

Japan: The Nation without Nationalism¹

By Michael Smitka

Overview

I present three examples of contemporary Japanese economic nationalism below, and assess their import. What I found surprised me: the best examples I could come up with suggest recent “nationalistic” economic policies are either mislabeled, impotent or silly. A more systematic analysis may locate problem areas. But contrary to my thinking 5 years ago, my initial conclusion is that nationalism is not and will not be a threat to either Japan's neighbors or to itself.

The three cases I examine are (i) protectionism in trade, (ii) efforts to "internationalize" the yen, and (iii) immigration. Conveniently these also reflect, respectively, the broad topics of the international flows of goods, of finance and of people. They thus also cover the gamut of explicitly international areas of economic policy.

Let me provide an overview in inverse order of the paper itself. Immigration is thus first. Here, I expect that over the next decade Japan will welcome an increasingly large population of "guest" workers, who will in fact settle down and stay. This will of course cause problems, but my initial impulse to claim this as a symptom of "nationalism" represented fuzzy thinking on my part. The underlying issues are really those of plain old prejudice. That distinction may be scant comfort to those who face discrimination personally, but it does lessen its saliency for those concerned about broader policy issues. Second comes the yen. Japan is clearly pursuing the internationalization of the yen, largely for political reasons, but it is hard to discern what policymakers really mean by the term “internationalize”. In general, I believe that policies in that area will prove impotent; in fact, the term "silly" is a more apt descriptor.

My main example, protectionism in trade, continues to puzzle me. By and large Japan has one of the most open international trading systems, even if it has at the same time one of the most incumbent-friendly domestic regulatory and business environments. For the past decade import penetration has increased, coupled with recession. Many sectors of manufacturing are

¹ The initial draft of the paper was written for the September 26, 2002 Conference on Nationalism and Identity in Japan at the Meridian Conference Center, Washington, DC, sponsored by the Bureau of Intelligence and Research, US Department of State.

experiencing pain, and can point their fingers at imports. On top of this, basic political science suggests recent electoral reforms will encourage politicians to focus upon “issues” rather than the previous pattern of cash-intensive grassroots campaigning through local *koenkai*. Protecting local industry strikes me as a natural focus. Once I set out to look for it, I thus expected to find a wave of Japanese antidumping suits, VERs and other trade-restricting measures familiar from the US and EU environment. To my surprise that has not happened, and I am not sure why. In any case, it is ironic that during the past couple years Japan has proved a better global citizen on the trade front than have the US or the EU.

Before my case studies, and my attempt to intrude on fellow panelist Len Schoppa's turf and play the political scientist, I need to face the issue of defining "nationalism" head-on. To put it bluntly, for an economist there is no such thing; it is simply not an analytic category within my discipline. Of course states do adopt international economic policies, designed to enhance national welfare and prestige. Some of these are beggar-thy-neighbor in nature, but others are innocuous, and some are even beneficial to the world trading and financial system, or given the concern of this audience, to the United States. These are what I suspect the conference's organizers had in mind when they used the term "nationalism," and I will try to be a team player and stick to the topic. Of course, the vast majority of day to day behavior in politics and administration is undertaken in pursuit of purely local goals, casting no shadow beyond Japan's borders. There are exceptions where such behavior has international ramifications, and this represents a thorny problem for policy makers, since there is no established interface for discussing, much less influencing, policies far removed from the normal purview of foreign relations. But let me be consistent with my definition of terms: the problem in such cases is not “nationalism,” but that all politics is local.

Before I proceed, let me note limitations of my analysis. There are many examples beyond the three I give that might fit within the rubric of "economic nationalism". Given the need for brevity, two must suffice. One is the area of industrial policy, such as Japan's insistence on maintaining not one, but two separate space programs. Others lie in regulatory policy, such as the favoring of domestic firms. Now I know little about the specifics of the "Buy Japan" element of Tokyo's defense procurement policies. But the presence of a "home" bias is surely taken for granted in that area, regardless of country. I thus see no value in dwelling on military procurement as an example of “nationalism.” Similarly, a "home" bias in regulation is so

pervasive and indeed natural in any political system as to not merit special attention. After all, in almost any regulatory context, incumbents are known by and in turn know their regulators. It is really incumbency, not national identity, that is the distinguishing element. I believe other purported counterexamples will likewise innocuous. I will thus stick narrowly to my 3 examples.

Case One: Protectionism²

Japan is no more an industrialized country than is the US; manufacturing is a modest and shrinking share of the economy. That is to some extent reflected in public discourse; the layout of the *Nikkei*, Japan's main business daily, has less emphasis on manufacturing than was true 20 years ago. This secular trend is accentuated by the short-term impact of recession. Changes are startling in magnitude; Arthur Alexander, in a recent paper, notes that since 1995, output in the former core textile industry is down by 40% or more. Not surprisingly, there is constant discussion of "hollowing out" and (by implication) the need to "save" jobs. This past July, for example, the *Tokyo Shinbun*, a newspaper not thought of as a place one would go for serious analysis, carried a multi-day series of front-page stories, complemented by additional articles inside, on the rise of China. Combined with constant coverage of the ongoing recession, often told in the *Tokyo Shinbun* from the perspective of those who have lost jobs, stemming imports might seem a salient political issue among voters.

Even in the best of times, staving off protectionism is a political challenge. The gains from trade tend to be diffuse and incremental, so that few are willing to lobby on behalf of freeing up a specific market. In contrast, the losses from a rise in imports tend to be large in the eyes of the beholder, and to fall upon a small, often geographically concentrated set of firms and workers. They are willing to fight on behalf of their vested interests. Indeed, the puzzle for those working on the political economy of trade is why we have *any* cross-border flow of goods and services.

In Japan, the pressures should be greater today than in the past. Here I will point a finger at Len Schoppa. Comparative electoral studies find that single-member, first-past-the-post systems lead to two parties and an increased emphasis on issue-based campaigning. In today's environment, trade should be a "natural" issue for a politician on the hustings.

² The case study of trade policy is based on clippings from the Japanese-language press on the safeguard issue during 2001. I can provide a copy of my notes upon request.

I began to be concerned about this in the mid-1990s, when Japan pursued a WTO case against Indonesia over policies that favored a single "national" car producer over the affiliates of Japanese auto companies, only shortly after the US pursued the Japanese auto industry in the Framework talks. There was also a VER for Korean sweaters, and following examples set by the EU, cases involving the skewing of product standards for protectionist ends. This all seemed to represent a growing sophistication on the part of domestic industries in the use of domestic trade policy as a strategic tool. At the time, the frequency of such *ad hoc* measures was increasing. I feared this would generate the equivalent of the 1990s Japan lobby in the US: a group of Japanese bureaucratic and political actors and lobbyists whose careers are entwined with trade disputes, and whose continued power would be contingent on a steady stream of actions by Japan against one or another trade partner.

Then, in early 2001 when the agricultural lobby got into the act, I thought all my worst fears were being realized. In February 2001, after launching trial balloons to the domestic media, the Japanese Ministry of Agriculture, Forestry and Fisheries (MAFF) began discussions with China and Korea on a wide range of export restraints, with the threat that it would utilize "safeguard" measures to impose emergency tariffs on 14 items. Later that same month the Japanese towel industry also publicly asked for protection, the necktie industry was said to have begun preparations to do the same, and antidumping investigations started over the imports from Korea and Taiwan of polyester batting for *futon* sleeping mats. By late March the initial agriculture cases moved forward, with the Ministry of Agriculture formally entering into consultations with the Ministry of Economics, Trade and Industry (METI) and the Ministry of Finance over imposing "safeguard" measures for three Chinese products, *shiitake* mushrooms, leeks, and the straw for *tatami* floor mats. Those cases came to a head first. Negotiations with China stalled, and Japan implemented safeguards on April 23, 2001.

On the Japanese side, key politicians were involved; proponents were not limited to the Ministry of Agriculture. In particular, one important player, METI Minister Hiranuma, was a long-standing member of the *nozoku* or agricultural lobby, and a "prince" in the Kudo-Kamei faction of the LDP. This quieted any possible objections, or turf fights, between MAFF and METI, which normally handled trade issues. Japanese trading firms, who had contracted with wholesalers, extended technical assistance to Chinese producers and invested in warehousing fought these measures, but their objections were overruled. Chinese objections were ignored as

well. After all, China was running a large trade surplus with Japan, the affected goods were minor items among China's overall exports to Japan, the negotiations over China's accession to the WTO were still not complete, and projections suggested that China would soon have its own flood of agricultural imports as it implemented the reductions in trade barriers that the WTO would mandate. Besides, hadn't the French made the periodic protection of agricultural commodities an accepted part of the world trading system?

China, however, reacted swiftly and strongly, and in June 2001 implemented 100% retaliatory tariffs on auto imports (then running at about 26,000 Japanese cars a year), air conditioners and cell phones; they had apparently observed the 1995 Framework auto spat closely, when similar Japanese retaliation was successful in encouraging the US to back down. Toyota had not yet completed its plant in Tianjin, China, while European manufacturers seemed already well established. In the interim exports to China were important to the fledgling sales operations of Japanese producers. But the head of Keidanren, the largest Japanese business lobby, was Chairman Okuda of Toyota, who was already on record as opposing the safeguards. Now he was really energized, as were the heads of the large electronics firms that were affected. Import orders dried up almost immediately; among air conditioner producers the largest player, Daikin, soon was forced to shut down an assembly line.

Under the WTO, Japan could impose provisional safeguards for 200 days, but during that period a fact-finding process had to be undertaken, and then a formal petition filed with the WTO for approval of the implementation of emergency tariffs for a 4-year period (which could later be extended). In the end, when the 200-day provisional period ended in November 2001, they were allowed to expire. Negotiations with China continued, but when the fact-finding deadline was reached on December 21, 2001, the Japanese government formally dropped its safeguard measures, and China dropped its reprisals. In the interim, the formal implementation of textile safeguards for towels and neckties was put on hold, and in October 2001 the fact-finding process was extended for another 6 months. The final rationalization was that "these were minor products and not worth the fight." (*Asahi Shinbun*, 2001.10.23) Even the semiconductor industry had gotten negative feedback from METI in its exploration of an antidumping suit on chip imports. By the end of 2001, then, the whole set of protectionist measures had been shelved, and in the semiconductor case METI had managed to set a precedent that even "important" industries would not get a hearing.

In retrospect, Japan's avoidance of protectionism is not out of character with its behavior over the past 50 years, however startling it may be from a US or EU perspective. Japan has no more coal mines; the phasing out of the industry did entail one major political battle, but that was in 1960. The formerly large textile industry has faded away, with hardly any notice in public. Japan has no more domestic TV manufacturers, with nary a notice in the news, and certainly no round of antitrust actions and antidumping suits. And, most amazing of all, the current, elderly generation of farmers may be Japan's last. The battle over self-sufficiency in food was fought, and lost, around 1918, when Japan adopted a policy of grain importation. The process has not been immune from politics; unlike in the 1920s, rice farmers do not lack in "voice." But overall, Japan is quite remarkable in that industry after industry has faded into oblivion in the face of imports, with rear-guard actions that are at best modest in comparison to those in similar industries in the US.

Such Japanese exceptionalism is puzzling, and it is important to understand its source to predict whether it will continue into the future. I have two hypotheses on why trade policy has proved so impotent. One is the nature of the Japanese legislature, that Diet members have little direct role in formulating initial policies. They have small staffs and, given the factional basis of funding, exhibit a high level of interpersonal rivalry. This has inhibited the development of the sort of log-rolling that is particularly visible in US agricultural policy, which strengthens the hand of otherwise small lobbies by facilitating the formation of broad coalitions. Second, the bureaucracy is, if anything, even more fragmented. Japan lacks the interagency clearing process that is a systematic feature of trade policy in the US. In addition, there are no political appointees who can work directly with the legislature (and, in the US, the White House) to push their own agenda, or who can be drafted by outsiders in the political process as active allies. In Japan, the career ladder within the Ministries penalizes such independent action. Finally, that same career ladder, and a corresponding lack of horizontal mobility, impede the development of coalitions across ministries, or even across divisions within the same ministry. Bureaucrats are surprisingly impotent, and despite the predictions of early analyses of electoral reform, so are politicians.

Perhaps I should refer to this as the enigma of powerlessness, or to play upon Chalmers Johnson, the curse of the developmental state. In any event, I am now convinced that, instead of posing a threat to the global trading system through rampant and capricious protectionism, Japan may turn into one of the better citizens in the developed world.

Case Two: International Finance

Japan – or rather Japanese leaders – do, however, crave international recognition for their country's success, and public symbols of its weight in global trade and the Asian-Pacific region. One explicit attempt to achieve this was through a set of policies, trumpeted more loudly after the Asian financial crisis of 1997, to make the yen into an international currency. Tied closely to this were proposals, or probably more accurately trial balloons, for the formation of an Asian Monetary Fund or AMF.

Now the international financial system is at times short on liquidity; the IMF simply has not kept up with growth of the world economy, and is too small relative to today's middle income countries to be able to step in on its own. But if the IMF has a hard time garnering sufficient resources, why would the AMF do any better? Japan alone is too small, and too suspect. Furthermore, how would the AMF coordinate its activities with other players? – or would it in the end undermine their already limited effectiveness? In the end, this trial balloon did not rise very high.

Yen proposals were taken more seriously, and the international finance section of MOF was pressured into devoting part of its limited personnel resources to pushing that policy. But it is not clear what Japan would stand to gain, or how the use of the yen as a foreign reserve asset and a core currency for international transactions might be accomplished. First, Japan is a creditor country, not a debtor. Because it runs a chronic trade surplus, it has built up stocks of other countries' currencies, and so there is no natural mechanism through which countries in Asia would automatically end up holding yen. Second, returns on yen assets are low, or at least are viewed as such *ex ante*. Quite simply, private investors do not find holding yen assets attractive, and central banks throughout Asia share their opinion. There is nothing discriminatory about this; Japanese behave in the same way. That is, after all, why Japan is an international creditor: Japanese domestic investors want to hold foreign assets, too.

Finally, traders have no particular incentive to switch the “numeraire” currency in which they do their trades and even accounting. In most cases international contracts are denominated by dollars as much by habit as anything, even when neither side actually wants to end up with dollars. Now habits can be broken. But if habit is all that matters, then private traders see little benefit to using one currency over another. Even if Japan could somehow make yen a currency of preference for denominating foreign trade in the Asian region, it would generate few if any

benefits for Japan. Already firms routinely use forward contracts to lock in exchange rates 6 months or even a year into the future; they don't need yen denomination to lock in yen exchange rates. And most import prices are flexible, so that from a domestic standpoint using the yen as a trade currency with a "fixed" exchange rate would not remove the risk of price changes.

In private conversations, MOF officials shared this perspective: "internationalization of the yen" was not so much ineffective as silly. It represents a nationalism so vague and empty of policy significance as to not be worrisome. If this is all the danger that nationalism represents, then we have little need to pay further attention.

Case Three: Immigration

Looking toward the future, demographic shifts in Japan are already leading to a decline in the working-age population, and in the next several years will lead to labor shortages – as an economist I must add "at prevailing wages" – even if economic growth never really picks up again. This will be starkest at the industry level, particularly in health care, but also perhaps in a range of manufacturing sectors. Given the precedents of the EU and the US, I feel quite confident in predicting that immigrant labor will become a standard feature of the landscape. Indeed, in factory visits in July 2002, I found certain operations manned almost entirely by Brazilians, and for reasons I can only guess at, get a newsletter from Gifu every month printed in Japanese, Portuguese and Chinese. For some firms, and for some local governments, the presence of non-Japanese is taken as a matter of course, as is the need to provide for them.

That there will be tensions among ethnic groups is inevitable. I grew up in the city of Detroit, which was quite nasty in that regard, and then lived in Queens in New York, where the tensions were more along ethnic than racial lines. In Japan I have on a couple very rare occasions been made unwelcome; Japanese-Korean friends, especially older ones, have quite different experiences. But my personal judgment is that, first, in qualitative terms such tensions are no worse than in the United States, and second, that as in the U.S., the appropriate term is prejudice, not "nationalism."

Economic forces will increase the presence of ethnic minorities in Japan. They will become numerous enough to form communities that will make them more obtrusive than the isolated, individual "gaijin" tend to be at present. These communities will furthermore

increasingly be comprised of families, not individual male or female workers. In short, the immigrants will come to Japan and stay.

Clearly this will cause friction, but I judge that it will not cause much friction. One mitigating factor is that the process of urban development in Japan has resulted in neighborhoods with a mix of vintage and type of housing. Compared to the US or Europe, in the major urban centers ethnic communities will for the most part not be the same as ethnic neighborhoods. Ghettos will be the exception, not the norm, among immigrant populations. As a result, for example, elementary schools will have a smattering of non-Japanese of various parental ethnicities, but only infrequently large blocs of students from a single background. I believe that this will result in a less harsh experience for minorities in Japan than in countries where physical segregation has accompanied the migration of minorities in search of jobs. Furthermore, the electorate in Japan will be increasingly elderly, and will benefit directly from the services provided by guest workers; immigrants will not be competing with voters for jobs and government programs. In the US and Europe, taking an anti-minority stance has from time to time been a sensible if reprehensible political strategy. Japan will be different.

Summary

Nationalism is an awkward concept for an economist. Nevertheless, economics can offer many examples, such as beggar-thy-neighbor trade measures that others might term "nationalistic." I thus picked out likely examples, and analyzed them. Having done so, I conclude that Japan is really quite unusual in the lack of such nationalistic policies. This does not mean that Japan is an easy place for new entrants to break into markets, but that is due to policies that favor incumbents rather than ones intended to benefit "national" firms. Nor does it mean that economic policy in Japan should be a matter of indifference to the rest of the world. Poor performance of a major economy should always be a matter of concern, but it would be absurd to claim that a fit of nationalist fervor led Japan to shoot itself in the foot to drag down other countries. In contrast, in areas of explicit nationalism, such as trade policy, international financial policy, and immigration – the international flow of goods, services and people – Japan is, by and large, either being a good citizen, or moving in the right direction.