

Competing in a Borderless Economy

Interview with Mitsubishi Corp. Chairman Minoru Makihara



Mitsubishi Corp. Chairman and KKC Vice Chairman Minoru Makihara believes that, given the increasing movement of

goods, services, capital and people across national borders, it is only natural for Japan to bring business management practices in line with global norms. Moreover, short-term economic victories will not endure without full compliance with international rules, Mr. Makihara tells Masami Tashiro, Director of the KKC's international affairs department. Furthermore, the Mitsubishi chairman believes that the U.S.-Japan relationship can be lifted to a much higher level through a free-trade agreement that would encompass a broad spectrum of economic activity.

How to Approach the Global Era

KKC: As you know, the Japanese business community is divided on whether or not to adjust management practices in response to developments in the international marketplace. Some say that we should bring management practices in line with so-called global standards. Others argue that there are no such standards, just competition. What do you think?

Mr. Makihara: The trend definitely is toward a globalized economy. In other words, national boundaries are being dismantled, allowing for a freer flow of goods, capital and, in the future, people. This trend naturally will further increase global competition.

An important goal for any business is to be competitive. At the same time, in a globalized economy, a player must observe certain internationally recognized rules, such as those pertaining to transparency, accounting rules, environmental protection, and so forth, in order to win. Failure to observe such rules means that while a company may score short-term victories, it will not win over the long run.

With the advance of information and communications technology, the world is increasingly becoming a single market. To succeed in this environment, companies must take full advantage of the Internet. Also important, executives must be able to communicate in English, which has become the de facto language of business. This is not because so many people speak the language or that the Anglo-Saxon

world now dominates the international economy. Rather, English is well-suited for business communication and transactions.

KKC: Whatever mode of management a company chooses, a key to its success or failure will be speed. Would you agree that a managerial approach that lacks decision-making speed will place the company at a competitive disadvantage?

Mr. Makihara: Yes, particularly in the U.S. market. The American economy is changing so quickly, particularly in the information technology sector, that in order for Japanese businesses to keep up with it, they will have to move very rapidly, make quick and bold decisions and break out of existing molds.

KKC: What are your views on Japanese management practices—that is to say, lifetime employment, seniority-based wages and internal corporate labor unions? Will these practices act as a competitive drag? Are companies already beginning to phase them out?

Mr. Makihara: I think some of these management practices will remain, but most of them will have to change. One must remember that the so-called lifetime employment system and the seniority-based system were introduced in the postwar period when the Japanese economy was still labor-intensive and companies needed to secure a large pool of employees.

Job security remains important, however, because it is not as easy to change jobs in Japan as it is in the United States.

InSide No. 1 October 2000

The Myth of a Rigid Economy Threatens to Diminish Long-Term Prospects 4

Japan Business Dialogue 6

Competing in a Borderless Economy

Interview with Chairman Minoru Makihara Continued

At the same time, though, we must develop policies that encourage people to seek new employment, particularly if they are not satisfied with their current assignments.

KKC: Especially younger employees?

Mr. Makihara: Yes, but also middle-aged workers. But this will require the development of a better social safety net. By that I mean that there should be a more generous approach to unemployment insurance and improved retraining programs.

KKC: Recently, (management guru) Peter Drucker has been urging corporate Japan not to be so hasty in abandoning traditional management practices. The focus on shareholder interests will only last about a decade, Mr. Drucker maintains, after which time the interests of stakeholders again will enjoy the upper hand. Do you agree with his assessment?

Mr. Makihara: No, not completely, because heretofore, Japanese shareholders have played an extremely passive role. This is unfortunate. I think more active participation by shareholders naturally improves corporate performance.

The stakeholders whom Mr. Drucker refers to always have enjoyed a prominent place in Japan; businesses typically rank the interests of employees over those of shareholders. In the United States, in contrast, employee interests come in second to those of shareholders.

The Need for a Smaller Government

KKC: Some American analysts and policymakers maintain that competition policy in Japan is weak. What do you think?

Mr. Makihara: There is a lot of confusion surrounding this issue. Many people recognize that a more competitive Japanese market not only is necessary, but also is desirable. But there seems to be no common understanding of whether more rules or fewer rules would increase competition.

“... Japanese businesses ... will have to move very rapidly, make quick and bold decisions, and break out of existing molds.”

In general, though, the government is too large. Even without a formal competition policy, the central government bureaucracies should be far less involved in all aspects of business.

KKC: Related to competition policy, some American analysts are critical of the less-than-liberal attitudes in Japan toward foreign direct investment. However, corporate Japan generally has welcomed mergers and acquisitions by foreign companies. Moreover, foreign investors can

“Foreign direct investment... has been important in promoting a more rational allocation of human and productive resources.”

operate pretty much as they would in the U.S. or European markets. Do you think these developments are indicative of greater acceptance by the Japanese people of foreign direct investment?

Mr. Makihara: Corporate Japan has no choice in view of the fact that these foreign investors generally have contributed to the restructuring of the Japanese economy and increased competitiveness. Foreign direct investment also has been important in promoting a more rational allocation of human and productive resources.

You must bear in mind, however, that there are certain minimum standards that must be observed when doing business in

Japan. These would include an emphasis on human relations and the inability to move employees around easily. It is imperative that foreign investors take these factors into account when considering whether to move into the Japanese market.

KKC: The revival plan of Carlos Ghosn, chief executive officer of Nissan Motor Company, was rather bold.

Mr. Makihara: Yes, but it is important to bear in mind that the substantial work-

force reductions stipulated in Mr. Ghosn's plan will be implemented over several years. That is a relatively long period of

time. Moreover, he is not just laying off workers. Mr. Ghosn understands the general framework of the Japanese economy and what Nissan must do to survive. He knows that he must restructure the company, but he also rec-

ognizes that he must observe certain Japanese business rules.

KKC: Is it fair to say that Mr. Ghosn is trying to observe Japanese customs and traditions?

Mr. Makihara: Yes, to a certain extent. In the past, Nissan would have tried to continue doing business with all of its longtime suppliers. Mr. Ghosn has severed some of these ties, which probably will make some workers redundant.

But in terms of sound management, it is rational to concentrate resources, avoid unnecessary waste and do whatever else is required to boost the company's competitiveness.

U.S.-Japan Free-Trade Agreement

Mr. Makihara: I would like to add that at Keidanren (Japan Federation of Economic Organizations), we are beginning to explore the possibility of a free-trade agreement with the United States. This is not a new idea. Mike Mansfield, the former U.S. ambassador to Japan, floated this proposal several years ago. But I believe the time has come for us to give it some serious thought.

Mr. Mansfield was probably thinking primarily in terms of the flow of goods, but now the interest, especially in the United States, is in the movement of services, investments, technology, etc. Discussion of a possible FTA, I believe, is now a very timely topic.

KKC: About the only issue that a FTA would settle, is tariffs, right? One could

argue, then, that a FTA would not be appropriate between two economies where large flows of capital and technologies are concerned.

Makihara: I disagree. Free-trade agreements, as they are now being developed, focus more on facilitating the movement of capital and people. They also address the

in Washington in October 2001. By doing so, we hope to be able to help governments in both Tokyo and Washington take a renewed look at the bilateral relationship, with the idea of raising it to a broader and more forward-looking level.

...we are beginning to explore the possibility of a free-trade agreement with the United States.

needs of e-commerce. FTAs are not just about quotas and tariffs.

KKC: At what sorts of venues would it be appropriate to study a FTA proposal? Do you think such forums should include only governmental officials? How about private sector input?

Mr. Makihara: A private-sector group, such as the U.S.-Japan Business Council, would be an appropriate vehicle to begin exploring a U.S.-Japan free-trade agreement.

KKC: Will you propose launching FTA-related discussions to the new administration, be it one led by Texas Gov. George W. Bush, or one led by Vice President Al Gore?

Mr. Makihara: First, I would like to see the (U.S.-Japan) Business Council tackle the FTA issue. And the Council will have a prime opportunity to do this at its Joint Executive Committee meeting in New York in April 2001. If the discussion at the JEC meeting proves feasible, it should then be taken up at our Annual Meeting

The Myth of a Rigid Economy Threatens to Diminish Long-Term Prospects

by Arthur Alexander

What are Japan's economic prospects for the next decade or the one after that? The answers start from the reality that Japan is a developed, rich country that possesses the habits, institutions, rules of conduct, and politics of a successful nation. It's an economy that works.

Japan will not collapse like Rwanda or Haiti; rich countries do not do that. It will not expand as it did in the 1960s; rich countries no longer behave that way, either. Instead, long-run real per capita growth will average around 1 percent to 2 percent a year.

The higher number, sustained over decades, would mean a doubling of output per person in each generation. Growth at the lower end of the range could cause troubles—political, if not economic—because paying off economic losers would retard needed reforms. Growth in the one percent range also would cause a gradual slippage in Japan's relative international ranking.

These predictions are based on three empirical observations: the relationship between growth and income levels; the similarity of Japan's institutions to those of the United States and other rich countries; and the relative adaptability of the economy.

The first regularity comes from observations reported in the Penn World Tables, a compilation of national economic accounts for 152 countries over 40 years.

High-speed growth occurs only among less-affluent countries. However, being poor is no guarantee of a strong economic performance. Every collapsing country was also a low-income nation.

Among richer countries, however, growth rates converge. The variance declines as per capita GDP increases. For the 19 economies that had attained a real

Japan is not likely to fall apart—or to grow much above 2 percent a year for extended periods.

per capita output greater than \$10,000 in 1985 dollars (excluding the oil exporting countries), the annual expansion rate over 10-year periods averaged 1.75 percent, with a range between 0.2 percent and 3.7 percent.

Japan generated the high figure the year it entered the big leagues. According to this historical experience, Japan is not likely to fall apart—or to grow much above 2 percent a year for extended periods.

The second set of observations is based on comparisons between Japan and other countries across a wide variety of variables. The revisionist authors who gained prominence in the late 1980s argued that there were significant differences between American and Japanese economic behavior. It does not require much insight, though, to discern that most countries are quite different from each other. The challenge is to understand the

extent to which the Japanese economy differs from other industrial nations.

To assess the differences or similarities between Japan and other countries, the data from 11 separate studies on as many as 150 countries were combined into a unified data base. When measured along 46 different dimensions, the United States is most similar to the United Kingdom,

Canada, Australia and Japan. Several other statistical methods were used to test this approach. They all tell the same story: Japan

falls among the Anglo-American countries.

Significantly, a country's real GDP per capita is highly correlated with its similarity to the United States. Countries are rich because they have adopted institutions that work. Clearly, Japan is not an outlier in this process.

The third type of information deals with adaptability. A common myth about Japan is that its labor force is immobile and its

industry is inert. Structural change in Japan and the United States,

A common myth about Japan is that its labor force is immobile and its industry is inert.

based on GDP originating in 40 comparable industries, reveals that Japan paralleled the American experience. From 1980 to present, in fact, the two curves are virtually indistinguishable. Accordingly, the two countries' employment data follow a remarkably similar pattern.

Despite Japan's having attained a high level of economic achievement, these gains will not be preserved automatically. There will be constant struggle on both the political and the economic fronts to generate the productivity advances that fuel economic growth.

Deregulation in industries as diverse as finance and air transport is producing markets that are open and competitive. The unfolding of this process has implications for the future.

Take air travel, for instance. Fares and passenger traffic indicate that deregulation has not occurred just on paper—but it has had a distinctive Japanese cast. Ministry of Transport officials placed deregulation on their agenda in 1980. However, given the Japanese penchant for predictability and MOT's desire to give airlines time to adjust to the new regulatory environment, decision-makers planned to phase in the changes over decades. In fact, a combination of technology plus foreign and domestic pressures compressed the timetable to 20 years.

This was deregulation with uniquely Japanese characteristics. These attributes include: manifest fairness, time to adapt, reluctance to engage in confrontation, and difficulty in abandoning employees and others with whom one has longtime relations.

Managing change in such a civilized manner may not always be possible. In the meantime, U.S. carriers have adopted new methods that leave Japanese industry at a competitive disadvantage. In the time that

it takes to open up markets "Japan-style", the world moves on.

Japanese airlines are struggling to lower costs and increase efficiency almost a quarter-century after their American counterparts faced the same challenges. In the meantime, U.S. carriers have adopted new methods that leave Japanese industry at a competitive disadvantage. In the future, it may not be appropriate to deregulate according to a schedule set in Tokyo that fits Japanese sensibilities.

In many different areas, other advanced countries have demonstrated the possibilities for productive change. This experience demonstrates the utter feasibility of accelerated GDP gains in Japan. According to conventional

In the time that it takes to open up markets "Japan-style", the world moves on.

wisdom, change in Japan is both unprecedented and unwelcome. However, employment figures indicate that the job market is not as static as lifetime employment norms suggest. Most of the people who lost their jobs in the 1990s managed to find new ones.

The notion that people do not move from job to job in Japan, that the country's industries and companies are static, and that Japan is different from the Anglo-American economies is belied by the evidence. Such thinking restricts policy choices.

The myth of a rigid economy could, in fact, be the biggest barrier to political efforts to achieve greater competitiveness and higher productivity.

The myth of a rigid economy could, in fact, be the biggest barrier to political efforts to achieve greater competitiveness and higher productivity. Since this belief is so widely held, it may be some time before the reality of Japan's economic adaptability reaches the level of popular acceptance and policymakers, in turn, proceed vigorously toward realizing Japan's true potential.

Arthur J. Alexander is President of the Washington, DC-based Japan Economic Institute.

In each issue, KKC will feature an Op-Ed article.

Japan Business Dialogue

KKC's monthly program featuring Japanese experts on the economy.

"Will the Japanese Economic Recovery Come Soon?"

Yoshio Nakamura, Managing Director, Keidanren

Many economists still are pessimistic about the outlook for the Japanese economy. Not Yoshio Nakamura, managing director of Keidanren (Japan Federation of Economic Organizations). He argued at the KKC's Japan Business Dialogue on July 26 that the economy finally is on a path to recovery. Mr. Nakamura cited increased exports and greater investment in plants and equipment as evidence of an upward trend.

The chief executive officers of Keidanren member companies agreed. According to a June 2000 survey of these top executives, more than 90 percent said they expected Japan's real gross domestic product to grow by more than 1 percent, which is twice the growth rate of FY 1999.

Mr. Nakamura pointed out, however, that a full economic recovery will be out of reach without a substantial increase in consumer spending. And for this to occur, the Japanese government must dispel for consumers a sense of uncertainty about their economic futures.

Tokyo must tackle such structural problems as the social security system, tax rates and the budget deficit. Mr. Nakamura believes that an increase in the consumption tax to 10 percent from the current 5 percent would provide the revenue needed to address some of these problems. GDP then could to grow by 3 percent. In the absence of these reforms, Japan will have no choice but to accept an economic growth rate of only 1 percent, Mr. Nakamura maintained.

"New Business Investment Opportunities Without Borders in Emerging Markets"

Sumio Takeichi, Director, International Finance Corporation

As the second-largest shareholder in the International Finance Corporation, Japan plays an active role in establishing the IFC's investment priorities, IFC Director Sumio Takeichi told attendees of the KKC's Japan Business Dialogue on August 3. Given the increasingly borderless nature of business, Mr. Takeichi said that, it is important for such advanced industrial countries as Japan and the United States to foster the development of the high technology sector in emerging markets.

Facilitating the development of this fledgling sector will have a leap-frog effect on the economies of developing country, Mr. Takeichi pointed out. This not only would raise the living standards and quality of life in countries with developing economies, but also create more markets for exports and foreign investment from Japan and other advanced industrial nations.

Mr. Takeichi underscored that the development of high technology in emerging markets represents the IFC's "new frontier." In terms of specific technologies and products, the IFC will focus on fostering information technology and the Internet, financial technology and credit assessment, educational technology and distance learning, healthcare and medical technology, distance Medicare and social infrastructure technology and electrical and optical products. Developing country

recipients of technology-related IFC assistance include the African nations of Mozambique, Zambia and Chad as well as Jamaica and the People's Republic of China.

Upcoming Japan Business Dialogues:

How to Cope with Environmental Issues
... a Japanese Company's view.

Toyota Motor North America Inc.,
Vice President, External Affairs,
Shinichi Goto

October 27, 2000

Publisher, Keizai Koho Center

Director, Hideaki Tanaka
kkc1@kkc-usa.org

1900 K Street NW
Suite 1075
Washington D.C. 20006
202 293-8430

www.kkc.or.jp

Keizai Koho Center (KKC) is an independent, non-profit organization designed to promote the understanding of Japan's economy and society at home and abroad. Its financial resources are derived entirely from the private sector.

KKC offers numerous programs designed to create a favorable business environment within Japan and worldwide. Its efforts extend to promoting free and stable trade by eliminating sources of friction in the global economic community.

KKC fosters a deeper understanding of Japan's basic social structure. Furthermore, it conducts public affairs activities to improve the Japanese people's recognition of Japan's global role.

The views expressed in this newsletter are of the contributors and do not necessarily represent those of the Keizai Koho Center.