

Special Report:

THE RETURN
OF JAPAN, INC?





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Ever since the stock market crash of 1989, Japan's economy has been down in the dumps. Despite being the world's second largest economy, it has struggled to regain the momentum of the early 1980s, when "Japan, Inc." seemed to be an unstoppable force. Since last year, though, signs have begun to appear that the economy may be picking up — and mergers are returning in the shape of high-profile takeover battles. Has Japan rebounded at last? Experts at Wharton and elsewhere offer their insights.

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In most of the world, eBay is synonymous with online auctions — but not in Japan. The world's second largest economy, with the third highest Internet population, has remained as impenetrable as the moat-protected walls of the Emperor's palace in the center of Tokyo. In this case, the undisputed winner is Yahoo! Japan, a joint venture between U.S.-based Yahoo! and Japan-based Softbank. The CEO of Yahoo! Japan spoke with participants of the Wharton Fellows program about how his company outbid eBay to win Japan's customers.

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Time was when Japanese rivals such as Honda, Suzuki, Yamaha and Kawasaki left Harley-Davidson in the dust. During the 1970s and 1980s the U.S.-based motorcycle maker went down some rocky roads, which almost brought it to the brink of bankruptcy. Today, however, the company has roared back into the Japanese market and has snatched control of the large-motorcycle market away from its rivals. How did that happen? Toshifumi Okui, president of Harley-Davidson Japan, spoke about the turnaround to participants of the Wharton Fellows program.

- ◆ **What Is the Global Economy?** Page 9

The *Financial Times* once described Kenichi Ohmae as "Japan's only successful management guru." Armed with a PhD in nuclear engineering from MIT, he joined McKinsey & Co. in 1972 and ran the consulting firm's Japan office for several years. In his most recent book, *The Next Global Stage: Challenges and Opportunities in Our Borderless World*, Ohmae argues that globalization has already occurred, is here to stay, and is about to move to a new stage. An excerpt from the book examines the principal features of the global economy.



Japan's Economy: It May Be Aging, but It's Agile

To understand the seriousness of the crisis of the aging of the Japanese population — as well as the nation's equally serious infatuation with high technology — one need only take a look at a partner robot prototype developed by Toyota. The white biped, which looks a bit like a human-scale LEGO figure, can stroll onto stage and play the trumpet with its own breath and fingering. This robot is not designed to do anything as practical for the business as assembling automobiles; it has other, more alien-looking cousins for that task. Instead, this humanoid is designed to assist people, particularly Japan's growing elderly population. While the Japanese economy has been rebounding in the short term, Japan's aging workforce is among the biggest clouds hovering over the nation's economic future. And it will take more than an army of androids to address it.

Rising Sun?

Since the stock market crash of 1989, Japan has been struggling to regain the momentum of the early 1980s when "Japan, Inc." was snatching up high-profile U.S. real estate properties and entertainment companies. Corporate bankruptcy laws and banking practices, which helped keep companies from failing in the post-war rise of Japan, ultimately became a burden. Weak corporations and troubled banks and insurers, which should have been weeded out, were sustained through government protection.

The current picture is more upbeat. Recent reforms led by the Bank of Japan have boosted the money

supply, contributing to increases in business profits and stock market valuations. And many observers hailed last year's takeover battle between banking giants Sumitomo and Mitsubishi for Japan's fourth largest bank as a sign that reforms are creating healthy competition. That fight pales in comparison to the one that has riveted Japan during the past month as Livedoor, an Internet upstart, has been waging a legal battle to take over Nippon Broadcasting System (NBS).

"The most important factors for the long term are human capital and technology."

—Hiroshi Yoshikawa, professor of economics,
University of Tokyo

There are also indications that consumer spending may be coming back. The recovery in Japan "is a real one," said Hiroshi Yoshikawa, professor of economics at the University of Tokyo, at a recent Wharton Fellows class in Tokyo. He cited an economic growth rate that increased from 3.2% in 2003 to 3.5% in 2004. Last year, it appeared as though the banking problem had largely been solved, unemployment had declined and consumption was going up. Growth was expected to be 2% to 3% this year, though observers also hoped its impact would be greater because Japan's population is shrinking. "The most important factors for the long term are human capital and technology," Yoshikawa said.

Showing Its Age

While there should be celebration over the recent economic progress, there is only consternation and debate, primarily focused on “human factors.” Unfortunately, the strong signals the economy gave out last year have weakened to some extent in 2005. Economists now believe growth this year will be just 1.6% (not 2% to 3%), and the unemployment rate has begun to climb again. In February, the jobless rate rose to a six-month high of 4.7%, which stoked fears that last year's recovery might have been too short-lived. Another worrisome figure recently released by the Ministry of Internal Affairs and Communications refers to household spending, which dropped 3.8% in February compared to February 2004.

Disappointing as these economic numbers are, a more serious concern is the aging population. The number of people of working age (15 to 64) has been dropping since 1995. By 2050, the working population is expected to dwindle to just 54 million from its peak of 87 million. At the same time, the number of people 65 and older will rise from one-fifth to one-third of the population. This means that a declining pool of young workers is being asked to carry the growing burden of Japan's national pension or social security system.

“To make a true recovery, there have to be changes.”

—Ikuo Nishioka, president,
Mobile Internet Capital

Prime Minister Junichiro Koizumi pushed through an unpopular pension reform bill last June, but it became a source of contention. The bill balanced the pension system squarely on the backs of workers, requiring employees to pay more into the system and receive fewer benefits. In the midst of that debate, a series of pension scandals further roiled the waters. Several revelations showed that key leaders had failed to make payments into the national system over the past decade. The scandals led to the resignations last year of the chief cabinet secretary and the head of Japan's opposition party.

Business Reforms and Entrepreneurship

It is not just government that needs to change. The Japanese business environment and culture also need to be shaken up to spark innovation and entrepreneurship. The start-up rate for new businesses in Japan is an anemic 4%, the lowest among industrialized countries. Genichi Tamatsuka, COO of Fast Retailing Company, a major Japanese retailer, notes that total Japanese retailing has been stagnant at \$1.4 trillion over the past decade, while U.S. retailing has more than doubled. He also is concerned about the many small, unproductive players as well as the large companies that have become complacent and unable to change, and suggests more reforms are needed. “The Japanese market is very attractive, but we need strong organizations that can clearly say no to the weaknesses of Japanese companies. We need a catalyst to break the bad element of the Japanese economy and create a totally new way of doing business.”

“To make a true recovery, there have to be changes,” says Ikuo Nishioka, former head of Intel Japan and president of Mobile Internet Capital. He notes that by the time managers work their way up to president of a major Japanese firm, they are in their 60s and “want to be quiet and have no change.” The venture capital market is also a limiting factor in Japan. When venture capital investors made significant returns during a technology bubble several years back, the funds were not reinvested.

Japan sometimes is believed to have a so-called dual economy, with some stellar global performers such as Canon and Toyota, but also many less successful companies. The bad may outweigh the good. George Fields, a Japanese marketing expert and government advisor, notes that a study of Japanese manufacturing firms found that global exporters had a productivity score of nearly twice that of domestic manufacturing firms. The problem is that these exporters account for just 10% of the total Japanese manufacturers. “You can't talk about Japan as if it is a unity. There are two Japans,” says Fields.

Japan and China

As it has throughout Japan's history, China will have a big impact on the country's future. While China, Japan's largest and closest neighbor, poses an economic threat to the country — and its low

manufacturing costs have led to concern about the “hollowing out” of the Japanese economy — it also has been a source of tremendous opportunity.

The reason is that the economic nexus between Japan and China has been changing. Kenzo Yamamoto, general manager of the New York office of the Bank of Japan, told the Wharton Asia Business Conference recently that economic ties between the two nations are growing stronger. China has replaced America as Japan's largest trading partner; Chinese imports from Japan exceed American imports.

According to Yamamoto, two other factors are helping drive economic growth in Japan. First, the debt overhang that has long plagued the business sector has started to diminish; and second, the ongoing restructuring of industry has contributed to economic growth, with manufacturing pressing forward heavily, improving efficiency, reducing debt and enhancing profitability. Yamamoto views Japan's prospects for the future with cautious optimism. Although Japan's economy is still vulnerable to its continued dependence on oversized companies, he says that the economy has several strengths, such as a solid infrastructure, high-quality labor and its system of law.

Shigeki Morinobu, a senior fellow in Japan's finance ministry, also is upbeat about Japan's economic future. He discussed Japan's tax policy at the conference, noting how half of the expenditure of the general account was financed by tax revenues, while the other half was by government bonds. This gross financial debt was 1.6 times the GDP, which was a risky situation. He said it was a good time to start a debate about fiscal consolidation, which might not necessarily lead to an economic slowdown if the government takes appropriate measures. For example, he explained, cuts in expenditure could increase consumption in the private sector.

Japan's Global Role

Naotaka Matsukata, chairman of the strategic international business practice of Hunton & Williams, a New York City-based law firm, sees hope for Japan's global economic role. Noting the strong relationship between the current U.S. and Japanese governments, he is optimistic about the fact that trade liberalizers within the Japanese government seem to

be succeeding over conservative protectionists. The power of these liberalizers still remains to be tested, though. A major sticking point in U.S.-Japan trade relations is Japan's continued ban of American beef imports, imposed two years ago because of fears of Mad Cow disease. To the U.S., this represents the loss of a \$1.7 billion business opportunity.

In fact, Condoleeza Rice, the U.S. Secretary of State who visited Asia last month, raised the beef question during her visit to Japan. She also praised the country's role on the world stage and backed its desire for a seat on the U.N. Security Council. The gist of her message to the Japanese people — including businessmen and women — seemed to be that in a world that is increasingly preoccupied with China's growing economic might, the world's two largest economies have a lot to contribute to one another and the rest of the world. Aging population or not, Japan and its businesses still have a lot of oomph left. ♦



How Yahoo! Outbid eBay for the Japanese Online Auction Market

In most of the world, eBay is synonymous with online auctions. Tens of millions of members buy and sell on local sites in Australia, Austria, Belgium, Canada, France, Germany, Ireland, Italy, Korea, the Netherlands, New Zealand, Singapore, Spain, Sweden, Switzerland, Taiwan and the United Kingdom. eBay also has established a strong presence in Latin America through investments in MercadoLibre.com and in China through its ownership of EachNet.

“We knew the people and had the user base.”
—Masahiro Inoue, president and CEO, Yahoo! Japan

But one glaring exception exists to eBay's nearly universal reach — the Japanese market. The world's second largest economy, with the third largest Internet population, has remained as impenetrable as the moat-protected walls of the Emperor's palace in the center of Tokyo. And the undisputed emperor at the center of these walls is Yahoo! Japan, a joint venture between U.S.-based Yahoo! and Japan-based SoftBank.

Bidding War

It isn't that eBay hasn't tried to make forays into Japan. The company launched its Japanese business just five months after Yahoo! fired up its auction site in September 1999. But five months is an eternity in Internet time (and Yahoo! already had a strong presence in other online businesses). A year later, eBay had managed to carve out only about 3% of the nation's auction market, which had grown to \$1.6 billion. By 2002, the San Francisco-area company admit-

ted defeat, laying off all 17 of its Japan employees and shutting down the site with about 25,000 listings.

How was Yahoo! Japan able to succeed? “We knew the people and had the user base,” said Masahiro Inoue, President and CEO, during a presentation to the Wharton Fellows program in Tokyo. “When eBay came in, the company insisted on using its own management from California. A lot of Internet users didn't accept the ways of the eBay site. They also had to use their own money to advertise. We didn't have to do that. We only had to approach people on our own site.” And eBay's reliance on word-of-mouth, commission structure and demand for credit card payments also put it at a disadvantage to Yahoo!, which advertised, didn't initially charge a fee and offered non-credit payment options.

In auctions, there is a significant first-mover advantage. A site with more sellers attracts buyers and more buyers bring sellers. This was a lesson both companies had learned through a very different experience in the U.S. There, eBay led the way and Yahoo! tried with limited success to build an auction business in its shadow. “Yahoo! started the U.S. auction site free of charge, with a huge advertising campaign, and still it could not succeed,” says Inoue.

Yahoo! also benefited from synergies from its other online businesses in Japan. In addition to being the “eBay” of Japan — the No. 1 auction site, with 7 million subscribers — Yahoo! Japan is the country's largest Internet access provider, with 7 million members. In addition, Yahoo! Japan is that country's primary e-commerce site and also the largest portal, with 82% of home users and 90% of office users.

Of course, Yahoo! Japan also has its share of problems. For one thing, competition is emerging in some of its markets. For example, Google Japan has recently launched an aggressive advertising campaign, spearheaded by the Grey Worldwide ad agency, aimed at wooing online users to its Google News service. According to some media reports, though, Google — which has some 1 million home users a month — has a long way to go before it catches up with Yahoo! Japan — which gets more than 13 million monthly home users.

A more serious threat is that customers seem to be rebelling. This month, 572 users sued Yahoo! Japan, alleging that the company had engaged in so-called “online scams” in which customers who had taken part in auctions to buy items such as digital cameras did not receive the goods for which they had paid. *Japan Today* magazine reported on April 2 that according to the plaintiffs' attorney, Yahoo! Japan, as the intermediary, was obliged to help execute deals smoothly. This represents Japan's first class action lawsuit, and its outcome could have a significant impact on Yahoo! Japan's future credibility and also its business prospects.

Growing Market

Still, so far, Yahoo! Japan has been forging ahead. Internet usage in Japan is estimated to have increased by 13% since 2003 and is likely to grow more in the future. Increasing broadband penetration will boost users, page views and time online. To continue to build the business, Yahoo! Japan is expanding vertically and horizontally. Horizontal movement is taking the company into areas such as financial services, employment services, entertainment and selling automobiles. The company moved into travel, in collaboration with the Japan Travel Bureau, building the nation's largest travel site.

Some services haven't sold. While dating is popular via cell phone in Japan, it is not a large service online. “There is a social problem with online dating,” Inoue says. Gaming also has not taken off. “We expected more from the success in the Korean market,” he notes. “We thought it would be the killer app of broadband but it wasn't. Some people think that is because we have so many console game machines at home.”

While cell phone penetration in Japan is high, few Japanese surf the Internet on mobile phones. Yahoo! Japan does offer services on all three major carriers and is one of the largest players in this small market. Yahoo! Japan auction members use their cell phones only to receive alerts when the end of an auction is nearing. (The highest volume in Japan is Sunday night, compared to a Monday morning peak in traffic for eBay in the U.S., which may be a commentary on the surfing habits of workers in the two countries.) Pricing of wireless phone service also limits cell phone use, because customers have to pay packet-by-packet for service, although one carrier recently started a fixed-fee for data connection.

Yahoo! Japan has been posting record results, with operating revenues for the April-June quarter of 2004 of 24.50 billion yen, up nearly 60% year on year, and a net profit of 8.31 billion yen, up 83.1%. The company has succeeded by serving users, Inoue notes. “When we started Yahoo! Japan, we said the priority was users, not revenues.” He notes that “in many cases, we have to choose whether to be nice to advertisers or users, and we always choose users. We believed from the beginning that the Internet business has low barriers to entry. It takes a relatively small investment and no big facility or factory. The most difficult part is to maintain existing users and introduce new users. We still believe we are in that stage where users have more priority than revenues.”

eBay has made it clear it intends to return to Japan at some point in the future. Yahoo! knows from history that the island nation cannot be complacent about the world around it. This is a world in which rival eBay is spreading its reach and power. While this is not a threat to be taken lightly, Inoue expresses confidence. “When eBay's chairman is asked if she will return to Japan, she has said she would be back,” he said. “If they come to Japan and offer service free of charge, they may get some impact. But we will survive.” ♦



Born to Be Wasabi: How Harley-Davidson Roared into the Japanese Market

In the U.S., Harley-Davidson suffered some rough years in the 1970s and 1980s, mostly at the hands of Japanese rivals such as Honda, Suzuki, Yamaha and Kawasaki. These competitors emphasized reliable transportation and achieved standards of product quality that left Harley in the dust. Even after a management buyout in 1981, Harley went right to the brink of bankruptcy in 1985. Then, it reinvented its brand and roared back in the U.S. One year before special high tariffs on Japanese imports were due to expire, Harley announced it no longer needed them to compete in large motorcycles. It is now one of the strongest global brands.

“Harley-Davidson motorcyclists buy our products for pleasure, not for transportation.”

—Toshifumi Okui, president,
Harley-Davidson Japan

Then the brand raced into the Japanese market, snatching control of the large-motorcycle market away from its competitors. How could this icon of American independence succeed in a land of consensus and collectivism? Partly, its success was due to its Western rebel image. But its emphasis on a “family” atmosphere and community of riders also is, remarkably, quintessentially Japanese.

A Tough Road

The prospects did not look so promising when Harley-Davidson Japan was established in 1989. It

faced several seemingly insurmountable hurdles. The overall market for motorcycles in Japan had been declining since 1982, and it continued to fall from peak annual sales of more than 3 million units to just 700,000 in 2003. Harley's motorcycles were twice the price of giant rivals such as Honda, Suzuki, Yamaha and Kawasaki who dominated the market (and still lead in smaller motorcycles).

Yet Harley-Davidson Japan President Toshifumi Okui, who joined the struggling company in 1990 after a career as one of the most successful salesmen for Toyota, has defied giant competitors and the declining market by posting continuously rising growth in a “sunset market.” Since 2000, Harley-Davidson Japan has been the market leader in motorcycles above 751 cc., now with 30% of the market compared to the 16% held by nearest rival Honda. While it is a small company in a relatively small but growing niche (major players still control 70% to 80% of the total market), the company demonstrates the unexpected opportunities for building a successful brand in the Japanese market through creative approaches.

A Collection of Enthusiasts

Part of Harley's success in the U.S. market and in Japan has been excitement about the brand. “Harley-Davidson motorcyclists buy our products for pleasure, not for transportation,” said Okui at a recent session of the Wharton Fellows program in Tokyo. Harley-Davidson Japan uses lifestyle marketing and events as contact points for attracting new customers. An annual Blue Sky Heaven event is expected to attract 200,000 participants this year for demonstrations, pet fashion shows, test drives and other activities to reinforce the brand experience

and attract new customers. Store design and activities are focused on creating a fun experience or “retailtainment,” as Okui calls it.

“Harley invented the philosophy that the brand is an asset of the owners, not of the company,” said Hotaka Katahira, chairman of Marunouchi Brand Forum and a researcher at the University of Tokyo who has studied Harley’s Japanese business. “Harley is not a machine, but a world, a collection of enthusiasts.”

This message of community appealed to Japanese customers as much as Harley’s open-road U.S. image. “The idea of getting people to come together around one theme is a strength of the Japanese people,” Katahira said. “While Americans are basically independent, Japanese tend to gather together. Okui focused on that point and found a good match between the approach and the character of the Japanese people.”

In addition to the strength of its brand and its “family” network, Harley has a coherent process for bringing new riders into the fold that includes events allowing prospective customers to try a motorcycle, driving schools to earn their licenses and then the final purchase at a dealership. While only about 5% to 7% make it through the entire process, this has been enough to fuel the company’s growth. Harley-Davidson Japan even has events for children, bringing them into the Harley family long before they can become customers.

“The brand is a fantastic experience, like Disneyland,” said Katahira. “If anyone isn’t interested in Disneyland, just take them there for the experience. Harley dealers complain that it costs nothing to sell Harley-Davidsons, but it costs a lot to entertain the owners. They are offering them the pleasure of being an owner.”

Delightful Relationship

Harley’s approach is relationship marketing in its purest sense. The company doesn’t talk about locking in customers, but rather about embracing them as part of the family. “To stay at the top, we must continue to make efforts to sustain our delightful relationship with customers,” Okui notes. “We often hear companies say that when they develop relationships, they are trying to ‘encircle’ customers or ‘fix’ the customers. Would you encircle your wives

or sons? Is that the way you secure them? How can you do that with the customers? The bond or the tie is a delightful relationship we have built with the customers. That is the difference between us and some others.”

At the center of this relationship with customers is Harley’s independent but exclusive dealer network. There are just 116 Harley-Davidson Japan dealers in that country, representing a drop in the sea of 12,500 total motorcycle dealers nationwide. But Harley dealers have more than four times the number of employees and more than 10 times the sales of the average motorcycle retailer in Japan. The network is expected to remain relatively small. With just 200 dealers, the company could double its sales.

“Harley invented the philosophy that the brand is an asset of the owners, not of the company.”

—Hotaka Katahira, chairman,
Marunouchi Brand Forum

While other motorcycle retailers in Japan represent multiple brands, dealers that are part of the Harley “family” only sell its products. Harley-Davidson Japan spends a lot of time managing dealer relationships, using both carrots and sticks. It uses its own sales force automation and customer relationship management applications to collect real-time data on dozens of marketing activities, and it works with dealers that have low sales using a systematic process. The company also builds relationships with dealers through a Dealer Guide Book, with photos of every dealer and all their employees. The company sends flowers and cards to dealer employees on their birthdays and anniversaries. “Unless we have this attitude of working together with the dealers, we cannot build bonds with customers,” Okui notes.

Where some cycle retailers had been greasy garages, Harley worked with dealers to create showrooms that would demonstrate the fun of the brand. Harley-Davidson Japan also trains mechanics to service its motorcycles and offers safety courses for customers. The company recently created its first “concept shop” — a showcase of products and

experiences — and expects to build others. While the company has a web site with links to dealer pages, there are no direct online sales per corporate policy. “For us, after-services and the lifestyle program is so comprehensive based on building solid relationships with customers,” Okui says. “You need to build on activities and interfaces. The web is only a supplementary measure.”

While the company has a relatively small staff at headquarters, it has focused on building pride. “Our employees have to be proud of our company,” says Okui. “Our motto is to be a small, world-class company.”

The Road Ahead

Harley-Davidson has a fairly unique product and image, but is its model transferable? Could Okui have done the same thing with Corvette? “At this point, it would be quite tough,” he notes. “How good is Corvette? Does the company have a world view it could offer to Japanese customers so that they would be able to share that view and lifestyle? How much culture and lifestyle is in Corvette? Does the company have those assets? I don't think we could be successful with Corvette alone. Is Corvette well distinguished from competitors? The main brand Harley was well established.”

Harley-Davidson Japan sees strong prospects for the future. It has a phenomenal 90% repurchase rate (although the average life of a motorcycle in Japan is 60 years), and Harley has posted increasing customer satisfaction. Ridership among women is also rising, with about 7% female ownership, comparable to the U.S. And the large and aging baby boomer population may have the financial resources and desire to rediscover its youth. Harley's brand continues to be strong, with surveys finding that 70% of people either own or want to own a Harley someday. “For the next ten years, at least, we are in a pretty good position,” Okui says. ♦



What Is the Global Economy?

The Financial Times *once described Kenichi Ohmae as “Japan’s only successful management guru.” Born in 1943, he holds a PhD in nuclear engineering from the Massachusetts Institute of Technology. After working as a senior design engineer for Hitachi, Ohmae joined McKinsey & Co. in 1972 and co-founded its strategy practice. As a senior partner in the consulting firm, he ran its Japan office for several years.*

Ohmae is the author of several books, including The Mind of the Strategist, The Borderless World, and The End of the Nation State, among others. His most recent work is The Next Global Stage: Challenges and Opportunities in Our Borderless World (Wharton School Publishing), in which he argues that globalization has already occurred, is here to stay, and is about to move to a new stage. In the following excerpt from the book’s first chapter, Ohmae discusses the main features of the global economy. The chapter begins by pointing to examples of the global economy in places as diverse as Dalian in China, Dublin in Ireland and Helsinki in Finland:

What are the characteristics of this new global economy relished in places as diverse as Dalian, Dublin, and Helsinki? Terminology is always an inexact science. Every term is a linguistic sieve. So, before attempting to define it, let’s just say at the outset what the global economy is not.

What can be said is that the global economy should be differentiated from the notion of the “new economy” that sprang up in the late 1990s. This trumpeted a brave new economic order based on the fantastic technological advances unleashed through the Internet. It was a model that mistakenly saw a paral-

lel and unstoppable rise in productivity. The wheels fell off this conceptual wagon in April 2000 with the sudden decline in technology stocks.

Apart from its manifest intellectual weaknesses, this “new economy” has very little in common with what we will talk about. The global economy is based on a world in which borderlessness is no longer a dream or an option, but a reality. This has been helped by the cyber-revolution, but it is not the same phenomenon as the cyber-revolution itself.

The global economy has its own dynamic and its own logic. It is no longer theory; it is reality.

Multiples of stock values, as well as derivatives and financially engineered products, also matter far more in the global economy.

The global economy has its own dynamic and its own logic. It is no longer theory; it is reality. It is going to grow stronger rather than weaker. It will feed on its own strengths. It is irresistible, and it is destined to have an impact on everybody—businessmen, politicians, and bureaucrats, but, most important, ordinary citizens. There is no use complaining about it or wishing it to go away. People will have to learn to live with it.

The emphasis here is on learning because success and even survival depend on acquiring novel outlooks and relationships with the rest of the world. This book hopefully goes some way toward pointing a route toward these new outlooks and relationships.

Some people and countries might be determined to fight against the reality of the global economy, using the old mind maps and the old paradigms. However, the cost in economic and especially human terms will be enormous. Progress is as inevitable as death and taxes. Traditional nation-states and national governments face a great challenge. Some seem to want to approach this new world with one foot stuck stubbornly in the shore of the past for support while they gingerly test the water with the toes on the other.

Some are better placed to take advantage of the global economy's opportunities. History favored the United States by providing it with a truly federal form of government. As a result, states such as North and South Carolina, known as the Carolinas, can pursue an innovative economic agenda without risk of being stymied by central government. The battles between state and center have been fought over and resolved. The constituent states are each well placed to take advantage of the global economy. This does not mean that all 50 states do so. Some still seem to be wedded to a past based on Canute-like protection of "strategic" economic sectors.

But at the opposite extreme, there are states such as Japan, Russia, and Indonesia, which maintain centrality of decision making in theory and practice. No region succeeds because no region is permitted to succeed independently of the rest of the state. Their central governments are jealous of allowing any directional role to escape the center. They are swimming against a tide that could yet inundate them. Of the BRICs, only China has the governance structure to help its regions to work interactively with the global economy. Others have a long way to go before their central government really wakes up to the calls of the rest of the world.

The task of describing what this new world is may be difficult. If all the news stories and clippings about globalization are assembled, the integrated picture that emerges is distorted. Not all the components fit neatly together; it is a wild, abstract mosaic rather than a jigsaw.

But let us forget the scare stories and the merchants of bad news, and instead try and see what we can say positively and with certainty about the characteristics of the global economy: It has innate characteristics, which I list in no order of importance.

The world is an increasingly borderless place. Tariffs are evaporating as countries realize they need each other to survive economically.

Borderless

First, as I have long argued, national borders are far less constrictive than they once were. Some of this has been thanks to technology, while some has been the result of international and bilateral agreements, especially in the area of trade. The world is an increasingly borderless place. Tariffs are evaporating as countries realize they need each other to survive economically.

Other federal states in the world do not allow their constituent members anything like real autonomy, and the central government maintains a tight rein on regional developments. Examples include India and Brazil, two of the BRICs (Brazil, Russia, India, and China), according to Morgan-Stanley's new jargon of promising new economies. In terms of the global economy, these nations are still asleep as a whole nation. Nevertheless, some of their regions have begun to take their places on the global stage. China adopts a somewhat schizophrenic policy; in theory, it follows a rigid, centralized political formula. In practice, unprecedented economic autonomy has been allowed to regions and cities, particularly since Zhu Rongji's reform of 1998.

It is not yet completely border free, as nation-states still have reasons to maintain controls on the movement of people and goods in the interest of security and public safety. But in terms of four key factors of business life, the world has already attained the position of being effectively without borders. These business factors I have labeled the four C's: communications, capital, corporations, and consumers.

Effective communications always depend on the nonexistence of borders. It was one thing when communication was predominantly physical. If a person wanted to go from A to B or send something there, be it a letter or a product, the inert force of

gravity often slowed the process down. Slowness of movement was further added to by border check-points, the need for visas, and passport control, not to mention custom and excise inspection. People viewed these as obstacles and deterrents. But technology spurred an improvement. Telephone lines allowed a person to speak with someone directly on the other side of the world, without having to go through a host of intermediate exchanges. Once such lines of telecommunication, existed they could be used for data transfer. Improvements also occurred in the production of cables using fiber-optic technology. A barrier to communications remained while the conduits of this communication still had to pass along wires, which, in turn, had to be laid across mountains or oceans. The latest technological advances do away with wires and their costly installation and maintenance. When data is carried by radio frequencies, it is absurd to believe that lines drawn on maps can have any impact on its movements.

Telecommunication benefited from a process of deregulation in the 1980s, and many former state monopolies were privatized, thereby increasing competition and lowering costs for consumers. Domestic markets that had formerly been imprisoned in the clutches of national communications monopolies were opened up. Many communications companies co-operated and entered into alliances; others merged so that the telecommunications world was changed from a patchwork of state monopolies into a far more dynamic and colorful kaleidoscope that did not respect national borders. Many telecom operators, including TeliaSonera, Vodafone, and Telefonica, have become truly global.

Yet it was the development of the Internet from the mid-1990s onward that has probably had the greatest impact on making the world of communications truly borderless. This is a technology that is widely available, accessible from personal computers anywhere. Traffic passes through it oblivious of borders.

The second C, capital, is also a beneficiary of a borderless world. This, too, has been aided by deregulation of financial markets. It has also been assisted by the position of the U.S. dollar as a monetary platform. Not only is it the major trading and settlement currency, but it is also the currency of choice for many savers throughout the world. In most devel-

oped countries, the aging population save money for their retirement. The trouble is that no OECD member country offers adequate returns for an investment at home. This is one of the biggest reasons why a massive cross-border migration of capital, both short and long term, has occurred.

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Some corporations have successfully responded to the borderless economy by shedding the trappings of the nation-state that hindered their self-awareness. It was far too common in the past for a successful corporation to identify closely with a "home base," a company headquarters, or a corporate "home town, where it all began." Some of this might have been sentimental, but it was outdated if the corporation saw the world as its marketplace. Improvements in telecommunications mean that companies do not feel tied down to a corporate headquarters in a certain city. If circumstances demand it, they might even dispense with legal ties to their home bases by reregistering in another, more favorable location.

The last two decades have seen a remarkable decomposition of corporate functions, ranging from R&D and manufacturing to sales/marketing and financing. It is now common within an individual company for these functions to be located across national borders—for example, R&D in Switzerland, engineering in India, manufacturing in China, financing in London, while the marketing function and HQ remain in the United States. More recently, indirect work has been outsourced: Witness the growth in call centers in India and elsewhere, and the outsourcing of logistics to specialists such as FedEx, DHL, and UPS.

It is in terms of the last C, consumers, that the borderless element of the global economy has made itself felt most keenly. Consumers have the ability to do what they have been urged to do many times:

shop around. The Internet gives consumers the ability to compare products and prices and make a much more informed choice more easily. Platforms for paying by credit card then allow the purchase to be made, processed, and delivered. There might still be some who are emotionally tied to the ideal of the nation-state, who support demagogues seeking greater protection of domestic businesses and jobs, but when they are presented with a choice of two similar products, one (product A) available locally at a price considerably higher than product B, which originates elsewhere and still enjoys a price advantage when delivery charges are added on, only the most die-hard partisan of the nation-state will opt for the pricey product A. The reality is that it is almost impossible to buy a shirt that is genuinely "Made in America." Its fabric may come from Egypt, threads from Japan, and buttons from the Philippines. If only the sewing process takes place in the United States, how American does that make the finished shirt?

Some of the most important developments are earth-shaking in their potential, but their implications are not fully understood outside of a small circle of players. As a result, they are not headline news; they are lucky to feature in the news at all. As for the print media, they may be buried rather inconspicuously in the business pages.

Consider a few aspects of this invisible world. Transactions and settlements of money now take place mostly on and through computers. Some products are also purchased in the plaza known as B2B and B2C trade exchanges, or as C2C auctions. Most ATMs around the world spit out local currency if you use your home country cash/credit card with Plus or Cirrus membership. There is no way for the government to know how much cash you have withdrawn abroad or how much you have spent with a credit card to purchase goods and services across national borders.

Cyber-Connected

The global economy would not be possible, or even comprehensible, without cyber technology allowing large amounts of data to be transferred incredibly quickly. It would not be possible without the corresponding drop in technology prices. The Internet is only the most public part of this. Today, the Internet protocol (IP) is capable of handling transmission of not only data, but also images, voice, music, and videos. Voice over IP (VoIP) is rapidly making inroads into the world of traditional telecom providers, but music and movies are also downloaded across national borders, as long as there is a line with IP routers. Everything and everyone connects.

Outsourcing, for example, rests on the capability to model new processes and instantly deliver critical software components, all within minutes of a conversation. The success of Indian software houses, such as Infosys, WiPro, HCL, Tata Information Services, and others, underscores the fact that 24x7 development is no longer a wish, but a reality.

Measured in Multiples

Money makes the world go around. And so the role of money in a global economy must be important. Money is no longer seen only as a unit of value in the short term. The late 1990s and the first years of

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Invisible

Observers might be forgiven for not fully realizing the potency and prevalence of the global economy. It is largely invisible. It might be better said that it is not totally visible to the naked eye. This should not be taken as implying that it is secretive or reclusive. It is because the actions that it performs often take place not on the streets or the debating chambers of national parliaments, but on computer terminals. One of the mechanisms whose development has enabled speedy cash transfer is a piece of plastic: the credit card. It is the preferred means of carrying and spending money for hundreds of millions of consumers. Yet the money that credit-card holders spend is never seen. Sometimes, payment occurs so quickly that not even the most sophisticated camera with an incredibly high shutter speed could record it.

the new century have witnessed a number of corporate takeovers and restructurings that would have been viewed as surreal two decades earlier: In these, a company that had only recently emerged and maybe was not actually profitable successfully acquired a much larger, longer-established, and seemingly solid part of the corporate landscape. None of this was possible without those who assess corporate value looking at a far bigger picture, not one based on the here and now alone and the currently quoted price on whatever share index they chose, but on what the situation was likely to be in 10 or 20 years, and on how this was reflected in price/earnings ratios.

Multiples are signs given to the management by the shareholders to shoot at the business opportunities on the horizon. If the management does nothing other than business as usual, the multiple will come down, reflecting the disappointment of the ammunition givers. Multiples are fictitious, in that they often do not reflect corporate value, but they express an expectation. This can become reality if a company is bought or a new investment is made to fully utilize the multiples.

So the global economy is borderless, invisible, cyberconnected, and measured in multiples. Many of these elements are self-nurturing: They feed off one another. They all involve taking a leap, if only an intellectual leap at first, into uncharted waters.

This global economy is in its infancy. Unfortunately, this description contains an analogy with human development, from the state of the infant, the child, and the uninformed. It might be better to say that the global economy is in the early stages of development, but there is nothing childlike or uninformed about it. It has not emerged like an extraterrestrial from on board a meteorite. It has entered the world through the actions and intellect of human beings. It has not been foisted onto the world by some small, nefarious network intent on world domination. It has developed collectively. And, as we will see, it promises to be beneficial to the world at large.

The excessive capital in developed countries is looking for opportunities to breed. If you understand the logic of the global economy, you can attract companies, customers, and capital to your region or company from the rest of the world. You do not have to

be born rich or be born in a wealthy country to prosper. All four C's can and will come to you if you have the right recipe. Alternatively, if your logic and systems are out of sync with the global economy, the four C's will evaporate, and you will not have an opportunity to perform on the global stage. ♦

Additional Reading and Information

- ◆ Knowledge@Wharton
<http://knowledge.wharton.upenn.edu>
- ◆ Wharton School Publishing
<http://www.whartonsp.com>
- ◆ *The Next Global Stage: Challenges and Opportunities in Our Borderless World*
By Kenichi Ohmae
<http://www.whartonsp.com/title/013147944X>
- ◆ The Wharton Fellows Program
<http://execed.wharton.upenn.edu/course.cfm?Program=FEB>

