Japanese Firms Reveal a Grim Long-term Outlook —August 2002 Nissay Business Conditions Survey

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1. Introduction

Since the early 1990s, Japan's economy has struggled with a range of problems including persistent stagnation, declining equity and land prices, and general price deflation. If these problems persist, their impact could extend beyond the present and determine the economy's future. Corporate managers, increasingly pessimistic about the future, may restrain spending on capital investment and research & development, thus further delaying economic recovery.

The latest Nissay Business Conditions Survey (jointly conducted by NLI Research Institute and Nippon Life Insurance Co. in August 2002, covering 2,767 companies nationwide) asked companies about their long-term (five-year) outlook for the economy and business environment, and the key business issues that lie ahead.

According to the results, the overall economic outlook for the next five years is grim, with approximately 60% of companies predicting zero or negative economic growth. This suggests that the business environment could worsen as domestic competition intensifies. Moreover, less than 20% expect Japanese firms to become more competitive, while over 60% believe that human resources management and wage systems need to be thoroughly revised.

2. 60% Predict Non-Positive Economic Growth for the Next 5 Years

Regarding the average nominal GDP growth rate in the next five years, an equal proportion of companies predicts zero growth (38.4%) as moderately higher growth (38.2%). This is followed by the prediction of the same negative growth level as in the past five years (19.2%). Only 0.2% predict a higher economic growth rate (Figure 1).

By industry, predictions for a moderate growth increase are most prevalent in finance (51.7%), specialized services such as legal, accounting, and consulting (47.8%), and steel (46.3%). On the other hand, negative growth predictions (including the same negative growth as in the past five years, and negative growth) prevail in the restaurant (40.0%), construction (28.0%), and personal services industries (26.0%). By company size, predictions of negative growth as in the past five years and zero growth tend to increase as size decreases.

Figure 1 Economic Growth Outlook for the Next 5 Years

(%)

	Higher growth (over 3%)	Slightly higher growth (0～3%)	Zero growth	Negative as in past 5 yrs (-1～0%)	Negative growth (under -1%)
All industries	0.2	***38.2***	***38.4***	19.2	2.6
Selected industries					
Steel	0.0	***46.3***	40.7	11.1	1.9
Construction	0.6	36.3	32.5	***22.3***	5.7
Wholesale	0.0	43.8	34.9	18.4	2.0
Restaurant	0.0	22.2	35.6	***37.8***	2.2
Specialized services	0.0	***47.8***	34.8	8.7	***8.7***
Personal services	0.0	30.4	43.5	***24.6***	1.4
Finance	0.0	***51.7***	31.0	6.9	6.9
Company size					
Large	1.0	40.7	40.2	15.5	1.5
2nd-tier	0.0	38.7	38.8	19.0	2.4
Small & medium	0.2	37.9	38.1	***19.6***	2.8

Notes: Refers to average annual nominal GDP growth rate. Numbers may not add up to 100 due to incomplete responses.

3. 63% Expect the Business Environment to Deteriorate in the Next 5 Years

Looking ahead five years, the largest proportion of companies expect the business environment to become somewhat more severe (37.7%), followed by more severe (25.4%;). On the other hand, 21.0% see a slight upturn, while only 2.0% predict a strong upturn (Figure 2).

By industry, companies predicting an upturn (including slight upturn) are most prevalent in information services (44.4%), followed by electrical machinery (31.9%) and steel (29.6%). Companies predicting a downturn (including a slight downturn) are most common in communications (81.4%), utilities (78.7%), real estate (73.6%) and construction (68.1%). By company size, pessimism tends to increase as size decreases.

Regarding reasons to expect a business upturn, the most common response is a demand increase due to economic recovery (52.5%), followed by a demand increase due to the introduction of new products (32.8%), decrease in competitors (29.3%), demand shift to higher value added products (27.1%), and expansion of foreign markets (13.6%; Figure 3).

Figure 2 Business Environment Outlook for the Next 5 Years

(%)

	Better	Slightly better	No change	Slightly worse	Worse
All industries	2.0	21.0	13.1	***37.7***	***25.4***
Selected industries					
Steel	0.0	***29.6***	9.3	31.5	29.6
Electrical machinery	1.5	***30.4***	13.3	26.7	28.1
Construction	1.3	19.7	8.3	24.8	***43.3***
Communications	3.7	7.4	3.7	***40.7***	***40.7***
Real estate	0.0	13.2	11.3	***41.5***	***32.1***
Information services	***11.1***	***33.3***	16.7	31.5	7.4
Elec. power, gas, water	0.0	10.6	8.5	***46.8***	***31.9***
Company size					
Large	0.5	***25.8***	12.4	36.1	24.7
2nd-tier	2.0	21.8	12.5	37.7	24.9
Small & medium	2.2	20.2	13.4	37.8	25.7

Note: Numbers may not add up to 100 due to incomplete responses.

Figure 3 Why the Business Environment May Improve in the Next 5 Years

(%)

	Eco-nomic recovery	Demo-graphic shift	New products	Higher value added	Overseas market growth	Less compe-tition	Tech. inno-vation	Forex rate	Other
All industries	***52.5***	3.8	***32.8***	27.1	13.6	***29.3***	11.0	0.8	7.2
Selected industries									
Foods	***78.9***	5.3	42.1	21.1	0.0	21.1	0.0	0.0	15.8
Machinery & precis. instr.	57.9	0.0	***57.9***	21.1	18.4	13.2	***18.4***	0.0	2.6
Electrical machinery	44.2	0.0	***55.8***	***34.9***	20.9	9.3	***20.9***	0.0	4.7
Transport equipment	32.0	0.0	***52.0***	16.0	***36.0***	24.0	16.0	4.0	8.0
Publishing & printing	57.1	0.0	14.3	***42.9***	14.3	28.6	14.3	0.0	0.0
Construction	57.6	0.0	12.1	12.1	3.0	***72.7***	6.1	0.0	6.1
Information services	25.0	***8.3***	33.3	29.2	0.0	12.5	***29.2***	0.0	20.8
Company size									
Large	47.1	0.0	33.3	***37.3***	***23.5***	29.4	11.8	0.0	5.9
2nd-tier	53.7	4.0	33.3	25.4	19.2	31.6	6.8	0.6	6.2
Small & medium	52.8	4.2	32.5	26.7	10.0	28.1	12.7	1.0	7.6

Note: Numbers may not add up to 100 due to incomplete responses.

By industry, economic recovery is cited most in foods (78.9%), and demand for new products in machinery & precision instruments (57.9%), electrical machinery (55.8%), and transport equipment (52.0%). Notably, 70% of construction companies cite a decline in competitors. By company size, large companies tend to cite the demand shift to higher value added products (37.3%) and growth of foreign markets (23.5%) more than second-tier and small & medium companies.

As for causes of the deteriorating business environment, the most common response is greater competition among domestic companies (53.5%), followed by a slumping domestic economy (46.8%), request for price cuts from clients (31.9%), and increased competition from foreign companies (16.2%; Figure 4).

Figure 4 Why the Business Environment May Deteriorate in the Next 5 Years

(%)

	Eco-nomic slump	Domestic compe-tition	Foreign compe-tition	Imports drive prices down	Clients seek price cut	Clients move abroad	Demo-graphic shift	Forex rate	Other
All industries	***46.8***	***53.5***	16.2	8.3	31.9	10.0	13.4	0.8	8.2
Selected industries									
Textiles & apparel	30.8	19.2	38.5	***53.8***	***42.3***	11.5	3.8	0.0	0.0
Steel	57.6	36.4	27.3	12.1	33.3	***24.2***	3.0	0.0	0.0
Electrical machinery	28.4	31.1	***50.0***	13.5	37.8	***28.4***	4.1	0.0	1.4
Transport equipment	27.4	28.6	***47.6***	7.1	***53.6***	***21.4***	6.0	2.4	2.4
Real estate	**66.7**	46.2	7.7	0.0	33.3	0.0	***23.1***	0.0	7.7
Retail	56.7	***70.1***	12.8	7.5	4.3	0.0	***29.9***	1.1	3.7
Restaurant	***67.9***	***85.7***	3.6	0.0	7.1	0.0	14.3	0.0	7.1
Company size									
Large	38.1	61.0	***23.7***	5.9	28.8	5.1	***22.9***	0.8	1.7
2nd-tier	48.2	51.0	17.0	7.3	33.3	10.3	15.3	1.1	8.0
Small & medium	47.0	53.8	15.2	9.0	31.8	10.4	11.6	0.7	9.0

Note: Numbers may not add up to 100 due to incomplete responses.

By industry, increased competition among domestic companies is cited most in foods (85.7%) and retail (70.1%), while a domestic economic slump is of greatest concern in foods (67.9%) and real estate (66.7%). A request for price cuts from clients is cited most by transport equipment (53.6%) and textiles & apparel (42.3%), and a decrease in demand due to clients moving overseas in electrical equipment (28.4%) and steel (24.2%). A price decline due to increased imports is cited most in textiles & apparel (53.8%). By company size, large companies appear to be particularly concerned with increased competition with domestic firms (61.0%), increased competition with foreign firms (23.7%), and decreased demand due to a demographic shift (22.9%).

4. Less Than 20% Expect Competitiveness to Improve

Regarding the competitiveness of Japanese firms in the next five years, the largest proportion of companies sees no change (42.0%), followed by those who predict a slight decline (26.5%), and those who see a slight increase (17.1%; Figure 5).

By industry, increased competitiveness (including a slight increase) is predicted most in information services (33.4%), followed by transport equipment (32.2%) and communications (29.6%). Reduced competitiveness (including a slight decrease) is cited most in textiles & apparel (67.5%), steel (53.7%), and construction (40.8%). By company size, the smaller the company, the more prevalent the view that competitiveness will decline.

Figure 5 Competitiveness Prediction for the Next 5 Years

(%)

	Stronger	Slightly stronger	No change	Slightly weaker	Weaker
All industries	1.4	17.1	***42.0***	***26.5***	7.7
Selected industries					
Textiles & apparel	0.0	14.0	16.3	***32.6***	***34.9***
Steel	0.0	13.0	31.5	***42.6***	11.1
Electrical machinery	0.7	**23.0**	36.3	30.4	8.9
Transport equipment	***3.3***	**28.9**	31.4	27.3	7.4
Construction	0.0	15.3	35.0	27.4	***13.4***
Communications	0.0	***29.6***	***51.9***	11.1	0.0
Information services	1.9	***31.5***	46.3	13.0	3.7
Company size					
Large	1.0	***22.2***	49.0	20.1	3.1
2nd-tier	1.5	18.5	43.7	24.5	6.3
Small & medium	1.4	16.0	40.6	27.8	***8.7***

Note: Numbers may not add up to 100 due to incomplete responses.

As for why Japanese firms may increase in competitiveness, the most common reasons cited are aggressive R&D (30.4%), followed by aggressive movement overseas (28.5%) and organizational reform (22.4%; Figure 6).

By industry, aggressive R&D is cited most in textile & apparel (66.7%), while an overseas shift is cited in transport equipment (48.7%) and machinery & precision instruments (42.9%). Organizational reform is cited most in steel (71.4%), followed by personal services (62.5%) and utilities (42.9%). By company size, aggressive R&D is more commonly cited among smaller companies, while organizational reform and innovation in human resources management and wage systems tend to be cited by large companies.

Figure 6　Why Competitiveness May Improve

(%)

	More R&D	Auto-mation advances	Organi-zational innov.	Govt., univ., bus. coop.	Quicker decision making	Move more functions abroad	HR & wage system innov.	Entre-preneur-ship	Other
All industries	***30.4***	2.5	22.4	1.6	2.5	28.5	3.9	3.3	4.7
Selected industries									
Textiles & apparel	***66.7***	0.0	0.0	***16.7***	0.0	0.0	16.7	0.0	0.0
Steel	14.3	0.0	***71.4***	0.0	0.0	0.0	14.3	0.0	0.0
Machinery & precis. instr.	35.7	0.0	14.3	3.6	3.6	***42.9***	0.0	0.0	0.0
Transport equipment	28.2	2.6	7.7	2.6	0.0	***48.7***	2.6	0.0	7.7
Specialized services	20.0	0.0	0.0	0.0	0.0	0.0	***40.0***	***20.0***	20.0
Personal services	18.8	0.0	***62.5***	0.0	6.3	6.3	0.0	6.3	0.0
Elec. power, gas, water	28.6	0.0	***42.9***	0.0	***14.3***	0.0	14.3	0.0	0.0
Company size									
Large	22.2	0.0	26.7	0.0	0.0	26.7	***13.3***	2.2	8.9
2nd-tier	29.7	0.0	23.6	0.7	2.0	33.8	4.1	2.0	4.1
Small & medium	***32.1***	4.1	20.8	2.2	3.1	26.4	2.5	4.1	4.4

Note: Numbers may not add up to 100 due to incomplete responses.

Regarding why Japanese firms may decline in competitiveness, the most prominent reason is expensive domestic infrastructure (31.7%), followed by growth of foreign companies (24.9%; Figure 7).

By industry, expensive domestic infrastructure is cited most in steel (58.6%) and non-ferrous metals & metal products (56.3%), while growth of foreign companies is cited most in retail. Stagnant R&D is of particular concern in machinery & precision instruments (20.0%). Lack of speed in decision making is cited most in communications (33.3%) and information services (22.2%), and outflow of human resources to foreign firms in specialized services (14.3%). By company size, stagnant R&D is cited most among second-tier and small & medium companies.

Figure 7　Why Competitiveness May Decline

(%)

	Stagnant R&D	Poor govt. univ. bus. coop.	HR outflow to foreign firms	Slow decision making	Growth of foreign firms	Decline of school system	High-cost domestic infrastr.	Weak entre-preneur spirit	Other
All industries	10.0	3.2	1.5	4.1	***24.9***	1.0	***31.7***	4.6	16.7
Selected industries									
Steel	3.4	0.0	0.0	3.4	20.7	0.0	***58.6***	3.4	10.3
Nonfer. metals, metal prod.	6.3	0.0	2.1	4.2	18.8	0.0	***56.3***	2.1	8.3
Machinery & precis. instr.	***20.0***	2.0	0.0	2.0	26.0	0.0	30.0	4.0	8.0
Transport equipment	0.0	0.0	0.0	***33.3***	0.0	0.0	33.3	***33.3***	0.0
Information services	11.1	***11.1***	0.0	***22.2***	11.1	0.0	33.3	0.0	11.1
Specialized services	14.3	***14.3***	***14.3***	0.0	0.0	0.0	28.6	0.0	28.6
Retail	7.8	2.6	6.5	1.3	***45.5***	0.0	14.3	7.8	13.0
Company size									
Large	2.2	2.2	0.0	2.2	***42.2***	2.2	31.1	6.7	11.1
2nd-tier	8.7	1.3	2.2	4.8	34.9	0.0	32.3	2.6	10.5
Small & medium	***10.9***	3.9	1.3	4.0	20.1	1.2	31.6	4.9	19.3

Note: Numbers may not add up to 100 due to incomplete responses.

5. Key Business Issue—Over 40% Cite Human Resources Management

With regard to key business issues in the next five years, the most prominent is human resources management (training & development and utilization) at 41.8%, followed almost evenly by greater financial strength (25.6%), enhanced manufacturing efficiency (25.0%), new business development (24.4%), and enhanced R&D capability (23.1%; Figure 8).

By industry, human resources management is cited most in retail (67.2%), improved financial strength in real estate (50.9%), enhanced manufacturing efficiency in publishing & printing (50.0%), and enhanced R&D capability in chemicals (56.5%). By company size, the emphasis on R&D enhancement, review of business areas, new business development, and development of overseas markets tends to increase with company size. On the other hand, the emphasis on enhanced manufacturing efficiency, human resource management, and review of marketing tends to increase as company size decreases.

Figure 8　Key Business Issues in the Next 5 Years

(%)

	Enhance R&D capacity	Enhance manufac. efficien-cy	Enhance logistics efficien-cy	Enhance HR manage-ment	Enhance financial strength	Review business areas	Review market-ing	Develop new busi-nesses	Develop overseas markets	Other
All industries	23.1	25.0	13.9	***41.8***	25.6	13.7	15.8	24.4	8.8	1.5
Selected industries										
Textiles & apparel	30.2	***39.5***	4.7	27.9	11.6	16.3	16.3	20.9	***27.9***	0.0
Chemicals	***56.5***	29.0	7.2	18.1	15.2	12.3	13.8	27.5	***14.5***	0.0
Publishing & printing	20.5	***50.0***	2.3	34.1	22.7	20.5	13.6	22.7	4.5	2.3
Construction	13.4	32.5	0.6	39.5	29.9	***26.1***	11.5	36.3	1.3	0.6
Communications	14.8	22.2	0.0	48.1	22.2	14.8	14.8	***40.7***	7.4	3.7
Real estate	5.7	3.8	1.9	41.5	***50.9***	15.1	***22.6***	***37.7***	0.0	5.7
Retail	6.2	10.8	***24.6***	***67.2***	37.7	6.9	***27.2***	8.2	1.3	2.0
Company size										
Large	25.8	18.0	14.4	35.1	27.8	18.6	11.9	27.8	***13.4***	2.1
2nd-tier	25.6	24.3	14.6	39.6	24.8	14.3	15.4	24.8	10.9	1.1
Small & medium	21.8	***26.1***	13.5	***43.5***	25.6	13.0	16.3	24.0	7.5	1.6

Note: Numbers may not add up to 100 due to incomplete responses.

6.　Key Organizational Issue—Human Resources Mgt. and Wage Systems

Regarding key organizational reforms necessary in the next five years, an overwhelming majority cites the overhaul of human resources management and wage systems (62.7%), followed by promotion of business tie-ups with other companies (34.0%; Figure 9).

By industry, overhaul of human resource management and wage systems is most prominent in machinery & precision instruments (75.9%) and restaurant (71.1%) industries. Promotion of business tie-ups is cited in chemicals (44.9%) and machinery & precision instruments (40.4%), while aggressive M&A activity in wholesale (21.6%) and real estate (18.9%), shift to multi-division and subsidiary organization in restaurant (20.0% and 15.6% respectively) industries. By company size, references to subsidiary organization, holding companies, withdrawal from non-core businesses, and aggressive M&A activity increase with company size.

Figure 9　Organizational Reforms Needed in the Next 5 Years

(%)

	Overhaul HR & wage system	Shift to multi-division organiz.	Promote subsidi-aries	Shift to holding co.	Shed noncore busi-nesses	Increase M&As	Promote business tieups	Reform board of directors	Other
All industries	***62.7***	9.4	5.9	1.9	9.5	12.7	34.0	3.5	13.3
Selected industries									
Nonfer. metals, metal pr.	60.5	5.9	4.2	1.7	***16.0***	9.2	39.5	3.4	12.6
Chemicals	58.7	11.6	5.1	2.2	10.9	10.9	***44.9***	3.6	8.7
Furniture, fixture, wood pr.	64.3	***14.3***	0.0	0.0	0.0	7.1	35.7	***21.4***	21.4
Machinery & precis. instr.	***75.9***	9.9	4.3	1.4	11.3	9.2	***40.4***	2.1	8.5
Real estate	37.7	7.5	7.5	1.9	15.1	***18.9***	22.6	1.9	17.0
Wholesale	59.1	8.9	7.8	2.3	11.8	***21.6***	32.9	4.3	11.0
Restaurant	***71.1***	***20.0***	***15.6***	0.0	6.7	6.7	6.7	2.2	13.3
Company size									
Large	59.8	10.8	9.3	3.1	12.9	***20.1***	27.3	1.5	11.3
2nd-tier	63.5	11.1	6.9	2.2	12.0	14.3	35.0	2.7	11.5
Small & medium	62.7	8.5	5.1	1.6	8.1	11.2	***34.4***	4.0	14.2

Note: Numbers may not add up to 100 due to incomplete responses.

Nissay Business Conditions Survey

Survey date: August 2002
Sample size and composition: 2,767 companies, as shown below

① By company size

	No. of companies	Composition (%)
Large	194	7.0
2nd-tier	742	26.8
Small & medium	1,825	66.0
No response, other	6	0.2
Total	2,767	100.0

Note: Large companies have over 1,000 employees; 2nd-tier companies have 301- 1,000; small & medium companies have up to 300.

② By region

	No. of companies	Composition (%)
Hokkaido	142	5.1
Tohoku	186	6.7
Kanto	685	24.8
Koshinetsu, Hokuriku	195	7.0
Tokai	309	11.2
Kinki	651	23.5
Chugoku	296	10.7
Shikoku	97	3.5
Kyushu	132	4.8
No response, other	74	2.7
Total	2,767	100.0