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# Osaka Renaissance News

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Welcome to “Osaka Renaissance News” - the email newsletter of Osaka City Government’s “Urban Revitalization Task Force”.

## **The Osaka Urban Revitalization Task Force**

We are the first *City Task Force* established in Japan to address urban regeneration and revitalization issues within a common framework. We also collaborate with the central government’s “Urban Renaissance Program”. The role of the task force is to coordinate and promote the set of initiatives that taken together form the Osaka Revitalization Plan.

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“Osaka Renaissance News” is distributed through multiple email channels to spread the word about important initiatives taking place in Osaka.

## **This Issue: “Economy Shift”**

The economy is changing towards a service structure, and lifestyle orientation. However, manufacturing, exporting, and distribution remain essential components still.

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## **The Osaka City Blue Print for Urban Revitalization addresses:**

- Urban Regeneration
- Business stimulation (notably in knowledge-based industries)
- Tourism and life-style
- Education – especially professional and life-time learning
- Foreign direct investment

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# ECONOMY SHIFT

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## AUTHOR'S INTRODUCTION

“It’s the economy, stupid”, one US president famously remarked. Osaka’s economy has been in need of fixing for many decades. However, changes in Japan’s economy, which have affected Osaka negatively, are now starting to turn. Manufacturing investment is starting to return after years of moving production offshore. The huge plasma display plant, built by Matsushita on Osaka Bay, is a leading example. The financial sector is settling down, after years of consolidation; one company, Fuji Fire and Marine, even decided to retain its centre of operations in Osaka, rather than move to Tokyo, citing improved efficiencies. China has become Japan’s largest trading partner, indicating a new shift in the direction of trade. Osaka benefits owing to an industrial structure that fits with the Chinese economy.

The economy hit bottom in Q1 2002. Land prices started to turn positive in 2004. Foreign capital has caused talk of a property bubble. This is a far cry

from the talk of business closures. There are still too many offices untenanted. On the other hand, many condos are being built in the city centre, and the growing residential population is creating new demand for services. Osaka is becoming a lifestyle hub, befitting its role as a metropolitan centre.

The most exciting change is in the mind-set, which is making Osaka open to foreign investment. Deregulation and the reform of local government finances are providing opportunities for the private sector. Although not obvious yet, changes in the Osaka economy, and the more open mind set make it possible that one day Osaka can become a real alternative to other Asian centres for logistics, and even manufacturing. At least one foreign company has recently made Osaka the base for its Asian headquarters. Now the question is will it start a trend.

**Alex Stewart**

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## ECONOMY SHIFT

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**In this issue we look at the structure of the economy, and growth potential.**

### **Structure**

The structure of the Osaka economy has changed significantly, since the bursting of the financial bubble. To illustrate this: in 1990, the manufacturing and services segments of the economy, each accounted for 18% of Osaka city's GDP. However, by 2004, manufacturing had declined to 11% and services had risen to 26%. During this period, not only manufacturing but the construction and financial sectors declined too.

The shift from a manufacturing centred economy is long standing, starting in the 1970s. It accelerated after the bursting of the Bubble, in 1991, especially as manufacturing shifted offshore to low-cost centres. After financial Big Bang in the late 1990s, many major companies moved head office functions to Tokyo, which also had a weakening effect on the economy.

The good news for the Osaka economy now is that the underlying trend to shift production or head office functions out of Osaka has slowed down and may have run its course. The result of this long-standing squeeze is that in every direction, slack has been cut from the system, and most major shifts have occurred. The shift of manufacturing offshore for example, and the shift of head office functions to Tokyo. At the same time, as this newsletter series has been describing, Osaka is turning into a more service-driven and lifestyle-oriented economy (for example,

tourism is now being strongly promoted).

The growth of the services sector follows naturally as living standards rise and consumers and corporates require more sophisticated kinds of services. However, Osaka (like much of Japan's economy) remains at heart a manufacturing economy. Even though manufacturing has shrunk to 11% of GDP in the city area (note, 18% on a prefecture basis), it generates many jobs downstream in service fields. Without manufacturing, and especially export sales, many jobs in the economy would be lost. Local government is therefore very sensitive still to the overall health of the sector.

### **Manufacturing**

Osaka is the fourth largest manufacturing centre in Japan, based on value of shipments, according to the METI "Census of Manufactures 2003", placed behind Aichi, Kanagawa and Shizuoka. However, if Kobe next door is combined, the "Hanshin" area would be the second largest centre. The comparative strength of the manufacturing economy derives from the large number of small and medium sized companies (SMEs), which provide a dynamic base; the City's port and transportation infrastructure enables products to be shipped efficiently; the local market is large; and finally, the growth of China is driving exports faster.

The SME sector suffered most when manufacturing shifted offshore. Lately however, the outlook is becoming

more positive following the review by major manufacturers of their overseas manufacturing strategies. According to the Chairman of the Kansai Economic Federation (Kankeiren), Mr. Yoshihisa Akiyama, major manufacturers in Kansai intend to maintain at least 50% of their manufacturing assets in the Kansai region. The new strategy is designed to save logistics costs, reduce the risk of advanced manufacturing know how leaking to competitors, and diversify the risk of dependence on China.

The expansion of investment in manufacturing is helped as well by relatively low land prices around the Osaka Bay area, government grants to purchase land around the rim, convenient logistic facilities. The most visible sign of this new investment is the massive Matsushita plasma display plant, which opened in 2005, and will be doubled in size by 2007. What is still required is further deregulation of the Factory Location Law, making it easier to open factories in areas previously barred to construction or expansion.

### **Trade**

Trade has always been a major function of the Osaka economy and many major trading firms are still active in the city. When small wholesalers are added, the sector's economic activity, including retailing accounts for about 24% of GDP, which is at least double the comparable level of other major cities in Japan. Literally all roads (and railways) in the Kansai region lead to Osaka. A second runway is due to open at Kansai International Airport in 2007, which will accommodate the next generation of mega air carriers. If China and Asia continue to develop then these facilities will be required to ensure that Osaka preserves its role as the primary

trading centre in the region. One day it may even set its ambitions higher to compete with Asian trade entrepots, such as Pusan in South Korea.

### **China**

The re-emergence of China as Japan's largest trading partner is clearly producing a relative shift in the pattern of trade from the US and Europe back to north east Asia. Osaka has long-standing economic relations with China. To emphasise this, when China began opening again to the West, it was Osaka City, which signed a friendship agreement first, with Shanghai, in 1970. Since then high level missions between the two cities have taken place almost every year.

Exports through Osaka's ports and Kansai airport have expanded every month since 2001, and the percentage of exports going to China has increased to almost 20%. Assuming that the Chinese economy continues to expand, the impact on Osaka will remain one of the most important long-term contributors to growth. The next major opportunity is to expand tourism from China. The City is placing particular emphasis on it, with most of its tourism promotion budget focused on Shanghai in particular.

The structure of trade with China is shifting too. In the mid-90s, over 60% of exports from the port of Osaka were textile machinery. By 2003, general machinery, including consumer and industrial machinery, occupied nearly 50% of total exports, and textile machinery had fallen to 13%. Textile products is the other major export category, accounting for over 20%. Textile products are the major import category, accounting for over 40% of Chinese imports through the port.

### **Business sectors**

The pattern of trade reflects Osaka's traditional manufacturing strengths. Matsushita, Sharp and Sanyo, the engines of the Japanese consumer electronics and household appliance industry, are based in Osaka. The "Keihan Corridor", connecting Osaka with Kyoto, is probably the largest centre for the production and design of advanced electron devices and components in Japan, and includes the headquarters of Kyocera, Rohm, Murata, Omron and Nidec. The region is also a major centre for the production of high-valued added parts for use in mobile applications, such as batteries, including fuel cells, and flat panel displays.

One important advantage that Osaka has is a strong base in materials and chemicals research and production, which creates a micro climate for the integration and production of new products. This has led to Osaka's strong position in both pharmaceuticals and synthetic textiles. Many foreign companies have entered the Japanese market by forming partnerships, joint ventures, or distribution agreements with companies in these fields. There are now over 100 major foreign corporations with their Japanese headquarters in Osaka, including four of the world's major pharmaceutical companies, Astra-Zeneca, Bayer, Abbott, and Aczo Nobel.

### **Business creation**

Traditionally Osaka is known as the engine of innovation in Japan. However, the collapse of the Bubble economy and shift of manufacturing and head office activity away from the city means that it must continue to re-invent itself in order to find new sources of business growth and employment. Government and the Osaka Chamber are actively

supporting new business creation by various practical means, including the Osaka Innovation Centre, which is probably the largest such business support centre in Japan, offering business incubation space, free consulting services, and access to loans.

Movements to deregulate and privatise more government services are also providing new opportunities for business creation. All government departments in Osaka are looking to outsource services as one solution to the public debt crisis; regulations which slowed down new business creation and company formation have been reduced or eliminated; the corporatisation of universities is also creating new business opportunities.

### **Growth areas**

Under the central government's support for new industry creation, Osaka has selected three areas to promote as engines of growth, namely: tourism, new manufacturing, and health care (including life sciences). They are projected to add Y13 trillion to GDP by 2010, according to a group of think tanks, co-ordinated by the Osaka Chamber of Commerce. If achieved it could increase total GDP in Osaka by around 10%.

Of the three areas, the health care sector is expected to generate the most new demand. Under the METI plan for new industry creation, the Kansai region, focusing on Osaka, is intended to become a key hub, drawing on its existing strong pharmaceutical base.

New manufacturing technologies include ubiquitous IT and intelligent robotics. Again, Osaka has existing industrial and intellectual assets within the corporate and university sectors. Osaka in particular is seeking to make itself into a "Robot Capital". The final

vision is to link ubiquitous IT networks (e.g. mobile phone technology with smart card functions) and intelligent robots to create services unique to Japan. Certainly, this will be realised first in Japan.

To turn Osaka into a robotics hub, with a unique service and entertainments infrastructure, capable of attracting tourists (from Asia) and new business investment, requires that the City promote itself effectively in a way which attracts this capital and talent. In this connection, the redevelopment of the former freight yard, next to Osaka Station, similar in scale to Shiodome in Tokyo, but in a much more strategic location, may hold the key to the transformation of Osaka into both a lifestyle city and robot capital. The core zone on the site will be the currently named, “Knowledge Capital”, consisting of university and corporate research labs, alongside venture businesses, in a range of fields directly or indirectly related to the ubiquitous robot city envisaged.

### **Lifestyle economy**

The other change in the city’s make up is the development of what urban planners in the UK call “urban villages” – areas which attract visitors and shoppers to their brand outlets, restaurants, bars and coffee shops. The Osaka Station Yard redevelopment will be the foremost “urban village” at the very heart of the city, and in easy reach of people across the Kansai region. Several department stores are already located, or locating there. In addition, existing stores are being expanded and upgraded.

A beneficiary is the property market where land prices are now rising in the areas around these “urban villages” for the first time since the Bubble. On top of this, the relatively low cost of land

(down by as much as 80% from its height in 1990) has made it attractive to construct high-rise condos in the city centre, which is now transforming the skyline. Noting these changes, the investment house, Merrill Lynch, describes Osaka as a leading example of a city, which has potential to grow by shifting towards a lifestyle centre, capable of acting as a bigger and more dynamic metropolitan hub within its region.

These changes are opening up fresh opportunities, not just for local companies, but foreign companies too. Foreign capital is strongly supporting the property market. Foreign brands are in strong evidence in the main shopping areas, and “urban villages”. A number of M&A transactions have occurred involving foreign capital. There is still plenty of opportunity for companies with new service models, or technologies. This includes tie-ups with mid-size companies in the manufacturing sector, which have excellent technologies and access to markets, especially Asia.

Osaka has excellent infrastructure, technologies, and favourable cost factors not only in comparison with Tokyo but even with some major Asian centre. The lack of bilingual staff is cited as a weakness, but many foreign companies based in Osaka do not share this complaint. The expansion of foreign-owned enterprises, together with the growth of executive search firms, is making it easier to match demand with supply.

The ease of doing business in Japan is steadily improving, not least in cities like Osaka, which are having to fight for investment. Foreign companies are looking to China, but Japan is still the bigger market, and the political risk is low. Hospira, a medical supply

company, spun off from Abbott Laboratories, decided to make Osaka its Asian base. It concluded that costs are not so far out of line with Singapore, Hong Kong, or even Shanghai, the location better, and the

quality of life good. The decision could be the start of a trend, if the advantages of Osaka can be more fully recognised.

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