SUCCESS STORIES JAPAN

Helping Non-Japanese Companies Succeed in Japan

November 2007

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ARE JAPANESE MANAGERS BETTER AT CULTIVATING IP?

The debate about whether Japanese managers are better at cultivating corporate intellectual property continues this month in the second of a two-part article from a published author in the field. Read Andrew Shipley's views on how Japan manages IP and what that may mean for the value of leading companies — Page 5.

A Merged Company Tries to Raise its Profile

The Nokia Siemens Networks Japan Story

Success Story

Technological developments and the speed and nature of consumer adoption in the mobile and broadband markets in Japan often indicate the direction those same developments will take in Europe and other markets. So, in a truly global market like telecom, the strategies and activities of mobile equipment and infrastructure providers to Japan's major carriers hold significance that is out of proportion to the actual size of the providers' Japan business.

That's why the state of affairs in Japan of the newly-formed Nokia Siemens Networks (NSN) is of interest. The joint venture firm is less than a year old and only now beginning to realize the most obvious synergies in its approach to the telecom market in each country in which it operates. According to Yasushi Ozu, NSN's Japan head, the task of bringing Nokia and Siemens together here has been made easier by the fact that Siemens had only a handful of network group employees in Japan. This means the firm had to spend very little time worrying about the proper type of organizational structure to bring the two companies together. (The combined entity now employs a total of 250 in Japan.).

This could prove critical, because even though Nokia and Siemens did not mention Japan at all in the announcement of their global merger, Japan's carriers are again experimenting with innovations in wireless, fixed-mobile convergence (linking together the features of landline and mobile phones) and next-generation mobile technologies in a way that offers substantial risks, and rewards, to telecom equipment providers who link up with them in the adoption of any new technology.

APPROACH: The firms each bring one key local relationship to the table — Nokia has long been a supplier of critical technology to J-Phone even before it became Vodafone and later Softbank Mobile (after Vodafone sold the business in 2006). Softbank Mobile's base station business accounts for 98 percent of NSN's Japan business, with a small wireless relationship with NTT DoCoMo accounting for the remainder, according to Ozu. Meanwhile, Siemens brings along its existing relationship with NEC that is based primarily on a leading global product for WCDMA mobile base stations. Siemens also has a stronger relationship with Japanese government ministries at various levels, says Ozu. Together, they hope to leverage different product offerings and become suppliers not only to incumbent carriers but also a group of emerging car-

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A Merged Company Tries to Raise its Profile

The Nokia Siemens Networks Japan Story (Continued)

riers that will be created in the coming years to provide WiMax wireless service in Japan. "Now we can sell fiber to the home [known as FTTH], IP backbone equipment, broadband access and VDSL [very high-speed digital subscriber line]," explains an excited Ozu.

The opportunities to raise NSN's Japan profile are assuredly out there [the firm does not disclose its level of Japan sales]. The company already serves Japan's VDSL market through its recently-acquired Korean subsidiary Dasan Networks. And it is primed to compete in the market for indoor base station products with a newly-launched interface that works with multiple vendors' equipment and helps provide a signal in very tall buildings as well as Japan's many underground pedestrian areas.

"In FTTH, NTT East and West are the big buyers but they're still only buying from Japanese suppliers like Mitsubishi Electric, yet the market is enormous," Ozu says. "So we're looking for a Japanese partner" that will help NSN break into supplying FTTH to NTT. In the market for IP transport and IPTV network equipment, "everyone knows that the operators must have their backbones upgraded," notes Ozu. And even though those upgrades were delayed "due to the after-effects of the internet bubble, we expect a whole new cycle of spending in this area beginning in 2008."

Any carrier's existing network might already have a combination of routers from Cisco, say, working over fiber networks from Alcatel Lucent or Nortel, in a very open architecture that Ozu believes makes it easier for other equipment providers to join in. "We have a very good chance with the fixed-line carriers," he feels. And on the wireless side, he notes with glee that Softbank Mobile's heavy investment (since it acquired Vodafone) in new handsets and a greater number of base stations is already under pressure from its success. "Their network was intended for eight million users and they already have ten million on their way to twenty million," he explains. "This means they will have to triple their network size by 2010."

Still another opportunity in wireless equipment that NSN is gearing up for locally, according to Ozu, is to serve the new carriers that will be formed to operate the two new nationwide licenses for high-speed WiMax that will be awarded soon, perhaps by the end of 2007. WiMax allows for internet access, mobile gaming and the use of internet appliances while in a moving vehicle, car or train, where the more commonly-installed WiFi technology only provides internet access around a fixed hotspot. Japan's government has smartly decided to limit the investment of incumbent carriers in new WiMax carriers to thirty-three percent, meaning that two new carriers will be born. Already alliances are forming -- KDDI is linking with Kyocera, Intel and railway operator JR East; NTT DoCoMo is partnering with ACCA Networks, Tokyo Broadcasting System, Keihin Electric Railway and JP Morgan; Softbank Mobile intends to work with eAccess, Goldman Sachs (which is a large shareholder of eAccess) and Singapore's Temasek Holdings; and Carlyle Group-controlled Willcom may also be a leading contender. "The Japanese government will require each of the new carriers to deploy at least 10,000 base stations within three years of getting the license," Ozu estimates based on the government's stated desire for ninety

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SUCCESS STORIES JAPAN

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A Merged Company Tries to Raise its Profile

The Nokia Siemens Networks Japan Story (Continued)

percent coverage within 3-6 years. [The government is also going to award a third, smaller license for the deployment of Wi-Max in more remote areas of Japan which cannot be reached by FTTH because they are so far from the carrier's central office, but pursuing this business is of less interest to NSN].

Success Story

And then there's the potential for LTE in Japan, or what some call 'Super 3G'. This is an area of great interest to NSN not only for its sales potential in Japan, where DoCoMo is leading its development, but also because the entire world will be watching to see which standards carriers select and how business models develop. Equipment providers like NSN that develop products that end up being adopted by major carriers deploying Long-Term Evolution (LTE), such as DoCoMo, will likely be able to market very similar products in a great number of other countries in later years, as these countries follow Japan's lead in deploying Super 3G. "From 2010, we will try to develop LTE products," reports Ozu, "and Siemens is already offering demonstrations of a prototype LTE product it has developed." An increasing number of carriers from Europe and the US have also recently shown interest in LTE.

Much of this opportunity is speculative at this point, however, as today NSN Japan's only major business is in base stations, where it is generally known to be one of Japan's three top vendors (the others being Ericsson and NEC). To build its business in these other technologies, it will have to hire more staff and compete in Japan with other strong global infrastructure providers like Ericsson, Alcatel-Lucent, Motorola, emerging Chinese competitors like Huawei and ZTE, and important players like Cisco.

NSN Japan also may not be finished feeling the effects of the politics of its parent companies, as Siemens has been consolidating divisions globally and both Nokia and Siemens have reduced headcount in Europe in favor of markets like India. Such moves could affect where some key company technical decisions with Japan impact get made.

GOING FORWARD: So far, Nokia and Siemens appear to be choosing their priorities cooperatively and working reasonably well together both at the parent level and in Japan, in contrast with last year's combination of Alcatel and Lucent, which has experienced some conflict. "Compared to Alcatel and Lucent, we have had no major changes in personnel and we have a deeper product portfolio," Ozu says, toeing the company line. "In the case of Finland, Nokia doesn't have a large domestic market to protect like Alcatel does, it went out to the global market very early on and thinks all the time about it." But also, he jokes: "I think Finns and Germans work better together than Americans and French."

Turning back to Japan, Ozu explains that "Japan's market is very special compared with other markets. All of the operators, especially the NTT group, have technical teams and they always want to have very detailed technical discussions and vendors need to have the same level of knowledge or even more. So [we] have been looking for sales and system engineers who have experience at a high technical level, and even better if they have R&D experience in Japanese vendors. We also will need a lot of quality control people with strong technology backgrounds who can work with our partners."

NSN's relations with Japanese government ministries will also increase in importance, as the combined Nokia Siemens will increasingly have to show its partners that it can have as much influence with local standards-setting bodies as an Ericsson or a Cisco. That influence comes in part from being the vendor with not just marginally-better technology, but technology that's clearly a step above all others.

"Regionally, we're looking to grow faster than the market. And given that NSN has a #2 position globally, we should be able to achieve the target in Japan as well," Ozu feels. "While we cannot expect to become the overall leading vendor in Japan because NEC and Fujitsu are so large that it would take a major acquisition for us to do so, our goal is to be the #1 foreign telecom infrastructure equipment vendor in Japan. And also to have customers and major business in multiple segments, not just one."

JAPAN INSIGHT

SHIRE'S JAPAN BUSINESS GROWS WITHOUT ON-THE-GROUND PRESENCE

Shire Pharmaceuticals has eschewed an on-the-ground presence in Japan but the company's business in the world's second-largest pharmaceutical market is becoming increasingly significant, *SUCCESS STORIES: JAPAN* has learned.

Earlier this year, the mid-sized UK-based specialty pharma firm launched Replagel, an enzyme replacement therapy for the treatment of Fabry disease that Shire currently markets in Europe, in a licensing agreement with DaiNippon Sumitomo Pharma. The drug was first submitted for approval in Japan in 2002. And just in October, Shire announced the Japan approval of Elaprase, another enzyme replacement threrapy for Hunter syndrome, that will be marketed starting in 2008 by US-based Genzyme Japan under the companies' global licensing arrangement. Both Replagel and Elaprase are products originally developed by the US-based biotech firm Transkaryotic Therapies that Shire acquired in 2006.

Back in 2001, Shire was reported to be very interested in establishing operations in Japan, and according to Rolf Stahel, its CEO at the time, it was also considering acquisitions of domestic Japanese pharma companies. But that has all changed in recent years, as the company has pursued licensing arrangements in Japan for each of its drugs individually and has not made any local acquisitions.

Since 2003, Shire has had an arrangement with Bayer Yakuhin, a unit of Germany-based Bayer Healthcare AG, for the Japan marketing of Fosrenol, a drug that treats end-stage renal disease, and Bayer Yakuhin has undertaken successful Phase II and Phase III clinical trials in Japan such that it now expects approval by the Ministry of Health in 2008. Also since 2003, Shire has had a partnership in place with the pharmaceutical division of Kirin Brewery to market Agrylin, a treatment for essential thrombocythaemia, a bone marrow disorder associated with excessive production of blood platelets. Kirin's pharmaceutical division, with an orientation towards the haemotology (blood) market, has worked to get the product approved and sales are expected beginning in 2011. And of course, sales of the company's Zeffix (Epivir) drug, "a key component in most of the HIV combination treatment regimes" according to Shire, increased by fourteen percent in 2006 over the prior year "due to strong growth in the Korean, Japanese and Chinese markets," according to Shire's 2006 annual report.

Additional expansion in Japan is likely to include the announcement of a Japanese partner to market Mezavant, a once-daily oral treatment for ulcerative colitis licensed by Shire from Italy-based Cosmo S.p.A. Shire applied for this drug's approval in the US, Canada and Europe in 2005 and 2006.

Shire Pharmaceuticals, which grew its revenue twelve percent globally to $1.8 billion in 2006, has achieved much of its growth in recent years via acquisitions since 2000 including those of Canada-based Biochem Pharma,

More Japan Insight on Page 8

MAJOR JAPAN CONFERENCE EVENTS

Hokkaido Business	Sapporo	11/07	Fax: 011-81-11-708-6529

A great way to connect with the re-energized business community in Northern Japan. 16,000 attendees and 200 exhibitors expected.

AsiaBev 2007	Tokyo	11/07	Fax: 011-81-3-3989-8727

Serving beverage marketers and packaging, equipment and service providers.

Image Technology	Yokohama	12/07	Fax: 011-81-3-3368-1519

A technical exhibition that combines cameras, image processing equipment, as well as output devices such as displays and screens. 250 exhibitors expected.

Eco Products	Tokyo	12/07	Fax: 011-81-3-5255-2860

Household products and services that use recycled materials, save energy, or offer increased efficiency in their use of resources. 140,000 attendees expected.

Tokyo Auto Salon	Chiba	01/08	Fax: 011-81-3-3368-0577

The event for auto detailing, car parts, systems, electronic products and accessories. 250,000 car lovers attended last year.

Souvenir Show	Tokyo	01/08	Fax: 011-81-3-3311-9502

A great way to understand Japanese consumers and consumer marketing, with a full display of popular gifts, hobbies, premiums and incentives.

Supermarket Trade Show	Tokyo	02/08	Fax: 011-81-3-3255-4829

Food, systems and equipment for retailers, convenience stores and supermarkets.

Osaka Automesse	Osaka	02/08	Fax: 011-81-6-6458-3199

One of the largest auto shows in Japan, with over 200,000 attendees expected.

Hoteres 2008	Tokyo	03/08	Fax: 011-81-3-3434-8076

Combined show for the hotel, catering and food service equipment industry, with emphasis on hotel, entertainment and leisure services.

Tokyo Anime Fair	Tokyo	03/08	Fax: 011-81-3-5298-2482

Influential cultural fair including on-stage events, competitions, anime creators.

Gourmet & Dining Style	Tokyo	04/08	Fax: 011-81-3-3843-9830

This show focuses on the dining table as a point of departure for lifestyle trends.

Sea Japan	Tokyo	04/08	Fax: 011-81-3-5296-1018

Biennial show that highlights marine equipment and logistics technology.

Japan Meat Industry Fair	Tokyo	04/08	Fax: 011-81-3-3663-2015

A rare look at Japan's highly-complex food distribution system, featuring over 100 exhibitors of meat and fish processing and packaging equipment.

All telephone numbers assume the person dialing is located outside Japan.

A SPECIALIST OFFERS ADVICE

Japanese Management Leads to Edge in IP Cultivation

By Andrew Shipley, Economist and Author (Part Two)

Part One last month discussed how Japanese firms are both more protective of their existing IP assets, and more focused on thinking about them strategically so as to maximize the revenue they can gain from them.

But the role Japanese management plays in cultivating valuable research is frequently overlooked. While, during the bubble years of the late 1980s, foreign observers uncritically hailed Japanese executives as brilliant and innovative gurus, in the following decade of financial crises and plummeting share prices, derision replaced admiration. Critics blamed lifetime employment systems and managers without specialized knowledge for dragging the corporate sector into a money-losing abyss.

Now scholars on both sides of the Pacific say market watchers have over-reacted in their condemnation of Japanese managers. They even suggest that traditional management techniques are providing Japanese firms with an edge in intangible asset cultivation.

Hiroyuki Itami of Hitotsubashi University speaks with an animated candor that may come from his many discussions with policy makers. Itami served on the Information Technology Strategic Headquarters and the Biotechnology Strategy Council of the Prime Minister's Office. He can flip conventional wisdom regarding Japanese management on its head with the careless ease of a grizzly bear toying with its prey. Never shying from an argument, he appears to relish rebuking views held by many overseas investors about Japanese firms during a recent interview.

The second edition of his classic 1980 treatise *Keiei Senryaku no Ronri* (The Logic of Corporate Strategy), which was translated with the collaboration of Thomas W. Roehl and published as *Mobilizing Invisible Assets*, established his reputation in the late 1980s as the father of invisible asset management. "My concept of invisible assets is broader than the usual concept of intangible assets, which tends to be colored by the accounting concept of the same name," says Itami. He refers to information-based assets such as consumer trust, brand image, technology, corporate culture, and management skill as invisible assets. Arguing that they are the most important resources for long-term success of a firm, Itami compares visible assets to the brushes, canvas and paint of a painter, and invisible assets to the ability to create a masterpiece.

Japan has a competitive advantage in the cultivation of such assets, which will enable it to prosper even when faced with low-cost Chinese production, he argues. In fact, many Japanese firms are re-thinking a widespread shift to production on the mainland. "Canon is already bringing factories back from China," he says. This firm is investing about ¥80 billion in a domestic toner cartridge plant in Oita, that started production from January 2007. Previously, Canon's main plant for such products was in Dalian, China. Former Canon president Fujio Mitarai had repeatedly voiced his commitment to relocating plants back to domestic locations. "In the field of advanced technology, it is often very inexpensive to do production in Japan," Itami notes. Much of the work is automated, driving down labor expenses. In addition, Japan enjoys a highly developed network for the supply of advanced parts. Since many firms order such inputs, even if individual orders are of a small quantity, parts suppliers can boost production, and keep costs down, he adds.

Itami cites increased discussion of corporate brand management as evidence of rising interest in invisible assets at Japanese firms. From April 2000 Hitachi, Ltd. embarked on such a strategic effort, announcing a slogan 'Inspire the Next'. Acknowledging that Hitachi brand awareness had weakened among young Japanese, the firm launched a direct mail and newspaper advertisement campaign to raise its profile. The firm stressed its origin as a venture capital firm and its possession of cutting-edge technology. The results were dramatic. Its ranking among engineering students as a desirable place to work jumped from 72nd in a 2004 *Nihon Keizai Shimbun* survey all the way to 14th. Hitachi also held symposiums in three Chinese cities in October 2004, to raise awareness of its brand in this crucial market.

Invisible asset management among Japanese firms is much different than at US firms, argues Itami. Japanese firms try to nurture invisible assets within the firm. US firms cultivate internally much less, relying instead on the market. "The notion that you can buy invisible assets from outside, is very foreign to Japanese firms," he said. Of course, not all US firms neglect cultivation of invisible asset, he concedes, citing IBM and Intel as two examples of firms actively trying to nurture and develop invisible assets internally. However, many US firms do not give such activities a high priority, he feels.

On the other hand, Itami points to Matsushita Electric, which has developed its own

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FROM THE EDITORS

'A JAPANESE STYLE OF CONDUCTING BUSINESS'

The media has reported on the recent suit by a US-based Dentsu America executive against Dentsu and his Japanese boss for creating a hostile work environment for him. Specifically, the executive alleges that his Japanese boss forced him to accompany him to a local brothel while on a business trip, and repeatedly demanded that he have sex with prostitutes while there.

One part of the lawsuit claims that the Japanese boss "maintained that having sex with prostitutes was a 'Japanese' style of conducting business."

Without commenting on the outrageous nature of the charges or whether any or all of the accusations might be true, we feel it is important to point out that for decades executives and managers of Japanese companies have been major consumers of erotic services, including prostitution, in many of the countries in which they do business. This is a fact confirmed both by the personal observations of our staff in several countries and corroboration by more than a few of our sources over the years.

But the sad truth is, Japanese managers are not unique in patronizing such services. A large proportion of the clients for erotic services and prostitution in major business centers around the world are managers and executives of companies from many different countries. Japanese executives do not have any higher propensity to engage in such activity than businesspeople of any other nationality. Global executives are major consumers of such services, period, because they have the means and the opportunity.

Such behavior as is alleged in this well-publicized lawsuit is not in any way a 'Japanese' style of conducting business. Mean and ugly people exist in Japan as they do in every country. Sad fact, but true.

Japanese Management in IP Cultivation

By Andrew Shipley (Part Two — Continued)

large-scale integration (LSI) for their plasma TV within the firm. "The technology they use in designing this has been nurtured, developed, and cultivated with the firm for the last twenty years," Itami says. And not just large firms are accumulating invisible assets, he adds. The only strength of many small- and medium-sized firms is their know-how and craftsmanship, said Itami, who served as chairman of the Management/Assistance Council of Small- and Medium-sized Business Firms at the Ministry of Economy, Trade, and Industry (METI). Itami just headed a committee to select the best three hundred small companies in Japan. He points to Okano Industrial Corp., a very small operation specializing in pressing technology, as a success story. The firm supplies needles to Terumo Corp., a major medical-equipment maker. Okano Industrial has succeeded in manufacturing needles so small that pain is greatly eased during injections. Many small Japanese firms have seventy percent of the world market in specified, minute niches, he adds.

Attention to minor details by workers on the factory floor or by salesmen in the marketplace place gives Japanese firms a competitive advantage. "The basic conviction, sometimes very implicit, of many Japanese managers is that invisible assets are cultivated by doing things correctly, day after day." Itami even argues that traditional Japanese corporate governance, long criticized by many foreign investors, is well-suited for managing invisible assets. "Managing a firm for the sake of employees first, and for shareholders second, that's the best practice," he provocatively declares. What is the incentive of workers to accumulate invisible assets "if they know the company is run for shareholders?" Itami asks.

Employees are also more likely to cooperate and share information if they are assured of keeping their jobs. Long-term employment and limited labor market mobility influence the behavior of Japanese employees, and therefore it is much easier for the Japanese firms to accumulate invisible assets internally. This advantage will be maintained in the future, Itami argues.

Japan has lagged in some industries, such as software development, but Itami points to language, rather than mistaken management techniques, as the reason for Japan's weakness in many of these cases. The Japanese language, with its hundreds of Chinese characters, demands much more computing power than English. At the early stages of personal computer (PC) development, PCs that could handle Japanese were much more expensive than ones built to use English software. This price differential resulted in a much slower diffusion rate for PCs in Japan. A computer with Japanese software cost three times more than a computer with English software with the same functions at the beginning of the 1990s, Itami explains. While there is no price difference now, he argues it will be difficult to overcome the advantages enjoyed by US software makers due to their huge market shares. But one exception he points to is gaming, where language is not an issue.

Despite traumatic restructuring of the banking sector during the 1990s, Japanese firms maintained their competitive positions in many fields. Throughout the 1990s, spending on research and development by Japanese firms continued to rise, from ¥7.2 trillion in 1989 to ¥11.6 trillion ten

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A SPECIALIST OFFERS ADVICE

Japanese Management Leads to Edge in IP Cultivation

By Andrew Shipley, Economist and Author (Part Two — Continued)

years later. Even as a percentage of sales, spending on R&D was up, from 2.6 percent to 3.1 percent during the decade, suggesting that firms were putting an even higher priority on their R&D programs than earlier. The number of researchers in the corporate sector rose from 295,000 to 431,000 over the same period.

Fujitsu alone has more than one thousand professionals working in its laboratories. Now that problems with the financial sector are getting worked out, Japan's industrial strength is once again on the surface, Itami argues. "Japan is becoming a sourcing country of many very important parts and materials," he says. In application-oriented semiconductor chips Japan is still leading the world, for example. Meanwhile, Japanese production of high-performance steel and high performance chemicals is continuing to rise, he adds.

JFE Steel, the leading steel company in Japan in terms of operating earnings, focuses on high performance steel to a much greater degree than its Asian competitors. Fully twenty percent of the company's production is not available from steel mills in China or South Korea. These 'Only 1, Number Products' include NANO Highten (a nanometer level grain-controlled high tensile steel developed by JFE) used in fuel-efficient cars. The company also produces very high grade electric steel, which has superior electromagnetic characteristics and is used in high efficiency motors, like those for hybrid cars. JFE also uses a thermo-mechanical control process to produce heavy plate steel for container ships.

Another seventy percent of JFE production is made up of high value-added steels such as hot dip galvanized steel sheet for automotive outer panels, regular high tensile steel sheet, tinplate steel for beverage cans, and regular electric steel used for electric transmitters and motors. Only ten percent of JFE production is oriented to commodity-grade steel, such as hot-rolled steel for construction use (like guard rails), a sector some Chinese firms focus on.

Japanese firms have long been thought by some to lack creativity, and to be mere copiers and improvers of basic technology developed elsewhere. However, Itami argues that the orientation of Japanese firms towards invisible asset accumulation suggests that they will become better at conceptualizing new products and forming new ideas. Before, Japan had no base to form ideas, Itami notes, saying that creativity is like the tip of an iceberg. A huge body of experience and knowledge is necessary before creativity is possible, and Japan has been accumulating this little by little, he argues. "Formation of ideas is a very stochastic phenomenon — you throw out many ideas, and one of them works," he observes. "Average people throwing out ideas have a very low probability of success," he notes. Corporate Japan now has the experience and knowledge now to become much more innovative, he suggests.

Thomas Roehl stresses the need to avoid over-generalizing about Japanese firms, noting that some manage invisible assets well and some do not. The associate professor in the MBA Program at Western Washington University collaborated with Itami in writing *Managing Invisible Assets*. Successful firms at invisible asset cultivation tend to be good at communicating across division and section lines, Roehl points out.

He cites the example of a Japanese assembly line worker who stops production when he discovers a faulty part. Rather than just taking a cigarette break, in many Japanese firms he is obligated to discuss how the part can be redesigned. The line engineer is also consulted. In short, workers from several different sections exchange information to improve the production process, he stresses.

Such an ability to overcome the 'silo effect' (the tendency in organizations to limit horizontal communication) is especially useful in cross-firm tie-ups. Many firms are joining together to develop new technologies. Japanese managers easily talk across organizational lines, giving them an edge in such ventures, he notes. Sony Corp. and Samsung Electronics signed a cross licensing agreement in 2004 regarding patents for some basic technologies, in order to avoid legal disputes and cut research and development costs. The two firms also inked a deal in 2006 to build a second plant making LCD panels for flat screen televisions for their joint venture S-LCD Corp. Both sides are learning and bringing back the joint knowledge to their internal and competitive ventures, observes Roehl. Sony's Bravia line flat-panel TVs are contributing to better-than-expected earnings for the firm in recent years, one data point proving that, at least in one case, such cooperation is a benefit.

This article is abridged and updated from 'The Money Tree: How Investors Can Prosper From Japan's Economic Rebirth', written by Andrew Shipley and published by Financial Times Press. Footnotes were excluded due to space limitations, with the contributor solely responsible for the accuracy of quotations attributed to others.

JAPAN INSIGHT

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Transkaryotic Therapies, and US-based New River Pharmaceuticals. It is also a global leader in the attention-deficit disorder (ADHD) category with its drugs Adderall XR, Daytrana and Vyanase. But a decades-old law prohibiting the sale of amphetamines in Japan, as well as the almost non-existent recognition by Japanese doctors of ADHD as a disease that requires traditional medical treatment, would seem likely to keep that part of Shire's business from gearing up in Japan indefinitely. Shire executives including Joseph Rus, its International EVP, did not respond to questions by presstime.

NEO MARKET FINALLY GETS A LISTING

It took three months, but the new Neo stock market for technology start-ups, an offshoot of Japan's JASDAQ market, has finally announced its first listing, Ubiquitous Corp., a developer of gaming software used by Nintendo DS games, as well semiconductor system solutions. Tokyo-based Ubiquitous will start trading on Neo this month.

Special markets for small companies and start-ups have had a mixed record of success in Japan, with Nasdaq Japan starting up with the backing of Softbank and much fanfare in 2000, only to pull out two years later. The Tokyo Stock Exchange's MOTHERS market, which also started in 2000, has garnered more success, having experienced a recent uptick of activity for certain internet stocks while also reaching the milestone of 200 listings for the first time.

In the case of Neo, JASDAQ has decided to require its own assessment of potential listing companies' technologies, rather than require the company to have any minimum level of sales or profits. That's lucky for Ubiquitous and the other tiny companies likely to list, since Ubiquitous is projecting total earnings of only ¥32 million for the year ending March, 2008.

But it isn't clear at all why such small start-ups should be allowed to list in the first place, nor is it clear what qualifies the officials at Neo to decide which technologies are likely to be good bets for investors. While it is possible that Neo may be able to offer wider exposure for promising young companies over time, it is also possible that it may end up being another case of Japanese bureaucrats, rather than the marketplace, trying — and ultimately failing — to predict winners.

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WAKE-UP FOR IBM JAPAN: US SOFTWARE FIRM PENETRATES JAPANESE BASEBALL

It may be another sign of a rapidly-globalizing world.

E-Solutions, a privately-held, Florida-based hosting provider and software firm that sells a scouting information product called ScoutAdvisor to fourteen Major League Baseball (MLB) teams in the US, has broken into Japan by selling its software to the Orix Buffaloes, which competes in the Pacific League of Japanese professional baseball (*puro yakyu*). The firm claims to be "the first US company to provide software development services to Japanese baseball" with its product that allows a teams' scouts and coaches to call up data and scouting reports on international players in either Japanese or English over any computer with an internet connection. In the US, the annual cost for a team to use ScoutAdvisor is less than $100,000, and for this the team receives contract information, statistics, qualitative reports, and histories of players' performances through-out their minor and major league careers.

The Japan sale by ScoutAdvisor resulted from a recommendation made by a MLB scout that consults for the Orix Buffaloes, according to a source with knowledge of the transaction. And since a growing number of former foreign athletes and coaches are employed as players, coaches and consultants for teams in Japan, it offers hope to other non-Japanese providers of sports equipment, services and apparel that they too can profit from growing Japanese interest in baseball, football, soccer, basketball and other US and European sports.

It also throws up a challenge to IBM, which pretty much owned the market for such scouting software until recent years, and which has a substantial Japan-based operation with thousands of employees but no sales to Japanese baseball teams as of yet. The IBM offering reportedly costs up to twice as much as ScoutAdvisor, with additional charges for software support after the first year. IBM Japan did not respond to questions by presstime.

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An Insurer Prepares One of Its Two Brands For The Bank Channel

The Prudential Japan Story, As Told By Kazuo Maeda, Country Head

Activity in Japan's insurance sector is poised to heat up next month. For the first time, banks will be able to sell almost any type of life and non-life insurance product at their branch locations, where up until now they had been limited to only certain types, such as universal life and variable annuities. This newest deregulatory phase invites innovative insurance companies and banks a chance to distinguish themselves from the 'me-too' nature of many of their competitors. At the same time, it creates risk for several giant institutions that dominate the market in certain segments, especially if they seek only to protect their existing positions.

Some market observers are already trying to pick winners among banks with proven distribution networks, such as Bank of Tokyo Mitsubishi-UFJ, and insurance companies with leading positions in certain product types, like Mitsui-Sumitomo MetLife and Hartford Insurance. But the effect of the latest deregulatory phase may well be that a group of what have, until now, been lower-profile firms, emerges far stronger than some would predict due to focused growth strategies and attention to execution.

One firm with the potential to surprise the market might be US-based Prudential Financial, one of the world's more important diversified insurance companies, with assets under management exceeding $600 billion. Unlike many of their Japan competitors, its domestic units Prudential of Japan (POJ), together with Gibraltar Life (the former Kyoei Life), distribute products through multiple channels. And as December's deregulation draws near, Gibraltar is moving beyond its traditional areas of strength for the first time, with plans to distribute Gibraltar-branded insurance products through banks.

This will not be an easy shift either for Gibraltar or its bank partners. Gibraltar will have to battle dozens of new entrants for 'shelf space' at major as well as regional and local banks, while its bank partners will be forced to battle other banks for new customers and the ability to offer those products, whether from Gibraltar or other providers, that prove to have the most customer appeal.

It is likely the market will be in tumult for several years before winners are clear. But with its financial strength and already-existing diverse distribution mix through POJ and Gibraltar, Prudential Financial may be able to endure its initial losses in Japan's bank channel for longer than some other entrants, while being able to bank on its dual brand names for what could be better-than-expected performance.

PRUDENTIAL OF JAPAN: POJ primarily sells life insurance products focused on death protection benefits, namely term life, whole life, retirement income, and endowment," says Kazuo Maeda, Prudential's Japan country head. "Business insurance refers to individual insurance products sold to business owners. They usually cover the business owner and/or his/her key employees. In most cases, death benefits of business insurance is used to cover the damage on the company caused by death, for business continuation in case of family businesses, or for employee retirement benefits." POJ also sells medical insurance, but in this area its offerings "are similar to the most popular type of medical insurance product available in Japan," admits Maeda, "so there is nothing unique about them." The policies cover hospitalization and surgery expenses, offering fixed benefits, as opposed to covering actual expenses. "We focus on death protection life insurance are best at that — our medical and annuity businesses are not as strong."

During the past decade's increasingly harsh environment for life insurance firms, characterized by slow population growth and more intense competition, POJ has tried to distinguish its traditional door-to-door field force from that of giant local firms like Nippon Life and Mitsui Life by upgrading its skill set and giving its army of agents a new title – Life Planners. The days when a longtime customer's loyalty to an agent who visited the home routinely resulted in regular policy sales and renewals is largely gone. So Life Planners are given more training in sales and product knowledge, and sent out to sell a variety of more sophisticated products to a wider group of small businesses and high net worth individuals in addition to housewives, mainly through referrals and home visits. And in contrast to the part-time females that comprise the sales force for many of its competitors, Life Planners are mainly men.

Interestingly, for the most part POJ only hires those with bank and securities experience, preferring to avoid those with insurance backgrounds, says Maeda. It then trains these hires intensively in the particulars of sophisticated selling of high-end insurance products. The training starts with one month of classroom training designed to ensure new hires get their sales licenses. Then staffers receive 3-6 hours of training one day per week for as much as four months. They then move back into the classroom for another month of training before they are hired individually into the field force by branch managers across

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An Insurer Prepares One of Its Two Brands For The Bank Channel

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the country.

Out of a total POJ staff of 4000, about 3000 are Life Planners, Maeda estimates, of which only a hundred or so are women. Call this a more sophisticated sales force – and a successful one too: "30-40 percent of our new sales is business insurance sold to small business owners," he claims.

Success Story

GIBRALTAR LIFE: Meanwhile, six years after its 2001 takeover of bankrupt Kyoei Life, Prudential has just about completed the process of creating a new brand name and firm, Gibraltar, that carries little of the stigma of the predecessor firm's financial failures, which were well-publicized at the time of its bankruptcy. Today Gibraltar employs about 8000 in total, of which some 6000 work in sales as 'Life Advisors', a number that's much lower than the nearly 11,000 salespeople Kyoei Life employed just prior to bankruptcy. "Of the 6000, about 2300 are ex-Kyoei staff and 3700 have been newly-hired since Prudential took over," Maeda estimates. Gibraltar serves the middle-market, such as teachers, nurses and other municipal employees, with basic and affordable traditional life and health insurance products, he says, such as term life insurance sold to teachers and variable annuity sales to retired teachers. Deploying Life Advisors as a less sophisticated field force (in comparison to POJ's Life Planners), and building on the former Kyoei's pre-existing relationships with unions and associations of municipal workers, Gibraltar has re-emerged as a stable, and viable, competitor. "Our Life Advisors, primarily housewives, visit elementary and middle schools around the country," he explains.

When Prudential took over Kyoei Life, the firm had extensive relationships with teachers, municipal workers, and even military servicemen. Today, the military business is gone, and Gibraltar's sales come largely through distribution partnerships with associations and unions located deep within Japan's communities, where most foreign firms have little or no presence. "Some examples [of our partners] are the Japan Nursing Association; an association of mostly elementary and middle-school teachers called the Japan Educational Mutual Aid Association of Welfare Foundation (*Nihon Kyoiku Koumuin Kousaikai)*; and an association of small business owners called the Central Federation of Societies of Commerce and Industry (*Shokokai*)," says Maeda. "In the case of *Shokokai*, it is actually their staff which sells our policies, the sales function is effectively outsourced. But our largest business is still with the teacher's association, in which we have nearly half the market share and the number one position" in a market of some 1.2 million public school teachers (and 3-4 million people overall when family members are included).

Gibraltar estimates that it serves teachers in some 39,000 schools, including nearly 23,000 elementary, 10,000 junior high, and nearly 6000 high schools across Japan. So the women who primarily comprise its field force must receive training not only in product know-how, but in how and when to approach teachers during special fairs and association events. They also must learn how to gain entry to school buildings, a much tougher task these days since Maeda says "the security situation has become more severe."

In all of its channels, Gibraltar also sells variable annuities, "but we do not consider variable annuities as one of our major products."

According to Maeda, "Gibraltar's brand is not necessarily well-known to the general public, but I believe almost all teachers recognize our brand. Up to now, we have been advertising that Gibraltar has recovered from bankruptcy, has become part of Prudential Financial, and that the company is financially sound. In addition, we have been communicating how we have been supporting schools through various activities." While he feels Prudential's business doesn't require advertising since it's primarily based on referrals, and Gibraltar hasn't needed to advertise until now due to its strong recognition by teachers, Maeda suggests that Gibraltar will now need to start some advertising in support of its entry into bank distribution. "But we haven't developed our ad message yet," he says.

OTHER BUSINESSES: Few outside those industry analysts who cover Prudential and its competitors on a global basis pay much attention to its other businesses, but typical of most giant insurers, the firm operates significant non-insurance businesses, including asset management and relocation, and also inherited several unrelated businesses from Kyoei, including tourism and leasing units that have since been shuttered, and a computer services provider.

The most important 'other' business, however, is real estate. "Prudential Real Estate owns over 500 properties [in Japan], but most of them are used as sales offices to run our business," explains Maeda. But he claims "we are not actively involved in the real-estate business." Yet Pru-

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dential's property management activities very likely give it a unique perspective on issues of concern to the teachers and municipal workers it serves in each community, and it's also a safe bet that the properties are available for sale when the right opportunities come along. Prudential's Japan real estate business also picked up a senior residence outside Tokyo from the former Kyoei Annuity Home that remains in operation.

GOING FORWARD: Maeda claims Gibraltar "has been growing by nearly ten percent on average in the recent years, measured by new business annualized premium." And overall surrenders from some six million former Kyoei policyholders taken over by Gibraltar have been manageable, too. This, he feels, is due to the fact that many Kyoei policies offered slightly higher guaranteed rates than similar policies offered by competitors at the time, while the agreement Prudential signed at the time it closed on the Kyoei takeover additionally required that special dividends be paid to Kyoei policyholders in the fourth and eighth year after the merger. There's also the general inertia of policyholders who might have considered moving their policies to another firm who decided not to incur surrender charges, says Maeda. "Schoolteachers are very conservative, they don't want to change [policies] if they don't have to."

But it's Gibraltar's entry into the bank channel that will require a major shift in its tactics. Insurance products are still often poorly understood and badly-explained to customers by bank staff (*SSJ*, March 2005 issue), and many of those like Hartford who have reported good sales growth have still not achieved steady profitability (*SSJ*, April 2005). Those firms competing in the channel must labor to provide sales materials and teach bank staff how to answer customer questions. Many also compete by paying commissions of ever-increasing amounts to their bank partners, which may cause bank staff to push some products over others that offer commissions at a lower rate. Whatever the particular costs of competing end up totaling , all the effort, training and commissions has pressured the profit margins of insurance products sold in the bank channel, a fact that Gibraltar's management is certainly aware of. "At the moment, we have business relationships with eight banks, and are negotiating with a few more," Maeda reports. "We plan to expand our bank channel product portfolio in selected banks, with growth in the bank channel being our key goal."

Other than the bank channel, Maeda isn't explicit about where Gibraltar will focus its growth, saying only that it "plans to add other segments 'later on'". But he expects initial sales volumes of all Gibraltar's products, including variable annuities, to remain limited even after they begin to be offered via banks.

As for POJ, Maeda boasts that it has also experienced ten percent annual growth in recent years (measured by new business annualized premiums), although he expects less than ten percent growth going forward. "Our POJ count of Life Planners should grow 8-9 percent per year," he offers, "while Gibraltar's Life Advisor count bottomed out in 2006." One new development Maeda sees as an advantage for the POJ unit is Japan's new FIEL law requiring significant new efforts by financial firms to ensure that customers understand and are appropriate for the products they buy. "We have a suitability check already in effect at Prudential," points out Maeda, "which gives us an advantage over other firms that will have to spend a lot of time and resources training their employees to follow the new law."

Maeda explains that Prudential declined to take over the Japan unit of the former Skandia Insurance back in 2003 when the firm's global operations were on the block and Prudential ended up purchasing Skandia's US unit. "We didn't think Skandia Japan was attractive due to all the regulations in the variable annuities market, plus that market requires a high level of reserves," he recalls. [Skandia Japan instead became a part of Japan non-life insurance giant Millea Group].

"We started from scratch in Japan in 1988 and we've had steady growth for twenty years at POJ, recently with ten percent growth consistently," says Maeda proudly. He offers this by way of explaining why POJ has no plans to enter other distribution channels at the moment. "At Prudential of Japan, we have always ranked high on customer satisfaction surveys, and the quality of our business is very focused, so we will continue the same way."

Nevertheless, the coming battles in the bank channel that Gibraltar will enter directly, will also likely have some effect on the medium-term success of POJ's business and that of other major firms with strong field forces, since bank sales trends will force changes in product offerings and customer expectations over time. In Prudential Financial's case, however, having two very different brands serving different market segments through distinct channels may give it an advantage of flexibility that others can't match.