

Pondering the Future of the Japanese Economy and Changes in the Corporate Community

■ Factors affecting trends in employment

Nikai: In Japan, what we call “non-regular employment,” which is temporary or part-time employment, has been increasing for



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the past 10 years. In comparison with regular employees, who are also called full-time employees, non-regular employees have less employment stability and security, and an unsatisfactory standard of living. Partly due

to recent positive economic trends, the idea has emerged that it would be beneficial, not only to individual companies but also to the Japanese economy as a whole, to maximize the hiring of full-time employees. What are your thoughts on this issue?

Emmott: The growth of non-regular employment in recent years has played a very important role in the recovery of Japanese companies by helping to cut costs.

But the growth of non-regular employment has also created two problems as a result, one a short-term problem, and the other a long-term one. The short-term problem is lower wages as the compensation for flexible employment, which is actually essential for cut-

ting costs. But it also led to reduced consumer demand, and thus is not a very sustainable basis for the economy. But the good recent news is that full-time employment is increasing again, and wages are rising as well, which is a much more sustainable economic situation.

The long-term problem is that it is very difficult to maintain a system consisting of two different types of employees, some with strong protection and others with much less. I think that all Japanese companies need to achieve faster productivity growth in the future. To realize this, you need a system in which everyone in a company cooperates with each other. If you have inequality among them, it will be more difficult to achieve faster productivity growth.

Pressure from shareholders and capital markets leading to changes within corporations

Nikai: During the Heisei Recession (mostly in the 1990s), two approaches were taken to weather the difficult times. Some companies boldly undertook very drastic restructuring, while others rode out the crisis through wage cuts negotiated between management and employees. The latter companies could be characterized as having a typical “Japanese” frame of mind. What are your thoughts on that point?

Emmott: In the past, the latter sort of Japanese-style company managed to adapt through the willingness of its employees to share the burden, and getting them to agree to big changes. But that is easier in a time

of fast growth than in a time of slow growth or recession. Today, probably, companies need the ability to restructure more easily than in the past.

I am very encouraged by the fact that there have been many M&As in Japan over the past few years. I do not mean hostile M&As, but friendly ones. It is a good way to reallocate finite resources. Also, it provides a way in which companies can focus their resources more effectively on what they are really good at. It is a positive transition.

I like the way in which shareholders in the recent capital market have increased the pressures on company management to promote efficiency.

In a very simple way, the Japanese economy was quite successful in the 1970s, or even earlier, because it had some discipline, particularly coming from the main bank system, and because it responded well to changes. It was very flexible at adapting to technological changes and new markets. In the 1980s, with the bubble, it lost discipline and the ability to adjust

to changes. Now, without throwing away the old strengths of the Japanese companies, you need a new source of discipline as well as the capability to adapt. From that perspective, the current situation in which corporate discipline is enhanced by shareholders is a good starter.

Aiming at an Asian version of the European Union

Nikai: I would like to hear your thoughts on the relationship between Japan and China. There is



Bill Emmott

Former Editor-in-Chief of *The Economist*, and author of *The Sun Also Sets* and *The Sun Also Rises*

an extremely long history of interaction between us. Our two countries are separated by only a narrow stretch of ocean, and better relations between us is one of the most important issues. It is not just a bilateral issue, but one that can have an impact on Asia and other countries around the world. How do you view the relationship between Japan and China?

Emmott: I think that China is a huge opportunity for Japan and could be a big problem at the same time.

It is a big opportunity because it is a great advantage to have such a large market developing so near your borders. You are very lucky that you are only separated by a small stretch of water from such a market.

As I mentioned, however, it could

also be a big problem, not only in political terms, such as the Yasukuni-related controversy, but also in the context of Chinese ambitions to be the leading country of the Asian region.

For the longer term, Japan needs to gradually establish a foundation and work step-by-step to develop some kind of Asian version of the European Union, in order to channel cooperation between Japan and China – and other countries – in a positive direction, and to prevent competitive or negative aspects of the relationship between the two nations.

Nikai: I am very grateful for your appropriate advice. I think our proximity to China may occasionally cause squabbles, given the 2,000 years of history behind the relationship. However, from a long-term standpoint, Japan and China need to

promote better relations, progress together, and contribute to Asia and the rest of the world.

In terms of an agreement among multiple countries, I think the ASEAN framework would be most suitable. I recently co-chaired an ASEAN meeting in Kuala Lumpur, and I believe Japan needs to respond to ASEAN members' high expectations by placing increased emphasis on these conferences. It is necessary to look for resolutions to various issues, including Japan's relationships with China and South Korea, in parallel.

Japan also considers India important. I have frequently exchanged opinions with Indian cabinet ministers at WTO meetings. We always talk about cooperating and contributing to each other's development by tapping our respective strengths. What I am now hearing from India is that they want us to bring in Japanese SMEs. Since the end of last year, I have sent five high-level delegations to India. Indian cabinet ministers are also scheduled to visit Japan in the near future.

“The Sun Also Rises” – What is required for sustained growth of the Japanese economy?

Nikai: Japan has a massive budget deficit. To eliminate this, it is necessary to implement an integrated reform of both revenues and expenditures. Simply reducing expenditures and raising taxes will not offer the Japanese people a bright future. That will require income growth, together with growth in tax revenues that result from an active economy, rather than higher tax rates. I think the most important issue is stimulating increased activity in the Japanese economy.



Nikai (left) and Emmott having a discussion about the future of the Japanese economy

And when the sun rises again, it will be necessary for the risen sun to continually shine on Japan and the rest of the world. To that end, the Ministry of Economy, Trade and Industry (METI) is placing emphasis not only on advanced, world-leading enterprises, but also on fields where Japan is lagging, and industries in which room for growth exists.

One of the areas we are actively supporting is SMEs in the manufacturing sector, which can be expected to give rise to innovation. We are also emphasizing service sectors, including the distribution and tourism industries, where Japan is lagging a bit behind other countries. Furthermore, we want to work on effectively using information technology (IT). *Innovate America: Thriving in a World of Challenge and Change*, the so-called Palmisano Report, was released in 2004. The objective of this report was to strengthen the global competitiveness of the US economy over the long term. Since its release, Republican and Democrat legislators, the corporate community, and academia have been involved in the submission of bills oriented toward achieving this objective. In this connection, President Bush clearly outlined a policy for strengthening global competitiveness in his State of the Union address this year. In view of these conditions, our country should also allocate resources to the strengthening of competitiveness. This is our New Economic Growth Strategy. I would like to hear your opinion on what is needed to produce sustained growth in the Japanese economy.

Emmott: Nobody predicted 15 years ago that the US retailer Wal-Mart would be one of the pioneers of the

productivity revolution, through the use of IT. There could be some potential growth in Japan's retail sector if they apply the lessons of Wal-Mart.

I also believe great benefits could be gained by stimulating more competition among companies so that they become even more competitive.

Nikai: Your focus on the retail industry and on promoting competition among companies is very interesting and pertinent. METI is working to resolve retail industry issues and stimulate regional economies by pushing reforms of relevant laws. In addition, METI is actively involved in measures to revitalize small communities through extending active support, even sending officials to help these communities.

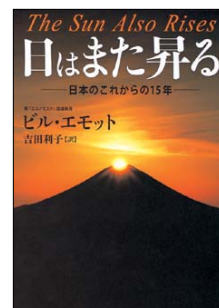
Emmott: That is very interesting.

Nikai: It is generally believed that achieving economic growth in the face of a declining population is difficult. However, I intend to stand that piece of conventional wisdom on its head and produce economic growth despite the declining population. I am resolved to ensure that the sun keeps rising.

Emmott: You are right. There is every chance, even with a declining population, that Japan can have strong growth in living standards, because there is so much potential



Emmott (left) and Nikai shaking hands after their discussion



The Sun Also Rises

Emmott's latest book

for productivity growth and promoting various reforms, perhaps even with the effect of the labor shortage, which may make it easier to produce reforms that affect parts of the economy that have employed a lot of people. And perhaps there will be jobs in other places for those people in the future.

Nikai: Thank you very much for this extremely encouraging conversation. **JS**

*Note : This column is an excerpt from 2006/April issue of METI Journal.