

A Policy Plan for Restructuring Japanese Industry

-MITI's policies for fiscal 1987-

By Shinji Fukukawa

Introduction: toward the 21st century

During the 1980s I have come to feel that substantive structural change is taking place in our economy and industry.

First, we are entering an era in which the international economic and social order will be maintained and managed through the solidarity and concerted action of the leading industrialized nations. I have dubbed this change a shift from *Pax Americana* to *Pax Consortis*.

Japan must bear its share of the responsibility for maintaining the international economic system in this new world. It must contribute to providing for the international public good.

The second change is that, in parallel with progress in technological innovation and the information revolution, our industrial society is evolving a new structure. Symbolic of this is the shift that has recently been taking place in the composition of industry in Japan—from a stress on so-called HTLL industries (heavy, thick, long and large industries such as steel and chemicals) to LTSS industries (light, thin, short and small industries such as semiconductors, new materials and biotechnology). The emergence of computer and communications technologies and the new materials that are today beginning to appear in increasing numbers presage a clear shift from the distinctive pattern of 20th century industrial systems—large-scale production stressing “economies of scale”—to that of the 21st century—small-scale production of a wide variety of goods, based on “economies of scope.” This change also signals the dawn of an era of proliferating

new technologies, made possible by the fusion of technologies from many disparate fields.

The third great change is the evolution of new lifestyles and life cultures. People today are likely to be more concerned with the quality of life than the merely material, and to find a growing enjoyment in intellectual and creative pursuits.

The most successful products put on the market today are beautifully designed and stimulating to the senses. They are “fun” products, and have a creative freshness about them. They are a clear manifestation of these new trends.

Confronted with these three transformations, the issue we must address is how they can be fused and developed to ensure a brighter future in the 21st century.

Imbalance: problems and solutions

Imbalances in international socio-economic structure

A number of problems of imbalance can be identified in the world today.

First, there are the imbalances in the current accounts of industrialized countries. Behind these lie the major role played by capital transactions in determining the formation of exchange rates. Today's floating rate system simply lacks the ability to control adequately current account positions. Savings and investment gaps between countries and, closely related, different stances on macroeconomic policy also contribute to the current account problem.

The second major imbalance is the widening gap between the economic

power of North and South. We were moving in the right direction to close this gap during the 1970s, but in the 1980s the disparities have once again begun to grow.

Third, and reflecting this North-South gap, is the global maldistribution of wealth, as symbolized by the expanding external debt burden of developing countries. Certain industrialized countries have growing funds surpluses, while developing countries lack even the means of making external payments.

Coming amid the deepening of interdependency among the nations of the world in various fields of the economy, from trade to technology, capital and financing, these imbalances indicate the importance of supplementary measures to preserve and strengthen the free trade system and enable concerted action on macroeconomic policies and the recycling of funds.

Imbalances in the Japanese economy

What imbalances are found in the Japanese economy? Let us begin with the problem of Japan's current account.

The real roots of this problem are to be found in the declining utility of exchange rate controls and the existence of a macroeconomic supply-demand gap. But additional key factors relate to Japan's industrial structure, which readily generates surpluses.

Measures to rectify this situation should include the promotion of imports and the greater internationalization of Japan's domestic markets. A solution also requires encouraging the international division of labor by such means as stepped-up overseas direct investment and the adoption of structural measures to expand domestic demand.

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Wall Street and other financial centers will see stepped-up Japanese direct overseas investment.

The second imbalance affecting the Japanese economy is the gap between savings and investment, which is closely tied to the country's current account surplus. If artificial means were used to bring about the appreciation of the yen, it might be possible to reduce the imbalance between savings and investment. This kind of deflationary solution would be undesirable, however, both domestically and internationally. The solution instead lies in the expansion of investment, where there is great potential for success. There are many areas of the Japanese economy that require expansion and improvement, from housing and public facilities to new types of industrial facilities for information exchange and facilities for international interchange.

The third problem is the economic disparity between Japan's central areas and its outlying regions. With cutbacks in public works spending—a result of fiscal austerity as the central government tries to reconstruct public finances—the disparities have again begun to widen. Progress in developing the foundations of an information-oriented society in Japan has dramatically increased the concentration of information facilities in large cities. Symbolic of this phenomenon has been the truly remarkable surge in land prices in Tokyo. From a long-term standpoint, the issue of promoting the regional development of secondary and tertiary industries must be addressed in earnest.

The fourth problem is the relatively

low level of basic research in Japan. Most expenditure on research and development is targeted on commercial production; basic research accounts for only 13.6% of total R&D spending. In view of the recent build-up of advanced technologies, I believe Japan must throw more weight behind basic research.

The fifth problem is socioeconomic: the large gap between Japan's vigorous economic activity and the living environment of its people. Although at current yen exchange rates Japan's per capita GNP exceeds that of the United States, this is meaningless for the average Japanese. Long working hours, the poor state of housing, extremely high land prices in major urban areas and expensive agricultural produce illustrate this point. As long as these phenomena exist, I believe a review of the causes inherent in the system is essential.

Structural adjustment and the role of MITI policies

In light of the three major changes reshaping Japan's industry and society, how should we resolve the various structural imbalances with which we are confronted? In order to foster development toward the 21st century, we should seek a solution through a plus-sum game. Other ingredients are to be found in respect for free trade and market mechanisms, in the pursuit of creative growth through technological innovation, in concerted

international action on economic issues and government policy and in contributing to the advancement of the international community.

Respecting the market mechanism and strengthening the free trade system

The Ministry of International Trade and Industry (MITI)'s 1987 basic guideline for trade and industrial policy addresses many of these questions. Respect for market forces is fundamental to industrial policy. And this of course presupposes that the exchange rate fairly reflects economic fundamentals. For this to happen, it is essential that the management of exchange rate policies and demand management policies be based on concerted international action. High expectations are held for the cooperative measures, supervision by the Group of Seven among them, agreed to at the 1986 Tokyo summit.

The recent appreciation of the yen is already bringing about marked changes in the economy. As a result of the yen's gains since the fall of 1985, the physical volume of Japan's exports has fallen below year-earlier levels, while the physical volume of imports, and particularly manufactured goods, has increased rapidly.

To derive maximum benefit from market mechanisms and to sustain efficient economic management, it is of the utmost importance that protectionism be thwarted and the free trade system preserved. The recent agreement on an opening declaration for the New Round at the latest GATT ministerial conference was an epoch-making achievement. It is important to take appropriate follow-up measures.

Transformation to an internationally harmonious industrial structure

1) Fostering international specialization

One effective way to correct external imbalances is to promote the international division of labor. For this, it is indispensable that Japan expand imports of manufactured goods and international capital flows.

During the next fiscal year a range of measures will be taken to expand imports. To encourage imports of manufactures, we at MITI will be sponsoring import bazaars and other promotion projects, expanding low-interest-rate financing for imports of manufactured goods and establishing an insurance scheme covering import-related business shutdowns. A variety of steps will also be taken to promote direct overseas investment. They include expansion of overseas investment credits and an overseas investment insurance scheme.

At the same time, moves to establish the Japan-EC Industrial Cooperation Center will be accelerated to foster industrial cooperation with the European Community. This center will provide Japanese language tuition and training in Japanese production and quality control techniques and Japanese-style management.

Steps will also be taken to aid industrialization in developing countries, and particularly in the nations of Asia. These will be embodied in the Project for Comprehensive Cooperation and Asian Industrialization, which will cover financial cooperation, training in industrial technologies and assistance in marketing.

2) Promoting the conversion of business activities

Structural change may increase social cost—for example, by creating unemployment—or heighten political pressures in favor of protectionism. That being the case, together with structural measures aimed at expanding domestic demand and developing new fields of business, there will also have to be supplementary measures to smooth the process of business switchovers.

MITI will promote projects for smooth structural adjustment, including internal shifts to new, growth-oriented fields, ex-

pansion of investment in new lines of business to absorb surplus labor and establishment of new industries in regions particularly hard hit by unemployment.

Smaller companies have greater difficulty tackling structural adjustment. A comprehensive set of measures is being implemented to facilitate their reorientation to new business activities, including technological guidance, personnel training and expanded and improved availability of financing. In addition, improved measures are essential to assist those regions most affected by structural adjustments, the promotion of new businesses in those areas being only one example. These measures are not designed to preserve the status quo of small- and medium-sized companies, but to assist the correction of external imbalances.

3) Measures for expanding domestic demand

A precondition for smooth structural switchovers is an expanded domestic market. The domestic economy has been characterized by a marked deflationary tendency since the summer of 1986.

In order to overcome the deflation brought on by the strong yen and to correct the country's external imbalance, it is essential that we expand domestic demand and aim for relatively high growth.

The government is now implementing a number of measures to this end, including expanded public works spending, stepped-up housing construction, promotion of private investment in plant and equipment in projects affecting the national economy, the passing on to consumers of windfall foreign exchange profits arising from the strong yen and flexible management of monetary policies.

There are several key points to expanding domestic demand.

First is the problem of building housing and improving urban areas. Only 2.4% of Japan's total surface area is devoted to housing, while conversely, 34% of land in urban areas is used for agriculture. These figures indicate that there is great potential for increasing the supply of land for housing. If regulations governing construction were relaxed and tax reductions and other incentives improved, demand for housing and other buildings would expand significantly. This would also bring to the surface still-latent demand for the equipment and consumer durables these activities require. We are now devoting considerable attention to technological development aimed at providing functional and efficient new types of multiple dwellings. We are also fostering lines of business that can direct the construction and improvement of comfortable office environments.

Second come measures to build infrastructure for a new mode of industrial society. The infrastructure to which MITI is devoting its attention includes facilities for joint research, the training of technologists and the collation and dissemination of technological information. We are also looking at facilities for international trade fairs and conferences, and community facilities incorporating new communications media.

We are also harnessing the vigor of the private sector in these undertakings. In May 1986 we promulgated the Private Participation Promotional Law to promote private-sector participation in such projects. We are now seeking to extend the scope of these measures to include the establishment of a "World Business Zone," replete with facilities for international business interchange and facilities for leisure activities.

The third set of measures is those designed to foster Japan's regional economies. MITI's policy stance is directed at eliminating the trend toward centralization and relocating facilities related to people's daily lives to outlying regions, taking into account changes in industrial structure, technological innovation and



Housing construction and urban redevelopment are spearheading expansion of domestic demand.



Aerial view of Tsukuba Science City: Technological innovation is one vital factor in the restructuring of Japanese industry and society.

the growing weight of information in people's lives.

Fourth, we must stimulate consumer demand. For this, it will be essential to improve housing and the living environment and shorten working hours. The increasingly diverse needs of today's consumers are likely to spur the rise of new service industries under the combined impact of internationalization, information-related advances and technological innovation. The development of these new businesses will help expand the frontiers of industry and expedite the shift to a domestic demand-oriented industrial structure. To this end, MITI is pushing forward with a comprehensive set of measures, including financial and credit schemes, provision of information and human resources training.

Expanding the frontiers of industry through technological development

Research and development in all aspects of technology are clearly expanding the frontiers of industry. It is contributing both to the creative development of the world economy and to the maintenance of Japan's economic and social vitality. It is even helping compensate for the decline in employment opportunities caused by the growing international division of labor.

MITI attaches great importance to developing research in basic technologies and will give priority to basic research in areas such as the develop-

ment of elements with new functions, fifth-generation computers and new materials such as fine ceramics. We also will support technological development in biotechnology.

MITI is giving high priority to furthering international joint research and international exchange in research. As one part of this effort, we have been calling for global participation in a large-scale international joint research program. The Human Frontier Science Program, as this massive and ambitious program is called, involves basic research directed at elucidating the outstanding functions of living organisms—metabolism, mobility and thought—and applying them to industrial technology. MITI officials responsible for the global promotion of the program have toured Europe and America, where they report it has aroused considerable interest. The concept has been highly praised by technologists and research experts, including Nobel Prize winners.

Conclusion: the significance of policy coordination

In conclusion, we cannot overemphasize the importance of coordinated international policy measures. Exchange rates today display a nervous oversensitivity to the utterances of influential figures. To stabilize exchange rates, countries must

always keep one jump ahead of speculators. The exchange rate of the dollar against the yen and Deutschmark has fallen, but if every year the size of the U.S. budget deficit continues to exceed forecasts, and U.S. investment continues to outpace savings, then it will be no easy task to find a solution to that country's external imbalance. At the same time, if a powerful country unilaterally makes abrupt changes in its policies, it must inevitably cause disorder in the world economy. Herein lies the significance of international policy coordination: It can help ensure that every country's role is in harmony with that of other nations.

Another point worth stressing in the context of policy harmonization is that, in addition to exchange rate and macroeconomic policy, we cannot overlook problems in industrial structure. Industrial structure is shaped not only by market forces but also by such factors as the level of technology, the quality of the labor force and the capabilities of management. If the European Community is to reduce its structural unemployment, it must encourage investment to foster dynamic development, and be willing to create an appropriate investment climate. If the United States is to bring back home the productive capacity that has fled abroad, it is essential that it prepare appropriate tax and other investment conditions.

To foster the dynamic growth of today's industrial society we must combine Adam Smith's "invisible hand" of market forces with the "visible hand" of policy foresight, sharp analysis and reasonable thinking. From this standpoint, MITI is preparing to establish during the next fiscal year the Research Institute of International Trade and Industrial Policy, an organization that will conduct theoretical research into industrial and macroeconomic policies from an international perspective. We also plan to hold international symposia to bring together researchers and policymakers, and to make further progress in international joint policy research projects.

We must not forget one vital fact. To ensure the creative development of global society toward the 21st century, it is essential that we work together to formulate schemes for wide-ranging international policy coordination. ●

This is a summary of a recent lecture by Shinji Fukukawa to foreign diplomats, businesspeople and journalists, outlining the future direction of Japan's economy and industry as it approaches the 21st century.