Chapter I

The Economy, Industries, and Corporations

1 The Japanese Economy: Current Situation and Outlook for the Future

Japan's Phenomenal Postwar Economic Recovery

Though the Japanese economy had been virtually destroyed by the end of World War II, the government made institutional forms and implemented far-sighted policies, achieving a recovery that is remarkable by any standard. During the period of high economic growth (1955 to the early 1970s), the economy expanded at an average rate of 10% per year.

Since the 1970s, the world economy has been shaken by profound changes in the international monetary system and by two oil crises. However, the Japanese government has managed to maintain Japan's relatively strong performance by adopting effective macroeconomic policies. Labor and management have made contributions also, by agreeing to set wages voluntarily. The industrial structure has been transformed through technological innovation, and Japan has succeeded in staving off inflation and keeping the unemployment rate under 2%.

Astoundingly Low Growth Rate

In the early 1980s, economic theories stressing the importance of the market mechanism gained support in Japan, as in other industrialized nations. Informed by these theories, the Japanese government implemented administrative and fiscal reforms, and privatized some state-run corporations. During this period, trade imbalances among the advanced nations worsened, leading to the Plaza Accord of 1985, which was signed amid growing demands for Japan to open its markets. With the substantial currency adjustments that ensued, the yen rose sharply against the U.S. dollar, resulting in a recession. Japanese companies, manufacturers in particular, sought to remedy this by moving their operations offshore.

The Japanese government attempted to promote domestic economic growth by lowering interest rates to stimulate demand. Its macroeconomic policies were influenced by negotiations with the United States, at which the removal of structural barriers to imports and the reduction of Japan's huge trade surplus were discussed. Unfortunately, this resulted in excess liquidity, which induced speculation in land and securities. The prices of land, securities, and other assets soared to abnormal levels, thereby creating the "bubble economy" of the early 1990s. When the bubble burst, the economy entered into crisis and was saddled with an enormous volume of bad debts. Japan has since struggled to dispose of these bad debts and to counter what the OECD (Organisation for Economic Cooperation and Development) has described as "astonishingly and exceptionally low economic growth."

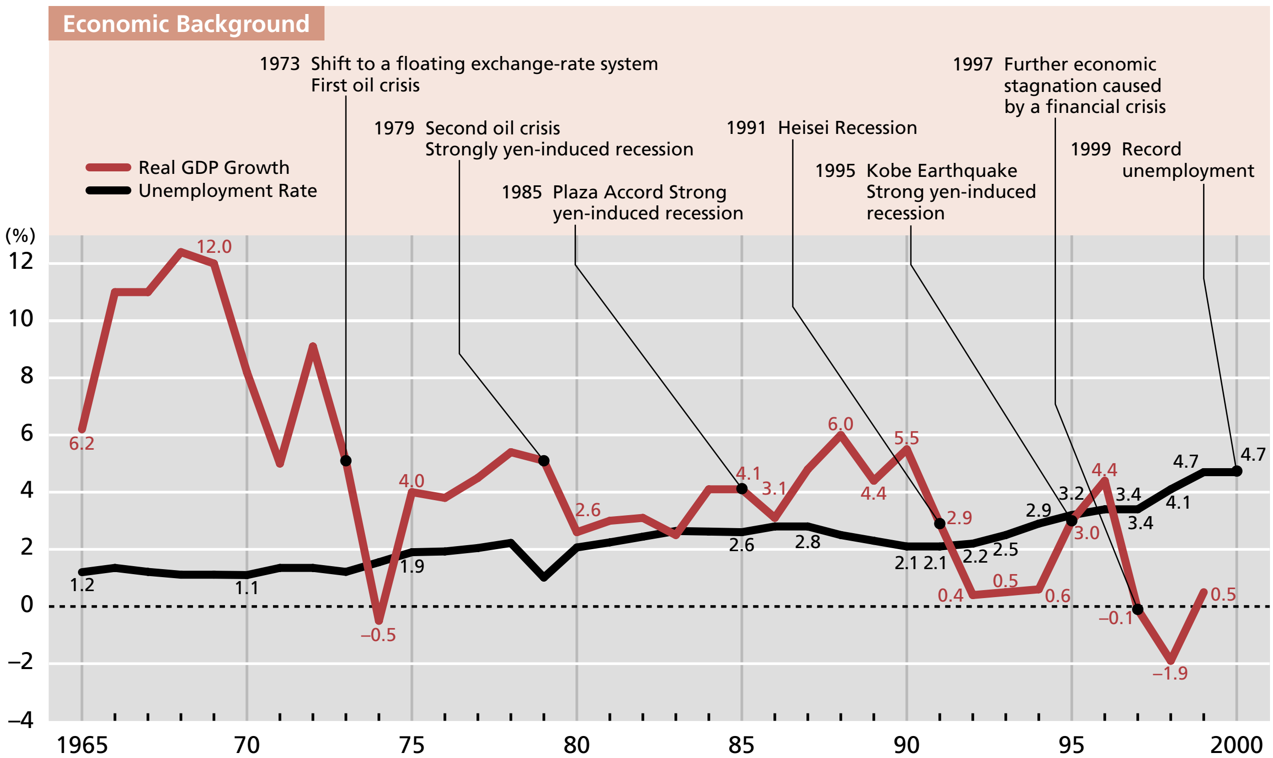
I-4 describe Japan's real GDP (gross domestic product), labor force, and real wage levels, compared with those of other advanced nations. Japan's real GDP grew at a robust and consistent rate for many years until 1992, when growth began to decline, while the labor force expanded at a relatively stable rate of 1% per year. Japan has succeeded in distributing the fruits of its high economic growth period equally, increasing both wages and the size of the workforce.

Movements Toward Self-sustained Economic Recovery

Since 1997, the Japanese economy has experienced, among other things, a rise in the rate of consumption tax aimed at fiscal reconstruction, reduced public demand, an Asian currency crisis, and the insolvency of major financial institutions, which contributed to an acute downward economic spiral from the end of 1997. In response, the Japanese Government has attempted to shift from "administrative policies aimed at financial protection" to one of introducing market principles into financial administration. It has also supplemented public works projects by emergency economic measures and taken measures to expand demand through steps toward permanent tax reductions. The effect of such policies brought a halt to the bottoming out of the Japanese economy in spring 1999, and since the later half of 1999 the recovery of the Asian economy has also been partly responsible for the subsequent succession of moderate improvements.

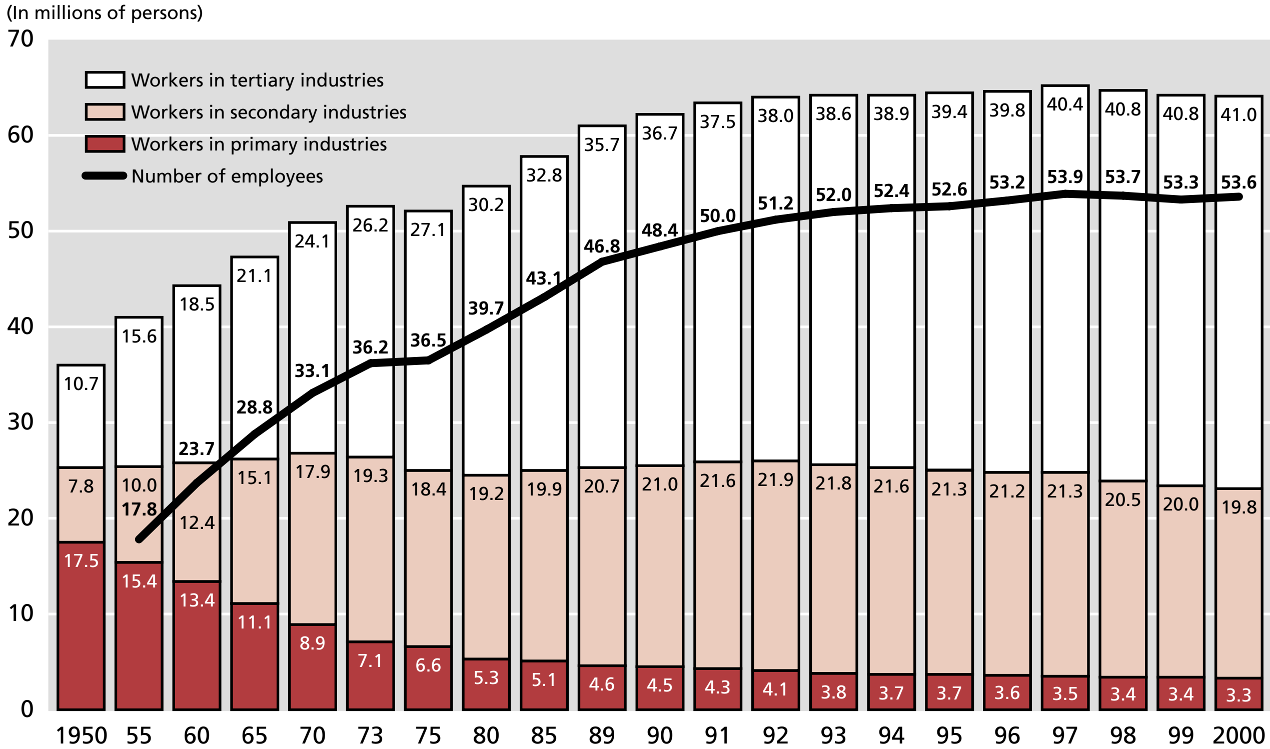
However, despite evidence of movements from inventory adjustments to increased production to increased corporate profit in the process of economic recovery, subsequent movements toward "increased consumption from increased income" are unclear. Although the fall in income is leveling out, there is no apparent trend toward an increase in consumption, and as such, Japan is still not on a full-fledged path to recovery despite the presence of "movements aimed at a self-sustained recovery."

I-1 Real GDP Growth and the Unemployment Rate



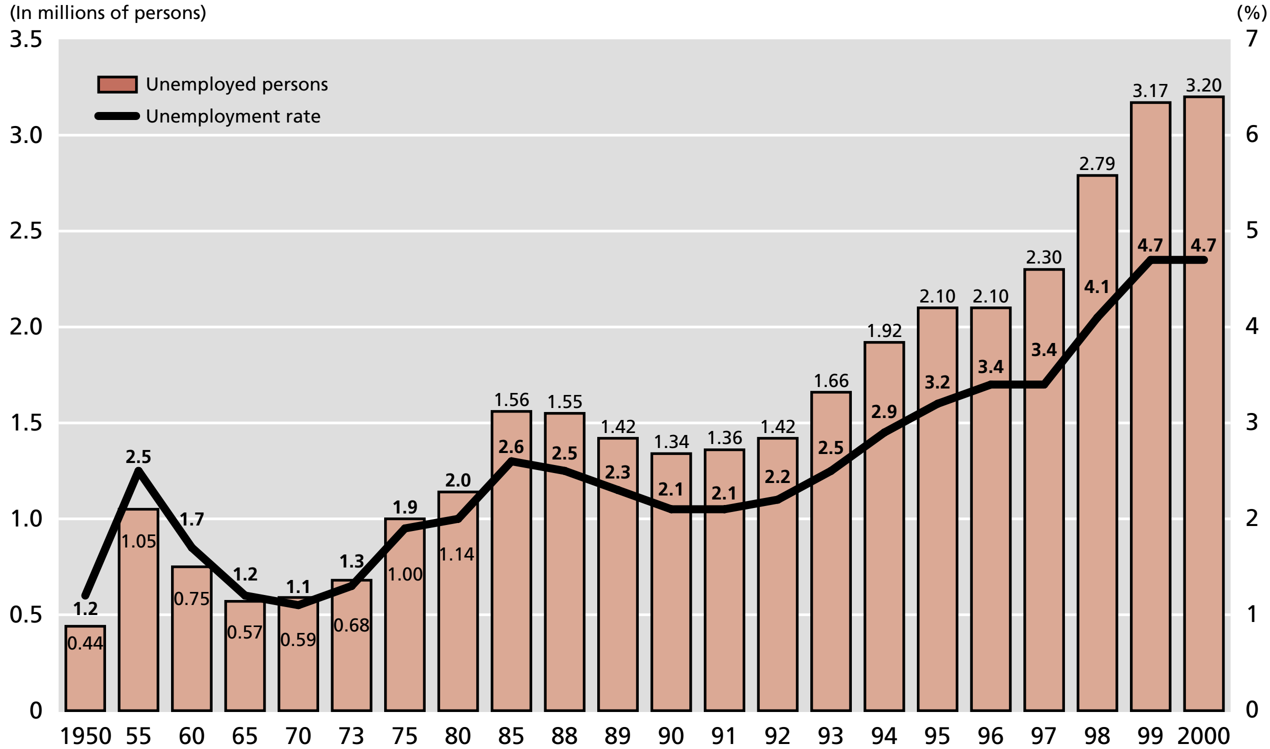
Sources: *National Accounts*, Economic Planning Agency; *Labor Force Survey*, Statistics Bureau, Management Coordination Agency, 1999

I-2 Labor Force Statistics



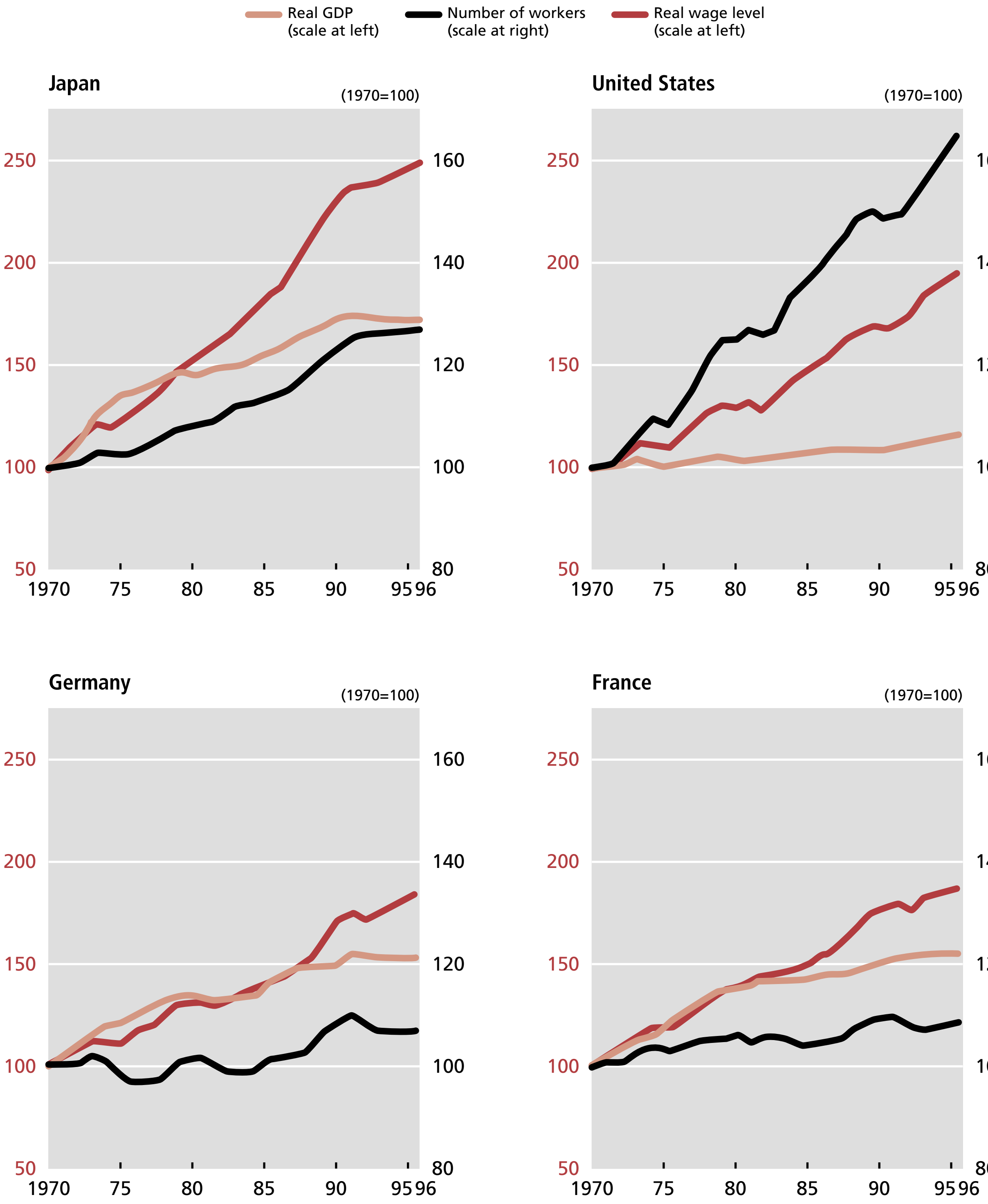
Source: *Labor Force Survey*, Statistics Bureau, Management Coordination Agency

I-3 The Unemployed and the Unemployment Rate



Source: *Labor Force Survey*, Statistics Bureau, Management and Coordination Agency

I-4 Changes in Real GDP, Number of Workers, and Real Wage Rates in the Advanced Nations



Sources: *Labor Force Statistics*,1998; *National Accounts*, OECD, 1998
Note: In the graphs above, real wage level was calculated by subtracting a private consumption expenditure deflator from income per employee.

2 Japanese Management Systems

Japanese Management Systems

Japanese corporate management systems differ from those used in the United States. American systems are characterized by the acquisition of and/or merger with other companies, followed by radical labor adjustments. Management systems in Japan, however, are influenced by the ways in which Japanese companies operate. Japanese companies pay relatively small dividends to their shareholders, due mainly to the reciprocal stock ownership system, the result of which is that a considerable portion of the shares issued by Japanese companies does not circulate, but is held by other companies belonging to the same corporate group. Besides preventing takeovers, this practice has stabilized management and contributed to corporate growth through capital gains produced by continuous stock-price appreciation.

Development of Business Groups

High stock prices have in turn enabled Japanese companies to raise funds needed to expand existing businesses and launch new ones, from capital markets, banks, and internal reserves. When Japanese companies branch out into new types of business or industry they tend to do so by establishing affiliates or subsidiaries, and entrusting the new business to them once they are viable. Diversification of this sort can ultimately result in the formation of a corporate group.

Keiretsu

Corporate groups most typically arise in industries that compete in the international arena, e.g., manufacturers of automobiles and electric machinery. They enable manufacturers of finished products, auxiliary equipment, and parts to establish an efficient division of labor. They also facilitate technological innovation and new-product development, since group members share management and technological information. The term used to describe these groups is *keiretsu*.

In-house Development of Human Resources

For human resource development, Japanese companies have traditionally focused on in-house training and education, partly because of the importance placed on expanding existing businesses and establishing new ones within the company or the corporate group. Companies are now upgrading their training and education programs, and familiarizing their employees with new technologies at in-house training centers and in on-the-job training.

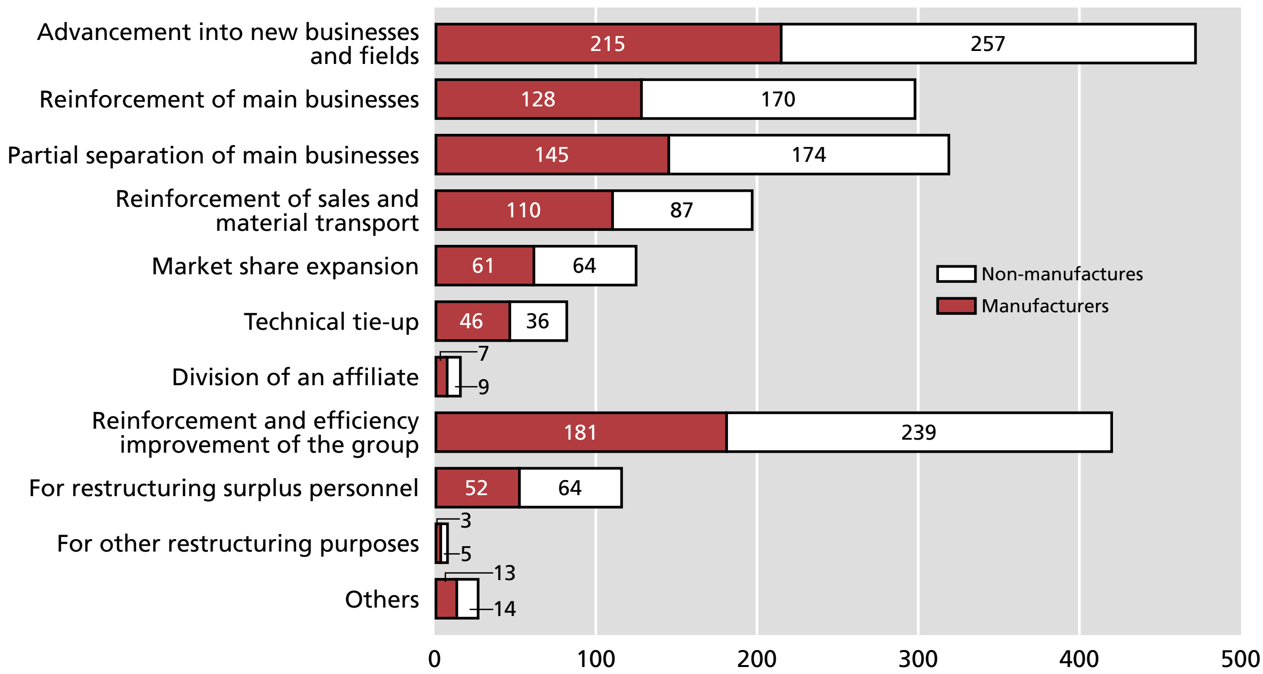
The "Lifetime Employment" Practice

The stability of Japan's long-term employment system (often called "lifetime employment") is owed largely to this emphasis on in-house human-resource development. Companies are extremely reluctant to discharge or lay oft their personnel. They make every effort to retain their employees by transferring them from slow departments to busier ones, or to affiliates, thus keeping cumulative expertise and technologies within the company. The long-term employment system has both contributed to the development of Japanese companies and prevented a rise in unemployment.

Imminent Management System Revisions

As the recession of the 1990s persists and the gap between successful and foundering firms widens, Japanese companies have been forced to address flaws in traditional management practices. They are now beginning to sell off stock shares that are unlikely to pay dividends or rise in price, and to cancel crossholding agreements. There is growing emphasis on mid-career recruitment, particularly of specialized positions, in areas where technological innovation typified by IT is proceeding at a rapid pace, because companies cannot rely on their labor resources for this type of employee. Labor movements are showing signs of increased activity. Faced with criticism from the international community, i.e., that the keiretsu system prevents foreign companies from doing business in Japan, and desirous of lowering costs, Japanese companies have, though slowly, begun to engage in more transactions outside their corporate groups.

I-5 Objectives and Reasons for Establishing an Affiliate within Japan



Source: *Japanese Corporate Groups,* Toyo Keizai Shimposha, 1998

Note: The research was done on the assumption that an affiliate would be established, not depending on, whether total numbers of enterprises in a group would increase or decrease. Valid answers were received from 1,004 enterprises (including 473 manufacturers and 531 non-manufacturers). (multiple responses possible)

I-6 Personnel Adjustment Status by Industry

(July–September 2000; %)

By industry		Total	Construction	Manufacturing	Transportation, telecom-munication	Wholesale, retail	Finance, insurance	Real estate	Services
Total		100	100	100	100	100	100	100	100
Companies implementing personnel adjustments		20	21	25	14	21	13	11	14
Personnel adjustment methods used (multiple responses permitted)	Restrict overcome work	11	9	13	6	11	2	5	8
	Increase number of paid holidays and vacation days	3	3	4	2	3	2	1	3
	Dismiss or refrain from renewing contracts of temporary, seasonal, or part-time workers	1	2	2	0	1	1	1	1
	Suspend of curtail mid-career employment	4	4	6	2	5	2	2	2
	Transfer personnel	7	5	10	4	6	4	2	4
	Transfer personnel temporarily	6	6	10	4	3	7	1	1
	Lay off personnel	1	1	1	1	0	—	—	—
	Recruit volunteers for early-retirement	2	4	2	3	1	2	1	1
None of the above		80	79	75	86	79	87	89	86

Source: *Survey of Labor Economy Trends*, Ministry of Labour

Note: These figures indicate the ratio of companies planning personnel adjustment to all respondents