INVESTMENT CLIMATE STATEMENT
JAPAN

JULY 2003

U.S. EMBASSY TOKYO

TABLE OF CONTENTS

A. Government Attitude Toward Foreign Investment: Liberalizing

A.1. Openness To Foreign Investment: Few Formal Restrictions

Japan, the world's second-largest economy, is an immense potential market for U.S. foreign direct investment (FDI). The Government of Japan (GOJ) imposes few formal restrictions on FDI in Japan, and has removed or liberalized most legal restrictions that apply to specific economic sectors. The government does not impose export-balancing requirements or other trade-related FDI measures on firms seeking to invest in Japan. Risks associated with investment in many other countries, such as expropriation and nationalization, are not an issue in Japan. Moreover, Prime Minister Koizumi has pledged to double the amount of FDI in Japan over the next five years.

The current low-growth environment in Japan has created many new opportunities for FDI in this extremely rich and broad market:

- Prices are down to their lowest point in a decade.
- More Japanese companies are actively looking for foreign partners to inject needed capital and know-how.
- There are distressed assets that can be profitably acquired and returned to economic viability.

The challenges facing foreign investors seeking to establish or enhance their presence in Japan -- many of the most important of which are matters of private business practice rather than of government regulation -- include:

- A high overall cost structure that makes market entry, exit, and expansion expensive;
- Cultural and linguistic challenges to doing business;
- Corporate practices and market rules that inhibit foreign acquisition of Japanese firms, such as insufficient financial disclosure practices, cross-holding of shares among companies belonging to the same business grouping (keiretsu), the low proportion of publicly traded common stock relative to total capital in many companies, and public attitudes about foreign takeovers;
- Exclusive buyer-supplier networks and alliances are still maintained by some "keiretsu," which limit competition from foreign firms and domestic newcomers;
- Laws and regulations that directly or indirectly restrict the establishment of business facilities and hinder market access for foreign products, services, and FDI.
- Labor practices which inhibit labor mobility, repress productivity, and negatively impact development of skills.

All of these issues are currently being addressed in government-to-government talks, and progress is being made in many areas.

Despite Japan's attractive characteristics as a potential investment site, however, FDI levels have remained small relative to the size of the economy. Given the continued sluggishness of the Japanese economy, last year's FDI results were reasonably positive. Annual FDI flows into Japan rose to 0.23 percent of GDP in CY02, from levels of 0.16 percent in CY01 and 0.18 percent in CY00. In CY 2002, FDI in Japan recovered to $9.2 billion, from $6.2 billion in CY 2001, and 8.3 billion dollars in CY 2000. The CY02 FDI value equaled 80.5 percent (yen basis) of the historic record of FDI in Japan, 12.7 billion dollars, registered in CY 1999.

Japan continues to host the smallest amount of inward foreign investment as a proportion of total output of any major OECD nation. Foreign participation in mergers and acquisitions (M&A), which account for some 80% of FDI in other OECD countries, although on an upward trend, also lags in Japan. Meanwhile, Japan continues to run an imbalance between its inward and overseas FDI (see Table 1). Japan's direct investment abroad declined in CY02 to $32.3 billion, from the $38.3 billion level of CY 01. Japan's relative lack of foreign investment also acts as a restraint on the expansion of imports.

Much of the FDI flows in recent years, have come in the financial services and telecommunications sectors, reflecting important restructuring in these areas.

In the past four years, ongoing economic restructuring (due in large part to the more competitive financial sector and greater emphasis on rate of return), and changes in Japan's financial markets contributed to growth in foreign direct investment in Japan in non-financial sectors. Distribution affiliations, joint ventures, and mergers and acquisitions involving foreign and Japanese financial services providers have accelerated rapidly, as foreign firms take advantage of business opportunities being created in Japan's financial sector as a result of the Japanese government's "Big Bang" and the U.S. government's deregulation initiative with Japan. Japanese financial firms have started to look overseas for assistance in the form of new products, technologies and capital to meet these challenges. In addition, foreign firms have stepped in to buy the assets of domestic financial services firms that have recently failed. At the same time, structural impediments to foreign investment remain, and it is not certain that inward foreign investment flows will continue to accelerate.

Acknowledging that FDI in Japan lags far behind that of other industrialized economies, the GOJ has in recent years taken some welcome steps to address investment-related problems. Of most recent significance is the GOJ initiative to revise the Commercial Code. Other legislation reforming bankruptcy procedures has provided M&A opportunities, as distressed Japanese companies are able to seek partners or buyouts. The Ministry of Economy, Trade and Industry (METI) in particular is taking seriously the challenge of attracting greater foreign investment to Japan. At the regional level, a number of prefectural and city governments are intensifying their efforts to attract foreign investors.

Liberalization of Investment Restrictions: Japan has gradually eliminated most of the formal restrictions governing its FDI regime. In 1991, the GOJ amended the Foreign Exchange and Foreign Trade Control Law (which also controls foreign investment) to replace the long-standing "prior notification" requirement for all FDI with an "ex post facto notification" requirement for investment in non-restricted industries. "Prior notification" (and thus case-by-case approval) is now required only for investment in certain restricted sectors, including agriculture, forestry, petroleum, electrical/gas/water utilities, aerospace, telecommunications, and leather manufacturing. Administrative approval for foreign investment in some of these sectors is quite certain, while in other sectors it is likely to be subject to greater scrutiny based on "national sovereignty" or national security concerns.

U.S. investment has become increasingly common in some traditionally restricted sectors, particularly in the petroleum and telecommunications industries. The only legal restriction on foreign ownership in Japan's telecommunications sector applies to Nippon Telegraph and Telephone (NTT): foreign investment in NTT, which is 46-percent owned by the government of Japan, is limited to one third by the NTT Law. In the fall of 2001, Europe's Vodafone mobile telecommunications group took control of one of Japan's competing telecommunications operators, Japan Telecom, with an $11 billion investment that remains the single largest foreign investment in Japan. Japan's Radio Law and Broadcasting Law limit foreign investment in broadcasters to 20 percent, or at one third for a broadcasters categorized as facility-supplying. This limit does not apply to communications satellite facility owners and program suppliers or to cable television operators.

Several sections of the Japanese Antimonopoly Law (AML) are relevant to FDI. For example, chapter four of the AML includes extensive antitrust provisions pertaining to international contract notification (section 6), stockholding (sections 10, 14), interlocking corporate directorates (section 13), mergers (section 15), and acquisitions (section 16). The stated purpose of these sections is to restrict any stockholding, management, joint venture, and M&A activities that constitute unreasonable restraints on competition or involve unfair trade practices. These provisions are not intended to discriminate against foreign companies or to discourage FDI.

Limitations on Facility Development, and Availability of Investment Real Estate:

While the price of real estate has fallen for 11 consecutive years (since 1992), potential foreign investors still find that high real estate-related expenses and regulations are obstacles to investment in Japan. Urban land prices, (although less than half the 1991 high) remain expensive, and the rate of property turn-over is slow enough that investors frequently have trouble assembling property of sufficient size to accommodate their operations. Lack of information on land prices and ownership also impedes foreign and domestic investors, by making it harder to assess the real asset value of potential business partners or acquisition targets. It also inhibits faster development of the domestic market for estate-related financial products.

Revisions to the Securities Investment Trust Law, enacted in November, 2000, lifted the ban on real estate investment trusts (REITs) to permit marketing of mutual funds that invest in property rights. Although growth has been slow, REITs are already increasing demand for transparency and accurate pricing in the real estate market.

Aiming to increase the liquidity of Japanese real estate markets, over the recent years the government has progressively lowered capital gains, registration, and license taxes on real estate. In fiscal 2003, land transaction tax rates for licensing and registration were reduced from 5 percent to 1 percent (they will increase to 2 percent from 2006). Inheritance and gift taxes were also reduced to promote transfer of land and other assets from the older to the younger generation. More changes in tax policy and accounting standards could increase real estate liquidity, but the market is still hampered by the shortage of legal and accounting professionals, the lack of information on prices and income flows, and taxes that discourage real estate transactions. Beginning March 31, 2001, the Japan Institute of Certified Public Accountants introduced a standard requiring companies to write off substantial losses (50% or more) on real estate inventories acquired for sale or development, further encouraging liquidity in real estate markets.

Japan continues to restrict the development of industrial and commercial facilities in some areas in an attempt to prevent excessive concentration of development in the environs of Tokyo, Osaka, and Nagoya, and also to protect land designated as optimal for agriculture. On the other hand, many prefectural governments outside the largest urban areas will make available property in public industrial parks. Generally speaking, Japan's zoning laws give local Japanese officials and residents considerable discretionary authority to screen almost all aspects of a proposed building. These factors effectively reduce the real estate available for development and often lead to delays in construction and higher building costs.

The Large-scale Retail Store Location Law (LRSLL) has been in effect now for three years. The law emphasizes the preservation of the living environment rather than the protection of small business. Local authorities implement the law in accordance with guidelines laid down by the Ministry of Economy, Trade and Industry (METI). The Embassy continues to monitor the local implementation to ensure that foreign and domestic large retailers do not experience difficulty establishing retail facilities under the locally administered rules.

Corporate Tax Treatment: Local branches of foreign firms are generally taxed only on corporate income derived from within Japan, whereas domestic Japanese corporations are taxed on their worldwide income. Calculation of taxable income and allowable deductions, and payments of the consumption tax (sales tax), are otherwise the same as those for domestic companies, with national treatment for foreign firms. Corporate tax rules classify corporations as either foreign or domestic depending on the location of their “registered office,” which may be the same as or a proxy for -the place of incorporation. The United States has a tax treaty with Japan that generally allows Japan to tax the business profits of a U.S. resident only to the extent those profits are attributable to a “permanent establishment” in Japan, and in addition provides measures intended to mitigate double taxation. The United States and Japan announced in June 2003 that an agreement in principle has been reached on a new tax treaty that when completed will replace the existing treaty.

Dividends on listed stock are subject to a 10 percent withholding tax until March 2008, when the rate will return to 20 percent; interest payable to a nonresident is normally subject to withholding of 15 percent, and royalties and fees paid to a foreign licenser by a Japanese licensee are subject to withholding of 20 percent. The current U.S.-Japan Tax Treaty provides for reductions in the withholding taxes for payments to U.S. residents. It was publicly announced that the agreement in principle reflects substantial reductions in the withholding taxes imposed on cross-border dividends, interest, royalties and other income, including the complete elimination of source-country withholding taxes on royalties, certain interest, and certain intercompany dividends. A special tax measure allows designated inward investors to carry over certain losses for tax purposes for ten years rather than for the normal five years. In JFY96, the scope of losses that qualify for this special measure was expanded.

As part of the JFY03 Tax Reform, Japan’s effective corporate tax rate, including local taxes, was reduced from 40.87% to 39.54%.

The option of consolidated taxation was made available to corporations since April 1, 2002. Consolidated taxation should facilitate investment and corporate restructuring, because the losses usually expected from a new venture or recently-acquired subsidiary can be charged against the profits of the parent firm or holding company. However, in order to partially recapture the anticipated loss in tax revenues, the GOJ imposes a 2% tax surcharge on firms that elect consolidated taxation as a two-year temporary measures.

Investment Incentives:

In Japan, both government and the private sector are increasingly promoting inward FDI. At a meeting in June 2002, the Cabinet established FDI promotion as one of the key strategies for revitalizing the Japanese economy, and resolved to put teeth into the measures needed to attract investment. In a General Policy Speech in January 2003, Prime Minister Koizumi pledged to double the cumulative amount of FDI in the next five years. Following this announcement, in March 2003, the Japan Investment Council (JIC) prepared a report setting out a "Program for Promoting Foreign Direct Investment," which discussed five target sectors and 74 measures. The Japanese Government endorsed these proposals and declared it would promptly implement them. (For more details of the report, see http://www5.cao.go.jp/access/english/jic_main_e.html)

Based on this report, the Invest Japan Business Support Center, a one-stop office to provide investment information to foreign companies, will be established in the Japan External Trade Organization (JETRO) on May 26, 2003. (More detailed information is available at http://www.jetro.go.jp/investjapan/). Furthermore, information desks will be established in all concerned ministries as a center for investment information and support for navigating administrative procedures.

Previous to this, in September 2002, the business sector established the Invest Japan Forum (IJF), composed of top Japanese and foreign managers. In December 2002 the IJF made recommendations for promoting FDI to the Prime Minister and the JIC. Many of these suggestions were incorporated in the IJF's report. The U.S.-Japan Private Sector/Government Commission held on April 14, 2003, also shared the view that the two countries should dramatically increase FDI and follow up on the suggestions made by the IJF.

Local governments are also increasing their efforts to attract foreign capital. Osaka and Hokkaido held the Investment Initiative Seminars in April 2003 during which these prefectures introduced their measures to attract foreign capital.[1] In order to support these local government efforts to promote inward FDI, the Japanese Government started a project in FY 2003 called the "Advanced Areas to Promote Foreign Direct Investment." Through this project, JETRO will give special support to local governments, that are actively trying to attract foreign capital. For fiscal year 2003, five regions have been selected: Osaka/Higashi-Osaka/Ibaraki, Sendai, Hyogo/Kobe, Hiroshima, and Fukuoka/Kita-Kyushu/Shimonoseki.

---

[1] Osaka Prefecture, Osaka City and the Osaka Chamber of Commerce established the Osaka Business and Investment Center (O-BIC) as a one-stop center for providing information on entering the Osaka market and shortened the processing time for starting a company to six months instead of 12 months. The prefecture also improved tax incentives so that incoming companies in Osaka Prefecture receive up to 90% corporate enterprise tax cuts as well as a 50% reduction in the real estate acquisition tax. Hokkaido Prefecture provided information on Hokkaido's investment environment by setting up Hokkaido industrial tours, targeting foreign diplomatic offices, promoting the prefecture's investment environment, and assisting JETRO's Invest in Japan Study Program (IJSP), which invites foreign companies interested in investing in Japan.

Another Japanese Government program started in April 2003 is called "Special Zones for Structural Reform." This program designates certain areas as exempt from regulations in order to develop the areas' special features. These zones are based on ideas developed by local governments and private companies. In the first phase, 57 special zones were certified on April 21. Among them is a Special Zone for International Distribution with a 24-hour/365-day customs clearance, which is expected to greatly enhance the environment for FDI. Under the zone program, it is possible to set up other special regulatory exemptions that benefit the investment environment. For instance, zones could eventually be developed allowing corporations to own hospitals, schools, agricultural enterprises and special elderly nursing homes that have been barred to private companies and could introduce special exemptions for visas/resident qualifications to expand the acceptance of foreign engineers, tourists and exchange students.

The Headquarters for the Promotion of Special Zones for Structural Reform will continue to invite ideas on new zones from local governments and private companies. Foreign governments and companies can also submit ideas to the local government. When local governments and private companies join with foreign governments and companies, creative ideas for new special zones could be developed that contribute to attracting inward FDI. Therefore, active involvement of all parties is encouraged.

A.2. Conversion and Transfer Policies: Generally Uninhibited

All foreign exchange transactions to and from Japan -- including transfers of profits and dividends, interest, royalties and fees, repatriation of capital, and repayment of principal -- are, in principle, freely permitted unless expressly prohibited. With the April 1998 revision of the Foreign Exchange Law, Japan moved to an ex-post notification system. This means that all foreign exchange transactions (unless specifically prohibited, including certain foreign direct investments, listed in the Appendix) no longer require prior notification or approval. In addition, the law eliminated the authorized foreign exchange bank system, whereby foreign exchange transactions all had to go through certain registered banks. All other restrictions on methods of payment -- including netting of settlements -- were also removed, enhancing the ability of foreign and Japanese financial firms to offer a fuller range of services in Japan. This has led to lower foreign exchange transaction costs for non-financial firms as well.

Japan is an active partner in the struggle to choke off terrorist financing. In coordination with other OECD members, the GOJ is strengthening due-diligence requirements for financial institutions. A new know-your-customer law was passed in 2002. These changes could have an impact on the transfer of funds.

A.3. Expropriation and Compensation: Virtually No Risk

In the post-war period, the GOJ has not expropriated or nationalized any enterprises, with the exception of the nationalization in 1998 of two large capital-deficient banks and, in 2002, of two small failed regional banks. Expropriation or nationalization of foreign investments is unlikely in the foreseeable future.

A.4. Dispute Settlement: No Outstanding Cases in Investment Area

There have been no major bilateral investment disputes since 1990, and there are no outstanding expropriation or nationalization cases in Japan. There have been no cases of international binding arbitration of investment disputes between foreign investors and the GOJ since 1952. Japan is a member of the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitration Awards. However, it has long been considered an inhospitable forum for international commercial arbitration. The Japan Commercial Arbitration Association, the only organization that arbitrates international trade and investment-related disputes, had only 63 cases submitted to it between 1998 and 2002. Of these, only 37 went to arbitration.

There are no legal restrictions on access by foreign investors to Japanese lawyers, and significant reforms in laws governing legal services and the judicial system are increasing the ability of foreign investors to obtain adequate legal advice on doing business in Japan – despite some foot-dragging by the Federation of Japanese Bar Associations (*Nichibenren*).

Based on the Program for Promoting Justice System Reform endorsed by the Cabinet in March 2002, the Government of Japan submitted legislation in March 2003 to the ordinary Diet session to promote cooperation and collaboration between Japanese lawyers (*bengoshi*) and foreign lawyers qualified under Japanese law (*gaiben*). The legislation included the "Bill to Amend the Special Measures Law Concerning the Handling of Legal Business by Foreign Lawyers" that provides for the following amendments (which will come into effect within two years of promulgation of the law based on the Cabinet order):

a. The elimination of the prohibition on the employment of *bengoshi* by *gaiben*;
b The elimination of the regulations on joint enterprises between *gaiben* and *bengoshi*; and
c. The abolition of legal provisions for <u>specified joint enterprises</u> (*tokutei kyodo jigyo*) and the establishment of <u>joint enterprises between *bengoshi* or *bengoshi* professional corporations (*bengoshi hojin*) and *gaiben*</u> (*gaikokuho kyodo jigyo*.).

Enactment of the bill will have the following results:
a. A *gaikokuho kyodo jigyo* organized as a single law firm or as separate firms will be able to provide integrated legal advice and legal services on any and all matters within the competence of its members;
b. *Gaiben* and *bengoshi* or *bengoshi hojin* in *gaikokuho kyodo jigyo* will be able to adopt a single law firm name of their choice;

c *Gaiben* and *bengoshi* in *gaikokuho kyodo jigyo* will be free to determine the profit allocation among them freely and without restriction;

d. *Gaiben* will be permitted to hire *bengoshi* to work with them directly or in a *gaikokuho kyodo jigyo* or in a *gaikokuho-jimu-bengoshi jimusho* composed of multiple *gaiben*; and

e. *Gaiben* and *bengoshi* will continue to be permitted to enter into relationships on an ad hoc basis that involve the sharing of profits and expenses.

Another significant step was the establishment of the Judicial Reform Promotion Headquarters on December 1, 2001, based on the Law on Promotion of Judicial Reform. The Headquarters has developed a reform program, based on the recommendations of the Judicial

Reform Council. On March 19, 2002, the Cabinet adopted a program that provides for the following:

- To increase the number of legal professionals, the Ministry of Justice (MOJ) will increase the annual number of persons who pass the Bar Examination to 1,500 by 2004 and to 3,000 by around 2010; and the Headquarters, in cooperation with the Ministry of Education, Culture, Sports, Science and Technology, will introduce a new system of law schools, commencing in April 2004, and in preparation will develop standards for selecting the universities that will be allowed to establish law schools.

- To reform the arbitration law, the Headquarters submitted legislation to the Diet in mid-January 2003, which will include a major revision of the existing Arbitration Law and improvement of the legal framework for arbitration, including international commercial arbitration.

- To increase the speed and efficiency of civil litigation, the Headquarters and MOJ submitted legislation to the Diet in mid-January 2003 to reduce by half the length of time required to complete court trials through measures to promote efficient scheduling of hearings, increase significantly the number of judges and court personnel, and facilitate litigants' collection of evidence at early stages of litigation.

- The Headquarters and MOJ submitted legislation to the Diet in mid-January 2003 to reduce filing fees for civil litigation.

- To strengthen judicial oversight over administrative agencies, the Headquarters is undertaking a comprehensive study of judicial oversight over administrative agencies, including review of the Administrative Case Litigation Law, and will take necessary measures to strengthen judicial oversight by November 30, 2004.

- To make the specialized departments concerning intellectual property rights in both the Tokyo and Osaka District Courts function substantially as “patent courts,” the Headquarters and MOJ submitted legislation to the Diet in mid-January 2003.

More generally, Japan’s civil courts enforce property and contractual rights, and the courts do not discriminate against foreign investors. However, they are sometimes ill suited for litigation of investment and business disputes. As in many other countries, Japanese courts operate rather slowly. As noted above, the Judicial Reform Promotion Headquarters is enacting a number of changes to speed the conduct of trials.

In addition, the courts lack contempt powers to compel a witness to testify or a party to comply with an injunction, and timely temporary restraining orders and preliminary injunctions are very difficult to obtain. While filing fees for large civil cases were reduced in 1992, they are still based on the amount of the claim, rather than a flat fee. Lawyers usually require large up-front payments from their clients before filing a lawsuit, with a modest contingency fee, if any, at the conclusion of litigation. Contingency fees familiar in the U.S. are relatively uncommon. A losing party can delay execution of a judgment merely by appealing, and in appeals to the high courts, additional witnesses and other evidence are sometimes allowed.

Courts do have power to encourage mediated settlements, and the courts have a supervised mediation system. Parties can manipulate this system to delay resolution, however, and because judges move frequently, continuity is often lost. As a result, it is very common for companies to settle out of court.

A.5. Performance Requirements and Incentives: None

Japan does not maintain a system of performance requirements. Japan also maintains no formal requirements for local management participation or local control in joint ventures or other forms of direct investment, except in restricted sectors.

A.6. Right to Private Ownership and Establishment: Secure for Foreign Business

Japan legally maintains the right for foreign and domestic private enterprises to establish and own business enterprises and engage in all forms of remunerative activity.

A.7. Protection of Intellectual Property Rights: Can Be Time-Consuming And Costly

Protection of intellectual property rights is an integral part of every successful U.S. exporter's basic market strategy in Japan. It is necessary to file applications to register patents and trademarks in Japan to obtain protection, but prior patent filing in the United States can provide certain advantages if applications are filed promptly in Japan. A U.S. patent or trademark attorney can provide informal advice, but it is necessary to hire a Japanese lawyer or patent practitioner (benrishi) registered in Japan to prosecute the patent or trademark application. In conformity with international agreement, Japan maintains a non-formality principle for copyright registration -- i.e., registration is not a pre-condition to the establishment of copyright protection. However, the Agency of Cultural Affairs maintains a registry for such matters as date of first publication, date of creation of program works, and assignment of copyright. U.S. copyrights are recognized in Japan by international treaty. U.S.-produced semiconductor chip design-layouts are protected for ten years under a special law if they are registered with the Japanese “Industrial Property Cooperation Center”-- a Japanese government-backed public corporation.

Obtaining and protecting patent and trademark rights in Japan can be time-consuming and costly, although patent fees have recently been reduced considerably. While the process to safeguard such rights might seem prohibitive, lack of protection would permit competitors both in and outside of Japan to copy a product or production process. Even when intellectual property rights have been acquired, pirating of technology and designs can occur in Japan, as in other countries. Each company in a trading or licensing agreement should understand clearly what its rights and obligations are with respect to the intellectual property rights owned or acquired by the other. Such a clear understanding helps to create a good rapport based on mutual trust, thereby ensuring the success of the trading or licensing agreement.

Patents, Trademarks, Utility Models and Designs: Unlike U.S. patent law, patents are granted to the first to file an application for a particular invention, rather than to the first to invent. Although Japan accepts filings in English (to be followed by a Japanese translation), companies should ensure that translations of their applications are perfect, as significant negative ramifications may result from translation errors. Prompt filing in Japan is crucial because printed publication of a description of the invention anywhere in the world, or knowledge or use of the invention in Japan, prior to the filing date of the Japanese application, would preclude the grant of a patent on the application. Also, unlike the United States, where examination of patent applications is automatic, an applicant must request examination of his patent application in Japan within three years of filing.

As is true in many countries, all patent applications are published 18 months after filing. If, during the examination, the Japanese Patent Office (JPO) finds no impediment to the grant of a patent for a particular invention, it publishes the patent application in the Patent Public Gazette a second time, including any changes that have been made during the examination. Under a recent amendment to the Patent Law, parties may contest the terms of a patent grant immediately after issuance by the Patent Office (for a period of up to six months), rather than prior to registration as had been the previous practice. The patent is granted and valid for 20 years from the date the application is filed.

It takes an average of 22 months, according to the latest JPO statistics in CY 2001, in Japan from the request for examination of application to First Action. An applicant can request accelerated examination, and efforts by the Patent Office to make the documentation necessary for the preliminary research required to request accelerated examination available electronically are expected to lower the cost of such requests to the applicant. During the examination period, limited effective legal protection exists.

Japan's Trademark Law protects trademarks and service marks. As is the case with patent applications, a resident agent (usually a lawyer or patent agent) must prosecute the trademark application. And as with the processing of patent applications, Japan's trademark registration process can be slow. Any company planning on doing business in Japan should file for trademark registration as early as practicable. Japan is subject to the Madrid Protocol (effective March 14, 2000) and trademarks registered at the WIPO Secretariat will be protected among member countries.

Japan's Utility Model Law also allows registration of utility models, a form of minor patent with a 6-year term of protection, retroactive from the date of application since January 1994. A separate design law allows protection of designs, with a 15-year term of protection from the date registration was made.

Unfair Competition and Trade Secrets: The only protection available for a trademark in Japan prior to registration is under the Japanese Unfair Competition Prevention Law. Under this law, the owner of the mark must demonstrate that the mark is well known in Japan and that consumers will be confused by the use of an identical or similar mark by the unauthorized user. In 1990, Japan enacted amendments to the law that provided some protection from theft of trade secrets, such as know-how, customer lists, sales manuals, and experimental data. The law, which was amended completely in 1993, also provides for injunctions against wrongful use, acquisition, or disclosure of a trade secret by any person who knew or should have known that the information in question was misappropriated. The judicial process, however, makes the enforcement of rights without loss of trade secrets difficult.

A.8. Transparency of the Regulatory System: Toward More Openness

Over-regulation in Japan continues to restrain economic growth, raise the cost of doing business, restricts competition, impedes market entry and exit, and impede investment. It also raises prices and increases the cost of living for Japanese consumers and for foreign businesses operating in Japan. The 1990s have been dubbed Japan's "Lost Decade", during which Japan's growth in gross domestic product (GDP) averaged a mere 1.05%, or less than half the 3.8% average of the preceding decade. This was brought about by Japan's inability to recover from massive asset deflation that followed the burst of the economic "bubble" (manifested in huge non-performing loans) and an inability to reform political, economic and social systems to adapt to the changing international environment of economic globalization and the Information Technology revolution. Typical of highly regulated economies, the Japanese economy is now suffering from a serious misallocation of resources, a lack of investment and a lack of entrepreneurial innovation. In addition to slowing growth, government over-regulation lies at the heart of many market access and competitive problems faced by U.S. companies in Japan.

An essential prerequisite for a vibrant Japanese economy is a regulatory system that is transparent, fair, predictable and accountable. It is important that domestic and foreign firms alike have full access to information and opportunities to participate in the regulatory decision-making process. The Japanese Government has made greater transparency a crosscutting theme of its Three-Year Program for Promoting Regulatory Reform (Cabinet Decision of March 30, 2001). The systemic measures set out in the Three-Year Program could contribute to needed improvements in the transparency and accountability of the Japanese regulatory system. They include: wide and effective use of the Public Comment Procedures for Formulating, Amending and Repealing Regulations; the strict enforcement and promotion of the use of the 1994 Administrative Procedure Law; increased transparency of administrative guidance; full and effective implementation of the Law Concerning the Disclosure of Information Retained by Administrative Agencies; expanded use of the “No Action Letter” system; comprehensive and objective evaluation of the regulatory process; and examination of the need, effects, and costs of new proposed and existing regulations.

Building on these measures, the United States in its Regulatory Reform Initiative submissions has recommended that the Japanese Government undertake additional improvements in its regulatory system to support Japan’s reform efforts and to ensure universal access to government information and the policymaking process. In particular, Japan needs to make the Public Comment Procedures more effective, to reduce the use of Administrative Guidance, and to encourage greater public participation in the legislative process.

The United States continues to hold bilateral working-level discussions in an effort to encourage the Japanese to promote deregulation, competition policy, and administrative reform measures that could help revive the Japanese economy, increase imports and foreign direct investment into Japan. The reader should consult the National Trade Estimate Report on Foreign Trade Barriers, issued by the Office of the U.S. Trade Representative (USTR) on March 31, 2003, for a detailed description of Japan’s regulatory regime as it affects foreign firms (both exporters and investors).

A.9. Capital Markets and Portfolio Investment: Some Restrictions

Japan maintains no formal restrictions on inward portfolio investment, and in fact foreign capital occupies an increasingly important place in Japanese capital markets. However, corporate practices such as cross-shareholding, while declining, still limit the percentage of shares in individual firms and in the overall market that foreign investors can actually purchase. Informal restrictions on management participation of foreign shareholders limit the attractiveness of Japan's equity market to foreign investors, although some firms have taken steps to facilitate exercise of shareholder rights by foreign investors, such as permitting electronic proxy voting.

Environment for Mergers and Acquisitions: Stock market-based takeovers of listed firms via tender offer, as widely practiced in the United States and parts of Europe -- both friendly and hostile -- remain rare in Japan.Viewed historically, of the roughly 400 foreign investment M&A transactions in Japan since 1991 (including divestitures of overseas firms held by Japanese), only five cases involved tender offers for companies listed in Japan. (Even this was an improvement over the previous two decades, which saw only one such case.) Japan's aversion to M&A activity is starting to fade, accelerated by the unwinding of extensive corporate cross-shareholding brought about by implementation of improved accounting standards and new government mandates that banks divest cross-held shares above a set level of holdings.

Friendly transfer of wholly-owned and majority-owned subsidiaries remains a more common form of M&A in Japan. Similarly, there are signs that owner-operated unlisted firms -- which traditionally would only sell out as a last resort before bankruptcy -- are becoming more amenable to acquisition by foreigners. Particularly in the more modern, more service-oriented sectors of the economy, purchase by foreigners is becoming less of a badge of shame than in years past.

Still, there remain a number of key factors limiting greater entry into the Japanese market through M&A with unlisted firms -- including tax policy, weak accounting and disclosure practices, Japan's underdeveloped OTC stock market (which if more developed would reduce the risks involved in M&A), lack of readily available information on firms that might be acquired, and the relative lack of a M&A "infrastructure" in the form of specialists skilled in making matches and structuring M&A deals.

Two new exchanges geared towards encouraging start-ups and venture capital investments opened in Tokyo in 1999-2000:Tokyo Stock Exchange introduced "Mothers," with less-stringent listing criteria for emerging companies and Nasdaq together with an Osaka-based exchange, opened Nasdaq Japan. But in 2002, Nasdaq pulled out of Japan and Mothers still has relatively few listed firms and suffers from lack of liquidity.

Commercial Code Revisions: A major revision of the Commercial Code is now underway. In January 2001, new laws designed to facilitate procedures for spin-offs to establish new firms and to transfer divisions from one company to another went into effect. Important legislation was passed in the 2002 Diet that will significantly increase the flexibility of capital structure and improve corporate governance:

Flexibility of Capital Structure:

As detailed in the document "Japanese Corporate Law: Drastic Changes in 2000-2001" issued by the Ministry of Justice on April 16, 2002, the Diet has enacted a number of revisions to the Commercial Code to improve the methods through which companies may obtain financing and services and to provide incentives to managers and employees, including amendments:

1. Relaxing the restrictions on the size of units of stocks, including abolishing the ¥50,000 per share minimum issue price and restrictions on the minimum net assets per share at the time of stock splits;

2. Authorizing the issuance of tracking stock;

3. Eliminating the prohibition on the issuance of non-voting common stock, and increasing the limit on the total number of non-voting shares that may be issued from one-third of the total issued shares to one-half of total issued shares;

4. Substantially liberalizing restrictions on issuance of stock options, including abolishing restrictions on the recipients of stock options, maximum number of stock options that may be granted and the permissible exercise period;

5. Permitting classes of shareholders of closely held corporations that have issued more than one class of shares to elect a specified number or percentage of board members;

6. Eliminating the prohibition against transfers of new subscription rights; and

7. Eliminating the requirement for court-supervised inspection procedure for valuation of in-kind capital contributions, allowing as an alternative certifications by professionals such as lawyers, accountants or tax accountants.

Improvements in Corporate Governance:

In addition, the Diet has enacted a number of revisions to the Commercial Code and the Industrial Revitalization Law to ensure efficient corporate governance, including amendments:

1. Providing publicly traded companies the option of adopting U.S.-style corporate governance system instead of complying with the statutory auditor (*kansayaku*) requirement. This option requires the appointment of executive officers and the establishment of a board committee system in which at least the audit, nomination and compensation committees would be composed of a majority or more of outside directors. The new measure is, however, under the Industrial Revitalization Law, which requires companies to submit their company revitalization plans to METI Minister to obtain Minister's authorization. MOJ plans to amend the Commercial Code to make the new measure available for companies in general within the next two years; and

2. Permitting companies to use the Internet or other electronic means to provide notices of shareholders' meetings and other similar communications to shareholders upon individual consent, and permitting shareholders to exercise their voting rights through the use of electronic devices. In addition, companies are permitted to meet their mandatory disclosure requirements for balance sheets (and profit and loss statements) by making the full text available for 5 years in an electronic format.

Cross-shareholding and M&A: Potential foreign investors in Japan frequently point out that extensive cross-shareholding (*mochiai*) in Japan greatly complicates market-based merger and acquisition transactions, and reduces the potential impact of shareholder-based corporate governance. Corporate governance practices which result in senior management emphasizing internal loyalties over shareholder return can also lead to premature rejection of M&A offers. At the same time, Japanese companies are unwinding cross-shareholdings, which has accelerated in recent years under the pressure of difficult corporate finances and stricter accounting requirements. Similarly, more corporations are hiring outside directors, and placing greater emphasis on shareholder value in their management practices.

To assist corporations in reducing the unfunded liabilities of corporate pension funds and to accelerate the unwinding of cross-shareholdings, the Japanese government implemented legislation in 2000 that allows corporations to transfer shareholdings to their related corporate pension funds. If the shares are directly transferred, the pension fund is able to properly execute shareholder rights, and sell the shares if it is deemed in the best interests of the pension-holders. However, many firms prefer the alternative of indirect transfer of shares through a trust whereby the sponsoring corporation retains voting rights and effectively influences when the shares can be sold. In 2001 the GOJ created the Banks' Shareholdings Purchase Corporation to facilitate sale of bank cross-held shares.

In another useful innovation, the Diet approved amendments to the Commercial Code permitting creation of a stock swap system, through which one of the parties becomes a wholly-owned subsidiary company and the other a parent company, as well as a stock transfer system to establish a parent company. Special tax treatment will be implemented in conjunction with the creation of the stock exchange and the stock transfer system to allow deferment of taxes on capital gains on stocks at the time of exchange and transfer. To take advantage of these new rules, however, foreign investors must legally establish a Japanese subsidiary firm to act as the counterpart to the stock exchange/transfer.

Legislation to allow foreign firms – and Japanese firms operating internationally – to use similar transactions when conducting M&As based in other markets has been adopted as part of an amendment to the Industrial Revitalization Act. Unfortunately, deferred tax treatment was not part of the package, though it may be taken up at a later date. Indications are that the Ministry of Justice Legislative Council intends to recommend more complete legislation as part of the Commercial Code revisions planned for 2005.

Accounting and Disclosure: Accounting and disclosure standards are an extremely important element in assessing and improving any nation’s environment for mergers and acquisitions. Before any merger or acquisition can take place, it is critical that the merging or purchasing corporations have the best possible information on which to make business decisions. Implementation of “Big Bang” -associated reforms since 1998 has significantly improved Japan’s accounting standards.

A shift to consolidated accounting was made mandatory in FY99 and "effective control standards and influence" standards were introduced in place of conventional holding standards, expanding the range of subsidiary and affiliated companies included for the settlement of account. Consolidated disclosure of contingent liabilities, such as guarantees, began in April

1998. Since FY01 all marketable financial assets held for trading purposes including cross-shareholdings and other long-term securities holdings are recorded at market value in Japan.

Also starting in FY00, companies were required to disclose unfunded pension liabilities by valuing pension assets and liabilities at fair value. Fixed asset impairment accounting is scheduled for FY05. This new rule would require firms to record losses if the recoverable value of property, plant or equipment is significantly less than book value.

The greater focus on consolidated results and mark-to-market accounting is already having an impact and is encouraging unwinding of cross-held shares. Corporate restructuring is accelerating, and companies are rushing to reduce pension under-funding. Banks have stared disposing of low-yield assets. While the recent improvement in accounting standards and growth in M&A activity have been welcome, they have also exacerbated the shortage of accounting professionals.

Taxation and M&A: Preferential tax treatment of initial public offerings remains a problem. Under current regulations, if a company is sold in an M&A transaction before the IPO listing,, a 10% capital gains tax rate applies for listed stocks, and a 26% capital gains tax applies for all others. If the founding shareholder of a qualified company "goes public" and then sells shares of the company into the market, a capital gains tax rate of as low as 5% applies (if the sale is within three years of being listed).

Bankruptcy Laws: An insolvent company in Japan can face liquidation under the Bankruptcy Act or take one of four roads to reorganization: the Civil Rehabilitation Law (Minji Saisei Ho), the Corporate Reorganization Law (Kaisha Kosei Ho), corporate reorganization under the Commercial Code (Kaisha Seiri) or an out-of-court creditor agreement.

In April 2000, Japan overhauled its bankruptcy law governing small and medium size firm bankruptcies by enacting the Civil Rehabilitation Law, which focuses on corporate restructuring in contrast to liquidation. The new law provides improved protection of debtor assets prior to the start of restructuring procedures, eases requirements for beginning restructuring procedures, simplifies and rationalizes procedures for the examination and determination of liabilities and improves procedures for approval of rehabilitation plans. Japan’s Corporate Reorganization Law, generally used by large companies, was similarly revised in April 2003. Amendments made corporate reorganization for large companies more cost-efficient, speedy, flexible and available at an earlier stage. By removing many institutional barriers to the restructuring process, the new bankruptcy regime has already accelerated the corporate restructuring process in Japan.

In the 1990s, most corporate bankruptcies in Japan were dealt with by out-of-court creditor agreements because court procedures were lengthy and costly. Also the fact that bankruptcy trustees had limited powers to oversee restructuring meant that most judicial bankruptcies ended in liquidation, often at distress prices. In 2001, a group of Japanese bankruptcy experts published a set of private rehabilitation guidelines, modeled after the UK-based INSOL guidelines, for out of court corporate rehabilitation in Japan. Out of court workouts in Japan tend to save time and expense, although they sometimes also lack transparency and fairness. In practice, because 100 percent creditor consensus is required for out-of-court workouts and the court can sanction a reorganization plan with only a majority of creditors' approval, the last stage of an out-of-court workout is often a request for a judicial seal of approval.

Credit Markets: Domestic and foreign investors have free access to a variety of credit instruments at market rates. In general, foreign companies in Japan have not experienced significant difficulties in obtaining funding. Most foreign firms obtain short-term credit by borrowing from Japanese commercial banks or one of the many (close to one hundred) foreign banks operating in Japan. Medium-term loans are available from commercial banks, as well as from trust banks and life insurance companies. Large foreign firms have tended to use foreign sources for long-term financial needs, although increasingly sophisticated derivatives products are becoming available to assist in hedging foreign investors' perceived risk.

A.10. Political Violence: Rare to Unknown

In general, political violence is rare in Japan, and acts of political violence involving American business interests are virtually unknown.

A.11. Corruption: Evolution Towards Stricter Ethical Standards

The penal code of Japan covers crimes of official corruption. An individual convicted under these statutes is subject, depending on the nature of the crime, to penal servitude ranging from one month to fifteen years, and possible fines up to three million yen or mandatory confiscation of the monetary equivalent of the bribe.

While corruption usually involves the exchange of moneys, the methods by which business is conducted in Japan can often lead to what some foreign Japan-watchers have described as "institutionalized corruption." For example, the web of close relationships between Japanese companies, politicians, government organizations, and universities has been said to foster an inwardly-cooperative business climate that is conducive to the awarding of contracts, positions, etc. within a tight circle of local players.

Bid-rigging activities continue. Bid-rigging harms both the competitive process and Japanese taxpayers, and undermines respect for competition principles and for the Antimonopoly Act. Most damaging is government official support and assistance in bid-rigging conspiracies. The Bid-Rigging Prevention Act came into effect on January 6, 2003. That Act authorizes the Japan Fair Trade Commission (JFTC) to demand central and local government commissioning agencies to take corrective measures to prevent continued complicity of officials in bid-rigging activities, and to report such measures to the JFTC. The Act also contains provisions concerning disciplinary action against officials who have participated in bid-rigging and compensation for overcharges when the officials caused damage to the government due to willful or grave negligence.

Amakudari is the practice whereby senior government officials retire into top positions in Japanese companies, usually in industries that they once regulated. These officials then function as in-house consultants on regulatory matters and as lobbyists to their former ministries and agencies. *Amakudari* individuals are particularly common in the financial, construction, transportation, and pharmaceutical industries -- which, not coincidentally, are traditionally heavily-regulated industries. Foreign companies usually do not enjoy such pipelines into the bureaucracy, and thus are somewhat disadvantaged in their ability to understand and deal with laws, regulations, and informal ministry guidance. This disadvantage has been ameliorated somewhat in recent years by the introduction of more transparent administrative procedures.

While there have been some high profile exposures of officials having either given or accepted bribes, the Japanese government has not had an aggressive record of criminal prosecution. Those prosecuted have generally received suspended sentences. In some cases, the government is in the dilemma of deciding how to handle past activities such as “wining and dining” which were commonplace at the time, but which are now more explicitly banned. The recent revelation of several corruption scandals may reflect an evolution towards stricter ethical standards.

Following reform in 1993, numerous shareholder civil suits have been filed. Japanese law also provides for company directors to be found personally liable for the amount of the bribe, and some judgments have been rendered against company directors. This change may significantly impact the payment of bribes, as individuals are held personally liable without the shield of the company to protect them, although there is currently discussion within the ruling political party of new rules to make it harder to file shareholder derivative lawsuits.

Japan has also ratified the OECD Anti-Bribery Convention, which bans the bribing of government officials in countries outside Japan. The OECD has identified some deficiencies in Japan's implementing legislation, which the Government of Japan has committed to rectify.

In June 2001, Japan made amendments to the Unfair Competition Prevention Law which closed the important loophole for foreign subsidiaries and extended the definition of "foreign official" to include executives of parastatal enterprises. Other changes recommended by the OECD Bribery Working Group, such as increasing the level of penalties for bribery, extending national jurisdiction to cover the crime of bribery, and providing for confiscation of bribery proceeds, are still under consideration by the GOJ. METI announced in late January 2003 that the GOJ intends to enact a new law (or at least amend the implementing legislation again) further regulating bribery. Discussion at the working group level has already started; while some believe that amendments/revisions could be submitted to the Diet as early as fall 2003, no timetable has been officially set.

B. Bilateral Investment Agreements: Continuing Discussions under EPG

The 1952 U.S.-Japan Treaty of Friendship, Commerce, and Navigation gives national treatment and most favored nation treatment to most U.S. investments in Japan.

U.S.-Japan Investment Arrangement: U.S. Government concerns regarding barriers to foreign investment in Japan continue to be addressed through bilateral discussions under the U.S.-Japan Economic Partnership for Growth (EPG), established by President Bush and Prime Minister Koizumi in June 2001. The Investment Initiative Working Group has conducted two full years of meetings discussing policy measures to improve the investment atmosphere in Japan and has pursued a vigorous program of public outreach. In order to increase business awareness and receptiveness to FDI, investment promotion seminars were held in the Japanese cities of Kobe, Fukuoka, and Nagoya in March 2002, and in Osaka and Sapporo in April 2003. Similarly, investment symposia were held in New York and Chicago in July 2002, and in San Francisco and Chicago in June 2003.

C. OPIC And Other Investment Insurance Programs: Not Available

OPIC insurance and finance programs are not available in Japan. Japan has been a member of the Multilateral Investment Guarantee Agency (MIGA) since it was established in 1988. Japan's capital subscription to the organization is the second largest among member countries, after the United States.

D. Labor: Toward More Flexibility

The Japanese labor market today suffers from demographic, macro-economic, and structural pressures, which are beginning to change traditional Japanese employment practices. The regulatory philosophy that has formed Japan's post-war labor laws is also changing. Foreign investors seeking to hire highly qualified workers in Japan will welcome most of these changes.

Japanese employment practices have been said to rest on "three pillars:" lifetime employment, seniority-based wages, and enterprise unions. In fact, these three aspects of the Japanese labor market have always applied only to the larger firms, and today all three are undergoing transformation. Demographic pressures – fewer young workers and a rapidly aging labor force – as well as the need for structural changes in the Japanese economy are forcing most firms to abandon both lifetime employment guarantees and seniority-based wages in favor of merit-based pay scales and limited-term contracts. Also, although labor unions play a role in the annual determination of wage scales throughout the economy, only 20.7 % of Japanese workers were union members in 2001. In firms with less than 100 employees, only 1.3 % were unionized in 2001.

Investors should be aware of Japan's high wage structure. In 2001, workers earned an average of approximately 305,800 yen per month (1.2 % increase from the previous year) in base wages including benefits, with significant variations by education, age/seniority and position. Occupational wage differentials are much smaller than in most countries. However, the Japanese Federation of Employers estimates that base wages, including basic benefits, were only 72.7 % of total wage costs in 2001. Annual summer and year-end bonuses added, on average, another 27.3 %. Relatively high statutory welfare contributions are also required for basic government pensions, health and accident insurance, and unemployment insurance. Most companies also incur other employee welfare costs for family and/or transportation allowances, company-provided pension schemes, and such in-kind payments as housing for some employees. Off-setting these high wage costs, of course, is the fact that the Japanese work force is highly educated, disciplined, loyal to their employer, and motivated to assure the economic well-being of the company.

Japanese workers have traditionally been classified as being either "regular" or "other" employees and this system is, to a considerable degree, still in place today. Regular employees are usually recruited directly from schools or universities and given an employment contract with no fixed duration. Other employees are given fixed duration employment contracts, which generally cannot exceed one year but may be renewed several times over. Still other employees include part-timers, interns, and "dispatched workers" -—as workers from temporary work agencies are called in Japan. Until very recently, only a few occupations could be handled by dispatched worker agencies but this is one area where Japanese labor law has in fact been deregulated, thus the number and types of dispatched workers have increased geometrically over the past several years.

The regulation of private, fee-charging employment agencies – including executive search firms – has also recently been liberalized. Although a fairly time-consuming and bureaucratic licensing procedure is still required, private employment agencies can now serve virtually the entire range of occupations. On-line, Internet based, job seeking and placement services are, however, still in their infancy in Japan – constrained at least partly by a Ministry of Labor requirement that every employment agency must personally interview each of its clients.

Defined contribution pensions, introduced in October 2001, should promote labor mobility, as workers will be able to carry their pension funds to other jobs.

E. Foreign-Trade Zones/Free Ports/Special Zones for Structural Reform

Japan no longer has any free-trade zones or free ports. Customs authorities, however, do allow the bonding of some warehousing and processing facilities in certain areas adjacent to ports on a case-by-case basis. The GOJ established a law in 1992 entitled the "Law on Extraordinary Measures for the Facilitation of Imports and Foreign Direct Investment in Japan" (effective July 1992 and valid until May 2006). Under the law, the GOJ helps increase access to the Japanese market for foreign goods and capital at government-designated "foreign access zones" near harbors and airports.

Prime Minister Koizumi is taking new approaches to restructuring Japan's economy. His administration's Special Zones for Structural Reform (SZSR) initiative is working to revitalize Japan's regional economies through locally-led regulatory and structural reform. The newly established Special Zones initiative could help remove the regulatory barriers that limit U.S. business market entry and foreign investment into Japan. (for more details see also pages 7-8)

F. Capital Outflow Policy: Net Exporter of Capital

Japan has continued to be a net exporter capital, as reflected in Japan's current account surplus, which totaled $ 112.8 billion in 2002 and $87.7 billion in 2001.

G. Investment Data: FDI in Japan Recovered in CY 2002

The following tables incorporate CY 2002 data for both inward and outward foreign investment in Japan. Until last year, the Report used Fiscal-Year and notification-based data announced by the Ministry of Finance (MOF). MOF used to announce this data by mid-June every year. This year, however, the Ministry has not released this data as of July 8, 2003. FDI data available at the moment are only Calendar Year- and balance-of-payment-based statistics announced by MOF on June 11, 2003.

The official statistics used thus far represent notification to the Ministry of Finance (MOF) of authorization by MOF of specific planned investment projects (as reported to MOF by companies), not necessarily actual flows of investment. In addition, the notification-based FDI statistics do not exclude investment that was withdrawn afterwards. Thus these figures generally exceed by a substantial amount actual investment flows as reported in Japan's balance of payments data. For those reasons, from this year's report we use balance-of-payments data as much as possible, particularly for the stocks of FDI. Balance of payments data, however, provide only overall FDI values by country, and do not cover industry-by-industry FDI and the number of cases of FDI. For those data, we still have to rely on MOF's notification-based data. (At the same time, neither notification-based data nor balance of payments statistics capture re-investment of profits by foreign firms operating in Japan, or Japanese firms operating overseas. Therefore, according to some academic researchers, both types of official data misstate actual foreign capital investment by a wide margin.)

In CY 2002, FDI in Japan recovered to $9.2 billion, from $6.2 billion in CY 2001, and 8.3 billion dollars in CY 2000. The CY02 FDI value equaled 80.5 percent (yen basis) of the historic record of FDI in Japan, 12.7 billion dollars, registered in CY 1999. Given the continued sluggishness of the Japanese economy, last year's FDI result was reasonably positive. This, however, reflected a rapid rise of FDI in Japan from European countries, increasing to $6.3 billion in CY02 from $2.9 billion in CY 01. European name-brand retailers appear to have invested heavily in Japan, taking advantage of declining prices in lands and commercial buildings. Last year, U.S. direct investment in Japan fell to $2.6 billion from $3.5 billion in CY01. Annual FDI flows into Japan as a percentage of Japan's GDP rose to 0.23 percent in CY02, from levels of 0.16 percent in CY01 and 0.18 percent in CY00. Japan's direct investment abroad, on the other hand, declined in CY02 to $32.3 billion, from the $38.3 billion level of CY 01. Last year, while Japan's direct investment in the U.S. gained slightly to $7.6 billion from $7.1 billion in CY 01, such investment in Europe plunged to $9.8 billion, compared with $17.9 billion in CY 01.

All data in the tables below is from MOF, current as of June, 2003, and converted into dollars using each year's average exchange rate: CY00 data at 107.77 yen to the dollar, CY 01 data at 121.53 yen to the dollar, CY 2002 data at 125.31 yen to the dollar, and "Cumulative Total" data as of the end of CY 2002 at 122.27 yen to the dollar.

Table 1a: Annual New FDI into Japan (Billions of Dollars; notification basis until JFY 1999, and balance-of-payment basis for CY 2000, 2001, and 2002)

JFY	1992	1993	1994	1995	1996	1997	1998
	4.08	3.08	4.16	3.83	6.84	5.53	10.47

JFY	1999	CY 2000	2001	2002
	21.5	8.32	6.24	9.24

Table 1b: Ratio of Japan's Inward to Outward FDI Flows **(notification basis until JFY 1999, and balance-of-payment basis for CY 2000, 2001, and 2002)**

JFY
1992 – 1:8.4
1993 – 1:11.7
1994 - 1:9.9
1995 - 1:13.4
1996 - 1:7.02
1997 – 1:9.77
1998 – 1:3.9
1999 – 1:3.1
CY
2000 – 1:3.8
2001-1:6.1
2002 – 1:3.5

Table 2: Foreign Direct Investment in Japan, by country (Million dollars; annual flow; balance-of-payment basis)

	CY 2000	CY 2001	CY 2002	Cumul.tot. (CY 2002-end)
N. America	58	4,252	3,128	37,479
U.S.	- 976	3,495	2,564	34,895
Canada	1,036	758	565	2,584
Europe	4,048	2,927	6,316	32,559
Neth	1,691	2,556	1,710	9,634
U.K.	225	-1,219	541	2,631
Germany	1,932	243	555	4,044
Switz.	98	128	1,045	2,712
France	2,277	424	2,305	10,102
Asia	986	129	12	3,617
Thailand	-15	-195	–134	17
Singapore	83	20	124	469
Taiwan	297	165	-23	1,347
Hong Kong	569	94	-14	1,426
Korea	48	38	63	204
L. America	2,883	-1,011	-189	2,351
Cayman Isles	2,549	-1,050	-114	1,707
Brazil	1	0	0	11
Total	8,322	6,241	9,245	76,628

Note: Negative figures indicate capital outflow on a net basis.

Table 3: Foreign Direct Investment in Japan, by industry
(Million dollars; annual flow; reporting basis -- not updated due to a delay in the data announcement)

	JFY 1999	JFY 2000	JFY 2001	Cumul.total '89-'01
Manufact.	8,783	7,254	2,611	39,693
Machinery	7,757	3,228	1,103	22,458
Chemicals	541	1,640	920	9,318
Metals	160	17	1	1,431
Rubr/Lthr	63	10	56	746
Petroleum	121	2,352	70	3,251
Textiles	2	22	22	175
Foods	13	0	280	945
Glass/Cer	51	0	75	177
Other	76	11	84	1,192
Non-manuf.	12,727	21,417	14,729	82,097
Finance/Ins1	4,586	9,443	5,261	28,546
Trade	3,124	2,536	865	17,297
Services	1,845	2,170	1,325	14,473
Real Estate	151	317	586	3,496
Telecom	2,959	6,888	6,597	17,061
Transport	20	52	18	355
Construction	20	0	68	159
Other	22	11	6	710
Total	21,511	28,671	17,340	121,791

Table 4: U.S. Direct Investment in Japan, by industry
(not updated due to a delay in the data announcement)
(Note: Data is actually North America, not U.S.)
(annual flow; reporting basis)

	JFY 2000		JFY 2001	
	$ Million	# of cases	$ Million	# of cases
Manufact.	1,909	37	775	44
Machinery	828	24	581	28
Chemicals	553	7	179	8
Metals	27	1	--	--
Foods	--	--	--	--
Non-manuf.	7,977	637	4,736	411
Finance/Ins.	6,360	98	3,447	101
Commerce/Trade	228	148	529	75
Services	980	343	409	191

Real Estate	28	24	50	23
Telecome	403	20	230	16
Construction	--	--	68	4
Total	9,887	674	5,511	455

Table 5: Japanese Direct Investment Overseas, by country
(Million dollars; annual flow; balance-of-payment basis)

	CY 2000	CY2001	CY 2002	Cum.tot. (CY 2002-end)
N. America	14,165	7,675	8,649	137,638
U.S.	14,112	7,081	7,592	132,961
Canada	58	595	1,057	4,677
Europe	10,941	17,911	9,764	70,686
U.K.	6,801	12,856	2,053	25,675
Netherlands	2,273	3,073	1,455	22,373
Germany	548	686	576	70,686
France	292	225	4,009	5,283
Spain	183	-73	-87	830
Sweden	830	-110	326	1,041
Asia	2,173	7,836	8,177	57,035
Thailand	593	1,590	524	6,137
Indonesia	588	483	303	5,456
China	937	2,161	2,610	12,114
Singapore	-1,512	970	1,880	10,181
Hong Kong	-123	504	224	5,341
Malaysia	-1	574	261	3,843
Philippines	511	276	1,094	2,900
South Korea	1,082	653	433	5,121
India	174	152	149	1,280
Taiwan	104	362	456	3,689
L. America	3,984	4,327	4,072	17,736
Cayman Isles	3,659	1,492	3,457	8,380
Brazil	-324	885	741	3,880
Mexico	374	2	240	2,515
Oceania	290	669	1,424	11,570
Australia	161	554	1,142	9,725
Africa	-193	183	227	1,203
South Africa	12	9	106	507
Middle East	-42	0	89	872
UAE	-7	-3	26	42
Saudi Arabia	-28	35	81	801
Total	31,556	38,333	32,301	298,336

Note: Negative figures indicate capital inflow on a net basis.

Table 6: Japanese Direct Investment Overseas, by industry
(not updated due to a delay in the data announcement)
(Million dollars; annual flow; reporting basis)

	JFY 1999	JFY 2000	JFY 2001	cum.tot. '89–00
Manufacturing	42,310	11,845	13,893	236,111
Electrical	16,350	3,090	3,646	70,111
Chemicals	1,694	1,942	1,486	29,641
Transport	4,781	3,182	4,138	13,263
Food	14,908	261	815	26,239
Metals	1,458	717	633	17,017
Machinery	995	1,430	1,214	19,039
Lumber/Pulp	116	150	729	5,646
Textiles	260	226	202	7,877
Other	1,749	849	846	25,288
Non-manufact.	24,178	37,158	17,312	438,925
Finance/Ins.	9,885	8,523	10,712	129,187
Comm/Trade	3,877	3,391	2,568	64,120
Real Estate	2,114	370	523	85,267
Services	4,314	1,784	1,545	84,639
Transport	2,771	22,185	1,335	51,532
Mining	922	650	478	16,230
Construction	182	91	64	4,870
Ag/Forestry	81	27	33	1,643
Fisheries	26	134	27	1,075
Other	8	2	26	367
Total	66,694	49,257	31,487	243,164

Table 7: Foreign Direct Investment in Japan relative to
GDP (FDI figures until JFY 1991 are on a notification
basis, and on a balance-of-payment basis for CY 2000, 2001, and 2002)

	JFY1997	1998	1999	CY 2000	2001	2002
Nominal GDP (a) (trillion yen)	507.6	487.3	493.8	511.8	500.3	499.99
FDI Inflow (b) (trillion yen)	0.68	1.34	2.4	0.90	0.76	1.16
b/a (%)	0.13	0.27	0.49	0.18	0.16	0.23

Table 8. Examples of Major Foreign Direct Investments by US companies and other Foreign Nations' companies

Financial/Insurance Services

Merrill Lynch – acquired Yamaichi securities
GE Capital – acquired Toho Insurance
Manulife (Canadian) – acquired Daihyaku Insurance
Ripplewood – acquired Long Term Credit Bank
AIG – acquired Chiyoda Life Insurance
Prudential – acquired Kyoei Life Insurance
City Financial, Japan – acquired assets of Marufuku (a consumer loan company)

Information Technology/Telecommunications

C and W (British/US interest) acquired IDC
MCI World Com – Greenfield investment
Level 3 – Greenfield investment
Time Warner/Media One – TITUS
Global One (Sprint JV with European firms) –greenfield investment
Cisco Systems –capital participation in Soft Bank
Microchip Technology – acquired assets of Fujitsu
Intel – capital participation in Nikon

Distribution/Retail/Hotel/Real Estate

Toys-R-US
Costco
Sports Authority
GAP
Disney stores
Nike
Amazon.com
Starbucks
Ripplewood – acquired Phoenix SEAGAIA Resort
Walmart (Business tie-up with Seiyu Supermarket)
CB Richard Ellis – acquired equities of New City Corporation (a real estate company)

Manufacturing

(tie ups)

Renault-Nissan
Ford-Mazda

GM-Suzuki
Daimler-Chrysler
GE - acquired Kawasaki LNP (Kawasaki Steel's chemical manufacturing subsidiary)
Dow Chemical – acquired Leich Hold (Dai Nippon Chemical's subusidiary)
IBM- acquired Display Technology (Toshiba's CD/LSD manufacturing subsidiary)
Solectron – acquired NEC's PC manufacturing business department)
Micron Technology –acquired KMT Semiconductor (Kobe Steel's semiconductor manufacturing subsidiary)
Micron Technology – acquired assets of Dominion Semiconductor (Toshiba's subsidiary)