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The trends in FDI inflows from Japan to India

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Abstract

This report on Foreign Direct Investment (FDI) provides insights into the characteristics of FDI inflows from Japan to India. It outlines the changing nature of the inflows in terms of industry characteristics, volume of inflows and other aspects such as the business and regulatory environment, based on secondary sources of information. It compares the experience of Japanese investment in other emerging economies with that in India. The report explains that despite having a Comprehensive Economic Partnership Agreement (CEPA) between the two countries and government support, there exist unexplored synergies and business opportunities. However, renewed interest between the two countries is propelling their interaction. Technology transfers in infrastructure and other areas such as the IT-ITeS, healthcare, and financial services sectors will help India's development, while Japan can benefit from the young talent pool that is diverse, cheap and easily available, mitigating its demographic problems due to an ageing population.

Keywords: FDI, emerging economies, India-Japan relations, institutional regulations, ODI.

1 Introduction

Japan and India have had a long history of bilateral ties. Cultural and religious exchanges began with the spread of Buddhism from India to Japan, followed by intermittent exchanges till the signing of ‘Treaty of Peace between Japan and India’ in 1952. This treaty established more formal diplomatic relations between the two following India’s independence. This was accentuated by two policies; Japan’s ‘Free and Open India and Pacific Strategy’, and India’s ‘Look East’, and presently, ‘Act East’ policy. Trade between the two nations began with India supplying iron ore to aid Japan’s reconstruction after the Second World War, and Japan began to provide aid in the form of Official Development Assistance (ODA), from 1958. At present, Japan is India’s highest ODA donor. Despite cordial diplomatic relations and numerous facilitation mechanisms, there is much unrealized scope to increase bilateral trade and investment flows. Over the years, Japan’s trade with China has increased, while trade with India has remained stagnant despite China and India having similar growth trajectories in the 20th century. However, with the advent of India’s liberalization policy and robust economic growth, Japanese companies and both governments have shown renewed interest in expanding bilateral relations.

1.1 Statement of the research problem

Despite abundant trade and investment opportunities between the two nations, bilateral trade and investment between the two remains low. This study is a preliminary exploration of the existing pattern of Foreign Direct Investment (FDI) inflows from Japan to India and discusses the problems and prospects of the same. The study analyses the main hindrances to the growth of FDI from Japan and suggests relevant areas for further study.

1.2 Research methodology

This study uses secondary data sources from online databases, government surveys and reports, publications and books to carry out qualitative and descriptive analysis for the stated research problem. Data for this study is obtained from journal articles, books, speeches by academic and industry experts; government websites like DIPP, MoSPI, JETRO reports, JBIC reports, .; and data repositories such as IndiaStat, OECD and the Worldbank.

1.3 Scope and objectives of the study

The report studies the pattern of sector wise FDI inflows from Japan to India for the time period post 2000. It identifies the trends and hindrances to FDI inflows from Japan to India by comparing Japan's investment experiences in other countries with that of India. In conclusion, the study aims to provide solutions to facilitatefurther Japanese investment in the Indian market and suggest other areas that need to be studied if bilateral investment relations are to be strengthened. In addition to analyzing the facilitators ad constraints to FDI flows from Japan to India, it also analyses the implications of the CEPA for investment ties between the two countries.

2 Review of literature

There are numerous theoretical underpinnings to explain the complex phenomenon of FDI in the world. According to IMF (1993), FDI is defined as international investment made by one economy's resident entity, in the business operations of an entity resident in a different economy with the intention of establishing a lasting interest. According to WTO (1996), FDI occurs when an investor based in the home country acquires an asset in another country (host country), with an intention of managing the said asset. The Benchmark Definition of FDI, the OECD (2008), defined FDI as the net inflows of investment undertaken to acquire a lasting management interest (10% or more of the voting stock) in a firm conducting business in any other economy but the investor's home country.

Most FDI theories rely on two aspects to explain FDI between different countries. A macroeconomic perspective is offered that draws upon the fields of international economics and international business, specifically, locational advantage and internationaltrade and often employ the gravity model to explain FDI movement across the globe. The other perspective that several theories offer rests on firm-specific elements. Market entry strategies, firm-specific advantages and other microeconomic perspectives are offered that relate to the field of industrial economics.

One of the most renowned FDI theories is the eclectic paradigm, (Dunning, 1980, 1993) that looks at FDI movement in terms of ownership advantages, locational advantages and internalization of the firms in the host country. Well known empirical studies on the OLI triad have found that market size, openness, labor costs and productivity, economic growth, infrastructure, tax regime, political risk are some of the main determinants of FDI in both developing and developed countries.

Japan's direction of FDI has undergone a radical shift in the past decade. Much like other foreign investors, the focus has shifted from investing only in developed countries to the newly emerging economies due to benefits in terms of increasing market size, low labor costs and other locational advantages. This often results in a bandwagon effect (Knickerbocker, 1973) as rival investors rush to invest in the same regions. Thus, concentration of FDI often occurs in popular regions with a concurrent deceleration of investments into other formerly popular regions (Sethi et al, 2003).

Japan's engagement with India through FDI is important for our country. Japan is the fourth largest foreign investor in India and is also looking to increase bilateral engagements between the two through economic and strategic partnerships. As observed by numerous scholars, the political, legal and economic framework of a country is important for shaping bilateral trade and investment engagement. According to North (1990, 1995), people form institutions due to imperfect insight and information asymmetry. He defines institutions as 'humanly devised constraints that shape human interaction'. Since time immemorial, institutions have been necessary to lower uncertainty in exchange, lower transaction costs, thus increasing efficiency. Hence, in this study, in addition to assessing FDI inflows from Japan to India, we also study the numerous institutional arrangements framed by both governments to facilitate India-Japan bilateral trade and investment relations. The 'new institutional theory' (North, 1990, Scott, 1987) posits that byestablishing and administering the rules to guide private players, the host country institutions play an important role in moderating and regulating the behavior of investing entities. Thus, the overarching interests of the government are important to keep in mind while studying FDI inflows from Japan to India.

The 'new institutional theory' approach has been previously used to explain the internationalization of Japan's ODI which has adapted to the changing macroeconomic conditions in the host country (Buckley & Horn, 2009). According to Cross & Horn (2009), Japan's ODI has also aligned corporate behavior to the institutional constraints present in the host countries.

Japan's business community has now understood the potential of India's market, especially its rising middle class. In the past, research by Japanese firms on India led to deferral of market entry, which is not the case anymore. More and more firms are looking to enter, not only because of the potential of India's economy, but also due to the visible success of several South Korean firms (Masanori, 2012). This study also assesses Japan's strategies in adjusting to the Indian business climate.

Furthermore, it is important to look at India-Japan cooperation from a more strategic perspective. So far, India's engagement with other South East Asian nations has been below its potential. Despite India's 'Look East' and 'Act East' policy, India's involvement with ASEAN, Japan, China and South Korea has been much less compared to that with other nations in this area (Das, 2014). The CEPA between India and Japan is expected to bolster India's involvement in this region. Apart from the obvious advantages that would accrue to India from greater integration with Japan, for the latter, there are clearly geo-strategic and political considerations. China's growing dominance in Asia is of common concern to both India and Japan. Thus, the establishment of a robust sustainable strategic partnership can counter this growing Chinese influence through greater economic and defense cooperation. India's latent potential as an economic and security powerhouse coupled with Japan's established Asian presence provides a strong basis to their burgeoning strategic and economic relationship. Prime Minister Abe's critical efforts in the past few years have led to the bilateral relationship being institutionalized in special ways that will make it durable, if not as dynamic, when Abe leaves office (Lynch & Przystup, 2017).

3 FDI from Japan to India

Trade between India and Japan began after the signing of the Peace Treaty in 1952, which formally marked the start of diplomatic relations between the two nations. India supplied iron ore to aid reconstruction in the aftermath of the Second World War, while Japan began giving Overseas Development Assistance (ODA) to India from 1958 and is now India's largest foreign donor. However, despite the cordial beginnings, trade never picked up to a great extent. At present, Japan's trade with India lags considerably when compared to Japan's other Asian trade partners like China, South Korea, Thailand, Vietnam, etc.

Table 1: Trade in goods and services between India and Japan from 2011 to 2017

Figures in dollars (billions)

Year	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17
India's exports to Japan	6.33	6.09	6.81	5.38	4.66	3.85
Growth percentage	NA	(-)1.82	4.66	(-)1.29	(-)15.48	(-)17.38
India's total exports	305.96	300.27	314.4	310.33	262.29	276.28
Percentage share	2.07	2.03	2.17	1.73	1.77	1.39
India's imports from Japan	12.1	12.51	9.48	10.13	9.85	9.63
Growth percentage	NA	3.44	(-)23.62	6.86	(-)2.77	(-)2.2
India's total imports	489.32	491.94	450.2	448.03	381	384.32
Percentage share	2.47	2.54	2.11	2.26	2.58	2.53
India-Japan bilateral trade	18.43	18.61	16.39	15.51	14.51	13.48
Percentage change	34.3	1	(-)11.9	(-)5.36	(-)6.4	(-)7

Source: Embassy of India in Tokyo, Japan. https://www.indembassy-tokyo.gov.in/india_japan_economic_relations.html (Accessed on 5/10/18)

The trade structure between the two is complementary in nature. Japan exports machinery and other finished goods, while India exports natural resource based intermediate goods (Kondo, 2012). Japan’s interest in India lies in in the latter’s growing consumer market, human resource potential, and rising economic growth, while India hopes to gain superior technology and investments from Japan in order to aid its infrastructural, industrial and technological development. Trade between the two nations has doubled from the previous decade, the 2000s to the current decade of the 2010s, with US$ 13.8 billion in bilateral trade for the financial year 2016-17. However, these figures are lower from their peak value in 2012-13 at US$ 18.61 billion. Table 1 shows the change in trade in goods and services between India and Japan from 2011 to 2017. The share of India-Japan trade in Japan’s total trade hovers at 1%, while it is at about 2.34 percent of India’s total trade (Embassy of India in Tokyo, Japan). This slow growth of trade between the two nations reflects the vast untapped potential in growth of the trade of goods and services. The government has numerous institutional initiatives, like the India-Japan Comprehensive Economic Partnership Agreement (CEPA) to aid better trade and investment relations between the two.

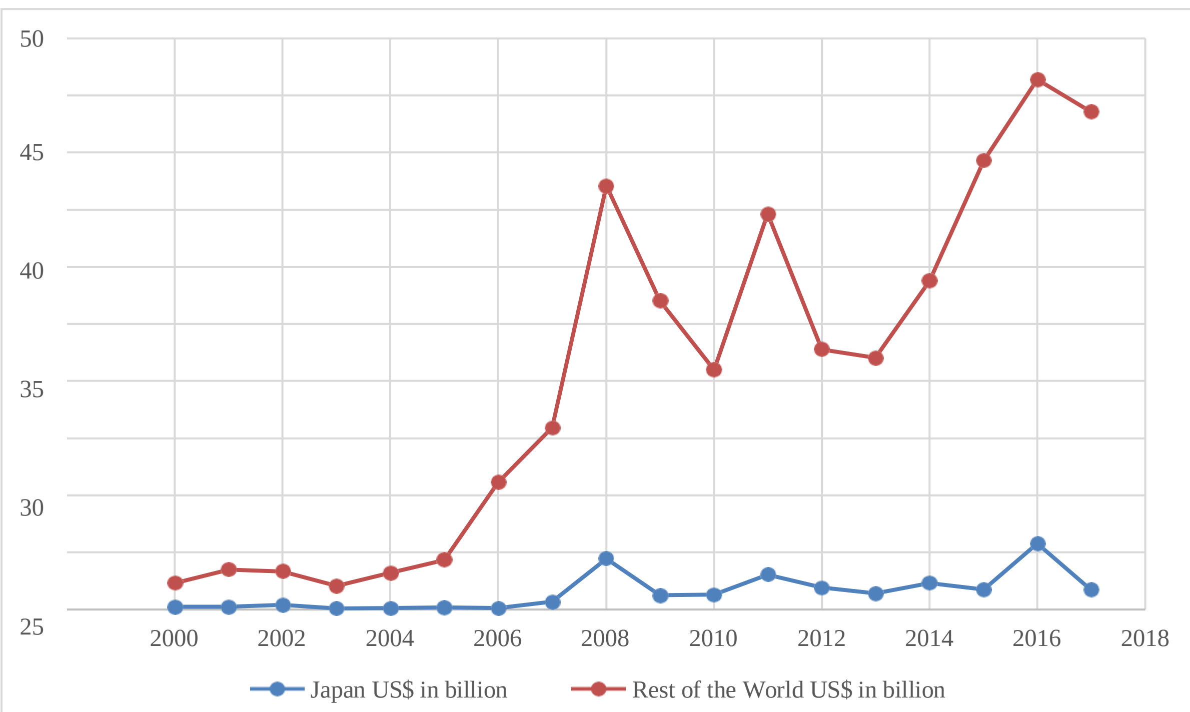
India’s primary exports to Japan have been petroleum products, chemical elements and compounds, fish and fish preparation, non-metallic mineral ware, metalliferous ores & scrap, clothing and accessories, iron & steel products, textile yarn/fabrics, machinery, feeding-stuff for animals, etc. India’s primary imports from Japan are machinery, iron & steel products, electrical machinery, transport equipment, chemical elements/compound, plastic materials, manufactures of metals, precision instruments, rubber manufactured, coal/coke and briquettes (Embassy of India in Tokyo, Japan).

3.1 Japan’s FDI inflows to India

Japanese involvement in terms of investment renewed in 1996, after India’s liberalization policy (LPG) wherein foreign investment regulations were relaxed in the Indian market. Due to the growing momentum of India’s economy following liberalization, Japanese investors were attracted to the Indian market. In 1996, which is the first year for which investment outflows from Japan to India are available in the Embassy of Japan’s records, there was an estimated US$ 262 million in FDI outflows from Japan to India. The numbers have slowly grown since then and in 2016, US$ 4.1 billion dollars was invested in the Indian market by Japan, making it the third largest investor country after Mauritius and Singapore. However, in 2017 there was a drop in Japan’s investment in India, falling to US$ 1.1 billion (Embassy of Japan). Despite the general increase in FDI from Japan into India and the growing engagement of the two countries through economic partnerships, a comparison with Japan's FDI in other countries indicates that there is room for much greater growth, given the sizeable economies of the two nations. For example, India's neighbor China is a hefty recipient of Japan's FDI with total Japanese FDI inflows to China at US$ 9.7 billion for the year 2017 (Embassy of Japan).

The two governments are working to increase the level of interaction through high level political visits between Prime Ministers Narendra Modi and Shinzo Abe, economic partnerships like the Comprehensive Economic Partnership Agreement (CEPA) signed in 2011, strategic partnerships and other governmental facilitation mechanisms. According to surveys conducted by the Japan Bank for International Cooperation (JBIC), India has emerged as the most attractive nation for Japanese investors regarding long term and medium-term investments.

Figure 1: FDI inflows from Japan vis-à-vis total FDI inflows to India



Source: FDI Synopsis Report 2016 DIPP, Ministry of Commerce and Industry, India, http://dipp.nic.in/sites/default/files/Chapter6.1.A.iii_2.pdf (Accessed on 05/10/2018)

Figure 1 gives a comprehensive view of the overall FDI inflows from Japan to India from 2000 to 2017. These amounts only include inflows received under RBI's automatic route, FIPB/SIA route, and acquisition of existing shares. Apart from a brief hiccup in the amount of investments in 2006, the overall trend of FDI inflows has remained fairly level. In 2008, there was a jump in the FDI inflows due to Daiichi Sankyo's acquisition of Ranbaxy. The following two years, 2009 and 2010 saw the effects of the recession with reduced FDI flows, which is also reflected in the decline in total FDI inflows to India. There is a possible causal connection of higher levels of investment in 2011 due to the signing of the Comprehensive Economic Partnership Agreement (CEPA) to facilitate economic relations between the two. The Fukushima Daiichi nuclear disaster coupled with the earthquake in 2012 led to the destruction of many supply chains and trade links across Japan. This is in line with the lower FDI inflows received in the two years 2012 and 2013. Investments finally picked up in 2014, with the highest reported inflows in 2016. The following year, 2017 was lacklustre in comparison.

Table 2: RBI regional offices which receive the highest FDI equity inflows from Japan

Ranks	Regional offices of RBI	States covered	Amount of FDI equity inflows		Percentage of equity inflows from Japan
			Rs in crores	US$ in millions	
1	Mumbai	Maharashtra, Dadra & Nagar Haveli, Daman & Diu	35,398.16	6,136.89	24.26
2	New Delhi	Delhi, part of UP and Haryana	27,438.95	5,106.65	20.19
3	Chennai	Tamil Nadu, Pondicherry	11,458.30	2,024.92	8.01
4	Ahmedabad	Gujarat	8,350.92	1,279.00	5.06
5	Bengaluru	Karnataka	5,917.84	1,030.07	4.07
Total of the above			**88,564.17**	**15,577.53**	**61.59**

Source: FDI Synopsis Report 2016 DIPP, Ministry of Commerce and Industry, India, http://dipp.nic.in/sites/default/files/Chapter6.1.A.iii_2.pdf (Accessed on 05/10/2018)

According to the figures updated by Embassy of Japan in India and JETRO, as of October 2017, there were 1,369 Japanese companies in India and 4,838 business establishments. Haryana and Maharashtra take the top spots for the number of Japanese companies having presence in India. Haryana had 369 companies while Maharashtra had 220 as of October 2017. Most of the already established firms are engaged in the manufacturing sector while new firms are venturing into the service sector. However, there have also been firms that have exited the market due to downsizing or turned non-Japanese due to restructuring or change of ownership.

3.2 Sector wise distribution of FDI flows

The top sectors which attract investments in India include the Service sector, Computer software and Hardware, Construction development, Telecommunications, and the Automobile industry (DIPP, 2016). This is also reflected in Japan's share in case of the automobile, services and telecommunication sectors. The following section and Table 3 highlight the sectors which attract the most investment from Japan in India. The section also outlines a few other sectors that are picking up in terms of investment inflows and business opportunities.

Table 3: Sector wise distribution of FDI inflows from Japan to India (January 2000 to December 2016)

Rank	**Sector**	**Amount of FDI equity inflows**		**Percentage of FDI equity inflows from Japan**
		Rs. in crores	**US$ in millions**	
1	Automobile Industry	26,634.46	4,729.42	18.7
2	Drugs and Pharmaceuticals	22,082.46	4,463.71	17.65
3	Services Sector*	21,301.07	3,746.75	14.81
4	Metallurgical Industries	12,297.24	2,274.44	8.99
5	Telecommunications	12,723.82	1,980.64	7.83
Total of above		**95,039.05**	**17,194.96**	**67.98**

*Services Sector includes Financial, Banking, Insurance, Non-Financial/Business, Outsourcing, R&D, Courier, Tech, Testing and Analysis

Source: FDI Synopsis Report 2016 DIPP, Ministry of Commerce and Industry, India, http://dipp.nic.in/sites/default/files/Chapter6.1.A.iii_2.pdf (Accessed on 05/10/2018)

3.2.1 Automobile Industry

The automobile industry in India has seen high growth from the beginning of the 21st century owing to India's improving infrastructure and the growing segment of middle-income consumers. The automobile sector contributes to about 7% of India's total GDP (FY 2015-16) and is the highest sector wise recipient of Japan's FDI. Japanese companies are key players in this industry. Maruti Suzuki is Japan's forefront automobile maker in India. For the financial year 2017-18, Maruti Suzuki had the largest share in India's passenger car segment with 49.98% market share. It has also expanded its activities to exporting cars and other automobile parts to the Middle East and Europe. The car 'Baleno' is a key export by the firm. This attempt also helps facilitate the 'Make-in-India' initiative in which the Japanese government has expressed interest. Toyota and Honda are other key players with 5.27% and 5.17% market share, respectively. Nissan's current activities in India primarily consist of exporting automobiles and automobile components to the Gulf countries, Latin America, Europe and other regions from its plant in Chennai. However, Nissan is also looking to boost its presence in India and is stepping up its investments in the industry. Its plans are quite ambitious as it is now looking forward to capturing 5-6% of the Indian market in the next five years.

Japanese players are quite active in the two-wheeler segment. Initially, the entry was mostly through Joint Ventures (JV) like TVS-Suzuki, Hero-Honda, Bajaj-Kawasaki. However, at present most of these ventures have split up and are now riding solo in the Indian market. Currently, the two-wheeler segment is dominated by Japanese firms like Honda, Suzuki, Kawasaki, and Yamaha.

3.2.2 Drugs and Pharmaceuticals

Japan's run with the Indian pharmaceutical industry has been filled with its shares of ups and downs. From 2000 onwards, Japan realized the potential of investing in India's pharma market due to its strong cash flows, low leverage and high debt capacity, according to Sohini Das and Aneesh Phadnis. Several Japanese firms have aggressively invested in the Indian pharmaceutical industry. The infamous Ranbaxy acquisition by Daiichi Sankyo in 2008 is one such case. The Japanese medicine giant invested US$ 4.4 billion in Ranbaxy, only to realize that Ranbaxy was facing legal action due to numerous violations against the US FDA (Food and Drug Administration) rules. The company paid a hefty penalty and Daiichi Sankyo's valuation plummeted. Further legal complications in the corporate governance of the firm led to Daiichi selling its share to Sun Pharmaceuticals in 2014. Mitsui and Co. acquired Arch Pharma, but this decision was unsuccessful as well due to issues over corporate debt restructuring.

Despite the sour experiences, Japanese interest in this sector has brought in a huge amount of investments making it the second largest sector attracting FDI in India. These companies are now making a comeback with new strategies to tackle the Indian market. Most investments are now going forward by way of collaborations, solo activities, and numerous product launches, instead of the previously popular M&A route. The key Japanese players in India at present are Eisai Pharmaceuticals, Takeda, Astellas, Dainippon Sumitomo, Mitsubishi Tanabe, etc. Furthermore, according to estimates, the supply is shifting fromcheaper medications and devices to cutting edge products in areas such as oncology. Due to high product development costs in Japan, many firms are looking to obtain manufacturing contracts in India, wholly or through joint ventures with Indian companies. According to Dr. P V Appaji, Director General Pharmexcil, as many as 20 Japanese companies have expressed interest in using the contract manufacturing benefits from the US FDA-approved facilities in India. (RIS report, 2016).

3.2.3 Service Sector

Japan's growing interest in the Indian services sector has led to increased FDI inflows from the island nation. This pattern is in line with Japan's total outward direct investment as the Finance and Insurance sector has the highest outward FDI from Japan. Sub sectors like finance, banking, insurance, non-financial/business, outsourcing, R&D, courier, tech, testing and analysis make up the Indian service sector. Japan's involvement in these sub sectors is discussed below:

(i) Banking

Three major banks from Japan have their operations running in India. Mizuho Bank has branches in Delhi, Mumbai, Bangalore, Chennai and Ahmedabad. Bank of Tokyo Mitsubishi UFG (BTMU) was one of the first foreign banks to operate in India, when they opened their branch in 1953. Their operations mostly consisted of lending to Japanese firms operating out of India. Currently they have five branches and are looking to in scale in 10 years (RIS Report, 2016). In 2013, Sumitomo Mitsui Banking Corporation (SMBC) launched their operation out of Delhi.

At present, 'samurai loans' are gaining popularity in the Indian borrower market. Samurai loans are yen denominated cross border syndicated loans offered by Japanese investors to non-Japanese borrowers. They have very low interest rates and ample liquidity options, making them a more convenient option in comparison to American and European foreign currency loans. Most Japanese investors prefer to invest in top-rated Indian firms like Reliance, ONGC Videsh, Hindustan Petroleum, etc., but are also willing to invest small amounts in unrated or unlisted borrowers.

(ii) Asset Management

On October 2008, Nomura Securities acquired a majority share of Lehman Brothers in India at US$ 225 million and was able to extend its operations in numerous onshore financial operations like securities brokerage, securities underwriting and advisory services. Sumitomo Mitsui financial Group bought a 4.5% stake in Kotak Mahindra Ltd at US$ 296 million in 2010, with the deal allowing them to team up with Kotak Mahindra in asset management, stock broking and investment banking operations. A strategic alliance with Kotak Mahindra Company, Sumitomo Mitsui Banking Corporation (SMBC) and their subsidiary Nikko Securities conducts M&A advisory activities for cross border transactions with Indian and Japanese firms (RIS Report, 2016). In 2016, Nippon Life Insurance increased its stake in Reliance Capital Asset Management from 26% to 49%. Reliance capital received 2265 crore for the deal. Due to the change in the shareholding structure, the company is henceforth known as Reliance Nippon Life Insurance Company Limited (Hindu Business Line).

(iii) Life Insurance

Many Japanese life insurance companies have collaborated with Indian and foreign companies to set up their base in India, primarily through joint ventures. Nippon Life Insurance Company Ltd has a stake with Reliance Capital. In 2008, Bank of India, Union Bank of India and Japan’s Dai-ichi Life entered into a joint venture, called Star Union Dai-ichi Life Insurance Co. Ltd. Dai-ichi Life’s stake at present is 26%, but they are planning to increase to 44% in future. Edelweiss Tokio is another joint venture between Edelweiss Financial Services and Tokio Marine Holdings Inc, incorporated in 2011. Tokio Holdings is looking to increase their stake to 44%.

(iv) Healthcare Services

Notwithstanding Japan’s unfavorable experience with the Indian drugs and pharmaceutical sector, interest in the healthcare services sector is rising. Sakra hospital in Bengaluru is India’s first 100% FDI hospital. The majority shareholders are Secom Medical Systems and Toyota Tsusho Corporation. Furthermore, interest in healthcare start-ups is on the rise. Spiral Ventures and India Japan Partnership Fund LLP are investing in local health related start-ups and exploring investment opportunities in the healthcare sector. Japanese firm M3 entered a JV with Indian HealthCare at Home to provide internet-based health services. Panasonic Corporation started offering new solutions to aid rural healthcare in India. Growing demand to provide affordable healthcare services to the population, improvement in internet connectivity, lack of adequate government spending in the healthcare sector are some of the factors attracting start-ups to venture into the healthcare market in India. Japanese firms are now targeting this niche market, both directly and by funding local start-ups that cater to this field.

3.2.4 Metallurgical Industries

Key Japanese players in India's metallurgical industry are Kobe Steel, Nippon Steel & Sumitomo Metals and JFE Steel. Some players entered the market as joint ventures, Nippon Steels & Sumitomo Metals entered into a joint venture with Tata Steel in 2013 to produce automotive cold rolled steel at an investment of 2,300 crore (RIS Report, 2016). JFE purchased 14.9% stake in Jindal Steel Works, an investment of 4,800 crore in 2010. Other high-profile investments include Kobe Steel's joint venture with Steel Authority of India (SAIL) at 1,500 crores in the Durgapur Steel Plant.

3.2.5 Telecommunications

Japan's biggest investment in India's telecommunication industry happened through TATA and NTT DoCoMo's joint venture when DoCoMo entered the market in 2009. However, due to a margin denting price war, uncertainty regarding telecom policies, and controversies over license allotment, DoCoMo's entry in the Indian market did not have the expected success. After several investments, and a dispute with TATA Sons, DoCoMo exit the Indian market in October 2017. However, the unified brand name of TATA DoCoMo is still in use for Tata Teleservices Limited. In contrast, telecom giant SoftBank from Japan is planning to invest US$10 billion by 2022. However, their reach is primarily in the sector of financial services, rather than telecommunications.

3.2.6 Tourism

Apart from strategic and business exchange, the two nations are also focusing on cultural exchange. The tourism sector, and especially business and religious tourism is a segment that is attracting investments. The Japan National Tourism Office opened in Delhi in 2017 and as of

January 2019, the third ‘India -Japan Tourism Council and Summit’ has been organized. It is a bilateral dialogue which discusses potential areas to work on in tourism. The India Japan Friendship Forum is another initiative to invigorate the tourism sector, alongside other areas like knowledge, culture and art. According to the previous Minister of Tourism Dr Mahesh Sharma, the Buddhist circuit along the lines of Bihar, the North East states, and Nepal are some of the preferred destinations for Japanese tourists. Medical and Ayurveda related tourism is also popular. In terms of investment, the telecom giant Softbank has invested in Oyo rooms. However, most Japanese companies that are in the hospitality business primarily cater to providing accommodation to Japanese expatriates and business people.

4 Institutional initiatives

Apart from private investments, the Japanese government has several projects lined up in collaboration with the Indian Government. The two nations are in the process of building up a strategic partnership, which extends to cooperation in different spheres like infrastructural development, defense and even nuclear energy. At present, Indo-US-Japan relations are at an all-time high in terms of strategic partnerships, and both nations have had military drills as a demonstration of their growing cooperation. This chapter provides an overview of the government investments and Japanese projects in India. It provides a look into the major investments, JICA’s part in India’s development, the Shinkansen project and facilitation mechanisms like Japan Plus, to name a few.

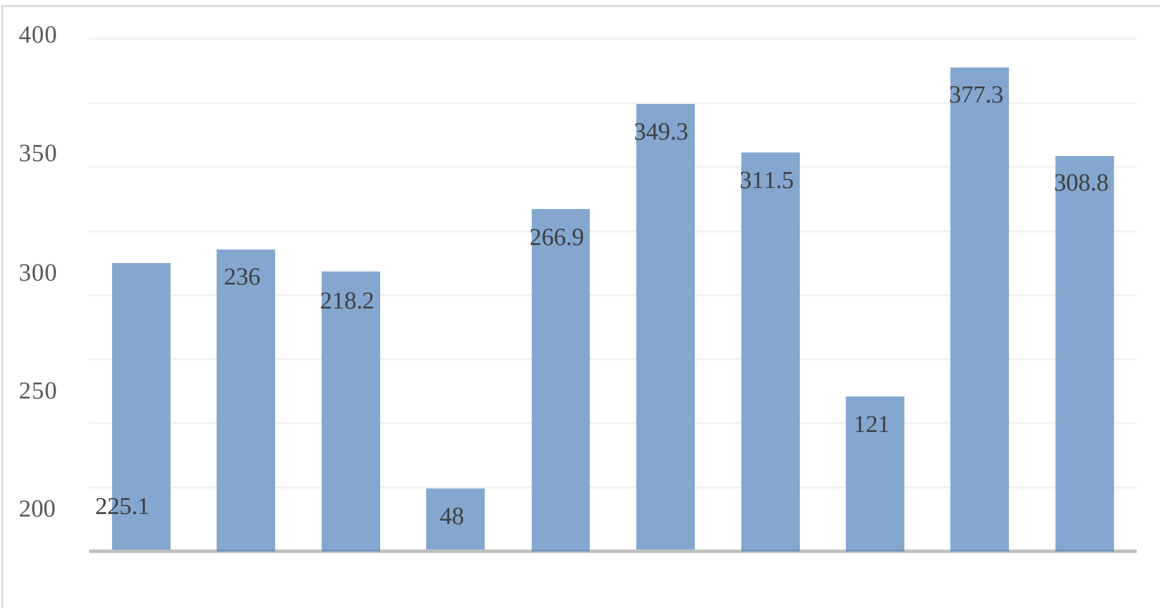
4.1 Japan International Cooperation Agency (JICA)

JICA is a governmental agency that administers Japan’s ODA to developing countries. It helps in bolstering economic and social growth in developing nations and enhancing international cooperation. The ODA by Japan is administered through three distinct channels, namely, loans, grants and technical cooperation. The loans are long term with low interest rates and include concessional funds. ODA loans are primarily to help build large scale infrastructure that requires substantial funds. These projects are supervised to promote efficient use of the borrowed funds. Grants-in-aid are transfer payments. Technical cooperation extended involves dispatching of experts, training of personnel and provision of necessary equipment. For the financial year 2016-17, there are 72 ongoing projects, with a total commitment of 309 billion yen from Japan. The total disbursement was at 208 billion yen, while the grant in aid was around 1.5 billion yen (JICA Report, 2018).

Figure 2 shows the amount of ODA loan commitments by Japan for the last ten years. There is a uniform trend in the loans for the most part, excepting in financial year 2010-11 and 2014-15 due to the earthquake and the change in central administration, respectively (JICA Report, 2018).

Figure 2: Trends in ODA loan commitment (FY2007-08 to FY 2016-17)

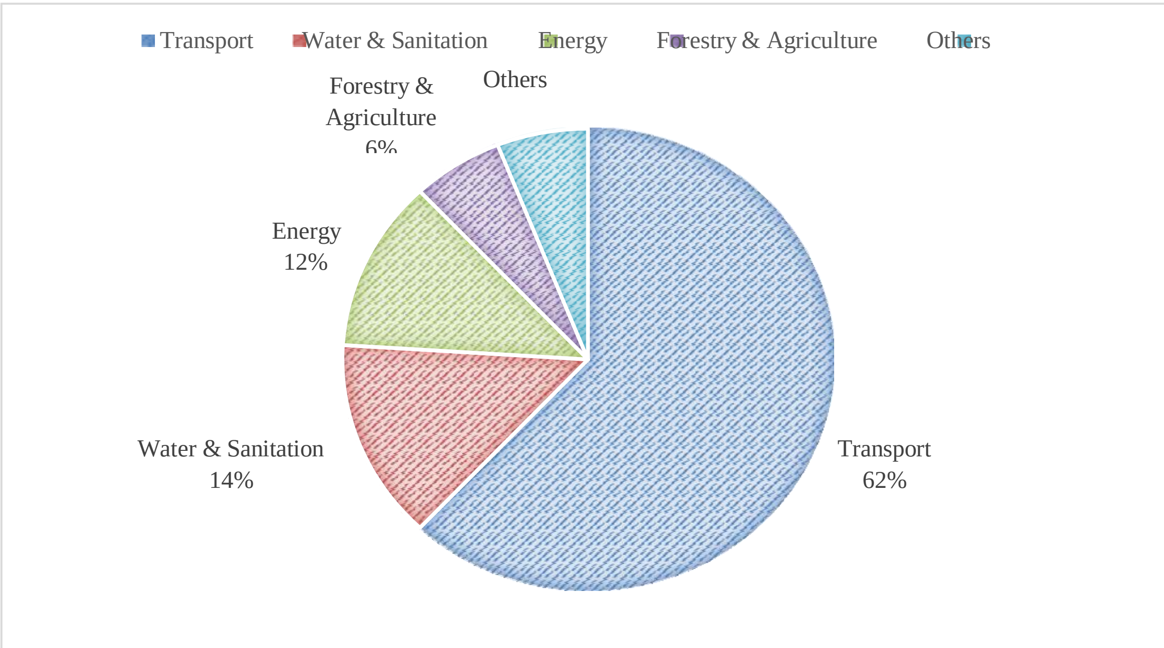
Figures in billion Japanese yen



Source: JICA Report: Operations & Activities in India, https://www.jica.go.jp/india/english/office/others/c8h0vm00004cesxi- att/brochure_12.pdf. (Accessed on 05/10/2018)

Figure 3 shows the top four sectors that JICA has invested in from FY 2007-08 to FY 2016-17. The total investment for this period stands at 2,462 billion Japanese yen. JICA has made 62% of its investments in the transportation sector, making the latter the largest sector to receive ODA assistance. JICA has assisted in building over 400km of Metro Rail network in Delhi, Kolkata, Chennai, Bangalore. It has cooperated in setting up roads and bridges in various parts of India including the North East to build the nation's regional connectivity. JICA has supported the development of port areas by increasing their capacity and connecting them with inland areas. The most ambitious project of all is the high-speed rail corridor from Mumbai to Ahmedabad which will run using the Shinkansen or bullet train technology. Japanese and other international firms doing business in India often face problems due to underdeveloped infrastructure, especially due to bad transport networks like road and train delays, which the project aims to address.

Figure 3: Trends in ODA loan commitment by sector (FY 2007-08 to FY 2016-17)



Source: JICA Report: Operations & Activities in India, https://www.jica.go.jp/india/english/office/others/c8h0vm00004cesxi- att/brochure_12.pdf (Accessed on 05/10/2018)

4.2 Ahmedabad-Mumbai bullet train project

One of the most ambitious projects by the heads of both nations is the high-speed network from Mumbai to Ahmedabad using the shinkansen technology from Japan. The project was agreed upon in the December 2015 summit by Japan's Prime Minister Shinzo Abe and his Indian counterpart Narendra Modi. Japan is financing 81% of the project with a soft loan of 13.8 billion yen, with a 0.1 interest rate. The construction began in August 2018, while the target date for completion is set for the year 2023, but Indian officials say they will attempt to inaugurate the train on 15th August 2022 to celebrate the 75th Independence Day. Japan will aid in technology transfer for the project but the components for the train are to be locally sourced to support the government's 'Make in India' initiative. Japanese officials claim that the higher initial costs will be offset by the low repair costs and extended lifespan of the trains. India expects a boom in employment and the benefits of economies of scale from this project, apart from the obvious upgradation in India's infrastructure.

4.3 Industrial townships

According to the Department of Industrial Policy and Promotion (DIPP), Japan Industrial Townships are envisaged to be integrated industrial parks with readymade operational platforms, world class infrastructure, plug in play factories and investment incentives for Japanese firms. The Action Agenda for India-Japan Investment and Trade Promotion and Asia-Pacific Economic Integration signed by Japan and India in 2015 agreed to 12 potential sites for Japanese Industrial Townships. The potential state governments have suggested incentives like exemption of CST, electricity duties, stamp duty, amongst others. The townships in Mandal, Neemrana, Ghilot and Supa Parner are funded by JETRO, while two townships in Tamil Nadu are private projects. One such hub in Chennai is a collaborative project between JGC Corporation and Mizuho Bank and the Sojitz Motherson Park in Tamil Nadu is a collaboration between Sojitz Corporation and Motherson Group. It has been agreed by both nations that the investment incentives will not be lower than in SEZs and National Investment and Manufacturing Zones (NIMZ). Various fields in the manufacturing sector like textiles, automobile, food processing and engineering are attracting investments in these townships. Firms specializing in the development of soft skills are also setting up bases in such townships (RIS Report, 2016).

4.4 Smart Cities

A ‘Partner City Affiliation’ MoU was signed by the two heads of Government in 2014 to help build cities like Varanasi as a ‘smart city’ in cooperation with Kyoto. JICA has also taken up projects to build 3 cities as ‘smart cities’; Ponneri in Tamil Nadu, Krishnapatnam in Andhra Pradesh and Tumkur in Karnataka in the Chennai-Bangalore Industrial Corridor (RIS Report, 2016). JICA has signed an agreement with the Indian Government to provide loan assistance to the tune of 8.08 billion yen (500 crores approximately) for the installation of intelligent transport systems.

4.5 Japan Plus

Prime Minister Narendra Modi and his Japanese counterpart Shinzo Abe signed the Investment Promotion Partnership in Tokyo in September 2014. Under this partnership, Japan agreed to 3.5 trillion yen in the next 5 years. Thus, the Japan Plus facilitation mechanism was especially created to manage and fast track investment proposals from Japan to their end goal. Japan Plus is to be headed by 4 representatives from the Government of India and 3 from the Government of Japan;

one nomination from METI, one from JETRO and one nomination from Aichi Prefecture. The team helps handle investment promotion for SMEs from Japan through research, outreach, promotion, facilitation and aftercare. The team also provides updated information on investment opportunities to Japanese firms across different sectors, especially in the industrial corridor projects.

5 A study of Japan's investment experience in India vis-à-vis the world

As of 2018, Japan is the fourth largest economy in the world, and the second largest in Asia, with several important trade and investment links. In terms of trade, as of 2016, Japan has Economic Partnership Agreements (EPA) with 14 nations, including Singapore, Chile, Australia, Switzerland, Philippines, Vietnam, Thailand, ASEAN amongst others. Furthermore, in 2017, Japan and EU reached agreement on an EPA that will remove 95% of tariffs that the two have, although there are many details left to be negotiated. Parallelly, a strategic agreement between the two is also being negotiated, as reported by the EU press release. Japan has ongoing negotiations for the Regional Comprehensive Economic Partnership (RCEP) with 6 countries; Australia, ASEAN countries, China, India, South Korea and New Zealand. For the year 2017, Japan's exports were at US$ 698.2 billion (Trade Map, International Trade Centre). For the same year, Japan's top export destinations were USA, China, and South Korea.

In terms of investment, Japan's foray into outward FDI was influenced by the steep rise in the value of the yen against the dollar, triggered by the Plaza Accord of 1985. The latter resulted in a rapid transfer of production lines by Japanese firms to East Asian nations in the late 1980s (Bank of Japan Report, 2007) These trends positively impacted the establishment of an industrial base in the region that energized trade in raw materials, parts, intermediate and finished goods with partners both inside and outside the regions, including local companies from the host region. This further propelled more direct investment from Japan into the countries in this region, which contributed to Japan's high growth. This is illustrated by the balance of payments statistics given in Table 4. In the early 1980s, the annual average was US$ 1.8 billion, which tripled to US$ 5.1 billion in the latter half of the decade and then increased to US$ 6-7 billion in the 1990s and US$ 9 billion in the 2000s (Bank of Japan Report, 2007).

Table 4: FDI to East Asian countries from 1981 to 2005

Figures in billion dollars (annual average)

	1981-85	**1986-90**	**1991-95**	**1996-2000**	**2000-05**
Hong Kong	NA	NA	NA	33.8	23.4
Singapore	1.4	3.3	6.4	12.7	11.3
Korea	0.1	0.8	1	5.8	4.4
NIE-s3	1.5	4.1	7.4	52.3	39.1
Thailand	0.3	1.2	1.9	4.6	2.4
Malaysia	1.1	1.1	4.5	4	2.7
Indonesia	0.2	0.6	2.3	0.8	-0.6
The Philippines	0.1	0.5	1	1.6	0.9
ASEAN 4	1.7	3.4	9.8	11.1	5.4
China	1	2.9	22.5	41.1	54.9
Total	**3.9**	**10.4**	**39.7**	**104.4**	**93.4**

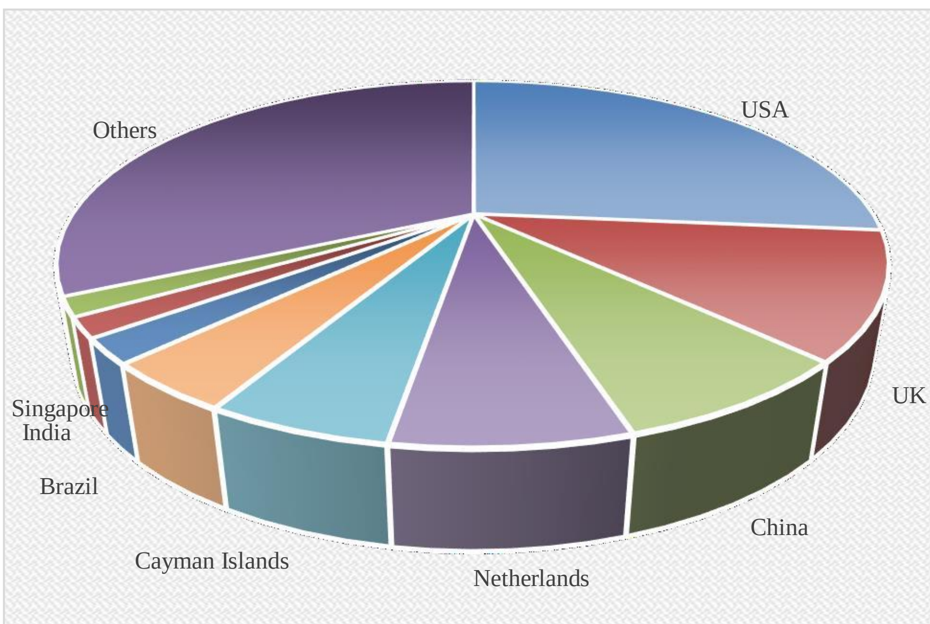
Note: China covers 1982-85 for the period marked 1981-85; Hong Kong covers 1998-99 for the period marked 1996-2000; Except for Hong Kong, Thailand and China, the period marked 2000-05 covers 2001-04

Source: External Aspects of East Asian Economies and Finance, Bank of Japan, 2007
https://www.boj.or.jp/en/research/brp/ron_2007/data/ron0701a.pdf (Accessed on 05/10/2018)

At present, Japan is one of the highest investors in the world, with cumulative FDI outflows across all countries of US$ 1.58 trillion between 2000 to 2017, as reported by JETRO. The most common investment destinations for Japanese firms are the USA, Europe and Asian countries, which are also the world's largest FDI recipients. These three regions have received more than 80% of Japan's FDI since 1996. However, the USA's share has reduced from 50% of Japan's FDI in 2000 to about 30% in 2017. As of 2012, Europe and Asia's share has increased from 38% to 58%. In terms of cumulative FDI inflows from 2000 to 2017, the USA received the most inflows, the UK placed second, China third and India was in the 9th position. Two other important destination countries for Japanese FDI are the Cayman Islands which is a tax haven with little to no tax liability and the Netherlands which is famous for being a low tax country (Kiyota, 2015). the latter two countries attracted US $1.55 trillion of Japan's ODI at the end of 2017 was US$ 1.55 trillion.

As reported by JETRO, for the year 2017, Europe received the highest ODI from Japan, with North America and Asia following closely. Furthermore, 2016 marked a record high in outward FDI from Japan, especially due to a rise in investments to the UK. The USA has been holding the position of the highest investment recipient country for the last seven years. On the Asian front, Japanese companies have been increasingly restructuring their production and investment bases from China to ASEAN (JETRO Report, 2017). In comparison, India fares quite poorly, with FDI inflows of US$ 1.1 billion for the year 2017, well below its potential. Despite India being a globally popular investment destination, as surveyed by the FDI Confidence index, Japan's investments in India were 0.6% of its total investments abroad, while the top contender, the USA, received about 30% of Japan's total outward investments.

Figure 4: Cumulative FDI inflows from 2000-2017



Source: Trade & investment statistics, JETRO 2017, https://www.jetro.go.jp/en/reports/statistics.html (Accessed on 05/10/2018)

Table 5: Direct investment assets by type of investment on a gross value basis (investments of 10 billion yen or more)

Direct investment assets	M&A type transactions	Greenfield investment	Underwriting of extension of capital for expansion of business operations	Investment for financial restructuring	Other investments	For reference: gross investments in equity capital
2012	2,224.60	65.2	1,795.00	524.10	64.10	9,783.70
2013	4,570.30	143.4	2,411.40	435.20	273.80	12,491.60
2014	4,013.90	81.9	1,370.20	484.90	77.20	12,565.40
2015	5,419.20	55.1	2,285.70	304.90	NA	12,998.00
2016	8,761.70	101.5	2,848.80	530.00	38.00	18,785.40
2017	5,781.60	77.7	2,544.40	594.20	467.60	15,072.90

Source: Balance of Payments Appendix, Bank of Japan, 2017. https://www.boj.or.jp/en/statistics/br/bop_06/data/bop2017c.pdf (Accessed on 05/10/2018)

Table 6: Direct investment liabilities by type of investment on a gross value basis (investments of 10 billion yen or more)

Direct investment liabilities	M&A type transactions	Greenfield investment	Underwriting of extension of capital for expansion of business operations	Investment for financial restructuring	Other investments	For reference: gross investments in equity capital
2012	277.3	NA	187.7	270.5	35.5	1,973.70
2013	165.8	NA	63.8	276.6	68.2	1,496.40
2014	656.9	NA	351.1	345.3	29.5	4,202.80
2015	577.1	NA	177.2	183.4	NA	2,028.80
2016	403.8	NA	513.1	83.3	22.3	2,122.70
2017	644.1	NA	361.5	32.2	21.7	2,294.20

Source: Balance of Payments Appendix, Bank of Japan, 2017. https://www.boj.or.jp/en/statistics/br/bop_06/data/bop2017c.pdf (Accessed on 05/10/2018)

Development in direct investment assets show that mergers & acquisitions make up the largest share of FDI outflows through large scale acquisitions of foreign firms by Japanese firms. Underwriting of the extension of capital for the expansion of overseas business operations also continues to account for a relatively large share, while greenfield investments by Japanese firms in host countries continue to be less, as reported by the Bank of Japan, as seen in Table 5. When compared to assets, the direct investment liabilities continue to be low, as seen in Table 6. M&As and underwriting of extension of capital for the expansion of business operations accountW for the larger share, as reported by Bank of Japan.

As of the end of 2017, globally, Japan's total share of ODI in the manufacturing sector amounted to 7,01,469 hundred million yen, while the non-manufacturing total was 9,85,990 hundred million yen. The top five sectors that received direct investment from Japan for the year 2017 were finance and insurance services, wholesale and retail, transport and equipment, chemicals and pharmaceuticals and communications. Table 7 illustrates the numbers, as reported by the Bank of Japan.

Table 7: Top 5 industries to receive ODI in 2017

Top 5 sectors receiving ODI in 2017	FDI in 100 million yen	Percentage
Finance and Insurance	3,47,505	20.60%
Wholesale and Retail	2,32,274	13.76%
Transport and Equipment	1,41,902	8.40%
Chemicals and Pharmaceuticals	1,31,470	7.80%
Communications	1,14,402	6.78%
Others	7,19,905	42.66%
Total	**16,87,458**	**100.00%**

Source: Balance of Payments data, Bank of Japan, 2017, https://www.boj.or.jp/en/statistics/br/bop_06/index.htm/#p0103 (Accessed on 05/10/2018)

5.1 Japan's investment experience in India

As discussed earlier, bilateral relations between India and Japan have been boosted by governmental measures such as the bilateral CEPA that was signed in 2011, multiple facilitation mechanisms to aid Japanese firms in India and media attention. According to surveys by JETRO, Japanese firms view India as one of the most profitable investment locations in the medium and long-term. This section qualitatively analyses Japan's investment experiences in India by looking into overall investment figures, ease of doing business, infrastructure, policy and institutional issues that help or hamper Japanese firms in India. The chapter shall also draw comparisons between other investment locations preferred by Japan such as the USA, UK, Netherlands, China and regional trade blocs such as the EU and ASEAN.

5.1.1 Business and regulatory environment

According to the 2017 Report on Investment Climate by the Bureau of Economic and Business Affairs, US Department of State, India continues to send out mixed signals regarding FDI inflows. The government actively seeks investments through economic reforms but is lax in following up on implementation of the same. Non-performing assets continue to hold back banks' profits and limit their lending. However, stable, relatively low inflation and strong management from India's central bank, the Reserve Bank of India, have mitigated the negative impact on credit. Employment, while difficult to measure given the large informal economy, appears to lag growth, while a demographic boom means India must generate over ten million new jobs every year. In contrast, Japan has a demographic problem due to the high median age in the country and a negative population rate of -0.1% as of 2016.

According to the Ease of Doing Business Report in 2018, India ranks 100th among the 190 countries that were assessed. Despite the low rank, this is a massive jump for India in comparison with last year's report when India was placed 130th. Japan's leading FDI destinations rank much higher globally with the US at 6th position, the UK at 7th, the Netherlands at 32nd, Singapore at 2nd and China at 78th. The report assesses the country based on certain parameters. Among these parameters, India ranks high in terms of getting credit and protecting minority investors. Dealing with construction permits, registering property and enforcing contracts are some of the worst ranked parameters for India according to this report. Furthermore, according to the 2014 Enterprise Survey, corruption and electricity were the biggest obstacles for firms doing business in India.

With respect to the business environment, Japanese firms surveyed by JBIC (2014) on overseas business operations cite lack of infrastructure to be the worst hurdle that they face in India. Local agents often promise adequate infrastructure to the firms which is later not implemented as the hard infrastructure in India has several quality issues. Japanese firms have had trouble with infrastructural issues such as roadways, uninterrupted electricity, problems with water pipelines, etc. However, the Japanese government has been very involved with improving India's large-scale infrastructure through ODA assistance administered by JICA. The top three sectors receiving ODA are transport, water & sanitation and energy. The massive boom in the telecommunications industry has led to an improvement in internet and phone connectivity that the firms require. Furthermore, many firms that operate in locations like Haryana and Maharashtra have not faced problems with infrastructure as these regions are suitably developed to support the endeavors of these companies (ICRIER Report, 2009). The list of Japanese business establishments in India provided by JETRO shows a concentration of Japanese firms in Haryana and Maharashtra with Tamil Nadu, Gujarat and Karnataka rising in the ranks. All five states are ranked among the ten best states in terms of infrastructure (National Institute of Public Finance and Policy Report, 2016). Severe competition by other firms, both Indian and foreign, ranks as the second most common problem according to the report. Japan has been keen on replicating the South Korean strategy of localization of production and low-priced, market specific goods to counter the intense competition that they face (Masanori, 2012). Furthermore, as a strategy Japan has expressed interest in the Make-in-India initiative to manufacture products in India and export to other nations. The automobile giant Suzuki is a market leader in exporting such finished automobiles to other countries, including Chile, Indonesia and developed markets in the EU. Japanese and other foreign firms also face problems with business regulations in India due to lack of transparency and a complex tax system.

Other problems faced by firms in entering the Indian market include the long and arduous process of land acquisition and associated approvals, poor governance, and corruption. Apart from entry, big corporations which are looking to expand their operations often encounter the same hassles once again. A common strategy is to use the help of their experienced partners, the joint venture firms, to take care of such administrative procedures. Toyota Kirloskar Motors, which had done an extensive survey before entering the market purchased large tracts of land for expansion and was able to avoid this problem. Other strategies used to counter this problem are through the help of consultants and other local agents (ICRIER Report, 2009).

The Innovation Index quantifies the level of creativity and innovation that a nation is capable of in its present state through certain indicators like institutions, quality of human capital, infrastructure, market sophistication, business sophistication, knowledge and technology and creative outputs. India ranks at 57 out of the 126 countries surveyed while the USA ranks 2nd, the UK 8th, Netherlands 4th and China 17th. Level of infrastructure and institutions are some of India's major weaknesses, while technological development, creative output and market sophistication are parameters on which it is strongest, as reported by the Global Innovations Index 2018. In comparison to most countries that receive a high amount of ODI from Japan, India's rank in innovations is much lower. The Indian government has launched an innovation program to improve the quality of Indian start-ups and attract more investors. Digital India is another pet project of the government to enhance India's innovating capabilities. SoftBank which heavily invests in some of India's major start-ups has decided to invest over 2 billion US dollars in the Indian market by the year 2020.

The existing perception that the Japanese have of human resource capabilities in India is not very favorable. The level of human resource capabilities in India has often daunted new firms, especially the SMEs with lower resources that are trying to break into the Indian market. Several Japanese firms believe that despite having an intelligent workforce, Indian workers lack skills in practical application, are low on operational efficiency and take more time to train. Toyota Kirloskar Motors (TKM) considered human resources to be the biggest obstacle they had to face in market entry. Other firms that were surveyed conveyed that the labor problems are intrinsic to their industries. In the automobile industry, TKM faced trouble with the labor union in 2001 and 2002 with strikes and a 53-day lock-out (ICRIER Report, 2009). One of the worst labor problems took place in Manesar, Haryana with Maruti Suzuki. The workforce demanded the establishment of a new union, a pay hike and more vacation time. There were also problems concerning the abusive behavior of supervisors. The turmoil finally culminated in the murder of a senior executive, extensive property damage and many injuries. However, Honda has had a much better experience with its labor union. After initial suspicion, the company trusted the workforce to form a union, which has had cordial relationships with the management through regular communication. Despite the trouble faced by the automobile industry, other sectors have not faced such problems and do not consider labor practices to be much of an issue. This is reflected in the experiences of the manufacturing, pharma and IT industries.

The state of skilled labor in India is looked upon with favor and several Japanese firms are keen on recruiting people to work in Japan. Japanese IT service companies face a shortage in terms of both the number and quality of IT engineers and are thus eyeing the budding IT professionals in India. However, training cost due to the language barrier is a concern. The Japanese government and private firms are also keen to mitigate the demographic problem facing the country given its ageing population. This is an area where India with its large, skilled workforce can complement the needs of the Japanese economy.

Since Japan is looking to boost its economy with newer businesses, it is quite interested in the 'start-up' culture in India. The aspect of creativity and innovation is appreciated. However, the bigger firms are critical of the 'jugaad' element of Indian businesses. This goes completely against the traditional Japanese management practices which have thrived on extensive planning, scrutinization of every detail and strict discipline. The work culture between the two is quite different, but both sides are now making attempts to meet each other halfway. The Japanese are aware that communication between the management and the employees will result in smoother functioning of their firms.

5.1.2 Institutional aspects

Apart from the CEPA which is in place to facilitate Japanese investment into India, India's FDI policy plays a major role. Furthermore, in January 2018, India's FDI policy was further amended by the Indian Cabinet to liberalize and simplify the process of ushering in FDI inflows. These reforms target the retail sector, aviation, pharmaceuticals, construction development, power exchange and FDI in investment. Japan's investment into the Indian pharmaceutical and construction development sector falls in the top 5 sectors in India that Japan invests in, and thus may positively impact firms operating in these sectors. Despite Japan's less than favorable experience with the Indian pharmaceutical sector, this reform will amend the definition of 'medical devices' in the FDI policy and permit a wide range of such devices into the market which can attract 100% FDI via the automatic route. Furthermore, a major share of Japan's outward FDI goes to the retail sector. This reform, which allows 100% FDI in single brand retail into the market without government approval may induce more Japanese retail players to venture into the Indian market in future, especially since Japan's fashion retailer UNIQLO is set to launch their first store in New Delhi in 2019.

According to the Enterprise Survey Report of 2014, 20% of the firms assessed, cited corruption as the main hurdle to business. The Corruption Perception Index 2017 ranks India at 81 out of the 180 countries assessed. Japan's top three ODI receivers are ranked at 16^{th}, 8^{th}, 9^{th}, respectively. Despite China's low rank at the 77^{th} position, it is the fourth highest ODI receiver from Japan.

However, foreign firms have an incentive to invest in China owing to its better infrastructure, business climate, conducive FDI policies, and availability of capital to name a few. However, in his book ‘Selling China’, Huang Yasheng points out the corruption in China’s governance is discriminatory and supports certain foreign firms, hampering the competitiveness of private domestic firms.

Despite the release of the National IPR Policy and the establishment of India’s first intellectual property (IP) crime unit in Telangana in 2016, India’s IP regime continues to fall short of global best practices and standards. Several “Notorious Markets” across the country continue to operate, while many smaller stores sell or deal with pirated content across the country. India made some progress in fulfilling its mandate to become more market-oriented and competitive in 2016, but Prime Minister Modi’s courtship of multinationals to invest and “Make in India” has not yet addressed longstanding hesitations over India’s lack of effective IPR enforcement (Investment Climate Statement, 2017). The Intellectual Property Index tabulated by the US Chamber of Commerce Global Innovation Policy Center, which analyses the intellectual property climate of 50 countries, India ranks 44th. US is ranked first and has the most robust IP climate and North America and Europe rank very high on this list due to their developed and mature economies. Most emerging economies still struggle with the issue of ethics in business.

5.2 A study of Japan’s investment experience in other new emerging markets

Japan’s investment in South East Asia has been on the rise since 2011 with 50% of its investments in Asia going to ASEAN-6 (DBS Report, 2016). Despite high costs arising from the lack of infrastructure, market openness and growth are attracting Japanese investors to this region. As explained in the above sections, Japan’s foray into outward FDI picked up in the early 1980s, and from 2011, its FDI has been targeted at emerging markets in Asia, and to some extent Central and South American nations like Mexico and Brazil. Cayman Islands is one of the top recipients due to tax exemption policies. South Africa is the only African nation to attract FDI from Japan, though at nominal levels. According to the JBIC survey in 2015, 56% of Japanese investors were looking to invest in ASEAN countries, especially in Vietnam, Indonesia and Thailand. In contrast, the survey reported a 48% fall in the number of investors looking to expand to China. In 2011, Japan’s investment in China stood at US$12.6 billion, which reduced to US$ 8.6 billion in 2015. In contrast, Japan’s FDI inflows to ASEAN rose from US$ 15.7 billion in 2011 to US$ 20.2 billion in 2015 (JETRO, 2016). Initially, Japan's rise in FDI to the South East Asian region could be attributed to diversification strategies and a tendency to reduce investments in China, owing to economic considerations such as high labor costs and increasing domestic capacity in China. Other geopolitical considerations include the deterioration of bilateral relations between Japan and China in 2012 due to the Senkaku Islands dispute. However, the sustained rise in FDI to the South East Asian region could plausibly reflect broader economic considerations due to the growing market in this region (DBS Report, 2016). According to the JBIC surveys, Japanese investors face problems in South East Asia mainly due to rising labor costs, problems in hiring efficient management level staff, unclear legal systems, political instability and underdeveloped infrastructure. When juxtaposed with the investment experiences of the Japanese in India, we see that underdeveloped infrastructure, implementation problems arising from non-transparent and inefficient regulatory mechanisms are some of the common issues. In contrast, efficient skilled labor and low labor costs in several sectors make India a favorable investment destination.

Amongst the ASEAN countries, Japan has been a long-time investor in Vietnam. It is the second largest FDI investor in the country, after South Korea, with 3,835 projects as of July 2018, representing a total investment of US$ 39 billion, (Ministry of Planning and Investment, Vietnam). Japan is Vietnam's highest ODA provider and is also the fourth largest trading partner of Vietnam. The investments were stable at US$ 500 million from 1995 to 1998. The period from 1999 to 2003 saw a reduction in the amount of inflows, after which there was a marked improvement with a peak in investments in 2008. The amount of investments lowered in 2009, following the global financial crisis. The numbers have recovered since then. (Hanh et al, 2017). Majority of Japan's investments have focused on the sectors of manufacturing, infrastructure and energy projects. However, over the last five years, investments have grown in consumer goods sectors, including retail and hospitality services.

Vietnam and Japan launched a Joint Initiative in 2003 to improve the business environment in Vietnam. The aim was to increase Vietnam's competitiveness and attracting other FDI investors, as Vietnam's economy is highly influenced by FDI inflows. The 'action plan' for the Joint Initiative is being conducted in phases by the two governments and even the private sector, and the 7^{th} phase of this plan began in late July 2018. Evaluation studies conducted by JICA on the Joint Initiative has seen positive reviews in fields of customs and intellectual property.

The Vietnam Japan EPA was signed in 2008 and came into force in April 2009. It is expected to liberalize and facilitate trade between the two countries through reduction and exemption of tariffs according to prior commitments between the two nations. Apart from the VJEPA, the ASEAN Japan Comprehensive Economic Partnership (AJCEP) has boosted trade between the two through further reduction and exemption of tariff lines with 3426 tariff lines with zero percent rate effective from April 2018, in several industrial goods such as machinery, equipment, iron, steel copper, metals, etc. According to a survey by JBIC in 2015, Japanese investors have faced problems in Vietnam owing to rising labor costs, unclear execution of legal systems, intense competition from other companies and underdeveloped infrastructure. These problems are common across other emerging markets that Japan invests in, including India.

Japan is Thailand’s largest investor, with cumulative inflows from Japan to Thailand for the period 1985 to 2016 standing at US$ 85 billion, which is more than double the cumulative inflows from Thailand’s second largest investor, USA. Furthermore, cumulative investments for the aforementioned period indicate that 43 percent of Thailand’s total investments come from Japan. Thus, Thailand’s FDI climate is considerably influenced by Japan. The JBIC Survey in 2015 reveals that, much like Vietnam, rising labor costs and intense competition from other companies are the two most cited problems faced by investors. Apart from this, social and political instabilities are an issue as Thailand often faces natural disasters like floods and political coups. In addition to the AJCEP, Thailand and Japan have signed the TJEPA, the Japan Thailand Economic Partnership Agreement in 2007. The TJEPA registered little immediate change in investments and there was a drop in investment in 2009, which can be attributed to the Global Financial Crisis. A political economy approach by Hartley (2017) postulates that global economic events such as the Asian Financial Crisis in 1998 and the global recession in 2008-09 have affected Thailand’s FDI climate negatively, while positive changes have been brought about by domestic economic reforms such as Thailand’s Board of Investment’s (BoI) economic plan. However, after a peaking of inflows from Thailand to Japan in 2012 and 2013, there has been a rapid drop in investments from 2014 that lasted till 2017.

Japan’s large immigrant community in Brazil, the ‘Nikkei jin’, continues to be a massive influencer in Japan’s and Brazil’s bilateral relations, improving dialogue and cooperation due to the human assets in the country. Japan’s cumulative outflows in the period 2000 to 2017 shows higher outflows to Brazil in comparison to India. Direct investment for the year 2016 was at US$

1.4 billion. Japan is the 6th largest FDI investor in Brazil, in terms of FDI stocks and the two nations are now looking at further cooperation in the fields of science, technology and energy. Initially, Japan's investments in Brazil were restricted to obtaining natural resources. However, by 2015 Japan was investing 40% in the manufacturing sector, 35% in the service sector and 22% in the primary sector (Embassy of Japan). Brazil's business environment is plagued by problems such as its opaque bureaucracy, a complex tax regime, credit risks in the market, underdeveloped infrastructure, etc.

There are commonalities in the problems that the Japanese investors face in investing in other emerging markets in Asia as well as in Brazil. Institutional issues regarding implementation of regulatory mechanisms, lack of transparency in the legal system; and underdeveloped infrastructure are the most commonly cited problems. Intense competition from other companies, both local and other foreign investors are also cited by the Japanese investors doing business in these regions. Firms from South Korea, China and Singapore are the most common foreign investors that the Japanese regard as competition in the widely popular South East Asian region.

6 Conclusion

According to the United Nations Conference on Trade and Development's (UNCTAD) 2018 World Investment Report, India is one of the top 10 host economies that attract FDI. The year 2016 saw a record high in FDI inflows at US$ 44.5 billion (UNCTAD). The subsequent year, 2017 recorded a decline and the FDI stood at US$ 39 billion, reflecting the global downward trend. India's specialized service sector, English speaking competitive workforce, large potential market size and growth; have contributed to India's attractiveness as an FDI destination. As of 2017, Japan is the 5th largest FDI investor in the India and accounts for 4% of India's FDI inflows. The top sectors that Japan invests in India as mentioned in Section 3 are reflective of the top sectors that attract FDI in India. Notwithstanding Japan's importance as a source of investment, the secondary data analyzed suggests that Japan's investment experience has a lot of unrealized potential in the case of India. Despite constraints posed by infrastructure and regulations, both nations would clearly benefit from building stronger relations. Technology transfer in infrastructure and other industries would help India's development, while Japan could benefit from India's young talent pool that is diverse, cheap and easily available.

Japan has been aggressively attempting to stimulate its economy since April 2013, after the onset of ‘Abenomics’. Quantitative and qualitative easing by increasing the money supply, negative interest rates and export promotion are some of the major facets of ‘Abenomics’ to bring out Japan from its two-decade long stagnancy. At this juncture, Japanese firms have more incentive to accelerate overseas business, which is where India can prove to be a promising candidate. The JBIC Survey on overseas business operations 2014, identified the potential growth of the labor market, labor costs, size of the local market, India’s potential as a production base for exports as the most attractive aspects of the Indian market, which are of interest to Japanese corporations.

Improvement in business regulations is needed to propel Japanese FDI into India, as the cumbersome business environment in India is one of the main reasons cited by Japanese firms as hurting their profitability in India.

Japan’s established presence lies in providing superior quality products with high prices that cater to cross national consumer segments (Enatsu, 1997; Nonaka & Katsumi, 2007; Horn, 2015). However, this strategy has better chances of success in advanced economies, and not emerging ones which are overflowing with spurious products, cheap alternatives and lower consumption capacity. Japanese firms thus engage in strategic planning that will suit the needs of the Indian consumers. However, they also have been dealing with risks of political and economic uncertainty (Khanna et al, 2005) including geographical complexity and a very diverse socio-cultural environment (Itou, 2006; Oku, 2008). The Japanese are now adopting some of their strategies of localized production and actively targeting the needs of the Indian middle-class consumer. From primarily investing in the manufacturing sector, several firms have diversified their interests into more niche markets such as healthcare, start-ups, etc. Furthermore, Japan’s interest in India’s service sector is on the rise. This reflects the sector wise distribution of Japan’s total outward FDI as well.

According to the assessment by Research and Information System (RIS), the CEPA has been effective in introducing better security measures for investments while introducing a liberalized framework for trade of goods and services. Notwithstanding criticism about the tariff reduction process, there has been a stable and continual rise in the number of Japanese in India after the introduction of the CEPA, indicating a positive impact of the same.

This paper has explored some of the factors influencing Japanese investments in India. Many areas, such as the role of culture or organizational set up, quality, however, remain unexplored. The discussion clearly indicates that despite numerous governmental measures to facilitate Japanese firms in India, which are well advertised in the Indian media and in government press releases, the level of bilateral trade and investment does not reflect its full potential. Exhaustive primary research on sectoral trends and problems faced by individual firms may provide a more insightful understanding of the prospects for the said challenges facing Japanese businesses in India and the steps required to strengthen bilateral trade and business relations between the two countries.

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