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Japan Country Report

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Japan Country Report

Chapter 1: Overview

The Japanese economy is continuing to recover at a moderate pace, posting a real economic growth rate of 2.1% in fiscal 2006. In fiscal 2007, improvements in the corporate sector are expected to trickle down into the household sector, and moderate economic growth supported by private domestic demand is expected to continue.

Japan's construction investment is still sluggish. Construction investments in fiscal 2006 were valued at ¥52.3 trillion yen (¥18.4 trillion in government projects, ¥33.9 trillion in private projects), about half of the peak value (fiscal 1995). While government construction has consistently declined over the past several years, private construction has increased, and this trend is expected to continue.

Recent trends in the construction industry are as follows:

- (1) Small and medium-sized companies with fewer than 100 employees account for 97.9% of construction companies, and their share of the market has been increasing in recent years.
- (2) Statistics on the number of construction industry employees by occupation show a noticeable decline in the number of employees working for general contractors.
- (3) The trends toward decreased construction investments and declining labor productivity in the construction industry, due to various productivity impediments at construction sites and within companies, are continuing.
- (4) The cost of materials has been on the rise in recent years due to high steel prices worldwide. On the other hand, employee wages are lower in the construction industry than in other industries.
- (5) The overseas construction orders received by Japan reached their highest level ever in fiscal 2006, hitting ¥1.648 trillion. Growth has been particularly significant in the Middle East.

Chapter 2: Macroeconomic Review and Future Projections

2.1 Overview of the Japanese Economy

The Japanese economy is gradually recovering. The real economic growth rate has remained consistently higher than 2.0% for four consecutive years since fiscal 2003, reaching 2.1% in fiscal 2006. The growth in exports, made possible by a robust international economy, has contributed to the growth of corporate earnings, and this has led to an improvement in business sentiment and increased capital investment. This trend has been a major factor in the economic growth rate trend. In fiscal 2006, net exports of goods and services increased 25.6% over the previous year (contributing 0.8 points to GDP), and corporate capital likewise increased 7.9% (1.2). Both have contributed to the economic recovery.

This moderate economic recovery, sustained by private demand, is expected to continue in fiscal 2007. The Research Institute of Construction and Economy (RICE) estimates that the real economic growth rate for fiscal 2007 will be 2.0%. The year-on-year growth rate for various categories are (figures in parentheses indicate points contributed to GDP) 1.8% for private final consumption expenditures (1.0), 4.1% for private corporate capital (0.7), 14.2% for net exports of goods and services (0.6), and 1.0% for government final consumption expenditures (0.2). Since personal consumption is expected to increase gradually as the employment situation improves, these figures reflect particularly high projections in the growth rate of private final consumption. This means that improvements in the business sector are showing a domino effect on the household sector, thus helping to sustain private domestic demand. Capital investment is expected to continue to increase as a result of continued improvements in corporate earnings, and though there are still challenges to be overcome in the employment situation, improvements are evident in the form of a decrease in the total unemployment rate and an increase in the number of employees. Meanwhile, government policies to constrain public works projects are expected to result in a significant 8.6% (-0.3) decrease in public fixed capital formation. It will be important to keep an eye on factors that could exert downward pressure, such as overseas economies (particularly the United States), and the trends in crude oil prices.

Figure 1 Macroeconomic Trends (fiscal year)

FY	Actual							Estimated	
	1990	1995	2000	2003	2004	2005	2006	2007	2008
Real GDP	467,913	482,750	505,622	517,715	527,827	540,430	551,755	563,012	574,682
(Y-o-Y growth rate)	6.0%	2.5%	2.6%	2.1%	2.0%	2.4%	2.1%	2.0%	2.1%
Real private final consumption expenditures	249,477	273,764	283,758	293,069	296,888	302,492	304,682	310,232	316,091
(Y-o-Y growth rate)	4.8%	2.5%	0.7%	0.6%	1.3%	1.9%	0.7%	1.8%	1.9%
(Contribution to GDP)	2.6	1.4	0.4	0.4	0.8	1.1	0.4	1.0	1.0
Real government final consumption expenditures	62,230	74,716	85,714	92,331	93,891	94,773	95,599	96,551	97,515
(Y-o-Y growth rate)	2.9%	4.1%	4.3%	2.6%	1.7%	0.9%	0.9%	1.0%	1.0%
(Contribution to GDP)	0.5	0.6	0.7	0.5	0.3	0.2	0.2	0.2	0.2
Real private housing	26,457	23,953	20,361	18,357	18,662	18,475	18,548	18,432	18,154
(Y-o-Y growth rate)	6.0%	-5.6%	-0.1%	-0.2%	1.7%	-1.0%	0.4%	-0.6%	-1.5%
(Contribution to GDP)	0.3	-0.3	0.0	0.0	0.1	0.0	0.0	0.0	0.0
Real private business capital	90,489	67,869	72,963	73,316	77,904	82,384	88,894	92,558	97,158
(Y-o-Y growth rate)	12.0%	3.1%	7.2%	6.1%	6.3%	5.8%	7.9%	4.1%	5.0%
(Contribution to GDP)	2.2	0.5	1.0	0.8	0.9	0.8	1.2	0.7	0.8
Real public fixed capital formation	29,824	40,602	34,445	28,104	24,525	24,183	21,872	19,985	18,475
(Y-o-Y growth rate)	4.1%	7.5%	-7.6%	-9.5%	-12.7%	-1.4%	-9.6%	-8.6%	-7.6%
(Contribution to GDP)	0.3	0.6	-0.6	-0.6	-0.7	-0.1	-0.5	-0.3	-0.3
Real inventory increase	2,487	1,774	2,043	1,127	1,839	1,451	1,650	1,709	2,045
(Y-o-Y growth rate)	-11.7%	15458.8%	192.2%	626.1%	63.1%	-21.1%	13.7%	3.6%	19.7%
(Contribution to GDP)	-0.1	0.4	0.8	0.3	0.1	-0.1	0.0	0.0	0.1
Real net export of goods and services	6,949	959	6,295	11,263	14,083	17,043	21,410	24,446	26,142
(Y-o-Y growth rate)	11.8%	-79.2%	7.5%	57.0%	25.0%	21.0%	25.6%	14.2%	6.9%
(Contribution to GDP)	0.2	-0.7	0.1	0.8	0.5	0.5	0.8	0.6	0.3
Nominal GDP	451,473	496,457	504,119	493,748	498,275	503,317	510,421	521,803	535,154
(Y-o-Y growth rate)	8.5%	1.9%	0.9%	0.8%	0.9%	1.0%	1.4%	2.2%	2.6%

(Unit: ¥billion, real values are chain linking method from 2000)

Source: Research Institute of Construction and Economy (RICE)

Today, the Japanese economy is facing serious challenges as it strives to adapt to world trends, such as the onset of an aging society combined with a falling birthrate, rapid globalization, and the worldwide dissemination of information technology. To meet these challenges and continue to achieve economic growth, Japan must promote the efforts described in the Basic Policies for Economic and Fiscal Management and Structural Reforms 2007. Specifically, “comprehensive efforts to increase productivity,” “efforts to open up the Japanese economy,” and “efforts to create an infrastructure that can support people’s lives in the future.” It is also important to accelerate the pace and increase the depth of reforms aimed at strengthening Japan’s capacity for growth.

2.2 Major Economic Indicators

Figure 2 List of Major Economic Indicators

	2002	2003	2004	2005	2006	2007
GDP and its components (monetary unit: ¥ billion)						
GDP (real value, FY)	507,015	517,715	527,827	540,430	551,755	563,012
GDP growth rate (% , FY)	1.1%	2.1%	2.0%	2.4%	2.1%	2.0%
GDP (nominal value, FY)	489,875	493,748	498,275	503,317	510,421	521,803
GDP (nominal value, calendar yr.)	49,131	49,029	49,833	50,134	50,765	—
Total production, agriculture, forestry, and fisheries industry, mining industry	901	884	853	800	—	—
Growth rate (%)	-0.9%	-1.9%	-3.5%	-6.2%	—	—
Total production, manufacturing industry	10,127	10,276	10,541	10,520	—	—
Growth rate (%)	-2.7%	1.5%	2.6%	-0.2%	—	—
Total production, construction industry	3,389	3,233	3,295	3,170	—	—
Growth rate (%)	-4.6%	-4.6%	1.9%	-3.8%	—	—
Service industry	34,713	34,636	35,143	35,644	—	—
Growth rate (%)	-0.5%	-0.2%	1.5%	1.4%	—	—
Demographic indicators						
Population (thousands)	127,486	127,694	127,787	127,768	127,770	127,730
Rate of population growth (%)	0.13%	0.16%	0.07%	-0.01%	0.00%	-0.03%
Labor force population (thousands)	6,689	6,666	6,642	6,650	6,657	6,542
Labor force population growth rate (%)	-0.93%	-0.34%	-0.36%	0.12%	0.11%	-1.73%
Unemployment rate (%)	5.4%	5.3%	4.7%	4.4%	4.1%	4.0%
Monetary and financial indicators						
Short-term interest rate (%)	0.10	0.05	0.03	0.04	0.26	0.6
Long-term interest rate (%)	1.007	1.380	1.445	1.456	1.634	1.650
Consumer price index (%)	100.6	100.3	100.3	100.0	100.3	100.4
Short-term prime rate (%)	1.375	1.375	1.375	1.375	1.625	1.875
Long-term prime rate (%)	1.65	1.7	1.55	1.85	2.35	2.25
Avg. US dollar exchange rate	125.31	115.93	108.19	110.22	116.12	123.16

Source: Construction Economy Estimates (RICE, July 2007), Annual Report on National Accounts (Cabinet Office, July 2006). Websites of the Ministry of Internal Affairs and Communications and Bank of Japan, Financial and Economic Statistics Monthly (Research and Statistics Department, Bank of Japan, July 2006).

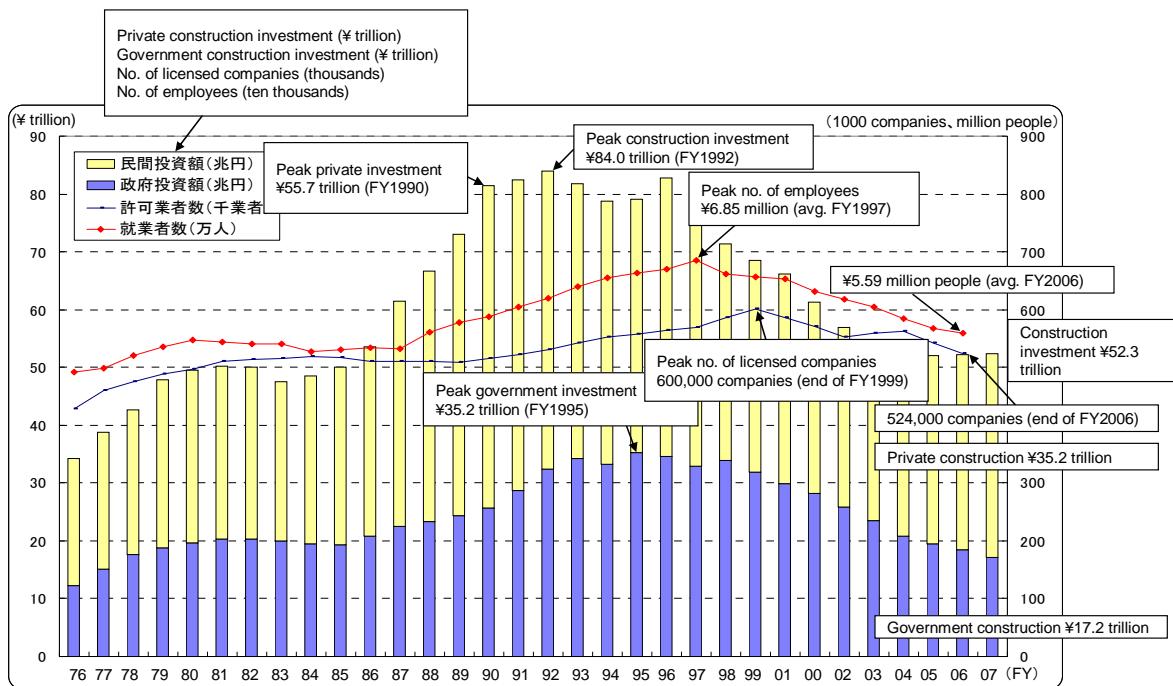
- GDP figures for fiscal 2007 are estimates. Real figures use fiscal 2000 prices.
- All total production figures are nominal figures for the calendar year.
- Population figures are as of October 1 each year. The fiscal 2007 figure is an estimate.
- The working population and unemployment rate figures are for October. Figures for 2007 are as of May.
- The consumer price index is based on 2005 as 100.
- Interest rates in 2007 are as of the end of May. Others reflect the year-end rates.
- Short-term interest rates reflect the domestic average offering rates on commercial paper.
- Long-term interest rates reflect the long-term (10-year) national bond applicant rate.
- The consumer price index for 2007 is as of the end of May.
- Standard loan rates (commercial banks) use the short-term prime rate.
- Standard loan rates (finance companies) use the long-term prime rate.
- Exchanges rates are annual averages, except for 2007, which is the rate as of the end of June.

Chapter 3: Overview of the Construction Industry

3.1 Construction Investment

Construction investment figures in Japan (figures shown hereafter are nominal) were slightly up in fiscal 2006 versus the previous year, but the situation remains tenuous. Construction investment in fiscal 2006 was valued at ¥52.3 trillion yen, of which ¥18.4 trillion consisted of government spending and ¥33.9 trillion of private spending. Total construction investment was down 37.7% compared with the peak year (indicated in parentheses, fiscal 1992), while government investment was down 47.6% (fiscal 1995) and private investment was down 39.2% (fiscal 1990). Recent trends in construction investment show that while government investments are consistently declining, private investments are rising.

Figure 3 Trends in Construction Investment (Lower left: Government construction investment; Lower right: Private construction investment)



Source: Construction Investment Forecast and Study of the Numbers of Licensed Companies, MLIT

Notes:

- Investments shown are actual figures up to fiscal 2004. Figures for fiscal 2005 and 2006 are estimates, and figures for FY2007 are projections.
- The number of licensed companies reflects the number at the end of each fiscal year (as of the end of March in the following year)
- The number of employees is the annual average.

Source: Materials prepared by the Construction Industry Policy Research Materials Council, MLIT

RICE estimates the construction investment figures for fiscal 2007 and 2008 as follows (announced July 2007). Construction investment in fiscal 2007 is expected to decrease by 0.8% from the previous year to ¥51.8 trillion. Government construction investment is expected to continue to decline for the ninth consecutive year, sliding 7.5%. Private residential investment is expected to rise for the fourth consecutive year, rising 1.3%. Private non-residential construction investment is expected to increase 4.7% overall, reflecting a 4.0% increase in private civil engineering and a 5.2% increase in private non-residential building investment.

Construction investment in fiscal 2008 is expected to decrease 1.1% from the previous year to ¥51.3 trillion. Government construction investment is expected to continue its decline, by 7.4% over the previous year. Growth in private residential construction investment is expected to slow compared to the previous year, with only a 0.3% increase anticipated. Private non-residential construction investment is expected to show an overall increase for the fifth consecutive year, by 4.2%, reflecting a 3.1% increase in civil engineering and a 4.8% increase in private non-residential building investment.

Figure 4 Construction Investment Estimates

FY	1990	1995	2000	2003	2004	2005 (Estimated)	2006 (Estimated)	2007 (Projected)	2008 (Projected)
Nominal construction investment	81.4	79.0	66.2	53.7	52.8	52.1	52.3	51.8	51.3
(Y-o-Y growth rate)	11.4%	0.3%	-3.4%	-5.5%	-1.7%	-1.2%	0.3%	-0.8%	-1.1%
Nominal government construction investment	25.7	35.2	30.0	23.5	20.8	19.5	18.4	17.1	15.8
(Y-o-Y growth rate)	6.0%	5.8%	-6.2%	-9.4%	-11.5%	-6.0%	-5.6%	-7.5%	-7.4%
(Contribution to GDP)	2.0	2.5	-2.9	-4.3	-5.0	-2.3	-2.1	-2.6	-2.4
Nominal private residential construction	25.7	24.3	20.3	17.9	18.4	18.4	19.1	19.3	19.4
(Y-o-Y growth rate)	9.3%	-5.2%	-2.2%	-0.3%	2.6%	0.3%	3.6%	1.3%	0.3%
(Contribution to GDP)	3.0	-1.7	-0.7	-0.1	0.9	0.1	1.3	0.5	0.1
Nominal private non-residential construction	30.0	19.5	16.0	12.3	13.6	14.2	14.8	15.4	16.1
(Y-o-Y growth rate)	18.4%	-1.8%	0.7%	-4.9%	10.5%	3.9%	4.1%	4.7%	4.2%
(Contribution to GDP)	6.4	-0.4	0.2	-1.1	2.4	1.0	1.1	1.3	1.3
Real construction investment	84.0	77.7	66.2	54.8	53.3	52.0	51.2	50.0	48.8
(Y-o-Y growth rate)	7.6%	0.2%	-3.6%	-6.1%	-2.8%	-2.3%	-1.7%	-2.2%	-2.4%

(Unit: ¥trillion, real values are based on fiscal 2000 prices.)

1. Figures up to fiscal 2006 are from the FY2007 Construction Investment Forecast issued by the MLIT.

2. Private non-residential construction investment = private non-residential building investment + private civil engineering investment.

Source: RICE

3.2 Construction Companies

A breakdown of Japanese construction companies by size (number of employees) reveals that of the 270,000 construction companies that implement ¥1 million or more in construction projects annually, one-third have fewer than 10 employees, and 99% have fewer than 100 employees. Small and medium sized companies clearly make up the vast majority of construction companies. Comparing these figures to those from fiscal 1994 reveals that while the total number of companies in the construction industry has decreased by about 30,000 over the past decade, there has been virtually no decrease in companies with fewer than 10 employees. Thus the weight of those companies has effectively increased in the market place.

Figure 5 Number of Construction Companies by Size (No. of Employees) in FY1994, 2004

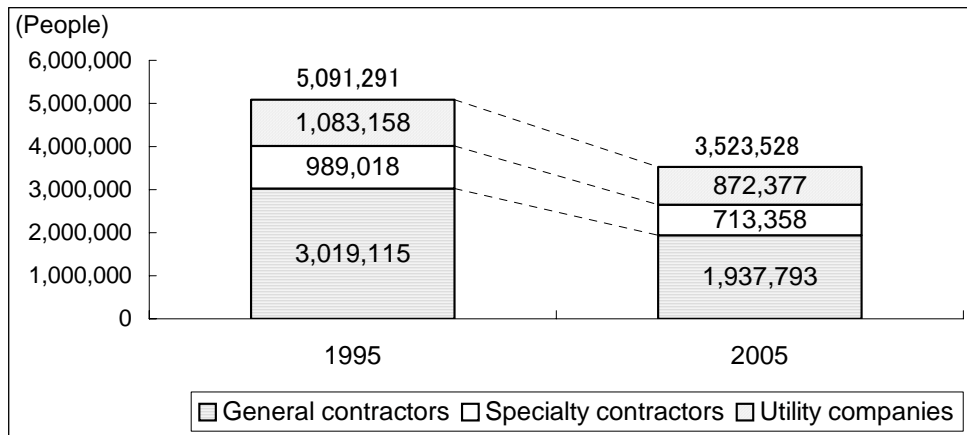
No. of employees	FY1994			FY2004		
	No. of companies	Ratio	Cumulative	No. of companies	Ratio	Cumulative
1-9	168,637	55.7%	55.7%	168,298	61.5%	61.5%
10-99	126,334	41.7%	97.4%	99,443	36.4%	97.9%
100-999	7,216	2.4%	99.7%	5,233	1.9%	99.8%
1,000 or more	785	0.3%	100.0%	543	0.2%	100.0%
Total	302,972			273,517		

Source: Report on the Survey of Construction Project Statistics, MLIT

3.3 Employees and Construction Labor

The numbers of construction industry employees by occupation shows that 1,937,793 (55.0%) work for general contractors, 713,358 (20.2%) work for specialty contractors, and 872,377 (24.8%) work for utility companies, for a total of 3,523,528 (100%) employees. This total is down 1.5 million from fiscal 1995, reflecting a particularly large decrease in the number of general contractors.

Figure 6 Number of Construction Industry Employees by Occupation in 1995,



	1995		2005	
General	3,019,115	59.3%	1,937,793	55.0%
Specialty	989,018	19.4%	713,358	20.2%
Utility	1,083,158	21.3%	872,377	24.8%
Total	5,091,291	100.0%	3,523,528	100.0%

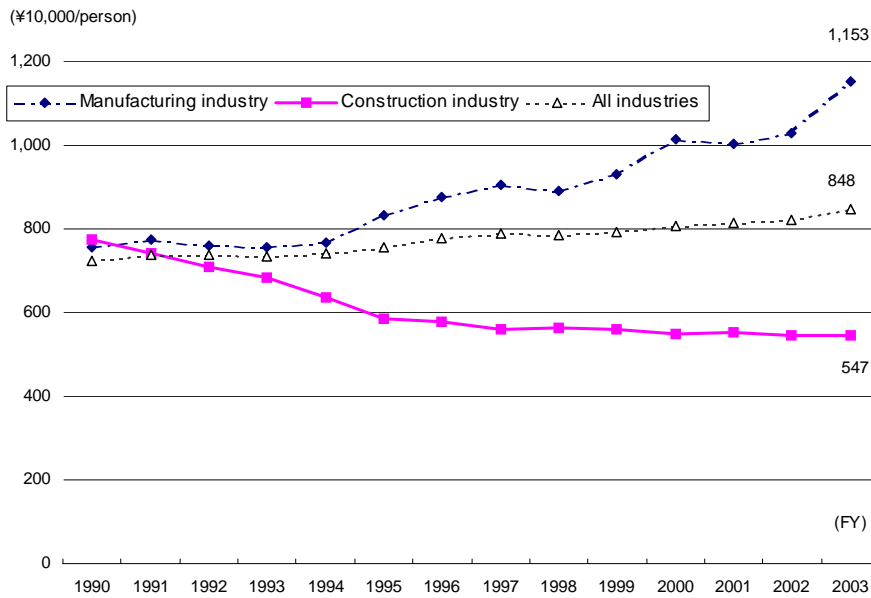
Source: Report on the Survey of Construction Project Statistics, MLIT

3.4 Productivity

Against the backdrop of a rapid decline in construction investment, labor productivity in the Japanese construction industry has continued to drop since the early 1990s. The factors involved in this decline are listed below, and include macroeconomic factors such as the decline in construction investment, as well as micro level productivity impediments at work sites and within companies.

- (1) Although construction investment has begun a dramatic decline, the construction industry has played the role of providing employment as a pump-priming measure. Thus, the industry carries relatively high employment in spite of the decrease in construction investment.
- (2) Production continues to occur outdoors, on individual projects, and on a build-to-order basis. Adequate measures have not been taken to improve workplace productivity and bring about significant reforms in the production system in this industry.
- (3) The ratio of employees in indirect work sectors is increasing due to the rise in the number of construction companies, a result of past pump-priming measures.
- (4) The production system is inefficient, with too many layers of subcontractors and increasing costs.

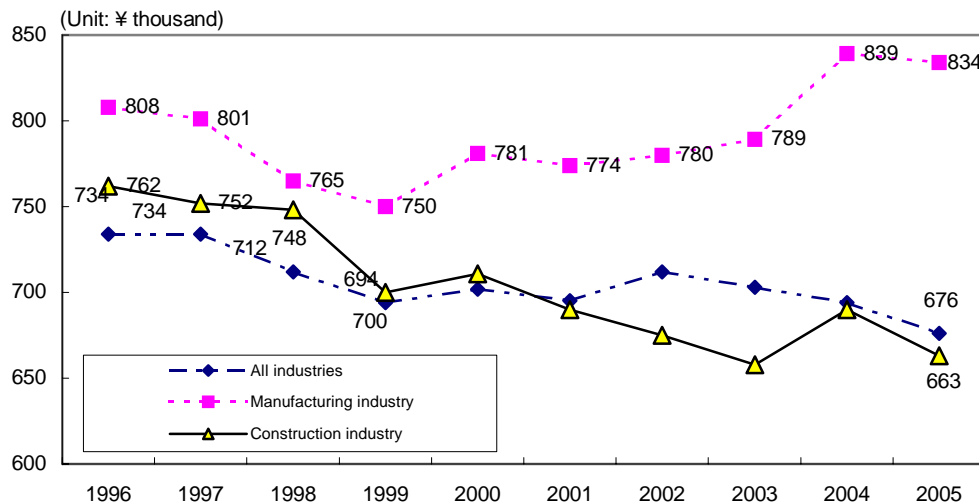
Figure 7 Trends in the Real Labor Productivity in the Construction Industry



Note: Real labor productivity = GDP by economic activity as reported in the national accounts (real) / No. of employees engaged in each economic activity.

Source: Prepared by RICE using the 2005 Comparison of Productivity by Industry, Japan Productivity Center for Socio-Economic Development.

Figure 8 Value Added Per Employee



Note: Value added = operating income + personnel expenses + interest expenses, discount expenses + taxes and public fees, etc.

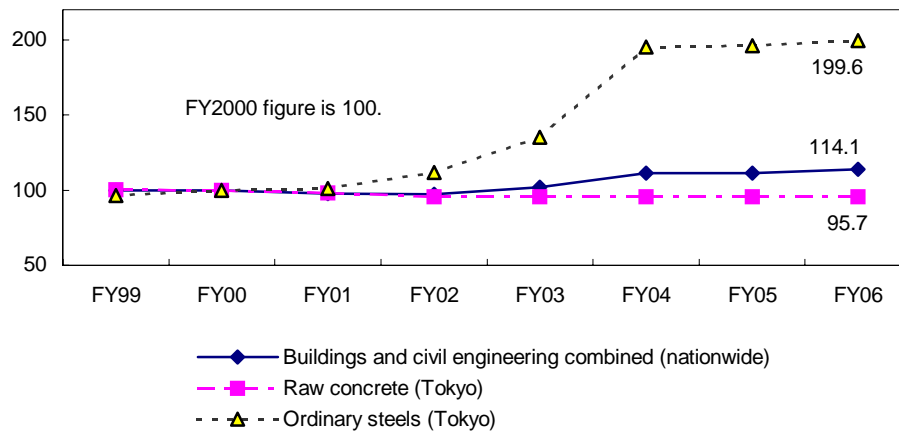
Source: Corporate statistics.

3.5 Construction Costs

(1) Average Construction Material Prices

Figure 9 shows an index over price trends of major materials, which is based on average prices in fiscal 2000 (construction material price index). The nationwide index combining building and civil engineering has been increasing slightly since fiscal 2003. This is largely due to high worldwide steel prices. The price of ordinary steels soared in fiscal 2003 and fiscal 2004, and prices have continued to remain at high levels even after the increase slowed. Raw concrete, on the other hand, has slightly decreased.

Figure 9 Trends in the Construction Material Price Index

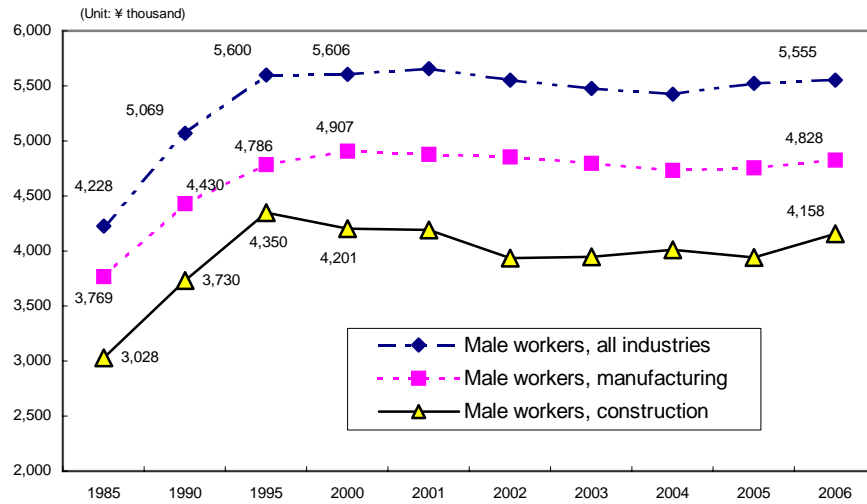


Source: Economic Research Association

(2) Construction Industry Wages

The wages of production workers in the construction industry increased significantly up until the early 1990s, and the gap between wages in the construction and other industries, such as the manufacturing industry, was closing. However, construction industry wages began to fall sooner than wages in other industries, and they fell further, thereby causing a wider wage gap. Wages increased significantly year-on-year in fiscal 2006, but at ¥670,000 annually, they were still 13.9% lower than the manufacturing industry.

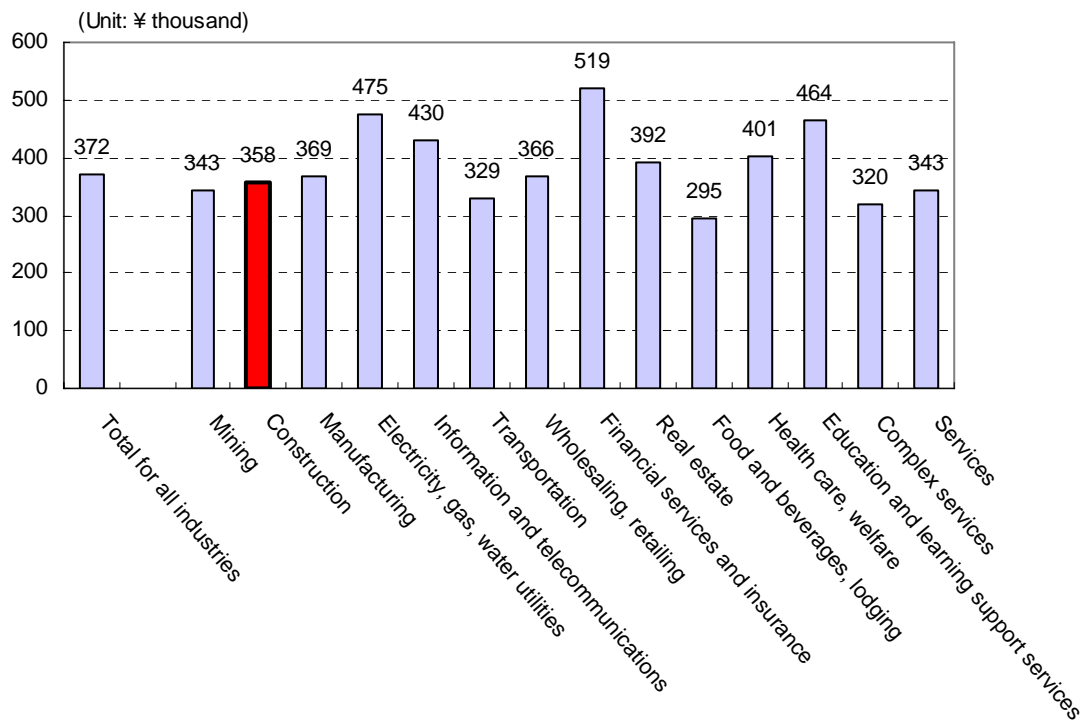
Figure 10 Trends in Total Annual Wages Among Production Workers



Source: Basic Statistical Survey of Wage Structures, Ministry of Health, Labour, and Welfare

Figure 11 shows the monthly wages by industry among male workers (salaries based on monthly wages, not including bonuses). While the monthly average for all industries was ¥372,000, the construction industry monthly wage was ¥358,000, 4% lower than the average.

Figure 11 Monthly Salary by Industry (Males, fiscal 2005)



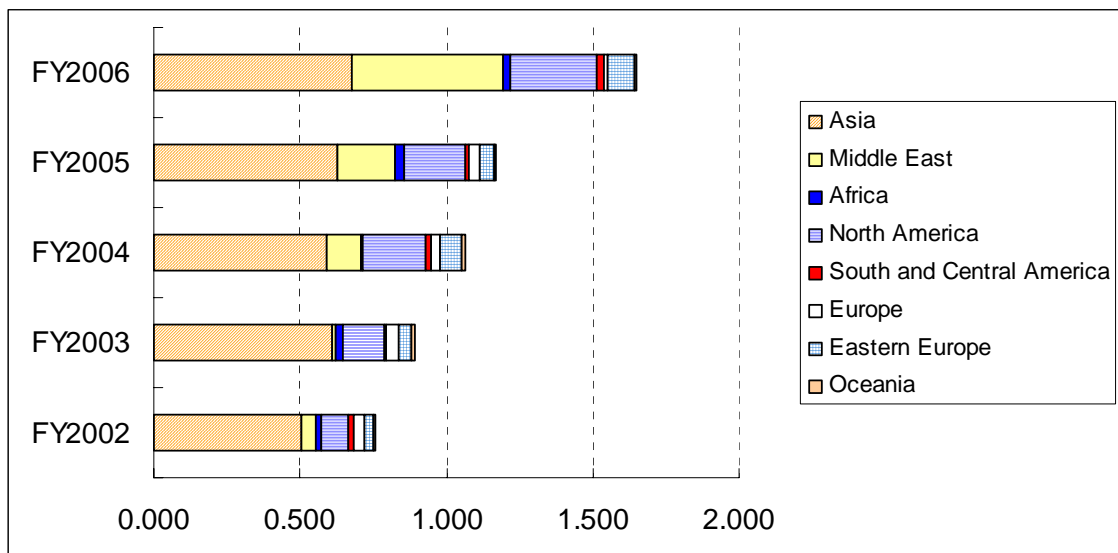
Source: Basic Statistical Survey of Wage Structures, Ministry of Health, Labour, and Welfare

3.6 Overseas Expansion of the Japanese Construction Industry

Overseas construction orders have lingered at the ¥1 trillion level for more than 20 years since the ¥1 trillion threshold was first crossed in fiscal 1983. In fiscal 2006, they reached the highest level ever, hitting ¥1.648 trillion. The ratio of the overseas to the domestic market has grown in recent years, hitting the 3% range in fiscal 2006. Orders from the Middle East, which has seen a surge in construction, increased 2.6 times over the previous year.

Figure 12 Overseas Construction Orders in FY2002-2006

(Unit: ¥ trillion)



	FY2002	FY2003	FY2004	FY2005	FY2006
Asia	0.502	0.611	0.589	0.630	0.677
Middle East	0.053	0.011	0.117	0.194	0.514
Africa	0.018	0.023	0.011	0.030	0.024
North America	0.093	0.142	0.210	0.209	0.299
South and Central America	0.014	0.006	0.020	0.016	0.024
Europe	0.041	0.048	0.032	0.033	0.013
Eastern Europe	0.026	0.039	0.077	0.050	0.092
Oceania	0.010	0.015	0.007	0.007	0.005
Total	0.758	0.894	1.062	1.171	1.648

Source: Overseas Construction Association of Japan