



**Urgent Recommendations
to Encourage Innovation
~Creating Disruptive Innovation
from Super Connections~**



April 17, 2013

Foreword

On April 16, the Japan Association of New Economy (JANE) held the New Economy Summit (NES) 2013, focusing on “Disruptive Innovation”. To this forum, we invited the world’s leading entrepreneurs, people creating the new values and markets that are changing the way we live and do business. We received the participation of many people from the government, industry, and academic sectors.

The event showcased the latest trends in innovative services overseas. There was also an extremely fruitful debate on the kinds of policies we need in order to encourage innovation as we work for the revitalization of the Japanese economy.

Given the speed at which technological innovation is occurring, it is difficult to conceive that a repetition of the old ways of doing business will allow us to develop greater international competitiveness. We have entered an age in which we must seriously question how we can realize the “new connections” defined by the economist Joseph Schumpeter.

As His Excellency the Ambassador of the United States to Japan Mr. John V. Roos said at the Summit, “There is nothing more patriotic than founding a company or working at a start-up. We should applaud such activities with pride.”

The encouragement of entrepreneurship and innovation is truly the issue of pressing concern.

JANE has compiled these urgent recommendations based on the discussions in this summit, considering the ongoing discussion in the Industrial Competiveness Council. In doing so, it is my hope that we can encourage further debate on the growth strategy of Japan.

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1. Background to These Urgent Recommendations

The Abe Administration is currently promoting and considering a three-pronged strategy for the revitalization of the Japanese economy. The growth strategy will be the most important facet in energizing the Japanese economy and ensuring its sustainability.

One famous theory of growth strategies was proposed by the economist Joseph Schumpeter. He argued that the crucial element of any growth strategy is innovation, which he defined as “new connections”.

At NES 2013, it was made clear that if we continue to operate in the same way we have up until now, we will be left behind by our global competitors in the race to keep ahead of rapidly accelerating technological innovation. We have reached an era in which we must truly examine how we can cope with “new connections.”

In consideration of the indispensable need to promote the innovation that will encourage new connections by using the internet, JANE has prepared these emergency recommendations to stimulate the revitalization of the Japanese economy.

2. Seven Messages from the Speakers at NES 2013 to the Government and People of Japan

Participants at NES 2013 had a lively debate on the best methods by which to promote innovation in Japan. We received the following seven messages from the speakers.

- (1) Japan needs to create a society and culture that praises and supports the existence of entrepreneurs who take risks and create new kinds of value that change the world.
- (2) Japan needs to develop national systems that support entrepreneurs.
- (3) There is strategic value in further enhancing the highly latent strengths of Japan (excellence in design, hospitality, attention to details, etc.).
- (4) Japan needs to globalize the public and private sectors.
- (5) Japan needs to assemble superior entrepreneurs and engineers from abroad while at the same time educating the next generation who will take charge of innovation for the future (emphasizing the importance of IT education, programming, and marketing education, among other topics).
- (6) Japan needs to establish tax system that can allow entrepreneurs in Japan to receive support equivalent to the kind given in other countries.
- (7) Japan needs to radically reform regulations that impede innovation.

For further details, please see the Reference section.

3. Specific Recommendations

Around the world, we can see countries that are constantly metabolizing their economies, reforming their industrial structures through disruptive innovation. We believe that a strength of these countries is the existence of an ecosystem to foster innovation.

Promoting innovation is the single most important factor that will determine the international competitiveness of Japan in the future. Japan needs to create an ecosystem for the promotion of innovation, one that is perfectly suited to encouraging innovation in every part of society. We seek the start of an entrepreneurship renaissance in Japan.

Based on the seven messages of NES 2013, we recommend the realization of the following four needed proposals through government initiatives.

- Recommendation 1: Establish a national policy to encourage innovation and foster an entrepreneurial culture.
- Recommendation 2: Reform the tax system to promote investments into venture firms and encourage the creation of new businesses and industries.
- Recommendation 3: Foster and invite to Japan the next generation of global and innovative human resources.
- Recommendation 4: Radically reform regulations for the creation of new markets and new industries.

Recommendation 1: Establish a national policy to encourage innovation and foster an entrepreneurial culture.

The Government should communicate in a clear and visible way, to both inside and outside of Japan, about the policy of making innovation promotion the cornerstone of the new growth strategy. It should foster a culture that encourages and praises innovation throughout Japan, supports those founding new businesses, and creates new industries. And it should create an environment that can inspire young people to dream.

- (1) Provide role models for others by establishing a system to offer commendation and financial awards to people who start businesses or cause disruptive innovation (tentative title: the “Japan Breakthrough Award”).

- (2) As a symbol of innovation promotion, the Government should create a Japanese silicon valley for industry-academia collaboration, as well as a center for R&D incubation in Asia. These should be created as special economic zones, and the Government should promote them inside and outside of Japan, creating innovation success cases.
- (3) A Hackathon* should be held at the Prime Minister's Office. This would produce an environment to praise the engineers and programmers of Japan and promote competition for the creation of new technology and services, and be an excellent opportunity to encourage private sector investment into new business promotion and services.

*Hackathon: A project contest in which programmers, graphic designers and others come together for team-based work to develop and improve software.

- (4) Create opportunities for the Japanese people to interact with global entrepreneurial culture.
 - Hold international events that bring together leading entrepreneurs from around the world. At these events, create far-reaching opportunities for students and others to participate as volunteer staff. Post footage of event activities online, and spread word about the events far and wide using social networking sites and other opportunities.
 - Enhance the tax system in relation to donations made to the civic organizations serving the public good that are supporting the operation of international events like the kind mentioned above, study abroad trips by young people, and so on (e.g. Change from income deductions to tax deductions).

Recommendation 2: Reform the tax system to promote investments into venture firms and encourage the creation of new businesses and industries.

- (1) Work to enhance preferential tax measures for venture investments.
 - Enhance the tax system for angel investors (shift the treatment of contribution deductions for investments into venture firms from being classified as “income deductions” to “tax deductions,” expand the range of eligible businesses, etc.).
 - Create a preferential tax system for groups and others that provide venture capital or invest into venture firms.
- (2) There are plans to abolish the system that makes it possible to record capital gains

earned by publicly and non-publicly listed companies on profit and loss statements within three years. This system should be maintained.

- (3) Allow for flexibility regarding investigations of individual investors when auditing stockholders as part of the standard procedures for listing on the Tokyo Stock Exchange.
- (4) Introduce and strengthen a tax system to promote spin-off companies created from the in-house ventures of existing corporations.
- (5) Strengthen locational competitiveness by lowering corporate tax to a level in line with global standards.

Recommendation 3: Foster and Invite to Japan the next generation of global and innovative human resources.

- (1) Introduce TOEFL to university entrance and civil service examinations, and shift the focus of English classes from elementary school onward to the kind of real-world English that is actually used in conversations.
- (2) Promote IT education and education for starting businesses.
 - To raise Japan's IT skills, introduce and enhance class topics for education related to computer science, computer programs (use of Scratch, etc.) and app development.
 - Give one electronic device to each student and improve IT literacy. Shift the focus of education to fostering critical thinking skills and discovering the different ways in which each student solves problems. Set the case study of Denmark as a benchmark.
 - Have those with experience programming and starting businesses act as teachers, and offer practical and high-quality education at every school through the use of distance learning.
- (3) Introduce finance, management, and marketing curriculum in order to improve Japan's capacity for business innovation.
- (4) Implement initiatives to gather excellent entrepreneurs and engineers from around the world.
 - Work to fundamentally strengthen measures to lure human resources to Japan, including easing of visa requirements and realization of preferential income tax systems.
 - Strategically promote the strengths of Japan overseas and implement activities to invite excellent companies to Japan via embassies and other organizations.

Recommendation 4: Radically reform regulations for the creation of new markets and new industries.

- (1) Eliminate systems that inhibit the use of the internet (eliminating the principles of face-to-face and on-paper delivery, etc.).
- (2) Promptly create a detailed work plan to realize the separation of power generation and power transmission/delivery at the earliest possible date, without any return to the old system.
- (3) Thoroughly carry out regulatory impact analysis (including the international benchmarking) when introducing new laws and ministerial ordinances, and construct a system through which the Regulatory Reform Councils shall make reports before the final decision as needed.

4. Future Activities of JANE

- (1) Continue strenuous efforts to propose specific policies for innovation.
- (2) Following up on the international event this time, which gathered entrepreneurs from across the globe who had developed services that revolutionized the world, continue to hold events, inspire young people to dream, and undertake activities that encourage and praise innovation.

Reference: Highlights from Statements made by Panelists at NES 2013

(1) Fostering a society and culture that support the entrepreneurial spirit

- “Innovation means doing something differently from other people. You cannot have innovation in a culture that believes that ‘the nail that sticks up gets hammered down.’ You need a culture that thinks, ‘The nail that sticks up should be praised.’”
- “The good thing about silicon valley is that there are a lot of people around who will support start-ups. They don’t ask ‘What if you fail?’ they ask ‘What if you succeed?’”
- “America praises its successful entrepreneurs like heroes. That’s why young people want to be entrepreneurs.”
- “Entrepreneurs are the heroes that create future jobs. Everyone should support them.”
- “For the young people in Japan today, the post-bubble world is all they have ever known. They don’t know what success is like. We need to spread the word that companies can succeed, and that growth can be wonderful.”
- “We don’t just need a culture that doesn’t fear failure, but one that forgives failure too. It’s rare for anything to go well from the beginning. What’s important is to learn from mistakes, and to use that learning immediately to fix your business.”
- “When I first started a business, I lost about 4 billion yen. But after that, I was successful”
- “We need to take good care of our engineers.”
- “It’s important to start businesses. Entrepreneurs have big dreams, they take risks, and they don’t fear the future.”

(2) National systems to promote the development of an entrepreneurial culture

- “One action that the Government can take immediately is to praise entrepreneurs. If the Government talked about entrepreneurs every day, people’s attitudes would change.”
- “We need to create incentives that motivate people to start businesses. And of course this includes social incentives, but we also need monetary incentives.”

(3) Enhancing the strengths of Japan

- “I think Japan has three strengths. It has great design, it’s great at service, and it pays attention to details.”
- “Everyone outside of Japan thinks it is a magical place. People think Japan is creative. It is the Japanese people who are pessimistic.”

- “In terms of the quality of human resources, there is no difference between Japan and other countries. If anything, Japan is stronger in math than America is. What Japan lacks is confidence and positivity.

(4) Globalization

- “There is nothing so different about the Japanese consumer. Products successful in Japan can be successful overseas. i-mode was a wonderful eco-system. It had the potential to take the global market.”
- “My one-year study abroad experience changed my outlook on the world. It dramatically widened my view of things.”
- “Attracting excellent human resources from abroad means more than just appealing to them using the charms of Japan – you need to sell them on coming here. For instance, in the United States, they prevent top-class people from leaving by giving university graduates priority for visas. That is the level of competition there is in the struggle to attract personnel around the world.”
- “The governments of countries everywhere are working to attract companies from other countries. Just the other day we were visited by the Embassy of Singapore and invited to expand there.”
- “You need the kind of resolve that would aim to make Japanese services the major services used worldwide.”
- “The world is moving toward the modularization of homes and cities, and the industry will become more about providing packages.” “We haven’t seen compact cities in Japan yet, but there is the chance to develop this idea during reconstruction of Northern Japan. And Japan’s model could be exported overseas.”

(5) Educational reform

- “If I was going to propose anything to Japan, it would be the reform of the university education system. University educations are too specialized. We need people with more general educations too.”
- “The Japanese education system creates docile children. It kills their creativity. Not everyone needs to be original, but we must recognize that we do need a certain proportion of people who are inventive.”
- “Japan must start teaching programming and marketing curriculum as soon as possible if it wants to increase the number of entrepreneurs.”

(6) Tax reform

- “It isn’t at all the case that Japanese engineers are less skilled than their foreign counterparts. If there is anything clearly wrong in Japan, it is that salaries are

too low.” “That is a result of the high corporate tax in Japan. Most IT companies abroad pay an effective tax rate of around 10%. Japanese companies pay approximately 40%. There aren’t enough funds to reinvest, including in personnel.”

- “I am investing in a number of companies in Japan, China, and the United States. The environment in Japan for new business promotion is absolutely the worst. First, high taxes are levied on venture capital. In order to create an environment equivalent to the one in China, Japan should free venture firms from tax obligations for a period of about five years. And it should be possible to exercise stock options at a low cost.”

(7) Regulatory reform

- “We have branched out into countries all around the world and dealt with the regulations each time. But the regulatory situation in Japan really is terrible. The regulatory agencies have created many irrational rules that only serve to protect the industries that they are regulating.”