

Survey Report on Overseas Business Operations by Japanese Manufacturing Companies

—Results of the JBIC FY2022 Survey:

Outlook for Japanese Foreign Direct Investment (34th Annual Survey) —

Strategic Research Department, Corporate Planning Group
Japan Bank for International Cooperation

1. Introduction

Japan Bank for International Cooperation (JBIC) has released the “Survey Report on Overseas Business Operations by Japanese Manufacturing Companies.” In this survey, questionnaires were sent out in July 2022 and collected by September (946 target companies, 531 valid respondents, 56.1% response rate.) We would like to express our gratitude to the companies who participated in the survey.

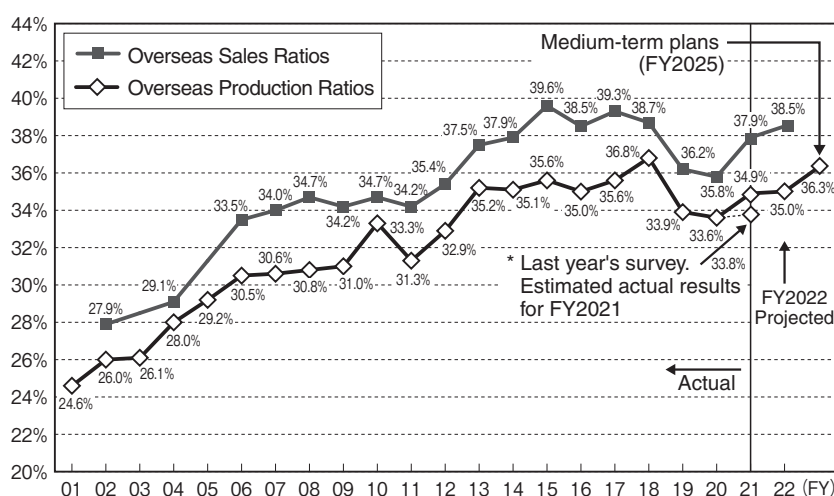
In this survey, we set out not only the regular questions, such as “Overseas Business Performance,” “Business Prospects,” and “Promising Countries/Regions,” but also “Impact of the Invasion of Ukraine,” “Supply Chain and Geopolitical Risks,” and “Sustainability Initiatives” as the special themes. This article attempts to overview the outlook of the survey result.

2. Overseas Production/ Sales Ratios

The overseas production ratio¹ in FY2021 recovered to 34.9%, exceeding the estimated FY2021 result (33.8%) in the previous year’s survey and turning upwards for the first time since the COVID-19 pandemic. The estimated FY2022 result will remain almost unchanged at 35.0%, but in the medium-term plan (FY2025), the ratio will increase to 36.3%; The recovery trend is expected to continue.

The overseas sales ratio² in FY2021 was 37.9%, up 2.1% from the previous year and the largest growth rate in the past ten years. The FY2022 forecast is for a further increase to 38.5%, close to the FY2018 (38.7%) level before the COVID-19 pandemic. (Figure 1)

Figure 1. Trends in Overseas Production/Sales Ratios (FY2001 onwards, all industries)



Note 1: Overseas Production Ratio = Overseas Production / (Domestic Production + Overseas Production)

Note 2: Overseas Sales Ratio = Overseas Sales / (Domestic Sales + Overseas Sales)

3. Medium-term (Next 3 Years) Prospects for Business Expansion (Overseas/Domestic)

In this section, we asked about their medium-term (the next three years) prospects for overseas and domestic business in general. The proportion of companies that said they would ‘strengthen/expand’ their overseas business in the medium term this year turns to be 67.2%, which increased by 3.5 percentage points from the previous year. While until last year, several companies said that it was “difficult to make a forecast now” under the spread of COVID-19, this year’s result suggests that an increasing number of companies are making business plans with a view to the new normal after the pandemic. (Figure 2)

Regarding the domestic business prospect, the proportion of companies ‘strengthening/expanding’ have been increasing second year in a row, reaching its highest

Figure 2. Medium-term (Next 3 Years) Prospects for Overseas Business Expansion

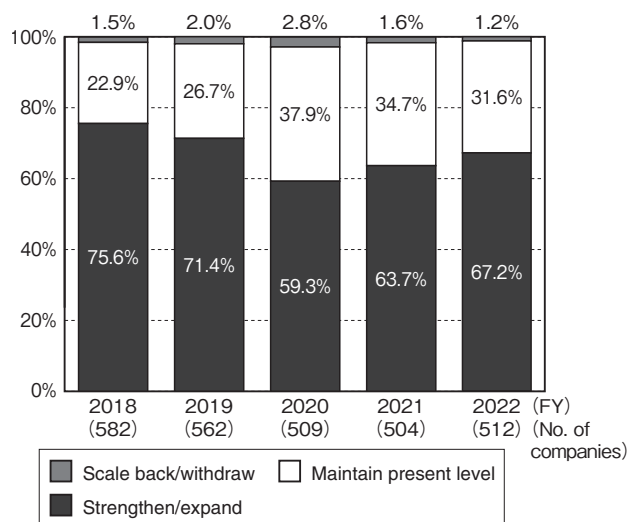
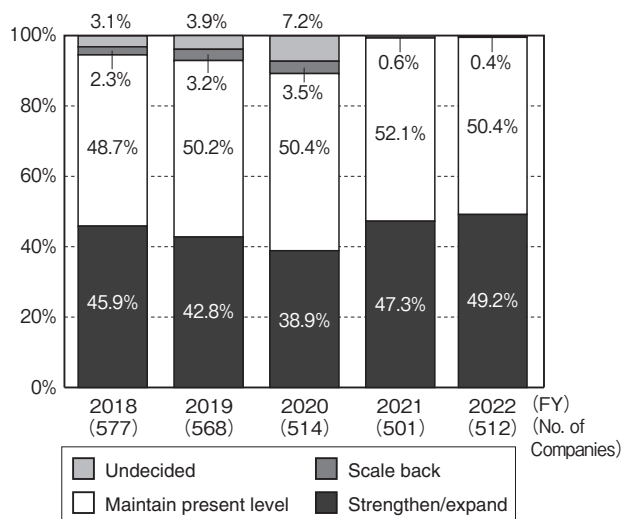
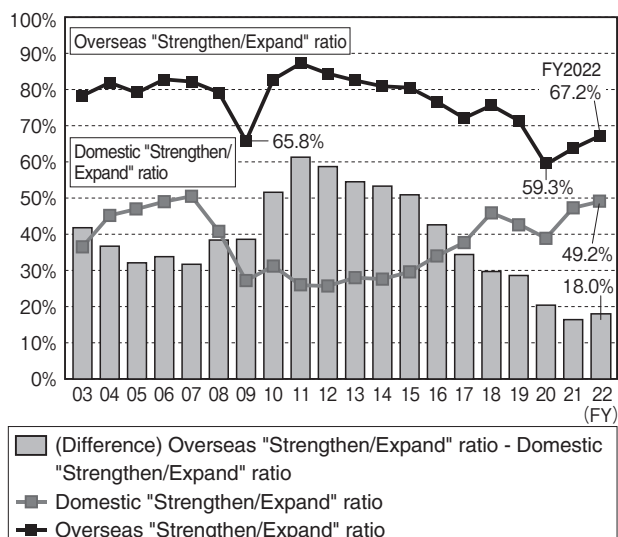


Figure 3. Medium-term (Next 3 Years) Prospects for Domestic Business Expansion



Note: The answer choice “undecided” was eliminated from the previous year’s survey.

Figure 4. Shift in Intentions to Strengthen/Expand Business (2003-2022)



level in the past decade at 49.2%, partly due to the resumption of capital investment plans, including renewal investment postponed due to COVID-19 and new investment for decarbonization. The proportion of companies that will strengthen/expand overseas operations is also rising, suggesting that strengthening domestic operations does not necessarily reflect an inward-looking orientation of companies, with some stating that they would like to “strengthen and expand” their domestic operations and “increase the ability to transmit information from Japan to overseas, assuming industry-academia collaboration” (a company from metal industry). (Figure 3)

Overall, the proportion of companies strengthening or expanding overseas operations continues to rise. However, although there is a trend towards recovery from the impact of the COVID-19 pandemic, it is different from the V-shaped recovery seen at the time of the Lehman shock, and there appears to be a reasonably large number of companies that show modest attitudes in their prospect. (Figure 4)

4. Promising Countries/Regions

In this section, we asked the respondents to name up to five countries/regions where they see promising business opportunities in the medium term (next three years), and the results were ranked as shown in the Figure 5 below.

Figure 5. Promising Countries/Regions for Overseas Business over the Medium-term (Next 3 Years)

Ranking	2022 ← 2021	Countries (Total)	No. of Companies		Percentage Share(%)	
			2022	2021	2022	2021
1	▲ 2	India	148	131	40.3	38.0
2	▼ 1	China	136	162	37.1	47.0
3	— 3	US	118	113	32.2	32.8
4	— 4	Vietnam	106	105	28.9	30.4
5	— 5	Thailand	85	77	23.2	22.3
6	— 6	Indonesia	77	67	21.0	19.4
7	▲ 9	Malaysia	31	27	8.4	7.8
8	▼ 7	Philippines	28	31	7.6	9.0
9	▼ 8	Mexico	27	30	7.4	8.7
10	— 10	Taiwan	23	19	6.3	5.5
11	— 11	Germany	21	17	5.7	4.9
12	— 12	Korea	17	16	4.6	4.6
13	— 13	Brazil	15	13	4.1	3.8
14	— 14	Australia	13	12	3.5	3.5
15	▼ 14	Singapore	12	12	3.3	3.5
16	— 16	Bangladesh	10	10	2.7	2.9
16	▲ 24	UK	10	4	2.7	1.2
18	▼ 16	Turkey	9	10	2.5	2.9
19	▲ 21	France	8	6	2.2	1.7
20	▲ 21	Cambodia	7	6	1.9	1.7

China and India swapped the first place in this year's result, with India gaining 2.3 points increase in vote share to return to first place for the first time in three years since 2019. On the other hand, China dropped to second place with a significant drop of -9.9 points from the last year's result. In contrast to India, where economic activity has recovered from the COVID-19 pandemic and high expectations are being placed on future market growth potential, China has lost a large share of the vote, mainly due to the economic downturn caused by its strict 'zero COVID policy' and other factors, as well as the intensifying diplomatic tension between the U.S. and China.

The U.S. stayed in third place with continued strong support from responding firms. While the U.S. is a mature developed country with a huge market and high expectations for its growth potential, resulting in the number of votes has been steadily increasing since 2019, the number of companies cited rising labor costs as an issue due to rapid inflation happening this year.

The number of votes received by the ASEAN countries, which all fell in the rankings last year due to the Delta stock epidemic, increased slightly this year, while the rankings of the top countries have been unchanged.

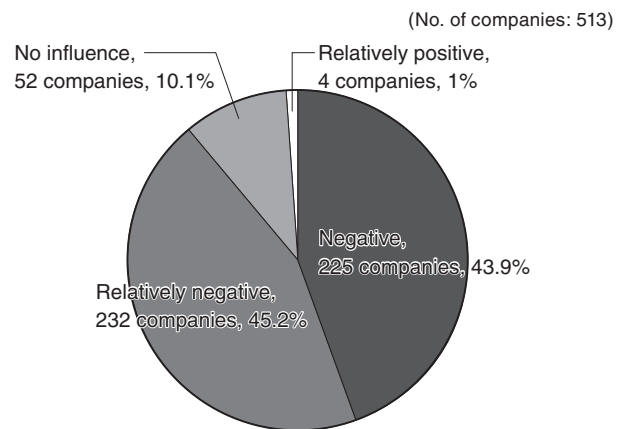
It is important to note that the rankings after the 11th through 20th places tend to shift around due to the small number of votes received. Still, Germany remains the top-ranked country in Europe, with the U.K. and France newly ranked in the top 20, and Eastern European countries can also be found in the 21st and lower places. It remains to be seen whether interest in Europe will continue to grow as the negative effects of the invasion of Ukraine become more prolonged.

5. Impact of the Invasion of Ukraine

Given the upheaval of the Ukraine crisis, we explored whether the invasion of Ukraine had an impact on their business operations regardless of the location of their overseas bases. In fact, approximately 90% of the companies responded that there was a "negative" or "relatively negative" impact from the invasion of Ukraine. By industry, the chemical industry was the most negatively affected, suggesting that companies that handle products derived from crude oil have been affected by the sharp rise in raw material prices that has accompanied the instability of energy supplies. The analysis by size showed a more pronounced negative impact on large firms than on small and midsize firms. This may be due to the fact

that large firms have more extensive operations around the world and are more affected by the suspension of local operations and supply chain disruptions due to the disruption of raw material supplies following the invasion of Ukraine. (Figure 6)

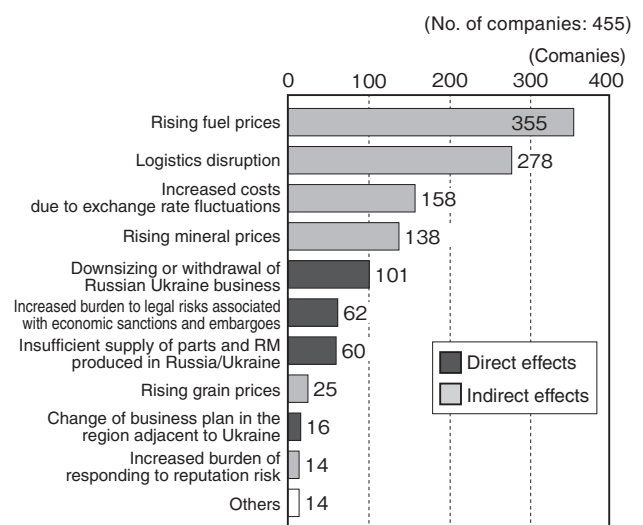
Figure 6. Impact of the Invasion of Ukraine



Note: Percentages are calculated using the number of responding companies as the population parameter.

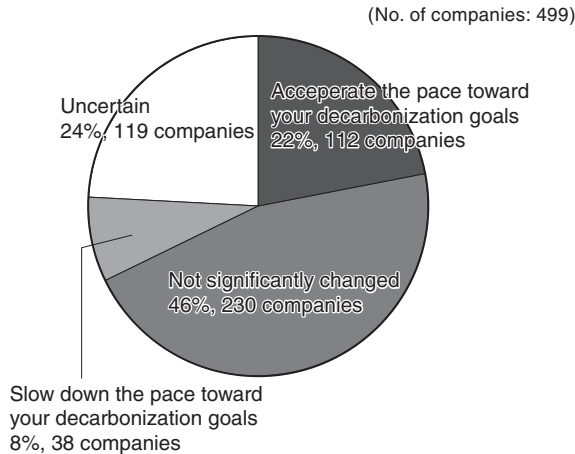
The following question was designed to explore the specific reasons for the negative impact; The top three responses were "Rising fuel prices," "Logistics disruption," and "Increased costs due to exchange rate fluctuations," indicating that the responding companies have suffered a wide range of indirect impacts as a result of the invasion of Ukraine. On the other hand, direct consequences such as "Downsizing/withdrawal of business in Russia or Ukraine" and "Increased burden to legal risks associated with economic sanctions and embargoes" were relatively small. (Figure 7)

Figure 7. Reasons for Negative Impact of the Invasion of Ukraine



We also asked whether the invasion of Ukraine had changed their attitude toward decarbonization. The result shows that 46% of respondents said there had been no change in their decarbonization efforts, while the number of firms that said they would “accelerate” the achievement of their goals far exceeded the number that said they would “slow down.” (Figure 8)

Figure 8. Impact on Decarbonization Initiatives



Note: Percentages are calculated using the number of responding companies as the population parameter.

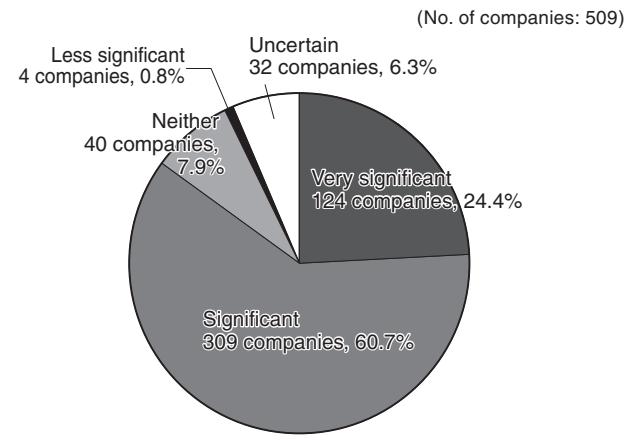
This result reflects the rising price of fossil fuels in the wake of the invasion of Ukraine and the resulting expectations for increased investment in and use of renewable energy. Responding firms voiced the view that “the industry-wide efforts are accelerating in line with requests from suppliers in Europe and elsewhere” (Electrical and Electronics) and that “the industry is facing pressure to switch to alternative heat sources as coal prices soar, and as a result, decarbonization is accelerating” (Ceramic Industry).

6. Supply Chains and Geopolitical Risks

Regarding the importance of geopolitical risk in business strategy, a total of 85% of responding companies answered that geopolitical risk is “very significant” or “significant,” indicating that a large majority of companies recognize geopolitical risk as important when developing overseas business. A cross-sectional analysis of the importance of geopolitical risk and the locations of overseas offices of the responding companies shows that the importance of geopolitical risk is uniformly high regardless of the country or region in which the companies have their production bases. This suggests that geopolitical risk is no longer a specific matter in a particular country or region

but rather a global management issue for Japanese companies. (Figure 9)

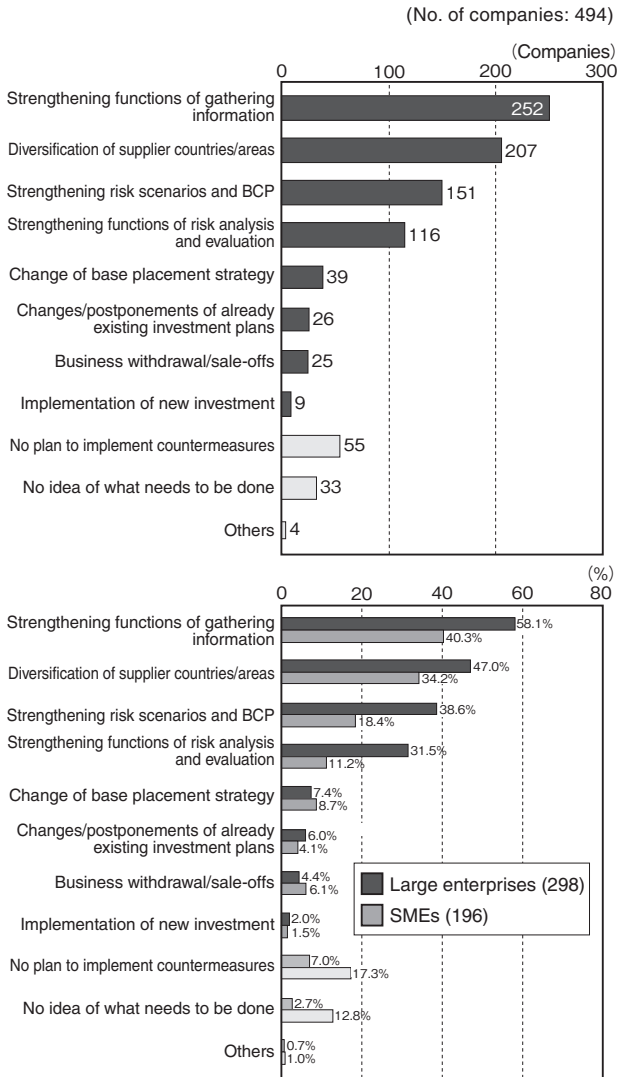
Figure 9. Importance of Geopolitical Risk in Business Strategy



Note: Percentages are calculated using the number of responding companies as the population parameter.

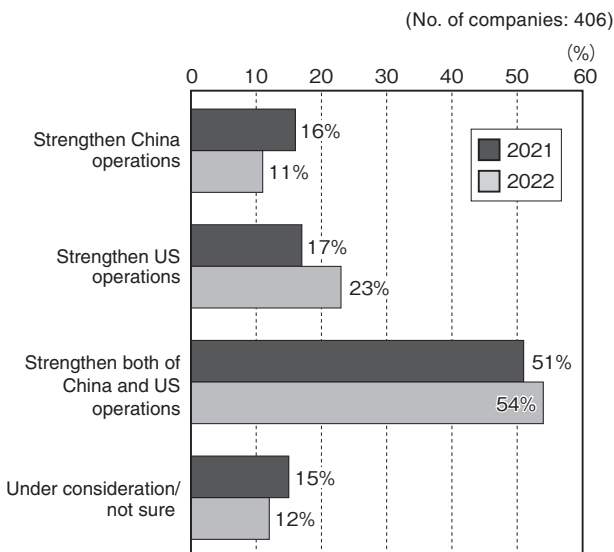
As the importance of considering geopolitical risks in each company’s business strategy is widely recognized, the specific measures taken by responding companies are concentrated on “strengthening functions of gathering information,” “strengthening risk scenarios and BCP,” and “strengthening functions of risk analysis and evaluation,” as well as “diversification of supplier countries/areas,” indicating that companies are increasingly aware of the need to gather and analyze information actively. Specifically, some respondents raised their measures that they “set up a working group within the company to discuss geopolitical risks” (Electrical and Electronics) and “set up a secretariat focusing on economic sanctions-related geopolitical risks such as OFAC” (Chemicals). On the other hand, relatively few companies have taken concrete steps to change their bases, withdraw from the business, or change their investment plans. (Figure 10)

Figure 10. Measures to Address Geopolitical Risks



Note: Percentages are calculated using the number of responding companies in each size as the population parameter.

Figure 11. Response to US-China Decoupling



Note: Comparison between the respondents that answered this question for two consecutive years.

Regarding “U.S.-China decoupling,” which separates U.S.-bound business and China-bound business given the intensifying U.S.-China friction, the same questions from the previous year’s survey were set in order for comparison over time. Although there was no indication that the U.S.-China decoupling debate has deepened over the past year, the result suggested that the percentage of companies that responded that they would “strengthen China operations” decreased from the previous year, while those who “strengthen US operations” increased. The main reasons for this trend are likely to be the sluggish economic activity and uncertain economic outlook resulting from China’s strict zero-corona policy. Still, it is also believed that companies are aware of geopolitical risks, such as the possibility of a Taiwan contingency. (Figure 11)

7. Sustainability

In response to the growing social demand for sustainability, we asked whether or not they are considering sustainability in their overseas business management. 76% of all responding companies answered that they are “considering” sustainability. In the analysis by company size, nearly 90% of large companies responded that they “consider” sustainability, while only about 60% of SMEs answered that they “consider” sustainability, suggesting that large companies are taking the lead in sustainability efforts. (Figure 12)

Figure 12. Initiatives for Sustainability (by Scale)

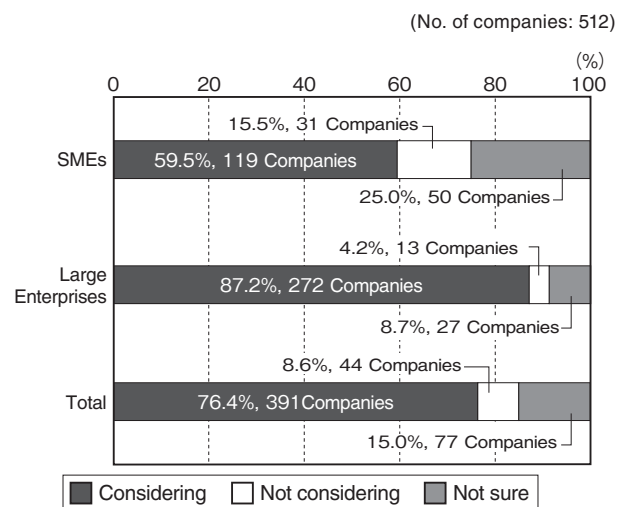


Figure 13. Initiatives for Sustainability in Stances on Future Overseas Business

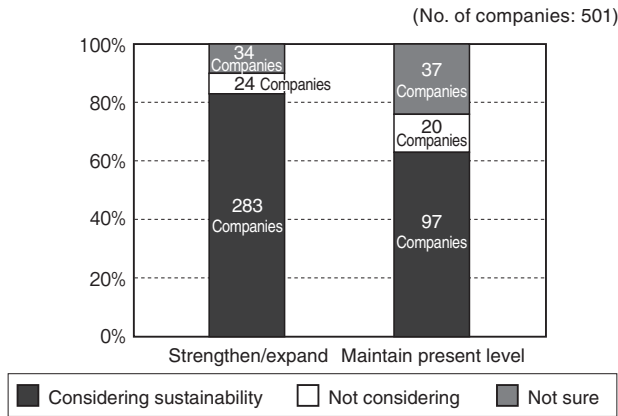


Figure 14. Initiatives for Sustainability in Stances on Geopolitical Risks

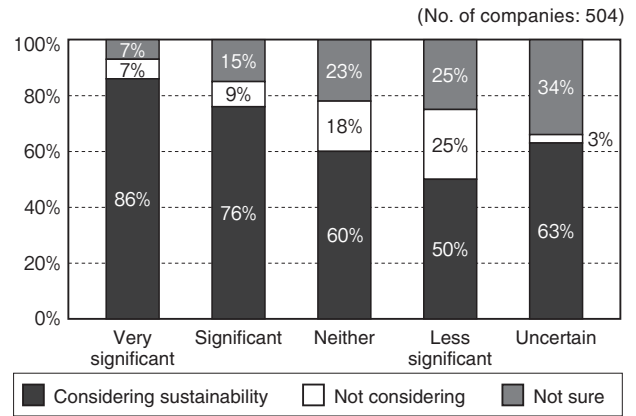


Figure 15. Hot Topics in Sustainability (by Scale)

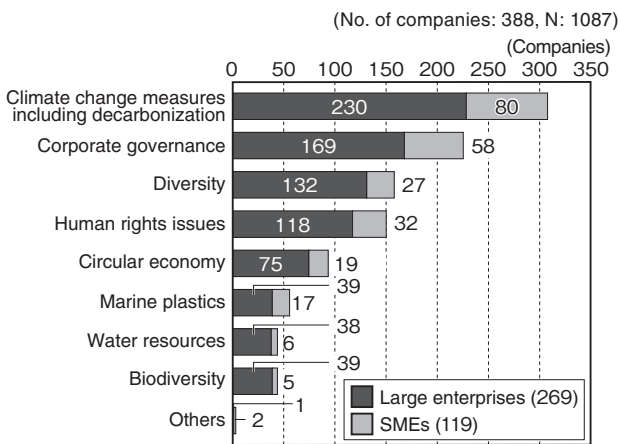
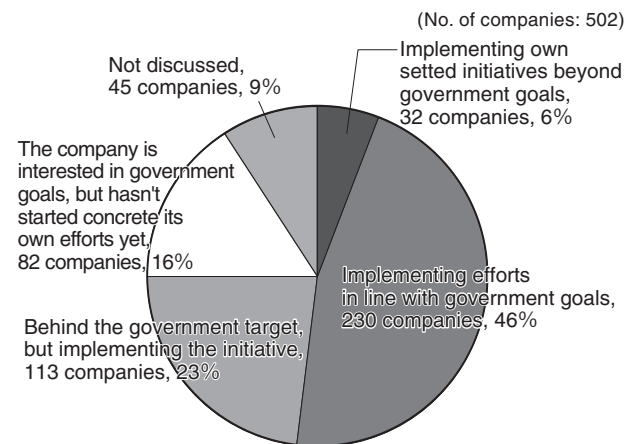


Figure 16. Initiatives for Decarbonization



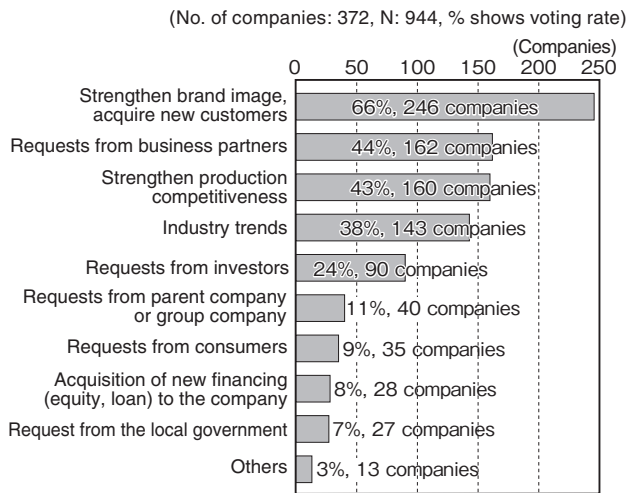
Cross-analysis of the other questions revealed that companies highly motivated to develop overseas business and place more importance on geopolitical risks are more likely to conduct their business operations with sustainability in mind. Companies that are eager to engage in global business are exposed to a wide variety of risks on a daily basis, and this suggests that they are highly aware of and eager to address external factors and global issues that can have a significant impact on their business environment. (Figure 13, 14)

There are a variety of topics within “sustainability.” In the question following the above, those companies that responded that they “consider” sustainability were asked about topics of interest within sustainability, with “climate change measures including decarbonization,” “corporate governance,” “diversity,” and “human rights issues” receiving the most votes in that order. Among these, “climate change measures including decarbonization” is by far the most crucial aspect of sustainability for Japanese businesses, regardless of size; It was suggested that about

75% of companies have already started to take some action on decarbonization, and more than 50% have met or exceeded the government target of achieving carbon neutrality by 2050. (Figure 15, Figure 16)

When we asked the companies to choose between “proactive” and “reactive” motives for their decarbonization efforts in response to various external requests and pressures, the active motive of “strengthen brand image, acquire new customers” came out on top, indicating that Japanese manufacturers are proactively working to decarbonize their operations, seeing it as a business opportunity. (Figure 17)

Figure 17. Motivations for Decarbonization



Lastly, we asked each company about its efforts to address “human rights issues” in its supply chain. In the previous year’s survey, the total of “no discussion” and “under consideration/ nothing yet” accounted for 76% of the respondents. However, in this year’s survey, the percentage of companies that have not taken any action has decreased to less than 50%, suggesting that Japanese manufacturers have made considerable progress in addressing human rights issues in light of the recent increase in social demands related to business activities and human rights. It seems that the increased demand is partially induced by the enactments of laws and regulations on business and human rights, particularly in Europe and the United States since last year and the formulation of the “Guidelines on Respecting Human

Rights in Responsible Supply Chains” by the Japanese government in September 2022. (Figure 18, 19)

8. Conclusion

This year’s survey result shows signs of recovery in the overseas business development of Japanese manufacturers, which had slowed or stagnated until the last fiscal year due to the COVID-19 pandemic. On the other hand, Russia’s invasion of Ukraine last year February greatly affected many companies’ business operations. Combined with the U.S.-China conflict, many companies have recognized the importance of geopolitical risk in their business strategies. Given this context, the survey also revealed that many companies are working to diversify their procurement sources and strengthen their information-gathering and analysis functions. In addition, concerning sustainability, which has become a global issue in recent years, Japanese companies are placing particular emphasis on decarbonization initiatives; They are actively addressing this issue while taking it as a business opportunity. Besides, significant progress has been made over the past year in addressing human rights issues in the supply chain in response to rapidly growing social demands. In the following year’s survey, we will continue to monitor the efforts of Japanese companies in each of these areas and devise the survey design to capture the trends in a more detailed manner.

Figure 18. Initiatives for Human Rights Issues Survey (FY2021)

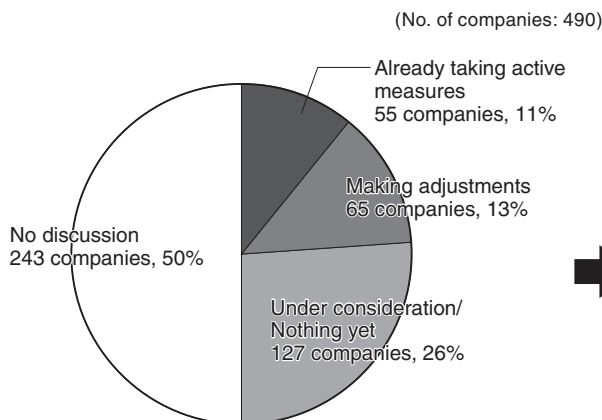


Figure 19. Initiatives for Human Rights Issues Survey (FY2022)

