Interminable Oscillation,or Steady Trend: State and Market

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In their most recent book Franco Mazzei and Vittorio Volpi speak of “una fase cruciale di transizione di un processo pendolare che, in meno di cent'anni, ha visto per ben tre volte capovolto il rapporto tra "mano invisibile" del Mercato e "mano visibile" dello Stato.”

The Mulino journal *Stato e Mercato* is having its 30th anniversary in November. It was born at a time when the world of political science was preoccupied with the notion of “corporatism”/corporativismo, largely because of the increasing resort of governments in the 1970s to incomes policies as a means of controlling inflation without stagnation – the stagflation that was a feature of all western economies in the 1970s. In the Anglo-Saxon economies a clear turn-around occurred in 1979-80, with the election of Margaret Thatcher in the UK and the Volker deflation in the US,followed by the election of Ronald Regan. Not quite so decisively in Europe, however, where in countries like Germany, the idea of the “social partners”—employers asociations, trade unions and government – is still very much alive.

It’s worth thinking a bit more about corporatism. Political scientists lost interest in corporatism in the 1980s without coming to any consensus as to what the word should be made to mean. One definition which was frequently quoted was that of Philip Schmitter written in1974.

> A system of interest representation in which the constituent units are organized into a limited number of singular, compulsory, non-competitive, hierarchically ordered and functionally differentiated categories, recognised or licensed, (if not created) by the state and granted a deliberate representational monopoly within their respective categories in exchange for observing certain controls on their selection of leaders and articulation of demands and support.

In a book summarising research on corporatism in the 1980s, which Colin Crouch and I edited[1], we quote the Schmitter definition, note its vagueness and offer instead a definition not of “corporatism” but of a “corporatist arrangement” – as follows

> . An institutionalized pattern which involves an explicit or implicit bargain (or recurring bargaining) between some organ of government and private interest groups (including those promoting ‘ideal interests’ – ‘causes’), one element in the bargain being that the groups receive certain institutionalized or ad hoc benefits in return for guarantees by the groups’ representatives that their members will behave in certain ways considered to be in the public interest.

[1] Colin Crouch and Ronald Dore, eds. *Corporatism and Accountability*, Oxford, OUP, 1990

Clearly, leaving aside whether one could call 1970s and 1980s Japan a corporatist society, it was a society riddled with corporatist arrangements in the form of delegation of governance powers to industry associations. Examples are the way the car industry was left to work out each firm's export quotas, when the government had set the overall quota for exports to America and Europe as a means of solving trade friction. Or the way in which the textile industry was allowed to set production quotas for individual firms in recession cartels. Or the way in which the five firms in the beer industry were allowed to deny entry to contesting newcomers.

The other characteristics of the Japanese economy which differentiated it from most other, and certainly from the Anglo-Saxon economies, were

1. Long-term relational obligated trading patterns, in which the parties ignored cyclical fluctuations in markets at the expense of short-term profit-maximization, particularly between large assembler firms and their small and medium suppliers, and between a corporation and its "main bank"
2. The way in which, although the Commercial Code made corporations the property of shareholders, in much the same way as in the Anglo-Saxon economies, in practice shareholders were treated as debt-holders, paid with a standard percentage of the face value of their shares and denied any control over managers.
3. And the reinforcement of this emasculation of shareholders by the fact that all major companies had a large part of their shares in the hands of their banks or trading partners, an arrangement which was often reciprocal and controlled by the equity=debt consensus.

Thus it was until the bursting of the bubble, wrecked the confidence in the system which had hitherto sustained it. And thus it was until all of the characteristics listed above were subject to intense American criticism in the Structural Impediments talks of 1989-90 which were the result of American frustration at the fact that Japan's trade surplus continued to grow in spite of a 50% revaluation of the yen in 1985 and all the concessions Japan had made in the industry-specific trade friction talks.

The new trend , accelerated particularly by the Hashimoto and Koizumi governments was towards the erosion of all those features listed above -- shareholder sovereignty rather than managerial sovereignty, the dissolution of cross-shareholdings, the end of "administrative guidance", market-rationality trading rather than relational trading, the end of life support for near-bankrupt firms etc -- all those features now derided as "crony capitalism"?

Is that trend, as Mazzei and Volpe suggest, likely to continue unabated until the Japanese economy is a simulacrum of the American? Is this the "End of history" for state/market oscillation? Let me first quote at some length an assessment I made in 2009[2]

Beginning of quotation

A 2009 assessment

Such is the world's preoccupation with "national competitiveness" and with growth rates as a measure thereof that the overwhelmingly dominant interpretation of contemporary Japan is "the miracle turned sour" or alternatively "the miracle that never was". How we were taken in, says the American triumphalist literature[3]. Who can now read with a straight face all that stuff that was written a decade ago about Japanese vitality and American stagnation, about the superiority of Japanese management, the dedication to the long term, cooperative industrial relations, quality circles, relational contracting, mutually protective share cross-holdings, and all the other ways in which the Japanese were supposed to be prospering by defying the logic of the market? The last decade has proved that, after all, it is market competition, not patterns of mutual support, that make for vitality and competitiveness. It is economic rationality in the pursuit of self-interest that pays off, not hugger-mugger regulation by a nanny-state with a blind eye for cartels.

The book which ten years ago started the "types of capitalism" debate – Michel Albert's *Capitalism vs. Capitalism* – did indeed suggest that Rhenish capitalism – the category in which he put Japan along with Germany, Holland, etc. – had long-term efficiency advantages over the alternative, Anglo-Saxon variety. But he was also concerned to point out that it had moral advantages – a concern for "solidarity and social justice", "prudence, patience and compassion", in contrast with Anglo-Saxon

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[2] "Japanese management goes hesitantly American" paper for some forgotten symposium.

[3] e.g., Richard Katz, *Japan: The system that soured: The rise and fall of the Japanese miracle*, London and Armonk, M.E.Sharpe, 1999

capitalism which was bidding fair to make "the industrial nations…jungles of dog-eat-dog competition and naked greed"[4]. He could only lament that it was Europe which seemed hell-bent on importing Anglo-Saxon values and institutions, not the other way round.

The virtues of Rhenish systems which he extolled, were both "good society" virtues and efficiency virtues. Instead of efficient markets, relying on the invisible hand to guide the purest individual self-seeking to the greater good, what the Japanese had was the self-restraint to enter into long-term commitments which could override short-term opportunities to maximize profit. Lifetime employment, long-term and not purely contractual business relations between manufacturers and their suppliers and customers, a sense of the enterprise as a focus of community sentiment, were the chief "cultural" ingredients. And the chief outcomes, which proponents said gave Japanese firms an edge over their American counterparts, were: collegiate management, relationship banking rather than market finance, cooperative industrial relations, willing shop-floor engagement in productivity improvement efforts, a collective pride in quality, and a willingness to sacrifice short-term profit for long-term investment, research and development.

Business magazines in the 1980s frequently published the results of surveys comparing what Japanese and American managers claimed to be their objectives. American managers gave pride of place to returns on equity, maintaining their share price. For Japanese managers those came well down the list, after market share in product markets, raising employee wages, maintaining the firm's reputation.

The secret: shareholders hardly counted

How could they be thus indifferent to shareholder pressure for profits, given that company law gave shareholder rights the same priority as in the Anglo-Saxon countries – unlike Germany where the parallel rights of employees were enshrined in co-determination laws? The answer was: not in the way that American managers were generally shielded from investor pressure in the 1960s, because of the wide dispersion of shareholdings which Berle and Means recorded, and writers like Galbraith celebrated. Rather, it was because of ownership concentration, but concentration in friendly hands.

[4] M. Albert, *Capitalisme contre capitalisme*, Paris, Seuil, 1991, *Capitalism against capitalism*, London, Whurr, 1993. the quotations are from the British edition, p.256

Most of the big firms had a large share of their equity held on a long-term basis by “stable shareholders”. Some were (mutual) insurance companies with which they had on-going business relations which were much more important for those partners than the profits from their shareholdings. Others were reciprocal cross-shareholdings with their banks and with friendly suppliers and customers, especially those from the same enterprise group to which they were bound by historical ties.(Hostile takeovers were practically unthinkable and even mergers took place only with difficulty; merging communities and seniority promotion systems always gave trouble.)

[Equity was treated as debt] Managers sought profits of course, but more as free cash for investment than as a means of keeping shareholders happy. How far they would allow increases in pay to eat into potential profits was primarily a ‘jam today or jam tomorrow’ question. And the jam in question was the managers’ own jam as well as that of their subordinates. The enterprise was a quasi-community; the top managers were its elders, so that when the annual bargaining round with the company union had settled a percentage increase, that was roughly the percentage by which managers upped their own salaries. Thus, their pay increases kept pace with those of people on the shop floor. A Ministry of Finance statistical series for the 2000 largest firms gives detailed figures for the pay, bonuses and non-statutory welfare payments of directors and ordinary employees separately. From 1975 to 1999 that ratio hardly varied from 2.5 to 1.

That same statistical series puts numbers to the shareholder-as-mere-creditor feature. In the recession that followed the Plaza Agreement in 1985, dividends fell the next year by less than 0.1 percent. In the four boom years leading up to the massive asset bubble that followed they increased by only 2%. And this was at a time when wages and directors’ emoluments went up by 19% and 22% respectively.

The new normality

The picture today is very different. Forget, for the moment the wild swings of the past year, from the growing panic after the Lehmann shock and the wholesale canceling of export orders, to the near despair of the spring 2009 panic when average large-corporation profit margins (operating profit on sales) plunged to a disastrous minus 0.3%, to the tentative sighs of relief as the second quarter figures uncertainly suggest that the worst has passed. Through all these ups and downs, the institutions, instinctive behaviors and mind-sets of managers are rather different from those of their predecessors twenty years earlier.

They have been ‘Anglo-Saxonised’. It is not market share, but the price of their shares in the stock market that has become their central measure of how well they are doing. The former executive of a large Japanese steel firm remarked: “Of course the share price is important; you let it go down and you are the target for a raider; you get it up and you can get equity finance. When I took over the chief financial job, (in 1993) I was concerned about our share price, but nobody else on the board seemed to be, I was the one then who took care of investor relations. Not nowadays. Now it’s the job of the president. He is the one to go off to Wall Street and the City. He’s always having to prepare for meetings with the analysts.” And there are a lot of the latter about in Tokyo. The Security Analysts Association of Japan, had a mere 1,000 members when it first instituted its professional examination in 1981. As of mid-August 2009, it boasts 22,577 members all, except 80 survivors of those pre-qualification days, possessors of a full diploma.

Structural reform through legislation is one reason for the change, beginning in 1993 with the simplification and cheapening of shareholder representative suits. (under strong official American pressure in the Structural Impediments talks of 1989-90, but from then on the indigenous reform movement needed little outside prompting.) It proceeded to the legalization of many hitherto forbidden practices, always with the US as a model – creation of holding companies, remuneration through stock options, buy-backs of one’s own shares, and using shares rather than cash to pay for corporate acquisitions. A complete revamping of corporate law in 2002, consolidated these changes and offered the choice of a American-style board structure dominated by external directors. A mark-to-market accounting system was enforced and tax legislation promoted a shift from defined benefit to defined contribution pension systems – both measures intended to help in the accurate valuation of companies for investors and corporate raiders. Labor market legislation vastly extending the scope for temporary work contracts, especially in manufacturing, gave companies the option of reducing their core ‘committed” labor force and cutting labor costs.

The post-bubble stagnation of the 1990s, also prompted change, especially the financial crisis of 1997 coming just at the time that the American economy took off, thus sharpening the contrast between the vigor of American free-market capitalism and the stagnation of Japanese “organized” pseudo-capitalism, and reinforcing the argument that “we must be more like them". The banks had to sell off much of the equity which had made them protective "stable shareholders". Financial difficulties and a change of mood forced the unwinding of many more of the reciprocal cross-holdings.

Nothing, in fact, more clearly symbolizes the shift in the dominant ideology accompanying, and reinforcing, these changes than the media's treatment of cross-holdings. They used to be seen as a means of letting managers get on with the substantive direction of the company, undistracted by bids and counter-bids. The media and the whole of corporate Japan rallied round to defeat an attempted hostile take-over by the American arbitrageur Boone Pickens in 1989. Now, attempts to rebuild cross-holdings are condemned as the actions of lazy, timorous, incompetent managers seeking to escape "the discipline of the market"

It is understandable that shareholders want to exercise discipline in a way that they used never to do. Until 1990 they were reasonably content to be ignored and treated as creditors. It was the seemingly endless capital gains, not dividends that they were after. Now with the stock market still at a quarter of 1990 levels their pressure for high dividends and more share buy-backs has intensified. And shareholders today are increasingly organized, foreign, institutional shareholders. Foreigners held 5% of Japanese shares in 1990, never less than 25% this century. Institutional Shareholders Services, and the Japanese Pension Fund Association vigorously press for higher dividends at shareholder meetings with organized votes against reappointment of directors. Even more crucial in making the share price the centre of managers' attention is the arrival in Japan of a number of private equity funds, ready to pounce on cheap firms with a lot of unrealized assets that they can squeeze with a threatened take-over.

Takeover battles and ideological battles

Nothing, in fact, has done more to bring shareholder sovereignty into focus than the controversies which have arisen over these attempts and the court cases to which they have given rise. They have pitted solid traditional management, usually technically efficient but hoarders of resources against a rainy day to secure the future of their employees, against raiders who promise to realize sleeping assets and give shareholders the benefit of what is, after all, their property. Sympathies are divided. The business magazines, which once filled their pages with articles by ex-Marxist Keynesian economists from the universities, are now dominated by MBA Japanese with English titles like Cheefu

Ekonomisuto at Tokyo-Mitsubishi or Sutoratejisuto (Strategist) at Merrill-Lynch. They are wholly in sympathy with the raiders who are finally teaching managers what maximization and financial efficiency mean. Less articulate, but more deeply felt are the sympathies of those who side with management. They draw on a widely shared "productivist bias", should one call it? The Japanese have a special pair of antonyms, "making things" as opposed to "making money". Belief in the moral superiority of the former goes back to Han dynasty Confucianism when society was first structured as the "four orders" and farmers and artisans were ranked, in nobility and moral worth, above mere merchants.

End of 2009 quotation.

Diminished fervour?

By 2013, however, I have a sense that those with "less articulate but deeply felt" sympathies with traditional managers have grown more articulate and acquired greater influence in the last few years. We will look at the evidence at the end of the paper, but first a few historical thoughts on why one might expect that to happen, given the rush of jingoist? chauvinist? Japanist? sentiment during the Noda and Abe governments, stirred up by the maverick Ishihara and stoked by the ineptness of the foreign policy of Noda and now, digging even deeper holes for themselves as the days go by, of the Abe government.

Nationalism has many mansions

It is a fascinating question because the nationalism comes out in practical politics in all sorts of paradoxical ways.

1. The simple "my country right or wrong" school playground competition view. That boy is /trying to steal my territory/my fish/erecting unfair barriers to the import of my goods/defaming me in the world's multiple media spheres/ treating my co-nationals with disrespect/ trying to gain unfair advantage by undervaluing its currency/propagating hostility to me in countries where I previously had a good reputation, etc.etc. Disputes with other countries are always caused by the other country. Hostility can only be met *kizento* – i.e. with unbendingly severe seriousness – and never mind if, particularly in the case of squabbles over territorial sovereignty, people get killed in the resultant confrontations. This is an attitude adopted and propagated by the Sankei Newpaper and certain Generals of the SDF, and on

Mondays,Thursdays and Saturdays, by the Prime Minister, Mr. Abe.

2. An extension from the private to the public sphere of that famous principle enunciated by the Victorian poet, Henley: “I am captain of my soul, master of my fate.” This is strongest among those who resent Japan’s subordination to the United States manifest in the Security Treaty, the Alliance, and the *de facto* commitment of Japanese diplomacy always to support that of “the Western world”, i.e. The United States. (Or always to consult with it when there seems a particular advantage in deviating from it, as in the case of the recent voting for the admission of the Palestinians to UNGA.) A leading propagator of this anti-American nationalism is the ex-diplomat and ambassador to Iran who sees the whole of post-war history as a battle within the Japanese elite between the “followers of Washington” and the “independents”. He has 57,000 “followers” on Twitter.[5]
3. Both of the above conceptualize “Japan” as an entity in contact/confrontation/cooperation with other national entities in an international world. There is always an “other”. The third type, an attachment, of sentiment or reason, to the nation’s own idiosyncratic traditions, does not require an “other”. You could still enjoy the ritual meditation of the tea ceremony, or admire Hokusai or Sesshu even if the whole world were Japanese. But a comparative element can greatly enhance the attachment. Most people did not have a concept of a distinct *Nihonteki Keiei* -- Japanese style of management -- nor commit themselves to praising or detracting it, until an awareness of how it differed from American style of management became widespread in the 1960s.

So, my question: has the recent rise of nationalism types 1 and 2, reinforcing nationalism type 3, had any effect in halting, or reversing the trend (legislatively reinforced since 1993) to move Japanese corporate government practices towards American models.

Historical Precedents

One can think of historical precedents. The 1887 failure of the negotiations to revise the Unequal Treaties of the 1850s, led to a reversal of the “westernization” consensus which had been justified as a means of proving that Japan was just as “civilized” as Europe and the US. The subsequent rise in nationalism, symbolized in the birth in 1890 of the

[5] Magosaki Ukeru His best seller in Nihon Sengo no Seishi(The true history of Postwar Japan). 2012

magazine, *Nihon oyobi* Nihonjin not only led on to Japan proving its superior degree of "civilization" in war with China, but also reversed the trend towards individualization in property laws and led to the prolonged debate over the restoration of Japanese, particularly family, traditions in the framing of the Civil Code in the first half of the 1890s.

Again in the mid-1920s, universal manhood suffrage (1925), increasingly outspoken liberty of the press and the gay foxtrot-mobo-moga (modern boy/modern girl)urban culture was accelerated while the army's unpopularity over the mess it had made of the Siberian expedition was at its height. As, in the second half of the decade, its adventures in China drew the country into increasingly bellicose positions, and increasingly drummed up jingoistic support, there was a parallel revival of domestic authoritarianism, beginning with the wholesale arrests of communists in 1927, and the crushing of the free-school/adult education movement, with competing state alternatives..

Left and Right

But before accepting these precedents as relevant, one needs to be a bit more explicit about what was being rejected then, and what one might expect to be rejected now. Left and right are fuzzy adjectives to apply to political positions at the best of times, and more so now as electoral politics gravitate to the centre, almost everywhere except the United States and Japan. But clearly one can say that the Kaikokuha, who lost out in 1890, with their espousing of free speech, individual property rights, elected parliaments and the like (not to mention some of their founders' proposals to adopt English as the national language and to start a campaign to marry foreign women) were of a Leftish inclination, and that the Nihon oyobi Nihonjin crowd were Rightist.

And undoubtedly the communists who were cracked down on in 1927, and the mobo and moga who became careful about referring any more to the Emperor as Tenchan, were Leftists. The Tanaka government that endorsed the Kwantung Army's assassination of Chang TsoLin in 1928 was undoubtedly Rightist. . There is no way in which anyone could count that original fervour as Leftist. And that is obviously a big difference between now and 1890 or 1927

The second half of the Noughties

But, leftish or rightist, what is one looking for here? Answer, signs that the "westernizing"fervour which has seized Japan since at least 1993 to change Japanese corporate governance practices to make them more similar to those of the United States, has abated, or perhaps been replaced by a feeling that the fervour went too far, and it is time to backtrack.

One indicator is the number of firms which have chosen under the 2002 law to become American-style “Corporations with Committees” (*Iinkai secchi kaisha)* rather than the more traditional “Corporations with an Audit Committee”(*Kansayakkai secchi kaisha*). In the first year, 2003, it was 44. The number grew to 71 in 2008 but has since declined to 57, of which 15 are the subsidiaries of other Committee firms, which take the Committee form because it enables executives of the mother firm to control the boards of the subsidiaries as “external directors”.[6] (The definition of an external is somebody who has never been an employee of the firm he is directing.)

Secondly, I have no firm data to go on, but I sense a slightly different atmosphere reigning in the offices of the Nikkei Shinbun today as compared with five years ago. (A content analysis of the Nikkei Shinbun in 2007 and over the last 12 months looking for signs of different attitudes towards shareholder/stakeholder conflicts of interest would be a good subject for a PhD thesis.) The popular fence-sitter journalist Ikegami Akira had an extended several-part article[7] addressed to graduates entering the labour market, which acknowledged and illustrated conflicts of interest between shareholders and stakeholders, and warned these graduating youths that they might have to make had choices, but without giving any indication of what choice they should make. The one thing he did seem to approve of, however, was the dissolution of cross share-holdings, the means by which shareholders were kept at bay by managers. It led to managers becoming lazy, he says, developing an, “as long as we are making profits why bother” attitude.

But more convincing evidence of a back-tracking from the Americanising fervour can be found in the following figures.

Two recoveries from recession and one recession compared

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[6] **Japan Association of Corporate Directors,** *委員会設置会社*に関する資料 - 日本取締役協会
www.jacd.jp/news/gov/130801_post-102.html
2013/08/01 - 当協会では 2002 年の設立時より、*委員会設置会社*に関する研究を行ってきました。 昨今のコーポレート・
13/09/17 にこのページにアクセスしました。

[7] “Kaisha wa dare no mono ka” *Ikegami Akira no kyouyou kouza, Nikkei Shinnbun, 3 June 2013*

	Growth% 86-90	Growth% 02-06	Growth % 07-11
Wages, bonuses, benefits per employee	**18.7%**	**--3.1%**	**0%**
Dividends	**1.6%**	**192%**	**--16%**
Directors' Salaries +Bonuses per dir	**22.2%**	**97.3%**	**--0.4%**
Ratio: Dividends / Reserves+ Depreciation	**0.36→0.28**	**0.81→ 1.99**	**1.7 →0.7**
Valueadded per firm	**--1%**	**+11%**	**--4%**
No. of firms in the 1bn capital category	**+41%**	**+0.1%**	**--3%**

Figures derived from the Hojin Tokei for firms with capital exceeding one billion yen. The number of such firms was >2000 in 1986 and >5000 in 2011. See last row for the effect changing composition of the sample my have had on the results.

Most striking is the movement of the employee remuneration/director remuneration differential. The two rose by much the same amount in the run up to the bubble, but in the first half of the 2000s, directors paid themselves 97% more and their employees3% less. During the second half of the decade, though, there is a reversion to parallel movement.

In the early half of the decade, too, dividends going out grew to become greater than the cash flow into the firm from reserved profits and depreciation. In the second half, however, the trend is the other way, though it has not yet got to the pre-bubble ratio when dividends were around a third of the inflow of cash from reserved profits and depreciation.

Inequality and Geopolitics.

The shifts in income distribution illustrated in that table, the *kakusa* which was so much discussed five years ago and still is a favourite theme of critics of the establishment, came at a time when America, the country most tolerant of extreme inequality, was not only an ally but also a model for Japan's "structural reforms", deregulation and shareholder sovereignty in corporate governance. Think the unthinkable. What if Japan had been allied with China against the US, rather than the other way round. China may have gross inequalities, but it has an official ethic of egalitarianism which prompts considerable effort on the part of government to try to correct them. (Including the so-called Chungking model of the now-disgraced Bo.) Would that have made any difference to Japanese attitudes towards deregulation and shareholder value?

Probably. At any rate, speculation about the relationship between the strength of nationalist sentiment and the "our proud and uniquely Japanese traditions" vs. "business school rationality in pursuit of shareholder value", leads naturally to questions about the relation of both variables to geopolitical alignments. The height of the Americanising fervour, mounted with the strength of the US-Japan alliance against China. Okinawa/Futenma didn't do a great deal to weaken that alliance, but the weak and reluctant support for Japan over the Senkaku islands has, especially when it was recently learned that Obama was spending 8 hours with Xi, whereas he had spent only 2 hours with Abe.

If the two would-be hegemons really did get together and establish a Pax Pacifica, Japan would be left out in the cold. That seems pretty unlikely in the long run: the Americans are at the moment calling truce in the US-China cold war because they are preoccupied by the US-Russia cold war, and the hot wars that are intimately intertwined with it in the Middle East. If ever they are settled, the US-China competition is likely to heat up again, with the balance of power, both hard and soft, shifting gradually in China's favour.

But for the moment the Japanese can postpone all the hard choices (*sakiokuri* – sending into the future -- is a favourite Japanese word) and concentrate on immediate questions like who is going to take the blame for raising the sales tax!