in America may not be high quality in Japan as Jiro Kawake, chairman of the Japan Paper Association, says. The Japanese customer wants products adjusted for Japanese taste, primarily higher quality, and this is something you have to consider. The Americans complain that Japanese customers are not buying their cars, but if the steering wheel is on the wrong side it is no wonder they are difficult to sell.

These factors can together with the strong brand loyalty experienced in Japan explain most of the odd peculiarities regarding Japanese trade that are mentioned in the trade theory section. For example the low intra industry trade can be seen as a result of brand loyal customers wanting Toyota cars or Honda cars with right hand drive instead of switching to now available competitors.

What can be seen also may be a lag in the data, as most research and analysis is made on historical statistics and a slowly changing general opinion about something that Japan did in the past.

Today Japan is adjusting more than before to international standards. This is taking place in many fields such as for example telecommunications where the 3G networks are both according to European and American standards while the 2G networks were a special Japanese standard. This has helped foreign entry by companies such as for example Vodafone.

Other induced barriers have also been reduced. Japan has now one of the highest patent application rates in the world, suggesting strong intellectual property right legislation and the number of regulated industries is quickly decreasing with for example rice becoming available for both import and export.

⁶⁷ <http://www.iie.com/publications/papers/posen0905.pdf>

Foreign direct investments

When it comes to the question of FDI then the pattern is quite obvious. Historically there has been a strong culture of barriers to foreign entry in many sectors. This has manifested itself in both formal barriers such as regulations regarding anti-monopoly laws and other areas and informal barriers such as Keiretsu, long-term trading ties and the marketing system.

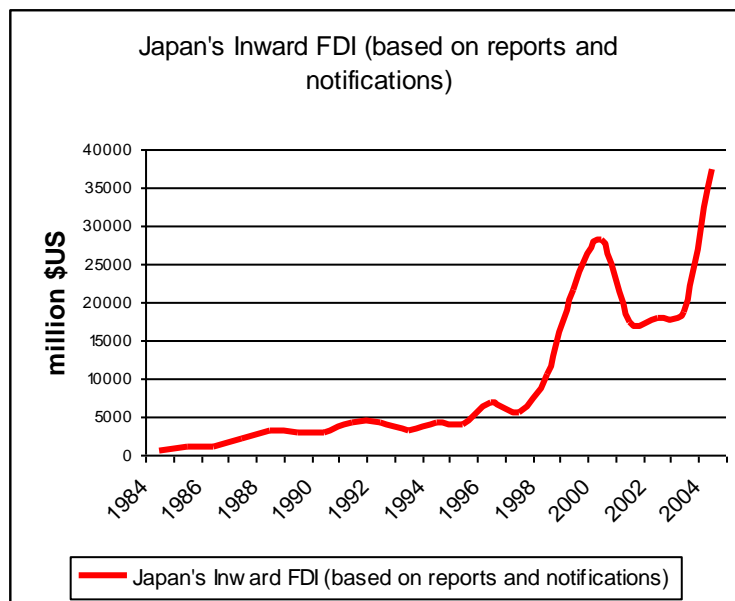
What has happened recently is a change in the view on market efficiency and a realization of the need for restructuring. This has involved large scale deregulations and the voluntary removal of much of the keiretsu system. One area that has not changed is the retail system of decided prices. In spite of some court rulings against fixed sales prices the practice is still strong in Japan. For many products you know the price, and it is the same in every store, vending machine or kiosk. In general though, change is progressing rapidly.

Japan is now changing into a more westernized economy with more focus on efficiency. The crisis during the 1990s helped to facilitate this change as it made the problem obvious. Today for example it is acceptable with inefficient companies going bankrupted, something which before very rarely was allowed. Göran Edman

This change and a realization of need for “*risutora*”, as Blomström et al writes, has opened up the market for foreign entry. This can clearly be seen in the level of FDI that has multiplied since the beginning of the 1990s. Today, all the interviewed agree that, Japan is an open market and that it is changing rapidly.

“At this moment everything is changing in Japan ... it is not a gold rush but step by step and with a little patience and the right attitude...”
Bengt Jönsson

“During the last two years and particularly during the last six months, the trade council has experienced an increasing interest.” Johan Rugfeldt



This change is not only experienced by Swedish firms. Looking at the development of FDI in Japan and reading the literature gives a unanimous picture of a shift in policy and conditions. This perception of increased openness can be seen in the entry of many high

profile foreign firms since the 1990s. Examples of such entries are Wal-Mart, Carrefour, Costco, Tesco, Hartford Life, IKEA, Zara, H&M, GAP, Citigroup, Morgan Stanley, Charles Schwab Corp, Merrill Lynch & Co and many more.

These companies have all felt the sentiment described by U.S Ambassador to APEC in his “Now is a Good Time to Invest in Japan”.

Japan is now an attractive destination for foreign companies wishing to take advantage of its highly skilled labor force and reach its affluent population of potential customers. Michael W. Michalak, U.S Ambassador to APEC

Japan has taken significant steps to open up its economy, recognizing that FDI brings with it innovation and management improvement et cetera. This increased openness and the efforts to attract FDI has so far worked to help increase the stock of FDI from ¥6.6 trillion in 2001 to over ¥11 trillion in 2007.⁶⁸

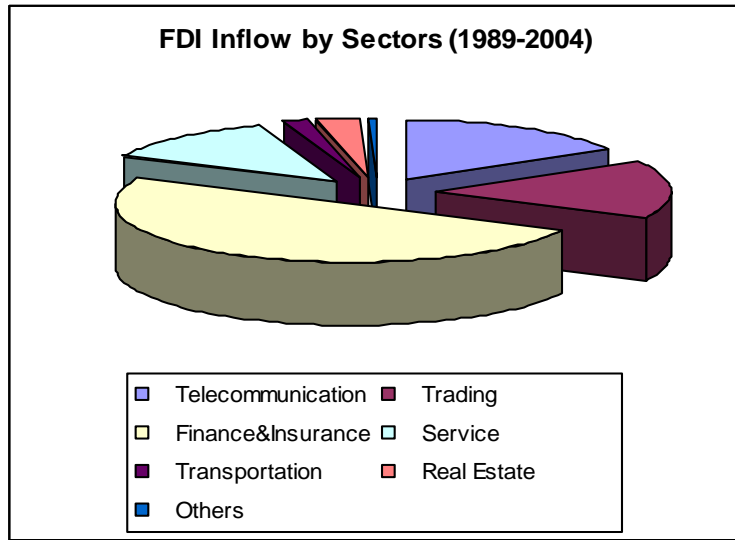
One surprising aspect is that none of the interviewed managers mention Keiretsu, a rather predominant issue in much of the theory and often mentioned when discussing Japan and entering the Japanese market. This could be a sign off what some researchers have called the end of Keiretsu and for many businesses this structure does not seem to be a noteworthy obstacle anymore.

There is however still some remnants left of it and in some cases you still hear about companies considering their ties to other keiretsu companies when deciding their strategy or business activities. This practice is also occasionally criticized by people working in these companies as they see it as hindering their company’s performance. While talking to companies in Japan I have experienced them giving advice on how to work around the problem, even if that involves going to their competitors.

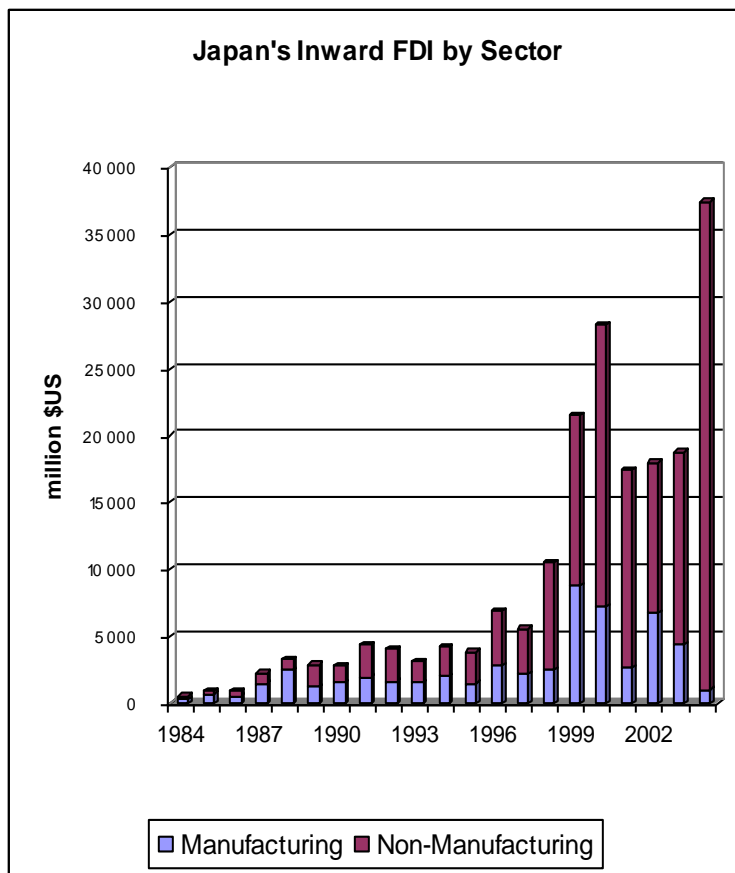
⁶⁸ http://www.jetro.go.jp/en/invest/newsroom/newsletter/pdf/ij_16_3.pdf

Firm behavior and business culture

The FDI taking place in Japan by Swedish companies is mostly aimed at benefiting from the large potential of the domestic market. Not so much attention is focused on using special endowments available in abundance in Japan. The one endowment available in Japan that one can say interest foreign companies is the world's most fastidious and qualified customers.



This focus on the Japanese consumer may also be why almost all FDI recently taking place in Japan is in the non manufacturing sector. The Japanese service sector has for a long period been underdeveloped and underperforming compared to the Japanese manufacturing sector. This indicates that foreign companies investing in Japan think that taking advantage of specific business opportunities in underdeveloped sectors is more important than excess factor endowments as H-O theory would suggest.



Regarding culture the liability of being foreign might be greater in Japan than in any other industrialized country. Japan has, according to the famous culture researcher Geert Hofstede, no culturally similar neighbors and no close ties to any cultural group of countries anywhere in the world. In the case of Sweden–Japan the difference is particularly significant as Sweden and Japan on most of

the researched cultural topics, rank at opposite ends of the scale. For example the Japanese society is the world's most masculine dominated and Sweden the most feminine. Sweden is among the most uncertainty accepting cultures and Japan is among the most uncertainty avoidant and it continues like this.⁶⁹

This difference and the need for understanding of this is one of the key factors for a successful entry of the Japanese market. In the interview the need for personnel on place in Japan, market studies, the need for experienced people knowledgeable of Japan etc are points that are reoccurring continuously.

“To adjust to the cultural differences between Japan and the western world takes time. This is something that most expatriates do not have as they are often there for a limited period. Many are not fully functional until after at least 3 years, then it is often time to return to the home country.” Bengt Jönsson – Country Manager Swedish Match

This also creates problems of internal consistency within the firms as the local subsidiaries have to adapt to the Japanese business culture. This makes them either very different from their mother company or from local business. This has been a problem for many of the firms entering and a number of them have chosen to withdraw from the Japanese market after facing structural and cultural issues. This seems to have been an issue particularly for American firms and most notably among investment banks where an exceptionally high number of withdrawals have been experienced, often after internal control issues.

The increased openness and the resulting increased interest in the West for the Japanese market, and also culture, is decreasing the differences between culture, and business in particular. This has lead to more Japanese workers being employed by foreign companies and to more influences by foreign firms. In September 2004 foreign-affiliated firms employed more than one million workers in Japan. This figure however is lower than for other developed countries, for example the U.S. and Germany has relatively more than twice as many workers employed by foreign firms.⁷⁰

In Sweden the interest for Japanese culture, language and economy is also strongly increasing. This is for example manifested in an increasing number of courses and educations at universities focused on the topic, such as for example the one at SSE. This increased interest should create a better understanding and reduce the perceived distance, something that for example IKEA relied heavily on during their launch. In the context of the Uppsala model this decreased perception of distance can explain the increased Swedish activity in Japan.

⁶⁹ Hofstede, G., 1991, p 84, p 113

⁷⁰ <http://www.jetro.go.jp/en/news/releases/20050413221-news>

One good example of how foreign firms are bringing new ideas and exert pressure on the local society to adapt also is when Tommy Kullberg, for example, mentions during the interview that he was summoned to the Prime Minister and the government to discuss how IKEA offered the same possibilities to female as well as to male employees. This was in contrast to the traditional way of looking on female employees in Japanese companies.

The changes are not only perceived in regulatory changes and changes in business structure, it is also seen in attitude and especially among the young in Japan.

“...young people in Japan will not accept the same kind of working hours and conditions as the previous generations” Tommy Kullberg

These changing values and more openness to western culture, ideas and values are creating new business opportunities for foreign companies in Japan. However it is still important to remember that what works in the “rest of the world” does not always work in Japan. All the interviewees have stressed the importance of understanding and adapting to of the peculiarities of the Japanese market and customer.

If you are selling cars with the steering wheel on the wrong side of the car, then it is no wonder the Japanese customers are not buying it. The same goes for more intrinsic values such as taste, design et cetera. This has been observed and utilized by all successful foreign companies in Japan.

This understanding of difference is probably the key factor of success. It has been mentioned by most people interviewed and is repeated over and over in literature, though interestingly not as frequent in American literature. Spending time in Japan also gives a good insight in the necessity of adjustment, or as a friend of mine said “in Japan, even if it looks exactly the same as in Europe, there is always something about it that is different”. This is a direct hit on the global market theory presented by Levitt who suggested that companies should only sell global products with no adjustment.

Conclusions

Bridging the gap

Japan today is much more open to outside influences and the Japanese market is in most cases not more protected than other markets. This is a radical change from how it was 30 years ago when Japan was famous for both formal and informal barriers of trade and restrictions and regulations were common in more or less every single industry. Now the key questions are not anymore how to manage a difficult regulatory system or how to get in to the Japanese market, avoiding the structural difficulties often associated with Keiretsu and other Japanese “specialties”. This has instead been replaced with the question of how to appeal to the Japanese taste.

Now after waves of regulatory change and increased openness, focus has shifted to the cultural differences and the need to understand the local business environment. To be successful in Japan you need to identify the taste and desires of the Japanese customer, you have to offer them service and variety of choice of equal quality as the local competitors and you have to convince some of the world’s most loyal customers to change supplier to a brand they do not recognize. This often requires a superb offer that cannot be matched by local Japanese competitors.

Many authors are talking about global markets and praising companies that manage to build global brands and introduce their “standardized” products to satisfied customers in every corner of the world. Typical companies mentioned are Coca Cola or McDonalds that are sold from Champs Elysées to Ginza and from Moscow to Bahrein. What authors such as Theodore Levitt in his article “The Globalization of markets”⁷¹ tend to miss is that these products are actually not the same in Ginza and Moscow. If you buy a McDonalds hamburger in Japan then, and only there, you can have it with teriyaki sauce and if you buy a can of Coca Cola in Tokyo it will taste sweeter than if you buy a can in Europe. If you go to Starbucks in Tokyo they serve you Macha frappuccino based on traditional Japanese green tea. If this adjustment is not enough to please the local taste, then you can also buy Coca Cola tea and many other even more locally adapted drinks in stores. These are examples of how important it is to know your local customers and realize what you have to do to be competitive. This has not changed over time and was also observed by Knut Gadelius already on his travels to Asia more than 100 years ago.

However, when you do your homework well, prepare thoroughly and offer good products, then the Japanese market is like any other market and given the vast size, and the earlier seclusion, it offers huge possibilities.

⁷¹ Levitt, T., 1983

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<http://www.oecd.org/dataoecd/21/38/38179491.pdf> (Investment Newsletter Feb. 2007)

Statistics Bureau, Director-General for Policy Planning (Statistical Standards) & Statistical Research and Training Institute

<http://www.stat.go.jp/data/nenkan/zuhyou/y0201b00.xls>

Swedish Embassy in Tokyo

<http://www.exportnytt.swedishtrade.se/docfile/5866.doc>

<http://www.regeringen.se/content/1/c6/06/03/01/a4849126.pdf>

Swedish Match

<http://www.swedishmatch.com/Eng/SvenskaTobaksAB.asp>

<http://www.swedishmatch.com/Eng/SwedishMatchAB.asp>

Swedish Trade Council

<http://www.swedishtrade.se/japan/?objectID=564>

http://dbl.swedishtrade.se/list_subsiary.aspx?countryid=32

Wikipedia

<http://en.wikipedia.org/wiki/Asia>

Institute for International Economics

<http://www.iie.com/publications/papers/posen0905.pdf>

Interviews

Bengt Jönsson - Country Manager Japan at Swedish Match,

Johan Rugfeldt - Secretary of Trade at the Swedish Trade Council in Tokyo,

Göran Edman - Board member at Gadelius, earlier at the Trade Council, Invest in Sweden Agency, companies in Japan and author of Frankly speaking Mr. Foreigner,

Tommy Kullberg - Former CEO of Ikea K.K, now involved in H&M's launch in Japan and other projects,

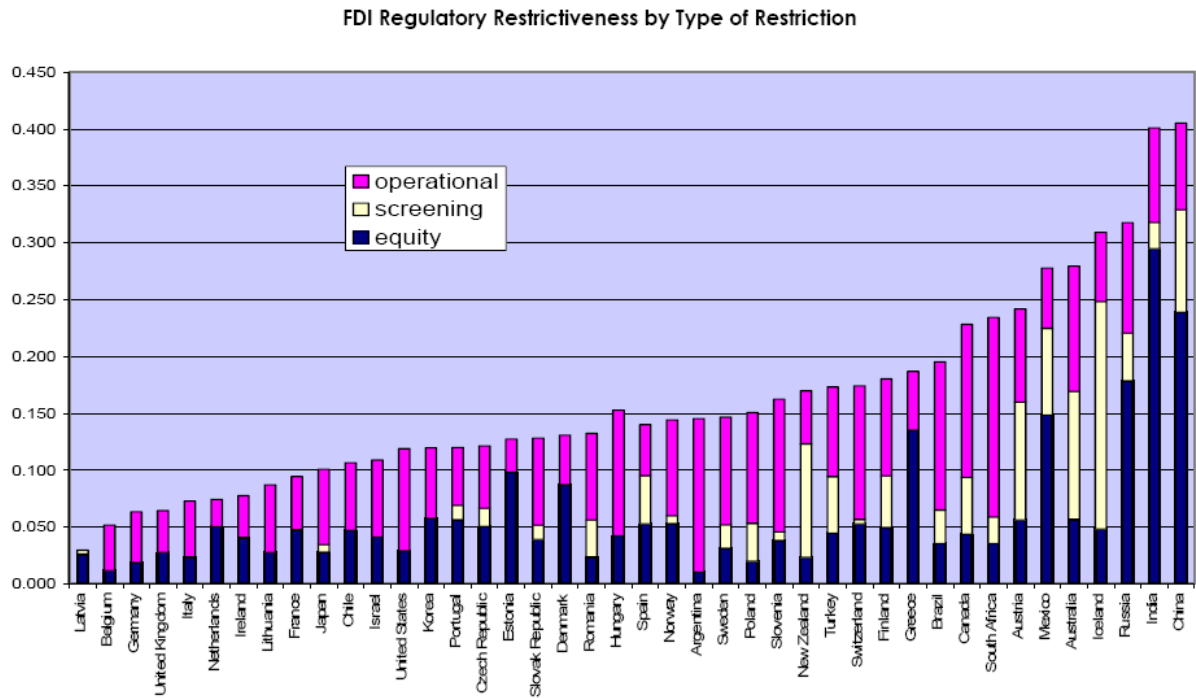
Nobuyoshi Ota - Director Human Resources at Gadelius,

Atsushi Hasegawa - Head of European Institute of Japanese Studies Tokyo Office

Appendix

FDI regulatory restrictions

Japan has removed most of the barriers facing FDI and is today one of the most open countries to invest in. More open than for example Sweden.⁷²



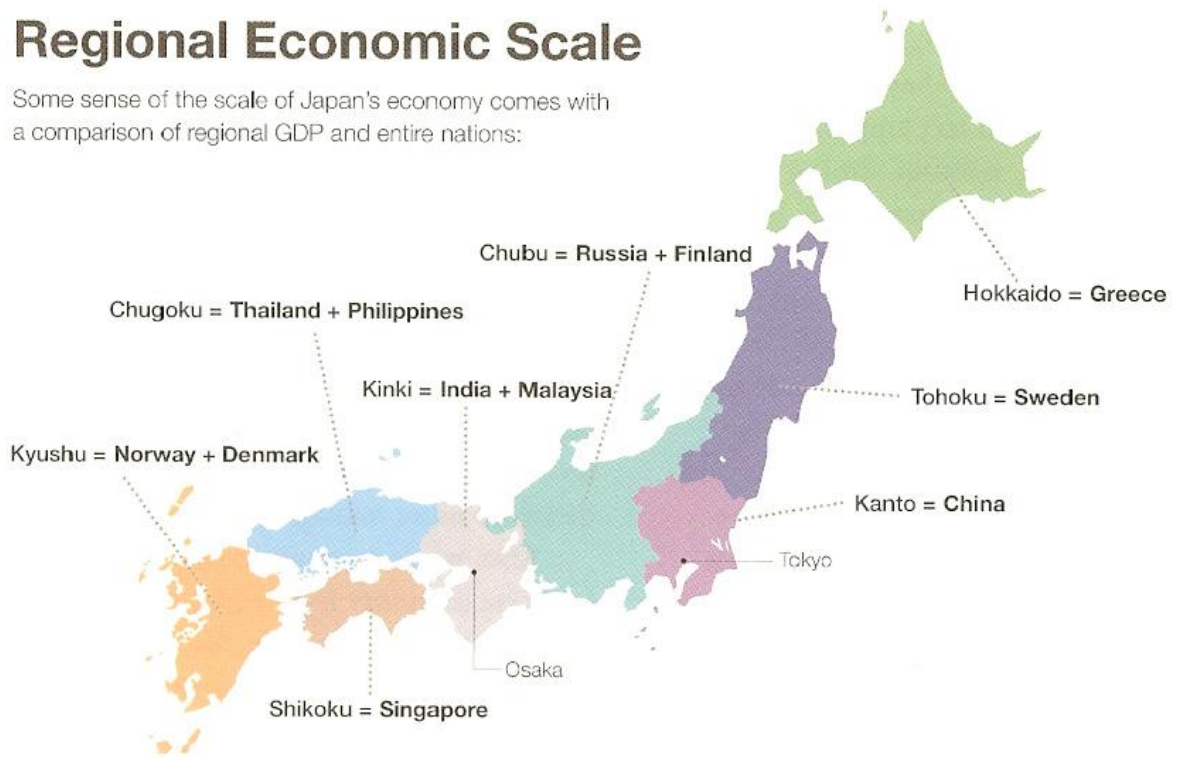
⁷² OECD Investment Newsletter February 2007

Regional Economic Scale

This gives a graphical description of how important Japan is as a market. For example Tohoku area alone has a GDP equal to that of Sweden.⁷³

Regional Economic Scale

Some sense of the scale of Japan's economy comes with a comparison of regional GDP and entire nations:



⁷³ Gadelius 1907-2007 – The Story of a Century in Japan.