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# Vox pop

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young Japan

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# Banking on

JONATHAN

**A**ny thoughts Masaru Hayami may have had about a quiet retirement were put on hold this spring when Prime Minister Ryutaro Hashimoto picked him to be 28th governor of the Bank of Japan. These are not the best of times for Japan's central bank, and, at 73, Hayami is the oldest man to fill the position.

Given the circumstances under which his predecessor left, Hayami may prove to be an inspired choice. A respected business leader, he replaces Yasuo Matsushita, who was forced to stand down after a senior BOJ official was arrested on graft charges.

Hayami's appointment brings to an end the long-standing and much criticised arrangement whereby the governorship alternated between career officials of the BOJ and retired Ministry of Finance ones. Given that the MOF is also mired in scandal, the prime minister had no option but to make a bid to restore the bank's tarnished reputation.

**ALTHOUGH AN UNEXPECTED CHOICE**, Hayami fits the bill. He brings to the post successful private sector credentials and stewardship of a leading business organisation. Moreover, he's no stranger to the central bank.

Upon graduation from the Tokyo University of Commerce (now Hitotsubashi University) in 1947, Hayami spent 34 years at the BOJ, rising to the post of executive director via stints in New York and London, and making international finance his specialty.

Then, in 1981, he "descended from heaven" to join Nissho Iwai, the trading house his father-in-law helped to found, which at the time was reeling from a payoff scandal. Within three years Hayami had been promoted to president (and later chairman), being seen as the best chance for cleaning up the firm's tainted corporate image. The fact that he pulled this off evidently weighed heavily in his favour with Prime Minister Hashimoto as he narrowed down the list of candidates.

From 1991 to 1995 Hayami also served as chairman of the Japan Association of Corporate Executives (Keizai Doyukai), one of Japan's leading business organisations. These were turbulent times in Japanese politics, and Hayami was unusually outspoken in his calls for political reform as administrations came and went under prime ministers Kaifu, Miyazawa, Hosokawa, Hata and Murayama. Indeed, at the press conference to announce his ascension to the Keizai Doyukai's top post, he caused a stir by drily remarking that Japanese politics would be the better for having some principles.

It is his reputation for being "spontaneous" and "unconventional" as evidenced by such remarks that lead some to wonder whether Hayami is cut out for a job that

# Iceberg

GERARD

**T**itanic and *As Good as it Gets* dominated this year's Oscars. Both titles are apt for discussing the world's two largest economies. It is hard to imagine the US economy getting much better. Growth is strong, unemployment is falling, inflation is low and the stock market is booming. For the US it certainly seems to be as good as it gets. By contrast, the Japanese economy seems to be sinking fast. At the end of April, the *Yomiuri Shimbun*, a conservative daily paper that traditionally supports the governing Liberal Democratic Party, devoted its front page to demands for a change in economic policy as it likened Japan to the Titanic.

Perhaps this analogy is right. Yet if problems in Japan turn out to be that bad then it might be more apt to view Japan in the role of the iceberg that sinks the rest of the world. Make no mistake, problems in Japan can have a global impact.

It is best to be cautious about immediate prospects but it is important to realise that Japan has bounced back many times from economic shocks. It has the ability to bounce back now particularly as recent weakness is triggering a rethink in economic policy and forcing companies to

restructure. The net result should be positive for the economy but it could take some time.

## STRUCTURAL PROBLEMS

Japan's present problems stretch back to the bursting of the economic bubble in 1990. The consequences were more dramatic than many realised at the time and eight years later Japan is still facing economic problems, because there remains the need for deep-rooted changes in the Japanese economy.

For some years now I have described Japan as being affected by the four 'Ds' of debt, deregulation, deflation and deindustrialisation.

Debt has been a problem ever since the Bubble burst in 1990, with banks left nursing sizeable bad loans.

Deregulation has been the most pressing need throughout the 90s. Some has taken place, but not enough. Japan needs to deregulate in a host of areas, opening the economy up to

# experience

LLOYD-OWEN

requires strict political neutrality. On the other hand, there is no doubting his grasp of monetary policy and international financial markets, and his wealth of experience both inside and outside the bank.

As Chief Cabinet Secretary Kaneko Muraoka explained the appointment, Hashimoto chose Hayami "because he is well versed in economic and financial affairs from the point of view of business circles and the financial authorities, and because he has a good reputation abroad." Adds an analyst, "He knows how the place works, but also he can be portrayed as a clean pair of hands."

HAYAMI'S ARRIVAL COINCIDES with revisions to the Bank of Japan Law designed to strengthen the bank's independence and bring greater transparency to its dealings. He also brings to the job his own views on the role of a central bank, which must serve as "the economic conscience of the nation... a public institution that gives people a sense of security by maintaining the stability of the financial system."

With a new man at the top and a new structure, the bank hopes to change its ways. However, after more than a century of being shielded from outside criticism, it may not be that easy to reform itself. Following the arrest of the Credit and

Market Management Department chief, the bank launched an internal investigation resulting in a decision to punish 98 officials for accepting excessive amounts of entertaining from commercial banks. Many observers fear, however, that this is no more than a slap on the wrist, and much more must be done to stamp out the culture of collusive relations between BOJ officials and executives at private banks that results in leaks of confidential information.

What with the parlous state of the economy, international pressure for Japan to do something about it, and Japan's Big Bang to oversee, the central bank chief looks to have his work cut out. The question is, given his age and the demands of the job, will he complete his full five years in the post? According to one scenario, he will serve out the remaining 19 months of his predecessor's term, before making way for Toshihiko Fukui, the former deputy governor who resigned along with his boss last March. Just as Hayami was seen to be sufficiently removed from the central bank after his second career in the private sector, so Fukui may be ready for a comeback after a period of reflection off stage.

Either way, Hayami's appointment marks the start of a new chapter in the bank's history, and one that is being written at a momentous time. As the BOJ's oldest governor told its newest recruits at their April 1 induction ceremony, "Looking back over the 116 year history of the Bank of Japan, I don't think it has ever been exposed to such changes or such ordeals as we now face." □

# ahoy!

LYONS

greater competition, removing barriers to trade, improving openness and transparency.

Deflation has been a recurring theme in Japan, as firms have cut costs in response to difficult times. Now deflation is again a concern, with a squeeze in firms' profit margins resulting in a cutback in jobs, inventories and investment.

Deindustrialisation – known in Japan as hollowing out – had a great impact in the early 90s, as manufacturing firms shifted production to lower cost centres elsewhere in Asia.

There is a general perception that Japan needs to change further, particularly in the wake of ongoing political and financial scandals, as these highlighted the lack of transparency in some areas of the economy.

## TURBULENT PERFORMANCE

In recent years Japan's economy has had a turbulent time. In 1995 Japan was on the brink of recession and financial meltdown. In response, the authorities relaxed policy

significantly, weakening the yen, relaxing fiscal policy and cutting official interest rates to only 0.5 per cent. This policy easing worked. In 1996 Japan became the fastest growing of the major industrialised economies. Strong consumer spending resulted in economic growth in excess of 4 per cent.

Just when it seemed that people and companies were regaining their confidence, the situation turned sour. 1997 was a bad year. The Government misread the economic situation and announced badly timed tax increases in April 1997. Consumption slowed. Then the Asian currency crisis later in the year hit the economy hard, forcing Japan into its present recession.

When Japan ran into trouble earlier this decade the impact on the rest of the world was muted. Now things are different and there is a clear need for the rest of the world to sit up and take note. As Japan is Asia's biggest and most powerful economy, if the economy falls from recession into a slump it could pull economies in Asia down with it. There could be another round of currency devaluations in Asia.

Since the Asian currency crisis, there has been intense international pressure on Japan to change policy and turn

its economy around. In particular, America has put immense pressure on Japan to play a lead role and be a solution to Asia's problems, not a symptom of them. For this, its economy needs to be buoyant – but it is far from that.

#### CURRENT WEAKNESS

In early April the Bank of Japan released its quarterly economic survey, the *Tankan*. This is the most comprehensive survey of its type in the world and 9,308 firms took part, including every major Japanese company. The result was not good, highlighting a significant decline in business confidence.

Last year's tax increases and fears about job losses have led to weak consumption, as people have increased their savings. Moreover, 42 per cent of Japanese exports go to the rest of Asia, highlighting the significance of problems elsewhere in the region.

When the economy was weak in the early 1990s the Government responded with a series of packages, each one injecting huge amounts of money into the economy. As the impact of one package wore off, another was announced. These packages prevented the economy from falling into a slump earlier this decade, but they also resulted in a deterioration in the Government's finances and deterred private companies from undertaking necessary restructuring.

By last summer the Government decided that the economy no longer needed its help; it was time to reduce the level of government debt and improve public finances. Japan's rapidly ageing population fed such concerns about the fiscal outlook.

Prime Minister Hashimoto announced Japan's version of Europe's Maastricht Treaty in the form of the Fiscal Structural Reform Law, which aimed to reduce Japan's budget deficit.

This aim for better public finances could only be achieved by reducing the Government's flexibility to spend and to cut taxes. As the economy began to weaken last year this new Law soon became a hindrance, not a help.

Since last autumn, the US authorities, the Japanese Opposition and many in the financial markets, including myself, have called for Japan to relax its Fiscal Law and to give a boost to the economy through permanent tax cuts in order to encourage people to spend. Since then five economic packages have been announced. The initial focus was on stabilising the financial sector and promoting deregulation. These measures were good, but not good enough.

The Government believed that once the financial sector stabilised, confidence would return to the general public and the economy would rebound. Then, following the disappointing April *Tankan*, the Government realised the economy needed a bigger boost and announced an economic stimulus of ¥16.65 trillion. This is a huge amount. It should help the economy improve before the end of the year. But financial markets are suspicious. There is no doubt this latest package will keep Japan afloat but the question is whether Japan's private sector can learn to swim and survive without the Government's help. I think it can.

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## The British Research of Japanese Companies

LOUIS TURNER, DAVID RAY, TONY HAYWARD

More than 100 Japanese companies are now conducting Research, Development and Design in the UK. These operations range from straight product development ventures, such as Nissan at Cranfield and Sony's Liverpool computer games subsidiary Psygnosis; through classic medium-term R&D (Sharp's three-dimensional display work outside Oxford just one example); to "Blue Sky/North Star" research with British universities (Hitachi and Toshiba with Cambridge University's Cavendish Laboratory).

This new study by Louis Turner, Chief Executive of the UK-Japan High Technology Industry Forum, and co-authors David Ray and Tony Hayward describes the main cases of Japanese research in the UK; discusses their motives and the impact on the UK; and argues that, generally, this area of British and Japanese collaboration is a positive sum game, from which both sides gain.

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