

JAPAN ECONOMIC CURRENTS

A COMMENTARY ON ECONOMIC AND BUSINESS TRENDS

To Our Readers:

The Keizai Koho Center and its member companies in Japan are filled with sorrow about the terrorist attacks on September 11, 2001, and extend our deepest condolences to the families and colleagues of the victims of these terrible tragedies.

We are profoundly pained by the loss of lives and suffering in New York, Virginia, and those aboard the four hijacked flights. We share America's sadness, as well as the understanding that this terrorism is aimed not just at Americans but all of us in the modern, global community.

Those terrorist attacks were an appalling assault on humanity, democracy, freedom, and the innocent people who work hard for their families' well-being. Many Japanese business people, as well, were among those lost in the World Trade Center. The Japanese business circle supports the American people. The Vice Chairman of Keidanren (Japan Federation of Economic Organizations), Mr. Minoru Makihara, spoke out in the message below:

“The series of terrorist attacks in the United States of America leave me speechless. It is most painful to learn of so many precious lives lost, and on behalf of Keidanren I would like to extend my heartfelt sympathy and condolences to the victims and the concerned.

Terrorism is a coward and vicious act of violence that cannot be tolerated and never be forgiven. Japanese businesses share the pains incurred by the U. S. and the global community. Terrorism, after all, is an attack against the citizens on the globe who support democracy and freedom.

Japanese businesses support the United States in its fight against terrorists. The international community must unite in its effort towards total elimination of terrorism from the globe.”

September 12, 2001

The heroism of fire fighters and police officers truly represents the American spirit. I have been amazed and moved by the massive rescue efforts, the volunteers, and the generosity of donors. I believe in the strength of American people.

We stand by you.
Hideaki Tanaka, Director
Keizai Koho Center – U.S. office

Non-Profit Organizations in Japan—Where Do We Go From Here?

by Yoshinori Yamaoka, Japan Non-Profit Organization(NPO) Center

In late July 2000, a group of Japanese non-profit organizations (NPOs) representatives, municipal government employees, and journalists visited New York and Boston. The purpose of the visit was to study how American non-profits are tackling the problem of homelessness and how to apply what they learned to Japan.

American non-profits have made strides in working with the problems related to homelessness in large cities over the past 10 years. The major catalyst has been the initiatives taken by social entrepreneurial non-profits. But the support of local governments and the cooperation of the private sector in the U.S. should not be underestimated.

Throughout Japan, small grass-root NPOs have begun to address similar issues and their activities

are running full-bore. Japanese NPOs – the importance of which have just begun to be socially recognized – are quite different from those in the U.S., in terms of the underlying cultures and systems. But the bold concepts of American NPOs and their ability to get things done may provide valuable lessons for Japan.

(1) Issues that Japan's NPOs face in a society undergoing transition and the important role that they must play Japanese society is undergoing a period of great change that may be termed a third reformation. (The first reformation began the creation of the modern system, starting with the Meiji restoration in 1868, and the second was the postwar reformation, which began at the end of World War II in 1945).

Major social changes include the devolution of power to local governments; the amendment of the health care system began in April 2000; the reorganization of the national government begun in January 2001; and the enactment of the Information Disclosure Law this April.

The cumulative effect represents a sea change from large to small government, from governmental to private leadership, and from central to local. The Koizumi Administration

is trying to initiate even more dramatic structural reforms.

These changes were in part due to the tremendous social developments that have occurred over the past 20 years – the end of Japan's high economic growth and resulting changes in its industrial structure; the heavy concentration of the population into large cities and the consequent depopulation effect in local towns and rural areas; the onset of environmental issues arising from changes in production and living patterns; a low national birth rate which is resulting in the rapid aging of the population; an increase in new cultural and social issues as a result of the influx of foreigners; the rise of developments related to juveniles following changes in their values; and the collapse of Japan's educational system.

As Japanese society has been undergoing these profound changes, the government has responded as best it can. Companies have also responded to market needs as fully as possible, but there are some limits to what they can do. Problems born of social change have not only proven insoluble but are becoming even more serious, resulting in confusion in Japanese society. Japan's NPOs must face those issues squarely.

What kind of role should Japan's NPOs play in the future? Although

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most NPOs are still in the development stage, they should propose measures aimed at resolving Japan's social issues, the creation of new social projects on their own initiative, and the establishment of new and equal cooperative relationships between the government and private companies.

(2) Enactment of the Specific Non-Profit Activity Promotional Law and new initiatives taken in its implementation

When discussing NPOs in Japan today, it is helpful to understand the so-called NPO Law, the Specific Non-Profit Activity Promotional Law, enacted in March 1998. This law relatively easily awards legal status to organizations involved in certain non-profit activities – a status long sought by civic activists.

Japan's civic organizations grew steadily in the latter part of the 1980s but most were volunteer groups, and not allowed to register as a principal party to a contract. Not surprisingly, their organizational development remained severely limited.

Their exclusion prompted civic groups and researchers to press for the establishment of non-profits as legal entities, capable of taking advantage of the autonomy of private organizations. Their campaign was bolstered by the gratitude of

the public for the energetic activities by volunteers and civic organizations following the destructive 1995 earthquake in the Hanshin (Kobe) and Awaji areas. After considerable debate in the Diet and social discourse, a bill was unanimously adopted in December 1998 that would allow for the registration of non-profits as legal entities. Henceforth, the official name for an NPO was the awkwardly-named Specific Non-Profit Activity Juridical Person.

The new law's scope was wide-ranging. Unlike conventional public interest corporations (corporate juridical persons and foundations), social welfare juridical persons, school juridical persons, and similar groups are doubly bound by the government's hierarchical structure. (As a juridical system, the conventional public interest corporation status remains unchanged, thereby resulting in a confusing dual structure.)

The law is significant, because as soon as civic organizations are accorded legal status, they are allowed to carry out social projects as a principal party to a contract. For Japanese NPOs, as important was the official recognition that private and independent non-profit activities are indispensable to society.

(3) Present status of NPOs and the trends concerning them

In the nearly three years since the implementation of the NPO Law, some 5,000 Japanese NPOs have emerged. Most recently, the number of NPOs has increased at the rate of 150 per month. Anecdotal evidence indicates that a significant number of them are involved in the fields of medicine, health and welfare, and related to the start of the new health care insurance system that was implemented in April 2000.

Since the new NPO Law was implemented, organizations can more easily attain legal status. But not all have secured legal status. That is because organizations that are small in scope, have no paid staff, and have never signed large business contracts, typically see no need for securing such a legal status. According to a September 2000 survey by the Economic Planning Agency (now a part of the Cabinet Office), about 88,000 voluntary organizations engage in civic activities.

A survey of those organizations revealed that 43 percent of their activities are in the medical/health/welfare fields, followed by environmental preservation and promotion of cultural/art/sports activities, followed by international cooperative activities.

(4) Desirable measures to strengthen NPOs

In the future, Japan will increasingly look to NPOs as the vehicles to deal with change during a transitional period in Japanese society and to pave the way to a new era. Every August, government ministries and agencies sit down to establish budgets for the following year. This year they are including proposals concerning certain NPOs in hopes of enhancing employment opportunities.

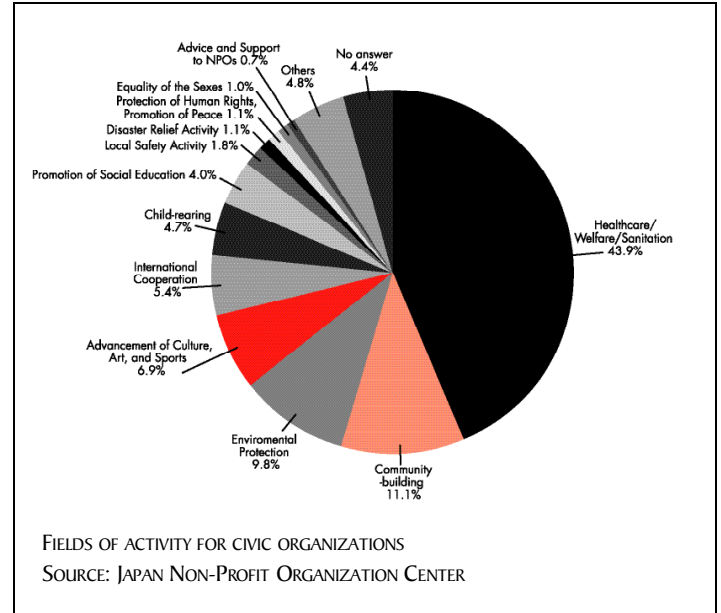
That said, the base of NPOs in Japan is at present not strong. In reality, their ability to provide employment opportunities is limited. In the future, therefore, efforts should be made to strengthen these areas. NPO support centers that are being created in various locations can help, but the funding and staffing of those support centers themselves are still inadequate.

Regarding funding sources, an amendment to Japan's tax system pertaining to donations is absolutely indispensable to the future development of NPOs. Some 800,000 American non-profits reportedly receive preferential tax treatment because contributions made to them are tax-deductible. By contrast, in Japan, only social welfare juridical persons, school juridical persons, and a handful of corporate juridical

persons and foundations (a total of 1,000), enjoy such a benefit.

There is not even a mechanism by which new NPOs can qualify for such a status. Immediately following the enactment of the NPO Law, civic organizations worked together to lobby for tax-exempt status for civic groups. In March 2001, the law was amended to accommodate them. As a result, effective October 2001, when individuals or corporations makes a contribution to a NPO approved by the National Tax Agency, they will be eligible for certain tax exemptions. But the governmental regulations will likely prove too stringent to be of much help to most NPOs. Additional work is needed to further ease requirements for the future benefit of NPOs.

But even if the requirements are relaxed, they aren't likely to translate to a big jump in donations right away, because to date no such ethos has existed in Japanese society. Japanese will have to become



aware of the importance of NPOs and feel that they want to participate in those activities themselves in the future. But things will not change overnight. Therefore, in addition to improving their management capabilities, Japan's NPOs must propose bold plans for the solution of social issues, execute them effectively, and produce results.

If they succeed, I am convinced that there will be a steady increase in the public's understanding of and sympathy with NPO activities, so that the level of public participation will steadily expand. ■

Yoshinori Yamaoka, Executive Director, Japan NPO Center, Professor, Hosei University

Can Wireless Lead Japan to a Competitive Edge?

by Diane Cornell, Cellular Telecommunications & Internet Association

The Japanese economy has experienced a rocky ride over the last few years, and its communications sector has generally suffered through the same trials as the high-tech sector overall. The July issue of this newsletter carried an article on one of the bright spots of Japan's economy—the spectacular success of the mobile wireless market, particularly DoCoMo's i-Mode service. Indeed, this wireless internet service has grown far faster than predicted, leading many analysts worldwide to point to i-Mode as the most commercially successful wireless internet access service on the market today.

This success raises the question whether i-Mode, and the Government policies which helped enable it to come to market, suggest a model that could help Japan achieve a competitive edge in the economically vital communications sector, and perhaps more broadly in the high-tech world. There is no question that the Japanese wireless market has proven to be far more dynamic than its wireline counterpart, which clearly suggests some lessons for communications policymakers. But the question remains whether the Japanese wireless

model is sustainable in the long run—or whether it simply looks good compared to the sedentary wireline marketplace.

It is certainly true that the wireline market in Japan does not measure up especially well to international benchmarks, particularly in the context of facilitating Internet access. While the monthly subscription fees are comparable to other countries, the once-in-a-life time installation fee of more than

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¥72,000 (slightly less than \$700) is dramatically higher than in Japan's major trading partners.

More importantly, its usage-sensitive charges are more than in most developed countries, and dramatically more than the United States, making computer access quite expensive for the average citizen. Not surprisingly, wireline Internet penetration is less than 20 percent in Japan, compared to more than 50 percent in the United States. Most analysts would point to the continued market dominance of NTT as the driving factor behind these market characteristics.

The Japanese wireless market has proven to be significantly more competitive than its wireline counterpart—resulting not only in more rapidly declining prices than in wireline, but also in innovative services like i-Mode. Indeed, these factors have resulted in wireless fast becoming a substitute for wireline service in Japan, both for voice and data. The wireless competitors have picked up a lot of voice traffic that would otherwise have gone over the

wireline network by eliminating the daunting up-front fee of over \$700 USD charged for a landline phone line, and having reasonable per-minute charges.

Moreover, DoCoMo dominates the internet access market by offering an “always on” internet access service through i-Mode, with a pricing structure far more attractive than the expensive internet access offered by NTT on the wireline side. As a result, more Japanese consumers turn to i-Mode for internet access than to their wireline computers, and DoCoMo's subscriber base has exploded.

These comparisons suggest that Japanese policies for wireless communications provide a better model for consumers and economic growth than exists on the wireline side. The

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Can Wireless Lead Japan to a Competitive Edge?

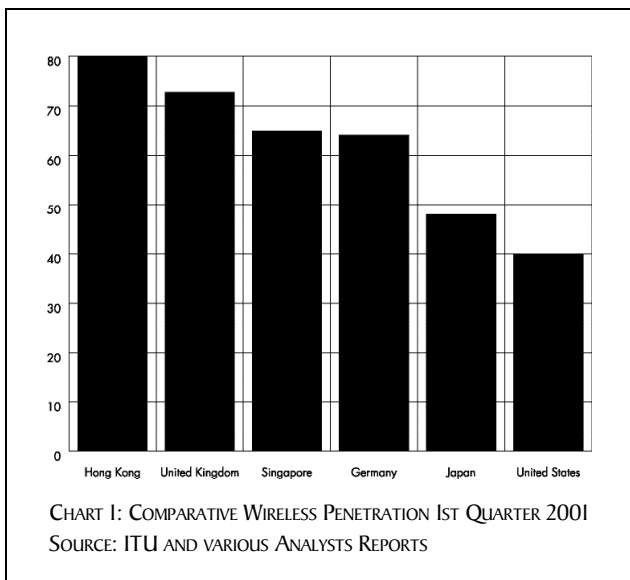
relative success of wireless compared to wireline in Japan is most likely attributable to the presence of several carriers in the market who each have the essential inputs they need to compete. The Japanese Government has given the two smaller competitors very large

better than its wireless counterpart in Japan. But, before concluding that the wireless market provides an effective and sustainable model for the communications and other high-tech sectors in Japan, it is worth considering how this success compares to other international wireless markets.

Despite the success of i-Mode, as Chart 1 indicates, mobile wireless penetration in Japan is lower than most European countries, Hong Kong and Singapore, although it is slightly higher than in the United States. Many analysts have noted that wireless prices in Japan are still relatively high compared to its major trading partners. A monthly price for 120 peak minutes is approximately \$75 USD in Japan, compared to \$53 in the United Kingdom, \$45 in the United States, \$40 in France, and \$29 in Hong Kong. U.S. users now have access to monthly plans which offer unlimited off-peak minutes for less than \$30 per month, with enormous buckets of "anytime" minutes available for a few dollars more.

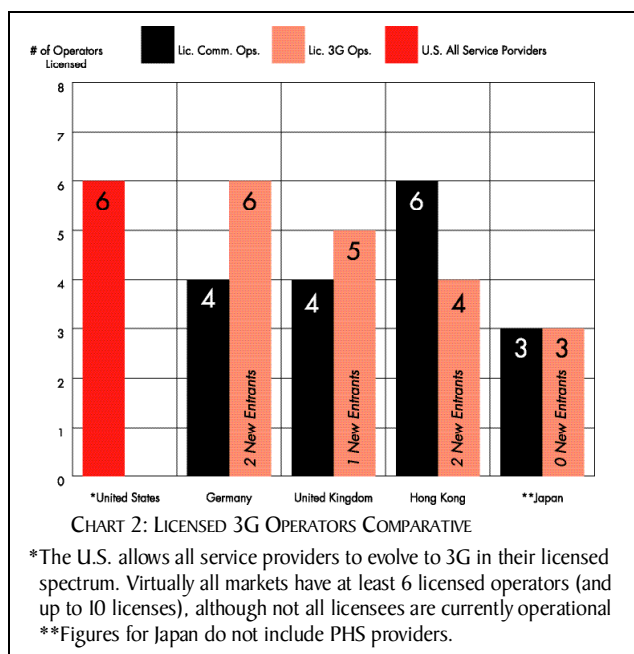
The most likely explanation for these differences is that Japan has fewer wireless carriers than its major trading partners. There are only three major commercial mobile wireless providers licensed in Japan. By contrast, the U.K. has four providers for digital cellular service and five licensed for next generation "3G", Germany has four currently operating and six licensed 3G operators, and Hong Kong has six digital operators, with four for 3G service (see Chart 2). In the United States, 75 percent of consumers have access to five or more providers, and 46 percent have access to at least six providers. Indeed, virtually all the major developed countries have licensed more than three competitors for their wireless markets.

Japan's wireless markets could be expected to grow even faster if more competitors were licensed, and given the tools they need to build out their wireless networks. The experience in other countries has been that prices declined significantly after multiple carriers were licensed, particularly when more than three carriers were competing in a market. Consumers have responded to lower prices by signing up faster for mobile service and talking more on their wireless phones. For example, in the United States the proliferation of monthly "bucket" plans has resulted in a dra-



blocks of spectrum (KDDI even has more than DoCoMo), ensuring some leveling of the playing field. And the Japanese Government has afforded the wireless companies unprecedented flexibility in the technical standards they may deploy, allowing for increased competition in service offerings and quality of service. This relatively light regulatory hand no doubt contributed to the spirit of innovation that gave rise to i-Mode.

It is unquestionably true that the wireless market is performing far



matic increase in average monthly usage per customer, to almost double the level of only two years ago.

Japan's wireless market has been a success story—so far. But part of its success is that wireless is able to shine by comparison to the relative inflexibility and high costs of the wireline market. I-Mode has far exceeded expectations, but it is less clear if it would be as popular if PC penetration and usage were more prevalent in the Japanese wireline world. Further, the future of i-Mode is clouded by the fact that its data speeds are relatively low, and while they are adequate for cartoon characters and sports scores, they offer limited data capability. More importantly, i-Mode's technology is unique to Japan, so that it loses the scale

economies of more widespread deployment in other countries. There is a very real risk that the Japanese wireless phenomenon could look more like France's ill-fated Minitel experience than an evolving and vibrant market in a few years.

Japan's wireless experience nevertheless offers some lessons that could serve the country well if applied to other parts of its communications market. Japan's wireless carriers have attracted a significant percentage of the communications minutes, diverting them from the less nimble wireline operators. And the wireless carriers have introduced dramatic innovations in service offerings and pricing models that have proven very attractive to consumers. Much of this success can be attributed to the existence of multiple carriers who are increasingly being permitted the flexibility to introduce whatever technologies and services they need to meet consumer demand. In addition, while DoCoMo has some advantages over its wireless competitors, it does not have the dominant position its

affiliate NTT enjoys in the wireline market. DoCoMo's track record seems to confirm that even a major market player performs better when it is forced to compete in the marketplace.

Japan would do well to learn from the successes of its wireless market—and from the experiences of other international wireless markets. Indeed, it should build upon those lessons to ensure that success is sustainable in the long run. If more than three wireless competitors were allowed in the market, innovation and price competition would increase, to the benefit of consumers. If those competitors are given the flexibility to deploy whatever technologies and service offerings they choose in response to consumer demand, creative offerings like i-Mode will be the rule, not the exception. These lessons provide a future roadmap not only for wireless, but for the communications sector overall. Market growth and innovation should be the norm, not the sensation. ■

Diane J. Cornell is Vice President for Regulatory Policy at the Cellular Telecommunications and Internet Association (CTIA) and former Associate Chief of the Wireless Telecommunications Bureau of Federal Communications Commission (FCC).

Japan Business Dialogue

KKC's monthly program featuring Japanese experts on the economy.

"Deregulation of Electricity Industry In Japan: A Corporate View"

*Toshihiko Furuya, speaker,
Tokyo Electric Power Company
(TEPCO), July 18, 2001*

Japan's electric power industry's experience with competition began with the 1995 deregulation of the retail electricity market, explained Toshihiko Furuya, General Manager of the Tokyo Electric Power Company (TEPCO) office in Washington, DC.

Japan has ten general electric utility companies that are privately held and vertically integrated, the largest of which is TEPCO, which supplies 30 percent of Japan's total electricity consumption, more than that of the U.K. or Italy.

Between 1996 and 1999, 41 independent power producers – many of them major petrochemical and manufacturing companies – entered Japan's wholesale power market. Additionally, nine new entrants – mostly subsidiaries of well-established companies – have also entered Japan's retail energy sector. Finally, foreign companies, including Enron of the United States, have also expressed their intent to build several thermal coal-fired power plants in Japan.

Japan's energy needs are met by five sources of power – oil (11

percent), hydro (11 percent), coal (15 percent), liquefied natural gas (25 percent), and nuclear (36 percent). The current partial liberalization of the Japanese electric power industry will be reviewed in two years, Furuya said, emphasizing that Japan must be prudent in designing the market in order to secure a reliable power supply.

Due in large part to the fierce competition in the energy sector, Japanese power companies have been working hard to develop their non-core business. Indeed, Furuya said, TEPCO's new president, Nobuya Minami, set the ambitious goal of having non-core business (gas distribution, service, information and communications, household real estate) account for 10 percent of TEPCO's total revenues by 2005.

Furuya said TEPCO believes that deregulation itself will provide them with a good opportunity to expand business. Moreover, TEPCO is increasingly focused on building its overseas consulting services, such as those in China, Malaysia, Russia and Jordan, as well as in investment projects in Vietnam, Australia, Taiwan and the U.S. As a result of overseas business ventures, Furuya said TEPCO's corporate culture is changing. ■

Publisher, Keizai Koho Center

Director, Hideaki Tanaka
kkc1@kkc-usa.org

1900 K Street NW
Suite 1075
Washington D.C. 20006
202 293-8430

www.kkc.or.jp

Keizai Koho Center (KKC) is an independent, non-profit organization designed to promote the understanding of Japan's economy and society at home and abroad. Its financial resources are derived entirely from the private sector.

KKC fosters a deeper understanding of Japan's basic social structure. Furthermore, it conducts public affairs activities to improve the Japanese people's recognition of Japan's global role.

The views expressed in this newsletter are of the contributors and do not necessarily represent those of the Keizai Koho Center.