

**JAPAN'S ROLE IN
A CHANGING WORLD ECONOMY**

Saburo Okita

Occasional Paper No. 15

**Occasional Paper Series
Center on Japanese Economy and Business
Graduate School of Business
Columbia University
June 1994**

JAPAN'S ROLE IN A CHANGING WORLD ECONOMY

Asian foreign policy, and particularly Japanese foreign policy, is gradually becoming more proactive. There are four main reasons for this. First, the end of the Cold War has forced countries to shift from their traditional security concerns to an emphasis on economic relations and industrial competitiveness. Second, the end of the Cold War bipolarity has led to greater multi-polarity, and this heightened economic interdependence has resulted in more complex inter-linkages of national economic interests. Third, the tremendous economic growth of Asian countries is decreasing the economic frictions with America and Europe. And fourth, the sheer size of the Japanese economy and Japanese assistance programs has forced Japan to become more aware of its role and influence in the world.

Japan has become increasingly more involved in international affairs, particularly in the last few years with the collapse of the Soviet Union. Furthermore, the importance of military strength has decreased, whereas the importance of economic strength has increased in international relationships.

Japan, the United States and Asia

Some have suggested that this new economic situation may force Japan to choose between the United States and Asia. I do not agree. Rather, Japan can and should emphasize multilateralism to close the gap between the United States and Asia. For example, Japan can develop specific policies and make tangible contributions to APEC. Recently Malaysia has proposed an East Asian Economic Group, and there has also been talk about an East Asian economic focus

advocated by Indonesia and other ASEAN countries.

The United States has responded with concern at the possibility that Japan and other Asian countries might form an exclusionary economic block. A couple of years ago, then Secretary of State James Baker said that we should visualize American relations with Asia as a fan: a fan with the United States as its hub and Asian economies as its spokes. Underlying that vision was the basic assumption that Asian economic relations, like Asian security relations, are still primarily bilateral relations centering on the United States. This is the same concept that we heard from Mr. Baker when he spoke in Tokyo a few months ago.

Yet times are changing. Asian economic development has been accompanied by a tremendous surge in intra-regional trade. It is thus essential that America not apply American expectations to these developing countries in a rigidly uniform manner, but expect initiatives by Asian countries themselves. Rather than viewing Asian countries as spokes radiating from the United States, it would be better if the United States viewed its long-term relationship with Asian countries as a relationship of equals.

Paralleling the long history of U.S.-Asian relations is a long-term trend toward increased intra-regional economic relations among Asian countries themselves, particularly in East and Southeast Asia. The relationship between the United States and Europe is completely different from that between the United States and Asia. The United States, for example, does not emphasize bilateral relations with Germany or France; Europe is perceived as a single region. As Asian countries gradually develop closer economic and political relations, the U.S. attitude will also

change. Eventually the United States will not deal with Asia as separate countries, but with Asia as one region. APEC may be one of the most important instruments for developing this type of relationship.

I was involved in establishing the Pacific Economic Cooperation and Coordination (PECC) conference some ten years ago. At that time we noticed that the ASEAN countries were skeptical about Pacific cooperation. Indonesia and other ASEAN countries voiced concerns that we were trying to change ASEAN. They argued that wider Pacific Basin cooperation would reduce the importance of ASEAN, and other major Pacific countries, such as the United States and Japan, would dominate. Therefore, some Southeast Asian countries were reluctant to join PECC. I tried, together with the late Sir John Crawford of Australia and others including Hugh Patrick, to convince them that wider Pacific area cooperation would not mean domination by the major countries, but a strengthening of ASEAN itself. It took some time to persuade them, but eventually PECC was formed. The conference represents a unique type of cooperation for it involves both highly industrialized nations and developing countries; these countries are not only in different stages of development, but have different backgrounds, religions, and cultures.

Step by step, closer Pacific cooperation is being achieved. China and Taiwan joined PECC almost simultaneously five or six years ago, and Hong Kong has also become a member. Recently China has suggested the possibility of utilizing the PECC conference for summit meetings. Since China is not able to participate in official summits of heads of state because Taiwan and Hong Kong are involved, the use of a non-governmental body such as PECC would make it easier for China to attend high-level meetings.

Despite the political implications and complications, PECC members are developing closer economic ties. An example of this is the recent normalization of relations between China and South Korea. In this part of the world there is relative stability, and there have been moves toward more reconciliation. The former Soviet Union established a relationship with South Korea two years ago. Sharp divisions have been gradually reduced, although the Korea question is still a source of tension. There are also problems with Kampuchea, and most recently there have been some concerns about China's naval build-up. But overall, diplomatic and economic relations among the countries of Southeast and Northeast Asia are steadily improving. In this respect, the region compares favorably with greater Europe and other parts of the world.

The Role of China

Political questions regarding China remain, however, and there are some differences between Japan and the United States in this respect. The United States believes that human rights is the most crucial issue concerning China, and that political democratization is essential. However, Japan is more lenient towards China on human rights questions and democracy. Japanese recognize that strong government leadership may be necessary at some stages of modernization. If the government plays a leading role in modernization and industrialization, political democratization is likely to follow. This was the case in South Korea and Taiwan, and likewise for Japan.

A strong government can bring about economic modernization at the expense of sacrificing some political freedom. But once industrialization and modernization occur, democratization is likely to follow. This is one of the major differences of opinion between the United States and

Japanese governments. My prediction is that in the coming 10 years China will experience significant political change.

At a recent seminar in Tokyo there were representatives from China and Japan, as well as the United States, Russia, Singapore and the United Kingdom. Most everyone agreed that there should be harmonious relations between the three major powers: China, Japan and the United States. These countries must try to maintain relations in spite of their differences, otherwise there will be instability in the world.

Clearly one of the dangers to stability is a regional arms race which would undermine the international economy and create great political tension. Regarding the Sino-Japanese relationship, one danger is mutual mistrust. What if China does not trust Japan, particularly because Japan sent peace-keeping forces abroad? What if Japan becomes suspicious of the Chinese military build-up?

Market Economies and the Role of Government

Another question concerns the developing countries of China and India and the transforming countries of Eastern Europe and CIS. In the transition from centrally planned economies to market economies, what kinds of policies and processes should be adopted? Some American economists have recommended decisive measures of deregulation and privatization. The experience of Japan and other Asian countries suggests that a combination of government leadership and planning, along with the dynamism of privatization might well be a more realistic and effective policy for those economies.

This is a highly controversial question, for there are different types of capitalism. The structure of the Japanese and East Asian economies differs from the free market type of capitalism in the United States or the United Kingdom. Even within Europe there are differences between the capitalist economies of Germany, France and the United Kingdom. Regardless, the leading economic movement within the developing and transitory countries is either complete free market privatization or a combination of government leadership and the market mechanism.

Chalmers Johnson of the University of California, San Diego has argued that the Japanese style of capitalism is a form of developmental capitalism. Perhaps it might be more useful to consider it capitalism of the era of late industrial commerce, or "catching up" capitalism. For developing and transitioning countries it may be worthwhile to ponder a combination of free market capitalism along with a role for government along the lines of Japan's "catch-up" capitalism.

One of my books is entitled Approaching the 21st Century: Japan's Role. The first chapter is about the role of economists in government and focuses on the planning and market mechanisms in Japan. This is a very interesting topic for economists to study. I also argue that there should be a distinction between privatization of management and privatization of ownership. Naturally, for small enterprises the separation between ownership and management may be neither feasible nor desirable, but this is not necessarily the case for large enterprises. In China, for example, maintenance of the supremacy of the state proceeds simultaneously with developing management strategies in line with market forces. Sometimes this distinction faces severe difficulties, but the Chinese have been working in this direction for the past 15 years, emphasizing that the separation between state-run and state-owned enterprises is sometimes necessary.

India is faces this same problem, raising additional questions about the distinction between management and ownership. Most financial institutions in India are state-owned. In Japan there are 100 percent state-owned financial institutions such as the Japan Development Bank, the Japan Import-Export Bank, and the Japan Overseas Economic Cooperation Fund. Although these are government-owned, they are managed fairly efficiently. In the case of the Japan Development Bank (JDB), for example, the government gives general instructions regarding resources, reserves, and lending policy. Since the lending policy of the JDB influences the direction of investment of commercial banks, government policy has some indirect influence on the allocation of financial resources. This case may serve as a useful model for India.

In the case of the former Soviet Union, since there is no war-time destruction to deal with, it should be easier to make the transition to a market economy than it was for Japan following World War II. Nevertheless, the Soviet Union is disadvantaged in terms of monetary matters and other aspects of the real economy. Production--at the very least, the production of energy resources--needs to be stepped up. In the post-war period, Japan increased the production of coal, which was a combined economic policy emphasizing the recovery of the production of basic materials, particularly energy, as well as training human resources toward the transition to a market economy. In Russia there is too much emphasis on the financial side and insufficient attention to the real aspects of the economy. Large amounts of financial aid need to be extended to the real side of the economy for complete reform to succeed.

Russia has requested a sizable amount of overseas direct assistance (ODA) as well as lending, preferably soft loans in very large amounts, from Japan. But Japan is not sure if the Russians

are ready to receive such large financial transfers from industrial countries. Japan should carefully monitor the progress of the Russian economy, which so far does not look good. Production has dropped 20 to 30 percent in the last three years.