

Interview with Dr. Hugh Whittaker of St. Antony's College, Oxford University, author of *Building a New Economy: Japan's Digital and Green Transformation*, published by Oxford University Press, 2024

Investing in Human Capital is Necessary to Restore the Japanese Economy

By Japan SPOTLIGHT

JS: First of all, could you please tell us about your motivation for writing this book?

Whittaker: In the mid-2010s, I was struck by the overwhelmingly negative view of the Japanese economy. Many economists didn't have anything good to say about the Japanese economy, but when I visited Japan or other people visited Japan, they saw quite a few positive things in the economy. So there was this gap and economists were particularly negative. Then in late 2015, the Council for Science, Technology and Innovation came out with the idea of Society 5.0. I was initially skeptical about it, but I heard a member of the council give a presentation and explain that the Fifth Science and Technology Basic Plan envisages a fundamental shift in innovation from competitiveness and technology push-type innovation to responding to social needs. The member said that this shift in thinking was a response to the triple disaster of March 11, 2011, thinking that we have to plan for an unknown future and also need to be responsive to social needs. So I wondered if innovation policy and thinking in Japan were changing.

At the back of my mind, I had an idea that in the post-war period, Japanese institutions worked together very well, centered on manufacturing, as they did in a lot of other countries. It was called the golden era of capitalism. That fit was broken in the 1990s and 2000s as it was in many other countries. I wondered, is it possible that there is a new configuration of institutions for a post-industrial – not necessarily de-industrial – society, which is different from the postwar period of the 1950s and 1960s? That was the kind of theoretical, conceptual puzzle that I had in my head, and I thought maybe Japan could give me some answers for that.

JS: Yes, I see. Do you think the Japanese economy or Japanese political economy is responding well to social needs? Is the economic policy side providing good answers to social needs, against the backdrop



Dr. Hugh Whittaker

of rising geopolitical risks?

Whittaker: That's a very big question, and a difficult question. My first response would be that I don't think any country is dealing with the tensions that you mentioned very well. Certainly, the United Kingdom is not, and the United States is not, and often the failure in the economy is reflected in politics. From the 1980s and 1990s we had a shift in policy from maintaining full employment and Keynesian policies towards more neoliberal policies, and associated with that was growth in financial institutions and financialization, and associated with that, a rise in inequality. And the tensions resulting from the rise of inequality, in my view, produced the election of Donald Trump and Britain's decision to

leave the European Union (Brexit). Japan also experienced a significant rise in inequality in the 2000s and 2010s. I don't think Japan has dealt particularly well with inequality, but it's been fortunate that it hasn't had the same political tensions as in the US and UK, perhaps because Japan never moved so far in the direction of neoliberalism. The policies were kind of halfway between neoliberalism and the postwar system. So perhaps the political consequences haven't been so extreme because Japan did not move so far.

JS: Japan is well known for what we call Japanese socialism. Japan has long been considered one of the representatives of capitalist economies. However, many people visiting Japan, and economists in particular, would say this country is very much like a socialist country, and that's the reason Japan has been successful in responding to social needs compared with other countries. It's a sort of mixed, capitalist economy, with a kind of socialism in people's subconsciousness.

Whittaker: Yes. That subconsciousness says that we shouldn't let

inequality grow too much. It's not necessarily egalitarianism, but more like we shouldn't let poverty grow too much, and we should look out for the weaker members of society. I agree with that and that's possibly one of the factors why the political effects of inequality haven't been so extreme. But quietly, inequality has grown in Japan, and it has serious consequences that are not always visible to visitors and economists. I wouldn't say Japan has avoided these things, but the postwar stakeholder model, which had a growth and a distribution element, was compatible with the way of thinking that you mentioned, and I think it's a very good thing.

Thoughts on Institutional Economics

JS: My next question is about institutional economics. Do you think institutional economics would be a relevant theoretical instrument for analyzing the Japanese economy.

Whittaker: Well, institutions are important, but institutional economics takes different forms. For example, varieties-of-capitalism is a form of institutionalism, and the problem with a lot of the varieties-of-capitalism writing is that it puts Japan in a certain box of a coordinated market economy like Germany, as opposed to the liberal market economies of the US and the UK. If you are in a certain box, you are supposed to have certain kinds of innovative strengths and certain weaknesses. It's a very static and deductive approach. I think if you are interested in institutions, you also have to be interested in agency and entrepreneurship and how institutions change. For me, the question is how do institutions change? Why do they change? Not, "Is there a static, regular pattern and a box that Japan should be put into"?

Also, how do different institutions work together or not work together? I think that's a critical issue, and varieties-of-capitalism literature tends to think that institutions work together, basically. That's why you have varieties of capitalism, and they tend to underplay the tensions between different institutions, but there are tensions between different institutions. There was a kind of very compatible set in the postwar period, but perhaps more normal is that the institutions can clash, and how those clashes are resolved is really important. That's what my interest in institutions comes from.

JS: Many people say that reform in Japan is very slow and not sufficient, but I think any country has to be reticent and slow, as far as the reform is based on institutional change. Do you think we need to study more about historians' analysis of society and

institutions?

Whittaker: Yes, I quite agree that a historical view is really important. I think you are right that institutions change relatively slowly, but politicians like to think they can change them instantly. And so you have a lot of empty slogans by politicians that don't get enacted.

JS: You seem to have a positive view on the recent three-decade struggle of the Japanese economy because institutional change is slow and it was all of Japan struggling in the right direction, with concern for social needs. Do you think Japan is reaching a new equilibrium between the market and the government, toward a new institutional change?

Whittaker: I think a lot of economists' view of the so-called lost decades is that Japan did not change, and that was the problem. But I think there was a lot of change in Japan during the 1990s and 2000s and 2010s, and sometimes the change was contradictory. For example, in the late 1990s banks were trying to clean up their bad loans, and then there was a financial big bang and the restructuring of the finance ministry. There were so many things going on at the same time that I think it was difficult to actually focus on cleaning up the bad loans. In the early 2000s, METI, or MITI, said that Japan was going to become the leading global IT country. At the same time, the government of Prime Minister Junichiro Koizumi was intent on deregulation and not very interested in industrial policy. There was a contradiction between those two things.

I think there was a lot of awareness that Japan had to change in the early 2000s, but there was a desire to keep the good points of the stakeholder, postwar, productionist model. There was also a lot of pressure from the US to open up financial markets, so there were lots of different currents in the pressures for change, and some of the changes were contradictory. Some resulted in *kakusa shakai*, or growing inequality in Japan. I think like other countries, Japan was trying to make sense of a lot of different competitive pressures with the growth of IT and global value chains, and the rise of China. The world was changing rapidly. I don't think Japan was resisting change; I think it was trying to figure out how to negotiate the very complex, changing environment. And so I have sympathy towards the difficulties that Japan faced in the 1990s and 2000s.

JS: I agree with you, I think Japanese are basically doing relatively well in dealing with short-term, rising issues, but what we critically lack is long-term thinking.

Whittaker: I agree with you precisely on that point. I think the responses were often short term, and particularly around investment in people. Companies responded to the competitive pressures by increasing non-regular employees, and that allowed them to restore their profitability. The long-term effect of that is that, to deal with short-term competitive pressures, Japan lost a lot of the advantages in human resources that it had. Companies cut back on expenditures in training and in research and development. The government cut its spending on education, and the administrative reform of universities curbed spending. There was a long-term sacrifice or cost in responding to those pressures, and I think you're exactly right.

Possible Lessons of Japanese Struggle During the 3 Lost Decades

JS: What lessons could Japan have for the Global South in coping with some rising issues from the development process?

Whittaker: My book is not so much about the struggles of the so-called lost decades, it's about what happened in Japan after 2015. I think all countries – developed countries and developing countries – are struggling on the innovation side, with the issue of digitalization, and now we have artificial intelligence (AI) coming at us very quickly. And there's growing tension between DX (digital transformation) and GX (green transformation). On the other hand, on the distribution side, Prime Minister Fumio Kishida promoted a new form of capitalism and wanted to create a kind of virtuous growth and distribution circle.

I think, actually, all countries are struggling with this and what I see as interesting in Japan is an attempt to think into the future with Society 5.0 and say, "What kind of digital society with green characteristics do we want to create, and what does governance look like?" In other words, optimistically put, an attempt to get companies and civil society organizations looking towards the future and thinking, "How can we create a society in which we can manage these tensions, and hopefully create a fairer society?" I think there are lessons for the UK and the US and for developing countries as well. We can't simply take what Japan is doing and do it in other countries, but we can certainly learn from how Japan is approaching those challenges.

JS: I see. One concern about technological innovation might be a possible increase in unemployment because of AI or the IT revolution. What do you think about this social aspect of innovation?

Whittaker: In the UK there is a lot of concern about jobs being lost through AI. People always say it may be helpful in Japan because of the labor shortage, and perhaps AI can compensate for that. There is a much more positive view of AI and digital transformation in Japan. I think it's more complicated than that. There are complex issues of skills, and I think the background in Japan of this kind of a regular and non-regular employment divide is problematic. I think there has to be new thinking about different types of employment because AI is potentially going to change the way we work and introduce new working patterns. We have to be thinking about when people are working at home more, perhaps shorter hours, more flexibly, or different kinds of work. How do we create a social system around these different types of jobs compared with what we had when manufacturing was the core of the economy and most people – men – had secure, long-term jobs related to that?

JS: Increasing labor mobility and raising immigrant labor could perhaps be solutions for achieving a balance between welfare and efficiency, but both seem to be very difficult. In the case of Japan, where lifetime employment and seniority-based promotions and salary still exist, do you think it will be easy to raise labor mobility? And on immigration, do you think it will be easy to increase immigration in Japan?

Whittaker: The assumption about labor mobility is that people are trapped in the wrong place, so productivity suffers because people are not where they can be most effective. And we can see that with the shortage of IT-trained people and so on. For me, barriers to mobility in the form of pension portability, eligibility for re-skilling course support, and whether you can get unemployment insurance that helps you pay for those courses and so on should be addressed and should be removed. But I think this dichotomy about *job-gata* versus *membership-gata* is misleading. The word that was used in Japan's three pillars of employment was *nenko joretsu*, where *nen* is seniority and *ko* is effectiveness. *Nenko* was justified in the postwar period on the assumption that people's skills increased with their age. So if companies train people, they want to keep those people because they're becoming increasingly effective. I agree that wage systems need to be based around the effectiveness of skills, but the golden treasure is not mobility, it's companies having the right skills for the jobs. I think mobility and job-based wages help immigrants and women do better in the labor force, but I don't think the enemy is *nenko joretsu*, or lifetime employment. It's companies getting the skills that they need, and if they invest in people, they want to keep

those people. I'm skeptical about this dichotomy between *membership-gata* and *job-gata*.

Immigrant labor is going to be a big issue and a problematic issue for Japan. With immigrant labor, immigrants want to have families, and the social aspect of providing Japanese language and support for families of immigrants is a big issue that Japan hasn't really faced yet. I think that is a real, serious challenge for Japan. It creates political problems, and nationalists always want to expel immigrants. They ignore the fact that immigrants do a lot of the work that the nationals don't want to do – on farms and cleaning jobs and in the care sector – so it becomes a political problem, and it will be the case in Japan.

JS: Your book talks a lot about Society 5.0, but there seem to be some impediments to Japanese society's development of applications for IT, or even AI. What do you see as the basic cause of this? Does group-oriented behavior prevent IT applications from expanding, or are the insufficient English language skills of many Japanese people a serious impediment?

Whittaker: Those may be impediments, but I think there are two other issues. One issue is probably the flip side of *monozukuri* (manufacturing). That is a cultural value of producing things, and a kind of a lack of value placed on software and software skills in companies. It has been difficult for software engineers to become influential in companies, as there is kind of a hardware mentality. The undervaluing of software skills has been one issue. And a second issue, which I came across 30 years ago in the 1990s, is that people described the software industry as being similar to the construction industry, in that it's outsourced and there are tiers of suppliers doing contract work, without building up software skills in the companies themselves. I think the two of those are linked, and that is a legacy problem. The strength of the manufacturing economy created this weakness in appreciation of software in core companies.

Restoring the Japanese Economy as a New Economy

JS: Thank you. One last question: what do you think would be the key factors for achieving Scenario 1 in your book – the restoration of the Japanese economy? Is it a bad idea to measure economy restored in terms of GDP, when Japanese GDP growth is much lower than in other countries. What

do you think will be vital for the Japanese economy to reverse that trend?

Whittaker: I think this is connected with what you said earlier about the so-called lost decades – the short-term response versus a long-term response. There is a long-term cost for companies' short-term responses of cutting down on capital investment, on research and development, and on personnel costs, and that is a sacrificing of long-term competitiveness and productivity. Companies were very successful in controlling their costs and they built up very big internal reserves, and now maybe they're starting to increase their capital investment again, but they haven't really increased their investment in human resources. I think overcoming that legacy of the so-called lost decades will be important for Japan.

And I think social investment is going to be a critical issue, because AI is going to change the nature of jobs and the structure of labor markets. Investing in people so that people can get jobs that add significant value is a crucial challenge, that I think is recognized in Japan. Late Prime Minister Shinzo Abe had his *hito zukuri kakumei* (people-creating revolution) and Kishida had his idea of investing in people and making them the center of the economy, but quite often the measures adopted were short-term, temporary measures. I don't think they have had much of an impact. I do think investing in people, as a kind of a Japanese version of a social investment state, is going to be a critical issue for Japan.

JS: I see. So investing in human capital would lead to the building of a new economy. In that sense, institutional economics or studies of history should be important analytical tools.

Whittaker: Indeed.

JS: Thank you very much.

JS

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