Rattling the supply chains

Businesses struggle to contain fallout from the diplomatic crisis

A slight business risk

Anti-Japan riots, the torching of car showrooms, bloody attacks on hapless drivers of Japanese cars—all these have eased in China since the row over disputed islands reached its peak last month. But in Japan, the sense of injury runs deep. Japan's mass-selling weeklies, a barometer of public opinion, have spent weeks fantasising about such once-unthinkable scenarios as a mass pull-out of Japanese companies. "It will be China that collapses," crows one, the Shukan Bunshun.

Not so. According to Keidanren, Japan's business lobby, there are almost 30,000 Japanese firms in China, the result of 40 years of mostly thriving trade. Japan has invested $85 billion in China in the past 15 years, including over $6 billion last year alone. With Japan's economy stagnant, its population shrinking, and energy costs and the currency rising, its firms in China have little choice but to lower their heads and hope that the row blows over. The toll is heavy, nonetheless. Car exports to China, for instance, may drop by 70% in the fourth quarter compared with the third, says J.P. Morgan, a bank. Japan's GDP may dip as a result.

Despite the unfavourable climate, many firms are resolved to press on. Even as its sales in China plunge, and after some soul-searching about the timing of the announcement, Mitsubishi Motors said on October 12th it would launch a long-term tie-up with Guangzhou Automobile Group to make and sell sports utility vehicles. Japan's biggest clothes retailer, Fast Retailing, says it plans to open another 1,000 Uniqlo stores in the country. Shin Tanaka of Fleishman Hillard, a public-relations firm, says retailers are more inclined to keep their plans in place than producers are. Partly that is because they cannot afford to ignore the vast and growing Chinese market. Also, they have less to lose from vandalism.

Others, meanwhile, choose to emphasise different risks in China, especially those of slowing growth. Hiroaki Nakanishi, the boss of Hitachi, Japan's largest electronics conglomerate, had several trips to Beijing cancelled this summer because of the dispute. Hitachi's automotive-parts firms—among 440 Japanese companies supplying carmakers in China—have been hit by the consumer boycott of Japanese cars. But that appears to have been overshadowed by the slowing economy. Before the island dispute, Hitachi's sales of construction machinery, such as earth-movers, had fallen by almost half, year-on-year, he says.

Stunned as both Japanese producers and retailers are by the outbursts, there may be a sting in the tail for China. In contrast to 2005, the previous time anti-Japanese riots flared, China is not the only fast-growing, well-populated, low-cost market around. Back then, Japanese firms hedged their China risk with a “China-plus-one” strategy, implying that they would find an extra Asian supply hub, such as Thailand. Now, that has grown into a wider “China-plus” strategy, because their options these days have widened to include Indonesia, Myanmar, Vietnam, Cambodia, the Philippines and India.

As China’s wages rise and its economy slows, analysts say the risk that multinational supply chains may find alternative locations is something the government may want to think about the next time it lets vandals loose in the name of nationalism. Japanese businessfolk, meanwhile, might try harder to gag their clumsy nationalist politicians, who sparked the row over the islands in the first place.

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