
**Introduction: Corporate Restructuring and Political Reform in Japan**

Kenji E. Kushida and Kay Shimizu

Japan had a remarkable twentieth century. It entered the period as a rapid industrializer, and over the course of the century, although interrupted by wartime devastation, its economy grew to become second only to the United States. Yet, during the last decade of the century, Japan faltered – spectacularly. In the 1990s, Japan’s economy grew virtually the least among major advanced industrial nations and observers both inside and outside Japan pointed to an ever-expanding list of structural, political, and economic problems facing the country. Extensive scholarship was devoted to understanding the lack of change in Japan despite (or because of) its lackluster economic performance following the burst of the bubble in 1990.¹

Japan’s first decade of the twenty-first century has been at once disappointing and bewildering, producing wildly contrasting evaluations by observers. The domestic and international press as well as the Japanese public at large have come to call this period the “second lost decade,” characterized by policy paralysis and overall lackluster economic growth. Japanese themselves often reflect on the decades since 1990 with pessimism.

However, to those who study Japan more closely, the same decades reveal nothing short of a broad transformation in many of the core tenets of Japan’s postwar political economy.

In the *economy*, the financial system which was once dominated by main-bank centered financing increasingly came to accommodate a capital market-based system. Employers came to depend much more heavily on non-regular workers, overwriting the once predominant image of life-time employment for all. Foreign multinational corporations made significant inroads into

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traditionally closed sectors such as banking and insurance. Corporate governance practices changed with the adoption of holding companies and international accounting standards. Regulatory changes in a wide range of sectors reshaped industry dynamics, including retail, finance, pharmaceuticals, telecommunications, and distribution.\(^2\) Large firms increasingly became more selective and specialized in their product and service offerings, with a new focus on profitability and return-on-investment.\(^3\) And new firms such as Softbank, Rakuten, and Uniqlo grew into major global corporations, reshaping their respective industries to become symbols of a “New Japan,” characterized by visionary and daring entrepreneurs, disruptive market strategies, a global outlook, and a new dynamism.

Politically, major changes were under way. In 1993, the LDP lost power for the first time since 1955, but quickly regained power less than a year later by entering into a series of coalition governments. An electoral rule shift restructured the logic of electoral competition, and a wave of scholarship was devoted to understanding the broad effects of this institutional change.\(^4\) A decade later in 2005, the LDP won a landslide victory thanks to a mold-breaking Prime Minister, Koizumi Junichiro. He was not a product of standard LDP factional politics, and he captured widespread popular support by promising to destroy the “old LDP” by reforming it—thereby saving the very party he promised to destroy. But the LDP’s revival was short lived as Koizumi’s successors succumbed to intra-party jostling and backtracked on many of the Koizumi-era reforms. In 2009, Japan experienced its first direct electoral change in power in the post-war period, with the Democratic Party of Japan (DPJ) ousting the LDP.\(^5\)


In the relationship between politicians and bureaucrats in policymaking, new regulations and practices reduced bureaucratic discretion. Elite ministries, rocked by scandals through the 1990s, were reorganized at the end of the millennium, notably with the powerful Ministry of Finance (MOF) broken apart. The political leadership increasingly asserted greater authority over bureaucrats with a strengthened Cabinet Office and more political appointments to top ministry positions.

The role of informal coordination between politicians, bureaucrats, and economic actors – the so-called “iron triangle” – also weakened, driven by regulatory changes and normative shifts following the bursting of the bubble in 1990. In a variety of domestic-oriented sectors, new business strategies swept away traditional business models that emphasized relations with the government. In finance, for example, a regulatory overhaul led to new competitive dynamics, rendering “MOF handlers (MOF-tan),” employees devoted to cultivating relations with MOF officials, obsolete.

While Japan’s political economy has transformed decisively and irreversibly, it has also exhibited a remarkable amount of structural resilience. In the economy, few major firms went bankrupt, or sold themselves off. Longstanding inter-firm relationships such as main banks and keiretsu corporate groups did not disappear; instead, they bifurcated, with main banks strengthening control over weaker firms and keiretsu groups diverging in their function. Long term employment in large firms have not disappeared either; they merely shrank in numbers as firms increased reliance on temporary workers to cut costs.

At a more basic level, Japan’s national debt, though climbing to over 200% of GDP by 2010, was almost entirely bought by domestic entities and kept within Japan. With Japanese banks, insurers, public pension funds, and households accounting for about 80% of Japan Government Bond (JGB) purchases, a sudden run on Japanese national debt remains hard to conceive—particularly when the banks were aided by government-orchestrated mergers, and regional banks are required to buy low risk assets. This underlying fiscal and financial stability is

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7 Amyx, Japan's financial crisis: institutional rigidity and reluctant change.
in contrast to the sovereign debt in crisis-stricken European countries such as Greece and Spain, which are largely held by foreign entities.\(^8\)

Politically, even the charismatic Koizumi failed to usher in an entirely new era of reform and policy-oriented politics. His successors reverted to traditional LDP-style, non-populist politics by readmitting the LDP members Koizumi had expelled, and even promulgated platforms of “undoing the damage caused by the Koizumi reforms,” which, as we will see later, did not track reality and was ultimately rejected by voters. Neither did the DPJ’s historical win usher in decisively new politics, as they too appealed to rural voters through direct financial assistance, and became embroiled in intra-party infighting that hindered policymaking. Moreover, the DPJ’s policies in many areas did not depart as far from those of the LDP as initially promised.\(^9\)

The Puzzle: Restructuring and Reform in Japan

The core questions we seek to answer surround issues of change and continuity: What drove the changes and shaped their trajectories? What has been the pattern of change? Why do we see dramatic transformations side by side with deep-seated continuities and resistance to change?

This volume originates from a conference held in 2006 at Stanford University. In hindsight, it was a propitious time to begin an analysis of how Japan was transforming. It was the tail end of major economic and political reforms, but it was followed by a period of significant reversals of fortune for the economy, for reform, and for the LDP. As the contributors revised, updated, and added new chapters, it became manifestly clear that many of the forces driving the Japanese political economy beyond 2010 cannot be understood without a clear picture of the late 1990s and early to mid-2000s. We firmly believe that any analysis of how the country will

\(^8\) For details on the technical difficulties of selling off truly large quantities of JGBs and Japan experiencing capital flight, see Masahiro Yamaguchi, *Naze Nihonkeizai wa Sekai Saikyo to iwareru no ka [Why the Japanese Economy is Considered the World' Strongest]* (Toho Shuppan, 2012).

change moving forward must be rooted in an understanding of the transformation that has already occurred since the 1990s.

**Japan’s Syncretic Model of Change**

We contend that the transformation of Japan’s political economy since the early 1990s is best characterized as *syncretism*—new ideas, organizations, and practices that combine *and* coexist with previous ideas, organizations, and practices.¹⁰ We observe elements of *traditional* and *new* characteristics of the Japanese “model” that coexist with one another, such as long-term employment and increasing reliance on a whole new market of temporary workers. We also observe *hybrid* forms of organization and strategies, such as multiple employment systems within single firms—a track with higher upfront pay and lower job security, and another track with seniority wages and higher job security. This combination of *new, old, and hybrid* best captures both the dramatic transformations and long established characteristics.

In politics as well, new aspects such as the increased role of the media and broad public appeal, coexist with traditional forms of local electoral campaigning focused on providing support to rural and agricultural areas. Politicians with new strategies such as Koizumi were succeeded by traditional LDP interest group leaders such as Aso Taro. Even the new party in power, the DPJ, quickly adopted many of the LDP’s traditional tactics of appealing to the countryside. Yet, the new focus on media and popular appeal did not disappear, as Osaka Mayor Hashimoto Toru (as of this writing) rides a wave of populism and attempts to gather enough political force and allies to become a major player in national politics.

**Contributions to the Volume**

The chapters in this volume provide important pieces in answering the questions of continuity and change in Japan since the early 1990s. Kushida and Shimizu examine Japan’s financial system—both the conventional financial sectors such as banking, securities, and

¹⁰ Syncretism, a word often used in the context of cultural or religious combinations, refers to the process of melding multiple different forms of beliefs or practices. Kushida applied it to the context of Japan’s transforming political economy. Kenji E. Kushida, "Inside the Castle Gates: How Foreign Firms Navigate Japan's Policymaking Processes" (Doctoral Dissertation, University of California Berkeley, 2010).
insurance, as well as the massive postal savings system. They argue that Japan’s pattern of change is one of syncretism in which new ideas and practices are coexisting with pre-existing organizations and norms. Regulatory reforms allowed new entry, possibilities for reorganization, and strategies. Yet, while some financial institutions aggressively pursued new opportunities, others retained traditional organizations and strategies, and some hybridized—thus resulting in syncretism.

Furthermore, the authors go beyond the characterization of the transformation as syncretism to contend that a specific set of political dynamics shaped Japan’s process of change, which they call *syncretization*. This distinctive pattern of regulatory reform entailed strong political leadership pushing through reforms against the traditionally powerful interest groups who were most affected by these reforms. This pattern of reform enabled long powerful interest groups to slow or even reverse reforms when political leadership for reform waned.

Gregory Noble’s chapter analyzes Koizumi’s reform coalition, how it operated, and the constraints it faced. He argues that Koizumi’s reform coalition consisted of three complementary elements: political leadership by Koizumi himself, support from big business, and academic analysis by economists who provided the intellectual foundation for Koizumi’s neo-liberal reforms. Koizumi held together this coalition with pragmatism and persistence, despite broad opposition from a variety of forces, some within the LDP itself. Koizumi’s reforms were, however, also constrained by the main constituents that supported him, namely big business and the middle class who were not fully dedicated to neo-liberal competition and preferred social and government absorption of some risk. His chapter sheds light on how Japan underwent bold reforms in certain areas in the early to mid-2000s, and how the opposition to those reforms later led to a retrenchment once the strong leadership for reforms eroded.

Ulrike Schaede stresses the extent to which core tenets of the Japanese economy transformed. She argues that Japan underwent a strategic inflection point between 1998-2006, in which a reconstitution of the legal setting for business irreversibly transformed industry dynamics and corporate strategies. She contends that in the new competitive environment, the traditional roles of main banks, *keiretsu* business groups, and cross-shareholding are all but obsolete. Their continued existence is therefore the result of inertia, and since they are a drag on corporate strategies needed to compete, they actually drive change by pushing firms decisively away from those arrangements by providing counterexamples. Her chapter reveals some of the
dynamics of syncretism, as some firms move towards new strategies and organizations and others—though outcompeted—still do not disappear overnight, resulting in multiple coexisting norms and practices, as well as hybrid forms.

Kay Shimizu examines small and medium enterprises (SMEs) which have received little attention in the political economy literature to date, but deserve a much closer look, especially in Japan where they employ nearly 70% of the labor force. Shimizu finds that SMEs have been bifurcating along two dimensions: by firm performance and by employment structure. In terms of firm performance, on the one hand, zombie firms continue to be propped up by numerous government policies that align the interests of lending banks, local politicians and bureaucrats, and the SME borrowers. Such protective policies have also allowed numerous regional banks themselves to remain above water by extending a helping hand to many of their weaker SME customers. On the other hand, Japan is also home to a vibrant group of SMEs who are competitive in the global marketplace and have become providers of niche products and parts for a wide range of businesses and their global supply chains. For both types of firms to remain financially viable in a place like Japan, however, employers must rely more heavily on non-regular workers, creating a clear divide in earning power between regular and non-regular workers. Thus firm survival and low unemployment has come at a cost to Japan’s non-regular workers, many of whom are young and but remain underemployed.

Harald Conrad examines compensation system reforms in Japan since the 1990s. He finds that while performance factors are gaining in importance, seniority-based wages continue to play an important role for blue collar workers and white collar employees up to a certain managerial level. Wage systems and occupation pension systems remain highly complex, with a growing diversity of wage and benefit systems. While overall employee coverage of retirement benefits has declined, the mix has changed significantly since reforms in 2001-2002, with defined contribution plans increasingly replaced by defined benefit pension plans. He contends that while certain aspects of human resource practices are increasingly market-based, they are hardly converging to an Anglo-American model. He finds syncretism, with the same companies that introduce new performance factors to their wage systems often continuing to use a wide range of traditional welfare benefits, while others create hybrid systems that combine existing and traditional systems.
Kenji Kushida analyzes the foreign multinational corporations in Japan, particularly in the financial sectors, automobiles, pharmaceuticals, and telecommunications, which experienced massive foreign direct investment inflows after the mid-1990s. He finds that regulatory shifts, driven by political logic, reshaped the competitive environment facing foreign firms. Not only were formal and informal entry barriers removed, but the rules governing industry dynamics shifted to advantage the business models of foreign firms over existing domestic incumbents. The distinctive characteristics of Japan’s political economy such as main banks, long-term labor, and keiretsu corporate groups, which had hitherto made it difficult for foreign firms to compete in Japan, actually transformed in function to aid foreign firms in making inroads into Japanese markets. Foreign firms often exploited gaps in what the new regulatory structures allowed and the slow adjustment by incumbent Japanese firms, took advantage of being able to offer alternative employment structures, and even found large customer bases in traditional keiretsu group companies struggling to adjust. They did not replace major Japanese firms, but introduced new norms and practices that coexisted and melded with older, preexisting norms practices – what we call syncretism.

To provide a broader context for the reforms discussed in this volume, the remainder of this chapter provides an overview of Japan’s political economy during the two decades after the economic bubble burst in 1990.

**Japan Transforming Since the 1990s: An Overview of the Politics and Economy**

This section provides the backdrop for chapters in this volume by providing additional economic and political context. There are two key contributions: updates on Japan’s politics and economy that go beyond the chapters, and charts that provide an overview with a breadth that more focused books and journal articles seldom include. In particular, the horizontal time axis that plots each Prime Minister’s time in office provides a useful visual timeline for mapping the political dynamics on to economic factors over time. We begin by examining the political shifts over the last two decades, and then turn to the major corresponding economic indicators.

**Prime Minister Approval Ratings**

The bursts of reform in Japan during the 1990s and 2000s, particularly under Prime Ministers Hashimoto and Koizumi, are noted in the chapters by Kushida and Shimizu, Schaede, and Noble. Their reforms occurred in the context of high approval ratings by the public. Chart 1
shows the approval and disapproval ratings of each Prime Minister’s administration from 1989 onwards.

At the most basic level, we see a pattern of approval ratings for each Prime Minister’s administration falling below disapproval ratings, followed by a new Prime Minister.

Chart 1. Prime Ministers’ Approval Ratings, 1989-2000

Source: TV Asahi

It is worth capturing this volatility in approval ratings with a brief narrative of the broad political developments. After the bubble burst and a series of scandals enveloped the elite bureaucracies and politicians, Prime Minister Miyazawa Kiichi’s approval rating fell to the 10% level while his disapproval ratings shot up to almost 80%. When LDP member Ozawa Ichiro fled the long-ruling LDP and forged a coalition government of former opposition parties, Hosokawa Morihiro became the first prime to lead a non-LDP government since 1955.

In a stark reversal of Prime Minister Miyazawa’s ratings at the time of his departure, almost 80% of the people supported the Hosokawa administration initially, while only 10% disapproved. However, his ratings slid as bold reform was hindered by the wide range of policy positions within the ruling coalition. Allegations of the misuse of funds accelerated the end of
Hosokawa’s time in office, and he was replaced by Hata Tsutomu as Prime Minister, to average approval and disapproval ratings. Then, even before the next election, the ruling coalition split, an event largely blamed on Ozawa driving the LDP’s traditional opposition, the Socialist party to form a coalition with the LDP, thus bringing the latter back into power. The head of the Socialist party, Murayama Tomiichi, became Prime Minister, but his approval ratings fell as he abandoned the key tenets of the Socialist party’s positions to become indistinguishable from the LDP.

In January 1996, LDP leader Hashimoto Ryutaro came in as a reformer and passed numerous major reform bills, many of which served as predecessors to the reforms addressed in this volume, such as the financial “Big Bang”, commercial code revisions, and a reorganization of the government bureaucracies that included splitting apart the powerful Ministry of Finance. His high approval ratings, however, eroded rapidly and his disapproval ratings skyrocketed after he pushed through an ill-timed consumption tax hike, which, combined with the Asian Financial Crisis of 1997, is widely blamed for pushing the economy into recession. The LDP’s poor results in the Upper House elections of 1998 forced Hashimoto to resign, and he was succeeded by Obuchi Keizo.

Obuchi’s ratings took an unusual turn, as he started out being highly unpopular, but improved quite dramatically as his disapproval ratings dropped sharply and his approval ratings rose. His quiet consensus-building style and many of his reforms were appreciated by the public, and the economy began to recover after the Asian Financial Crisis.

Chart 2. Prime Ministers’ Approval Ratings, 2000-2009
Chart 2, which begins in 2000 and ends in 2009 when the LDP lost power, first shows the remarkable political context that gave rise to Prime Minister Koizumi. The Mori Yoshiro administration that followed Obuchi was extreme in its unpopularity, and dramatic reversal from Obuchi. Mori came to power in a most unusual fashion, as Obuchi incurred a stroke in April 2000, slid into a coma, and passed away—but, according to Mori, after telling the latter to take over after him, in a private meeting in the hospital room. The general public was skeptical, and Mori’s Prime Ministership began with a high disapproval rating. As the IT bubble burst, and the GDP and stock market growth that had occurred during Obuchi’s time in office reversed with slow growth and a stock market dive, Mori’s approval rating worsened further. Combined with several verbal gaffes and a general skepticism towards his non-populist, traditional LDP-style backroom deal-making, Mori earned the dubious distinction of setting records for the highest disapproval and lowest, single digit approval ratings.

Koizumi Junichiro’s popularity upon his ascent to the Prime Minister-ship was unprecedented and unparalleled. The public thoroughly approved Koizumi’s promise to reform the old-style political of the LDP, his maverick reputation, his hard-line stance on anti-reformists, and unprecedented media savvy that took advantage of his good looks. Although his approval rating slid through his tenure, it still remained around 50% for most of his time in office and disapproval ratingss never reached 50%.
Koizumi’s successors, however, were a different story. Each started with high approval ratings only to have them drop precipitously as they progressively reverted to traditional LDP political styles of the type that Koizumi had rejected; Abe readmitted LDP members expelled by Koizumi, Fukuda appointed his cabinet according to traditional faction lines, and Aso campaigned to fix the “damage created by Koizumi reforms,” for example. After the global financial crisis in 2008, leading to a precipitous drop in exports and sharp recession for Japan, Aso’s popularity dropped severely, though not quite to Mori’s levels. It was at this time that the LDP was voted out of power and became the opposition for the first time since 1955.

Chart 3. Prime Ministers’ Approval Ratings, 2009-mid 2012

![Chart 3](image-url)

Source: TV Asahi

Chart 3 shows the approval and disapproval ratings of the DPJ governments after they came to power in 2009. The first DPJ Prime Minister, Hatoyama Yukio, came to power with high approval ratings, sharply reversing the numbers at the end of the Aso administration. Peoples’ hopes were high as they voted the LDP completely out of office for the first time since 1955. However, the approval ratings quickly slid, as the DPJ seemed to have difficulty implementing policy, and with the increasing prominence of Ozawa’s campaign financing scandals. Ozawa had headed the DPJ until financial scandals led to his stepping down. When Hatoyama, close to Ozawa, came to power, it became clear that Ozawa, who had long called for a strengthened Cabinet leadership, was actually holding much of the power despite not being in
the Cabinet himself. The Hatoyama administration therefore had an odd power structure, where one the one hand, it claimed to take power from bureaucrats to the Cabinet political leadership, while on the other hand, Ozawa, who had a party position but was not in the government, had much of the authority. A financial contribution scandal to Hatoyama himself contributed to his plummeting approval ratings, and he was replaced by Kan Naoto.

Kan enjoyed an increase in approval ratings as the economy recovered, but after peaking in September 2010, his popularity began to slide. After the March 11, 2011 disaster, when information was confused and his role in the nuclear disaster was played up in the media as damaging, his disapproval ratings soared. After he resigned and was replaced by Noda, the Prime Minister’s approval ratings again began high and began to slide, as Noda staked his political capital on an unpopular increase of the consumption tax, and he pushed through with restarting nuclear power plants to meeting summer peak demand, despite lingering questions about the safety and regulatory structure over Japan’s nuclear power. Weekly peaceful demonstrations in front of the Prime Minister’s Office against restarting nuclear power plants, which began in early 2012, grew to an estimated 10,000 or 20,000 participants by the end of June.

**National Diet Seats: The Transition from the LDP to DPJ**

The power transition from the LDP to the DPJ reinvigorates the puzzle of why the LDP was able to stay in power for so long, while adding the question of why the DPJ rose quickly to become an electoral force to be reckoned with. The chapters by Kushida and Shimizu, and Noble shed light on this question. The approval ratings in the previous section suggest a correlation between periods of reform under Hashimoto and Koizumi, though causation can run both ways; their popularity was buoyed by promises of reform, which then gave them leeway to undertake reform. Kushida and Shimizu’s analysis point to the interest group dynamics of political leadership oriented towards reform trumping entrenched interests, along with the subsequent backtracking—that contributed to the LDP’s eventual ousting from power. Noble’s analysis reveals the political support coalitions underpinning the Koizumi reforms.

Charts 4 and 5, which show the percentage of seats held by each party (parties or coalitions controlling the house are bracketed) provide context by clearly showing the
remarkable boost the LDP received under Koizumi for the 2005 lower house election, the rapid rise of the DPJ, and dramatic fall of the LDP.\textsuperscript{11}

**Chart 4. Party Strength in Japan’s House of Representatives (Lower House), 1986-2009**

![Chart](image)

Source: National Diet

\textsuperscript{11} For details on Japan’s electoral politics up to the time of Koizumi, see, among others, the introductory chapter to Krauss and Pekkanen, *The rise and fall of Japan’s LDP: political party organizations as historical institutions*; Steven R. Reed, Kenneth Mori McElwain, and Kay Shimizu, eds., *Political change in Japan: electoral behavior, party realignment, and the Koizumi reforms* (Stanford, CA; Baltimore, MD: Walter H. Shorenstein Asia-Pacific Research Center; Brookings Institution, 2009).
Economy Growth Patterns: Not Simply “Two Lost Decades”

Schaede’s chapter points to deep, irreversible changes to Japan’s economic structures during the 1990s and 2000s. This section provides broader context for these changes by mapping economic indicators onto an axis showing each Prime Minister’s administration.

Chart 6 shows the need for a corrective against the persisting image, particularly in the popular press, of Japan’s “lost decades” of the 1990s and 2000s. Compared to the 1980s, growth rates in the 1990s and 2000s were far lower. Yet, it was certainly not “two decades of recession” or “stagnation,” since there were actually only two pronounced recessions of more limited duration. These recessions coincided with or immediately followed broader international crises: the 1997-1998 Asian Financial Crisis unfolded and the global financial crisis of 2007-2008.

Source: National Diet
Chart 6. Japan’s GDP Growth, Prime Ministers, and Prime Minister Approval Ratings (1980-2012)

What we actually see is a pattern of recovery punctuated by abrupt drops into brief recessions. Note the first recovery was after the low point in 1993 which ended in 1997, and the second from around 2002 until 2007. The listing of prime ministers along the horizontal axis provides context to Prime Minister Mori Yoshiro’s extremely low public support, Koizumi’s high support, and Aso Taro’s support dropping to the point that the LDP lost control of the government in a landslide election.

A look at the Nikkei stock index across time provides further context. Chart 7 shows the magnitude of the bubble, as the Nikkei peaked acutely around 40,000 yen, dropped precipitously, then hovered between 15,000 and 20,000 yen for much of the 1990s. The chart also shows the continued decline during the Mori administration as the index value dropped almost in half by
the first years of the Koizumi administration. Then, during the Koizumi administration, it almost doubled, from just less than 8,000 yen to around 17,000 yen. This partly explains the optimistic mood that took hold during the Koizumi administration among investors of all sorts. Enthusiasts included many households that had been burned by the bubble bursting, regaining confidence and re-entering stock markets, with some making substantial gains. Conceptions of the “second lost decade” too often overlook the details of this period—the stock market did double during that period, after all, and it was only the global financial crisis that sent it plunging again.

Chart 7. Japan’s Nikkei Index Share Price and Prime Ministers (1980-2012, yen)

![Chart 7](chart7.png)

Source: Thomson-Reuters

Employment: The Rise of Non-Regular Employees

Conrad’s chapter examines Japan’s changing compensation system reforms. The backdrop to that chapter is Japan’s changing composition of employment, to which this section provides context.

Chart 8 reveals that the number of employed people in Japan through the 1990s and 2000s was greater than in the 1980s, although the growth rate was slow.\(^{12}\) We see that although the number of “regular” employees dropped, the rise of non-regular employees, which include

\(^{12}\) It should be noted that self-employed are not included in this data.
temporary and part time employment, rose. The Koizumi years were notable for the modest levels of employment growth and falling unemployment.

Chart 8 also shows a fallacy behind the political campaigns waged by Koizumi’s successors. Aso Taro, in particular, tended to blame rising income inequality to Japan on the Koizumi reforms. However, the growth of non-regular employment began well before Koizumi came to power, and unemployment actually dropped during his tenure.

Finally, we see the sharp recession that hit Japan in 2008 leading to an upsurge of unemployment.


The shifting composition of the labor market is also illustrated by the rapid growth of a new industry that barely existed under the post-war Japanese model: temporary labor, or “dispatch workers” agencies. Dispatch worker agencies serve the needs of large companies who desire short term employees, both white collar and blue collar, who can be deployed flexibly. This industry doubled in size roughly between 1992 and 2000, but then grew exponentially 2004,
when labor law and the Worker Dispatching Law revisions took effect, enabling a more flexible deployment of temporary workers.\(^\text{13}\) (See Chart 9)

Chart 9. Sales Growth in Dispatch Workers Industry, 1992-2010 (100 millions yen)

Source: MHLW

**Expenditures, Savings, and Deflation: Buying More, Getting More, and Saving Less**

The cognitive dissonance that struck most who visited Japan during the “lost decades” was that, particularly in urban areas, Japan seemed to get wealthier. Despite media articles portraying Japan as facing “anemic” growth or a “moribund” economy, it did not feel like a prolonged recession on the surface, and particularly in urban areas. Household expenditures were higher through the 1990s and 2000s than they were in 1990—people were buying more (See Chart 10). And since there was no inflation, with a bout of deflation between 1998 and 2002, as seen in Chart 11, people’s buying power was increasing.

Chart 10. Japan’s Household Expenditures (billions of USD), 1990-2010

Source: World Bank Development Indicators

The other side of rising consumption, however, was a marked decrease in household savings rates; people were consuming more, but saving less. Chart 11 shows the drop in household savings as a percentage of household income.

**Chart 12. Japan’s Household Savings Rates, 1990-2012 (percentage of household income)**

Source: OECD Economic Outlook, based on MOF data

**Non-Performing Loans: A Crisis Diffused**

In Chapter 3, Gregory Noble notes that arguably the most notable achievement of the Koizumi administration was to overcome Japan’s deflationary spiral and decrease the burden of non-performing loan held by banks. As additional context, Chart 12 shows how NPL levels at the city banks decreased rapidly during the Koizumi administration.
Chart 13. Non-Performing Loans in Japan’s Banking Sector (trillions yen), Ratio of NPLs in Total Loan Portfolios (%), 2000-2010

Public Works Spending:
Public works spending, a staple of the clientelistic politics characterizing the LDP’s traditional exchange of local votes for infrastructure projects, declined over time. Chart 14 shows the amount of public works spending in the government annual budget. Note that the sharpest decrease came under the first Koizumi budget, and the trend was followed by his successors until Aso. Aso increased the public works spending as part of a stimulus package after the global financial crisis. Also note that the lowest expenditures are under the DPJ governments – although the latest budget is likely to reflect spending to rebuild the areas devastated by the earthquake and tsunami in the Tohoku region.

Source: MOF

Japan’s Continuing Internationalization: Investment Flows

Since the early 1990s, Japan’s economy became far more enmeshed with the global economy. Figure X in Schaede’s chapter shows how the foreign ownership percentage of Japan’s Tokyo Stock Exchange grew from around 4% in 1990 to just over 25% in 2010. Foreign direct investment flows are shown in Chart 15 below. The chart shows how inward foreign direct investment rose in the late 1990s before dipping once in the mid-2000s, before rising again around 2008 before dipping again. Outward flows rose rapidly, spiking just before the global financial crisis hit Japan’s economy in 2008.
Sources of Stability: Japan’s Export Dependence, Foreign Assets, and

The previous sections provided a brief overview of several major substantial changes in Japan’s political economy since the 1980s. Yet, as we point out through our framing of syncretism, many aspects of Japan’s political economy remained surprisingly stable. This section reveals a few sources of that stability through economic indicators that we believe have not received enough attention.

First, the image that Japan’s economy is still heavily dependent on exports is misleading. In fact, as a percentage of GDP, Japan’s export dependence was only 15% in 2010, compared to over 50% for Korea and 27% for China.
The effects of a stronger yen, which hit its first peak in 1996 and approached similar levels in 2012, is not necessarily disadvantageous to the economy to the degree that many (relatively uninformed) observers suggest.

Second, Japan’s manufacturing portion of the economy consists of only 19.4% of its economy in 2010, decreasing from 27% in 1980, 26% in 1990, and 21% in 2000. See Chart 17 for a comparison among G-20 countries. With few natural resources and shrinking agriculture, the majority of Japan’s economy consists of services. This trend has increased as manufacturing operations are increasingly undertaken abroad, through the pressure and opportunity created by a strong yen (see Chart 18).
Chart 17. Manufacturing as a Percentage of GDP, G-8 Countries and China, South Korea, 2010


Chart 18. Yen-Dollar Exchange Rate and Overseas Manufacturing Production (1990-2012)

Source: METI, Survey of Overseas Business Activities
Combined with the low export dependence noted above, this suggests that Japan’s economy is strongly supported by internal demand.

Third, it should be pointed out that Japan is the world’s largest creditor nation. Chart 19 shows the net international investment positions of G8 countries, along with China, Taiwan, and Switzerland.

**Chart 19. Net International Investment Positions, G8+ Countries, 2011**

Source: MOF Net International Investment Positions 2012

Finally, as mentioned briefly in the beginning, Japan’s record-high national debt is unlikely to create an immediate crisis. Japan Government Bonds (JGBs) are held overwhelmingly by domestic entities, as seen in Chart 20. Moreover, most of the domestic JGB holders are highly unlikely to suddenly jettison their JGB holdings, since banks were essentially rescued by government-orchestrated mergers, insurers and pension funds are mandated to hold a significant proportion of safe assets, which include JGBs. (See Chart 21) In any case, there are doubts whether the market could sustain the liquidity for a sudden sale-off of truly massive quantities of JGBs, and the consequent rising interest rates are likely to create vast new demand
for JGB holdings. Thus, the Japanese national debt situation is surprisingly stable for at least the short-medium term.


![Bar chart showing the percentage of Japanese government debt held domestically and overseas from 1993 to 2010.](chart)

Source: Adapted from MOF, Japanese Public Finance Fact Sheet 2011, and MOF, Debt Management Report 2011

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14 For an extended version of this argument, see Yamaguchi, *Naze Nihonkeizai wa Sekai Saikyo to iwareru no ka [Why the Japanese Economy is Considered the World' Strongest]*.
Having provided the broad political and economic context for the chapters in this volume, focusing on change and continuity, let us now turn to the chapters themselves.

**References**


