Japan

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Game on as Abenomics takes off

Inside »

Taking aim
Economic recovery package continues to please observers
Page 2

The big prize
Governor deploys a princess and spying tactics to secure Olympics
Page 3

Safe return
The property market is enjoying a new lease of life
Page 3

Highs and lows
A tale of mixed fortunes for two giants: cars and electronics
Page 4

Positive leadership and the prospect of the Olympics returning to Tokyo are boosting confidence, writes *Jonathan Soble*

Resurgence: jubilation met Japan's successful bid to host a modest, compact and efficient 2020 Olympic Games in Tokyo Getty

In the course of Japan's seven-year campaign to bring the Olympics back to Tokyo – the city that broadcast its postwar resurrection when it first hosted the event in 1964 – a central characteristic of its pitch was modesty. There would be none of the suburb-devouring construction or spiralling budget overruns of recent games. A Tokyo Olympics would be, in the words of the city's proposal for 2016, "the most compact and efficient Olympic Games ever".

Although Tokyo's bid did not make it for that year, the description seemed to fit contemporary Japan itself – meticulous, unassuming, happy enough with small ambitions.

Ever since their country's stock and property bubble burst at the start of the 1990s, beginning two decades of economic decline, Japanese have been adjusting to the idea of a diminished place in the world.

They have done so quite smoothly. Most shrugged when China's gross economic output overtook Japan's in 2010. As a government minister said, questioning public funding for a project to build the world's fastest supercomputer: "What's wrong with being number two?"

On September 8 in Buenos Aires, the International Olympic Committee chose Tokyo to host the 2020 games. The decision was greeted with (mostly) jubilation in Japan and visitors can expect all the scrupulous small-footprint-ism that Japan has been promising.

The games will use many of the city's existing facilities, and most events will be staged within a few kilometres of the Olympic Village, a short hop from the downtown Ginza shopping district. The budget, at about $8bn, is less than half that submitted by Istanbul, one of two cities that Tokyo defeated.

Yet the narrative of modesty has given way to something else. It is not chest-thumping bravado, exactly – this is still Japan – but a sense that, as in 1964, the games could become a symbol of Japanese resurgence, a chance to climb a rung or two back up the global status ladder.

The change in mood owes much to Shinzo Abe, the prime minister, whose motto since winning office in December last year has been "Japan is back". He has embarked on an ambitious effort to "reflate" the economy, using a combination of government spending, aggressive monetary stimulus and the promise of structural reform. The hope is to reverse a prolonged slide in consumer prices and rekindle growth.

"I want to make the Olympics a trigger for sweeping away 15 years of deflation and economic decline," he said after the IOC decision.

"Abenomics" is going almost eerily to plan. Japan's economy grew at an annualised rate of about 4 per cent in the first half of the year, easily the fastest pace among the Group of Seven big developed countries.

The yen, which had been strengthening relentlessly since 2007, when other countries' central banks started flooding markets with their currencies in response to the global financial crisis, has weakened, aiding Japanese exporters. The stock market is up by two-thirds since last year's election campaign and even consumer prices are creeping up.

Doubters remain. Some focus on the unfinished business of Abenomics, not least deregulation. Under Mr Abe, Japan has entered talks over the Trans-Pacific Partnership, a proposed 12-country bloc whose members would be committed, in theory at least, to eliminating virtually all barriers to trade. Joining it would jolt protected Japanese industries such as agriculture. The government has submitted eight deregulation bills to parliament for the autumn, covering areas from farmland ownership to competition in the electricity industry.

Some parts of Mr Abe's reform agenda, such as loosening Japan's strong job protections for full-time workers, remain little more than wishlist items. He wants to cut corporate taxes – the second-highest in the OECD, at 38 per cent – and faces opposition from the finance ministry and parts of his ruling coalition.

He must balance his reflation strategy with the long-term risks presented by Japan's public debt, the growth of which has accelerated under his government. It will soon reach the equivalent of two and a half years' economic output, by far the highest ratio in the developed world.

On October 1, Mr Abe approved a long-debated increase in the sales tax, which is to rise from 5 to 8 per cent in April. New fiscal stimulus worth Y5tn ($51bn) will cushion the blow to growth, but only by sacrificing some of the budget-balancing effect that the tax was designed to create.

Japan is experiencing a period of political stability unknown since Mr Abe's mentor, Junichiro Koizumi, was in charge from 2001-06. Six prime ministers followed in six years, including Mr Abe from 2006-07.

Ten months into his second term in office, Mr Abe's approval ratings remain above 60 per cent in most polls, with no national elections planned until 2016. The ruling coalition, led by Mr Abe's Liberal Democratic party, added control of the upper house of parliament this summer to the lower-house majority it won in December, ensuring that it can pass most bills.

The prime minister's "Japan is back" agenda includes a more assertive foreign policy. He describes it as "active pacifism" and has ordered the first rise in defence spending in 11 years. He wants to reinterpret the anti-war constitution to allow Japan's forces to fight in defence of its allies.

"We can't preserve peace in Japan by thinking only of Japan itself," Mr Abe says. "Peace in Japan depends on regional stability and on the world as a whole becoming more peaceful."

When he was prime minister the first time, he repaired relations with China after they were damaged by Mr Koizumi's regular visits to the controversial Yasukuni war shrine. This time, the gulf between Tokyo and Beijing is bigger, with the sides stalking each other near the Japan-controlled Senkaku Islands, which China claims and calls the Diaoyu. Behind-the-scenes efforts to arrange a summit meeting have proved fruitless so far.

Park Geun-hye, president of South Korea, has been cool towards Mr Abe, who is loathed by many Koreans for his attempts to play down official responsibility for the wartime abuse of women by occupying Japanese forces. Mr Abe's best bet for a diplomatic success might be Russia, which has agreed to resume long-frozen talks over four islands seized from Japan by the Soviet Union at the end of the second world war. Vladimir Putin wants to sell Japan natural gas and Mr Abe needs new energy sources after the Fukushima nuclear disaster. A deal to normalise the border and develop the islands looks tempting.

The aftermath of the March 2011 earthquake and tsunami remains a problem. Leaks of contaminated water at Fukushima were the final hurdle for Japan's Olympic bid and it was cleared only after Mr Abe pledged to intervene more forcefully in the clean-up. That has been left largely to the plant's owner, Tokyo Electric Power. Protests against Tepco and the nuclear industry that swelled last year have died down, but the leaks threaten to make more Japanese oppose the restarting of some of the 50 undamaged reactors made idle following the accident.

After Tokyo's Olympic-bid victory, some Japanese complained that spending money on the games was obscene when tens of thousands of people in the disaster-stricken north-east remained without permanent homes. Political wrangling and bureaucratic inertia actually appear to be bigger obstacles to recovery.

As such, Mr Abe has work to do before all of "Japan is back".

Editor's introduction Welcome to the FT and Nikkei's editorial co-operation

Today's Japan Special Report marks the start of closer editorial co-operation between the Financial Times and the Nikkei, Japan's premier business media group.

It contains two comment articles by distinguished Nikkei journalists as well as the usual mix of analysis and features from FT correspondents stationed in Tokyo.

The report will appear in both newspapers and on both our websites. In this way, we hope to provide added insights to our respective readerships by combining the best of the FT's "outside" view of Japan with the Nikkei's deep understanding from inside.

In addition, the Financial Times and the Nikkei will soon link to each other's English-language websites through shared headlines and explore other ways in which we can combine our joint editorial excellence for the benefit of our readers.

Both news organisations maintain an extensive network of domestic and international correspondents and remain committed to providing objective and insightful news and analysis to our busy and sophisticated audience.

This is a time of heightened interest in Japan. The world wants to know whether "Abenomics" is for real and whether it can lead to a period of sustained economic recovery in the world's third-biggest economy. This year, in which the FT is celebrating 125 years in print, seems an appropriate one in which to deepen our already friendly ties with the Nikkei, which boasts a similarly long history and a readership of more than 3m.

I am delighted to offer this report to our readers and to those of the Nikkei. I hope it will be the start of a long and fruitful collaboration.

Lionel Barber

Leaders choose to play it cool in a global pitch of national identity

Culture

Idiosyncratic brands are seen as a crucial to success, reports *Jennifer Thompson*

It is a concept that links brand names as disparate as Hello Kitty and Issey Miyake and activities from sushi to sumo.

The notion of "Cool Japan" has long been embraced by government officials and business leaders as a framework to encourage foreign demand for Japanese consumer goods and services.

The term "Gross National Cool" was brought to public attention by US writer Douglas McGray in a 2002 article for Foreign Policy. He cited Japan as an example of how a country that was not a superpower in the military sense could nevertheless project its influence and culture across the globe.

"What made Japan a superpower, more than just a wealthy country, was the way its great firms staked claim to a collective intellectual high ground that left competitors, even in the United States, scrambling to reverse-engineer Japanese successes," he wrote.

In 2010, Japan's ministry of economy, trade and industry (Meti) established a creative industries promotion office to champion sectors such as fashion, food and music under the Cool Japan banner.

The new administration of Shinzo Abe has continued the trend. "Japan's strengths in content, fashion and culture and tradition are also attracting attention from the world," Mr Abe told lawmakers in a February speech.

He added: "As we work to ensure that the boom in *anime* and other content does not end as a temporary fad, besides promoting Japan as a tourism-oriented country that attracts people from around the world, let us also make Cool Japan into a world-class business."

The rationale goes beyond national pride. Mr Abe is leaving no stone unturned as he attempts to reverse 15 years of stagnant growth, against the backdrop of a rapidly ageing and shrinking domestic population.

About 32m people, a quarter of the overall population, are aged over 65 according to official statistics. Japan is the first country to hit the 25 per cent mark. In the face of a declining domestic market, the government has gone further than any other to encourage the consumption of Japanese goods abroad to help drive growth.

It has set up a Cool Japan fund, administered through Meti, with promised backing of Y50bn. It is hoped that a further Y10bn will be raised through contribu-

Cool for cats: Hello Kitty is part of a nationwide strategy

Continued on Page 4

Two arrows on target but third yet to hit home

Economy Companies have yet to respond to the improved outlook, says *Ben McLannahan*

On track so far: Shinzo Abe, Japan's prime minister

A plan seems to be coming together. Before Japan went to the polls in December, Shinzo Abe set out his stall. If elected prime minister, the Liberal Democratic Party leader would end the "corrosive" deflation that had lingered in the world's third-largest economy for most of the previous 15 years.

He would get things going with a supplementary budget. He would lean on the Bank of Japan to embrace "unlimited" monetary easing to achieve a higher, harder inflation target of 2 per cent. And he would start tackling some structural impediments to growth, while leaving some of the trickier matters – such as how to protect certain industries in multilateral trade deals, or how to restart idled nuclear power plants – until after upper-house elections in July.

A happy side-effect of this big effort, Mr Abe's advisers agreed, would be a weaker yen. The subsequent lift to corporate profits, stock prices and summer bonuses should ensure victory for the LDP in the upper-house election, thus cementing Mr Abe's grip on power for the next few years.

Ten months on, and it is remarkable how much of this scenario has played out. Thanks largely to fiscal and monetary stimulus – the first two "arrows" of Mr Abe's programme – Japan's real growth in the first half of the year was about 4 per cent on an annualised basis, eight or nine times higher than the potential growth rate.

The election, framed by the LDP as a referendum on "Abenomics", was no contest. Inflation rose to a five-year high of 0.8 per cent in August, pushed up by a big fall in the currency.

And some longer-term growth initiatives are now under way. Eight bills will be submitted to the Diet in the extraordinary session that began on October 15, covering areas such as farmland reform, renewable energy and the establishment of special "strategic zones" for investment.

Just about the only pre-election economic policy pledge yet to be fleshed out is a cut in corporate taxes, to bring Japan's 38 per cent effective rate closer to Germany's 29 per cent, China's 25 per cent and Korea's 24 per cent. The ministry of finance says it is now working on a plan.

"We've seen several false dawns, but this seems much more aggressive than before," says Adrian Brindle, a long-time Japan hand now building a financial services firm under the Evolution brand. "It's a dangerous experiment. But to escape deflation you need to knock the orb off its axis."

But will it work? The biggest obstacle could be the private sector. Government and BoJ officials are united in exasperation that companies have yet to respond to the improved outlook by raising base salaries or ramping up plans to spend more in Japan on plant and equipment. Both measures are seen as vital to create a virtuous cycle of higher profits, wages and consumption.

Yet recent data on private consumption have been softer than expected, suggesting rising prices – and higher fuel bills, in particular – have begun to weigh on households' purchasing power. Many policy makers fear that if total cash earnings remain flat in the run-up to the rise in consumption tax next April and beyond, the economy could take a big hit, threatening Japan's exit from deflation.

Mr Abe has built in safeguards in the form of a stimulus package worth about Y5tn ($51bn), which more than offsets the theoretical knock to the economy from the tax increase of about Y1.8tn. There will also be handouts to those on low incomes.

'It's a dangerous experiment. But to escape deflation you need to knock the orb off its axis'

But within ministries there is a feeling that base salaries have to go up to buttress demand. Last month, the government held a meeting with business leaders in which it discussed tax incentives to boost incomes, and is due to hold another this month, to be chaired by Mr Abe himself.

Employers' associations have long resisted politicians' calls to pay people more, arguing that lifting fixed costs amid uncertain global demand will hurt Japan's competitiveness. Yoshihide Suga, chief cabinet secretary, told a press conference last month the government aimed to reach a "shared understanding" with the private sector by the end of this fiscal year.

Capital spending, too, is yet to make a convincing recovery. Quarterly investment by businesses in new plant and equipment shrank for five straight quarters before rising 1.3 per cent between March and June.

A pick-up is possible from here, says Masayuki Kichikawa, chief Japan economist at Bank of America Merrill Lynch in Tokyo. But many companies have "lingering capacity overhangs" and manufacturers will be looking to produce where the demand is, to avoid exchange rate exposure.

"As a result, business investment is likely to increase in emerging countries rather than in Japan," he says.

Most analysts agree that getting groups on board depends on the incentives in Abenomics' "third arrow" – a set of linked initiatives across policy areas. Mr Abe deserves a lot of credit, they say, for challenging broad assumptions of continuing decline. But the hard work starts here.

Complacency is biggest threat to resurgence

Abenomics

Prime minister must stay the course with successful measures, writes *Yoichi Takita*

NIKKEI

Last October, posters suddenly appeared on the streets of the Japanese capital declaring that "the centre of the world economy is coming to Tokyo".

The posters were referring to the annual meetings of the International Monetary Fund and World Bank, then being held in Japan.

To many, however, the phrasing must have seemed ludicrous. Deflation-plagued Japan was mired in an economic slump under the last days of a failing government led by the Democratic Party of Japan.

One year later, the mood is much brighter. The Liberal Democratic Party's Shinzo Abe, back in the prime minister's post for a second time, addressed the New York Stock Exchange in September. He told his audience to "Buy my Abenomics", suggesting Japan was back and had a central role to play in the global economic recovery.

The "three arrows" of Mr Abe's programme – aggressive monetary easing; flexible fiscal policy; and a private-sector-led growth strategy – seem to be on target. The results have been impressive.

The super-strong yen has reversed direction and the stalled stock market is up nearly two-thirds. The nation has recorded annualised real growth of about 4 per cent for two straight quarters.

Many like to bathe in the reflected glory and claim to have supported the idea all along. In fact, when I used the word "Abenomics" in the Nikkei last November, many experts were decidedly cool about the idea.

Typical of the comments was: "Extreme monetary and fiscal policies engender more adverse effects than intended ones."

Behind the criticism lurked a cynicism and masochistic psychology borne of years of disappointment.

Mr Abe and his aides have sought to counter such scepticism through vigorous activism.

The Bank of Japan made the first move by introducing a "new dimension" to monetary easing, helping stem the yen's appreciation and reverse the stock market's long slide. The administration moved quickly to join the Trans-Pacific Partnership free trade talks. And it unveiled a plan for tax breaks related to corporate capital investment.

The programme has drawn its vigour from an acute sense of crisis over Japan's decline

Mr Abe's pattern has been to announce headline-making measures every month or two, winning over the markets, investors and public who crave signs of change in Japan. This approach, unusual for a Japanese prime minister, has been crucial to Abenomics' success so far.

When the stock market was going through a downward correction in June, for instance, Mr Abe brought forward the announcement of the corporate tax breaks.

He used the same tactics to the fullest effect in deciding to go through with the plan to raise Japan's 5 per cent consumption tax to 8 per cent next April, a policy supported by most, if not all, market participants.

Using the success of the 2020 Olympic Games bid as leverage, Mr Abe had the ministry of finance prepare a Y5tn ($51bn) stimulus package in return for the consumption tax rise.

He also started a discussion on lowering Japan's effective corporate tax rate. He was thus able to announce the tax increase in conjunction with growth-oriented initiatives.

But does the prime minister have any blind spots that could imperil his programme? Some argue that he could risk his economic achievements by wasting political capital on diplomatic and national security issues. Still, the Abe administration looks pragmatic, and its stance of prioritising the economy is unlikely to change until a recovery is in full swing.

It is at that hypothetical point, when Japan has defeated deflation and returned to steady growth, that the real threat to Abenomics may appear. The programme has drawn its vigour from an acute sense of crisis over Japan's decline. If that urgency fades, policy makers may grow complacent and Abenomics could unravel.

Robert Feldman, chief economist at Morgan Stanley in Japan, says that since the bubble economy collapsed more than 20 years ago, Japan has been stuck in a "CRIC cycle" – crisis, response, improvement and complacency. Mr Abe's ability to avoid slipping back into complacency may be the most important factor determining whether Abenomics will lead to Japan's economic resurgence, or not.

Yoichi Takita is a senior Nikkei staff writer

Importance of TPP to more trade leaves no room to monkey about

Commentary
YASUHIKO OTA

NIKKEI

Almost all those Japanese who oppose the Trans-Pacific Partnership, a planned 12-member economic bloc that Japan is involved in creating, get much of their information from a single website.

In Japanese, it is called: Saru Demo Wakaru TPP. Loosely translated, it means TPP for Monkeys. The site is run by a non-profit organisation in a part of the country that specialises in organic farming.

In Japan, a Twitter search for TPP will turn up a bevy of tweets that portray the agreement as a US plot to sap Japan's economic power and weaken its sovereignty.

Since Prime Minister Shinzo Abe announced in March that Japan would join the negotiations, the online anti-TPP campaign has lost some steam. Yet, although most Japanese understand the importance of the country's alliance with the US and recognise the value of dismantling trade barriers, there remains a group of internet dwellers for whom the TPP is a dangerous plot.

According to TPP for Monkeys, if Japan becomes a member of the bloc – which would regulate the flow of goods, money, intellectual property and even impinge on some national laws – many things that the Japanese take for granted would come under threat. "Our universal health insurance coverage may disappear," the cute monkey character on the site shouts. "An appendectomy would cost as much as Y2m. Those who do not have that kind of cash would be left to die."

The site also sounds an alarmist note about what it says would be the TPP's effect on Japanese farming. "Food self-sufficiency would fall from 39 per cent to 11 per cent. With the world bound to experience a food shortage in the near future, a sudden disruption of food imports would bring starvation."

Such scaremongering undermines the case of those opposed to the TPP. In Washington, Brussels, London and other bastions of capitalism, most people have probably never heard of the TPP. So why has the issue aroused such controversy in Japan?

The hysteria is probably a reflection of an anti-American sentiment nursed by some frustrated segments of the population, especially those who have grown up during the "lost two decades" of deflation and economic decline.

Part of their objection is political. They cannot stomach the existence of what they perceive as a US that behaves as though it owns Okinawa, where the bulk of US bases in Japan are located.

But there has been almost no protest against a proposed free trade bloc between Japan and the European Union that is every bit as wide in scope.

One mystery is why manufacturers, which have much to gain through better access to foreign markets, have not been more vocal in their support. It may be because US tariffs on Japanese products are already pretty low, while some of the other nations sitting at the TPP negotiating table – such as New Zealand and Singapore – are too small to make much of an impact on Japan's exports.

That makes the country's industrialists less prepared than they otherwise might be to stick their necks out in support of the TPP.

But Japan's economy has more to gain than this implies. In August, Japanese journalists, officials from agricultural co-operatives and politicians beholden to farmers flocked to Brunei, where closed-door TPP talks were taking place. Yet no one came to represent Japan's internet services, IT sectors, financial industry, or music and entertainment studios. Their absence was in stark contrast to the crowd of lobbyists from other countries.

This reveals a flaw in Japanese thinking. Most Japanese still associate trade only with the export and import of physical goods. Japan as a whole has yet to grasp the significance of trans-border rules governing intellectual property rights, investment and electronic commerce, all of which are integral to today's economy.

Participating in the creation of these rules – while reforming the domestic economy so that it shifts more quickly to these high value-added industries – would bring great benefits.

Mr Abe's government has made the service and software sectors pillars of its growth strategy. But if corporate Japan cannot overcome a mindset that neglects "soft" industries and regards physical exports as all-important, it might find itself turning to a new website for advice: Economics for Monkeys.

Yasuhiko Ota is a senior Nikkei staff writer

Yasuhiko Ota

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From proverbial basket case to a sensible bet

Real estate Easier monetary policy has given a boost to the sector, writes *Ben McLannahan*


High times: rents have risen 10 per cent in Tokyo's business districts Dreamstime

Twelve months ago shares in Ichigo Group Holdings, a Tokyo-based property manager, were languishing at about Y45 ($0.46). They are now 10 times higher, and on average daily trading volumes more than 80 times greater. But this is no bubble, says chairman Scott Callon.

What has happened, says Mr Callon, is that monetary policy has been "normalised" by a new Bank of Japan governor. Under Haruhiko Kuroda, installed by prime minister Shinzo Abe in April, there is a much clearer commitment to bringing an end to the deflation that has sapped spirits and stifled investment for much of the past 15 years.

Mr Kuroda has said he aims to hit a 2 per cent target for consumer price rises by doubling Japan's monetary base by the end of next year. That pledge, followed up by about Y7tn of bond purchases each month, has had a transformative effect on risky assets in general and the property sector in particular, with a near-60 per cent rise in the Topix real estate index since the turn of the year.

"For two decades the BoJ was running too tight a monetary policy, cutting off oxygen from the system," says Mr Callon, a resident of Japan since 1989. "For guys like me, it's an effort to remember when Japan was more vibrant. We've not experienced this kind of operating environment in an entire generation."

In the commercial sector, there is mounting evidence of a pick-up in rents in Tokyo, which had slid pretty steadily – 2006-2008 excepted – over the past two decades. Data from Miki Shoji, a real estate agency, show new buildings in the five central districts achieved about a 10 per cent rise in asking rents between January and September. Total rents across these main business areas – Chiyoda, Chuo, Minato, Shinjuku and Shibuya – dropped about 2 per cent over that period.

But Ichigo's Mr Callon says that real rents – defined as advertised rent minus incentives – have been increasing for a while. After the global financial crisis, some landlords desperate to fill space were offering tenants as much as eight months rent-free on a two-year lease, he says. As vacancy rates continue to fall – down to a three-year low of 7.9 per cent in September, from a peak of 9.4 per cent last June – freebies are falling too. "The first move is always in incentives, which have collapsed", he says.

Analysts say that preparations for the 2020 Olympics should keep prices firm in the relatively rundown area of Shinagawa, which is set to be redeveloped as a transport and accommodation hub for passengers arriving from Tokyo's two main airports.

Other obvious beneficiaries are the unfashionable Harumi and Toyosu districts on Tokyo Bay, where the Olympic Village and other event facilities will be built.

"To get to Toyosu from Ginza takes six minutes by subway, but judging by occupancy and rents, you might as well have slid off the face of the earth", says Christian Mancini, chief executive of north Asia at Savills, the property services group.

The residential property market is also picking up steam.

Year-on-year growth in new Tokyo condominium sales averaged almost 40 per cent between May and August, according to the Real Estate Economy Research Institute – five times the rate last year.

Brokers say some of that demand was due to buyers seeking to avoid a higher rate of consumption tax, set to rise from 5 per cent to 8 per cent next April. But equally, as "Abenomics" begins to generate expectations of inflation, borrowers are becoming conscious that ultra-low interest rates may not be around forever. Banks are also taking a more positive view of price rises, pushing out mortgage loans to as much as 95 per cent of the value of the property.

A new Mitsubishi-built complex at Chidorigafuchi, one of the prettiest spots on the perimeter of Tokyo's Imperial Palace, achieved the highest prices since the financial crisis when apartments were sold in September. All 22 units found buyers immediately, at an average price of Y270m.

"Unit prices above Y100m were hard to sell a year ago; now units above Y150m are selling very well," says Akihiko Mizuno, head of capital markets Japan at property consultants, Jones Lang LaSalle.

Much of the activity at the high end is driven by rich Asian families, who have seen the recent fall in the yen as an opportunity to pile into Japanese assets. Tokyu Livable, a Tokyo-based company that began ventures in Shanghai and Singapore within the past year, is now planning to set up shop in Hong Kong and Seoul.

"This is just the beginning," says Toshihiro Kitagawa, senior executive director. "The trend has turned."

Institutional investors in Europe and the US are circling too, lured by funding costs below 2 per cent and rental yields of about 5 per cent.

"Japan has been the proverbial basket case for the past five years", says Mr Mancini of Savills. "But now, against, say, overheated Hong Kong or Singapore, or mainland China, where competition with domestic money is too intense, it stacks up very favourably."

Mr Callon of Ichigo adds: "If rents take a hammering, you'll get [a yield of] 4 instead of 5 per cent. It's the best risk-adjusted investment in the world."

Spy tactics and princess help seal the deal

Olympics

Tokyo's governor tells *Jonathan Soble* how the 2020 games were won

Perhaps only in a conversation with Naoki Inose, the voluble nonfiction writer turned governor of Tokyo, could a question about the Japanese capital's Olympic bid elicit a 20-minute discourse on Pearl Harbor, James Bond and the Russo-Japanese war.

We are sitting in a reception room at the Tokyo metropolitan government headquarters in Shinjuku ward, a skyscraper complex commissioned during the 1980s bubble years that now has dingy, yellowed wallpaper and fading carpets.

His point, when we get to it, is about information, and its value in winning battles of both the military and sports-diplomacy kind.

The British, Mr Inose says, are masters of information gathering. He knows this from history – British spies helped Japan beat the Russians in 1905 by passing along intelligence about Russian ship movements – and also from more recent experience.

When Tokyo was honing its bid to host the 2020 Olympics, the governor, who chaired the campaign, asked London games officials how to woo the International Olympic Committee. Act like a covert operative, he was told.

"It's the country of 007. They said to find out when IOC members were visiting different competition venues, then to go and pretend you just bumped into them there. You have to have that information," he says.

Mr Inose is the second consecutive governor of Tokyo to have had a previous career as an author. His predecessor, Shintaro Ishihara, started out in fiction before becoming the outspoken champion of Japan's nationalist right. Some blame his disparaging comments about foreigners and women for Tokyo's failure to win the 2016 games.

In April, Mr Inose caused some trouble when he was quoted in a New York Times interview as maligning the facilities in Madrid and Istanbul, Tokyo's rivals for the games. He sought to weaken Turkey's appeal as potentially the first Islamic country to host the Olympics, by saying Muslims were always "fighting with each other". (He later qualified his remarks, though the civil war in neighbouring Syria ultimately did hurt Istanbul's case.)

Mr Inose shares Mr Ishihara's disdain for Japan's national bureaucracy. The ministries, he says, are beholden to special interests and territorial to the point of ignoring the national good – a complaint he illustrates with a story about preparations for war in the Pacific, in 1941.

"The navy and the army wouldn't tell each other how much oil they had stockpiled," he says. "This is before fighting the enemy. Government had already collapsed. That's the condition in which we fought America. There was no way we could win."

For the Olympic bid, Mr Inose had to corral a group of mutually distrustful bureaucrats, sports federations, corporations and the minders of the royal family.

"I visited the Imperial Household Agency many times, always surreptitiously of course," he says. He wanted a royal to add glamour to Tokyo's delegation in Buenos Aires, but worried he might be criticised for involving the monarchy in a political venture.

All this work came at a difficult personal moment for the governor. Seven weeks before the Olympic decision, his wife, Yuriko, died of a brain tumour. He kept up his schedule and rarely mentioned it, save for a few obliquely mournful messages on Twitter.

Mr Inose got his royal in the end: the Cambridge-educated Princess Hisako of Takamado, widow of the emperor's cousin, made a well-received presentation at the IOC meeting. "The atmosphere really changed because of that," he says.

"Madrid had brought out Prince Felipe at the IOC general meeting in Lausanne on July 3, so they'd already used their trump card. They had no surprises left . . . We were clever to save our princess for the end."

Voice of youth
Ayami Ohno

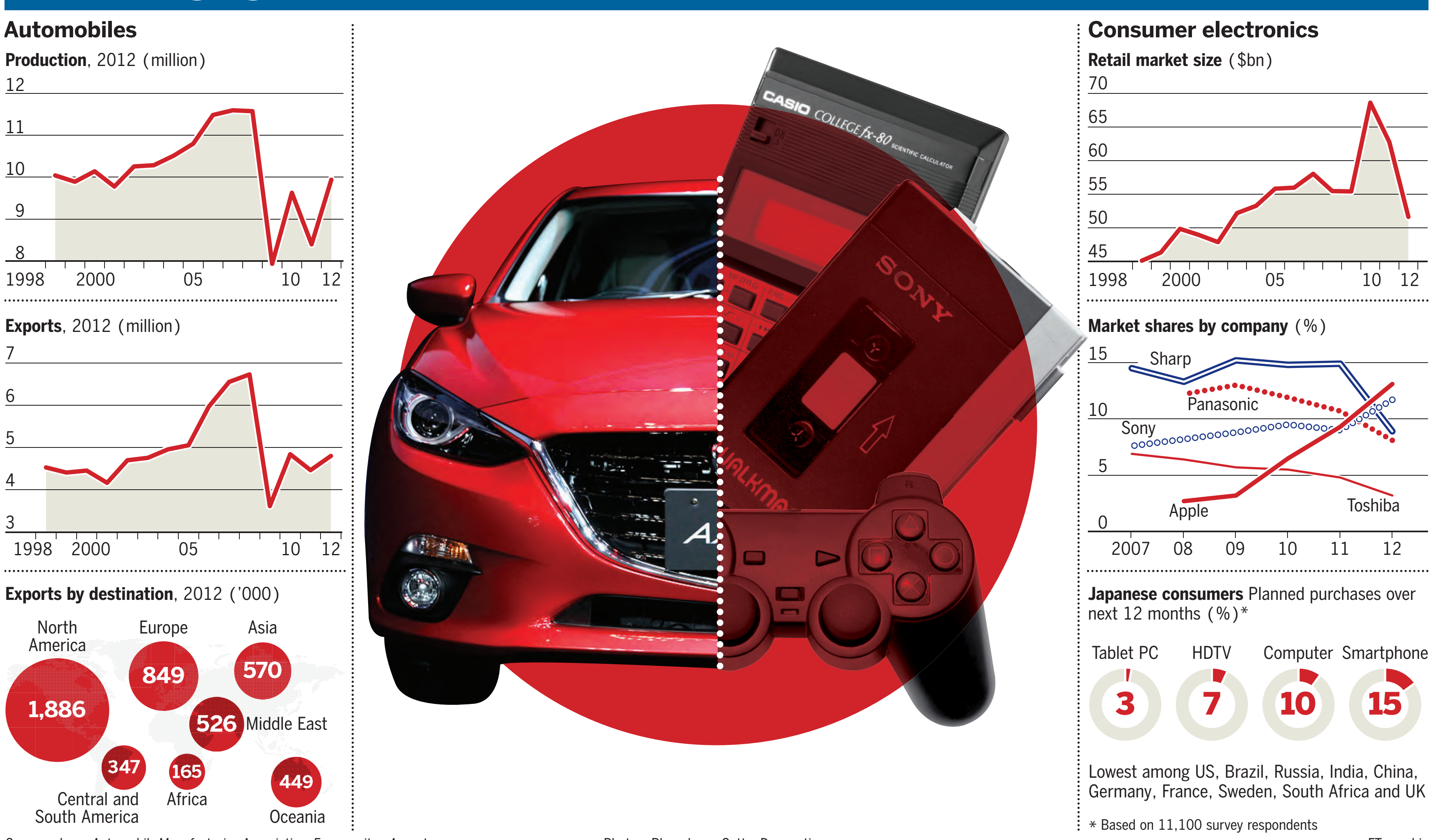
'The government has protected agriculture too much, so it doesn't have enough ability to compete with foreign industries. It should quit protecting them and get them to become global competitors. To this end, the Trans-Pacific Partnership is a great chance.'

Ayami Ohno, 21, student, Keio University, Tokyo

Former export giants try to bounce back

Industry Electronics in search of a new competitive edge, says *Jennifer Thompson*

Manufacturing: highs and lows



Sources: Japan Automobile Manufacturing Association; Euromonitor; Accenture

Photos: Bloomberg; Getty; Dreamstime

FT graphic

The two pillars of the electronics and automobile industries defined postwar Japan. Raising living standards for ordinary Japanese and providing the expectation that a job was for life, they also gave the wider world such indispensable gadgets as the pocket calculator and the Sony Walkman. Meanwhile, Japanese cars were ubiquitous.

Those days of unbridled success, however, are long gone.

The biggest Japanese companies have suffered from 15 years of deflation in their domestic market, while a strong yen made their products uncompetitive abroad.

Yet Japanese carmakers have come roaring back after the financial crisis, fuelled by renewed global demand, especially from fast growing economies in Asia, and aided by cost-cutting and now a cheaper yen.

This stands in sharp contrast to consumer electronics groups which are focused on restructuring in an attempt to stem multibillion dollar losses.

So why are these former giants languishing? The most obvious explanation is intensifying competition. In televisions, the old guard is competing not only against South Korean groups such as Samsung or LG, which make high-quality models and have invested aggressively in marketing, but against Chinese makers such as TCL or Hisense Electric, which focus on cheaper alternatives.

Japanese groups are having a tough time. In television sales, they have lost market share. Mark Newman, analyst at Bernstein, says: "TVs capture a large part of total consumer electronics revenue, but are a low-growth and low-returns business.

"Only Samsung and LGE [LG Electronics] plus some of the low-end television makers are profitable, with these groups gaining share at the expense of the Japanese, which are stuck in the middle."

The share of global market sales of those "stuck in the middle" has roughly halved since 2006. Korean makers dominate, with 37 per cent, while Chinese manufacturers have 28 per cent. Japanese makers account for less than a fifth of sales.

For the smartphone market, the situation is similar: Apple has stolen a march in software and design innovation; at the same time huge-scale, low-cost hardware makers such as Taiwan's Hon Hai have emerged.

Demand for certain goods is also on the wane. Games console makers have come under pressure, as mobile gaming becomes more popular, while TV sellers have suffered from the rise of the smartphone and tablet devices. By contrast, carmakers have seen demand rise, spurred by demand in India, China and southeast Asia.

Electronic consumer goods that are being sold are not as profitable as before. Their producers have battled against falling prices, as manufacturing becomes more efficient, driving down costs. So, what can Japanese companies do? The most obvious, and most painful, option is restructuring.

Toshiba recently announced it was halving its television production unit, with the loss of 3,000 jobs, and shuttering two of three factories. After the cuts, production will be at one overseas factory and a joint venture in Egypt. When operating four factories three years ago, the company was making some 14m units annually. In 2013, it hopes to make 11m.

Other Japanese television makers have also retreated from manufacturing in recent years. Sony cut its mid-term sales target for liquid-crystal display units by half, from 40m to 20m, two years ago. It expects sales of 15m sets in the present fiscal year.

This year, Panasonic agreed to sell to private equity group KKR a majority stake in its healthcare business, which makes blood-sugar monitoring equipment for diabetics and medical record-keeping systems, in an attempt to slim down. It is also stopping making smartphones.

Another option for groups would be finding new areas for growth. Toshiba's boss Hisao Tanaka cited data storage and healthcare as the most promising possibilities.

The more challenging route would be to regain the technological edge. Sony has sought to unite its expertise in cameras and smartphones by launching standalone lenses that attach to phones, in an effort to create the best-quality camera phone.

More broadly, Japanese makers are moving into the manufacture of smart television models that contain features such as access to the internet

They are certainly coming under more pressure to change tack.

Sharp made the deeply embarrassing admission late last year that there was "material doubt" about its ability to stay in business, and activist investor Dan Loeb called on Sony to sell part of its entertainment business to secure funds to revive the consumer electronics arm.

Masami Kashiwagi, analyst at Forrester, says: "The market is changing rapidly, and competition is intensifying, especially with Chinese and Korean manufacturers with much stronger cost competitiveness than Japanese groups." He says Japanese companies lack a sense of urgency to adjust their businesses. "Stakeholders surely want companies to spend dollars in profitable businesses."

Global pitch of national identity plays it cool

Continued from Page 1

tions from the private sector, including banks and the bigger manufacturers.

Based on the idea that Japanese small and medium-sized enterprises often make attractive and high-quality goods but do not have the capacity to invest in overseas distribution, the funds will be used to help them expand abroad in return for a small equity stake in the participating businesses.

"Japanese businesses have not invested enough by themselves in foreign countries" says Hideaki Ibuki, director of creative industries at Meti. "This investment fund should be the trigger." His department has received 80 proposals, with the winning projects to be selected next month.

The countries that Japanese businesses are most likely to focus on are those in Asean (Association of South-east Asian Nations) such as Indonesia, Thailand, Malaysia and the Philippines. Some companies are expected to strike out further.

Cosmetics goods suppliers are expected to target China. The US and Europe are regarded as promising markets for high-quality homeware.

Some of the 80 proposals were prompted by Tokyo recently winning the 2020 Olympics and the prospect that interest in Japanese culture will increase.

Meti admits the pressure is on for the project to be a success, given the size of the investment and fact that businesses that are not involved will be watching the Cool Japan fund's progress to decide whether they should follow suit.

Other challenges remain. The competition is intensifying between China, Japan and South Korea to promote their languages and cultures overseas. China's Confucius institutes have proliferated in southeast Asia over the past decade, for instance, while South Korean pop music has soared in popularity.

Like many "soft power" initiatives, the Cool Japan fund's success in economic terms will be difficult to measure.

Fukushima hurts nuclear revival hopes

Energy

Poll suggests that 80 per cent doubt Abe's Olympic assurances, says *Jonathan Soble*

Japan's successful bid to host the 2020 Olympics has reminded the world of the country's many attractive qualities, from delicious food to safe streets and punctual trains. But it has also refocused attention on a sore spot: the continuing efforts to deal with the aftermath of the Fukushima nuclear disaster.

Two and a half years after the triple meltdown, new failures at the stricken plant seem to be reported each week. Most have to do with contaminated water. Hundreds of tons of water cycle through each day, either as coolant pumped into still-hot reactors, or as groundwater seeping in and out of cracked plant basements.

Containing it all has proved to be beyond the capacity of Tokyo Electric Power (Tepco), the much-criticised owner. Some water has leaked out, exposing workers to radiation and contaminating the sea around the coastal site.

Experts say there is little risk to Olympic-hosting Tokyo, 240km south, but the situation looks a shambles: in a Nikkei newspaper poll, 80 per cent of respondents said they distrusted an assurance given to the International Olympic Committee by Shinzo Abe, the prime minister, that the clean-up was "under control".

All this has complicated Mr Abe's efforts to get Japan's nuclear industry back on its feet. In the months after the accident in March 2011, nearly all of Japan's 50 surviving reactors were closed indefinitely, amid public anxiety over safety and political wrangling between local governments and Tokyo.

The result pleased many Japanese – slightly more than half say they want the country to go nuclear-free – but left utilities struggling to replace an energy source that had provided 30 per cent of Japan's electricity.

Power bills have risen by 8-17 per cent, greenhouse gas emissions have jumped, and the cost of importing gas and other fuels has pushed a country that ran fearsome trade surpluses into a persistent deficit.

Mr Abe has been pushing gently but firmly for change – or, in the view of the anti-nuclear movement, a return to a scaled-down version of the pre-Fukushima status quo. Since coming to power in December, he has effectively abandoned a pledge by the previous, left-leaning government to end nuclear power by 2040. Instead, he has supported applications by utilities to restart a dozen idled reactors.

A new and more vocal nuclear regulator has both helped and hindered Mr Abe's cause. The Nuclear Regulation Authority has been more critical of safety flaws than its predecessors: at least one plant has been deemed unfit to reopen because it is sitting on an active faultline.

Mr Abe is counting on the NRA's perceived strictness to assuage public fears and inhibit opposition to restarting the plants. Utilities submitted the first applications for recertification in July; the NRA is expected to take until next spring to inspect the facilities, which have undergone safety upgrades, and make its first rulings.

Most expect permission to be granted. Still, even if all the reactors are allowed to reopen, Japan would have just a third the number of working reactors that it had before Fukushima.

More could be put back in service, but experts say at most half are new enough or far enough from Fukushima to be viable. That will keep pressure on the government to cultivate alternative energy sources, from renewables to US shale gas.

"Japan is thinking hard about its energy mix," says George Borovas, head of nuclear projects at Pillsbury, an international law firm. Japan's nuclear-equipment builders – Hitachi, Toshiba and Mitsubishi Heavy Industries – have become more assertive in pursuing deals abroad, he adds. Hitachi's acquisition of the Horizon nuclear project in the UK last year, for instance, put the company in charge of an entire atomic-energy enterprise – a departure from its usual, more limited role as a builder of reactors.

Meanwhile, there is still Fukushima to contend with. Ahead of the Olympic host-city decision in September, Mr Abe's government began asserting more control over the clean-up. In August, it said it would fund a project to freeze soil around the plant, to prevent groundwater seeping in and mixing with irradiated coolant.

"This is a critical issue of strong interest to the Japanese people," Mr Abe said at the time. "Instead of leaving everything to Tepco, we need to create a firm national strategy."

Some are now urging a re-examination of Tepco's future, reviving a debate dormant since the months after the meltdowns.

Clean-up and compensation costs had threatened the utility with bankruptcy until the previous government stepped in with Y1tn in capital and a promise to underwrite payments to tens of thousands of evacuated Fukushima residents.

Tepco is in effect owned now by the state, but through a complicated structure that allows the company to operate independently. Critics say that has left ultimate responsibility for the Fukushima site unclear, and may have contributed to the string of problems at the site.

Yasuhisa Shiozaki, a senior LDP politician and former chief cabinet secretary, says the government might end up taking clearer control – either of Tepco itself, the Fukushima site or of all Japanese reactors that are to be abandoned rather than restarted.

"I think it's inevitable," he said in September.

The Japanese premier (red hat) on a visit to Fukushima Getty

Voice of youth
Hiromi Hamashima

'Japan will have to resolve its problem of a declining and ageing population. This is reducing the number of workers, so Japan needs to employ foreigners. The country needs to be ready for this by improving people's communication ability, such as speaking English.'

Hiromi Hamashima, 22, student, Saitama

Tsunami zone waits in hope

Aftermath

Reconstruction in disaster area is mired in bureaucracy, says *David A McNeill*

The village of Odohama on Japan's beautiful northeast coast, once made its living from the world's largest ocean. Today, it exists only on old maps.

Thirty-one months ago the tectonic plates beneath the Pacific shifted violently about 60 miles east of here, triggering an earthquake and tsunami that carried away Odohama's 146 homes and sent its residents running for higher ground.

Most now live in temporary housing a few miles away, patiently waiting for their lives to restart. The government has offered Y2m toward the cost of new homes, and will cover the interest on old mortgages.

But even with that help, older villagers such as Koji Iwamura, nearing the end of their working lives, cannot get bank loans for new houses. "We will probably end up in a publicly owned apartment," he says. In the meantime, he and his wife while away their days in a two-roomed shelter.

The March 11 2011 disaster flattened hundreds of similar towns. Across Miyagi, Iwate and Fukushima, more than 1m buildings were damaged or destroyed and nearly 19,000 people declared dead or missing.

An initial damage estimate of $235bn by the World Bank is almost certainly too low, rendered obsolete by the price tag for cleaning up the Fukushima nuclear disaster triggered by the tsunami.

Mountains of twisted metal and splintered wood are neatly piled up on the outskirts of coastal towns and cities. But rebuilding has been agonisingly slow, stalled by bureaucracy and disputes over levees and where to relocate houses and businesses.

Futoshi Toba, mayor of Rikuzentakata, which lost most of its city centre and nearly a tenth of its people, said this year: "My sense of hopelessness for the future is shared by many of the victims."

Mr Toba cites a slow-moving plan to relocate hundreds of homeless families to hills overlooking the city, bringing him into collision with multiple bureaucracies. Clearing the hillside forest, levelling and rezoning land, and reconstructing large buildings must all be cleared by overlapping government agencies, eating up precious time.

The problem, for now at least, is not money. On the second anniversary of the disaster, Prime Minister Shinzo Abe topped up the reconstruction budget by Y6tn to Y25tn over five years.

"What's needed is imagination and politicians who lead and take responsibility," says Mr Toba.

This article appears in full at FT.com.

Voice of youth
Yuto Aoki

'The Japanese welfare state is now collapsing. Social security is basically sustained by today's generation for over 65-year-olds. I believe that the solution for now is either to accept more immigrants, or to raise the consumption tax.'

Yuto Aoki, 22, student, Kwansei Gakuin University, Nishinomiya