Mounting Expectations for Progress on Structural Reforms

The Heavy Responsibility that Comes with the Public Trust

By Izumi Masaki

THE Liberal Democratic Party (LDP) won a historic victory in the general election on Sept. 11, 2005, in which Prime Minister Koizumi Junichiro appealed to the country on the postal privatization by dissolving the House of Representatives. The LDP won 296 seats, and combined with its coalition partner, New Komeito, the ruling alliance controls 327 seats – more than two-thirds of the House of Representatives – gaining overwhelming public support for the structural reforms of the Koizumi administration. As a result, the postal privatization bills, which were rejected by rebels from within the LDP in the plenary session of the House of Councillors in early August, will be revived, and expectations are mounting that progress on structural reforms will gain momentum.

The postal privatization bills consist of six bills including the Postal Privatization Bill, which contains the basic principles of privatization, and the Japan Post Joint Stock Company Bill, which provides for a holding company. The bills require Japan Post to be privatized and split into four separate companies in April 2007: over-the-counter services, postal services, postal savings and postal life insurance, all under a holding company. All of the shares in the postal savings and postal life insurance companies owned by the holding company should be sold within 10 years of privatization.

Nevertheless, the government heaped compromise upon compromise to gain the agreement of the LDP, which accounts for the majority of the opponents of the postal privatization bills, and the content of the bills has significantly receded from the Basic Policy on the Privatization of Japan Post determine by the Cabinet in September 2004. The truth is that the introduction of the market mechanism and achievement of economic revitalization through fair competition as a private company, which were presented by Takenaka Heizo, the minister for privatization of the postal services, are strictly dependent on future efforts by the government and Japan Post.

The major differences between the Basic Policy and the bills are as follows. (1) For the location of post offices, the Basic Policy requirement that efforts be made to ensure locations are easily accessible to residents has been changed to state that offices should be located nationwide according to the principle of universal accessibility. (2) While the Basic Policy made no mention of uniform, nationwide financial services, this has been changed in the bill to a commitment to deliver over-the-counter financial services for the sake of local communities, using the social and local contribution fund. (3) On the complete separation of the two financial companies, the Basic Policy stated that the postal savings and postal life insurance companies will be sold during the transitional period to realized privately-run companies. Stockholdings in the postal savings and postal life insurance companies after the end of the transitional period will now be allowed in the bills in order to facilitate group management under the holding company. (4) Under the Basic Policy, employees were to lose the status of civil servants, but the bill pledges that public qualifications will be established in order to certify non-public servants handling content-certified mail and special deliveries. (5) The schedule for the postal privatization was set on April 1, 2007 on the Basic Policy, but it has altered in the bill to Oct. 1, 2007 in the case of delays in system development.

The criteria of post office locations were limited in a bid to encourage greater efficiency, with Takenaka taking the view that “If the obligation is based on the law, the government will definitely have to pay the cost somewhere. Minimizing obligations is the path to small government.” However, there was a series of calls from within the LDP demanding that the current post office network should be maintained out of consideration for local constituents who fear the loss of post offices in remote areas. As a result, the provision on obligation was incorporated into the bill. This makes it difficult to push for the consolidation of post offices in unprofitable areas, and it is possible that the high cost structure will persist.

The Basic Policy stipulated uniform, nationwide services only for the postal services company, based on the view that these are essential services which are not adequately provided by others and there is little need for obligation on the part of the postal savings and postal life insurance companies. However, because the post office’s source of profits is in fact its two financial businesses, it appealed strongly for the continuation of its profitable operations. As a result, this became a major point of contention in the course of the consideration of the bills by the government and the LDP. Finally, instead of obligating the two financial companies to provide a uniform, nationwide service, the bills established a “social and local contribution fund” to create a mechanism whereby the postal company will provide over-the-counter financial services as a business making a contribution to the local community in accordance with local demand.

In order to fully privatize the two financial companies, the bills also expressly stated that the two companies' shares will be completely sold for risk hedge and privatization, during the transition period as in the initial plan. However, the government and the ruling parties agreed that the holding company will continuously own shares of the two financial companies in order to facilitate group management. The possibility remains that a massive financial institution in which the government owns an indirect equity stake will be retained, and this framework could water down the significance of fiscal reform to change the flow of funds from the public sector to the private sector.

When the post privatization bills were rejected in the House of Councillors, though, the financial sectors including banks and life insurance companies voiced dissatisfaction that it was a "setback to reform of the bloated public finance sector." Postal savings and postal life insurance soak up about 30%, or ¥330 trillion, of the personal financial assets in Japan, and even though the content of the bill was inadequate, there had been an expectation that it would be a breakthrough in merging them with the private financial sector. Postal savings account for ¥210 trillion, and postal life insurance accounts for ¥120 trillion.

Even the major banks and life insurance companies cannot possibly compete in terms of the scale of funds. The common view in financial circles is that "placing a massive volume of funds outside market principles inhibits the efficient distribution of capital." (Maeda Terunobu, Chairman of the Japanese Bankers Association, and President and CEO of Mizuho Financial Group). Japan Post President Ikuta Masaharu has constantly stressed that "The postal service is in medium and long term decline. To overcome this, we hope the government will revise the Japan Post Law to help new entrants or privatize Japan Post." The postal service, which had sustained a loss-making structure for many years, has tried to reduce procurement costs and increase the efficiency of its operations since the creation of the public corporation in 2003, making a small surplus in the process. However, with the increasing popularity of e-mail, the decline in the number of postal items handled has not stopped, and making up for this decline with cost reductions alone has its limits. Although sales of "Yu-Pack" postal parcels have risen, the market share lags far behind major delivery companies such as Yamato Transport and Sagawa Express.

The balance of postal savings, which is Japan Post's biggest source of income, also fell below ¥210 trillion at the end of July, declining by ¥50 trillion from its peak in 1999. This trend will continue because a series of fixed term deposits are approaching maturity, and under the simple business model of offering low interest rates for secure assets such as government bonds, the reduction in assets will lead to a decline in income.

In these circumstances, Koizumi literally stuck with the privatization of Japan Post, and took the decisive action of dissolving the House of Representatives while consistently emphasizing to voters, "If we do not achieve postal privatization, there will be no progress with other structural reforms." Koizumi's high-handed tactics were criticized for being "undemocratic," "focusing only on postal privatization," and "diverting attention from more important problems such as pension reform and diplomacy." Nevertheless, in the eyes of the people, who have suffered from the collapse of the bubble economy for many years and have pent-up dissatisfaction with the delay in reforms, the LDP rebels must have appeared as conservatives only defending vested interests, while the opposition parties' arguments seemed like tactics to contradict everything and cloud the issue, and they have given Koizumi unprecedented authority through their voting behavior.

With the landslide victory for the LDP, Okuda Hiroshi, Chairman of Nippon Keidanren (Japan Business Federation), released the comment, "This shows that Koizumi's structural reforms have received the endorsement of the people. We hope that the prime minister will get the postal privatization bills approved as soon as possible, and use this as a breakthrough to take decisive action on outstanding structural reforms with a sense of urgency." The governor of the Bank of Japan, Fukui Toshihiko, also expressed his expectations for the progress of reforms, saying that "postal privatization will be a major plus for the national economy in the long term. The fact that funds which are now only used to certain ends will be put to a variety of uses is extremely positive."

In addition to postal privatization, there is a throng of reform issues, including the integration of government-affiliated financial institutions, a review of social security-related expenses, a reduction in public service personnel and personnel expenses, and the "trinity of reforms" which center on the transfer of tax revenues to the regions. The abolition an amalgamation of government-affiliated financial institutions is positioned as the gateway reform for freeing up the postal savings funds, and is arguably unavoidable in promoting the efficient allocation of funds from the public sector to the private sector. Koizumi will have to accelerate his efforts on a series of issues and show the people the outlook for the total reform package until the expiry of his term as leader of the LDP in September 2007. JS

– This series will be written by Aoki Masaru from the next issue –

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