







Exploring for Better Global Governance Based on Holistic Approaches to Achieve Welfare, Equality & Security

17 articles have been selected for the Annual Review 2019 from the six issues of the past year.

-  May/June 2019 Issue (#225)
-  July/August 2019 Issue (#226)
-  September/October 2019 Issue (#227)
-  November/December 2019 Issue (#228)
-  January/February 2020 Issue (#229)
-  March/April 2020 Issue (#230)



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Introduction

Japan SPOTLIGHT's Annual Review 2018 highlighted an article on the digital society and it depicted digitalization as volatile, uncertain, complex and ambiguous. This description can also be applied to the new globalization. At the start of FY 2019 we began our Cover Story with remarks on such issues as income inequality, trade, and aging societies that were set to be discussed at the G20 Osaka Summit in June by some distinguished think tank leaders known as the T20 (global think tanks whose mission is to provide analytical materials for G20 leaders so that they can make better decisions in their meetings). This was when *Japan SPOTLIGHT* started to highlight stories on the issue of global governance. The decline in social cohesion among developed nations triggered by expanding income inequality was a crucial issue, as it is considered a reason for rising nationalism against globalization, a principal source of volatility and uncertainty in 2019. Complexity and ambiguity are also intensified by another aspect of the new globalization, namely the advance of digital technologies. All this means that global governance in 2019 truly faces significant challenges.

Digital technologies are complex by nature, since they can have an impact not only on the economy but also on national security, depending on how and for what purpose they are used. Their impact on national security is ambiguous. Only private business people engaged in working on developing or applying these technologies really know exactly which ones would be sensitive to national security concerns. Digital technologies would also transform North-South international relations. With digital technologies, knowledge – the most important production factor in the digital age – could be easily transferred from developed nations to emerging nations. This would bring about a great convergence of economic performance among nations rather than great divergence. Thus fast-growing emerging nations could be a serious threat to developed nations and provoke anti-globalization or nationalistic sentiment among the latter. This is one interpretation of the background to the US-China tech cold war. This geopolitical risk and other rising ones such as North Korea or Iran could transform the major nations' foreign policies.

Bringing national security discussions into the technology domain has another consequence for global governance. As technology has a crucial impact on the economy and one that should be largely positive, while its impact on national security is mostly negative, we would need to find a balance between economics and security. This means that we would have to find a good global governance venue for discussing economics and security together. Better global governance thus has two connotations: first, maximizing the benefits of globalization by mitigating income inequality, and second, doing so also by mitigating national security concerns.

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Japan has been considered a country very slowly changing in its economy and society to keep up with the trends of the global economy. However, its significant changes during the Heisei Era (1989-2019) are noteworthy. Though women in Japan are not yet well established as business or political leaders in society compared to, say, the Scandinavian nations, they started to take some leading positions from men during the Heisei Era. The hierarchical order of Japanese companies does not seem as appealing as before and many young employees today leave their companies after working for a certain number of years, having given up the possibility of promotion to pursue their individual interests. Thus at the beginning of Reiwa Era we can see more independent men and women in Japan. Meanwhile, Japan preserves its social cohesion with its attention to elderly people. Japan's long-term care insurance system is one example. Will an employment system that encourages older people to work longer with the support of such an insurance system help Japan to mitigate the challenges of aging societies in Asia and other parts of the world?

The changes in globalization are also reflected in Japanese foreign policy, which has started to adopt more regionally balanced diplomacy. Prime Minister Shinzo Abe's "Initiative in Africa" is a good example. Some interviews with young Africans on this initiative are available in this review. Last, but not least, the Rugby World Cup 2019 in Japan has left unexpectedly good memories for Japanese at the start of the Reiwa Era. The interview article on this topic suggests how this legacy could be further enriched by the Tokyo Olympics and Paralympics 2020, leading to a new growth strategy in Japan.

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Naoyuki Haraoka is editor-in-chief of *Japan SPOTLIGHT* & executive managing director of the Japan Economic Foundation (JEF).

Roundtable with Dr. Satoshi Inomata, Masashi Kurose, Michitaka Nakatomi & Dr. Shujiro Urata

R

oundtable Discussion on a Rules-Based Global Economy

By Japan SPOTLIGHT

The year 2019 will be remembered as a year of rising protectionism. The US-China tech cold war is at the center of the risks facing the global economy due to restrictions on trade. METI's White Paper on International Economy & Trade 2019 highlights the background and the demerits of protectionism as well as the need to recreate a new rules-based international trading system. This new rules-based system should be discussed with due regard to business interests, as businesses would be the primary actors affected by the rules. Thus, the White Paper is not a theoretical argument but is based on practical ideas and discussions with business people.

In this light, our roundtable discussion on the White Paper consists of leading thinkers in Japan knowledgeable in both theoretical thinking and real business practice. Dr. Satoshi Inomata, chief senior researcher at the Institute of Developing Economies (IDE-JETRO), is a distinguished trade economist who has devoted many years of research to the analysis of global value chains (GVCs). Masashi Kurose, a patent attorney and president of Kurose IP Management, is an expert on IP dispute settlements in Asia. Michitaka Nakatomi, vice chairman and senior executive director of the Japan Machinery Federation (JMF), is a former METI official who has engaged in many trade negotiations and also a distinguished trade policy researcher as consulting fellow of the Research Institute of Economy, Trade and Industry (RIETI). Finally, Dr. Shujiro Urata is professor of Economics at the Graduate School of Asia-Pacific Studies at Waseda University and a well-known economist with expertise in international trade.

The former director of the Policy Planning and Research Office of the Trade Policy Bureau and author of the White Paper, Mineko Ota, leads the discussion with the following introductory remarks. She is currently director of the APEC Office at METI's Trade Policy Bureau.

(Roundtable on July 11, 2019)

Participants



Satoshi Inomata



Masashi Kurose



Michitaka Nakatomi



Shujiro Urata



Mineko Ota

Introduction

Ota: I would like to mention three major points in this White Paper. First, our quantitative analysis shows that in our global economy all nations are closely interdependent through expanded trade and vertical division of labor in the manufacturing industry, so-called GVCs, which is also expanding. Rising trade friction between the United States and China would affect not only the two superpowers

but also Japan and the rest of the world because of this interdependency.

Second, we strongly warned readers that current trade tensions could be the most serious crisis for free trade since the establishment of the WTO. We pointed out rising economic disparity as the background to the crisis, in that expanding inequality has provoked the belief that trade is the main culprit of rising income gaps. We also focused on suspected market-distorting practices by

China such as low interest rate financing or subsidies, as well as international competition in high-tech areas, as the subjects of our analysis. In addition, we have done a number of analyses on how protectionist measures or trade restrictive measures would affect the global economy. Our conclusion is that those trade restrictive measures would affect extremely negatively not only the nations directly involved in trade wars but also third countries and eventually the overall global economy. Based on these analyses, we strongly recommended strengthening WTO functions as quickly as possible to roll back such protectionism.

Our third point is, against such a background, to recommend the Japanese business community enhance its overseas presence not only in the manufacturing industry but also in retail and service industries to avoid too heavily depending upon the manufacturing sector in the international arena or to move towards other growing markets rather than Asia, such as Africa or Latin America, where Japanese businesses are not yet fully active.

JS: Thank you for your introduction. I think a major point is how to respond to protectionism. The first issue is how protectionism is to be interpreted in the context of GVCs. Dr. Inomata, could you please start the discussion?

Current International Relations to Be Revisited in the Context of GVCs

Inomata: GVC studies have shown notable development in the last 10 years or so. They aim to capture the dynamics of global production systems evolving from the time of the Industrial Revolution. In the 19th century, a country exported products which were produced within its national borders using only domestic production factors. However, thanks to the rapid advancement in transportation modes and information and communication technology, production systems have undergone significant changes in recent years. Consider the case of producing a shirt; the production process can now be fragmented into designing by a Milanese designer, patterning by a tailor in London, and final mass-production at a factory in Dhaka, in a way that each task is transferred to the place where it can be performed most efficiently.

In line with the fragmentation of production processes, many developing countries, notably China and Asian Newly Industrializing Economies (NIEs), have achieved remarkable economic growth. This is because GVCs allow individual countries to choose and specialize in particular segments of a production process as appropriate for their own technological levels, and hence enabling them to produce even a high-tech product such as a smartphone at the global scale.

At the same time, it also generated an intense competition over value chains between developed and developing countries. As seen in the US-China trade friction as a symbolic example, there is a growing disharmony of views on how production should be shared across borders. Developed countries fear that their domestic jobs, especially those using unskilled labor, will move out to developing countries in search of a cheap labor force, while developing countries are worried that their economies will be “locked in” to the

low value-added segments of supply chains. As a result, we observe a rise of protectionism in developed countries, on the one hand, and aggressive industrial promotion in developing countries, on the other. I would call this phenomenon the “New North-South Divide” in the age of globalization, which is indeed nothing but a battle for value chain dominance from the GVC perspective.

Urata: The critical question is the speed of such transformations. The drastic change in international division of labor has happened only in these last two or three decades. As Dr. Inomata mentioned, in developed nations the demand for unskilled labor is decreasing, while the demand for skilled labor or experts is increasing and thus the wages of the former will be lowered and the wages of the latter will rise. This results in increasing income gaps. I would also like to point out that some capitalists are earning tremendously high profits in this system. I think it would be better to think about them in referring to increasing income gaps caused by GVCs, in addition to the gap between skilled and unskilled labor.

Inomata: Returns on capital became extremely high. GVC-driven globalization is indeed a process in which capital factors of advanced countries coalesce with unskilled labor factors of developing countries. This has a rather ironic implication for the US government that, in the light of protecting the benefits of US global firms, the anti-China campaign is quite self-contradictory in the line of GVC logic.

Urata: In a situation where the US-China trade war is intensified and China finds it difficult to export its products to the US, will GVCs be reconstructed to exclude China? Or, in the case of goods being produced and sold only in Asia, would there be a regional value chain instead of GVCs to take advantage of the big market in China?

Inomata: I am not sure if supply chains will be continually reconfigured in a way that production bases are shifted among developing economies, from China to other Asian countries, for example. Rather, I am more concerned about reshoring (or near-shoring) of production capacities back to advanced economies, which is made possible by the introduction of new technologies such as automated robotics or additive manufacturing (3D printing).

Nakatomi: The big issue is that international rules and domestic regulations are not keeping up with the rapid progress of innovation. Without the relevant rules and regulations, business will not gain the full benefits of GVCs brought about by new technologies. In the digital economy, we have such issues as privacy and consumer protection, localization of data and IPR protection. We welcome the Osaka Track established by the G20 Summit in Osaka in 2019 where the G20 countries declared they would start a rule-making process for the digital economy. But it is still uncertain where we should resolve this question. If we cannot achieve it and fail to catch up with the reality of such rapidly progressing innovation, there would be a world without disciplines where the more powerful will dominate against the interests of the others.

Inomata: I share that concern. In particular, in relation to the competition over future digital platforms, 5G, between the US and China.

Kurose: There are products that only China can produce and not Vietnam or any other place. I think many Japanese manufacturing companies would have no way but to maintain their production in China or some companies may even invest more in China.

Urata: I think the growth rate of Japanese business investment in China is now lower than before. This is because of rapidly rising wages in China due to a labor shortage as well as US-China trade friction. I think there are many Japanese firms transferring their production bases from China to Vietnam or some other Southeast Asian countries.

Another question is the possibility of lost job opportunities increasing in developing countries as production bases would be returned to developed nations due to labor-saving technological innovation, as Dr. Inomata mentioned.

Inomata: While labor costs are rising in developing countries, Industry 4.0 (the Fourth Industrial Revolution) is under way in advanced countries, making a human labor force less attractive. Accordingly, lead firms in advanced countries will find it increasingly expensive to move their production bases to developing countries. This may bring an additional divide to a group of developing countries, between those which managed to dodge or get out of the middle-income trap by introducing new technologies and those which have failed to do so.

Kurose: That is true. I think developing nations are today increasingly keen on promoting innovation by strengthened patent protection against such a background.

Background to Rising Protectionism – Chinese Market Distorting Policy Measures & Business Customs

Kurose: There is a research report issued by the USTR in March 2018 in accordance with the US Trade Act, Article 301. Among the four points mentioned in the report, there is a claim that the Chinese government is unfairly accessing through hacking US companies' computer networks to obtain confidential data including intellectual properties, technological data, trade secrets, etc. This has led to FDI restrictions but at this moment the restrictions are modified. There is also a claim that the US companies are forced to transfer their technology to Chinese companies if they are doing business in China. This is a matter of business customs and not a matter of regulation, as a few remaining regulatory problems were all eliminated by the Chinese government soon after the publication of the USTR report. So what the USTR pointed out as issues in the report do not exist anymore explicitly, though there could be some issues to be resolved in terms of business customs.

The largest issue for Japanese companies is that Chinese law

enables Chinese companies to improve the technology brought about by overseas companies. "Improvement" is not clearly defined and thus a mere change of design could be interpreted as improvement. One big issue was the Japanese Shinkansen. The Japanese initially thought they could win orders from China by teaching them the technology. But the Chinese improved it and got many patents for the improved technology, since the Japanese technology is basically just know-how that is not patented. They can sell these improved technologies even to the US or other nations.

There were also some regulations enforcing technology transfer, such as enabling a licensee to continue to use the borrowed technology even after the termination of a technology license contract. However, those were eliminated after the publication of the USTR report.

China, at the beginning of economic reform in the 1980s, pursued the import of technologies from overseas and digested and absorbed them. Around 2006 and 2007, they changed direction to recreation and improvement of the borrowed technologies. And thus we see a drastic increase in patent applications.

Another important issue is technical standards. We would have to apply Chinese domestic standards to our products manufactured in China for the big Chinese market. There was a case of a law suit a couple of years ago in which Sony Inc., being required to use a Chinese technology based on Chinese standards for selling their smartphones in China, lost to a Chinese company with a patent for a smartphone telecommunication system based on Chinese standards, and Sony had to pay them a license fee.

Finally, as the US often points out, China is promoting unification of military technology and private business technology as the latter has been well developed. Thus, today, private businesses in China are now working on military technology development. Patent applications for national defense-related technologies which should be received by the National Defense Patent Office are increasing. When the Chinese authorities assume a specific technology is a national defense-related one, it would be categorized as such.

In the case of those technologies, the patent applications are not open and thus for example in the case of 5G or other telecommunication systems, we would eventually find existing patents in China which are not known to us.

Chinese patent applications based upon the Patent Cooperation Treaty (PCT), those to be applied abroad, continue to increase every year. In particular, Huawei has so many patents based on PCT. Huawei could bring law suits in the US by using those patents.

I think what bothers Japanese businesses most today on this issue is that they would not be able to achieve joint research or other joint activities with a Chinese company if the US expels Huawei from global business or starts more serious economic sanctions against China. The case of development of a driverless car would be the one possibly most seriously affected by this. Without joint cooperation with Chinese companies, its development would be significantly retarded. Ultimately, we will need global rules to mitigate these concerns.

Nakatomi: On the question of global rule making, the Agreement on

Trade-Related Aspects of Intellectual Property Rights (TRIPS) is beyond the scope of the Doha Round negotiations. This was a decision strongly supported by the US, but it must have made the wrong decision. If there were loopholes in global rules then, WTO members should have initiated global rule making first, and it should have addressed its claims in accordance with those rules. I understand the US made a big mistake.

Kurose: TRIPS is annually reviewed by the WTO to see that members are observing the law. However, the technologies covered by the review are now rapidly changing and reaching much higher levels than before. Digital technology is one example. In this light, we should elaborate the rules on TRIPS, but many developing countries and recently the US are not ready to do so.

Nakatomi: This is probably because it thought it would be difficult to reach a consensus to further improve the agreement in the WTO. However, no matter how difficult it may be, all nations should do their best to revise the basic global rules on it. At this moment, without such efforts, we see great ambiguities concerning rules and their implementation. I think that is a big problem.

Kurose: The TPP covers the issue of Intellectual Property Rights (IPRs), but TPP11 fails to cover it. The RCEP does not have any binding rules on IPRs. Thus, unfortunately, the rule-making process for the IPRs does not seem to be working well.

Nakatomi: I was in charge of negotiations on the Anti-Counterfeiting Trade Agreement (ACTA) on behalf of the Japanese government. This was successfully concluded at the Quadrilateral Trade Ministers Meeting in October 2010 in Tokyo but due to opposition by European NGOs it could not be implemented. I share the view that the major nations should work together for global rule making to avoid a power game.

Urata: In China, is the issue of intellectual property rights now considered critical among Chinese companies? If so, we can be more optimistic in regarding China as rule abiding on intellectual property rights.

Kurose: Japanese businesses now believe that Chinese regulations on intellectual property rights protection are much improved and the US Bar Association also has the same evaluation. They are adapting well to rapid technological progress.

Inomata: Prof. Richard Baldwin, a distinguished trade economist, advocates for regulatory convergence and the establishment of common norms for 21st century global governance. Can China conform its own domestic rules to them?

Kurose: We do not have common rules now. China complements the incomplete WTO/TRIPS rules by its own domestic laws for digital technology.



Inomata: Without common global norms, there is a danger that two economic superpowers may pursue the entrenchment of their own specific rules, which would lead to system bifurcation and polarization.

Kurose: On the issue of patents, harmonization of rules is critical. Between China and Japan, their patent specialists have been closely working together to have common judging criteria for patent protection. Thus what is acknowledged as a patent in Japan will not be rejected by the Chinese.

Inomata: The number of China's patent applications is remarkable. However, in view of the "quality" of the patent applied for, can we still say that China has significantly accumulated technological capacity over time?

Kurose: It is certainly true that though they have so many patent application cases, there are many for applied technologies rather than basic ones. But against the background of an overwhelmingly large number of patent applications, the Chinese could win many law suits.

Nakatomi: Regulatory convergence is also an important issue. The WTO and Regional Trade Agreements (RTAs) cannot meet the needs of new rules reflecting the rapidly progressing technological innovation at this moment. In this situation, unless regulatory convergence is promoted sector by sector, business itself could be critically affected. We will need to utilize all the policy tools available and work together for a solution of this issue. On the issue of technology, I think we should eventually integrate the results of all those efforts into the WTO framework in the future.

Inomata: On regulatory convergence, strong leadership by advanced countries is the key for making common rules. For example, advanced countries may request developing countries to engage in domestic reforms in exchange for capital transfer (foreign direct investments (FDI)). Prof. Baldwin once described it as "my-factories-for-your-own-reform" strategy.

Now, such a strategy is effective only if there is a huge difference

in bargaining power, largely based on the amount of disposable capital, between developed and developing countries. In the near future, however, newly emerging superpowers such as China or India are likely to find the deal less attractive since these countries may have built up sufficient production capacities by then, so that they can afford *not* to give in to such a bargain. The terms of trade for advanced countries will rapidly deteriorate as time goes by. So how quickly we can realize common rules is an issue of particular importance.

Nakatomi: It is certainly true that regulatory convergence could be increasingly difficult to achieve today. But, first of all, it is indispensable to achieve collaboration among developed nations on this. At the same time, it will also be important for us to convince developing nations of the merits of regulatory convergence in promoting their own economy with the introduction of new technologies. Otherwise all of us would be losers. This must be understood by all.

Urata: I agree with you, but we should not forget that large market nations like India and China might have the illusion that their markets are sufficiently large to attract FDI even without regulatory convergence. These countries should realize that regulatory convergence would not only attract more FDI but also facilitate their companies to expand their business abroad.

Nakatomi: The WTO has failed to achieve a global consensus on making rules on such important issues as trade and investment, or trade and environment, both of which were initially adopted as part of the agenda of the Doha Round.

Consequences of Rising Protectionism Provoked by US

Nakatomi: Protectionism is contradictory to GVCs and nullifies the merits of international trade. It also damages the stability of international trade rules and the predictability of business. Protectionism can be simply defined as a violation of the international rules embodied in the WTO. Looking back at the history of the development of international trade rules, we can find the backgrounds and reasons for today's rising protectionism.

In 1995, with the establishment of the WTO, the prohibition of unilateral measures and an enforced dispute settlement mechanism were introduced. The adoption of panel reports by negative consensus (meaning a report will be adopted unless all member nations unanimously oppose it), and clarification of retaliation procedures against violations of WTO rules were also introduced and all member nations must generally observe the same rules, except for "special and differential treatment" for developing nations. Rule making in the WTO peaked around 1997, as shown in the achieved agreements on information technology (ITA) in 1996 and telecommunication and financial services in 1997. Since then, the only multilateral agreement was an agreement on trade facilitation in 2017.

Consensus in principle, an enforced dispute settlement mechanism, single undertaking (meaning all member nations in principle are obliged to follow the same rules), and definition of a developing country by its own announcement – these WTO principles have made it extremely difficult to carry out rule making in the WTO. The possibility of a free ride for developing nations, Special and Differential treatment for developing nations, and institutionalized retaliation against violations of WTO rules have all made it difficult for the WTO to do decision making and rule making.

Since around 2000, regional trade agreements (RTAs) have become the main tools for trade liberalization and rule making. In recent years, mega-FTAs such as TPP11 and the Japan-EU FTA, have contributed to rule making and trade liberalization. WTO rules have been basically on border measures and have not been able to keep up with the changing reality of international trade and business after 1993 when the Uruguay Round reached a consensus in substance.

For example, revisions of the General Agreement on Trade in Services (GATS) or TRIPS rules or in-depth exploratory studies of those agreements in the light of reality have not made good progress and new rules could not be adopted on important new issues such as trade and investment, trade and environment and e-commerce. The issue of IPRs that the US considers critical in US-China trade friction was even beyond the scope of Doha Round negotiations that started in 2001. Such an unfortunate historical background has generated significant energy for an explosion of protectionist measures today.

It is extremely difficult to try to respond to today's complex trade issues only with the interpretation of the principles adopted by the WTO in 1995. It is true that judicial processes cannot work without appropriately functioning legislative processes. Thus, it was foreseen in advance that the WTO dispute settlement mechanism would be paralyzed, assuming that the details of the rules were not clarified and developed.

Therefore, I believe that restoring and strengthening the function of international trade rule making is indispensable to mitigate rising protectionism. The best venue for this must be the WTO and if it is not possible, we should try to do it in plurilateral agreements or RTAs. Of course, we must commit to preventing proliferation of protectionist measures and avoid using the paralysis of the WTO's rule making functions as an excuse. In this regard, the G20's message of doing its best to realize a "free, fair, non-discriminatory, transparent, predictable and stable trade and investment environment" and keeping markets open is crucial, though not enough. In particular, proliferation of protectionist measures, using national security as a blanket exclusion clause, will be critically dangerous to the global trading system.

For Japanese industries that have achieved progress based on free trade and GVCs, proliferation of protectionist measures will have a serious impact. Decoupling of supply chains and rules of international trade would create a difficulty in responding to the crisis. Decoupling of supply chains would be a disaster for all nations' industries. I think the White Paper's analysis of the impacts of protectionist measures is very significant.

Urata: I would like to point out that protectionist measures are increasing not only in the US but also elsewhere. For example, at the global level, anti-dumping measures considered to be Non-Tariff Barriers (NTBs) are increasing. The reason for this increase at the global level is that more and more people are suffering from the demerits of globalization, such as those working in the Rust Belt in the US who have been robbed of job opportunities by globalization. There is research done by a group of distinguished economists proving several million jobs have been lost in the US due to imports from China. This finding has been used to justify protectionist measures. However, the researchers recommended raising mobility in the US labor market rather than protectionist measures so that the damage to labor due to the imports would be mitigated. Trade Adjustment Assistance, expected to encourage such labor mobility, should be effectively employed.

I believe, the demerits of globalization may as well be resolved not by protectionism but by a more flexible labor market or better functioning of market mechanisms. However, there are of course political issues behind protectionism, as advocates could win political support from those workers exposed to immediate threats from imports.

On the issue of the impact of a trade war on the global economy, increased uncertainty will definitely discourage trade and investment, slowing down economic growth. A number of quantitative analyses using a general equilibrium model show a negative impact on the nations waging a trade war, in this case the US and China, but a positive impact on the rest of the world due to trade diversion effects. For example, with the decline of Chinese exports to the US, Japan could enhance its export opportunities to the US, partly replacing that decline.

On the other hand, a macroeconomic analysis like the IMF's World Economic Outlook shows that global GDP growth will slow down due to further intensification of the US-China trade war. This would negatively affect Japanese business as well. I think while the general equilibrium model is only static and does not take account of uncertainties due to the trade war, the macro approach shows an important aspect of the conflict, namely a negative impact overall upon the global economy.

In order to cope with protectionism, first of all, I think Japan should clearly explain to the US and China that all nations would be damaged by a trade war. Second, assuming that US protectionist measures would be adopted against unfair Chinese trade practices, the US should work with Japan and European nations together to correct Chinese practices and not alone. That would, I guess, lead to a WTO rule-making process. Japan should convince the US of the utility of this approach and should advise China to observe international rules and understand well that observing them would have an extremely favorable outcome in the long run.

Lastly, I would like to stress the importance of maintaining and expanding a rules-based trade and investment environment to achieve global economic growth. Specifically, for Japan it is necessary to expand membership of TPP11 founded under Japanese leadership. It is also important to conclude other Asian-based mega-regional FTAs such as the RCEP or the China-Japan-South Korea FTA

as promptly as possible.

Inomata: The research paper that Dr. Urata mentioned demonstrates only a negative impact of China's exports on US employment. Apparently, there is also a positive impact from supplying low-cost intermediate inputs to US firms, which raises their productivity. The aforementioned research does not shed light on this point.

Urata: Yes, I agree with Dr. Inomata. Another factor that is often missed in the analysis is positive impacts on US exports to China. Though US imports from China are five times as large as US exports to China, the growing Chinese market could be part of the reason for growth in US jobs and production. Thus it would be misleading if we analyze only the impact of Chinese exports to the US. On the economic impact of Chinese exports, I am now conducting research on the impact of Chinese exports to Japan on the Japanese economy. My preliminary research reveals that the damage is seen as a decline of jobs in Japanese small and medium-sized enterprises (SMEs).

How to Revitalize Multilateral Trading System & What Would Be Japan's Role?

Urata: In the WTO, rule-making negotiations have not been working at all and the existing rules are outdated, and the dispute settlement mechanism is not working well due to the outdated rules. But no country has ever started an action towards WTO reform, even though all nations mention the importance of WTO reform.

Its unanimous consensus-based decision making has made it impossible for the WTO to initiate any flexible action for fixing trade frictions. To make a breakthrough on this, as Mr. Nakatomi mentioned, there are two alternatives: one is plurilateral agreements on rules on specific issues to be decided by a voluntary group of nations, and the other is RTAs and FTAs, in which fewer nations than in the case of plurilateral agreements get together and create a framework of comprehensive agreements such as the CPTPP. It is important to expand the membership of such RTAs or FTAs. With these two categories of agreements expanded, we would eventually upgrade and modernize the WTO. To carry out such an approach, the four important players – the US, China, Japan, and the EU – have to come to an agreement.

Nakatomi: I think the WTO's comprehensive regime for supporting free trade and its dispute settlement mechanism are unique and cannot be replaced. Nobody could stop rapid technological developments and resulting changes in international trade. The world without the WTO would be a world without rules and only the winner of the power game could dominate, and thus a variety of disharmonies and inconsistencies would proliferate. Until the WTO is back in the driver's seat, it is necessary for the time being to promote simultaneously plurilateral agreements, RTAs, regulatory cooperation, and strengthened alliances with other international organizations. It would, however, be critical to secure the WTO as the basic venue of multilateral trading systems. In this regard, it is

important for the G20 to perceive the need for WTO reform. It will be indispensable for the reform to tackle its decision-making mechanism to restore its legislative function.

As to what can be done immediately, I think strengthening notification procedures and securing transparency including stronger penalties for violations, utilization of regular committees and confirming implementation of existing rules and strengthening them, including in particular the rules on subsidies covering State-Owned Enterprises (SOEs), is important.

As for the role of Japan, it is important to lead WTO reform on restoring legislative functions and securing judicial functions, including solutions to the issue of the Appellate Body which has played a key role in dispute settlements at the WTO. Japan should also work to promote plurilateral initiatives and RTAs to maintain free trade and GVCs. Possible plurilateral initiatives can include those on digital trade and rules on subsidies. As for RTAs, expansion of membership of TPP11 and conclusion of the RCEP should be accelerated by Japanese initiatives.

The WTO is a lighthouse leading global trade. We must not turn off the light. I believe the role of Japan is significant in the midst of the trade war between the two superpowers.

Kurose: In the domain of technology, international standardization is the most crucial issue. For example, without having global standards for chargers, electric cars cannot be exported. In the case of driverless cars, we would have to decide on a global standard on telecommunications. There is what we call standard-essential patent claiming, meaning that an invention must fulfil some specific technical standards. In some cases we must use it. We would need to set up license rules as well. We will not be able to wait for a WTO decision under rapid technological progress. Developed nations have already started discussions on these matters. Thus, I think rule-making efforts are making good progress in the domain of technology.

Urata: In order to encourage the US to return to free trade, the integration of the CPTPP and the EU-Japan FTA could be a good idea for Japan to promote. Another point is to restore the WTO's credibility, and the WTO's secretariat functions such as research need to be expanded.

Final Comments on Global Economy & Free Trade

Inomata: I pay close attention to the issue of how new technologies will impact globalization. As I mentioned earlier, some sorts of technological innovation are causing a shift of production capacities back to advanced countries away from developing countries, giving a poorer prospect for economic development of the latter. The technological progress in this direction may dampen the globalization momentum.

On the other hand, the digitalization of production processes, such as e-commerce, FinTech, or “virtual presence”, can offer huge opportunities to firms/individuals in developing countries for joining

GVCs through advanced communication networks. This gives a further leverage to GVC expansion. Whether or not GVCs will continue to develop depends on the net impact of these opposing forces. The issue of inequality, domestic or international, is then up to how technologies work for GVCs.

Kurose: About China, it is such a vast country and there are huge gaps in development among the regions. In terms of intellectual property, Shenzhen, the most advanced place, has 47% of international PCT patent applications in China, while there are some underdeveloped regions with no PCT patent applications at all. Inequality of wealth has been rapidly increasing among the regions. The Chinese government has carefully addressed the existence of regional disparities in the country. At the same time, in order to strengthen international competitiveness, the government is promoting policies to promote further development of advanced regions. Most Chinese seem to support the current policies of the administration.

Nakatomi: We can stop neither globalization nor innovation. But we must be aware, for example, that digital technology can introduce such problems as privacy and consumer protection, competition issues and digital divide, while it can bring enormous benefits to all users and countries. We will need to find solutions to these consistent with globalization. Development of GVCs means that no single country will find solutions on its own, so we will need to continue our best efforts for international rule making without falling into protectionism. Japan has a responsibility to pursue this and that would protect Japanese industries' interests.

Urata: We would have to think about mitigating the income gap and how all people could benefit from economic growth and globalization. One way to achieve it is redistribution of income and assets. However, redistribution policy could hamper economic vitality and dynamism. A better policy would be to support disadvantaged people or groups, in order for them to be able to benefit from globalization and economic growth. For example, SMEs may be given technical assistance so that they can effectively use IT to be engaged in GVCs, while women could be given appropriate job opportunities to maximize the use of their talent and skills.

Kurose: I would like to add one more thing. In the domain of IPRs, it is highly critical to create new international rules. It will be necessary to elaborate TRIPS. I sincerely hope that international rule-making efforts to meet the present levels of technology will be promoted without fail. Otherwise, we will see disastrous confusion.

JS: We must ask Ms. Ota, who is now in charge of METI's APEC Office, to help activate the international rule-making process to achieve what her White Paper envisaged.

JS

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Interview with Dr. Dennis J. Snower, President of the Global Solutions Initiative, Senior Professor of Economics at the Hertie School of Governance, Berlin; Senior Research Fellow at the Blavatnik School of Governance, Oxford University; and Non-Resident Fellow, Brookings Institution & former President of the Kiel Institute for the World Economy

Restoring Social Cohesion – a Crucial Issue for the G20 in 2019

By Japan SPOTLIGHT

Lonely elderly people in an aging society, the unemployed in the new Fourth Industrial Revolution, those who feel left behind by globalization: all are symptomatic of growing social discontent and a lack of social cohesion. This lack of cohesion seems to be hindering political and economic stability even among developed nations. The G20 will address this issue at its 2019 summit in light of its growing impact on world peace and prosperity.

Japan SPOTLIGHT interviewed Dr. Dennis J. Snower, a distinguished labor economist who is president of the Global Solutions Initiative in Germany, a global collaborative enterprise to propose policy responses to major global problems, addressed by the G20, the G7 and other global governance fora. (Interviewed on Feb. 8, 2019)

Introduction

JS: Could you briefly introduce your academic specialty, labor economics, and also the Kiel Institute's mission and main activities.

Snower: I am a specialist in labor economics and give advice to governments on labor market policy, as well as on reforming welfare systems and how to get more incentives into the equitable distribution of opportunities. The basic idea is that we should move away from the redistribution of income, and instead redistribute economic incentives, enabling people to become employed and skilled. So, you take the most disadvantaged people and you give them employment subsidies and training subsidies, and the longer the duration of unemployment and the more disadvantaged they are, the higher these subsidies become. This has worked well in a good number of countries, as an underlying idea.

With Assar Lindbeck – who was then the chairman of the Nobel Prize Committee in Economics – I developed the insider-outsider theory of unemployment, which shows under what circumstances insiders whose jobs are protected in the labor market can benefit themselves, but not the outsiders who are outside this job protection, and how this can explain the persistence of



Dr. Dennis J. Snower

unemployment. In all of this, I have been fortunate that my economic and theoretical interests basically overlap with my policy advice interests. I have advised national governments (German, French, Spanish) but also at an international level including the OECD, the World Bank and others.

The Kiel Institute is one of the very few institutes in the world that examines the global economy from a global perspective as opposed to a national or regional one. From the perspective of the global public interest, how should global trade and global capital flows, global technological diffusion, be designed? The Kiel Institute has models that look at how the world's environmental systems are connected to the world's economic systems in order to see how the

economy influences climate and other aspects of our environment. We looked at the effects of offshoring and outsourcing worldwide, how value chains affect employment opportunities and how they change because of digitalization. The institute also has a forecasting department not only for Germany and Europe but for the world as a whole. Being president of the Kiel Institute gave me the opportunity to look at the inter-linkages between many different domains that are kept apart both in academia and politics. Climate, labor policies, social policies, demographic change – these are usually investigated separately but at Kiel we looked at how they interact, especially the inter-country linkages.

Role of Think-tanks in the G20

JS: Think-tank involvement in the G20 is a recent development. How do you assess this involvement?

Snower: As you said, this is relatively recent. Under the German G20 presidency, we restructured the process around task forces which produced policy briefs addressing the main issues of the G20 agenda. That proved to be very valuable to the German government, both in terms of the recommendations that we generated but also in terms of our overall narrative. We put all the recommendations under the umbrella of what we called the “recoupling narrative”, which basically means that social progress in terms of people’s well-being can become decoupled from economic progress. These sources of discontent are not necessarily closely related to the rate of economic growth, and therefore we recommended that the G20 should focus entirely on trying to recouple economic prosperity with social prosperity.

That, in fact, was very useful to the German government in the negotiations leading up to the G20 Summit in Hamburg in 2017. At that time, there were emerging protectionist activities, and President Donald Trump decided to leave the Paris Agreement on climate change, so it looked like the summit was in grave danger. The protectionists said that they are the only ones who represent the disadvantaged in the world, and as a result of our narrative the German government could say, “No, we are very concerned about the disadvantaged and we have a lot of proposals here about how to help them and protectionism is not effective in this regard.”

That helped change the discussion, and therefore we understand both the recommendations and an overarching narrative. Since the German presidency, Argentina has followed this structure of task forces and policy briefs related to the priority, and now of course in Japan there is another big step forward – the organization of the G20 process in Japan is extremely impressive. Many institutes are all cooperating with one another as well as with think-tanks abroad in generating proposals that are very closely related to the Japanese G20 priorities. Quality infrastructure, aging society, SME finance – these are all being pushed ahead under the Japanese presidency. Although the summit will occur relatively early in the year compared to other summits, the fact that the G20 has started its work in Japan so early meant that this has not been a problem.

JS: Would you agree that social cohesion is an inter-disciplinary issue, and as such is relevant to be handled by think-tanks?

Snower: The big challenge of our age is that we have witnessed the

integration of the global economy, and value chains have become truly global. However, we have not witnessed a similar integration of global society or global politics. Because societies and their politicians remain fragmented, this creates tensions between our economic interests and our social and political ones. Therefore, it is not sufficient to look just at the economic interests because that ignores something important in terms of social concerns and social cohesion. The reason why we have so many protests at G20 summits is that the people on the ground understand that social cohesion is often overlooked and that the G20 is depicted as a meeting of heads of state and technocrats to impose economic solutions on people whose societies are fragmented. By looking at social fragmentation directly in connection with economic activity, we can address the issue and make a real contribution to the G20 process.

Social Inclusion an Important Policy Goal

JS: You co-authored a book called *Caring Economics*. Could you elaborate on this and the concept of social inclusion?

Snower: Economists tend to assume that people are purely self-interested, concerned only with their own consumption. Therefore, economic policy provides incentives of a monetary nature and that induce people to follow their self-interest to take care of externalities and other public concerns. However, this misses something important in human nature, which is the need for people both to care for another compassionately and to affiliate or bond with one another in order to have a sense of belonging. When those needs are not met, people become psychologically unbalanced and they become unhappy. Taking those needs explicitly into account in our economic models helps us work out how to create social contexts that generate more of this cooperative activity. For example, we can choose at the workplace whether we promote competition among individuals or whether we have collaboration in teams. The same thing holds in our school system and is very important in the health system. Therefore, having a new approach to what motivates individuals can have very far-reaching consequences in terms of what we do for economic policy.

JS: This is particularly pertinent for an aging society.

Snower: Absolutely. The big challenge in aging societies is the challenge of loneliness. Older people are left after their families have moved away to work, or a spouse may have died, so they are left feeling very lonely. How to address this issue, particularly in aging

societies, becomes extremely important. Digitalization can help, and Japan is a world leader in how to connect older people to health systems, social services and so on through digital pathways. However, digital technologies are not able to provide a sense of care and belonging. For that, you need other human beings. Human interactions to overcome loneliness require lots of time in terms of interpersonal interactions. The technological progress of human interactions does not proceed as rapidly as other areas; for example, computers these days are millions of times more productive than 40 years ago, and we can do millions as many computations per second, but we are not in a position where we can spend one millionth of our time with our children and our parents and still have the same quality of relationship. We are moving toward a society where interpersonal interaction among different age groups and in the caring profession will become increasingly important, supplemented by the new digital technologies.

JS: To maintain inclusiveness of welfare, some kind of policy measures would be necessary to avoid a digital divide in that context.

Snower: That is absolutely right. There are two things that elderly people need: one is, they need more training than they have to become socially skilled. To be able to interact well with other people requires empathy; it requires perspective-taking, mind-reading, compassion. These things can be taught. Schools and universities tend to train people in reading and writing and analytical skills – cognitive aspects – but not so much in social skills. In the world of the future, social skills will need to be taught much more.

We also need to teach digital skills that will enable us to use digital technologies to promote these social interactions. Digital skills are going to become ever easier to acquire as time goes on because computers are going to become much easier to handle. When I started interacting with computers, you had to know various computer languages, whereas nowadays you can talk to your computer and it will answer. Look at how easy it has become to drive cars – 100 years ago you had to be a specialist to drive and it was seen as the prerogative of the few. Now, virtually everybody can do it. Computers will become like this too. The challenge that we have is to make lifelong learning and digital skills a fact of life throughout the whole of society while understanding full well that the digital needs of old people will differ from those of young people. So, this lifelong learning must give them the digital skills that they need – not for its own sake, but primarily to help them interact better through these digital technologies with other people. This will be a big source of social cohesion.

JS: We are living in a globalized world, and so we need to maximize the merits of globalization. At the same time, we should minimize its demerits relating to social discontent. There is the idea of structural economic reform as a way to smoothen the globalization process. One aspect involves promoting efficiency through, for example, competition policy. Another is achieving equal opportunity for economic incentives. How can we achieve consistency or relevancy between these two aspects?

Snower: Promoting efficiency can be done by internalizing the externalities of economic activity, promoting competition policy, and providing a better flow of information to avoid asymmetry of information and market power resulting from that. Equality of opportunity arises largely through redistribution of economic incentives.

Looking at what different countries spend on training their workforce and lifelong learning, it is very revealing because in the United States the percentage of expenditures per capita on this is far lower than in Denmark or Germany or Japan, and this helps explain a lot of the social discontent that you have there. However, that does not cover all the main issues underlying the problem of social cohesion; in addition to these economic opportunities, people have two broad needs. One is the need for empowerment – that one can influence one's own future and destiny through one's own efforts, that I can affect my fate by working hard or doing something through my own effort. That gives one a sense of empowerment. Empowerment is an extremely important means for human beings, and not always directly related to economic growth.

It is true that if people have equal opportunity then they become equally empowered, but empowerment is broader than that. Globalization has reduced people's subjective empowerment because global value chains are always adjusting, people adjust, and firms adjust where they want to locate their activities depending on where it is most profitable, so the people at the local level feel at the mercy of big international forces over which they have no control. Multinational companies used to have great regard for the locality in which they operate, but that has become less pronounced as time has gone on. Japan is an exception to this rule, but even in Japan globalization has affected the way companies operate with regards to their local workforce and local society. Globalization has clearly promoted great wealth, especially in emerging economies, but also has led to a sense of disempowerment in many places, which is negative. The way to address this problem is to move away from the old concept of the welfare state to a concept of the empowering

state, whereby governments give people skills that will help them to make a difference to their own lives. Let's take one example in aging societies: if you give old people who live in geriatric homes the opportunity to say when they want to eat, and give them a choice of menu, they will live longer, be healthier, and have a better immune system, because they feel empowered. There are many ways in which we can empower people.

There is also a deep need that people have for social belonging and interaction. This means that governments should also have regard for how to strengthen local communities. People tend to live in small groups and these small groups should be strengthened, and globalization has also affected this because people feel that their communities are often at the mercy of big global forces. Minimizing the disadvantages of globalization involves not only more efficiency and equal opportunity but also overcoming the problems of empowerment and social estrangement that globalization causes.

Consequences of Immigration & Innovation

JS: Continuing with social cohesion, I think there are two challenges facing society now: one is immigration in a globalized era, and the other is innovation in the Fourth Industrial Revolution. Both could affect labor markets. Could empowerment work well to overcome these two challenges?

Snower: For immigration, the issue that economists have looked at is how much more GDP per capita can immigrants provide? And if they provide significant positive returns in that regard, then immigration is considered good. Despite this, immigrants come from different countries and have different backgrounds, and this affects the society in which we live and our social context. These effects are often overlooked by economists and policymakers. The issue is not only the economic integration of immigrants, but also what sort of social integration is required so that people who live in the receiving country don't feel endangered. That means countries need to be clear about what they require of immigrants and also need to be clear in terms of how large the flow of immigrants is that they are able to absorb.

Japan has been a relatively closed society but is now considering more immigration. Nowadays, I think that the issue of social integration should be considered much more carefully. In a number of countries, society is considered like a marketplace. If you trade with one another and you gain from trade then everything is fine. But society is not a marketplace, it is a place where people interact with each other, and these interactions come with a lot of social prerequisites: respect, care for one another, and deep cultural

learning. This social integration part of the argument should not be neglected.

Regarding innovation, there is another set of issues, more related to empowerment. If innovation proceeds sufficiently rapidly, there is a big danger that people will become disempowered for the simple reason that human skills – if everything goes well – grow at a rate of maybe 1.5% to 2% per annum. The skills of machines grow at the rate of Moore's law, i.e. double every two years. Even if machine learning slows down a bit, machines will still be growing at a rate far faster than what humans can keep up with. Policymakers will have to try to predict when the crossover point comes where machines take over the routine jobs from human beings – because once the crossover has taken place and machines take over those routine jobs, there is basically no way humans can get those jobs back because their productivity will never grow fast enough. So, they will have to look at different skills that are complementary to the machine skills, and those skills will largely be creative skills and social skills.

Income Equality or Economic Growth Insufficient

JS: You mentioned that economic growth should not necessarily be the primary goal considering the increasing importance of social issues. However, economic growth is still one of the most effective ways to achieve social cohesion. As people become wealthier, social discontent would go down and we would see more social contentment.

Snower: Basically, there are no hard and fast rules on this issue. If one lives in a society with a lot of social cohesion already and people broadly feel empowered by their work, then simply promoting economic growth is a very good thing because it will give them more purchasing power, enable them to live healthier lives, and give them the opportunity to partake of cultural goods. So in many respects, people will be much better off. The problem arises when social cohesion in a society is not very strong and people feel disempowered. Take the American Rust Belt for example. Families are broken, and people are laid off long-term. If you simply promote economic growth, you may not solve these problems and we've seen this in the US where people are left behind, and even if they are at work and receiving salaries, they are still suffering from the lack of social cohesion and disempowerment. Social prosperity must be closely coupled with economic prosperity. If society is functioning well, then focus on economics. But if society is not functioning well, then you need to look elsewhere in addition to economics.

JS: In Japan, the issue of the Rust Belt in the US is sometimes interpreted as a question of income inequality. Is it the case that expanded income inequality would always bring social dis-cohesion?

Snower: The greater the income inequality, the more likely it is that you will have social disintegration, for all the obvious reasons. But that is not the whole story. The opioid epidemic has not arisen because people have too little money – in fact, they have too much money with which they buy drugs; they are destroying themselves with the money that they have. Self-harm is a good example of where social prosperity becomes decoupled from economic prosperity. Therefore, inequality is very useful to look at in societies that function well. But when they don't function well, economic inequality is not everything. You need to be embedded in a social structure that has sufficient stability for you to feel confident that you will be supported by family and friends.

Implications of Discussions on Social Cohesion in G20

JS: Turning to global governance, when these social issues are discussed at international fora such as the G7, what would be the merits of such discussions? Anti-globalization sentiment is growing and perhaps the G20 could be considered as one of the flag bearers of globalization.

Snower: I think these international discussions are absolutely crucial for the future of our world, not only with regard to social cohesion. Through the process of globalization, we have produced lots of global problems, including climate change, financial crises, and immigration pressures. These can only be solved on a global level, and similarly for financial markets. Our challenge nowadays is to make sure that people living in many different countries understand that if they wish to be truly patriotic to their country, if they wish to be a good citizen in their locality, then one of their jobs is to support the multilateral process in order to solve global problems. If the problems of climate change and financial crises are not addressed, then every country will be damaged. Therefore one should not see nationalism and multilateralism as conflicting objectives, they should be seen as complementary ones, and that will be the big job of the G20 to promote that idea.

JS: So, could these international discussions be useful in mitigating populism, which seems to be fueling protectionism?

Snower: What the G20 needs to do, in my opinion, is to acquire a human sense. The G20 needs to communicate that it is doing these things so that people in countries around the world can lead more fulfilling lives. What the G20 does should be interpreted in terms of the needs of people on the ground. That's what we encourage at the Global Solutions Initiative. By doing that, it will create a lot more understanding of multilateral processes and bring a different tone to how it communicates with the general public. There is a big understanding in the G20 under the Japanese presidency on this issue and I very much look forward to seeing how it plays out.

Japan as a Model for “Caring Economics”

JS: What is your outlook for the Japanese economy? Japan used to be quite well known for practicing the “caring economics” that you referred to.

Snower: Japan is an extraordinary country, where despite its economic success it has not lost sight of the importance of social interaction. The deep sense of customs and interaction that accompany Japanese life help promote these social bonds. This cannot be exported as it is to other countries with different cultures and different associations; but the idea of promoting social well-being consciously – not only just between people but also in terms of government policy – is an important issue that other countries can learn from.

At the same time, Japan is also in a leading role for aging societies and how to handle the problem of people who become disconnected from families and their localities. Connecting those older people with younger people in ongoing relationships will be hard, as the pressures of work will pull them elsewhere. Machines will take over more and more routine work, and if people do a lot of work that is routine, that will require some very significant changes in the way that we deal with economic challenges. It will also be an issue for social cohesion because most people's work involves a lot of routine elements, and if these routine elements start getting taken over by machines, what will this do to social cohesion? This is a problem that should be high on every government's agenda.

JS

Written with the cooperation of Joel Challender, who is a translator, interpreter, researcher and writer specializing in Japanese disaster preparedness.

The G20 & Global Governance

By Sachin Chaturvedi & Priyadarshi Dash



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Introduction

A diverse set of “movers and shakers” have explained the contours of global governance over the past decade. Some important developments that need mentioning in this parlance include the collapse of the WTO Doha Round of trade negotiations, the origination of the financial crisis of 2008-2009 in the United States (the most sophisticated financial system in the world), the unhealthy trade war between the US and China, the so-called proponents of free trade, protectionist and isolationist policies in the US, migration from conflict-ridden Arab countries and Africa, and human rights violations across countries. These unusual events happening across countries regardless of their level of development tempts the intelligentsia and ordinary citizens to question the relevance, adequacy and legitimacy of the existing superstructure of global governance. Moreover, the slow response to standard bailout and crisis financing packages by the IMF in the wake of the financial crisis in 2008-2009 and the prolonged and uncertain recovery have exposed inherent deficiencies in the current systems of global governance.

The post-crisis evolution of narratives on the role of multilateral institutions and country configurations or reconfigurations has been kaleidoscopic and introspective. While pressure on the institutions of global governance such as the United Nations, IMF, WTO, World Bank and regional development banks to undertake necessary reforms in their functioning, particularly on the issue of fair representation of emerging markets and developing countries, continues to mount, there is a greater recognition of the existence of a vacuum in international economic governance. Can the G20 fill this vacuum? In other words, can the G20 demystify and blur the conventional country configurations into stereotype categories of developed and developing, and nurture mutually-reinforcing engagement among countries?

Despite not having the legal status of an international organization, the G20 has gained substantial influence as a global platform in recent years, perhaps by leveraging the benefit of the doubt. This benefit of the doubt accrues from declining faith in the existing multilateral processes of promoting trade, investment and development cooperation. In the 1980s, the G7 lost its importance as a platform for international economic policy coordination and this skepticism lasted till the outbreak of the East Asian Financial Crisis in 1997. The severity of this emerging markets crisis in terms of contagious spread and magnitude of output and employment loss created the space for the

G20 to emerge (“G20 and Global Governance” by Stephen Kirchner, *Cato Journal*, 2016, Vol. 36, No. 3). Subsequently, the first meeting of the G20 finance ministers and central banks was held in Berlin in December 1999. Regardless of the efficacy of other country groupings, the expectations from the G20 appear to be high as the grouping has graduated from playing a stabilizing role (in the context of post-crisis inter-country coordination) to promoting development. This has been manifested in the widening and broadening of the G20 Summit agenda from its focus on restoring financial stability and ensuring global macroeconomic coordination in the first three G20 summits during 2008-2010 to a wide range of development issues like global value chains, food security, skill development, women empowerment, Africa compact, and so on. Being a club of developed as well as emerging markets, the G20 envisages a world that cherishes high and inclusive economic growth, protects the interests of the poor and marginalized, prevents financial crises, and ensures upward social mobility (poverty alleviation, food security, women empowerment, etc).

Basically, the business of the G20 over the years has evolved in two tracks – a finance track and a development track. Even though the leaders’ summits have not exclusively referred to these two tracks for practical purposes, they define the sequence of activities in the G20 platform. As this year’s G20 host, Japan has cautiously identified the core areas of these tracks. In development sectors, universal health coverage, aging, and quality infrastructure assume importance, while the finance track will probably continue to implement regulatory reforms in financial markets and envision new and innovative means of fund mobilization for development projects.

Finance Track

As the name suggests, the finance track largely covers the areas of global financial stability, fiscal and monetary policy coordination, exchange rate coordination, financial systems development, and development finance issues. The success of G20 initiatives in restoring financial stability to the global economy is laudable. However, a lot depends on the measures and commitments beyond crisis prevention and resolution. The vitality of the finance track can only be regarded as successful if finance contributes to inclusive and sustainable development in emerging and developing economies.

Functioning of Global Financial Systems

The G20 assumed prominence during the global financial crisis of 2008-2009 when it facilitated joint efforts by the advanced economies and emerging markets to restore financial stability and ensure a coordinated macroeconomic response, and resist resorting to beggar-thy-neighbor policies. The smooth and coordinated implementation of fiscal stimulus packages and adherence to monetary policy and exchange rate disciplines helped contain the crisis-related disruptions in the affected economies. These issues dominated the commitments of the G20 at the first three summits. While short-term crisis prevention and mitigation continued to occupy substantial attention in subsequent summits, the finance track of the G20 has widened significantly in terms of issues covered and the scope of commitments. A good number of commitments refer to long-term structural reforms, especially reform of international financial institutions, the expanded mandate of the Financial Stability Board (FSB), mobilizing private capital for infrastructure financing, promoting institutional and long-term finance for development, measures to address debt sustainability, and tax and accounting reforms.

In October 2018, the G20 Eminent Persons Group (EPG) submitted a report on the global financial system. The EPG was tasked with a mandate “to recommend reforms to the global financial architecture and governance of the system of International Financial Institutions (IFIs), so as to promote economic stability and sustainable growth in a new global era; and to consider how the G20 could better provide continued leadership and support for these goals” (G20 Secretariat, “Making the Global Financial System Work for All, Report of the G20 Eminent Persons Group on Global Financial Governance”). Unfortunately, most of the proposals of the EPG do not reflect this central mandate. On the contrary, the report reiterates continuation of certain practices which have long been the subject of criticism. A number of EPG recommendations seek for the G20 to allow the IFIs to lead harmonization of regulations, standardization of risk assessment and mitigation, mobilization of capital for infrastructure and development financing, and attracting private capital. There are many contentious issues in the provision of and access to global governance, especially in the economic and finance domain. Developing, less developed, small and vulnerable economies would ideally demand more space for representation in global affairs than remaining dependent on their fortunate large and developed economy peers.

In order to realize the full potential of a cooperative international order, it is important that developing countries are given fair and democratic representation in the decision making of IFIs, particularly the IMF and the World Bank. Despite repeated efforts by developing countries including India for action on long-pending reforms of the IMF and World Bank, not much has happened except some revision in the IMF quota formula and inclusion of the Chinese currency, the renminbi, in special drawing rights. As it appears, taking forward the EPG proposals in any manner would amount to empowering the IFIs, and contribute to perpetuation of existing inequities. It could also erode the policy-making space of the sovereign nations. Moreover, the proposals sound self-defeating as they would re-establish the flawed pre-eminence of the IMF in global macroeconomic governance. It is an over-optimistic claim that governance and human capital development have been at the core of the IFI's operations. Among IFIs, the IMF has supported countries during balance of payments crises as the lender of last resort but with conditionalities and Structural Adjustment Programs (SAPs). The efficacy of SAPs for developing countries implemented in the past has been mixed, especially taking into account the experience of small developing economies and Least Developed Countries (LDCs). The G20 should work to suggest and commit to reforms that bring inclusive development, not packaging old wine in new bottles.

The idea of country platforms or any kind of joint platform within the G20 is indicative of an unhealthy trend of cartelization among the IFIs. Without country platforms the G20 can unlock investments in the member countries. Creating an enabling environment for attracting investment should be left to the member states rather than the G20 as a whole. The G20 should enable countries to explore various sources of financing for development. Instead of the G20 creating any such platforms, IFIs can pool their own resources in a common platform without making countries party to that arrangement, and offer them development finance, if approached by any country. By that logic, regional platforms for promoting cross-border investments and connectivity are also not required. Regional platforms would have to necessarily align themselves with the priorities of the member countries in regional cooperative frameworks, like Bangladesh, Bhutan, India and Nepal (BBIN), the Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation (BIMSTEC), etc.

In practice, the IFI community has placed excessive emphasis on promoting financial liberalization in developing countries. So far, this paradigm has not led to holistic social and economic development in

the developing world. The pitfalls of such an approach were anticipated by Gunnar Myrdal long ago. Myrdal, in three volumes of *Asian Drama: An Inquiry Into the Poverty of Nations* and other works, underscored the importance of making a fine balance between a *laissez-faire* economy and state intervention. For example, Brazil had a very active stock market which virtually disappeared following liberalization that allowed local companies to be listed on the New York Stock Exchange. The EPG also argues for convergence of early warning systems, which is a no brainer. Early warning systems have not been effective in predicting financial crises in the past. Although there is a need for continuous surveillance and assessment of risk build-up, it is more efficient to have independent systems of macro-economic risk assessment by institutions such as the IMF, FSB and the Bank for International Settlements than the integrated system. It will help maintain the plurality of early assessment systems as well as contribute and validate the predictive ability of the alternative models. IFIs have failed in anticipating the occurrence of financial crises in Asia and Latin America in the past and most importantly in the United States and the Southern European countries in recent years. Moreover, the post-crisis policy prescriptions offered by the IMF and other IFIs to the crisis-affected economies proved counterproductive and resulted in unwanted economic adjustments. Interestingly, in the early years of these institutions, Harry Dexter White and John Maynard Keynes, eminent economists in this field, were apprehensive of the role and contribution of the IMF and World Bank in pursuit of growth and full employment.

The idea of reorienting development finance by involving the non-G20 constituencies and the IFIs appears to be an unnecessary step. This is an attempt to legitimise the leadership and intervention of the IFIs in G20 matters. This could be a barrier to developing country institutions such as the New Development Bank and the Asian Infrastructure Investment Bank in developing their own procedures. The G20 is not a legitimate global platform; therefore it would be a futile exercise for the G20 to take the responsibility of reorienting development finance by involving IFIs and non-G20 constituencies as it may not be acceptable to the global community. After all, at the meeting in Busan, the developed countries had attempted harmonization of approaches to aid which was rejected by the developing countries.

The report is misleading as it apparently assigns more weight to preventing short-term financial crises as an indicator of healthy development compared to the role of other important development

parameters. The IMF is mandated to primarily provide short-term balance of payments financing. The idea of combined assessment of development risks recognizes the undue emphasis on crisis prediction and management, which is unnecessary at this stage of the evolution of the G20. Financial stability and macroeconomic coordination were the over-riding objectives of the G20 in the immediate years following the financial crisis in 2008-2009. Since then the G20's agenda has expanded to include various development issues. Now that the global economy is seeing buoyancy after a prolonged slowdown following the financial crisis, the G20 should prioritize expeditious implementation of its commitments on various development goals.

Leveraging on Private Capital

Private capital, especially cross-border capital flows, has not been efficiently harnessed by developing countries. This pattern more or less holds across all regions, although there are slight differences. Most countries have relied on official aid flows and concessional funding which would not suffice given the extent of development gaps in developing Asia and Africa. Developing countries in Asia, Africa and Latin America need massive investment in physical and social infrastructure in the next 20 to 30 years. It would not only require efficiency in existing resource use but identifying new and innovative sources of funding, with significantly large contributions of private capital. Paradoxically, globalization has inverted traditional economic views of the desired direction of international capital flows. Rather than encouraging capital to flow to places where it is scarce, globally-mobile capital flows to places where it is most secure. This pattern is creating distortions in the efficiency and equity of investment around the world, especially of government investment.

While public investment would remain a vital component of development finance, the G20 should take proactive steps now to promote a more efficient allocation of private capital through new forms of public-private partnerships. A unified ecosystem, good governance and investment in human capital would attract private capital into desired sectors of investment. Blended finance and local currency financing facilities are novel supplementary financing windows. Small and medium enterprise (SME) financing and agribusiness have been dynamic sectors. Private financing in low-income countries and fragile states is feasible as healthy mobilization ratios (total cost of investment per unit of IDA resources) of 8:1 have been realized (International Development Association. *IDA18 IFC-*

MIGA Private Sector Window (PSW): IDA18 Mid-Term Review. 2018).

The G20 should promote long-term institutional capital from G20 countries into investments related to the Sustainable Development Goals (SDGs). Some countries face particular issues, especially low-income countries, fragile states and selected LDCs. For example, there are 12 LDCs that will graduate from this group in the next few years with consequent loss of duty-free, quota-free preferential market access and aid for trade under the WTO window. They may need special attention for financing to manage their current account deficits during this transition. A balance is needed between macro, micro and affordability/access concerns that should be based on detailed country considerations. Rules of thumb are not good proxies in these debates.

Financing Global Public Goods

Global public goods cannot be created with pure commercial terms of funding. There is a need for special or dedicated funds. International collective action is warranted to fund non-rival and non-excludable functions like research and knowledge sharing, control of pandemics and mitigation of global warming, and global standard setting, visioning, convening and advocacy on policies, such as the Food and Agricultural Organization's principles for responsible investment in food and agriculture ("We Need a Consensus on the Definition of 'Global Public Goods for Health'," by Gavin Yamey, Osondu Ogbuonji and Kaci Kennedy McDade, *Brookings Future Development*, Nov. 20, 2018). G20 members constitute the largest economies in the world and hence will be the main contributors to these potential funds. They should negotiate on such funds. They could learn from the experience of the UN in its new Funding Compact which strives to rectify the imbalance between stagnant core contributions and rising non-core, voluntary contributions that have to be continuously renegotiated. Wise use of new innovative sources of funding would be a pragmatic step in this endeavor.

Development Track

Unlike the finance track, the development track or the Sherpa track covers a whole range of sectors and issues which have larger development implications. To name a few, food security, economic empowerment of women, agriculture, and skill development have significant bearings on the lives and livelihood choices of the poor and excluded sections of the people. In the last 20 years, and

particularly since 2008, the G20 agenda has had commitments on various development issues. Some areas that could be potential game changers in the development track are discussed below.

Science, Technology and Innovation (STI) for Meeting SDGs

Technology development, deployment, dissemination and transfer to developing countries require suitable responses. Current institutional arrangements are not equipped to meet the genuine needs of developing countries in technology development and transfer. The UN has undertaken several initiatives over the years in the area of technology transfer, including 1) the Multilateral Fund under the Montreal Protocol; 2) the Green Climate Fund, 3) the Global Environment Facility (GEF); and 4) the Climate Technology Centre and Network of the United Nations Framework Convention on Climate Change (UNFCCC). These are necessary and are not sufficient as more is needed in terms of research and development, funding, technology transfer and adoption and in terms of synergy among them. The 2030 Agenda, *prima facie*, has only produced a rough skeleton of the proposed Technology Facilitation Mechanism (TFM). Mapping of capacity gaps in developing countries for technology assessment, particularly in the domains of development and sustainability in tune with the SDGs should be undertaken. Proper ecosystems with specific (cost-effective) technology solutions should come up in individual countries and contribute to the global repository. A universal technology bank should be created as the core institution of the TFM. The activities around a TFM technology bank and dissemination of technologies require careful policy design to mitigate informational asymmetries and address market failures and other systemic challenges.

Novel models for incentivizing innovation, such as open source, open innovation, crowd sourcing and innovation prizes, can be explored and adopted. In this regard, the literature on successful examples and models and their adoption in different sectors, ranging from agriculture to drug discovery, is growing. Addressing technology-related issues from a public goods perspective will enable finding workable solutions. Global public goods can be produced and adopted to find cures for communicable diseases, enhance productivity in agriculture, protect environmental commons, and enable access to information and knowledge. Successful examples of such cooperation include the Consultative Group on International Agriculture and the European Organization for Nuclear Research. Further, integrating the SDGs in STI cooperation has not happened

and there is a disconnect between STI cooperation and strategies for the SDGs. There is a strong case to use STI cooperation to meet the SDGs by developing specific programs and mechanisms. The current frameworks and agreements in STI cooperation can be analyzed from an SDG perspective, and institutions that facilitate STI cooperation can be asked to integrate relevant SDG targets as an objective for STI cooperation.

Global Value Chains

As production fragmentation intensifies globally, countries can benefit from integrating into global value chains (GVCs). Currently, trade flows and positioning in GVCs in Sub-Saharan Africa are far below their potential. Lower tariffs, better access to credit for the private sector and a conducive business climate can enable better integration of Sub-Saharan countries into GVCs. Since the G20 already has the Africa Compact initiative, GVCs may strengthen the export prospects of African countries. The same would apply to developing economies in Asia and Latin America as well. Trade facilitation in the form of modern customs and border procedures have the potential to facilitate efficient integration of African economies into GVCs as trade flows in intermediate products are more sensitive to trade facilitation changes. As wages rise in East Asia, production can be pushed to relatively low-wage areas, possibly Africa. However, Africa can only tap this opportunity provided appropriate policies are in place for developing requisite skills among the local workforce, as well as investment in institutional reforms, particularly in technical education and training. At the same time, liberal foreign direct investment regimes may attract investment into industrial sectors in Africa which would fuel local industrialization and strengthen participation in GVCs.

Trade Finance

Globally, one-third of international trade is backed by one or two trade finance instruments. By providing financial support and insurance for uncertainty in payments by importers and delays in meeting orders, trade finance instruments support the trading firms. In Africa, trade finance is a relatively low-risk portfolio for commercial banks. The overall default rate is 5% whereas SMEs face the risk of a 14% default rate. Better provision of trade finance would help integrate SMEs into the mainstream economy and expand their capacity to export. Lack of adequate collateral and poor creditworthiness often leads to rejection of applications by the banks.

Development banks like the African Development Bank and African Export-Import Bank could fill this perverse gap in trade financing and activate the hidden triggers for export growth in African economies. The G20 should enable adequate provision of trade finance to developing countries so as to enable them to benefit from trade liberalization, particularly from GVCs.

Conclusion

Good global governance is a *sine qua non* for achieving sustainable and equitable development in the world. The G20 has to play a critical role in this endeavor. Since countries have already embarked upon achievement of SDGs, the G20 must envisage and steer effective inter-country cooperation mechanisms for realization of this goal. Too much dependence on the IMF, World Bank and other IFIs would not help. In other words, the G20 relegating responsibility to IFIs using their own platforms would not serve the purpose. In fact, IFIs should undertake reforms of their organizations on their own. The finance track must keep the onus on reforming the Bretton Woods institutions and other institutions of global governance.

Global governance is not just about providing finance but putting in place institutional mechanisms that adequately address the vulnerabilities of countries in the long run. Private capital must supplement public investments in infrastructure development and other critical areas of social infrastructure. Cooperation in STI will be an important pillar in developing partnerships in the future. The G20 must nurture such partnerships which would not only help achieve SDGs but provide indigenous technological solutions to numerous development problems. GVCs offer vast opportunities for developing countries to benefit from integration with the rest of the world. Trade facilitation and financing would enable the countries to expand exports and create millions of jobs. With respect to contributions to global governance, the G20 should assign topmost priority to attainment of inclusive and sustainable development and promote global institutional architecture for minimizing country vulnerabilities. In that endeavor, the G20 should proactively advocate for necessary reforms in the existing institutions of governance and adhere to the spirit of mutually beneficial international cooperation. **JS**

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Economics & Security: Key National Interests for Discussion

By Naoyuki Haraoka



Author Naoyuki Haraoka

Geopolitical Uncertainty Influencing Global Economy

The IMF Economic Outlook published in October 2019 predicts world economic growth for 2019 to be 3.0% and for 2020 to be 3.4%. However, there are big risks such as trade and currency wars, cumulating government debt, and deep security tensions. Security risks include an unstable Middle East, uncertainty on the Korean Peninsula, China's assertive foreign policy and an unpredictable US foreign policy, and growing cyber risks, as well as weakening global governance. Before the global financial crisis in 2008, an emerging market could be defined as any country where politics mattered to the market as much as economic fundamentals, while the G7 countries provided a much more stable and predictable political landscape. But since that crisis, politics has started to affect economic and market performance more directly, even among those wealthy countries. The rising income gap between the wealthy and the poor has been the background to increasing discontent among ordinary voters, which has prompted moves against globalization and the free flow of goods and services, as these can trigger increases in unemployment or poverty among non-skilled workers. The move toward nationalism has destabilized politics even in developed nations, and has also brought an end to US-led global governance with Washington's withdrawal from a number of international arrangements for rule-making, such as the Trans-Pacific Partnership (TPP) or Paris Agreement on global climate change. Without solid leadership in global governance, geopolitical instability becomes inevitable. Thus, today it is not economics but geopolitics that is the main driver of global economic uncertainty.

Economics & Security Need to Be Discussed Together

It is noteworthy that in this growing geopolitical uncertainty digital technology plays a key role. Digital technology creates huge business opportunities, but it also brings malicious factors such as growing cyber risks and threats to national security through trade and investment in sensitive technologies. Digital technology, including quantum computing, machine learning and 5G, has transformed most domains of human activity, such as people's interactions or exchange of information in business management, and also in defense and security. The digital economy and society

has made countries vulnerable to cyberattacks by both state and non-state actors. We now need to reflect on how to maximize the benefits of digital technology in terms of economics, while paying proper attention to those technologies' implications for national security, though economics and security have been viewed largely as separate issues of national interest in the past. Economics and security should now be discussed together as inseparable issues.

In particular, at this moment, the major developed nations seem increasingly willing to advocate for their economic and security interests unilaterally. This has enhanced the need to discuss both issues together to create common rules. In this context, we should bear in mind that security will be key to achieving prosperity, and prosperity will in turn help pay for security. If social disharmony brought about by rising income disparities increases economic and security risks, then it becomes imperative to ensure social harmony to achieve security and prosperity.

This means that the silo approach to studying economics and security issues completely independently is now obsolete. Prosperity, security and social harmony are the important components of national interest. All three matter, and they need to be discussed together in order to mitigate the risks they face.

Tackling Risks to National Interests

Countries exposed to security risks need to balance possible solutions against their strong economic interests. Mitigations of security risks could be achieved by supporting market systems and people-to-people connections through migration or research collaboration rather than confrontation, as well as strengthened domestic defense and security governance systems. In this regard, globalization would not be contradictory to national security but rather promote it. Interdependence among nations through cooperation could lead to mitigation of security risks.

While defense and security are public goods to be provided by governments, risk mitigation can be provided by not only governments but also business and civil society. Governments are mainly responsible for creating incentives for the private sector to mitigate risks. Laws and governance institutions supported by effective enforcement would help business and civil society in contributing to risk mitigation over time.

A scenario approach would be useful for such risk mitigation and management, since risks are affected by a wide range of actors, such

as domestic politics, international relations in hot spots like the Korean Peninsula or the Middle East, and technological change and the impact of data and digitalization. There could be a number of scenarios depending upon those variables. Such scenario-making would enable policy practitioners or private businesses engaged in risk mitigation to have an analytical framework to eliminate arbitrary thinking and achieve a logical and strategic approach to a complex issue.

Strategic thinking is very useful in considering foreign direct investment (FDI) in digital and telecommunications infrastructure. First, we need to identify the risk of a cyberattack by malicious states or companies which could disable key telecommunications infrastructure. Then we should prepare strong defenses in firms and organizations against cyberattacks, endorsed by enforcement of strong laws. We should build up a much less oligopolistic market, since the risk of becoming a victim of cyberattacks will be lowered with more players in the market. In building up digital networks, creating more competitive and diverse market structures with less concentration of a small number of large actors would lead to better risk mitigation, rather than discussing only the issue of foreign ownership of the companies involved in building up these networks' infrastructures.

Another risk exists in data. There will be concerns about firms' susceptibility to theft of personal data by cyberattacks. This risk could be logically and strategically reduced by cyber defenses strengthened and supported by the enforcement of strong laws on the protection of privacy and by corporate transparency.

In order to meet the challenge of the risks produced by complex new digital technologies, first it would be important to assess these risks clearly and identify exactly what they are and try to use all kinds of standard knowledge to mitigate them. This must be done creatively and strategically. Most importantly, we will need international collaboration rather than confrontation. New technology has created the need for a new international cooperation order rather than confrontation among nations. So we will need new global governance for risk mitigation related to digital technology.

Japanese Leadership Needed to Achieve New International Order

To realize a world in which the United States and China work together on practical and mutually beneficial steps to address their

tech cold war, Japan would need to play a critical leading role. Japan could boost cooperation with China and the US by taking advantage of its unique position and providing each of them with incentives for cooperation in areas where their national interests coincide. Japan could at the same time work with like-minded nations, such as Germany, Canada, France and the United Kingdom, to defend and support existing international institutions and play a leadership role in global rule-making for trade, data transfer, and innovation policies. This could be possible in light of its achievements in having realized the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) despite the withdrawal of the US from the TPP in January 2017. Whereas the CPTPP was signed by 11 countries in December 2018 and is open to the US, the Regional Comprehensive Economic Partnership (RCEP), another Asia-Pacific regional FTA, was agreed by 15 countries in November 2019 for signing into law in 2020 and is open to India. These mega-regional FTAs could lead to the foundation of a new multipolar global order.

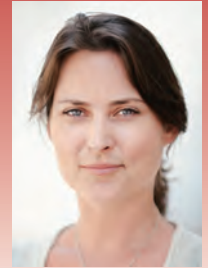
In addition, APEC, a wider regional group of Asia-Pacific nations including CPTPP and RCEP member nations, could be a good place for ministers and officials to discuss economics and security together to deliver prosperity, security and social well-being simultaneously. APEC also has an advantage in its informal connections with business and thus the private sector could express their views and concerns regarding risks to their national interests related to economics and security. Although APEC's discussions may have no binding effects, such informal exchanges of views on economic and security policies could result in reasonable peer review pressure upon the member nations. Japan, a member of all these three groups – the CPTPP, RCEP and APEC – could contribute effectively to policy discussions in APEC to initiate a new global order to help resolve the issues of economics and security together.

Finally, as for cyber security, Japan could continue to work on a cyber coordination and monitoring center. This would be useful in encouraging FDI in research and development which has been declining during these days of the US-China tech cold war.

A world without leadership that people can trust would be disastrous, especially in the light of digital technology. New technology progresses rapidly. We may not have much time to create a new order that people can count on. **JS**

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The EU & Japan: Partners for Stability in the Indo-Pacific?



Author Eva Pejsova

By Eva Pejsova

The European Union and Japan have never been closer. Although they have always been like-minded partners, sharing the values of democracy, rule of law and human rights, their bilateral relations have almost exclusively focused on trade and economic issues, neglecting the potential of closer political and security cooperation.

However, the last two years saw an important shift. The signing of the EU–Japan Strategic Partnership Agreement in June 2018 signaled the willingness to deepen consultations and cooperation on global security issues. The EU–Japan Economic Partnership Agreement, in force since February 2019, created the world's greatest free trade zone, connecting almost a third of the global market. Finally, on the occasion of the visit of Japanese Prime Minister Shinzo Abe to Brussels at the end of September 2019, the EU and Japan signed a “Partnership for Sustainable Connectivity” to promote “free, open, rules-based, fair, non-discriminatory and predictable regional and international trade”, outlining a concrete roadmap for functional cooperation in the domain.

These upward developments are not only a sign of a maturing relationship; they are a result of a growing number of shared security concerns. First, the current Washington policy of putting “America first” has led to the realization by many of its traditional allies, including Europe and Japan, of the need to bolster their own security profiles to defend their interests. The expanding influence of China in Europe and its neighborhood, accelerated in the context of its Belt and Road Initiative (BRI), has made the EU more aware and more concerned about Beijing's global strategic ambitions. Finally, the negative impacts of the strategic rivalry between China and the United States and the polarizing effect it has on the broader Indo-Pacific region is another reason for like-minded countries to defend more proactively the current multilateral rules-based order.

What role can the EU and Japan play in this changing strategic environment? This paper first analyzes the emerging security dynamic within the Indo-Pacific, defined by a new type of great power politics, and the dangers it poses for regional stability. It further highlights the type of foreign policy action that could ease down these tensions, broadly defined by the concept of “middle-power diplomacy”. Finally, it suggests some concrete areas for the EU and Japan to deepen their cooperation beyond connectivity, in the field of maritime security and security in Africa.

The Indo-Pacific: a New Playing Field

Ever since Japan first officially presented its vision for a “Free and Open Indo-Pacific” (FOIP) in 2016, the concept has become a synonym for the changing strategic dynamic in the region.

Geographically, the Indo-Pacific underscores the natural confluence of the Indian and Pacific Oceans, shifting the regional strategic balance westwards. It reflects the emergence of new security actors and policies, including China's BRI, the growing role of India as a regional player, the diplomatic rapprochement between Japan and India, and the increasing relevance of Europe.

Functionally, it focuses on boosting trade and connectivity to generate growth, prosperity and cooperation, noting also the importance of the African continent to Asian countries for trade and natural resources. Finally, the concept is loaded with ideology, emphasizing values and principles that should underpin it, such as freedom of navigation, free trade, and rule of law.

Although Japan's original idea was to promote an inclusive and cooperative regional architecture, it has been widely interpreted by China as an attempt to control its rise. Indeed, there is little doubt that the FOIP concept has been formulated in response to China's growing strategic influence across the region. Since its launch in 2015, large-scale investments in strategic infrastructure (ports, telecommunications, energy) along its BRI in the Indian Ocean, Africa and Europe have enabled Beijing to exert pressure on governments to achieve political goals. Culminating debt-traps have become a growing concern for the international community.

After Washington formulated its own “Indo-Pacific Strategy” in 2016, the region has become a theatre for a rising great power rivalry between the US and China. The decision of the US, Japan, India and Australia to revive the Quadrilateral Security Dialogue in 2017 is a sign of democratic powers stepping up in defense of the current rules-based order. Albeit it is only an informal consultation mechanism, it further added to the growing divide and tensions between the *status quo* powers and Beijing.

Theatre of Power Politics

Discussions about the regional strategic dynamic quickly shift to a broader debate on the emergence of a new world order, dominated by a new type of great power relations. In a recent opinion piece published in the *New York Times*, a group of distinguished former

world leaders warn of the grave impact of a US–China trade war on the global economy and stability, and the risk of recession it poses for developed countries (<https://www.nytimes.com/2019/10/11/opinion/china-trade.html>). Using the example of the Cold War, they raised concerns about the divisive character of the dispute, forcing many nations to choose between the two powers. While the current trade tensions have indeed accelerated this trend, polarization of the Indo-Pacific started even before, dividing countries along the competing spheres of influence through investments, historical linkages and ideological proximities. Many small and middle-sized countries in Southeast and South Asia feel the growing pressure to choose their strategic camps.

The impact of the current tensions is not limited to trade and security. The competition takes place on all fronts – including in research and technology – with implications for the broad spectrum of human and economic activities. It shifts attention away from everyday functional security issues, such as transnational crime, environmental or human security issues, which need to be addressed through cooperative efforts. Finally, it undermines the achievements and the potential of existing multilateral structures in the region – whether the ASEAN Regional Forum (ARF) or the Indian Ocean Rim Association – to provide some form of regional governance.

Time for “Middle-Power Diplomacy”

The US-China rivalry tends to define the Indo-Pacific in binary terms and limits the field of possibilities for other important regional actors – Japan, India, ASEAN, South Korea or even the EU. All these players maintain strong economic ties with China and close security relationships with the US, and all try to navigate the growing tide of power politics to protect their interests. But they also need to step up their efforts collectively to contain the risks stemming from the escalating competition. Importantly, some key global issues, such as climate change, technological progress, or much needed institutional reforms (such as the WTO) can only be addressed through effective international cooperation, with the participation of both the US and China.

This is where the concept of “middle-power diplomacy” offers some useful guidance. The term “middle powers” was widely used in the Cold War context to refer to countries that are neither great powers nor small powers that would simply suffer the hegemony imposed by others. They are usually stable, prosperous democracies that do not have substantial military capabilities to be strategic game

changers on their own, but can still exert influence on the international scene through economic and diplomatic means.

“Middle-power diplomacy” describes a specific form of foreign policy: one that seeks multilateral solutions, peaceful settlement of disputes, adherence to international norms and preservation of a rules-based global order as an essential prerequisite for global stability. In other terms, it is the “good citizen” behavior that could stabilize the global order through influence in international institutions and promote principles of preventive diplomacy and crisis management, but also human security and environmental issues.

At times when many countries find themselves caught “in the middle” of the US–China great power rivalry, joining forces in addressing these challenges and bearing a collective responsibility to protect the global order may be a way forward.

What Role for the EU?

The EU has been most overlooked in the Indo-Pacific debate. In Asia, Europe has traditionally been viewed as a distant player with little influence over regional security. This was partly due to its geographical distance, but mostly to its limited security toolbox and a profile of a solely economic power.

The EU decided not to adopt its own “Indo-Pacific” strategy for the region and keeps referring to the Indian Ocean, Asia and the Pacific separately. This is partly due to the EU’s heavy strategic baggage implicitly contained in the term. In the minds of many diplomats in Brussels, the Indo-Pacific remains connected to the US strategy for the region, which openly points fingers at China and Russia as main enemies. Although the EU may share most concerns *vis-à-vis* the regional threat environment, it does not share the same strategic culture. Its “strategies”, often criticized for being too vague and too weak, do not refer to specific actors. Rather, they refer to the type of behaviors and values it opposes and the kind of norms it wants to promote.

That does not mean it has not followed regional developments closely. As a global trading power, it has legitimate interests in security and stability in Asia. Also, the EU has legal responsibilities *vis-à-vis* its Asian partners stemming from its membership of the ARF and its accession to the Treaty of Amity and Cooperation in 2012. Finally, as a normative superpower, the EU has a strategic interest in promoting norms and principles that underpin the current rules-based order, including respect for international law and its institutions.

Over the past years, especially since its accession to the Treaty of Amity and Cooperation, the EU has been most vocal about its interest in playing a more proactive role in regional security. Although it may not be considered a “middle power” as such, its policy has always been to support the cooperative multilateral security architecture and preventive diplomatic measures to ease regional conflicts. Finally, it has been using its technical expertise and experience to build the capacity of regional countries in addressing various non-traditional, functional security issues – from transnational crime to border management and environmental issues.

EU–Japan Cooperation: From Connectivity to Security

The current strengthening of EU–Japan ties beyond economic cooperation is most timely. Both Japan and the EU are atypical security actors, with political constraints limiting their capacity to project power through military means. However, together they represent a third of the global market and weigh significantly in world affairs through their economic and diplomatic leverage. They share the same vision of building a stable and prosperous Indo-Pacific based on multilateral cooperation and the rule of law. Finally, they possess significant human and technological resources and expertise to address the many outlying non-traditional security issues, as well as global challenges related to climate change, research and innovation, and environmental governance.

Among the functional areas ripe for closer EU–Japan cooperation, connectivity has been the most logical starting point. Promoting physical, people-to-people and institutional connectivity is the backbone of the FOIP’s economic agenda, linking up to Tokyo’s tradition of infrastructure investments in Southeast and South Asia.

The EU published its “Connectivity strategy” (“Connecting Europe and Asia - Building Blocks for an EU Strategy”, Sept. 19, 2018, accessible at https://eeas.europa.eu/sites/eeas/files/joint_communication_-_connecting_europe_and_asia_-_building_blocks_for_an_eu_strategy_2018-09-19.pdf) partly as a response to China’s BRI, to underscore the rules and principles that should govern all connectivity projects in the region – namely, economic, social and environmental sustainability, transparency and the rule of law. The recent conclusion of the EU–Japan Partnership for Sustainable Connectivity, promoting high-quality infrastructure and free, fair, open and rules-based trade and investments is a logical step in a common direction and certainly most welcome. That said,

connectivity can only flourish in a safe and stable environment. Even the most environmentally friendly and efficient seaport, built according to the highest quality standards, will not prosper if it is located in a country torn by domestic conflicts or in waters affected by geopolitical tensions. Joining forces to address the various sources of instability across the Indo-Pacific is therefore essential to ensure sustainable growth and prosperity in the region.

Maritime Security

Maritime security presents a vast array of opportunities for cooperation for both partners. The outbreak of piracy (whether in Southeast Asia at the end of 1990s or in the Western Indian Ocean since 2008) is one issue that has managed to bring the international community together and steer an unprecedented level of cooperation.

However, there are many other issues that need to be addressed through concerted efforts. Unsustainable exploitation of marine natural resources, environmental destruction and proliferation of seaborne criminal activities (illegal fishing, drug smuggling and people trafficking) are lasting security challenges that keep undermining the economy and stability in Southeast and South Asia and Africa. Moreover, the region crucially lacks effective cooperative institutional frameworks for multilateral governance.

While Japan has contributed most to enhancing maritime safety and security in Southeast Asia, providing navigation systems, countering piracy, building law enforcement capacity and enhancing port security, the EU has been most active in similar activities in Africa. Building capacity for maritime law enforcement has been a key component of its comprehensive approach to countering piracy in the Horn of Africa as well as in the Gulf of Guinea. Projects such as EEOFISH have been targeting illegal, unreported and unregulated (IUU) fishing, and developing sustainable fisheries and viable blue economies in East Africa and the Indian Ocean (bilaterally and through the Indian Ocean Commission), crucial for sustainable growth and stability in the region. (In 2018, the EU provided 28 million euros to promote sustainable fisheries in the region under the EEOFISH program.) Finally, the EU has been investing most in enhancing shipping safety in the Indian Ocean and Africa through its Critical Maritime Routes programs, providing technological tools for better Maritime Domain Awareness, capacity-building and training for regional law enforcement agencies and setting up regional information-fusion and information-sharing centers (<https://www.crimario.eu/en/the-project/rationale-objectives/>). If the EU and Japan aim to improve connectivity at sea, they also need to promote

multilateral cooperation and institutional mechanisms in the Indian Ocean region. The Indian Ocean Rim Association is one such structure, dealing with maritime safety and the development of blue economies in the region. Although neither Japan nor the EU are members, they could consider gaining observer status to support their activities. However, much can be done through bilateral channels as well, in cooperation with individual regional countries.

Security in Africa

Another immediate concern for the EU and Japan to consider with regard to connectivity is security in Africa. East African countries border the Indian Ocean and are implicitly concerned by the Indo-Pacific concept and its future connectivity architecture. Yet many of them still struggle with economic, social and environmental challenges, organized crime, weak domestic institutions and sustainable governance.

East Africa has become known as the “Heroin Coast”, with up to 40 tons of the drug smuggled a year due to ineffective border controls (<https://www.unodc.org/easternafrika/en/illicit-drugs/drug-trafficking-patterns.html>). Wildlife trafficking, fueled by the increasing demand from Asia, has become one of the world’s most profitable organized crimes (https://www.unodc.org/documents/data-and-analysis/Studies/TOC_East_Africa_2013.pdf). Finally, illegal charcoal trade from Somalia to the UAE and Oman is another important destabilizing factor in the region, generating revenue for the local terrorist group Al-Shabaab, with links across the East African coast. (According to the UN Monitoring Group on Somalia report, illegal charcoal tax generates revenue of \$7.5 million per year: <https://undocs.org/S/2018/1002>). Due to its historical presence, European nations maintain active diplomatic and economic relations with countries across the African continent. The EU also deploys vast resources to provide development, security and stability in the region, as it is the first to be concerned by potential economic, climate or conflict-driven emigration. At present, the EU maintains eight civilian and military Common Security and Defence Policy (CSDP) missions and operations in Africa, including its counter-piracy naval operation ATALANTA off the Horn of Africa, military training missions in Somalia and Mali, civilian capacity building missions in Somalia, Mali and Niger, and a border assistance mission in Libya (<https://eeas.europa.eu/headquarters/headquarters-homepage/430/military-and-civilian-missions-and-operations>).

The newly established bilateral Strategic Partnership Agreement (SPA) between the EU and Japan is a promising framework for enhancing political and security relations. However, it still needs to

be completed with concrete initiatives of a practical nature. One useful tool for deepening security cooperation with the EU is the so-called Framework Participation Agreement (FPA), which allows third parties to take part in the EU’s CSDP missions for crisis prevention and management. Two Asian countries – South Korea and Vietnam – have signed the FPA so far. If Japan could consider such an agreement with the EU, it would gain not only a foothold in African security but also a closer operational experience with the EU as a security partner, which could be of use in other parts of the Indo-Pacific.

Conclusion

The EU and Japan have come a long way in fostering their economic and political ties. The emergence of the “Indo-Pacific” as a newly defined geostrategic space constitutes a common playing field and opens a vast array of opportunities also for closer security cooperation.

For the longest time, the EU was not considered by Japan as a useful security partner because of its low military profile, geographical distance and seemingly little to offer in dealing with Tokyo’s immediate security concerns, such as the military rise of China or the North Korean threat. But times have changed, the EU has become a more proactive security player, China’s strategic influence has become a matter of global concern, and Japan has stepped up its foreign and security policy beyond East Asia.

Both partners have much to offer to make the Indo-Pacific free, open, inclusive and prosperous. What the region needs today is not necessarily more military power, but more common sense, cooperation, development and sustainable management of resources. It needs more responsible and resourceful “good citizens” to take care of the global commons and to act in concert to contain the dangerous game of power politics currently at play – a role that Japan and the EU could well exert together.

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Contrasting Policies Regarding North Korea & Iran



Author Mark Fitzpatrick

By Mark Fitzpatrick

Introduction

My career has focused on the North Korea nuclear issue for 30 years, and on Iran's for two decades. With regard to North Korea, I, like everyone else, failed. After six nuclear tests, North Korea can produce thermonuclear bombs. It can probably miniaturize the warheads and attach them to missiles that can reach as far as Florida. With regard to Iran, we have not failed – not yet anyway, although with the 2015 nuclear deal in shatters, Iran is beginning slowly to resume its march to a nuclear weapons capability.

Both North Korea and Iran can be called “outlaw states” in that each violates many international norms. They are notorious for their nuclear programs, ballistic missiles, human rights abuses, aggressive actions and detention of foreign citizens. They are thus often cast in the same category. And why not, since they have cooperated in developing ballistic missiles and possibly in sharing some nuclear data, though the evidence for this is far less conclusive.

But Iranians, seeing themselves as culturally and economically superior, dislike being grouped with the backward hermit state. And to be fair, North Korea is a far worse actor. Unlike Iran, it has developed and tested nuclear weapons and intercontinental ballistic missiles; it has stockpiled and used chemical weapons, and it employs cybercrime as a regular tool of statecraft. While Iran has elections, however circumscribed, gender equality in many respects and religious principles, North Korea's dynastic system lacks civil rights and principles of any kind.

And yet, today, North Korea is treated far better. While both states are subject to extensive economic sanctions, North Korea has strong partners who provide a diplomatic shield and acquiesce in its sanctions-evasion techniques. Its alliances with China and Russia are less dependable than in the past, but having them on its side gives North Korea diplomatic options. Russia and China have friendly relations with Iran, and cooperate tactically, but they protect Iran to a far lesser degree.

Meanwhile, North Korea is courted by every major player with the sole exception of Japan. In the past two years, Chairman Kim Jong Un has met with the leaders of China, Russia, South Korea and the United States – three times in both of the latter two cases. I expect there will be yet another with President Donald Trump before long.

The US president excused North Korea's mid-2019 series of missile tests on grounds that they were only short-range and thus

not contradictory to Kim's moratorium on intercontinental ballistic missile launches. The rest of the US government knows that those tests were a violation of UN Security Council sanctions. They also know the missiles pose a threat to US military personnel and other citizens working and living in Northeast Asia, not to mention the combined 180 million citizens of Japan and South Korea. But Trump is trying to achieve a diplomatic breakthrough with North Korea that would redound to his glory, and thus he is willing to overlook evidence which strongly suggests that Kim has no intention of giving up his nuclear arsenal.

In Singapore last year, Trump agreed to suspend large-scale US-South Korea joint military exercises, and he excused North Korea's human rights violations, among other concessions. In a post-summit press conference, he even declared his willingness to unilaterally withdraw US forces. Trump stopped describing US policy toward North Korea as one of “maximum pressure” and he treats Kim with fawning affection, even going so far as saying that they “fell in love”. He was speaking metaphorically, of course, but what an odd metaphor to describe partnership with a despot.

Comparison to Recent Past

This coddling of North Korea is a new phenomenon – at least in the case of the US and South Korea. China and Russia were always willing to look the other way when North Korea broke the rules. Up until 2018, China did go along with tougher UN measures. When South Korean President Moon Jae-In and Donald Trump pursued a strategy of engagement, however, China relaxed its sanctions implementation. Japan, by contrast, has been consistently tough. But it can do little on its own. Hence, Prime Minister Shinzo Abe's persistent courtship of Trump, encouraging him to remain firm. Unfortunately, this courtship has gone largely unrequited. Trump pays lip service when he meets with Abe, then often does the opposite in his interactions with Kim.

Only in Hanoi in February 2019 did Trump refuse to give in to Kim. There, both sides overplayed their hands. Kim insisted on an end to all UN sanctions, in exchange for an ambiguous offer to close down the Yongbyon nuclear center while leaving other undeclared facilities producing enriched uranium. Trump demanded complete denuclearization before the US would offer sanctions relief. He does not understand that North Korea will not unilaterally disarm. Nuclear weapons are vital to the regime's sense of self-preservation. It would

be better to pursue more limited objectives, such as verified dismantlement of all fissile material production and an end to missile tests, while maintaining the goal of denuclearization.

Tough on Iran

Meanwhile, Trump has been exceedingly tough on Iran. Calling the 2015 Iran nuclear agreement the “worst deal ever”, he walked out on it in May 2018 even though Iran had been faithfully abiding by its conditions. Trump then imposed the harshest ever sanctions, which he has continued to tighten, even putting Iran’s Foreign Minister Javad Zarif on the US Treasury’s black list in August 2019. Trump’s claim to want negotiations with Iran is incompatible with blackballing Iran’s top negotiator. I believe the real purpose of the “maximum pressure” campaign is to weaken Iran and to encourage regime change.

America’s best friends are nevertheless still trying to mediate between Washington and Tehran. Abe offered to carry a message from Trump when he traveled to Iran in June. Unfortunately, the effort came to naught. Although Iran made a gesture by releasing an American resident whom it had detained, Supreme Leader Ayatollah Ali Khamenei rebuffed Abe’s effort, saying: “I do not see Trump as worthy of any message exchange, and I do not have any reply for him, now or in the future.”

French President Emmanuel Macron then tried. He twice sent his top adviser to Tehran and he invited Zarif to the G-7 Summit in Biarritz, in hopes of arranging a meeting at the UN between Trump and Iranian President Hassan Rouhani. But Iranians are not interested in such “photo-ops”. Unlike Kim, who derives international legitimacy by sitting at the table as an equal of the US president, it would be politically dangerous for Rouhani to appear friendly to a US leader who is trying to kill the 2015 nuclear deal. Rouhani was even unable for political reasons to shake President Barack Obama’s hand at the UN in 2013. After the G-7 meeting, Rouhani insisted that before there can be any positive diplomatic development, the US must first abandon its sanctions. Trump is highly unlikely to do this.

Why the Different Approaches?

There are several reasons why the US treats Iran more harshly than North Korea. One factor is psychological. Americans have not gotten over the anger and humiliation we felt when Iran seized our embassy in 1979 and held 52 US diplomats hostage for 444 days. We often forget that North Korea did something similar a decade earlier, when it seized the *USS Pueblo* spy ship, keeping its 83 crew members hostage for 11 months, even torturing them. North Korea still holds on to the *Pueblo*, using it as a propaganda museum. Yet Iran’s hostage taking is more seared into our memory because the

drama of it was aired daily on television news. By contrast, there were no foreign TV crews in Pyongyang to witness the humiliation of the *Pueblo*.

America’s history with North Korea suggests a second reason for different treatment. Having fought an inconclusive costly war in the Korea Peninsula, the US is not inclined to do so again. Hence, it is more willing to seek diplomatic solutions. America does not want another war in the Middle East either. Yet its main partners in the region – Israel and Saudi Arabia – often appear eager for the US to deal Iran a military blow. Leaked US diplomatic cables from 2008 recounted Saudi King Abdullah’s repeated call for the US to attack Iran to put an end to its nuclear weapons program. He urged Washington to “cut off the head of the snake” – meaning to overthrow the Islamic republic. In Northeast Asia, America’s allies are not similarly calling for the US to attack North Korea or to remove its regime. To the contrary, they advocate peaceful diplomacy.

Actually, of late, Saudi Arabia has not been calling for the US to attack Iran, even after Trump asked what they wanted him to do, after the Sept. 14, 2019 attack on the Saudi pipeline and oil refinery. The Saudis are wary about direct military engagement with Iran. As former US Secretary of Defense Robert Gates said, the Saudis always want to “fight the Iranians to the last American”.

Interestingly, Japan distanced itself from the US on this matter. While US Secretary of State Mike Pompeo expressed confidence Iran was responsible, Defense Minister Taro Kono expressed agnosticism. I have not seen the evidence, but I believe Iran had a motive: it made clear for months that if it cannot export oil, then neither should its Arab rivals. Iran does not want the Saudis to plug the oil supply gap caused by the sanctions on Iran. The US says it has high confidence about Iran’s culpability. If so, the evidence should be shared with Japan and other key allies.

Thirdly, Iran’s antagonism toward Israel adds to Americans’ sense of grievance. Iran’s call to “wipe the Zionist state off the map” should not be taken literally. It means if all Palestinians are allowed to vote, Israel could not remain Zionist. Yet such apparent calls for annihilation, sometimes expressed more luridly, evoke memories of the Holocaust and make Americans determined to protect Israel by any means. Most fervent in their protectiveness, America’s large community of evangelical Christians finds common cause with Americans of Jewish faith. Combined with the 1 million-strong Iranian diaspora in the US, many of whom came when the Shah was overthrown in 1979, the anti-Islamic Republic of Iran political lobby is formidable. Neither Iran nor North Korea has any friends in the US, but Iran has more avowed enemies, many of whom are well-placed to promote policies of antipathy.

Fourthly, there are factors involving geography. The most obvious is oil; over half of the world’s oil reserves are in the Middle East, and

Iran ranks fourth in the world in this regard. That makes it intrinsically more important than oil-deprived North Korea.

The other geographic factor is that South Korea's capital and one quarter of its population are within range of enemy artillery. Even before North Korea's nuclear tests, its conventional weapons held Seoul hostage. Despite repeated North Korean provocations over the years, South Korea and the US avoided a kinetic response that could have rekindled the Korean War. Now that Pyongyang has nuclear weapons, it has an even stronger means of deterring attack. In the Middle East, Iran troubles its neighbors in many ways, but it does not pose a similar existential threat. So that it can never pose such a threat, Washington is determined by any means to prevent Tehran from acquiring a nuclear weapons capability.

Defense thinkers in Japan and South Korea once thought that the US would similarly do everything necessary to block North Korea from getting nuclear weapons. Americans failed in this regard, because we and South Korea were not willing to go to war to stop the nuclear program. The cost seemed to be too high. In the Middle East, the cost of war appears to be lower.

A fifth reason for treating Iran more firmly is the nature of the threat it poses. Although North Korea is a worse actor, its bad actions are limited geographically. Iran's regional activities, including its patronage of non-state militias and promotion of a so-called "Shiite crescent", collide with US interests from Lebanon to Yemen. Because of its support for groups like Hezbollah that conduct terrorist acts, Iran is judged by the US to be the world's greatest sponsor of terrorism. By contrast, North Korea's *juche* ideology has no appeal beyond its immediate borders – and even many of the citizens within those borders surely see through the falsehood of the self-reliance slogan.

North Korea's bombing of Korean Air Flight 858 in 1987 landed the country on Washington's list of state sponsors of terrorism, but it was removed in 2008 to promote a diplomatic breakthrough and because it had not conducted more recent acts of terrorism.

There were legitimate grounds for restoring the state sponsor of terrorism designation in 2017. North Korea's use of chemical weapons to assassinate the leader's half-brother Kim Jong Nam at Kuala Lumpur airport that year was an act of terrorism by almost any definition. Why else use such a gruesome means of murder unless the purpose was to evoke terror? North Korea's cyber hack of Sony Pictures in 2014 and its cyber thefts from banks and cryptocurrency exchanges to the amount of \$2 billion, according to a new UN report, also qualify as terrorism by some definitions. Failure to fully account and make amends for its abduction of citizens from Japan and other countries add to the list of grievances among concerned states. Yet, to Washington at least, North Korea is seen as a less formidable foe, a more contained threat, in comparison with Iran.

A final reason for treating the two states differently is personal.

Trump is determined to outshine his predecessor Obama and to undo the latter's accomplishments. In Trump's mind, the Iran deal is bad because it was Obama's deal. And since Obama was unable to make any progress with North Korea, Trump wants to show the world that he is the one who can.

Prospective Deal with North Korea

Looking ahead, I see grounds for both optimism and cynicism. Given Trump's egocentricity and his need for a diplomatic achievement before the 2020 presidential election, I believe he will be inclined to try to strike a limited deal with North Korea. The prospects for this have improved now that John Bolton is no longer in the White House. He opposed engagement with North Korea and insisted on an all-or-nothing deal, surely knowing that North Korea will not give up its nuclear weapons entirely. The Hanoi summit thus failed.

The deal that might be possible with Pyongyang would not eliminate its nuclear weapons program, nor its missiles. And the verification measures would be limited. The deal would not address the other problems North Korea presents, including its chemical weapons, its human rights violations, its cybercrimes, its counterfeiting and its smuggling. The agreement I foresee would contain and reduce the nuclear threat to some degree. In many respects, it would resemble the 2015 nuclear deal with Iran, although with fewer constraints and less detail. It would be worse than what Trump repeatedly calls "the worst deal ever".

He is wrong to say so. In light of the alternatives, and the state of the Iran nuclear program before it was stopped, the 2015 agreement was good. It blocked any potential for an Iranian nuclear weapon for a number of years and thus also obviated the likelihood of war. So, I will not prematurely cast judgement on an imperfect deal with North Korea. To quote Voltaire, we should not let the perfect be the enemy of the good.

This essay is drawn from the author's presentation at the Third International Symposium on Global Risks, on Sept. 19, 2019 held by the Japan Economic Foundation in coordination with Komatsu Research and Advisory.

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The North Korean Economy After Economic Sanctions



Author Yong Sueng Dong

By Yong Sueng Dong

Introduction

Recently, global economic uncertainty has been growing due to the US-China trade war and Japan-South Korea dispute. Such clashes can develop into the form of economic sanctions. Economic sanctions are a step that the party imposing the sanctions takes against the receiving party in order to push through their demands. The US trade tariffs imposed on China are a measure to achieve policy change in China. The country imposing sanctions imposes the most effective ones by taking into considering the economic interdependence between the two countries. In the country on the receiving end of the sanctions, the inconvenience and disadvantages to the general public arising from the sanctions function as political pressure. Policy-makers calculate the cost benefit of maintaining power and decide whether to change policies or not. This is the general theory on economic sanctions.

Powerful economic sanctions are also being imposed on North Korea. However, rather than changing policies, North Korea is further strengthening its opposition. While we can interpret this reaction to mean it will take more time until its policies change, considering North Korea's past pattern of behavior, it is highly likely that opposition will escalate rather than its policies changing. The reason for this assumption can also be drawn from the general theory of economic sanctions. In the following paragraphs, I would like to look at the impact that the economic sanctions have had on the North Korean economy. After considering the general theory of economic sanctions, I will begin with a discussion on whether the sanctions imposed on North Korea by the international community are actually functioning and the changes that have emerged in the North Korean economy and society through analysis focusing on recent events. Then I will consider why a phenomenon that does not match the

primary goal of economic sanctions is being observed in North Korea.

General Theory of Economic Sanctions

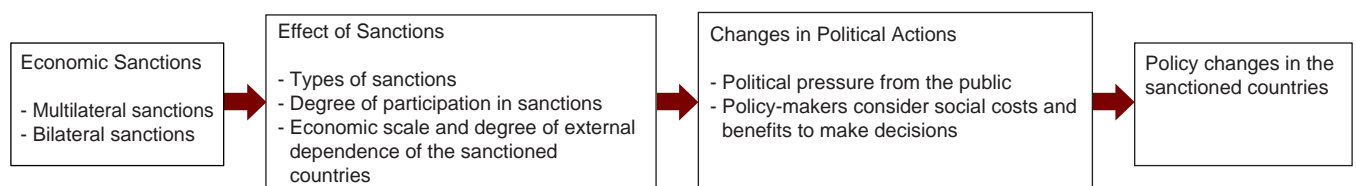
Academically, it is difficult to find an analysis that shows the general theory that economic sanctions are effective. This is because the effect of sanctions may differ according to the situation of the country in question. The results may also differ depending on the economic interdependence of the imposing party and receiving party, and the level of political stability within the country in question. I have summarized the general theory in the flow chart below ([Chart 1](#)).

Economic sanctions are used by the imposing party against the receiving party to push through the imposing party's demands. Therefore, whether to impose sanctions or not is determined by the degree of the relevant parties' benefits and disadvantages rather than by the legitimacy of the action. Thus it can be said that the imposing party is not always righteous, as well as the receiving party did not necessarily do something wrong. We must consider sanctions on the premise that we cannot apply right-or-evil values.

The form of sanctions can be largely classified into multilateral sanctions and bilateral sanctions. Multilateral sanctions are mainly measures taken by a resolution of an international organ such as the United Nations (UN). When a country in question takes action that goes against international standards, the international community decides to impose sanctions on that country in order to control or correct it. However, because the UN does not have the power to force implementation, individual member countries choose to orchestrate bilateral sanctions against the target country. Member countries report their degree of implementation of UN resolutions to the UN

CHART 1

Flow chart of economic sanctions



Source: Compiled by the author

and it then evaluates them. The disadvantages faced by a member country that does not implement sanctions by a resolution of the UN can also be regarded as sanctions in a broader sense. Representative examples of such sanctions in modern society are the UN resolutions for sanctions against North Korea and Iran and the implementation thereof by respective countries.

Economic sanctions can be categorized into trade sanctions, financial sanctions, and sanctions against individuals. Trade sanctions are cases in which trade with the receiving country is prohibited or restricted. In modern society, in which economic exchange in the international community is active, not being able to conduct trade is an extremely large disadvantage. The higher an economy's external dependence, the higher the degree of disadvantage is due to sanctions. Financial sanctions are a method to restrict financial transactions with the receiving country. When comparing it to the human body, finances in modern society are like blood. The main function of blood is to carry various substances throughout the body. Finances also have the function to make the transportation of goods possible in the international community. To restrict financial transactions is to naturally restrict the transportation of goods. Therefore, it is recognized as a powerful sanction.

Financial sanctions also include investment restrictions. Sanctions against individuals are cases that restrict the travel and residency of people. They limit the dispatch of workers from abroad as well as restrict the overseas visits and stays of people from sanction-receiving countries. Conversely, they include cases in which visits to the sanction-receiving country by citizens of the sanction-imposing country are restricted as well. In this way, the types of sanctions can be classified by targets: people, goods, and the currencies that link them.

The effects of sanctions manifest in different ways depending on the economic scale and dependence of the sanction-receiving country. With regard to economic scale, the economic sanctions between the United States and China are a representative example. The US and China boast the first and second most powerful economies in the world respectively. If the US imposes trade sanctions on China, the economy of China – called the world's factory – may face atrophy. However, we cannot underestimate the disadvantages the sanctions may cause to the US as well as to the international community. Because the US-China trade war would cause turmoil in the global economy, the two countries as well as the international community are concerned about the US-China trade war. That is the reason the two countries cannot head in a drastic direction. Iran and North Korea can be mentioned as representative examples of the degree of economic dependence. Iran's economic structure depends on exporting oil and importing industrial goods. Its external dependence is extremely high. On the other hand, North

Korea's economic structure depends on exporting goods in order to import goods that are not produced or are lacking in North Korea. Thus its external dependence is extremely low. Therefore, while Iran is highly susceptible to economic sanctions, North Korea's susceptibility is relatively low.

Susceptibility to sanctions is influenced in general by the political environment within the country in question. If the political voice of the people of the country in question rises as their inconvenience grows due to sanctions, and if the government can overcome this situation, it will not accept the demands of the other party regardless of sanctions. On the other hand, the weaker the political structure to the demands of the people, the less susceptible it is to sanctions. However, because sanctions have a relative effect, the sanction-receiving country is not the sole affected body. The citizens of the sanction-imposing country may also face disadvantages due to the sanctions, which may stumble as they continue. In such cases as well, the situation is swayed by the political voice of the citizens. Overall, the reason we still cannot consistently organize the effects of economic sanctions is that it is difficult to maintain sanctions continuously because of numerous variables existing due to the interconnection of the sanction-imposing and sanction-receiving parties, internal political environments, and so on.

Powerful Economic Sanctions Against North Korea & Their Impact

The economic sanctions imposed on North Korea span all areas: trade, finance, and people. It is no exaggeration to say that the most powerful methods that the international community as a whole and respective countries can mobilize are being employed. North Korea cannot export its biggest export goods such as coal, iron, textiles, and fisheries products. These account for over 70% of North Korea's exports. Because of the export bans, naturally, imports also become difficult. The import of crude oil is restricted to 2 million tons per year. Because China, which accounts for about 90% of North Korean trade, is also participating in these economic sanctions against North Korea, difficulties in trade are on the rise.

Financial sanctions are even more powerful. Foreign financial institutions conducting financial transactions with North Korea are subject to a secondary boycott by the US. Because of this, foreign financial institutions have revoked agreements with North Korean financial institutions and North Korea cannot conduct international bank transactions. Furthermore, North Korean corporations as well as individuals of North Korean nationality cannot open accounts at foreign banks. Therefore, most transactions in North Korea must be conducted in cash, more or less making transactions impossible. North Koreans residing overseas cannot conduct financial transactions either, making trilateral transactions difficult as well.

Expat North Koreans whose primary business is intermediary trade have lost their source of income. Most North Koreans working abroad have been sent back to North Korea. Even China and Russia plan to stop reissuing most of the work visas to North Koreans after their current employment term expires by the end of 2019. Of course, new applications for work visas for North Koreans for overseas stays will not be issued either. Because of this, the number of North Korean workers returning to North Korea through China is increasing. Maritime transactions are also difficult due to elaborate monitoring. In this way, North Korea is facing international sanctions in all areas.

Due to such circumstances, North Korea's foreign trade, which had been on a steep rise since 2010, has fallen by nearly 50%. Immediately after the collapse of the Eastern Bloc in the early 1990s, the scale of North Korea's foreign trade fell drastically from about \$4 billion to under \$2 billion. The current situation is reminiscent of North Korea's serious economic difficulties following this fall. Looking at the situation in terms of numbers or chronologically, it is clearly a similar situation to that of the early to mid-1990s. Therefore, if a little more pressure is applied, there should be changes in North Korea's policies. This is the view of the US and the international community.

While we cannot conclude that it is due to the impact of the sanctions, North Korea has set out to improve its relationship with the US. Taking the opportunity of the Pyeongchang Winter Olympic Games held in South Korea in February 2018, North Korea has also started to improve inter-Korean relations. In order to impress upon

the international community the suspension of nuclear experiments, North Korea closed the Punggye-ri Nuclear Test Site and suspended the testing of long-range missiles. In June 2018, a US-North Korea summit was held in Singapore. The US and North Korea agreed to make efforts towards establishing a new relationship between the two countries. Based on this agreement, North Korea returned the remains of US soldiers. With such shifts by North Korea, an optimistic view became dominant that maximum pressure had started to influence North Korea and that its denuclearization would be achieved as long as US-North Korea relations normalized. However, negotiations broke down at the US-North Korea summit held in Hanoi in February 2019 and the situation started to change. While North Korean leader Kim Jong Un professed that he was no longer fixated on ending the sanctions, he also resumed the testing of missiles (*Chart 2*).

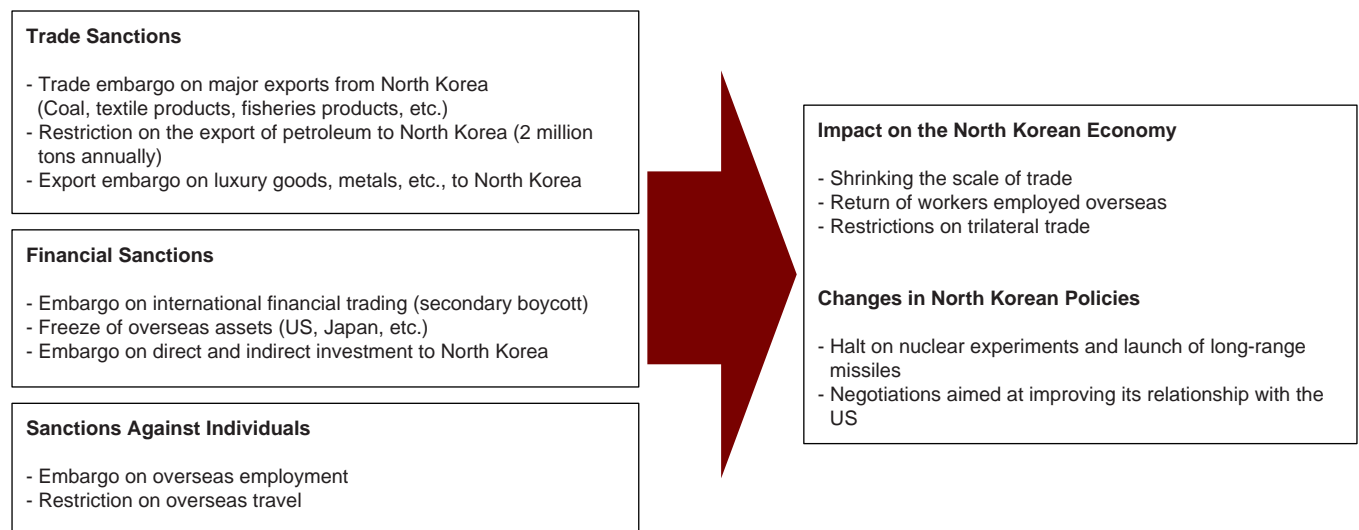
The Dilemma of Economic Sanctions Against North Korea

The international community has not eased up on economic sanctions against North Korea. Around the time of the US-North Korea summit, North Korea explored changes in its policies internally. However, an inexplicable phenomenon has emerged within North Korea. That is to say that no major fluctuation in market prices has been seen and an emphasis on self-rehabilitation has emerged once again recently.

It is widely known that in North Korea, the market became

CHART 2

Economic sanctions & changes in North Korea



Source: Compiled by the author

TABLE

Price trends in the Pyongsong Market in Jan.–Aug. 2019 (North Korean Won/kg)

	Jan.	Feb.	March	April	May	June	July	Aug.	Sept.
Rice	4,794	4,875	5,250	4,780	4,600	5,000	4,850	4,800	4,920
Corn	2,091	2,237	1,950	2,120	2,200	2,350	2,400	2,470	2,300
Soy	3,986	3,625	3,580	3,500	3,520	3,430	3,500	3,500	3,250
Cooking oil	12,150	9,387	9,765	11,000	13,500	13,100	12,800	12,600	11,100
Wheat flour	3,550	4,662	5,500	4,300	4,300	4,000	4,100	4,250	3,750
Gasoline	14,760	14,650	13,125	13,200	15,000	16,700	16,700	16,200	15,100
Diesel	8,610	8,692	8,725	8,800	9,700	9,400	9,100	8,900	8,700
Sugar	4,180	4,687	4,654	4,700	4,610	4,350	4,150	4,200	4,100
Chinese cabbage	985	965	898	1,200	1,200	1,350	850	920	950
Coal	150	175	165	170	230	190	180	180	210
Pork	14,700	15,100	18,750	17,900	17,000	8,500	9,500	14,000	16,000
Exchange rate (North Korean Won/US\$)	8,075	8,100	8,125	8,250	8,400	8,300	8,310	8,350	8,330

Source: Compiled by the author

widespread and established. Due to the amendment to its constitution, North Korea put into statutory form a socialist corporate responsible management system that in essence permits a market. This indicates just how much of an absolute position the market has in the lives of North Koreans. However, the market is starting to fall into dysfunction. According to North Koreans, they can no longer even think about new enterprises. It has come to the point that there are more people who want to sell things than people who want to buy things. The supply of goods, which provides the basis for market dispersion, was being fulfilled by Chinese-made goods. Additionally, even as many goods supplied on the market in recent years were replaced with North Korean goods as domestic production advanced – mainly food and clothing – from the supply of raw materials to final goods, Chinese goods still play an important role. However, the economic sanctions caused the inflow of goods to markedly decline. With the inflow of goods decreasing, the people who had been making money in the intermediary distribution stage fell into a difficult situation, and finally the diversity of products on the market fell. The market scale could not help but shrink.

However, market prices, which should naturally rise with decreased supply, did not show any major changes. Excluding changes in pork prices due to African swine fever (ASF) which broke out in China, changes in the price of other goods remained mostly a temporary phenomenon. This was due to withering demand, but the characteristics of North Korea's distribution structure also played a

part. For example, when importing Chinese products, the money for the products is paid after delivery. First, the products are sent to and sold in North Korea. The money is then paid to China from the sales of the products. The import price is decided before importing goods. North Korean merchants add their profit margin on to that price and sell the goods. This is why they cannot lower prices even if the goods do not sell. In the end, all they can do is return the goods to China or keep them in inventory until they sell. Most of the importers who paid in advance went bankrupt ([Table](#)).

On the other hand, the North Korean authorities are still holding up. While implementing the socialist corporate-responsible management system and field-responsibility system, the authorities have made an agreement with cooperating organizations to pay 30% of their production. However, this means 30% of the planned volume rather than 30% of the final products. So even if production decreases, the reality is that 30% of the planned volume must be paid to the authorities. Therefore, if corporations pay the government according to the planned volume, the amount they keep to eat decreases. This is the reason for the shortage of food – because currently, corporations are made responsible for the living of their workers. Additionally, in order to move forward with the large-scale projects directed by Kim, the government has implemented a quota system for each organization. Due to this, the North Korean authorities have yet to recognize the need to consider policy change. Furthermore, during the time when North Korea maintained a

planned economy, its external dependence remained around 6–7%. In recent years, its external dependence has risen to around 30%, but that is not relatively high. It means that North Korea is able to produce that much goods internally, and because the payment of planned volume is fixed there is relatively little difficulty. Looking at the situation comprehensively, the supply of goods that the North Korean authorities require is being secured by squeezing it out of organizations and citizens under the pretext of self-rehabilitation.

Next, let us look at smuggling. North Korea has been facing sanctions since the Korean War. Economic sanctions target normal transactions rather than illegal and abnormal transactions. Paradoxically, North Korea has been very familiar for a long time with international methods and routes to circumvent sanctions. A balloon effect is emerging in illegal external transactions. Because the scale of illegal transactions is expanding, North Korea has begun to receive VIP treatment in the global black market. Representative commodities are gold and human activity.

While it is difficult to estimate the scale of the black market for gold in the world, it is common knowledge that it is considerable. It is difficult to look for a breakdown of gold transactions even looking at North Korean trade statistics. North Korean gold mines are mostly controlled by the Workers' Party of Korea and the military (in principle, the Party, military, and government own a third each). North Korean bullion has long maintained transactions on the international black market, but recently it has come to the point that they have been forced to increase volume. The more the economic war between the US and China intensifies, the higher the international gold price will rise. Gold is the biggest source of foreign currency for North Korea.

As for human activity, computer hacking and arms dealing are typical examples. The US Treasury placed major North Korean hacker groups on the sanctions list, but the viability of the sanctions is unknown. While North Korea's cyberattack capabilities grow stronger on a daily basis, defensive abilities have not yet caught up. Most financial transactions including virtual currencies take place in cyberspace. North Korean hackers are the cream of the crop selected at a national level and are already recognized internationally as having considerable skills. As for arms dealing, we should consider that what is being traded is instruction on techniques provided by experts, rather than actual weapons. These are mainly related to missile technology. It is an open secret that North Korean missile experts are being dispatched to countries such as Iran and Syria. Such transactions are not conducted as normal financial transactions, but rather as various methods of money laundering. Therefore, they can circumvent the economic sanctions imposed on normal transactions.

In this way, the North Korean authorities are capable of securing the foreign currency they need through various routes. Internally as

well, they are securing goods by exploiting the people. While there are inconveniences due to the sanctions, it is not to the extent that North Korea would abandon its policies. Furthermore, it is not an exaggeration to say that there are no movements in the market to overthrow the government, which maintains a powerful centralized rule. So the sanctions do not function as pressure on the government. Rather, North Korea emphasizes self-rehabilitation and encourages the people to endure pressure from foreign powers. In fact, Kim says while giving onsite guidance that he often felt that the economy would make a turnaround as soon as North Korea's relationship with the US improved. The second US-North Korea summit held in Hanoi at the beginning of 2019 ended unsuccessfully and Kim blames the US for this. Because the market is in such a situation, the North Korean government can take an even more hardline stance against external pressure.

Additionally, the outside world has been paying close attention to the North Korean market, considering it is the driving force to change North Korea. However, a dilemma has emerged with the power of the market weakening due to the sanctions instead and the central government becoming comparatively stronger. Amidst this situation, the cost to the North Korean people and difficulties are increasing. This is the dilemma of sanctions. The aim of the economic sanctions against North Korea is its denuclearization. The choice of denuclearization is up to the North Korean authorities. However, while the power of the North Korean authorities is becoming stronger following the sanctions, the force of the North Korean market to raise a voice against the government is becoming weaker. The complete opposite of the general theory on economic sanctions – that the power of the market would grow and the North Korean authorities would face political pressure and change their policies – is occurring in North Korea. This might suggest that the strength of the sanctions imposed on North Korea should be adjusted accordingly. Perhaps we are still not at the stage to discuss the effect of the sanctions. However, in order to solve the dilemma of weakening the power of the market which should change North Korea from the inside with hardline economic sanctions, a more effective application of economic sanctions against North Korea is necessary.

JS

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Interview with Dr. Heather Boushey, President & CEO of the Washington Center for Equitable Growth

Institutionalized Income Inequality Hampers Social Mobility

By Japan SPOTLIGHT

If income inequality remains fixed due to established conventions such as inheritance or gender inequality, it would result in further diminishing equality of opportunity, such as access to good education or good health care. This would act to depress the economy structurally, as it would seriously hamper upward mobility in society. Income inequality is a hugely important issue, and economists are expected to find good methods of quantifying it.

Dr. Heather Boushey, the author of a new book, *Unbound: How Inequality Constricts Our Economy and What We Can Do About It* (Harvard University Press, 2019), president and CEO of the Washington Center for Equitable Growth, kindly responded to our questions in the following interview.

(Interviewed on Sept. 4, 2019)

Introduction

JS: Please could you start by telling us a little bit about your Center – its mission and its main activities?

Boushey: Thank you so much for reaching out to us and I am very glad to talk to you. The Washington Center for Equitable Growth was founded in November 2013, and I am one of the co-founders. It was founded to advance evidence-backed ideas and policies in pursuit of growth that is strong, stable and broadly shared. We have a unique institutional strategy: we work with academics in the United States with a large academic program that includes a call for proposals and an open and competitive grant program. We work with scholars to investigate whether and how inequality affects our economy and to explore all the different avenues. My team in Washington – which is about 40 people now – then takes that research and helps make sense of it so that it can be acceptable and useful to people who are in the policy-making community.

We have a blog, we use social media, and we do events with policy makers for them to understand what this research means for their work.

Income Inequality an Old Issue

JS: The issue of income inequality has drawn lots of attention since Thomas Piketty's book *Capital in the Twenty-First Century* was published in 2013. Yet I



Dr. Heather Boushey

think economists have been working on this issue since economics was born. Why do you think economists have traditionally concentrated mainly on market functions rather than income distribution?

Boushey: I think that there are a number of reasons. First, what Piketty and Emmanuel Saez did in 2003 (in a *Quarterly Journal of Economics* paper) was to re-introduce to economists data that they had not used for many generations. That is the data from tax records. In the US and other countries, starting in the 1960s and 1970s, economists have been increasingly reliant on survey data. When you look at how they had been

thinking about understanding the economy, it was models. Not empirical theoretical work, but theory. The extent to which it was empirical work was often using large national or sub-national surveys to get experiences. Starting in the 1990s, the profession started to undergo a significant shift where scholars began to gather their own data. They began to do natural or controlled experiments using new sources of data and information, and developing new methods that allowed them to show causality. When Piketty and Saez looked back at what Simon Kuznets had done in the mid-part of the 20th century using tax-return data, they found that inequality at the very top of the income ladder was growing much faster than that survey data had shown. That opened up expanded computing capacity and the ability to use new methods and computers to evaluate all this data. This ushered in a new way of thinking about the fact that economists can study inequality, and to see how

important this economic trend is.

Income Inequality & Politics

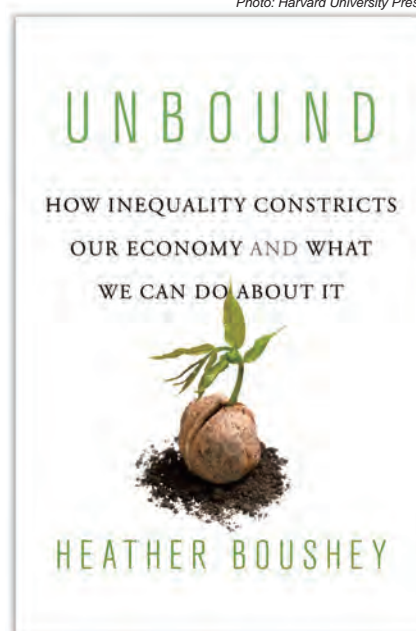
JS: Talking about politics, we are witnessing a rise in populism all over the world. Would you concur with the idea that increasing income gaps could be driving this populism?

Boushey: I think that the answer is “yes and”... Part of the reason that people are frustrated with politicians is that the way that we have thought about the economy and the way that we have talked about how to measure economic success has obscured the reality of rising inequality. This new movement of Piketty scholars and scholars that we fund who understand this – this is on the cutting edge. What most people hear about when they look at policymakers or when they watch the news is data about the economy that doesn’t reflect what is happening in their own lives. For example, on many news stations they talk about the changes in the stock market; that does not have anything to do with whether there are good jobs in your community. Or they will talk about indicators like changes in national economic growth or output, and indicators like GDP. Over the period of the 60s and 70s, GDP really was a great shorthand indicator for how the economy was growing that was reflected in people’s lives. When GDP went up by 2%, most Americans were seeing their incomes rise by 2% because we had less inequality. Since the 1980s – and especially since the rise of these new populist movements – the macro-economic indicators like GDP don’t mean anything for most of us. GDP rises by 2% but the vast majority of Americans do not see their economies rise that much. So when policy makers tout a new policy for growth or the economy, there isn’t a connection between what they are measuring and what is happening in family lives. It is not just that inequality has risen; it is that the political classes have not honored or recognized this significant change.

JS: Would you agree with Piketty’s analysis of economic inequality regarding the difference between interest rates and wage increases?

Boushey: I edited a book looking at his work, and certainly the data he has compiled is amazing and I do think it is relevant and very

Photo: Harvard University Press



Publisher: Harvard University Press
Available at: <https://www.hup.harvard.edu/catalog.php?isbn=9780674919310>

important. His argument that so long as the rate of return on capital is higher than a sense of the rate of return on wages – even in an era of high income equality – you see the income gap between the wealthy and the poor is to be further expanded by a high wealth inequality. Once you have wealth inequality, that creates obstruction and distortions in our whole economy; that wealth means that there are people holding onto that wealth rather than a society where people can get access to capital and start their own businesses or where children who did not grow up rich can go to the best colleges. I do think that this is a deep and important insight that he has regarding economics, politics and social sciences more generally.

JS: In light of today’s economic situation and rising populism, do you think that economists’ main responsibility for achieving sustainable growth should be focused on mitigating income inequality? Higher income inequality would not only lead to resolving social issues but also re-stabilizing market

economies.

Boushey: I have a book coming out next month that argues that inequality constricts our economy. I argue that high income and wealth inequality creates obstruction for people who aren't already rich to engage in the economy and move up the ladder. It particularly creates obstruction in the areas of health and education. In the US we have just had a scandal whereby parents are buying their children's acceptance into elite colleges when these entrances are supposed to be based on merit and getting high scores on exams. These rich parents were basically buying seats for their children even though they didn't qualify, which means that the children who weren't wealthy and might have been highly skilled don't have the access to opportunity. That means that the economy does not benefit from their skills and talent, so that is the way that it obstructs growth. You also see evidence of inequality in market powers across firms, and in the way that wealth inequality and income inequality affect political influence.

Both of these are subversions of how the market is functioning. We are in an era of rising economic concentration and in a way that is not for the public good but which allows some firms at the top to obliterate their competitors because they have all the market power and are able to charge higher prices, pay lower wages, and don't have to worry about providing high-quality goods and services. That is a subversion of our market economy, and at the same time you see the role of money in politics where our politics in the US has been focused on tax benefits for the very wealthy, while starving the public services that would create widespread opportunity.

Finally, we see economic inequality distort investment and consumption. There are a lot of scholars who trace the financial crisis back to the growth of inequality through the mechanism of the rising supply of credit. You have so much wealth circling around the economy looking for something to do, and what it ended up doing was to transform into increased credit supplies and too many families had credit pushed on them, which did not end well. So I do think that there are these destructive aspects of inequality that are dragging our economy down generally, and this is the theme of the book that I have coming out next month.

Institutional Drivers of Inequality

JS: You mentioned in your paper included in the book *After Piketty, The Agenda for Economics and Inequality* published in May 2017 that equality of opportunity should be assured by institutions but is not. Inheritance could affect the wealth gap between the rich and the poor, and you argue that women in the US are institutionally disadvantaged in the inheritance of wealth. Could you elaborate on this please?

Boushey: One of the things we know is that what constrain economic inequality are institutions, like governments through progressive taxation and progressive spending. Or institutions like unions that provide some boundaries on economic inequality, or institutions like a legal infrastructure that focuses on anti-trust. Those institutions have become much weaker in the US or in fact non-existent. So as the inequality rises, one thing that we learn from Piketty is that if income inequality translates into wealth inequality, then the way that people will become wealthy in our society may not be through being smart and innovative or coming up with a great idea or doing a good job at work, but rather through inheriting their fortune. I argue in my chapter in *After Piketty* that we have to think about what this means for gender equity. At least in the US, traditionally, parents give more of their wealth to sons than daughters, and marriage among wealthy elites becomes much more important. The trend now for marriage among the elites is often between two individuals who are highly skilled and earn a lot in the labor market – two lawyers or two doctors, for example. But if you have a world where wealth is transferred through inheritance, it creates an incentive for families to focus on preserving and growing their wealth through marriage, which has traditionally not been something that has led to emancipation for women. In a world where value in the economy is based on what you contribute, that creates a lot of incentive to value women and men much more equally, but in a society where wealth is created by handing down money from generation to generation, that creates a lot less incentive for gender equity.

JS: How do you think we can mitigate income inequality effectively? You highlight some

institutional drivers of income inequality and also cultural issues. How can we correct these institutional issues or cultural issues in favor of income equality?

Boushey: This is a great question. First, I think that we need to give people access to the information to understand the problem. We want policymakers to show the public what economic growth looks like across the income distribution. The first is changing the conversation from the metric of success being just GDP to saying that we need to look across the income spectrum in order to understand economic success.

Then, I think we need to craft a policy agenda that addresses the concentration of resources and addresses creating more economic opportunity. To address the concentration, a wealth tax or other ways of taxing income at the top. Addressing market concentration and ensuring that we have more competitive markets are very important. Then we need to create a counter balance in giving workers the capacity to be a counterweight to businesses in a way that unions traditionally were. I don't think this involves just going back to what unions used to do, but rather finding ways for civil society to create those counterbalances through either unions or government or community groups. It is also important to invest in universal opportunity and childcare and early childhood education in the US, to ensure that inequality is not creating obstruction to upward mobility.

Better Indicator to Measure Income Equality

JS: Finally, you mentioned that GDP might not be a good indicator to show economic performance; perhaps the indicator for income equality could be diversified? The Gini coefficient is to my knowledge the only indicator to show income inequality.

Boushey: We have done work building on research by Piketty and Saez and Gabriel Zucman, and their World Income Database where they are creating what they call distributional national accounts. These take GDP and look at what it looks like across the income distribution. Instead of just having one single data point – i.e. “GDP was 3%” – you have how much income growth occurred across the income spectrum that aggregates up to that 3%.

What inequality means is that there is a difference in income across people; but that does not tell you whether or not all the income is with people in the top 1% or if there is a huge middle class and a significant chunk of poor people. Looking at the percentiles across the distribution, it is very important that you understand what form inequality is taking because that is important for policy and politics.

Mitigating Inequality

JS: Is a wealth tax a good idea for mitigating wealth inequality?

Boushey: In a world where the vast majority of wealth is owned by a small few and where income gains are transferring into wealth concentration, a wealth tax becomes much more important than a world where you have a large middle class with a few rich people but are not that rich, and a large number of poor people. In such a society, a wealth tax might not be so important, but in the kind of inequality that we are seeing today which is growing so fast in terms of wealth distribution, that makes the case for why a wealth tax is so important because you want to open up that economy. Otherwise, we will become an aristocracy again! If you have this concentration of wealth among a small group of people, you will be soon dominated by that small group, so wealth taxes open that up, and if you use those resources to increase opportunity then you are creating a more competitive economy overall, a much more vital economy.

JS: The causes of rising inequality seem to be quite diversified among nations and so it would seem important for each country to share information regarding income inequality and how to deal with it.

Boushey: There are a lot of scholars working on this idea. The world income database is tracking inequality across countries and many of those scholars are working on understanding the differences. I couldn't agree more that this is an important goal. **JS**

Written with the cooperation of Joel Challenger, who is a translator, interpreter, researcher and writer specializing in Japanese disaster preparedness.

Interview with Dr. Mark Zandi, Chief Economist, Moody's Analytics

Income Inequality Destabilizes Business Cycle & Lowers Growth

By Japan SPOTLIGHT

What are the implications of income inequality for macroeconomic prospects? Dr. Mark Zandi, chief economist of Moody's Analytics and a distinguished macroeconomist working on economic forecasts, talks about the connections between income inequality, growth and business cycles in the following interview.

(Interviewed on Sept. 3, 2019)

Assessment of the Current Global Economy

JS: There is a lot of talk about the growing risk of a recession. How do you assess the possibility of a recession in the current global economy?

Zandi: The global economy is struggling, and global recession risks are rising and are uncomfortably high. Parts of the global economy are already close to recession. In Europe, Germany, Italy and the United Kingdom are near recession. In Latin America, Brazil and Mexico are barely growing. And in Asia, Hong Kong, Singapore and South Korea have weak economies. The escalating trade war between the United States and China and other trading partners is having a negative impact on global trade, and making the global economy vulnerable to a downturn.

JS: Do you think a trade war between the US and China is the principal reason why you consider the risk of a recession to be so high?

Zandi: Yes, I think that the trade war is doing significant damage to the global economy; not only weighing on global trade but also affecting business investment. Global businesses are very uncertain and do not know how this is going to play out, and as such they have pulled back on their investment and are turning more cautious in their hiring. There are other reasons to be nervous, such as Brexit, which could contribute significantly to the risk. Even in Japan there is a VAT increase coming that will have some negative consequences. Growing tensions in the Middle East and the impact



Dr. Mark Zandi

on global oil prices also poses a threat. But while there are many things to worry about, the trade war poses the greatest concern.

Income Inequality & Economic Growth

JS: Income inequality would seem to be one of the main drivers of rising populism around the world. How do you think income inequality affects your assessment of economic growth globally?

Zandi: The growing wealth and income inequality across many parts of the world is a corrosive on global economic growth. I do not think it is a reason for a recession this

year, the next year or the year after, but I think it weighs on the economy's long-term growth, particularly in places in the world where the income and wealth distribution is very significantly skewed. Wealthy and high-income households are able to capture the political regulatory process and change rules in their favor, and this exacerbates the existing income inequality, and such an inequality is of a structural nature.

Given the fact that the global economy is already growing very slowly and long-term prospects are for continued slow growth given demographic trends and other factors, the skewing in the income and wealth distribution means that we are more likely to suffer economic downturns and recessions. That is a real problem because there aren't effective policy tools to navigate and manage through those downturns. Japan is a very good example of this. Monetary policy is now much less effective than it was in the past, and given the heavy fiscal debt burden, there is much less capacity for fiscal stimulus, so this makes the economy much more vulnerable and

more likely to suffer periods of secular stagnation because there is no good policy response to it.

The skewing of the wealth distribution in itself is not a catalyst for an economic downturn but it certainly makes it a lot more difficult to avoid one and to navigate around a recession if it does actually hit. It is a very pernicious corrosive on long-term growth.

JS: You mentioned that in the short term, income inequality could have a limited impact, but could have a significant impact in the long term. What would the “channels” of such an impact be precisely?

Zandi: The first one is that high net worth households have the ability to capture the political and regulatory process where they do business. They can bend the rules in their favor and garner more of the benefits of government policy. So, it is more likely that they can collect the rents of protection that they receive, and these rents could increase.

This means that economic activity is not being allocated efficiently and that will weigh on long-term productivity growth and therefore long-term economic growth. This varies – in some parts of the world it is a significant problem, others less so – but as the income and wealth distribution becomes more skewed, it becomes more and more of an issue. It is very difficult to measure and quantify but is a very pernicious problem. You can see this in the industries of technology, media, telecommunications, and pharmaceuticals; these industries are dominated by very large companies that are owned by a very small number of people who do have a lot of political influence and are able to influence the government to create rules that work in their favor.

The second channel goes to the fact that the long-run potential growth of the global economy is much lower today and will be for the foreseeable future than has been the case since World War II. This is linked to demographic trends including aging populations. This affects not only the growth of the labor force but also productivity growth. So you have slower underlying growth, and the skewing in income and wealth distribution creates incentives for lower income households to take on debt leverage and greater financial vulnerabilities that make them exposed, and then when the economy goes into recession it is very difficult to get out of it because there is no effective policy response. So it is much more likely that we will see economies that are struggling to grow and to break free from these broader forces at work such as income inequality.

One final point is that it is difficult to explicitly connect the dots between income and wealth distribution and economic growth; the channels are more indirect and not as obvious as one might think.

Income Inequality & Business Cycle

JS: You also mentioned in your essay in *After Piketty: The Agenda for Economics and Inequality* published in 2017 that income inequality could destabilize the business cycle and that the debt problem in poor households would create this instability. Is that right?

Zandi: Exactly right. The crisis 10 years ago that emanated from the US was caused largely by the leveraging of lower- and middle-income households motivated in significant part by the skew in wealth and income distribution. These households had not experienced any significant increase in real incomes or wages or wealth for several decades and in the period prior to the financial crisis they had access to significant amounts of credit – mortgage debt, credit card debt, auto debt, and so forth. They took on a lot of debt and this was the main culprit for the downturn that followed. This kind of massive leveraging by households seems much less likely to happen today in the US given that in response to the financial crisis there were a lot of regulatory changes. It is now a lot more difficult for those households to take on that debt. But the risk exists in many other parts of the world – the economies where leverage has increased significantly and continues to increase significantly and in part probably due to the skewing in income and wealth distribution. Places like Australia and Canada, the Netherlands, the UK have all seen significant increases in leverage of debt and there are lots of reasons for that, but the fact that low- and middle-income households have not seen any increases in their wealth for decades may be one of the reasons.

JS: Not only poorer households, but also wealthy people seem to be depending significantly on asset prices. Would you agree?

Zandi: This is an excellent point. Wealthy households have significant assets and their spending and investment behavior is very much tied to the ups and downs in asset prices, much more so than in the past. Asset prices are highly volatile and in recent decades we have experienced significant bubbles in asset prices.

Something that also might be related to the skewing in income and wealth is that wealthier households have invested very aggressively in these assets that have appreciated significantly in value and at times into bubbles. This results in a more cyclical economy through so-called wealth effects in which high income and wealthy households change their spending behavior very sharply and dramatically in response to shifts in asset prices, including stock prices, housing values, commercial real estate values, bond prices, and so on. This makes the global economy much more cyclical and vulnerable. If interest rates are already low or negative, then the

heightened volatility in the economy is much more dangerous as it makes it much more likely to fall into a recession and harder to get out of one.

JS: With regard to the impact of income inequality on the business cycle and long-term economic growth, could there be some differentiation among developed economies?

Zandi: The skewing of the income distribution varies substantially across the globe, and indeed has become less skewed among developing economies in recent decades. Globalization has lifted hundreds of millions of people out of poverty; China is the best example as the wealth and income distribution has become much less skewed. In the developed world, and in particular in countries like the US and European economies, income and wealth distribution has become much more skewed as a result of the globalization process. The US is probably the best example of the skewing in income and wealth as it is much more unlikely to use government policy to redistribute income and wealth. In many European countries, there are very progressive tax codes – wealth and estate taxes that work to mitigate the skewing of income and wealth, but much less so in the US. That may change; a lot of the presidential candidates on the Democratic side are focused on this issue and want to increase wealth taxes and mitigate the distribution in income and wealth, but as of now this is not the case, at least not as much as in Europe, Canada and other developed economies.

Differentiation of Income Inequality Among Nations

JS: Do you think that income inequality in the US has been expanding and diminishing in Europe?

Zandi: It has been widening – the skewing has becoming more significant in the US and to a lesser degree in the rest of the world. If you consider government policy, taxes, benefits and other forms of public support, the skewing of the distribution is less pronounced everywhere, but much less so in Europe and Canada compared to the US. But even in Europe you can see there is a lot of tension among lower-income households, and a lot of this has fueled the populist movements there.

JS: Income inequality is different between developed and developing nations. In the case of developing nations, income inequality is emerging as a “middle-income” trap; the shrinking middle class in developing countries could hamper long- or mid-term economic growth. How do you evaluate the different

consequences of income inequality upon developing and developed economies?

Zandi: In general, in developing economies the distribution of wealth and income has become less skewed over the last quarter of a century, but that goes to the benefits of globalization on those economies. They have been able to reap the benefits of that globalization and have helped to lift everybody in their economy but in particular low-income households in the last few decades. At the same time, that is why lower- and middle-income households in the developed world have struggled, because they lost incomes, wages, and wealth to the developing world due to the globalization process, among other factors. Technology has also played a role in enabling globalization, but also the adoption of new technologies has been most pronounced in the developed world and that has significantly impacted lower- and middle-income households. This has been ongoing for much of the past half century.

Having said this, the impact of globalization on income and wealth distribution is about ready to turn, especially if the world doesn't pull away from globalization. Because of globalization, many developing economies now have large and quickly growing middle classes who are beginning to buy many of the high valued-added goods and services produced in the developed world. The developed world is on the cusp of selling much more to the developing world, which will create many jobs and ultimately work to reduce the skewing in income and wealth. It would be a dark irony if the developed world turned away from globalization now, just when globalization was set to benefit everyone, including lower income and less wealthy households.

JS: If China is suffering from the middle-income trap, its consumption would not grow so significantly and this would impede its economic growth, wouldn't it?

Zandi: Yes, it would and I think they realize that and are trying to address it. One potential solution to that problem is to strengthen their social safety net. Unlike many developed economies, they have very little in the way of retirement benefits or healthcare benefits or unemployment benefits, and therefore the population has to save a lot and does not spend very much; consumers and households bear all the risk. I think the Chinese understand that they need to harden their social safety net to address the problem and I believe they have been moving in that direction for the last decade. China is symptomatic of this problem in many developing economies.

Income Inequality & Policies

JS: Do you think this income inequality is the main driver of increasing populism today?

Zandi: It is a very significant factor, as lower- and middle-income households have not seen their wages or wealth increase for many decades. They now feel helpless and are worried that their children are going to do worse than they are financially and they are very upset by that. On top of that, massive global migration flows make them very nervous because they worry that immigrants will take their jobs and their incomes. So the combination of the skewing of income and wealth distribution and the very significant flows of people across borders has fuelled the populism that is evident across the globe, particularly in developed economies.

JS: Do you think that the capacity of the current fiscal and monetary authorities is good enough to stabilize the economy and business cycle by mitigating income inequality?

Zandi: I worry about it; I am not sure that policymakers are up to the task. I might have had a different view several years ago, but now I worry that populism is overtaking the political process and the resulting policy response is wrong-headed. Anti-globalization sentiment is not to anyone's benefit and will hurt everybody from the top to the bottom of the income and wealth distribution. We are also underinvesting in educating, training and re-training the workforce and we are not building the public infrastructure that is needed for economic development, especially in poor areas. I worry that policy is not moving in the right direction. On top of that, the fiscal health of many countries is deteriorating, reducing the resources available to address the skewing of income and wealth.

The political capacity for governments to address the income and wealth distribution is also eroding. Populist sentiment is overtaking the political process and we are unable to collectively deal with these serious problems and as such they are becoming self-reinforcing. I am as pessimistic about this as I have ever been, and I'm not at all sure we are going to be up to the task globally to address this problem. Something has to shift fundamentally before we can address these problems in a meaningful way.

JS: You mentioned tax policy and regulations in order to mitigate income inequality. Assuming that our government has serious constraints on fiscal and monetary policies, what kind of tax policies would be necessary to mitigate income inequality?

Zandi: In the US, there is increasing attention to the possibility of increasing existing estate taxes and implementing new wealth taxes on those at the very top of the wealth distribution. The tax revenues that would be generated would be used to finance policies that support lower- and middle-income households, including more affordable housing, increased childcare and health care, and greater

educational opportunities. There are many open questions regarding the efficacy of wealth taxes, as these households have significant means to avoid paying them, but increasing thought is being put into how to design these taxes to address these issues. Other types of taxes being debated to address income and wealth inequality include carried interest taxes on private equity firms and financial transaction taxes. Finally, increasing the income threshold for the payroll tax that funds the nation's retirement system is also a possibility. The effective tax rate on high income and wealthy households is generally much lower than in other parts of the developed world.

JS: In the future, do you think it would be necessary to create a macroeconomic model taking income inequality's long-run impact on the economy into consideration?

Zandi: Yes, macroeconomic models need to catch up to the growing chasm between the wealthy and the poor in many parts of the world. Until recently, most macroeconomists, at least those focused on the economy's prospects, have all but ignored inequality in their thinking. Their implicit, if not explicit, assumption is that inequality doesn't matter much when gauging the macroeconomic outlook.

This is a mistake, as inequality makes the financial system less stable, as credit-constrained low-income households are potentially significant risks, and the economy more cyclical, as wealthier households that account for the bulk of the spending are sensitive to swings in increasingly volatile asset markets. This may not be a big deal if financial markets and the economy move in a more-or-less straight line, but it could be a huge deal if they don't.

This is especially true given that the economy's potential growth will be much slower going forward than in the past, suggesting that recessions will be more likely. With monetary and fiscal policy almost certainly rendered more impotent by the zero lower bound and tighter political fetters, future recessions could be more severe.

A critical lesson of the Great Recession is that recessions do permanent damage to the economy, diminishing its potential. Few, if any, macroeconomists have models that account for this in their long-term projections. Macroeconomists should thus not be comfortable that they have a good grip on what inequality means for our economic prospects.

JS

Written with the cooperation of Joel Challender, who is a translator, interpreter, researcher and writer specializing in Japanese disaster preparedness.

C ompanies Have a Crucial Role to Play in National Security

By Elisabeth Braw



Author Elisabeth Braw

How Companies Are Targeted in a Cyberattack

Immediately after the United States killed Iranian general Qasim Soleimani on Jan. 3 this year, the warnings began arriving: Iran would retaliate by attacking US companies. It would not be the first time Iran has attacked a US business: today the private sector is increasingly a target as countries compete for geopolitical power without having to go to war against one another. But companies shouldn't simply consider themselves victims. On the contrary, they have a crucial role to play in national security.

Six years ago, unknown hackers inserted malware into the computer networks of Las Vegas Sands Corp., the world's largest gambling company. It was a sophisticated attack that brought down three quarters of the casino's servers; restoring them cost more than \$40 million. US authorities subsequently established that hackers working for the Iranian government had perpetrated the attack. Las Vegas Sands Corp. belongs to Sheldon Adelson, a controversial businessman and ardent supporter of Israel (and subsequently also of President Donald Trump). Four months before the cyberattack, Adelson had publicly proposed that the US should detonate a nuclear bomb on Iran.

History of Private Sector Being Targeted

The attack against Adelson's gambling empire was an early example of how companies are targeted as countries compete for global power. For centuries, civilians and subsequently also businesses have been targeted as tribes, principalities and countries went to war against one another. Such attacks were simply part of the warfare. The Geneva Conventions, passed between 1864 and 1949, subsequently introduced rules protecting civilians. Companies, however, remained targets in armed conflicts. During World War I, for example, Britain's Royal Navy – aided by France and Italy – blockaded all vessels bearing commodities for Germany and its allies. During World War II, “more than 12,000 mines were laid [by the US] in Japan's shipping routes, territorial waters, and ports as part of Operation Starvation. These mines sank or severely damaged 670 Japanese ships and strangled maritime commerce,” as Commander Timothy McGeehan and Commander Douglas Wahl (Retired) of the US Navy note in the January 2016 Proceedings of the US Naval Institute. And during World War II, Britain and the US controversially firebombed Dresden, a city with minimal military

value, reducing its companies along with its buildings to rubble. Nazi Germany, for its part, forcibly expropriated companies from owners (often Jews) in countries it had occupied.

What is different today is that companies are being attacked even though no war has been declared. Consider the findings in the 2019 Cyber Readiness Report by insurer Hiscox. Last year 61% of businesses in Belgium, France, Germany, the Netherlands, Spain, the United Kingdom and the US reported having been subjected to a cyberattack in the preceding 12 months, up from 45% in the previous year. Troublingly, an even higher percentage (65%) reported having experienced one or more cyberattacks as a result of a weak link in their supply chains. (This is the first time Hiscox included supply chains in its Cyber Readiness Report.) In addition, businesses are increasingly subjected to repeated cyberattacks. “In every one of the 15 sectors tracked in this report, the proportion of firms reporting one or more attacks has risen sharply. Across all seven countries, the most heavily targeted sector was TMT [technology, media and telecom], where 72% of respondents reported one or more attacks, up from 53% a year ago. Government entities came second (71% reporting an attack, up from 55%), followed by financial services (67%, up from 57%),” Hiscox reports.

Britain's 2019 Cyber Security Breaches Survey, in turn, says that 32% of businesses and 22% of charities report having experienced cyber security breaches or attacks in the previous 12 months. Medium-sized and large businesses are the most affected at 60% and 61% respectively. While the number of attacks has decreased, that does not mean that aggression is abating. The UK Department for Digital, Culture, Media and Sport, the publisher of the Cyber Security Breaches Survey, suggests that one possibility “is a change in attacker behaviour, with more attacks being focused on a narrower (though still numerous) range of businesses”.

Not all of these cyberattacks are, of course, linked to governments – but many are. The Council on Foreign Relations, a New York think tank, maintains a database of state-linked cyberattacks (including cyberattacks linked to Western governments). In April last year, for example, German pharmaceutical giant Bayer reported having been attacked by Wicked Panda, a Chinese hacker group linked to the Chinese government. According to cybersecurity firm CrowdStrike, the group's tools have been traced to “contractors who count multiple Chinese government agencies as clients, including the Ministry of Public Security. Observed targeting by the Wicked Panda adversary has focused on high-value entities in the engineering,

manufacturing and technology sectors, aligning with the PRC's strategic economic plans." A plant chlorinating Ukraine's water – a critical function – has been targeted by hackers working for Russia. An Iranian hacker group referred to as APT33, Refined Kitten or Holmium has managed to interfere with the operations of target companies such as power plants rather than simply disrupting them as most hackers do.

Other Forms of Aggression Against Businesses

Businesses are subjected to other forms of aggression as well. Last July, the UK-flagged, Swedish-owned freighter *Stena Impero* was seized in the Strait of Hormuz by commandos from Iran's Revolutionary Guard; initially Iran maintained that the freighter had violated international rules but later stated that the seizure was a response to Britain's seizure of an Iranian oil tanker suspected of carrying oil to Syria earlier that month. Following the *Stena Impero*'s seizure, insurance costs spiked.

Executives worry, too, that disinformation campaigns by governments hostile to countries where they are based or have significant operations could harm them. Imagine, for example, a successful disinformation campaign by Country A against Country B, where Company X is based. By spreading false information about the stability of Country B's government, Country A can – for example – fuel a run on Country A's currency, thereby causing significant harm to business including Company X.

Businesses are, in other words, being targeted and harmed by other countries and their proxies not because any country is pursuing vendettas against them specifically. Instead, they are being attacked as a way of weakening the country or countries they represent. The *Stena Impero* was seized not because the government of Iran wished to harm it or its Swedish owner Stena Bulk, but to protest at the seizure of the Iranian freighter by the UK. In addition, the seizure can be seen as a protest against the Trump administration's campaign against Iran and the Joint Comprehensive Plan of Action (JCPOA), better known as the Iran nuclear deal. By seizing the *Stena Impero*, Iran indicated that it could make the Strait of Hormuz unsafe for international commerce if it wished to do so. That would constitute a severe blow against companies dependent on the shipping route, and against a number of countries likewise dependent on the route.

Challenges for Companies Targeted by Foreign Governments

The reality that companies can be – and are being – targeted as

proxies poses a challenge, because virtually no business can defend itself against a nation-state. Even though rare ones might conceivably do so, the law bans private actors from engaging in offensive action against another country, a necessary requirement for credible defence. In the area of cyber, for example, a business is allowed to defend itself but is not allowed to strike back against its attacker through cyberattacks of its own. Nor are businesses permitted to conduct preventive attacks against individuals or groups it suspects of planning a cyberattack. Offensive cyber action is the domain of governments, and with good reason: through offensive attacks, businesses could escalate conflicts with a foreign government to the point where their home government would have to step in with military means.

Nevertheless, it is clear that the current arrangement, where governments are solely responsible for national security, is not appropriate for an era in which aggression is not only of a military nature. It is also in everybody's interest that a country – especially a liberal democracy, which is by definition vulnerable to aggression due to the open nature of its society – is able to minimize disruptions to its society. If hostile attacks result in repeated and extensive disruption, it will not only harm current business activities in that country, and the public along with it. It will also harm the country's standing as a safe place to conduct business. Businesses, in other words, have a role to play in national security.

Expected Role of Business in National Security

It may seem like a novel concept. Indeed, it is. Businesses played a role in national security in previous wars, including World War II, and defence contractors by definition still do so. Today, however, companies of all kinds can play a role in national security. Indeed, Western governments are too small to span a protective umbrella over the entirety of their civil societies – and their doing so would be neither affordable nor desirable for their societies.

But which role should businesses play? During the Cold War, the Nordic countries developed so-called "Total Defence" models that can provide lessons today, even though the threats during the Cold War were rather different from those affecting liberal democracies today. Total Defence was created by Sweden during World War II, when it was neutral and was faced with the overwhelming force of Nazi Germany. Sweden further developed its Total Defence during the Cold War, and Denmark, Norway and Finland too developed Total Defence.

As part of Total Defence, the Swedish government maintained close contact with companies considered of vital importance – including the Stockholm Stock Exchange, the postal service, the

telephone company and the railway company, but also Volvo and Saab – so that the country could keep functioning in a crisis. These companies, known as K Companies, were obliged to keep operations going during a crisis, and key staff were exempted from military service to guarantee that continuity of operations. In some cases, such as with Volvo, Saab and arms manufacturer Bofors, the government subsidized the construction of manufacturing facilities inside mountains, which would protect the companies' production against enemy attacks. Sweden largely dismantled Total Defence during the early 2000s, but is now rebuilding the system, albeit not to its Cold War size.

As part of its Total Defence model Finland has, in turn, perfected the National Defence Course introduced by Sweden in the 1950s. The course, an invitation-only three-week residential course (with subsequent refresher courses) in national security for emerging leaders in politics, business, civil society and the armed forces, is highly sought-after. One of its outcomes is that the Finnish business elite are well-informed about national security and take it into account in their activities.

During the Cold War it was, of course, helpful that many of the companies were government monopolies and thus at liberty to adjust their operations to the government's needs. As the involvement of Volvo, Saab and Bofors show, however, it was possible to get privately owned businesses competing on the global market to play a role in the country's security. To be sure, the Swedish government was able to appeal to the executives' sense of patriotism; at that time, all major Swedish companies were led by Swedish citizens, just as most major companies in other countries were led by nationals of the respective country, and the companies were not owned by an even larger foreign entity.

That is different today. In many countries, leading companies may be ultimately owned by a foreign entity; Volvo is, for example, owned by the Chinese automotive giant Geely. Indeed, even if a CEO feels that he or she has a responsibility to contribute to the security of the country in which his or her company is headquartered, such steps may not sit well with the foreign-based owner of the company. Furthermore, businesses worldwide are now led by the MBA generation, which excels at management and financial matters but has little understanding of national security. Some new market giants even take apparent delight in being as remote as possible from the governments of their home countries: consider Facebook's refusal to provide the US Congress and government with anything more than minimal information about the company's contacts with Russia during the 2016 election campaign.

At the same time, it is in businesses' interest to help keep the countries in which they operate as free as possible from disruptions

to everyday life, and free from disinformation that can harm investor confidence in the country and thus the country's economic performance. Finland's National Defence Course would be a good starting point for other liberal democracies. The course provides an ideal vehicle for the government to teach emerging leaders (including, crucially, business leaders) about the foundations of the country's national security and the threats facing it, and the refresher courses allow the government to provide information about new and emerging national security challenges. Furthermore, the course builds a network of rising leaders, who are likely to interact and consult with one another throughout their careers.

Government & Private Sector Collaboration for National Security

Governments of liberal democracies would also do well to regularly invite chief executives, especially of companies in strategic sectors such as telecoms, transportation, electricity, food and waste, to regular consultations, providing them with updates on emerging threats and the national security situation more generally. If those invited were given security clearance, such briefings could include classified information. The provision of regular national security updates by the government would allow business leaders to consider their operating environment in a more comprehensive context than what they are able to read in newspapers and reports from risk consultancies.

That does, of course, not automatically mean that they will alter their decision-making in a way that benefits national security. It does, however, mean that they have a better understanding of national security when making corporate decisions. One should bear in mind that in most liberal democracies, businesses today are not just led by the MBA generation but by a generation that has for the most part had minimal interaction with national security. By contrast, major American firms in the 1960s and 1970s were, for example, often led by men who had served in World War II, and almost all Nordic business leaders had performed military service.

Another step that ought to be considered is incentivizing companies in strategic sectors to play specific roles in support of national security, for example to develop comprehensive contingency plans. Today services that were mostly government-owned until the end of the Cold War (primarily telecoms, airlines, water, electricity and railways) have for the most part been privatised. In most sectors, a number of smaller companies now operate side by side, often as competitors. Companies agreeing to take on a role similar to Sweden's Cold War K Companies could receive government subsidies covering the additional expenditures. Alternatively, or

additionally, they could be awarded special government recognition akin to the Royal Warrant label used in monarchies, which would identify them as “best in class”.

A chief executive may, of course, still decide that involvement with national security is not a net benefit to the company. Indeed, with large companies operating globally he or she might decide that contributing to the national security of the large Western country where the company has its headquarters could harm its access to other markets. This freedom of business leaders to make decisions based solely on how they will benefit their company, not the country in question, is one of the weaknesses of liberal democracies. By contrast, in authoritarian countries such as China the government can command even officially private companies to perform specific activities or work in close collaboration with the government.

Legislation could solve this problem. It is, however, a blunt tool, and once a new law is in place, those affected by it tend to respond by only meeting the minimum requirements. A mix of limited legislation and engagement with business leaders, by means of consultation and national-security training, could therefore be the most productive way forward. It would build on business leaders’ desire for their companies to operate in stable environments and include government consultations to help inform their decision-making in a way that would benefit the country and by extension their companies. Because government should not favor one company over another, it would be important for the consultations to be open to chief executives of all major players within each strategic sector, the only requirement being that they should have security clearance.

Corporate Ownership Laws Could Play Significant Role

One additional aspect is of great significance: corporate ownership laws. Because even major companies are today not often independent but owned by even larger foreign entities, and because that restricts their executives’ freedom of action in the area of national security, liberal democracies should consider their rules for foreign ownership. Although most liberal democracies have legislation restricting foreign ownership of strategic companies, those rules are mostly limited to defence contractors and are remarkably permissive. In the UK, for example, between 2002 and 2018, the government only intervened in eight business transactions on national security grounds. There is, however, movement towards more restriction. In 2018 the US imposed stricter rules through the Foreign Investment Risk Review Modernization Act (FIRRMA). The same year, Germany lowered the ownership stake at which foreign

investments in strategic companies require government approval, from 25% to 10%. Also in 2018, the UK government presented a white paper which proposes government approval for acquisitions of over 25% in business selling “strategic goods”. The UK government estimates that such rules would lead to some 200 applications for approval each year.

Although similar developments are underway in other liberal democracies, the question is whether such tighter rules go far enough. Should there be an outright ban on foreign ownership of companies in strategic sectors, or would that harm the vibrancy of the global market on which companies in Western countries depend? It is worth remembering that China imposes severe restrictions on any kind of foreign companies operating in the country.

Conclusion

The prosperity of liberal democracies from Japan to Canada depends on the success of the market. Despite the messiness of a free and open society, during the Cold War the US outshone its rival, the Soviet Union, measured by standard of living. In 1989, the GDP per capita in the Russian republic within the Soviet Union was \$3,428 (measured in current US dollars), compared to \$22,857 in the US. Japan, no stranger to geopolitical aggression, performed better still, with a GDP per capita of \$24,813.

The challenge, as has been outlined in this article, is that today’s national security threats can – and do – directly harm companies. Not every proposal put forward in this article can be adopted by every liberal democracy. Each government can and should, however, urgently consider how it can involve its private sector in national security – whether simply by information-sharing or by also incentivizing companies to play an active role in minimizing disruptions to the country in case of a cyberattack or indeed another type of attack.

The former, of course, informs the latter: business leaders of companies in strategic sectors who properly understand national security challenges are more likely to be willing to commit their company to national security-related moves that an executive focusing solely on the next quarterly report would dismiss as a distraction. The equation boils down to one fundamental reality: because businesses today are targets of geopolitical aggression in a way they have not been in the past, it is unquestionably in their interest to do their part. They just have to be given the opportunity to do so, and the framework for collaboration with the government. **JS**

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Interview with Teruo Asada, former Chairman & Executive Advisor of Marubeni Corporation

Japanese Business Leader Is Cautiously Optimistic About the Global Economy

By Japan SPOTLIGHT

Think tank people are concerned about the possible harmful impact of the US-China tech cold war if it is prolonged on the world economy and trade. How does the business world view this? While think tank views are theoretical and have a macroscopic perspective, businesses tend to be more practical and focus on tangible effects.

Teruo Asada, former chairman and executive advisor of Marubeni Corporation, one of the largest Japanese trading companies, kindly spared time to respond to our questions on this issue. The views of a big trading company's representative are of great interest given the current turmoil in global trade and the possible impact upon global supply chains.

(Interviewed on Dec. 13, 2019)

Current State of the Global Economy

JS: I suspect that a prolonged US-China tech cold war will have a strong negative impact on the world economy. Many economists think the US economy is still in an expansionary stage at this moment, but I think a prolonged trade war would seriously harm the US economy, the Chinese economy and eventually the global economy. What do you think about the outlook for the world economy if this trade war continues?

Asada: In the light of the current business situation, I do not think the global economy will fall into a recession, as it did after the Lehman Shock in 2008, though it may slow down to a certain extent. I believe in the strength of the US economy. The US-China trade war would strengthen the need for restructuring global supply chains, which could lead to rising production costs. Tariffs are also rising, and developed nations are suffering from a labor shortage. Under such circumstances, in 2020 world economic growth will be slightly lower than in 2018 or 2019.

The US economy and Chinese economy will be negatively affected by the trade war. In particular, the Chinese economy would fall into difficulty due to a continuous decline in exports for the past two years. However, both the United States and China can still afford to implement active monetary and fiscal policy to stimulate their economies. I visited the United Kingdom last December just before the general election that determined the direction of Brexit on behalf



Teruo Asada

of the chairman of the British Market Council, a private organization aimed at promoting Japanese imports from the UK and supporting Japanese companies interested in setting up offices or factories in the UK. I talked with opinion leaders there and I was impressed by the robustness of the UK economy. It will not be in any serious difficulty due to whatever may happen after Brexit.

What I am most worried about is the Japanese economy. Japanese interest rates have already reached below zero and there will be little room to lift the economy by monetary policy. Our public finances are in the worst condition, with tremendous accumulated debt. There is also very little room for stimulating the economy by fiscal

policy. It is certainly true that the Japanese economy has been enjoying its longest expansion in the postwar period, lasting many months. But this can be considered as a consequence of the continued monetary easing policy so far and not of a consolidated growth strategy. I am particularly concerned about the delayed implementation of a growth strategy for raising industrial or national competitiveness by structural reform, compared with the rest of the world.

Overall, I think the world economy, including emerging economies and those of ASEAN nations, will not get into a serious recession, although there could be a tentative slowdown in 2020.

Japanese Business Suffering from Power-Based International Politics

JS: I guess there might be cases where Japanese business interests would be seriously harmed in

power-based global politics without rules. What do you think about this possibility?

Asada: I am not worried much about it. I participated in the Annual Joint Meeting held by the Japan-US Southeast Association and Southeast US-Japan Association as a chairman of the Japan side in October 2019 in the state of Georgia. This meeting regularly attracts the attendance of state governors and business leaders from the seven southeastern states in the US (Alabama, Florida, Georgia, Mississippi, North Carolina, South Carolina, Tennessee) and Japanese business leaders. At the meeting I raised with the seven state governors the possibility of Japanese business being negatively affected by the decision of the Committee on Foreign Investment in the US (CFIUS) to reject foreign direct investment (FDI) due to national security concerns.

Many Chinese companies today are finding their FDI in the US rejected. Our concern is that Japanese business could be involved in such US-China friction in the future. For example, if a Japanese company, in partnering with high-tech Chinese companies, is trying to invest either in the US or other countries, there would be a possibility of the US opposing it. Particularly in the case of large-scale investment either in the US or other nations, I thought there could be great concern about its being refused by the CFIUS. But, after having talked with the governors, I found it is quite unlikely that Japanese companies would be involved in any such trouble and they would neither suffer any serious loss nor would any new business be difficult to start.

I was also surprised to see in this meeting that the trade imbalance between the US and Japan was not an issue for discussion anymore. The largest bilateral trade deficit of the US is now with China, followed by Germany and Mexico. Japan comes next. The US-Japan trade imbalance or trade issues do not matter much anymore for the people in the US. There is also the fact that Japanese FDI in the US has worked well in convincing US states of its utility and this has lessened trade friction between the two.

Some 1,500 Japanese companies have invested in the seven southeastern states and created around 200,000 new jobs there. The investment balance in those states amounts to more than \$40 billion, while the investment balance overall in the US is around \$400 billion. This is greatly appreciated by local communities and I believe this is the best example of the win-win relations achieved by the US-Japan partnership since the 1970s.

As a business person who has worked for a trading company for many years, I believe that business is based upon human relations. That is an important lesson for us. Having seen such good human relations built up between the US and Japan, I think there will be little risk of Japanese business being hampered by the CFIUS decision, though the risk is not zero.

Rules-Based Trade Regime

JS: Even with little possibility of Japanese business being affected negatively by power-based international politics, would it not be better to have a rules-based trade regime that ensures free trade and

investment?

Asada: Yes, but it is difficult. The WTO's rule-making function has stopped working and even its dispute settlement mechanism has been seriously hampered by the lack of a majority among the seven members of its Appellate Body tasked with making a final decision on the relevancy of the dispute panel report. Can Japan take the initiative in reconstructing trade and investment rules? I think there will be a greater role expected of Japan in rule making for IPRs and national security-related issues. However, I am skeptical about Japanese leadership in WTO reform or in founding a new trade regime to replace the WTO. The US is a self-sufficient nation, as it can provide energy and food necessary for domestic use and survive even with its markets closed, though that could negatively affect the economy in the long run. How can Japan lead the US to a rules-based global regime?

President Donald Trump is doing well in having China accept a tentative agreement to modify its aggressive foreign economic policy by his tough countervailing policy. No other person could have earned such a gain from China. The US economy is still in good shape. The trade war is not significantly harming its economy at this moment.

Meanwhile, Japan is certainly doing well in having concluded the recent trade agreement with the US. I believe these provide good bilateral rules. But as for global rules, I think it will be questionable for Japan solely to create them on its own initiative or leadership.

JS: It may be difficult for Japan to create a global trade regime, but it would be possible to make regional trade rules like the TPP among Asia-Pacific nations.

Asada: Yes, that is true. Japan's contribution to mega-regional FTAs is significant, as shown in the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) which should have been even better with the US joining it, the EU-Japan EPA, and the trade agreement between Japan and the US, as mentioned, which stays largely within the framework of the CPTPP. Another mega-regional FTA, the Regional and Comprehensive Economic Partnership (RCEP), will be concluded with India's agreement soon. I think such regional FTAs can be achieved by Japanese leadership, and taking the initiative in concluding such regional trade rules will be a crucial role in the future for Japan, but the WTO or other worldwide trade regimes possibly replacing the WTO will be difficult to achieve only by a Japanese initiative.

JS: In such rule-making, economics and national security are increasingly discussed simultaneously. METI has recently set up an office focusing on the interrelations between the economy and national security. The recent revision of the Foreign Exchange and Foreign Trade Act in Japan, imposing restrictions on FDI over possible harm to Japanese national security, is one example of how economics and national security are closely related.

Asada: If national security concerns become too great they would push Japan into a contradictory stance on free trade, which it has been advocating until now. This could lead to many sanctions and we cannot deny any possibility of the global trade regime moving towards anti-liberalization. The revision of the Foreign Exchange and Foreign Trade Act could also provoke friction between Japan and the investing countries, even with a very small amount of FDI. Of course, Japan should respond to concerns about national security in balance with economics, as is the trend today. But it is necessary to bear in mind that excessive policy intervention based on concerns over national security could be disastrous.

JS: Australia and Japan seem to share the concern about the balance between economics and national security and agree that they should be discussed simultaneously. I think they can be good partners in this regard. Both nations play a key role in APEC. APEC could be a good venue for discussing economics and national security, assuming that the WTO does not work well. It would not enforce any obligation upon member countries but there would be peer review pressure on them. This would make it easy to achieve a consensus among member nations.

Asada: Unfortunately, the US is not paying much attention to APEC. Trump is not interested in attending multilateral forums, as he prefers bilateral discussions and negotiations. It is certainly a good venue for discussion, but I doubt if APEC would be the venue where new international rules are adopted.

Coping with Other Rising Geopolitical Risks

JS: Besides the US-China tech cold war, there are other geopolitical risks, such as Iran or North Korea. How does a trading company in Japan like Marubeni prepare for them?

Asada: Japanese trading companies have been pursuing business opportunities despite the wide range of geopolitical risks. We have been doing business with our partners and clients in close relationships for a long time under such risks. We would also pursue business opportunities in other countries and communities with Chinese companies even with the risks that may entail, if such business could bring those nations or communities invaluable benefits.

I believe that trading companies must continue their win-win business with their partners, while bearing in mind existing geopolitical risks. Of course, it would be thoughtless to continue business without any risk management policy. We trading companies have developed good risk management strategies for each country based on our knowledge and wisdom acquired from long worldwide business experience.

When there is any large-scale conflict in the world or a need to think about specific emerging risks, we rethink and revise such risk

management strategies on our own. Our company, through such a process, has developed our own ranking of country risks and country ratings and we define the limits of exposure to transactions with a specific country based on that ranking. We must also think about the means of hedging those risks while developing risk management.

We have been working with Japanese public agencies, such as the Japan Bank for International Cooperation (JBIC), Nippon Export and Investment Insurance (NEXI) and the Japan International Cooperation Agency (JICA), in financing our projects for hedging risk. Also I believe that working with international organizations such as the Multilateral Investment Guarantee Agency under the World Bank, which has long experience in Africa, or the IMF in terms of co-financing would be important in avoiding political and/or credit risk. Such a risk hedging strategy would be a product of our trading companies' wisdom born of our business experience.

Private Business Involvement in Rule-Making on Economics & National Security

JS: In rule-making on economics and national security, would we need to involve more private business people's views in policy discussions and formulation? For example, it is often said that there are some sensitive technologies which could harm national security. It might be only private businesses that could identify exactly what these technologies are.

Asada: Yes. Having participated in various meetings of advisory boards to Japanese government ministries, I found there were very few business people among the members, while there were many academics and economists. The arguments of the academics and economists were too theoretical and conceptual because most of them do not have actual business experience so that they are not fully aware of the real problems which businesses face.

I think the Japanese government should create more venues for policy discussion with private business people who are engaged in actual business and knowledgeable about business realities. They should take full account of those business people's views in policy formulation. Not only trading companies but also manufacturing companies or IT business should be more involved in exchanges of views on the economy and business with the policy makers in the government.

I think such dialogue between the government and private sector in Japan would strengthen the capacity of Japanese policy decision making and thus encourage Japanese leadership in global governance. I sincerely hope that such strengthened Japanese leadership can lead the world economy to better globalization. **JS**

Written with the assistance of TapeRewrite Corporation.

Interview with Phillip O'Reilly, Chairman of BIAC

OECD's Business & Industry Advisory Committee Could Contribute to Achieving Rules-Based Global Economy

By Japan SPOTLIGHT

Multinational companies, which are great beneficiaries of globalization, must have a strong incentive to stop any moves toward deglobalization and restore global governance for rules-based trade and security to prevent the US-China tech cold war from causing damage to the global economy. How can business lead this process in public policy decision-making? The Business and Industry Advisory Committee (BIAC) has long experience of playing an advisory role to the OECD in public policy and international rule-making discussions. We interviewed BIAC Chairman Phillip O'Reilly to discuss this issue.

(Interviewed on Jan. 10, 2020)

Introduction

JS: Could you give us a brief self-introduction and tell us a bit about your company?

O'Reilly: My name is Phillip O'Reilly, I am a New Zealand national. My role is chairing BIAC, which is based in Paris. I have a staff of 10-12 people, and I have chaired it for the last six and a half years now, and have been on the board for a bit longer. BIAC is the formal business partner of the OECD, set up a year after a trade union advisory committee was set up, so it's a tripartite structure. While we are technically part of the OECD, we are very independent and offer an independent advisory source. We have a number of observers from countries that maybe will join the OECD on the accession pathway, and have a number of other technical/international organizations – for example, on chemicals and banking – that also join BIAC because of the particular work that the OECD does. The core members are the business confederations, and in Japan of course that is the Japan Business Federation (Keidanren).

My company in New Zealand is called Iron Duke, based in Wellington. I used to run Business New Zealand, which is the equivalent of Keidanren in New Zealand. After 11 years of being CEO there, I left and formed this organization which is a public policy advisory firm. It's a commercial firm, and we have clients in central government, local government and in the private sector both in New Zealand and overseas. We are attempting to get to good public policy outcomes, and we do this by giving strategic advice to clients both in the public and private sectors.



Phillip O'Reilly

JS: Could you outline your recent activities at BIAC?

O'Reilly: BIAC is a formal part of the OECD framework. The core of the organization is about 33 committees that are made up of and chaired by members and align with the various committees within the OECD, such as trade, investment, and tax. There are hundreds of members engaged in advising the OECD process, and we also assist the OECD in terms of its outreach. We assist the outreach process in ASEAN, and also through the G20 and G7 processes, including the B20 and B7 processes. It's a busy job, and my role is really to make sure that the organization itself works. The policy work is done elsewhere, and my role is to make sure

that the organization is being run effectively. It is quite a complex organization but what it brings to the table is high-quality advice because it has these very big and well-resourced business organizations behind it. When we give advice to the OECD we can reach back to those federations and ask their opinion, so we can offer powerful and insightful advice. I will be travelling to Paris tomorrow for the Liaison Committee Meeting which happens every January and is our big set-piece meeting with the OECD to express what business wants, and how we respond to the OECD's work program. This meeting will be held by the most ambassadors and business people we have ever had. I am the chair of the process and have a board that I work with.

BIAC & Trade Policies

JS: You mentioned that BIAC is trying to influence

OECD programs. I am curious about programs on trade policies as today the international trade regime is facing a crisis.

O'Reilly: We work very closely with the Trade and Agriculture Directorate at the OECD. The head of that is a Canadian national, Ken Ash. We think that the OECD's trade work is second to none; I would rank it as the best trade work in the world. The reason it is important in the current times is that it brings evidence to the debate. The trade debate right now is often not one based on evidence but on slogans, on both sides. One of the reasons that the WTO is under such threat at the moment is that the trade debate has become rather isolated from the public. I make the joke that far too often in the past, trade negotiators said to the business end of the public, "This is our job, we will tell you when we are done," and they excluded people from their work because of secrecy and so on in the negotiations. That has got to stop. The work that Ken Ash and his team at OECD do is very important because it makes the benefits of trade much more real to the public and to the business community and that is a very important part of what the OECD does. We support that process; for example, the Services Trade Restrictiveness Index is a product that the OECD has put out, which measures trade restrictiveness and services. They have done a lot of work on trade and digital, around the costs of protectionism, and also about how to build advice around trade policy that makes it more inclusive. This is mission-critical work that they are doing.

JS: It seems to be very difficult for the trade policy people to convince the masses of the benefits of trade liberalization, in particular against the rising tide of populism.

O'Reilly: First of all, it is important to say that not everybody thinks in that way. We were recently in China, and they understand. In Japan, I don't think that people misunderstand the benefits of trade – I think they are generally on board with that. Indeed in the United States, citizens are more pro-trade than anti-trade. Two things have happened to the trade debate over the years.

One is that it has become isolated. It has become people of the WTO sitting behind their iron gates in Geneva and deciding things and then telling the world, rather than engaging with the world. That is not just the WTO, but other organizations too. Second, trade has become the thing to blame when people lose their jobs. If a country is struggling with welfare, trade is blamed. Yet it is often not to do with trade – for example, the US manufacturing job loss is largely the result of digitalization and is not much to do with China, but trade is blamed.

The other challenge is that oftentimes when politicians are faced with tough decisions internally – for example, reform of pension laws or taxation laws – they will often blame trade. How do we resolve that? I think that we need to make clearer to more people the value of trade. It is actually the job of our leaders and politicians to do that, and Prime Minister Shinzo Abe is doing an outstanding job of that in Japan, with the third arrow reforms and the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP). It is actually the job of politicians to communicate to the public the value of trade; it is the job of businesses to explain to their stakeholders the value of trade, including their employees. It is also their job to engage in trade in a responsible fashion, making sure that they truly are competitive.

There is no one simple answer to this, but we certainly need to engage more people in the clear and evident benefits of trade, and then hold politicians to account for what they need to do to make sure that trade is good for all. We all knew when free trade deals and the Doha Round happened that one of the things that was going to happen was micro-economic, internal economic reform in countries to make them more efficient and more open, as it has implications for social welfare, education and infrastructure. Far too few countries have taken that process and done it well; they have not done some of the things that needed to be done internally very well, and I think that they need to be held to account to do that.

“Decoupling” of the Global Economy

JS: Technology has an impact on jobs, but also on national security as evident in the latest argument between the US and China. Journalists are saying that this could lead to the “decoupling” of the global economy. How would you assess this?

O'Reilly: I am personally quite optimistic. (This is my personal view and not from BIAC.) My sense is that both the Chinese and the Americans will have to react to that because the Chinese undoubtedly have some technological leadership, and the US has a great deal more technological leadership than the Chinese do. When it comes down to it, they both need each other which is why we are seeing a softening of the trade tensions of the last couple of years. My sense is that this will resolve itself without some kind of technological cold war, but we need it to resolve itself because the world will be a poorer place if we do not. If the rest of the world is forced to choose between US and Chinese technology just because of the flag on the box, it will make us a very poor world and increase other tensions as well. So it is incumbent on all of us to make sure that we don't go down that track.

Japan is right on the edge of this. You have a long-standing relationship with the US and you also have an increasingly close relationship with China, neither of which is without its tensions, of course. Japan will need the best technology it can get from wherever it can get it, so we need to make sure we resolve this and I do think it will be resolvable over time, but it will require a change in behavior from both the US and China.

JS: Decoupling of the world economy would potentially be disastrous for it. Should we assume that business circles, such as BIAC or multinational companies, would have an incentive to intervene?

O'Reilly: Exactly right. Businesses will make their own decisions – businesses in Japan, businesses in New Zealand, businesses in the United Kingdom. They will decide which technology to use independent of governments and we will be safer because businesses will use the best technology for their needs. It's fair to say that in the OECD we don't get engaged in that debate, but what is clear is that the OECD is for trade and for globalization. There are obviously some implications to that in the way that we think about US-China relations more generally, and technology wars generally as well. We don't get engaged in the Huawei versus US thing as much as others; we are much more about trade.

JS: On the question of national security, there are some sensitive technologies. Without business knowledge it would be very difficult to make rules on sensitive technologies as government people do not know exactly what sensitive technologies are with regard to national security. So business involvement is inevitable to achieve rules-based governance.

O'Reilly: You are seeing those debates playing out in the B20 and G20 process, of course, as well as the B7 and G7 process. They are also playing out at the OECD but not so much because it has never been an organization about, for example, military security. I would make the point that there has always been a situation where particular technologies have been held secret for the national interest: technologies around canons, and around maps back in the 18th century were kept secret. The same applies today. Some of the challenges are where telecom companies are private but have a massive role to play in the national situation, such as broadband technology.

I think we must be driven primarily by the need for efficient, competitive markets and if there is fear or a logical view or a view upheld by evidence that something the US or China is doing is

impeding that, then it needs to be resolved. I don't think it means that we don't buy each other's stuff. We need to resolve issues around security knowing that actually trade will be the biggest driver of security in the long run, as it has been since World War II. Multilateral trade is the biggest driver of national security and peace and prosperity that we have ever seen in the world's history. We need to be clear about that, and not to stop trade.

JS: There seem to be lots of issues intertwined. In the case of trade policy and structural policy, those issues should be discussed together, otherwise we cannot reap the benefits of trade liberalization. Also, security and trade should be discussed simultaneously as otherwise we cannot achieve a rule-making process for them.

O'Reilly: Precisely. There are times when other things trump trade – security will occasionally beat trade. In the trade debate, we have separated these two issues and the OECD has worked hard to put these two things together. You can't have a conversation about welfare reform or about national security without thinking about trade and vice versa. It does not surprise me that trade has become a victim of debate when that has not been occurring, and it has not been occurring.

Some Good Venues to Restore Global Governance

JS: What kind of venues would be appropriate for discussing these issues simultaneously? The OECD is an interdisciplinary organization with a wide range of experts able to work together on various issues. But what about other organizations when global governance is in crisis. How do you see the future of the WTO for example?

O'Reilly: My ambassador David Walker is trying to achieve some outcomes with the US and others regarding the re-institution of dispute-settlement procedures. I am an optimist and I think we will get to some kind of outcome in time. One thing I know we need to do more of is to get the business community to step up more aggressively and to say that the WTO matters to us. This is another one of these institutions that sits between the big steel gates in Geneva and hasn't been particularly open to the business community and to others over the years, and it just needs to change. The WTO senior people recognize the need to reach out to business. Business can bring home the importance of the multilateral rules-based

system on trade much more powerfully than others, and to give an example of that, I was told by one of my chief trade negotiators in New Zealand that before the WTO's rule-making processes came in, when a ship of lamb meat left New Zealand for Hamburg in Germany we did not know what the tariff rate would be when the ship arrived. That's ridiculous, and now we do because of the rules-based system of the WTO.

I often tell people these illustrative stories to try and get them to understand the importance of a rules-based system – not just for small countries, but for big countries as well. So the WTO is definitely part of global governance, and other parts of the WTO move along. A piece of it has stopped, but there are lots of massively important issues that they are trying to resolve such as fishing subsidies, environmentally harmful subsidies. The point about global governance is that there is no one place – that is part of the challenge. Global governance is in the G20 this year in Saudi Arabia, through the WTO and the OECD, and also through the International Labour Organization and the UN agencies that are relevant to it. Parts of it aren't going too badly, but there is a lot of tension and it is not as powerful as it once was.

This is where the role of Japan in particular becomes important. It is the third-biggest economy in the world, and Abe is pro-trade, admirably pledging to lead the process through the CPTPP when the US left. So effective global governance requires leadership from leaders, and we need more leaders prepared to stand up and declare what they stand for. Global governance has some challenges; it is not all wrong though, and parts of it are going OK. We also need to recognize that global governance happens in lots of places and will only work effectively where leaders are prepared to step up and support it. Business leadership in the WTO is very important and people need to understand how important the WTO is so that it doesn't wither on the vine.

JS: Looking at other venues where issues can be deliberated simultaneously, APEC might be a good venue, but Americans have very little interest in APEC. Would the CPTPP be a better venue for initiating global governance?

O'Reilly: We need to be cautious and make sure that organizations stay within their mandate. I used to be a member of the APEC Business Advisory Council until very recently, and was asked a question in New York about whether or not APEC would be involved in the tensions in the South China Sea. The answer is no – APEC is successful because it sticks to its mandate of economic growth and integration and it does that well. If you start to give it rules-based or security roles it will immediately fail because that is not its mandate.

I would argue that the US has an interest in APEC that waxes and wanes, but it is actually pretty involved in APEC. The US has always had more of a suspicious view of multilateralism, even before President Donald Trump. If we get APEC right, then APEC can be a pathfinder for much else. If we get some rules around digital right at APEC through a voluntary approach, we can present them to the world and say look at those. In much of the work that APEC has done, there have been examples where because it was voluntary and done with many of the key countries of the world around the Pacific Rim, APEC work has become much more common elsewhere.

Likewise with the CPTPP, it is just a trade deal and is not technically part of global governance, but the fact that it exists and now countries like the UK want to join, implies that the UK may be prepared to comply with the rules and processes within the CPTPP. I have always been interested in the idea of taking a successful process or forum and running hard with it, making it successful. Others will want to join it, and by doing that you will reduce tension, get more economic integration, and get better things happening. APEC is a great example of that. The fact that the OECD has a number of countries that want to join suggests that it is successful, and once you join the OECD you have to sign up to all the investment criteria and anti-bribery legislation, so that is why business wants the OECD to expand these principles. For global governance, we need to show what is successful and what forms we can use to push a message of growth and integration and social success, and hope that others will join that process as a way of securing good outcomes.

JS: How about the Regional Comprehensive Economic Partnership (RCEP)? It is a bit generous to some protectionists and is not so ambitious, which could be a good thing as countries would find it easier to join. Structural reform would take time, so generous free trade agreements might work better.

O'Reilly: I would argue that you want the reduction of all tariffs to zero. You want free movement of investment and people over time, so for me the outcome of trade deals like the CPTPP or RCEP need to be tight and ambitious. The timeline for countries to get there is the issue. In New Zealand, we know that dairy subsidies around the world are massive, including in Japan, and so we want to get rid of them. But how long will it take to get rid of them? The point about RCEP is that if we can get countries like India to sign up eventually on the basis that it gets quite a long pathway to reform, then that is OK with me so long as it reforms and does not sign up to a free trade deal that is not very free at all. That would be where the business community would insist on ambitious outcomes. The way in which

people can link into those and move along at their own pace to some extent is very sensible and is common. The CPTPP does that, and the Doha Round did too.

JS: How about the idea of trying to have sectoral agreements, for example on digital products. Countries can get together on a voluntary basis to hold negotiations or discuss initiatives and perhaps this could be a good alternative to global governance?

O'Reilly: Global governance is a lot of things all at once, but as you know, these sorts of voluntary discussions go on all the time and are quite powerful. New Zealand and a number of other countries have started one on digital. P4 – the origins of the TPP – was a voluntary thing between these countries and done explicitly to say to Asia-Pacific and the rest of the world that they can play into it, and it leads to the CPTPP and more. I agree that if you can get countries to demonstrate to others and be open to others joining, it is a good thing that should be encouraged.

Role of Business in Rule-Making in the Global Community

JS: On the subject of discussions for rule-making, can BIAC play an important role ?

O'Reilly: It does. Through the mandate of the OECD, there are a number of rules on investment, chemicals, trade, anti-corruption, Corporate Social Responsibility and so on. There are a number of rules or quasi-rule processes that the OECD has through its mandate, and BIAC already plays a crucial role and will continue to do so. If you think about the other roles of the OECD, BIAC effectively follows the OECD around. So in terms of making those much more effective and a part of global governance, for example, OECD membership in ASEAN is poor. If the OECD can be assisted to improve membership among ASEAN nations, it would be good for business and a level playing field. We would encourage and support the OECD in doing that, and on a whole raft of issues. As well as rules on multinational tax, we support more countries becoming members, we support its role in the G7 and G20, and particularly for global governance. BIAC is one of the biggest repositories of business knowledge, information and research in the world, and is a massive engine of knowledge to assist governments in playing that role.

JS: In Japan, we are initiating discussions about how

to get businesses involved in policy decision-making, and how to play a key role in global governance in the international community. To be honest, business might be a little shy of doing so, and government people do not know how to attract business people to the policy discussions. Do you have any suggestions to ameliorate this situation?

O'Reilly: You would always start with the business associations. It is their role to bring business views together and put them in a language that policy officials and politicians can use. One of the challenges is that when you talk to business people about public policy, they think about it and describe it in a business way. Public policy officials and politicians are often unfamiliar with business, and so often we are talking in different languages to each other. Thus, it is a key role of business associations including BIAC and Keidanren to translate between the two, and to turn it both ways into advice that both sides can use. When business thinks something needs to change, government needs to listen to that and vice versa.

Also, we need to be clear about our respective roles. It is not the role of business to engage in global governance, as this is the domain of elected officials. It is, however, their role to try and ensure that the decisions made by public policy officials and politicians will make citizens better off, and from an economic development perspective business knows a lot about this. It is their role to advise the political process and then explain to their stakeholders what they have said and why, including their employees, the communities they serve, and their customers. Not the citizens – that is the job of government to explain to.

JS: The OECD is a global think tank. You mentioned some kind of mediating role between business and public policy. Could think tanks play this key role?

O'Reilly: Indeed they do, and there are many in Japan, the US and the UK. I always see business organizations as big think tanks too. A massive amount of thinking takes place within the OECD – the evidence is brought to bear, and the experiences of the companies around the table are massively important. So I would argue that business organizations are think tanks too, as they bring together the evidence, they distill it, and they represent it. Think tanks are important but it is about getting the right brains around the table. **JS**

Written with the cooperation of Joel Challenger, who is a translator, interpreter, researcher and writer specializing in Japanese disaster preparedness.

Interview with Dr. Atsushi Seike, President of the Promotion and Mutual Aid Corporation for Private Schools of Japan (PMAC)

Elderly Workers – Key to Achieving a Sustainable Super-Aging Society in Japan

By Japan SPOTLIGHT

What will Japan's super-aging society look like in the future? This will depend on the policies adopted from now on and the private sector's adjustability to the aging and depopulation of Japan. As aging in Japan continues in parallel with a declining birth rate, depopulation will be the eventual outcome, resulting in a labor shortage that could hamper economic growth. To avoid this, Japan will need to try to increase its labor supply. Among the ways of achieving this, encouraging elderly people to continue to work longer, even after their retirement at 60 or 65, would be at least a partial solution. As we are now the beneficiaries of longer lifespans with better health thanks to advances in medical science, why should we not take full advantage of these aging but still healthy workers today?

Dr. Atsushi Seike, a distinguished labor economist and former president of Keio University, kindly responded to our questions in the following Interview.

(Interviewed on March 27, 2019)

Introduction – Overall Picture of the Issue

JS: The aging of societies is one of the key issues today in global public policy discussions, and will be at the center of G20 discussions in 2019 in Osaka. To achieve sustainability in Japan's aging society, we will need to ensure the sustainability of our social welfare system. But on the other hand, we should discuss the possibility of enhancing the employability of elderly people, given that our enormous public debt will not allow us to increase social welfare expenditure very significantly. Would you agree with this policy direction?

Seike: Yes. I think that is exactly what we will need in terms of social sustainability as well as personal happiness. We will need to build a society in which anybody willing to work and competent could fully utilize his or her capacity. That would lead not only to the sustainability of society but also to personal content. Japan is now becoming a super-aging society that no other nation has ever experienced. The percentage of the population over 65 years old has already exceeded 28% of the total. This is higher than in any other country. This ratio will reach one-third in the middle of the 2030s.



Dr. Atsushi Seike

When a college student today becomes about 65 years old, namely in the 2060s, the ratio will be rising to around 40%. This phenomenon also means that the ratio of the much older people among the population aged over 65 is also rapidly increasing. The proportion of the 65-74 age group to the age group of those over 75 is now around 1:1, but by 2025 this proportion will be 2:3. This will be due to the fact that people in the baby-boom generation born from 1947 to 1949 will have turned over 75 years old.

Looking into the future further, around 2060 when 40% of the total Japanese population will be over 65, that same ratio will be 1:2. Thus, we will see a significant rise of the super-aged population. In such a super-aging society we will have two issues.

The first is rising social security costs. In order to reduce such costs per capita, it will be crucial to encourage anybody willing and able to work to continue to work regardless of age and support the social security system. The second is the decline in the size of the workforce. Assuming that we will need to shorten working hours and that raising value-added productivity at very high speed will not be easy to achieve, a significant decline in the labor force would end in a shrinking economy. So the aging population would be a serious constraint on economic growth on the supply side. It also leads to a large decrease in consumption in the economy. Since retired people would consume from their pensions, which will be half of the

average earnings of workers who are paying premiums, their consumption will significantly decline. This will be another constraint on economic growth on the demand side. Enhancing the employability of elderly people would therefore be a good solution to mitigate these two constraints.

Another key issue from an individual's perspective on aging is about how to maintain a sustainable life in a super-aging society. At this moment, statistically the expected remaining life span for a Japanese at the age of 65 would be about 20 years for men and 24 years for women. This means at the retirement age of 65, in general, you had around 40 years of working life and will have 20-24 years of life in retirement. With this balance, it would be difficult to have a financially comfortable life after retirement. You would need to continue to work a little further, such as until the age of 70.

Thus, in the light of social needs and an individual's needs, we will need many more elderly people to work longer and enhancing their employability will be a key to achieving the success of an aging society. One advantage for Japan in this regard would be the strong willingness to work of many aging people. A large portion of older people in Japan would prefer to work as long as they are in good health and connected with society. Realizing a life-long active society in which the willingness and ability of older people can be fully realized would be a relevant policy goal for Japan in this regard.

Possible Employment System Reform

JS: To enhance the employability of older people, what do you think would be the necessary reforms to the employment system in Japan?

Seike: First of all, it will be important to raise the mandatory retirement age to 65. The lower limit for mandatory retirement has been lifted gradually under the Japanese Law Concerning Stabilization of Employment of Older Persons and 60 is now the lowest retirement age defined by law. This law also makes it obligatory for an employer to keep anybody employed in some form, such as by raising the mandatory retirement age to 65 or reemploying those who retire at 60 until they are 65, if they want to continue to work after age 60.

The majority of the large Japanese enterprises still keep the mandatory retirement age at 60, but I believe they must raise it to 65. From 2025, the provision of public pensions for employees will begin at the age of 65. Unless the mandatory retirement age and the age for pension eligibility are connected, consistency between the employment system and public pension system will not be achieved.

So raising the lower limit of the mandatory retirement age to 65 is a minimum requirement. With this, you would have to continue to work until 65 and after that we should have as many alternatives as possible, such as continuing to work part-time in the same company or working as a freelance with more flexibility. There could be many people who, having worked hard until the age of 65, will feel like doing whatever they would like to do. In meeting their desires, we will need an employment system fixing the retirement age at 65 and providing more flexibility in continuing to work beyond that age.

JS: What do you think about total abolition of the retirement age, as in the United States?

Seike: It is true that in the United States the Age Discrimination in Employment Act (ADEA) prohibits a mandatory retirement age in employment, but employers there are not suffering any disadvantages from this law. There are mainly two reasons for that.

The first is that in the US an "employment at will" principle prevails. An employer is allowed to fire any employee it finds redundant under this principle. In Japan, we have the principle of prohibiting abusive use of dismissal rights. Apart from dismissal as a penalty, you need authentic and convincing reasons for dismissal, and even if you have those reasons you need to prove that all means and efforts to avoid dismissal, such as working hours, have been exhausted. You also need to demonstrate that there is a rational and objective reason for selecting the employees to be dismissed. Your personal opinion about those employees is not to be taken account of. Lastly, you need to get an agreement on the dismissal between management and labor unions or representatives of the employees. So in Japan, dismissal is considerably difficult. Therefore, mandatory retirement practice at a certain age is a useful means for a Japanese company to adjust employment to economic and business situations. If business slows down, a company would need to reduce employment. In this situation, a company would not replace retiring employees. This works very well as an adjustment process, and for employees as well ensures job security until the mandatory retirement age. In this light, it would be difficult in Japan to eliminate a mandatory retirement practice.

The second reason is that in the US most people retire at the age of 62 without being asked to do so. This is made possible because the public reduced early benefit provision begins around that age and also corporate pension systems are devised to maximize the amounts due to be paid on retirement at that same age. Here employees expect a retirement allowance by working until the age of retirement. This practice creates a mindset for workers to retire at

such an age. It is true that there are certain merits of the ADEA, but its introduction into Japan would damage the stability of employment.

JS: If elderly people's working styles were diversified as they choose to continue to work after the retirement age, would mid-career recruitment or reemployment increase, and Japanese management styles change accordingly? For example, would the seniority-based salary system be replaced by a performance- or expertise-based salary system?

Seike: The seniority-based salary system is already changing. Looking at the wage curve profiles of average workers since the 1980s in Japanese government statistics, it has been continuing to flatten. This is encouraging for promoting the employment of older people, as a company's personnel costs for salaries would rise significantly if the retirement age is prolonged under the seniority-based salary system.

However, in the current situation, if an employee reaches the mandatory retirement age of 60 and reemployed until 65, his or her salary would be 30-40% less than the one at retirement. This would be a disincentive to work. Therefore, I would suggest curbing a rise in wages starting while employees are in their 40s, making the current wage curve profile even flatter.

It is true that the seniority-based wage system works well during the first 10 years of working life, as before becoming a full-fledged employee, young and inexperienced workers in general need to catch up with their seniors by receiving on-the-job training that their seniors usually provide them with and a salary raise by seniority can be justified by their progress in job performance year after year at a relatively high speed. But after being a full-fledged employee, seniority-based salary raises would need to be more moderate.

It is generally considerably difficult to evaluate your working performance objectively, apart from jobs linked directly to sales. For example, it would be not fair to compare the job performance or competency of an employee assigned to a job that happens to be highly profitable and that of another assigned to a difficult job to restore a structurally less competitive business activity. So I do not think the seniority-based salary system will cease to exist completely. But the steepness of the seniority wage profile would be flatter starting from one's late 30s or 40s than now.

We have an employment system in Japan of which we should be proud. I think the Japanese method of simultaneously recruiting new graduates is an excellent system that could be promoted worldwide.

Thanks to this system, Japan enjoys low youth unemployment. In parts of the world where youth unemployment is high, it is economically and socially a big issue. In Europe, for example, young people start looking for jobs after leaving school or university, and they are statistically defined as unemployed. Companies also recruit those with experience for vacant posts that occur spontaneously. So the recruitment of youth is less prioritized and that also prolongs their periods of unemployment. But in Japan, young people are able to find jobs while they are still at school, and the new graduate recruits in Japan will undergo on-the-job training in a company and be trained under human resources development programs. They can master basic working skills at the initial stage of their professional life in their company. I think this is an excellent system that should be preserved in Japan.

Social Security Policies Consistent with Elderly Labor Force

JS: What would be the crucial social security policies to encourage elderly people to work longer?

Seike: Poor health would be the most important factor preventing older people from working longer and prompting early retirement. So the most important social security policy concerning the public health insurance system to encourage people to work longer would be to promote good health by preventing lifestyle-related diseases through precautionary care or promoting vaccinations and providing regular consultations on meals and physical exercise.

Another factor affecting the incentive to work would be a public pension system that could discourage them from working longer. A typical example in Japan is the public pension for employees to discourage those still working. The amount of pension benefits is cut in accordance with the earnings received by those who continue to work over 65, and thus it penalizes them for doing so. In cases where their earnings exceed a certain amount, the total amount of benefits has to be cut.

At this moment, the Japanese government is trying to encourage older people to work longer by committing to paying more in pension benefits to those who postpone receiving pension benefits than the amount paid at age 65. But with the public pension scheme for those still working which I described above, if you work hard after 65 and the pension due to you is cut in accordance with your earnings, you have less extra increase in pension or even cannot expect any extra increase in pension at all at the age of 70 even with this policy to encourage the aged to work longer. Thus, the old age

pension for those still working would nullify the effect of the good government policy to encourage postponing receipt of pension benefits and it needs reconsideration.

Capacity Building for Elderly People

JS: In order to avoid a possible productivity decline by the elderly labor force then, will we need better development of human resources or lifelong education?

Seike: There are two issues here. One is to take advantage of aged workers' capacities. There are many top SMEs in Japan with high competitiveness in niche sectors. They rely on skills, knowledge, long experience and sophisticated services to take care of their customers' needs, all of which could be provided by elderly workers. High value-added, order-made products or services would be what older workers excel in producing. Given that industries in Japan are pursuing higher added value, I think the key to raising our labor productivity is utilizing these older people's capabilities.

The other is to invest in older people's health to keep them fit and prolong their lifespan. We will also need technology to play a supporting role for the elderly when their physical functions decline. A robot suit enabling an elderly person to carry a heavy item would be a good example. The deteriorating eyesight of the elderly could be supplemented by mechanical support. One interesting example is that brain surgeons would be able to continue to work on operations even after their 50s with the help of endoscopes to supplement their poor eyesight or mechanical handles to correct any trembling of their hands. This is how we could continue to benefit from the skills and knowledge of older brain surgeons. We would be able to enhance our labor productivity overall in an aging society by fully utilizing elderly workers' competencies in producing higher added value with the use of technologies.

Helping the Aged Achieve Good Financial Management

JS: On a different note, could you talk about financial gerontology, which is helping the aged with worsening cognitive function in their financial asset management?

Seike: In Japan, as we have a practice of paying large lump-sum retirement allowances, the aged often have great amounts of

financial assets. But they are facing the risk of worsening cognitive functions and it is necessary to protect such people's assets. We should not allow them to invest in high-risk assets. The Japan Securities Dealers Association has a guideline in which sales persons of security companies should refrain from selling risky financial assets to their clients over 75 years old. There are two ways to avoid this guideline being an obstacle to financial investment overall for the Japanese economy as well as taking the possible earnings of financial investment from the aged investors. One is to conclude a contract on investments between a financial institution and the elderly before they face any worsening of cognitive function, so that they are assured of certain financial benefits from their investments if or when their functions worsen. Typically they are private pension plans and mutual funds. The other is to have financial institutions learn from a medical doctor about the cognitive functions of potential elderly clients and then decide in accordance with medical criteria what conditions they should stipulate in their contracts with them. In the future, it may be possible to connect a financial institution with a medical clinic, such as through the Internet. I hope this study of gerontology would lead to effective use of older people's assets in order to realize a wealthier life for the elderly or investments that can enhance the overall economy.

Coping with the Aging Population in Asia

JS: There is a high risk of significantly large-scale aging in Asia, in particular in China. Could the lessons of Japan be useful for these countries?

Seike: Yes. If Japan is successful in achieving a life-long active society in which the will and ability of older people are fully realized, it would be a good model for other Asian nations. This would be a very important Japanese contribution to Asia. The aging of societies is a common issue, in particular for Japan, South Korea and China, with respective birth rates of 1.45, 1.2 and 1.6. All three face depopulation, so it would be productive for them to discuss this common challenge and learn from each other's experience. Pursuing a collaborative path to build up affluent aging societies would be a good subject for a very productive discussion among these three nations, regardless of any political confrontations among them. **JS**

Written with the assistance of TapeRewrite Corporation.

Japan's Long-Term Care Insurance System & Community-Based Integrated Care System

By the Health and Welfare Bureau for the Elderly, Ministry of Health, Labour and Welfare

Introduction

With Japan's population aging more rapidly than that of any other nation in the world, the Long-Term Care Insurance System was established in 2000 as a framework for all of society to support long-term care for older persons. This article introduces the current state of this framework, focusing on the history of its introduction, an overview of the system, and the Community-Based Integrated Care System.

Background to the Introduction of the Long-Term Care Insurance System

The percentage of Japan's population aged 65 or higher is 28.1% (as of 2018), making Japan the country with the world's oldest population. The percentage of people aged 65 and higher has been rising steadily, from 5.7% in 1960 to 7.1% in 1970, to 9.1% in 1980, to 12.0% in 1990, and to 17.3% in 2000.

Along with this rapid aging and increased longevity, the number of people who are elderly and bedridden, or require assistance in their daily lives, is growing. Traditionally, these people were mostly cared for by their families, but in addition to the increased need for nursing care, changes in the social and industrial structure have brought about a shift from extended families to nuclear families, leading to a situation in which the problem of long-term care places a major burden on families.

In Japan, a system of welfare for older persons using tax resources has been in place since 1963, but with a shortage of facilities relative to overall needs, persons with low incomes and other special circumstances were given priority. In addition, procedures like means tests meant that the system was not necessarily easy for ordinary people to use.

In addition, in 1973 medical expenses for older persons were made free, and a social problem of "social hospitalization" emerged in which older persons requiring nursing care were hospitalized for extensive stays despite the fact that they had little need for medical care.

With these social changes, the limits of the traditional system became evident, and the Long-Term Care Insurance System was introduced as a new framework in which all of society supported the long-term care of older persons.

Basic Concept of the Long-Term Care Insurance System

Japan's Long-Term Care Insurance System is based on three main concepts.

The first is "support for independence" and this is the most important principle. Long-term care in Japan means more than just daily assistance with things like making meals, using the lavatory, and bathing. The basic principle is that support for persons requiring long-term care maintains the person's dignity, and allows them to live their daily lives as independently as possible in accordance with their capabilities.

The second concept is that the system is "user-oriented". Under the old welfare system for older persons, the government conducted means tests and other procedures and then unilaterally determined what service would be provided. Under the Long-Term Care Insurance System, however, the necessity for long-term care based on objective, impartial standards in accordance with each individual's nursing care needs is deemed a right, and appropriate services are chosen based on the user's selection.

The third concept is that a "social insurance system" is employed. The system is supported by all persons aged 40 and older, including older generations. The person pays insurance premiums in advance and receives services when they are needed, giving the system the unique feature of a clear relationships between benefits and contributions.

Framework of the Long-Term Care Insurance System

The basic framework of the Long-Term Care Insurance System is shown in [Chart 1](#).

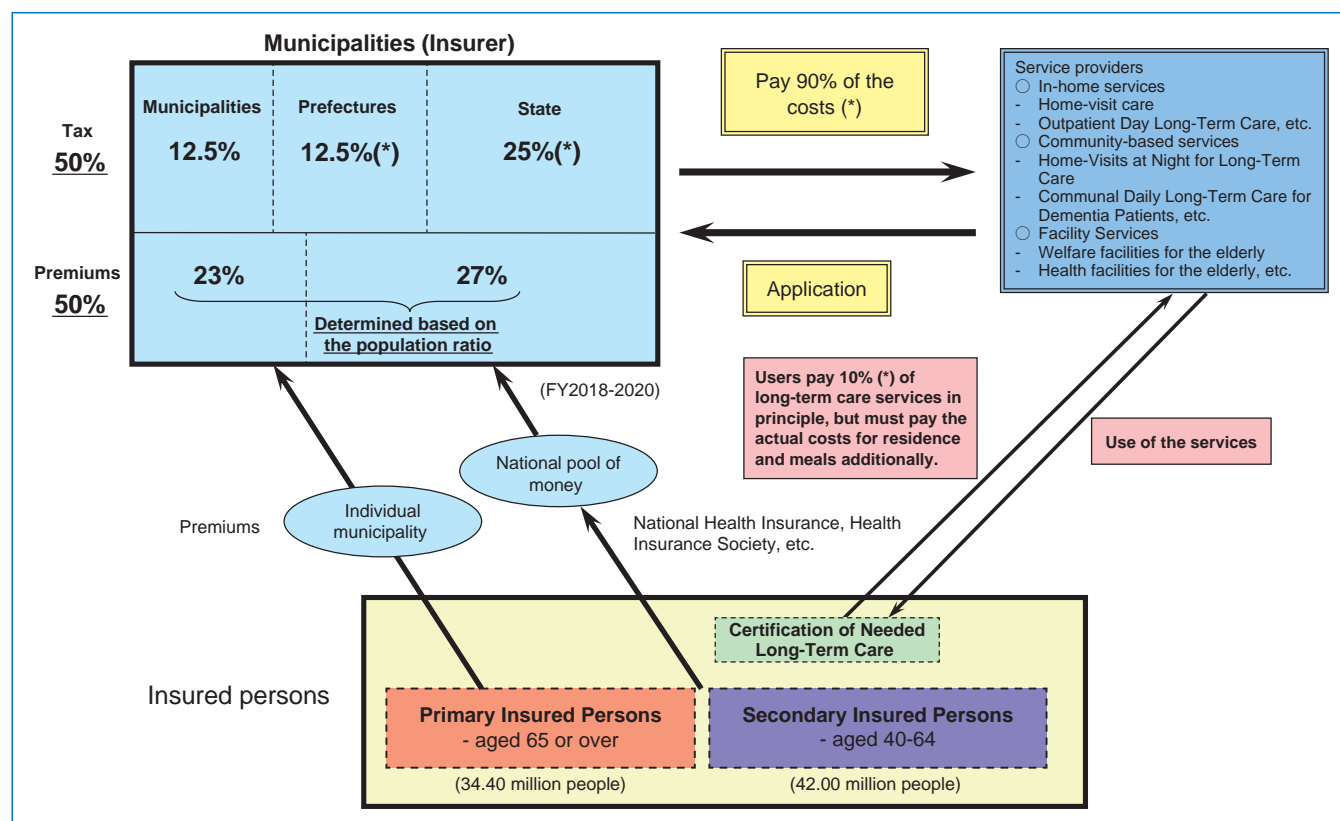
Municipalities (cities, towns, and villages) are the long-term care insurers in Japan. There are more than 1,700 municipalities in Japan, and each is the operator of its local long-term care insurance. The system is managed flexibly by municipalities, which are closest to the people, based on actual local circumstances.

Half of the system's financial resources come from taxes, and the other half from insurance premiums. The breakdown of taxes is 25% from the national government and 12.5% each from the prefecture and the municipality.

Insurance premiums are paid by insured people. People are

CHART 1

Structure of the long-term care insurance system



Note: The figure for Primary Insured Persons is from the Report on Long-Term Care Insurance Operation (2016), Ministry of Health, Labour and Welfare and that for Secondary Insured Persons is the monthly average for FY2016, calculated from medical insurers' reports used by the Social Insurance Medical Fee Payment Fund in order to determine the amount of long-term care expenses.

(*) Co-payment rate for persons with higher income than certain amount is 20% or 30%.

Source: Ministry of Health, Labour and Welfare

considered insured from the age of 40, and enrollment in the system is mandatory rather than voluntary.

There are two categories of insured persons – Category 1 Insured Persons (Primary Insured Persons – aged 65 or over) and Category 2 Insured Persons (Secondary Insured Persons – aged 40-64). Category 1 Insured Persons are residents aged 65 or older. Insurance premiums are determined by the municipality based on the level of income, and are deducted off the top from pension payments. Category 2 Insured Persons are residents between the ages of 40 and 64. These persons do not pay premiums directly to the municipality, but instead are charged premiums along with the medical insurance premiums paid by all persons enrolled in their respective type of medical insurance.

Insured persons are able to use services according to the nursing care they are deemed to require based on objective national standards certified by the municipality (insurer). There are seven levels of required nursing care certifications: care levels 1 to 5, and support levels 1 to 2. Classifications are made according to care requirements, and the type and amount of services to be received are determined according to the level. The two categories of insured persons also differ in terms of benefit requirements. For Category 1

Insured Persons, certification is given if the person requires nursing care in their daily life, regardless of the reason. For Category 2 Insured Persons, certification is given if nursing care is required because of illnesses caused by aging like dementia or cerebrovascular disease.

Insured persons who are certified to receive long-term care choose the service provider and conclude a contract for the use of the service. Long-term care service providers are primarily private-sector entities. Both nonprofit and for-profit corporations are able to enter the field, and services are provided by a diverse range of entities. Since the launch of the Long-Term Care Insurance System, the market for long-term care services has grown significantly.

When using services, in principle the user pays 10% of the cost themselves to the service provider, but if the user's income is above a certain level they are required to pay 20% or 30% themselves. The remaining 90% (or 80% or 70%) is paid from the insurer directly to the service provider.

Japan's long-term care insurance covers both care provided in the users home and at facilities. Many older persons want to live at home where they are comfortable with their surroundings, even when they require long-term care. Services can be combined in a

variety of ways. The user may have their home modified and receive care from visiting caregivers, nurses, and rehabilitation specialists, or they may go to the provider's facility to receive care. There are older persons who move to group homes having persons with dementia living together or nursing homes.

Japan has the specialist occupation of care manager, which entails putting together appropriate care plans in line with the user's needs, and coordinating among the various related parties.

Changes & Issues in the External Situation

Roughly 20 years have passed since the Long-Term Care Insurance System was introduced. While the system has stabilized and developed on the one hand, issues are also appearing for the future.

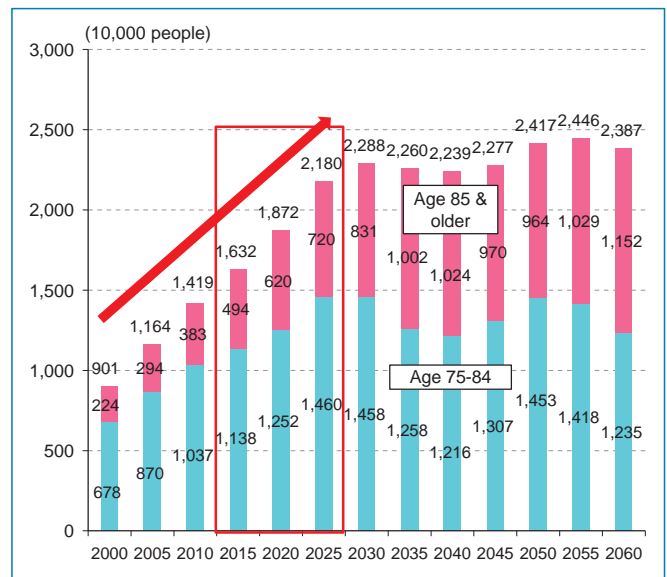
Japan's population has been aging since the system was established in 2000. The number of persons aged 65 and older has grown 1.6 times, from 21.65 million in 2000 to 34.92 million in 2018. At the same time, the number of service users has grown from 1.49 million in 2000 to 4.74 million in 2018, an increase of 3.2 times, showing that the number of users is growing at a faster rate than the aging of the population. The introduction of long-term care services has led to a wide spread in the number of people who require care and are using services as latent needs materialize, so it can be said that the people of Japan have embraced the system. Of particular note, while the number of users of facility services has grown 1.8 times, the number of users of home-care services has shown a significant increase of 3.8 times.

Naturally, as the population ages and the number of users increases, the total cost of long-term care insurance is proportionally increasing each year. From ¥3.6 trillion in fiscal 2000, costs have grown to ¥11.1 trillion in fiscal 2018 (budget basis). In addition, along with the growth in total costs, the amount of insurance premiums paid by each individual is also increasing. The amount of insurance premiums is recalculated every three years, and taking as an example the monthly premium paid by a Category 1 insured person aged 65 or over, the nationwide average during the first period (fiscal 2000-2002) was ¥2,911, and by the current seventh period (fiscal 2018-2020) this had roughly doubled to ¥5,869.

Furthermore, looking at population trends, demand for long-term care is expected to grow for some time. Looking ahead to 2025, a sharp increase in the number of persons aged 75 and higher is forecast (*Chart 2*). This is because in Japan by 2025, the large baby boomer generation born between 1947 and 1949 will all have reached the age of 75. Beyond that, the rapid growth in the population aged 75 and above will dissipate, but the number of people aged 85 and over will continue to grow. The percentage of people who require long-term care increases proportionally with age. Looking at the percentage of people certified to receive long-term care by age group, the percentage for people aged 65-69 is 2.9%, but this increases to 13.2% for persons aged 75-79 and to 50.7% for persons aged 85-89. Therefore, an increase in the number of older persons aged 75 and above, and 85 and higher, will lead to an

CHART 2

Changes in the population over age 75



Sources: Future population estimates were taken from the National Institute of Population and Social Security Research's "Population Projections for Japan (April 2017): Medium-Fertility (Medium-Mortality) Assumption". Actual past figures were taken from the Population Census by the Statistics Bureau of the Ministry of Internal Affairs and Communications (population with proportional corrections for those of unknown nationality/age)

increase in the number of people who require long-term care.

At the same time, the number of people aged 40 and over paying Long-Term Care Insurance premiums is expected to peak in 2021 and then decline. In addition, the number of working-age people, i.e. those who provide nursing care, will also decline. If the Long-Term Care Insurance System is to operate continuously in the future, we will need to make serious efforts to create a better system while conducting regular reviews.

Structure of the Community-Based Integrated Care System

Given these changing circumstances and looking ahead to 2025, the most pressing issue now is the creation of a Community-Based Integrated Care System.

The trend in the number of older persons outlined above shows the figures on a nationwide basis, but in fact the situation differs significantly by region. Many urban areas have baby boomer residents, and face the issue of a rapid increase in the number of people aged 75 and higher. In rural areas, there are regions where the overall population is contracting and the number of older persons is decreasing as well. It will therefore be more important than ever to implement measures that are consistent with the actual situation in each area.

The Community-Based Integrated Care System is based on the principle that even if someone requires intensive long-term care, they should be able to live out their lives as they are used to living where they are used to living. To achieve this, the system aims to

provide comprehensive support with five components – health (medical) care, nursing care, preventive care, residential care, and support for daily living (Chart 3). Municipalities are working to put this system in place by establishing community general support centers for each sphere of daily life, and handling consultations from residents and coordinating with related parties.

Next, we will introduce some of the key points for building a Community-Based Integrated Care System.

Coordination Between Medical Care & Nursing Care

One of the important points in the building of a Community-Based Integrated Care System is to have appropriate coordination between medical care and nursing care.

Many older persons live with multiple illnesses, and also require one-time hospitalization when they become ill or are injured. Enabling older persons who require both medical care and nursing care to continue to live in the area where they are used to living, and to be able to make a smooth return to home after recovering if they are hospitalized for medical treatment, requires a system in which various medical and nursing care staff in the area, including doctors, nurses, care managers, care workers, rehabilitation specialists, and pharmacists, can coordinate their work.

Under the 2014 revision to the Long-Term Care Insurance Act, the system is intended to promote coordination between medical care and nursing care. To build that system, municipalities identify their local resources and seek to promote cooperation among various professions. Specific initiatives vary depending on the area, but successful examples include training sessions for persons from various professions held jointly with local medical associations,

forums to report on sample cases and how to allocate roles properly among related professions, and creating face-to-face relationships.

Community Building

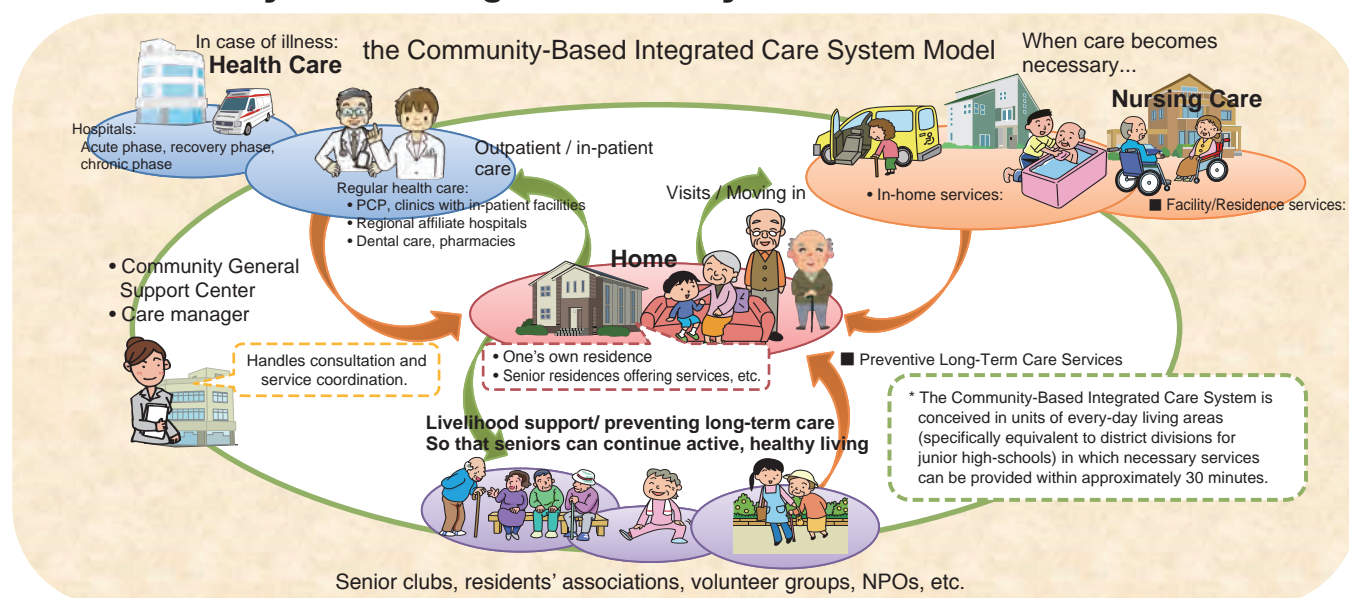
A system of medical and nursing care and the roles of specialists are in and of themselves insufficient for building a Community-Based Integrated Care System. Community building that includes local residents is also an important component.

Preventive care can also be seen as one form of community building. Currently, communities encourage resident-led initiatives that create places for older persons to go to engage in activities like physical exercise. There are no rules for where or how these events are held. For example, they might provide an opportunity for people within close walking distance to gather once a week to engage in light calisthenics for 30 to 60 minutes and then relax over tea. Participating in the calisthenics has the aspect of building health, while the act of gathering together has the benefit of building ties among local residents.

Sometimes, activities can come about from local residents using local resources to provide mutual assistance to support one another in their daily lives. As the number of households with an older person living alone and with an old couple increases, there are areas where these people require a minimum of support for things like daily mobility, shopping, sorting and taking out the trash, and changing light bulbs. Many of these tasks do not necessarily need to be carried out by specialist long-term care providers, and can be handled by local volunteers. Initiatives with local characteristics are beginning to appear in various areas, including the assignment of coordinators for daily support who connect local resources, or giving volunteers points that can be accumulated and exchanged for goods

CHART 3

The Community-Based Integrated Care System



Source: Ministry of Health, Labour and Welfare

or cash.

Policies to Address Dementia

Building communities that are compatible for persons with dementia is also indispensable for creating a Community-Based Integrated Care System. The number of older persons in Japan with dementia was 4.62 million as of 2012, and estimates are that this will reach 7.00 million by 2025. Seven million people correspond to one in five people aged 65 and over. Social costs related to dementia were roughly ¥14.5 trillion in 2014, and are estimated to reach approximately ¥19.4 trillion by 2025. Dementia can be seen as having a significant impact on overall daily life. Many fields in addition to medicine and nursing care are involved, in areas like money management, prevention of becoming a victim to fraud, and responses to getting lost, and therefore this issue needs to be addressed by the entire government, not only the Ministry of Health, Labour and Welfare.

In 2015, 12 Japanese government ministries and agencies jointly formulated a comprehensive national strategy to address dementia, called the New Orange Plan. The New Orange Plan has seven pillars: (1) Raising awareness and promoting understanding of dementia; (2) Providing health care and long-term care services in a timely and appropriate manner as the stages of dementia progress; (3) Strengthening the measures for early onset dementia; (4) Supporting those looking after people with dementia; (5) Creating age and dementia-friendly communities; (6) Promoting research and development and disseminating the results of prevention, diagnosis, cure, rehabilitation models, and care models for dementia; and (7) Prioritizing the standpoint of persons with dementia and their families.

The training of dementia supporters is one example of a specific measure in this area. Dementia supporters possess accurate knowledge and understand dementia, and assist persons with dementia and their families to the extent possible in the community and the workplace. Anyone from children to adults can take the course to become a dementia supporter, and more than 10 million supporters have already been trained.

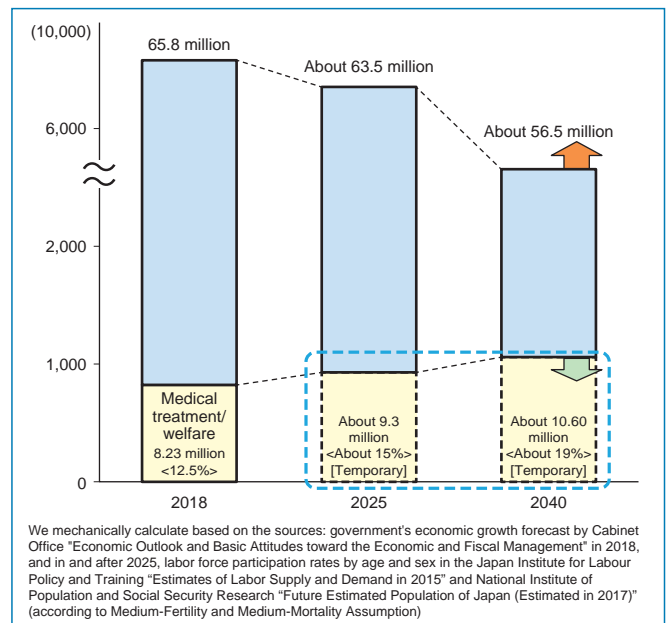
New policies to address dementia are currently being studied, to make government measures even stronger and more coordinated. We expect this new policy to expand measures to reduce the risks and delay the onset of dementia, while continuing to build dementia-friendly communities.

Looking Ahead to 2040

Finally, we would like to present a simple medium-term outlook extending to roughly 2040. As noted previously, the period to 2025 will see a push to achieve a Community-Based Integrated Care System against the backdrop of a rapid increase in the number of older persons. Looking beyond 2025, more than a rapid increase in the number of older persons, the bigger issue will be to address the rapid decrease in the working age population. The number of

CHART 4

Changes in the number of employees



Source: Ministry of Health, Labour and Welfare

employed persons is seen decreasing from 65.80 million in 2018 to 63.50 million in 2025, and to 56.50 million in 2040. At the same time, the number of required workers in the area of medical care and social welfare, including long-term care, is expected to increase from 8.23 million in 2018 to 9.30 million in 2025, and to 10.60 million in 2040. Estimates are that by 2040, roughly 19% of the workforce will be engaged in the fields of medical care and social welfare (Chart 4).

Based on these projections, we believe the social security sector as a whole will need to both secure labor and raise service productivity. With regard to securing labor, it will be important to promote diverse forms of employment and social participation, including for older persons, and maintain the vitality of society as a whole. A goal has been set to increase healthy lifespans by three years or more by 2040, and this will include stepped-up efforts in preventive care. In terms of service productivity, the use of technologies like robotics, artificial intelligence, and information and communications technologies can be seen as reducing the burden placed on workers and increasing productivity. In the long-term care sector, in addition to support by introducing nursing care robots like monitoring sensors, we are seeing the formulation of guidelines to increase productivity through specific operational improvements like streamlining operational processes and the use of information and communications technology.

Because Japan is facing issues associated with an aging population before the rest of the world, it has tried various responses including the establishment of a Long-Term Care Insurance System. Looking ahead, the populations of other countries, especially in Asia, are set to age more rapidly than Japan's, so we hope that this article will be useful to those countries.

Interview with Nico de Wet from South Africa working at the Global Business Division of SoftBank Corp's Enterprise Unit

Bridging Africa & Japan – Entrepreneurial Engagement for a Young African

By Japan SPOTLIGHT

Nico de Wet, a young South African, talks about his experience of the ABE Initiative, the “African Business Education Initiative for Youth”, one of the most important outcomes of the TICAD process so far. He also talks about the NGO initiative “Kakehashi Africa” (Bridge of Africa), an important offspring of the ABE Initiative. He works for SoftBank, a major Japanese telecommunications company that started as a venture, and is learning entrepreneurship from them.

(Interviewed on July 12, 2019)

Introduction

JS: How did you become interested in Japan, and why did you decide to stay working in Japan for SoftBank?

Nico: I am from South Africa, and before I came to Japan I studied philosophy and law at Stellenbosch University, which is located close to Cape Town, and worked for nearly five years for a group of companies specialized in space engineering, GIS applications and other technologies. I worked in a team that was specifically involved in using technology to help NGOs be more effective. Then I came to Japan under the ABE Initiative, spending two years at Ritsumeikan University in Kyoto, where I studied international relations, followed by a six-month internship at SoftBank Corp. The reason for joining the ABE Initiative was because I felt that Africa and Asia would become very important continents in the future, due to population and economic growth. At the same time there are not many people that can be a bridge between the two markets, so I thought it would be a good opportunity for me to specialize in that space. Two and a half years of the ABE Initiative sounds like a long time but it was not enough to build a deep understanding of how Japan works, so that's why I decided to stay longer in Japan. I was very fortunate to join a Japanese company that has a large appetite to change the world and has a lot of resources that can be used to satisfy that appetite. It also gives me a good opportunity to deepen my knowledge of Japan and to continue building my networks in Asia.



Nico de Wet

The ABE Initiative & “Kakehashi Africa”

JS: What do you think about the ABE Initiative? Is your assessment mainly positive?

Nico: From my perspective, it was a very good return on my own investment because I ended up working for a very good company. The mission of the ABE Initiative is to enable the creation of partnerships between Japanese and Africans, and in terms of that mission, in my personal case, I have accomplished that by being employed by SoftBank, who have given me the mandate to penetrate the African market. So for me, the outcome was very good. In addition to employment by SoftBank, during the ABE

Initiative and all the events created by the Japan International Cooperation Agency (JICA), I managed to meet a lot of Japanese companies and build a very good network. This helped me create a very good foundation for my future mission of building bridges between Africa and Japan.

JS: Kakehashi Africa is one of the NGOs acting in making bridges between Africa and Japan, and it consists of alumni of the ABE Initiative. Could you briefly explain about Kakehashi Africa?

Nico: Obviously, during the two to three years of the ABE Initiative program, each ABE participant has a great opportunity to build a great network and gain lots of knowledge, but if this is not followed up by a platform to make sure that the relationships that were built actually reach some kind of concrete result, then the return on

investment will never happen for the ABE Initiative. So the mission of Kakehashi Africa is to kind of continue the mission of the ABE Initiative even after it finishes by creating a platform that allows ABE participants and Japanese to continue their engagement. This is the reason why we created Kakehashi Africa: to continue the momentum of the ABE Initiative towards and beyond the point of making a meaningful impact for all stakeholders. We also felt that Japan has already done so much – the Japanese taxpayer has paid so much by bringing us here and giving us this education, internship and networking opportunities. So Kakehashi Africa is an initiative by us Africans, as it is our turn to take co-ownership and contribute proactively to this mission of the ABE Initiative.

In terms of what we do practically, currently Kakehashi Africa is focusing on building a formal member network where ABE participants and alumni, Japanese companies, NGOs, governments or anyone can become a member of the network and then they can have access to two platforms: a virtual online platform for knowledge exchange, sharing opportunities, requesting employment, funding, teams or skills – so a kind of a business intelligence and matching platform – and also a physical platform in the form of branch activities. We are creating branches across African markets, but also in Japan, where people can attend networking events, workshops or have business tours. So basically we want to develop Kakehashi Africa into an enabling platform to continue the idea of bringing Japanese and Africans together to do real business.

Currently, since we are still in the early development stages of the platform and need to get a few more things in place, we have limited the membership to ABE participants. We have about 500 ABE participants who have indicated their interest to be involved; more than 250 of them have formally registered and this number is increasing week by week. We have a board of directors, elected by our members, who have appointed me to lead the executive management. We have a lot of challenges, because all of us are doing this during our spare time as we have day jobs; nevertheless slowly but steadily we are getting things in place.

JS: How about your budget?

Nico: We don't have a budget at the moment. Recently, we legally registered the organization in Kenya and the expenses of registering the entity were covered out of our personal pockets. The Japan International Cooperation Center (JICE) – which has been contracted by JICA to help manage the ABE Initiative – has often supported our transportation and accommodation costs whenever we had major events or meetings. So, our first mission is to create a basic revenue stream. We want to do this by creating a way for people to pay a fee when they become a member of our network.

JS: Your members have mostly been working for Japanese companies. Are they successful in building up links between Japan and Africa?

Nico: The majority of ABE participants go back to Africa so only a few remain in Japan working for Japanese companies. I think there is some concern among those who return about what to do next. To

address that concern, I think that Kakehashi Africa can really help to continue creating opportunities for those who have returned to do some real business or projects with Japanese entities. It's a big challenge but we are committed to addressing it.

View of TICAD

JS: Moving to TICAD, the ABE Initiative must be one of the important products of the TICAD process. How do you assess what TICAD has achieved so far?

Nico: My only exposure to TICAD is the ABE Initiative so I can't talk more broadly about what has come from TICAD. I think that the ABE Initiative is a great program for contributing to the development of Africa while at the same time creating opportunities for Japanese companies to expand their business. However, since the focus of the ABE Initiative is human capacity development and relationship development, the results of the program will not happen overnight, so I think we will need to give it some more time to see the fruits of the ABE Initiative. There have been some small successes, such as people like me who joined Japanese companies to help them expand into Africa or people who have created new enterprises in partnership with Japanese, but to have the scale of success necessary to tell the Japanese taxpayer that this program was a good investment we will need to give it more time and seriously follow up the ABE Initiative with something like Kakehashi Africa. The real success will be determined and achieved by what we do next after the program.

JS: How about TICAD VII in Yokohama this year? Do you have any particular expectations?

Nico: It is now our turn as Africans to contribute to the success of the ABE Initiative, but it would be very helpful if the Japanese government and private sector could continue to commit their support and particularly help us to follow up the program and actively participate in the projects that we may organize for that purpose. The ABE Initiative has created all these relationship networks and ideas for business partnerships, but now we need other resources, such as venture capital, to invest in these ideas and make them happen. So if there could be some kind of investment fund that could help lower the risk for Japanese companies to enter into partnerships with ABE Initiative alumni, this could be very helpful. Furthermore, another type of ABE Initiative program could also be good, perhaps one that is focused on technical skills development – practical skills that could make an immediate impact.

JS: How do you think Japanese businesses could contribute to African economic development? The bottom-up pyramid approach would be an effective way to achieve economic development, but there may be other ways.

Nico: The answer to this question depends on the industry. Generally speaking, the challenge for Japanese companies is that there is a lot

of competition with emerging economies and specifically other Asian players who are offering a cheaper price on products and who these days are even increasingly providing high-quality products. So Japanese companies will have to be very creative and strategic in their thinking. One benefit they have is that because they are from a large and highly developed economy they are very cash rich; they could become very good investment partners. Secondly, Japanese companies still have a very good reputation in the world. They are respected and trusted. Other foreign players in Africa do not have that brand of trust, so if Japanese firms can leverage these things to their advantage, it could help. A company like SoftBank, for example, is very good at making investments and building partnerships, and helping develop ecosystems around a certain industry. Instead of competing, if Japanese companies could invest in the enterprises of other players or facilitate the building of partnerships based on common values, it could be an interesting approach. Generally speaking, Japanese companies are not geared towards the “bottom of the pyramid” as their products are very high quality and somewhat pricey, and most African countries do not have enough people in the higher ends of the market who could appreciate and afford those products yet. So Japanese companies are going to have to think differently, perhaps acting as a facilitator or partner in order to target the majority of Africans.

Digitalization in Africa

JS: I understand you are working on a digital business. Digitalization is spreading all over the world, and in particular in Africa there is a lot of progress. How do you assess the future of digital business in Africa? Is it limited to startup businesses?

Nico: No industry can escape digital business/technology these days, and this will increasingly become the case. If we as Africans do not create technological or digital solutions or adopt these solutions, we will lose out. The gap between us and the rest of the world will simply become wider. However, Africans have a good appetite for using tech, and mobile penetration is moving very fast, even compared to the rest of the world. Mobile wallets such as M-Pesa in East Africa, for example, show how eager Africans are to use digital solutions. There are many challenges that prevent Africans from using more digital solutions: tech infrastructure, especially telecoms infrastructure, is an issue, as are the political and business environments in terms of regulation and corruption. Some of these things could perhaps be leap-frogged or disrupted with new technology. However, education cannot be so easily leap-frogged. We cannot escape the hard work over a long period necessary to ensure that you have people with the right skills and mindset. Frankly speaking, Africa has the worst education systems in the world and this is preventing digital business from taking off properly. For a company like SoftBank – and I think this should maybe be the case for other Japanese companies as well – the correct approach would be to focus on building local partnerships, investing in local capacity development and making capital available for local people in a

supportive role. This would really help Africans to reap the benefits from the digital economy. It is not going to be easy; there is a lot of potential but a lot of challenges that need to be kept in mind.

JS: In the case of the digital economy, open innovation might be very important. Do you think that SoftBank could contribute to more innovation in your country?

Nico: SoftBank wants to be the player that makes the biggest impact in an industry. If we are talking about agriculture, they want to look at the whole ecosystem and be the platform underpinning that ecosystem. SoftBank can make a huge contribution to help develop the necessary technology infrastructure and make sure that the right players are in the value chain and that the right players are supported to enable value creation. Creating an open innovation platform is definitely good, but Africans need to be equipped with the right skills, knowledge and capital to really leverage this opportunity. African governments will also have to take ownership. Once again, education is an important key – if we don't have education the rest will not fall into place, or foreigners will just come to Africa, capitalize on all the opportunities and reinvest most of the profit in their own or other regions. If we want to enable Africans to become wealthy and be able to contribute to the world with their own solutions, we need to make sure that they have the necessary skills and mindset to do that. For that we need solid education.

The ABE Initiative is only one part of the bigger solution to the problem of education or human resource development, so we need to look beyond it. The ABE Initiative is the right approach however, and I really want to compliment Japan for it.

In terms of other anticipated outcomes of the upcoming TICAD VII, in addition to human resource development programs that bring people to universities, there is perhaps also a need to focus on technical or practical skills development, like giving Africans apprenticeships in factories, that may translate into immediate practical benefits. A follow-up to the ABE Initiative that further supports the skills development of alumni may also be helpful. For example, every year or more frequently, Japanese agencies like JICA could facilitate seminars or workshops in African countries to which ABE Initiative alumni are invited. The Japanese government is actually already supporting African governments through a wide range of activities to make an impact on the systemic challenges of education. However, Japan cannot make the necessary impact alone and needs to collaborate with the whole global community who are interested and involved in solving the challenges of education in Africa.

Prospects for South Africa

JS: South Africa seems to have a lot of growth potential. What is your view of its growth potential? Perhaps in two or three decades its economy will be bigger than Japan's.

Nico: I like that idea! I don't know if it will happen though. South Africa's current economic growth is nearly zero, and we had some quarters recently when we were technically in a recession. However, South Africa does indeed have tremendous potential because we have the best infrastructure on the continent. There are huge inequalities in South Africa, but the people who have skills have very good skills. Our large companies, like those listed on the stock exchange, are of global standard. South Africa has so much potential and we are geographically positioned in a region of emerging markets full of potential, so we really have the opportunity not to only leverage our own resources but those of the whole continent and really be a leader for Africa. We can be a regional leader that does things differently from the heavyweights in other regions in the world by truly creating shared value for the whole region rather than exploiting our neighbors primarily to our own benefit.

The problem is that we are our own worst enemy. We have a lot of internal issues that are a result of our past. We have gone through a stage over the past decade under the previous administration where we have not made progress and in fact have gone backwards. This is very unfortunate, but with the new current government and leadership I think there is a lot of new hope. I have a lot of faith in the new government and we are making slow but steady progress heading in the right direction. All we need to do is to maintain this momentum. There are still a lot of risks and challenges and it will be very difficult, but we are moving in the right direction. In a few decades, maybe we can be an important player even if we are not as big as Japan!

JS: When Africa hosted the World Cup in 2010 there were serious concerns about security. Has the security situation improved?

Nico: I believe there have been some small improvements to security, but the overall picture is still not that good. However, one needs to maintain perspective on this. I lived for a very long time in South Africa and have never experienced any serious incidents – nothing more serious than what you may typically encounter in the United States or Europe. It really depends on where inside cities you go, and as long as you follow common sense, you should be fine. So I don't think it presents a serious obstacle to doing business and should not stop us from moving forward.

JS: So mitigating the security risk might lead to more foreign investment?

Nico: If there is more direct investment and economic opportunities, our security situation will be alleviated, so it goes both ways. But we do need to take the issue of security very seriously and I think South Africans are doing their best to alleviate the security challenges.

Views on Japanese Culture & Business Life

JS: How do you find working in a Japanese company? The culture must be very different.

Nico: In terms of the long working hours, I often also worked long hours in South Africa before coming to Japan. So, I think the work hours may not be that different to many South African companies. However, Japanese do certain things very differently. For example, the way decisions are made and the way people act are very different from what I am used to in South Africa. I have learned a lot about humility, to really consider others, and about consensus in decision-making. Also to do things systematically by focusing on small details. I have respect for this working culture and have developed an admiration for it. There are challenges: for example, you don't always move as fast as may be necessary, but if you are open-minded about the challenges then it does not present a problem. I am always discovering new aspects to Japanese culture. The culture is very deep and sophisticated. It is a very interesting experience for a foreigner like me to be part of a journey to understanding it better.

JS: In particular, corporate culture is hierarchical and requires a lot of consideration of others.

Nico: Maybe I am not a good example because SoftBank is not such a traditional company, and moreover I am in the global business division which perhaps has a different business culture from the rest of the company. There is a lot of space there for you to take the initiative and not follow the hierarchy. My bosses are very open-minded people so I am not really experiencing hierarchy. I think we have a very healthy culture at my company. However, because you always have to accommodate people instead of going it alone, you have to slow down sometimes; but this teaches you humanity and to really consider others, which I see as a good quality. Of course, I benefit from this practically as well, when others in the company have to slow down to accommodate me.

Future Plans

JS: What are your future plans for continuing to be a bridge between Africa and Japan?

Nico: I would like to establish an office for SoftBank in Africa, and as its mission I would like it to become the best facilitator of partnerships between Japanese, other foreign companies and local African companies – partnerships that create real solutions that will address the real needs of Africans. But also to enable partnerships between African and Japanese companies or other companies that can be taken to the rest of the world. We need to create opportunities for Africans to generate their own wealth, and a part of doing that is opening up markets around the world for Africans – through partnerships, this can be achieved. I hope to facilitate such good partnerships between Africans and the global community. **JS**

Written with the cooperation of Joel Challender, who is a translator, interpreter, researcher and writer specializing in Japanese disaster preparedness.

Interview with Juvencia Deschamps Ralay Harisoa from Madagascar working in the Public Relations Group, Administration Department, of GPSS Holdings Inc. in Japan

Learning Management Will Help Bridge Madagascar & Japan

By Japan SPOTLIGHT

Juvencia Deschamps Ralay Harisoa from Madagascar talked about her experience in Japan through the ABE Initiative, the “African Business Education Initiative for Youth”, and her work with a Japanese renewable energy company, GPSS Holdings Inc., following her studies. She also discussed her plans after she returns to her country.

(Interviewed on July 17, 2019)

Self-Introduction

JS: Could you please briefly introduce yourself and tell us why you became interested in studying in Japan, and why you decided to stay and work in Japan?

Deschamps: I was born and raised in Madagascar where I had all my formal education. I worked in Madagascar for around nine years before coming to Japan, mainly in sales and marketing, and most recently quality management. That position brought me to Japan for two reasons – firstly, I was training people about the Plan-Do-Check-Act (PDCA) cycle and the Ishikawa Diagram, and also the theory of continuous improvement, and secondly, I got a scholarship from JICA to my current company. I chose Japan because I wanted to deepen my knowledge about leadership as part of my MBA. I was looking at different scholarships in various countries, but received a scholarship to Japan and that is what brought me here.

JS: Could you explain a bit about the Ishikawa Diagram?

Deschamps: This is a theory about PDCA and the 5Ms (Method, Material, Man, Machine, Measurement) as the elements of quality management in a factory, and this is something I trained employees about in my previous organization mainly when it is applied in the management field. My former CEO appreciated my work and said that I could go further, and that is why I came to Japan.



Juvencia Deschamps

View of ABE Initiative

JS: You studied under the ABE Initiative, and you are continuing to work for a Japanese company as a graduate from this initiative. How do you see the outcomes of the ABE Initiative in terms of your own studies?

Deschamps: The initiative provides more opportunities not just for Japan but for African countries too. I think I would not have had this opportunity to develop connections with other African countries if I was not in Japan. It is amazing that outside of Africa I can have the opportunity to meet people from 40 countries at the same time. The ABE

Initiative has provided me with a very valuable experience in this regard.

JS: The Abe Initiative has produced many people who are now active in Japan and other countries. Human resource development is a very important issue for all nations – and particularly for Africa – in achieving economic development. How has this initiative contributed to your country or other African countries in the respect?

Deschamps: The initiative has allowed people to gain experience and training in Japan and then go back to Africa to address the lack of human resource training there, particularly in developing countries. It may take a little more time for change to take place, but in a few years it will come.

View of TICAD

JS: You must be familiar with the TICAD process. How do you assess its achievements so far, apart from the Abe Initiative, and what do you expect from TICAD VII in Yokohama this year?

Deschamps: TICAD has strengthened the relationship between Japan and African countries not just in terms of economic development but also in cultural and social relations. There are a lot of improvements in contracts between my country's government and the Japanese government, including the Toamasina Port Development Project. I think this will result in a lot of commercial transactions between the two countries.

JS: TICAD has helped bring Japanese companies to Africa. How do you think they can further contribute to African development?

Deschamps: In terms of know-how, and sharing best practices and expertise, and in terms of technology and innovation, Japan can make contributions to African countries. When it comes to PDCA, there are things that Japan can learn from Africa, and that Africa can learn from Japan. It would not work to just take the methods from Japan and try to apply them to Africa, nor vice versa, so there needs to be an element of adaptation when sharing best practices. PDCA can work very well – when people see the results they are convinced and want to apply them effectively to achieve their goals in many fields, such as their businesses and their daily lives. As long as people know where we are going and what it is about, they tend to respond favorably to it, so I think it can be applied successfully across borders.

Current Working Experience in Japan

JS: Your company is involved in renewable energy, which is very important for Japan especially since the Fukushima disaster. What lessons learned in your company in Japan could contribute to the renewable energy situation or development in Africa?

Deschamps: Right now I am learning how to utilize sustainable energy, and I think that Japan has achieved local community collaboration to leverage energy use and bring it to the grid. This is something totally new to me. We can learn from this and implement it in Madagascar and also in other countries in Africa. Local community collaboration is very important and is one of the most important lessons to be learned from Japan when it comes to leveraging renewable energy. Another is reducing the use of nuclear



power. To achieve real sustainable energy we have to move away from nuclear, which is not at all easy. At the least, we have to raise awareness of this situation and bring together people who are interested in it, including policymakers and the political sphere. We need to promote the issue among the population.

JS: In Madagascar, what kind of renewable energy sources offer the most potential?

Deschamps: Solar and wind energy. There is geothermal but it is still limited – very little is used to generate electricity in Madagascar. Solar and wind are still under-utilized in terms of their potential. Since we have so much sunlight throughout the year, we can get solar energy very easily. The challenge lies with batteries, as we cannot store the energy yet, so we need to protect the environment, to use fewer batteries, and instead rely more on wind and hydro electricity, in the appropriate combination.

JS: As far as solar and wind power are concerned, do you think Japanese technology offers some advantages?

Deschamps: Yes, especially in terms of turbines. Japan has somewhat similar climate conditions to Madagascar – we are both islands and we face similar challenges. We have cyclones and this is a big challenge in terms of making turbines that can withstand the impact of cyclones, and this is something we can learn from Japan. I should also mention biomass. This is already ongoing and various organizations from Japan are in Madagascar to teach about biomass.

JS: You studied management rather than technology. For a renewable energy resources company, what



kind of management techniques would be useful? Not in terms of leadership, but for example, mathematics can be applied to renewable energy to handle all the data coming from the energy sources. Managers need to maximize the profits so I imagine that some mathematical techniques might be useful for achieving efficiency.

Deschamps: I am not sure if there is one thing that we have to follow. I would like to emphasize the point that if Japan wants to go to Africa or another country, there is no one singular route that it needs to follow. Management is one tool, but leadership is the key to opening it. We need to inspire people, and so I am not sure if a mathematical or theoretical approach is the most relevant. Rather, people and talented management might be more important in this respect.

Life in Japan

JS: How many years have you been in Japan so far? What is your perspective on living in Japan?

Deschamps: In total, two and a half years. What I love about the culture is that people are humble and polite, and very organized. Japan has a culture of excellence, which I really like, although it can be very difficult to achieve. Something that I do not like so much is that sometimes Japan puts too much emphasis on perfection instead of humanity.

JS: Working for a Japanese company, are you very conscious of the existence of a hierarchy?

Deschamps: Not really. While my company has a hierarchy, it is not like a typical Japanese company: the CEO is open-minded, and this extends to the employees also. I can share my ideas and can take initiatives at any point.

Talking About the Future

JS: How do you see future relations between Madagascar and Japan?

Deschamps: I foresee a very positive future for relations. Japan has been very active in the economic and social development of Madagascar over the last decade. There are projects with JICA, including the development of the port, and these will allow a lot of two-way traffic and transactions between the two nations. There will also be many opportunities for sharing knowledge and know-how in the future.

JS: In the future, you may wish to go back to your country to contribute to its economic prosperity. How do you view your future at the moment?

Deschamps: My plan is ultimately to be able to have my own company and to inspire the youth in my country using my experience in Japan. If my company can build some links with Japan it would be great. In the end though, I would like to run my own company. I do hope that we can create some business opportunities that benefit both countries.

JS: Will your company function as a bridge between Japan and Africa?

Deschamps: Not necessarily, but I think that the future is a very long time. It could start tomorrow or in several years. It might not be limited to Japan, but I am not yet sure exactly what kind of company I would like to create. I will try to use my networks in Japan to build up a company and then to facilitate some transactions between businesses in Japan and Madagascar. I am steadily growing my human network in Japan which will be very important for opening doors in future, and for uncovering new opportunities and potential markets. People management will be key, and I think I can achieve this through networking.

JS

Written with the cooperation of Joel Challender, who is a translator, interpreter, researcher and writer specializing in Japanese disaster preparedness.

Interview with David Bickle, President, the British Chamber of Commerce in Japan

The Legacy of the Rugby World Cup 2019 in Japan Will Be Good for the Olympic & Paralympic Games Tokyo 2020

By Japan SPOTLIGHT

The Rugby World Cup 2019 in Japan turned many Japanese who had never seen the game and knew nothing about the basic rules into rugby fans, thanks largely to the Japanese national team's achievement in qualifying for the quarterfinals for the first time. But will the legacy of the tournament prove to be even greater than the national team's performance? Could it provide some useful lessons for the coming Tokyo Olympic and Paralympic Games in 2020?

We interviewed David Bickle, president of the British Chamber of Commerce in Japan and former member of the Japanese national rugby team. This is his second interview with *Japan SPOTLIGHT*, following his first in the September-October 2015 issue.

(Interviewed on Nov. 5, 2019)

Self-Introduction

JS: Could you briefly tell us again about your connection with Japan and your experience as a former lock with the Japanese national rugby team?

Bickle: I'm currently the president of the British Chamber of Commerce in Japan (BCCJ). In total, this will be my 22nd year in Japan, and I've been based here on two occasions. My first time was after graduating from university, when I joined Kobe Steel, where I had a chance to play with the Kobe Steel rugby team for six years from 1993 to 1999. I was very fortunate that in 1996, I was also selected to play for the Japan national team, and in that year I played six times for Japan.



David Bickle

think the record top five viewing figures for television audiences of rugby matches are now all involving the Japan team, with nearly 55 million people in Japan tuning in to watch them play Scotland. More than 400,000 foreign visitors arrived in Japan to watch the tournament in person, and I think there were more than 1 million visits to the official fan zones. On social media, according to figures published by World Rugby, there were 1.7 billion views of videos and content, so the social media engagement was incredible – at unsurpassed levels. And I think the economic impact was huge as well – World Rugby estimates it to be 437 billion yen.

Importantly, beyond the economic impact was the engagement of people in Japan and the development of the game, and the

number of children in Japan who for the first time were introduced to rugby – not just through the tournament but with the community engagement exercises that took place around the tournament. The impact has been huge. That was during the tournament and before the tournament, but I think we all hope now that as a legacy of the tournament we'll see continued engagement, impact, and follow through.

Assessment of Rugby World Cup 2019

JS: How do you assess the Rugby World Cup 2019 in Japan overall? Everybody speaks about it as a great success.

Bickle: I think however you measure it, it's been a huge success, both in terms of the experience the fans have had and the quality of the rugby. It was historic that Japan won all of their group matches and were able to make it through to the last eight, their first time in history to reach the knockout tournament. If you look at the metrics, the television audience for all of Japan's games was incredible. I

JS: I recently came across the term “sports hospitality” for the first time. What are your thoughts on sports hospitality, and about that aspect of the legacy here?

Bickle: I think sports hospitality is clearly a new opportunity for

Japan. Particularly around the World Cup, it was the same company which delivered hospitality at the last three or four Rugby World Cups. They had a bespoke facility built in Yokohama, and the professionalism of the delivery really created a focus around corporate hospitality, a chance for companies and organizations to bring guests to a quality facility and enjoy themselves and network before and after a game. It's another way for companies and organizations to entertain their clients and guests in a very exclusive, unusual, and unique networking environment. There is a huge multiplier effect as well for the economy, so anything to do with the delivery of services – food, drink, entertainment – has a positive impact on the economy here.

If you look at sports hospitality in the United Kingdom, a lot of it is focused around the stadiums. A number of those are used not just on match day, but also throughout the year for conferences and entertainment. I think that's another angle to look at – whether sports hospitality offers a way to get better utilization of the infrastructure that there is already here in Japan.

JS: Travel agents and the hospitality industry in Japan seem to be looking forward to more tourists from all over the world.

Bickle: I think so, and tourists are increasingly looking for an experiential time, for experiences rather than just things. Certainly, around an event like the Rugby World Cup, I think being able to package a match ticket and travel to the game within a hospitality package makes it a more appealing offering to tourists.

British Chamber of Commerce's Involvement

JS: Would you please tell us a bit more about the British Chamber of Commerce's involvement in supporting the Rugby World Cup?

Bickle: Certainly. One thing we realized a couple of years ago was that the Rugby World Cup 2019 Organising Committee was very keen to speak to the foreign business community with one voice, so what the BCCJ did was to get together with seven other foreign chambers of commerce to form the Rugby Alliance. The original mission of the Rugby Alliance was two-fold: it was to support the delivery of a 2019 Rugby World Cup that all stakeholders here in Japan can be proud of, and secondly to foster a legacy that features more inclusive communities which embrace opportunities for international business and exchange. Working together with the other chambers of commerce, we collaborated closely with the organizing committee.

The BCCJ also hosted a think tank event in July on responsible tourism, where we had representatives from some of the regional economies in Japan, and people from the tourism, hospitality, and hotel industries. We talked about opportunities for tourism here, including those connected with the Rugby World Cup. And about some of the challenges Japan is facing. Particularly where the

hospitality industry is rapidly scaling up and also the number of visitors is rapidly increasing, and the challenges of being able to cater to those visitors. Not just to cater to them, but to cater to them in a sustainable way.

JS: Do you think Japan will be successful in keeping these great numbers of tourists, just like China was successful in having done so after the Beijing Olympics?

Bickle: I think so. What the Rugby World Cup has done is to open up the whole of Japan to a new audience. Tourism from Europe and the United States has traditionally been focused on the large metropolitan and cultural centers – Tokyo going down to Osaka, Kyoto, Nara, Hiroshima, and places like that – but the Rugby World Cup has been nationwide, from Sapporo in the north in Hokkaido down to Kyushu in the west. That's given overseas tourists a chance to see what Japan has to offer. I think a number of tourists still have the image of Japan being a highly urbanized country, and they are pleasantly surprised when they see that much of the country is beautiful mountains and forests as well. The key will be finding ways to enable foreign tourists to discover the rest of Japan. I think that is where the Rugby World Cup was so powerful, as a catalyst to get people to move beyond the traditional tourism centers to places where perhaps, were it not for the rugby, they would not have seen.

The Japanese National Team

JS: As a former lock, what is your opinion of the Japanese national team?

Bickle: The Japanese national team has been absolutely tremendous in this tournament. They played a brand of rugby which has thrilled the world. Everyone has been amazed, I think, about the way Japan played in this tournament. What we saw was a new level of skill and accuracy. Japan has moved on and improved to another level, and their skill and accuracy have enabled them to move on to play a very attractive brand of running rugby. The statistics bear this out, with 55 million people watching them on TV against Scotland. Most of the games were played in front of capacity crowds. We saw people who have never had an interest in rugby as a sport being excited and enthused to follow the national team during this tournament. I think that's because Japan's skill level has improved markedly, together with their competitiveness in all facets of the game. At the end of a couple of their matches, after 70 or 80 minutes when the players would have been exhausted, their forwards still had the reserves of strength, desire, conditioning, and also the skills, to challenge and win crucial penalties at the scrum.

Another Aspect of the Legacy of Rugby

JS: Going back to the question of the legacy of rugby, the sport has become very popular in Japan now

thanks to this World Cup. How can we maintain the popularity of rugby?

Bickle: It's going to be a challenge, because when you host a tournament there is going to be interest before and during the tournament because of the media coverage. There have been a lot of initiatives around the tournament, for example the Impact Beyond initiative, where there have been outreaches to schools. Hundreds of schools have been introduced to tag rugby, providing thousands of schoolchildren with access to try these sports. Seven-a-side rugby is an Olympic sport, obviously a different game from the 15-a-side code that we saw in the World Cup, but that's another very high-profile event and I think it's important to try and link the two, to maintain the momentum. Beyond the Summer Olympics, we've got the Paralympics as well, where wheelchair rugby will be a very key sport. We're also seeing some of the regions in Japan looking to promote themselves through rugby as well. One place is Kitakyushu, which hosted Wales during this World Cup, and is also working very closely with Team GB, the Great Britain Paralympics team. They'll be hosting the Great Britain wheelchair rugby squad in Kitakyushu before the Paralympics.

So first of all, I think it's about linking rugby – in its various forms – to these mega sporting events, and secondly it's about creating opportunities for youngsters to continue to enjoy the game. It's going to be key as well to find ways to involve the Japan national team into better quality competition. It's important to give fans the opportunity to see top-quality competition here in Japan and ensure that they stay enthused.

JS: I'm interested in what you said about local-to-local cooperation, such as Kitakyushu and Wales. Do you think that kind of cooperation will grow?

Bickle: I think so. It's a win-win process for both sides. A number of rugby unions worked very hard in the build-up to the Rugby World Cup, years in advance with the towns and the cities where the teams were going to be based, and they've been running rugby programs to promote interest in the sport, but also interest in their own country. We've seen the great work being done in Kitakyushu, and I think there's been tremendous work done up in Kamaishi too with the new stadium being built there. They hosted one game during the tournament but unfortunately because of the terrible Typhoon Hagibis, the second game was cancelled. But you saw the Canadian team working with the amazing local community afterwards in the cleanup. They were building relationships there, and hopefully these relationships will continue to endure over the years to come.

JS: Do you think Japanese schools should have classes on rugby?

Bickle: I would certainly love to see Japanese schools have classes on rugby, because the values of integrity, respect, solidarity, passion, and discipline are displayed. I think the "fun" aspect of it is also

hugely important. People ask why countries like New Zealand produce so many fabulous players. I think it's because kids from a very young age pick up a rugby ball and are just playing, they're throwing the ball around, and through doing that they are developing the awareness of the game, spatial awareness, subconscious things which are the key to decision-making. These are things that develop over time and cannot necessarily be coached, so I think it's about giving kids in Japan the opportunity to enjoy the game.

JS: Some have said that leadership might also be a good thing to be developed through rugby. What do you think?

Bickle: I agree, because if you look on the rugby field, there are many leaders. Someone is obviously designated the captain, but you see a lot of communication. There are people in a number of positions who have senior roles, and it's not just the captain. I think rugby and all team sports are a chance for an individual to develop leadership skills. You don't have to be labeled as the leader to show leadership, and I think kids can learn that through sport. They don't have to be loud and vocal, they can learn and show leadership by demonstrating their commitment, their drive and determination that all of their teammates can see, so that's leading by example. Leadership is beyond just being the captain; actually showing leadership is much, much broader – showing your commitment to the team and learning how to inspire and motivate other people as well.

What We Can Expect from the Tokyo Games

JS: OK, let's move on to the Tokyo Olympics and Paralympics. That will be another opportunity to promote sports and have people visit the host country. What do you expect?

Bickle: The Summer Olympics and Paralympics is a huge opportunity for Japan, as a catalyst and a magnet for foreign tourists. The Olympics itself is a shorter tournament and geographically is broadly limited to the Tokyo area, but I think it's still a tremendous opportunity to promote the country and to bring in tourists. Hopefully, Japan and Japanese regions will build on what they've done for the Rugby World Cup, and will continue to market themselves and appeal to the tourists who come specifically to watch the Games. I sincerely hope as well that beyond the Summer Olympics, we're going to see a fantastic Paralympic Games here in Japan, certainly in terms of the legacy after London 2012. That's one of the things the London organizers are very proud of, the success of the Paralympic Games. I hope that we see that here in Japan as well, with fans wanting to come to soak up the atmosphere and see the very high quality of competition that there is around Para sports as well.

JS: You said something interesting about the Rugby

World Cup, that athletes, coaches, and tourists stay longer, because rugby is a very exhausting game, so you need about a week between matches, and that will prolong your stay in the country. In the case of the Olympics, will the time be too short to attract a lot of attention to the Games and also to the country?

Bickle: Obviously the period of the Games is much shorter, but I think there are opportunities for Japan to market itself and appeal in advance to foreign tourists who are coming to the Games to come early, in advance of the Games, or to stay on afterwards and explore the rest of the country. Japan is blessed with a remarkably efficient and extensive transportation network. It's safe and it's easy to get around to all parts of the country, and I think more and more foreigners are waking up to that realization and understanding that there is much, much more to see in Japan. But in order for Japan to maximize the opportunity, and for the regions to maximize the opportunity, they will have to actively market themselves and get creative as well.

I think tourism is a great potential source of economic benefit for local regions, and can really be a source of economic vitality for the residents of those areas. Once again, hopefully it's a win-win situation. I think that the way Japan will be able to maximize the opportunity that tourism has to offer for the Japanese economy and the Japanese people is to ensure that it is spread throughout the country. In that way, hopefully, all the regions can benefit by participating in this tourism boom.

British Chamber of Commerce's Involvement in the Games

JS: I'm curious about your chamber of commerce's involvement in promoting the legacy of the Tokyo Olympics.

Bickle: What we will try to do in terms of the legacy is to develop tourism and other opportunities for internationalization. There is interest around global sporting events, but that is just one subsector of the tourism industry, one of the offerings. In our event earlier this year based around sustainable tourism, we were looking at what we can do to help the sector. We might be able to share some things from the UK experience, where the UK government has announced comprehensive plans to promote tourism, and then hopefully Japan will be able to refer to those in developing its own best practices. The UK is focusing on things like accessibility, making many parts of the UK more accessible for people with mobility issues. There is certainly a lot for Japan to work on in that area, and hosting the Paralympics is a great opportunity to shine a light on these issues, to open up Japan to a much bigger pool of visitors.

Expected Legacy of the Games

JS: Sports is expected to play a key role in

maintaining good health among older people, which is very important in an aging society. In terms of your experience or the UK experience, what do you think about this?

Bickle: Definitely, I agree. As society ages and people's lifespans are getting longer, the key challenge now is to give people high-quality lifestyles as they age. Helping to keep people healthy and active contributes to that. There are physical health benefits from regular exercise, so sport has a role to play there. I think an important point too is to enable people to feel fulfilled, so participating in sports activities, going out to watch high-quality sporting events, all these things can help. If such activities can be offered, or made more accessible to the senior members of our society, I think they can contribute to enabling a more stimulating and rewarding life for people in retirement. To create opportunities though, there will need to be additional investment in infrastructure, and also in organization.

JS: Sports hospitality, volunteer activities, and similar "software" are a key legacy of the Olympics and Paralympics. How can Japan further promote those activities?

Bickle: I think it's about reinforcing those strengths and successes; in sports, it would be great to see continued involvement and engagement from national team players, also continued support from companies. I think collaboration is the key here. There are areas where NGOs can work together in pursuit of their goals. In terms of opportunities to create healthy lifestyles for children, hopefully there's a chance for NGOs to work together with schools, with local authorities, and maybe with their local sports teams, to involve the top-quality sports players in the community, contributing, participating, and helping out. In Japan, we're seeing more investment now in all-weather pitches, and it will be great if we can see more of those. Obviously, the cost is an issue, but hopefully there will be more investment in facilities which will enable children to more actively participate in sport.

JS: Perhaps we can take advantage of information technology and other new technologies for networking?

Bickle: Certainly. These days, with social media and technology, it's much, much easier to collaborate and promote. Many of these organizations have a social media presence to enable them to share their goals and their activities with other people. That's an important aspect of helping to create and maintain these alliances.

JS

Written with the cooperation of David S. Spengler, who is a translator and consultant specializing in corporate communications.



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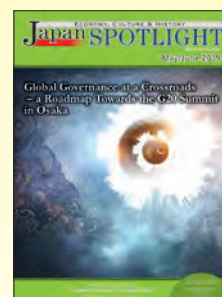
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