

Toward a Competitive and Participatory Society

21st Century Economic and Industrial Policy — Key Points from the Discussion Agenda

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Introduction

—Toward a New Self-Image

The Industrial Structure Council held a general meeting this past June 4 to discuss "21st-Century Economic Industrial Policy." In order to prepare for formulation of the so-called "Vision for the 21st Century," the "Discussion Agenda" was put forward by MITI, and announced to the public to solicit public comments before the start of all discussion at the Council.

MITI has prepared its policy visions once every ten years for the past several decades. The vision for the 1960s emphasized the heavy chemicals industry. The vision for the 1970s focused on a shift to knowledge-intensive industry. The vision for the 1980s stressed energy security. The 1990s version adopted as its main theme the issue of Japan's contribution to the international community. Discussion concerning the latest vision, which is being drawn up on the cusp of the 21st century, has been based on the realization that there is a need to formulate new policy goals and build economic and social systems with a long-range plan in mind. This effort must reflect an understanding that the historical conditions surrounding Japan's economic growth are undergoing great change. With earlier visions, there was a strong tendency for the national government to develop a forecast of its anticipated industrial structure, and for the vision to seek ways to achieve the targets set forth by the national government. The 21st-century vision, in contrast, accepts as a given that the future is very uncertain. Working on the basis of a long-term outlook through the year 2025, the new vision seeks to anticipate the main issues that Japan is likely to face, and upon this basis determine the general direction of economic and industrial policy as well

as the direction in which the Japanese economy and society should be moving. In other words, the main focus of the current effort has been to depict an image of Japan as it will look in the future. The outlines of this image, which are described in the MITI's Discussion Agenda, are as the following:

Tenor of the Times

—Post-war Economic and Social Systems Face Pressure to Change

A half-century into the post-war period, Japan has compiled a brilliant record of economic success. Its economy accounts for 15% of the world's total economic output, and the country boasts the highest per-capita income among the world's developed economies. In addition, social infrastructure, housing, and other assets built up during the course of the country's economic development contribute to the welfare of the entire population. Japan has enjoyed low rates of poverty and crime, and a high level of employment. We have built an economy and society that are noted throughout the world for stability and a sense of fairness and equality.

What has supported this post-war economic development, though? If one were to attempt to describe in a few short words the nature of the economic and social systems that we have built up, the following three descriptions might come to mind: "Massive intake of resources, massive output of goods." And here is another aspect: "Assumption of rapid growth, heavy reliance on a young labor force." (Note 1) And yet another formulation: "A system based on self-sufficiency, in which each organization possesses its own personnel and other resources." (Note 2) Structural change, however, has put an end to all of that. Youth now constitute an ever-

shrinking portion of the population, the economic growth rate has slowed, and the economy has lost its role model. Japan can no longer rely on such circumstances.

Looking ahead to the coming quarter-century, it would seem reasonable to anticipate the following:

- (1) Population will shrink and the population will age and decrease faster than in other countries. (Note 3)
- (2) A number of global problems will come increasingly to the fore, including global warming and the scarcity of energy resources, etc. (Note 4)
- (3) Markets will become integrated on a global scale.
- (4) The rapid development of information technology, biotechnology, and other new technologies will bring social change at a vertiginous pace.

If we sit idly by without attempting to make any change on our own part, Japan, with all its various limitations, could find itself plunging down a slippery slope.

Note 1: The government's fiscal policy was based on an assumption of continuing rapid economic growth. Assuming high GDP elasticity with respect to tax revenues, the government engaged in aggressive infrastructure spending and counted on its ability to recover the investment costs in later years (the GDP elasticity with respect to tax revenues for the past half-century has been 1.05, while the tax revenue elasticity with respect to public works expenditures has been 1.21).

The system was based on the assumption that the structure of the general population and the work force would always take the shape of a pyramid, with large numbers of young people supporting small numbers of aged persons. The

social safety net consisted of long-term employment, seniority-based promotions and pay raises, as well as pension systems and health care funding by an inter-generational transfer of income.

Note 2: The decision-making mechanism of this type of organization is not subject to the scrutiny of outsiders, and corporate governance is carried out by the group's main bank. Such organizations maintain in-house possession of all their personnel, technology, information, and other resources. Furthermore, they evaluate their management and carry out risk response on their own.

Note 3: Japan's population has risen continuously since the end of World War II, but it is forecast to peak in 2004 (at a conservative estimate of 127 million) before decreasing by about 10 million by

developed country (28% in Japan, as compared to 18% in the U.S., 20% in England, and 22% in Germany.)

Note 4: The average global temperature is forecast to rise by 1.0 to 3.5° C by the year 2100, thus causing the sea level to rise by 15 to 95 centimeters (according to a report by the Intergovernmental Panel on Climate Change). To resolve the problem of global warming, it will be necessary to reduce carbon dioxide emissions to less than half the current level.

In addition, the nations of Asia are expected to import 1.7 times more energy resources from outside the region in the year 2010 than they do now (according to the consensus of the APEC Energy Ministers' Meeting of 1998). In the future, the scarcity problem of energy resources is expected to be serious, especially in Asia.

in today's world are generating new opportunities. If Japan can develop a uniquely Japanese response to these problems — a response that reflects Japan's experience, culture, and spiritual milieu — we will have a chance to communicate our values to the rest of the world. If we can tap the same adaptability that enabled us to catch up with the West and respond successfully to the oil crises of the 1970s, there is a very good chance that we may be able to build a uniquely Japanese economy and society that respond to the changing times and yet are neither American nor European in form.

On the basis of this understanding, the idea of "active individuals and a secured nation" has been put forward as the type of economy and society that we should be aiming to achieve. In order to build a vibrant economy amidst rising uncertainty as well as a globally unprecedented trend toward smaller and aging population, society urgently needs active individuals who take full advantage of their individuality and abilities while seeking aggressively to achieve self-realization and to create their own values. At the same time, the nation must fulfill its fundamental responsibility to create an environment that is conducive to the cultivation of active individuals (participating actively in the creation of a new world order, eliminating obstacles in Japan, establishing rules, and building a social safety net).

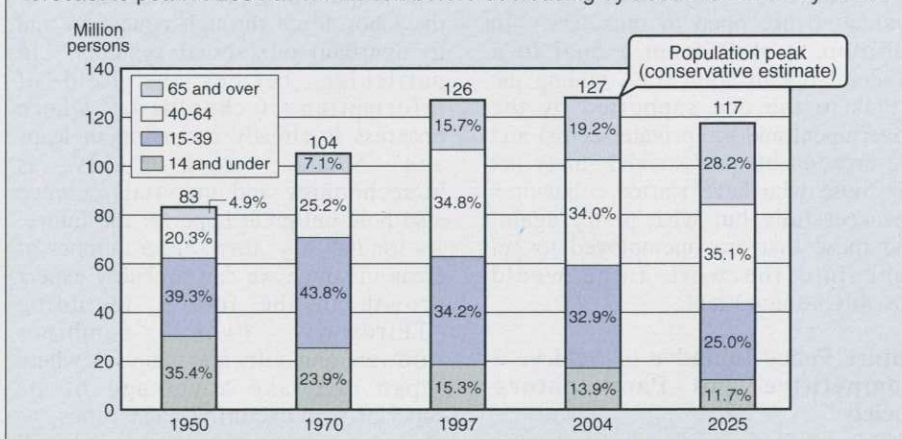
Basic Direction of Economic and Industrial Policy

—Formation of a Competitive and Participatory Society

As we seek to build active individuals and a secured nation, the basic direction of economic and industrial policy is to promote the formation of a competitive and participatory society. In other words, we must seek to achieve the following two goals: (1) strengthening competitiveness of economic and social systems; and (2) a widely participatory society in which

Figure 1. Population Trends

Japan's population has risen continuously since the end of World War II, but it is forecast to peak in 2004 at 127 million before decreasing by about 10 million by 2025.



2025 (See Figure 1).

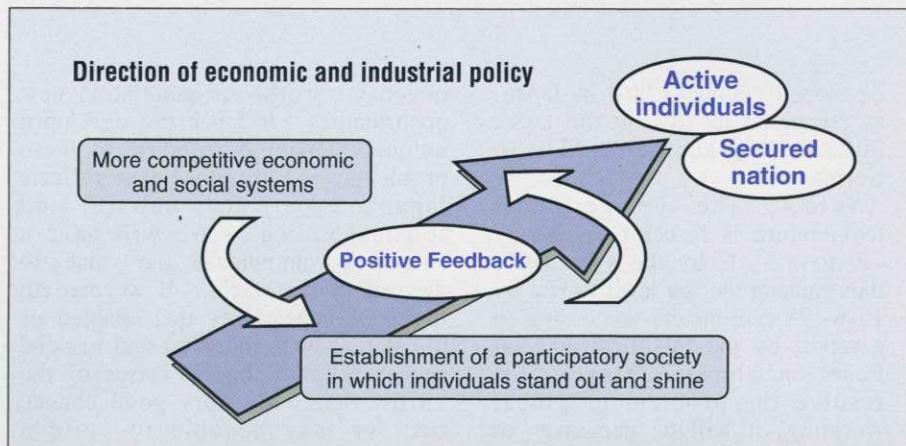
By the year 2025, the number of persons aged 65 and over is expected to increase by 13 million, and the percentage of the population accounted for by the elderly is forecast to increase from 14.5% (1995) to a level markedly higher than in any other major

Entering the 21st Century as a Forerunner

—Changing Times, Emerging Opportunities

Considering the fact that aging populations and environmental problems are common to all developed nations, the big changes taking place

Figure 2. Vision for 21st Century Economic and Industrial Policy



individuals stand out and shine (See Figure 2).

Against the backdrop of market integration on a global scale, we need policies that will advance economic structural reform and overcome various restrictive factors, thereby enhancing the international competitiveness of our economic and social systems. At the same time, amidst the growing demand for expression of diverse values, and with the arrival of an aging society, we need policies that are capable of bringing about the type of society which offers a wide variety of employment, ample opportunity for social involvement, and an atmosphere in which individuals can exercise their abilities to the fullest. We need to implement the kind of multi-focused policy described above in order to bring about the formation of: (1) an economy and industry capable of supporting a tough and vibrant supply base; and (2) a society in which individuals have hope for the future and are able to participate in society in many different ways. We believe that only when these two elements have both been achieved will we be able to build an economy and society capable of functioning smoothly on a sustained basis.

Toward this end, Japan's existing systems must be changed drastically. We will have to achieve a bold conversion to new systems that are in step with the needs of a new age. For example, the system of seniority-based pay raises could be completely done away with by altering the treatment

based on the evaluation of each employee's ability. The system of long-term employment, in the meantime, could be continued for core employees but replaced otherwise by a more flexible system of employment. This new system would need to take a neutral position with regard to job switching, would have to include a safety net, and would have to promote greater job mobility (especially among white-collar workers). In addition, there is a need to abandon the self-sufficient corporate model in favor of an open, decentralized type in which opportunities, information, and evaluation are open to outsiders. In addition, a shift from a dual to a trilateral organization (i.e., adding the NPOs to the one supported by the government and the private sector) and the creation of a substantial safety net for those who have started a business unsuccessfully but wish to try again, and those that are unemployed to get back into the work force would possibly be important.

Future Policy Initiative to Achieve a Competitive and Participatory Society

(1) Japan's Long-Term Economic Prospects

With Japan's population expected to begin contracting soon, there are many different views concerning Japan's long-term macroeconomic prospects, especially its prospects for economic growth, but the following three points must be noted. (1) Against the backdrop of increased take-home pay and an aging society, income

redistribution need to take place more smoothly and negative assets will be reduced. (2) Japan will seek to secure its national interests in the international community (i.e., it will see to it that the weight its voice carries in the international community fully reflects the size of its economy), fulfill its responsibilities in the international community, and respond to the expectations of countries throughout the world. (3) If people are to have hope for the future and be able to make a diverse range of values into a reality, economic growth of roughly 2% (driven by technological innovation) will be necessary in order to ensure the existence of an "economic frontier" where people can challenge themselves and pursue their dreams (See Figure 3).

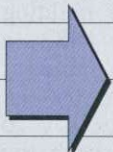
To achieve these goals, however, we will need to fully exploit our nation's growth potential by pulling out all the stops to achieve higher total factor productivity (TFP). To do this, we will need to implement the multi-focused policies described above as we work to achieve technological innovation, to improve the quality of the labor force through education and to overhaul our social systems. In particular, besides the field of information technology, where progress is already occurring in leaps and bounds, such fields as biotechnology and materials science also hold out great hope for the future. As for industry, there are a number of areas in which we can probably expect growth in the future, including "Thirdware" (which combines hardware and software), an area where Japan can take advantage of its superior manufacturing capabilities, as well as a number of industries that will meet the emerging needs of the Japanese society of the future. Such fields include industries that serve the needs of the elderly, environment, and *kansei* (industries that satisfy needs derived from a lifestyle of refined sensibility).

(2) Policies for Achieving a Competitive and Participatory Society

Figure 3. Direction of Future Macroeconomic Trend

If we stand by and do nothing, Japan's rate of economic growth will slip into negative figures, leading to a decline in per-capita take-home pay and an increase in the cumulative fiscal debt to more than 400% of GDP.

If we are to limit the people's tax burden and ensure that per-capita take-home pay continues to rise, we will have to take a series of bold reform measures to achieve higher total factor productivity (TFP).

FY 2010-2025	If no action is taken		If reforms are implemented
Economic growth rate	approx. ▲0.3%		approx. 1.8%
Per-capita economic growth rate	approx. 0.2%		approx. 2.3%
Growth rate of per-capita take-home pay	approx. ▲1.1%		approx. 1.8%
Tax burden	approx. 63%		approx. 49%
Cumulative fiscal deficit (as % of GDP)	approx. ▲442%		approx. ▲40%

Note: These figures were obtained by using the supply-side macroeconomic model based on the Cobb-Douglas production function. A certain margin of error must be allowed in their interpretation. (Source: calculations by the Ministry of International Trade and Industry)

Assuming that the previously described economic outlook holds true, and that Japanese industry develops its potential as noted above, we propose the following policies for achieving a competitive and participatory society.

In working to implement these policies, it is important that we seek to expand new "rent" (creative scarcity value), cut costs, and minimize risks.

[Policies to Enhance the Competitiveness of Japan's Economic and Social Systems]

(1) Increase technological innovation (building of a technological innovation system that relies on open network; a national initiative that identifies key fields; strengthen technological governance; more effective use of research personnel)

(2) Providing a business environment that takes advantage of the latest information technology (use of information technology to develop an entirely new business model, and to develop information infrastructure and social rules)

(3) Formation of a closed resource cycle economy that blazes a new path for the world (integration of the environment and the economy by converting external costs into internal costs through such means as recycling, reduction, and reuse)

(4) Achievement, both internationally

and domestically, of economic order and economic security (for the sake of enhanced competitiveness: reappraisal and reform of the domestic economy; building of international economic rules; achievement of energy security)

(5) Move toward the formation of an Asian economic sphere (establishment of a complementary economic relationship between Japan and the rest of Asia; alleviation of problems (energy and the environment) that restrict economic growth in Asia)

[Policies to Bring About a Participatory Society in which Individuals Stand Out and Shine]

(1) Training of personnel who are highly creative, possess specialized knowledge, and are well prepared to communicate with people from other countries (lifelong learning to develop a diverse range of specialized skills; reform of primary and secondary education; improvement of international communication skills)

(2) Providing a wide range of opportunities for employment and participation in society (home-based employment; flextime work scheduling; employment for older persons; an age-free model to allow expanded opportunities for participation in "a society that makes you forget your age"; facilitation of the activities of NPOs)

(3) Providing an environment which revitalizes entrepreneurship (support for home-based businesses or "SOHOs (Small Office Home Office)," microbusinesses, etc.)

(4) Providing an environment that enables individuals to feel proud and happy to give birth and raise children (reversal of the trend toward fewer children per family)

(5) Support for those who wish to re-enter the work force, and establishment of a more complete social safety net (encouragement of those who have started a business unsuccessfully to try again; facilitation of job switching; avoidance of the persistent inter-generational tensions over income distribution; establishment of a social safety net)

Conclusion

The purpose of this overview is to serve as a point of departure for further discussion by the Industrial Structure Council. The most important thing is that the public and private sectors come to a common understanding concerning the state of the nation, that they build upon this common understanding to discover the direction we should be moving in, and that they share a common process.

We are faced with the task of navigating through seas that are in many respects uncharted, but our real problem is yet even more serious — we do not even have a completely reliable compass in our possession. It is our hope that this document will spark wide-ranging and constructive discussion.

[Note] The Industrial Structure Council started to discuss the 21st Century Vision in September. The final report will be completed by March, 2000. The Discussion Agenda, of which the outline is described here in this article, is supposed to serve as a catalyst to facilitate wide-ranging discussions among the public, and not as a final draft imposed by the government.

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