

Młodawska, Jolanta

## Article

# Japan's new competitive advantage: the arguments and proposals for structural reorientation

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**JOLANTA MŁODAWSKA\***

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**Japan's new competitive advantage: the arguments and proposals  
for structural reorientation****Abstract**

*As forecasted by the Japanese government, the country's economy will grow, although slowly. This expectation is determined by the risk that the labour market situation and the worldwide business cycle will keep deteriorating. It is believed that the economy will not be spurred by exports growing as a result of worldwide recovery, but rather by a series of stabilization packages and gradually expanding domestic demand<sup>61</sup>. The expectations should be treated with a great deal of cautiousness, because of the highly unpredictable rate of unemployment, the concerns about deflation and the probability of the global recession turning out more serious than expected.*

*According to the AFP (Gazeta Wyborcza of 08 Dec. 2009), in the third quarter of 2009 the Japanese economy finally showed some signs of recovery and reached positive values; unemployment also dropped from 5.3% to 5.1% between September and October. The widespread opinion is that the recovery is very fragile, as proved by the steadily falling prices, deflation, and the rising yen exchange rate (the highest in the last 14 years – 84 yen to 1 US dollar), threatening the Japanese exports.*

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\* Ph. D., Professor at the University of Łódź

<sup>61</sup> Based on the Key Points of the Japanese Economy, internal documents of the Economic Section of Japan Embassy in Poland, 15 July, 2009.

## 1. Introduction

The present recession in Japan, induced by the global crisis, is the most serious of all recessions noted in the years of post-war development. The falling foreign trade turnover rapidly reduced exports and private investments, while growing unemployment and falling wages negatively affected the level of consumption. Even though it is believed that an expansive fiscal policy may have a positive, although limited, effect on economic growth, its rate will be below 1% throughout the year 2010 (see table 1).

The Bank of Japan is determined to counteract inflation by „injecting” additional funds into the economy, until a stable upward trend appears. However, once the economy is back on the growth trajectory, the primary goal will become the consolidation of government’s revenues, considering the large budget deficit and the huge public debt (around 140% of GDP). Some of the paramount strategic goals include the tax system and social security system reforms as well as a necessary structural reform addressing mainly the service sector, because of the aging of Japanese society.

**Table. 1 Japan’s real GDP as estimated by various institutions (%)**

| <b>Calendar year</b>                         | <b>2008</b> | <b>2009</b>        | <b>2010</b>      |
|--|-------------|--------------------|------------------|
| IMF „World Economic Outlook” (July)          | - 0.7       | - 6.0              | 1.7              |
| OECD „Economic Outlook 85” (June)            |             | - 6.8              | 0.7              |
| <b>Fiscal year</b>                           | <b>2008</b> | <b>2009</b>        | <b>2010</b>      |
| Government (January)                         | -3.3        | 0.0                | -                |
| Prime Minister’s Office (July)               |             | - 3.3              | -                |
| Council on Economic and Fiscal Policy (July) |             | -                  | 0.6 <sup>1</sup> |
| Bank of Japan (July)                         |             | - 3.4 <sup>2</sup> | 1.0 <sup>2</sup> |

<sup>1</sup> data presented only for the 2010 budget discussion

<sup>2</sup> a median derived from the projections of the Council on Economic and Fiscal Policy

Source: Internal documents of the Economic Section, Japan Embassy in Poland, 15 June 2009.

The short-term goals of the Japanese economic policy were laid out in the „Anti-crisis Package” of 10 April 2009. The package is valued at ¥ 15.4 trillion (the national budget) and ¥ 56. 8 trillion (local budgets)<sup>62</sup>, equivalent to US\$ 81 bn, to be spent in a twelve month period. The impact of this huge money supply is estimated at additional 1.9% of real GDP. The target amount in a long-term perspective is at least US\$ 274 billion. However, the Stimulation Package does not address the essential problems, such as the weakness of the global economy and deflation.

The main measures included in the Package are public works undertaken on an unprecedented scale, employment-supporting projects (re-employment and retraining assistance, creation of new jobs, unemployment benefits, social security benefits), as well as financial support for the qualifying entities and lines of economic development (SMEs, the stock exchange, residential building and transactions involving land). „Investments in future” are proposed, such as the development of alternative energy source (e.g. solar energy), the construction of low fuel consumption vehicles and new methods for storing and transporting energy. There are plans to support financially healthcare, the longevity of the nation and measures improving the rate of natural increase. An important goal is exploitation of reserves based on the development of the backward segments of Japan's economy, such as agriculture, forestry, fishery, and on the creation of new technologies.

From the wide range of the long-term problems, the article (Parts I and II) will discuss:

- 1.the „aging” of Japanese society,
- 2.the redefinition of economy's competitiveness,
- 3.capital flows – foreign direct investments (FDI),
- 4.the „dual” character of the Japanese economy,
- 5.the necessary structural reform and privatisation,
- 6.the concept of new industries.

The above subject will be discussed in relation to the traditional Japanese-continental (Rhine) model of corporate governance functioning in Japan in contrast to the Anglo-American model.

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<sup>62</sup> Ibidem.

## 2. The Japanese corporate governance model

H. Funabashi<sup>63</sup> indicated eight principles underpinning a traditional Japanese firm:

- clear, well-defined values, vision of operation and mission,
- long-term planning,
- accentuating the human factor in an enterprise,
- focus on customers,
- social functions of an enterprise,
- continuous innovation and improvement,
- frugality and effective use of resources,
- special organizational culture, tradition.

The above list well corresponds to the known characteristics of the Rhine corporate governance model<sup>64</sup>:

- workforce plays a vital role in an enterprise,
- pay inequalities are insignificant (i.e. the income differences between the managers and the workforce),
- dismissals are occasional,
- the major source of investment funds is bank debt,
- the in-house managers are promoted.

The above structure contrasts with the Anglo-American model where:

- the shareholders' rights prevail over the employees' rights,
- information on a firm is readily available and accessible,
- the short-term results are prioritized, which leads to employee dismissals in the downturn periods,
- managers' incomes are closely related to performance,

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<sup>63</sup> H. Funabashi, Longevity of Corporations in Japan, in: proceedings from the conference „Corporate Cultures; Universality and Differences”, Akademia im. L. Koźmińskiego, 13-14 May 2009.

<sup>64</sup> This is the traditional model – the socio-economic development in Japan and the globalisation processes have been inducing numerous modifications and major adjustments to it. See J. Młodawska, Reński model nadzoru korporacyjnego w Niemczech i w Japonii – charakterystyka i perspektywy zmian, „Gospodarka w praktyce i teorii”, 2006, no. 2.

- the investment funds are mainly raised on the stock exchange,
- the directors are recruited in the market,
- mergers and acquisitions are deemed a guarantee of good economic results.

### **3. The demographic situation and the necessary reform of the pensions and social security system in Japan**

Why is the aging of the Japanese society and the declining natural increase such an important problem at the present stage of development? In the 1990s, soon after the speculative bubble burst, the Japanese economy plunged into recession that continued for more than a decade, relieved by short spells of recovery that mainly resulted from the large-scale public works, tax cuts and other measures „feeding money” into the economy. Their influence radically diminished when the government reduced its expenditures. The stimulating package of 2006 was estimated at a still large amount of ¥ 15.4 trillion, though.

The business cycle improved in 2002 as a result of other developments, mainly the energetic activity of the private sector with the weakening fiscal impulse. In the next four years, Japanese businesses almost completely dealt with three excesses: surplus employment, production capacities inflated in the period of *prosperity* and bad debts. However, a continued growth calls for measures other than the extensive ones. The macro economic policy (fiscal and monetary) fell short of energizing the economy. The recession that followed the „bubble-driven growth period” had two special characteristics. Firstly, the annual rate of growth was ca 1%, i.e. much below its values in the other post-war decades, and the period of still noticeable decline is much longer. Secondly, deflation appeared (the GDP deflator was negative starting with the third quarter of 1994, excluding the fiscal year 1997, when the VAT rate was raised). After 2006, Japan's economic situation deteriorated again.

Deflation stayed at a moderate level of around 0.5% a year for a long time. In 1991, the Bank of Japan (BOJ) started following a zero interest rate policy, a solution without precedent in the world. Before the policy was abandoned in 2006, the BOJ had reduced interest rates as many as twelve times. The base interest rates stood at 0.1% from the year 1999. As they could not be reduced still lower, they lost their stimulating influence on the economy. At the same time, the “cheap money” policy pursued from 2001 completely lost its *announcement effect*, i.e. the ability of informing the public about the planned changes in the government policy. Although the negative growth trend in Japan has been slowly receding for seven years now, a structural reform seems to be

more and more desirable. The Japanese economy has today the highest unit labour cost in the world<sup>65</sup> and in 2005 the number of the Japanese population started to decrease for the first time. This is the main problem of the country where population aging is faster than elsewhere and where the rate of natural increase is also falling the fastest.

The present Nippon's population of 128 million is likely to fall to 118 million by the year 2030 and the percentage of seniors (aged 65+) is predicted to grow from 19.9 to 29.6%. This course of events will reduce the amount of savings that have been the major source of investment funds so far. In 1991, savings still increased at 15% a year, but in 2003 the rate was 7.3%. As projected, households' savings will reach negative values by 2030. The aforementioned necessity of launching structural reforms means therefore that the way of increasing capital gains should be FDI intensification as well as improved allocation of resources: seeking new high-tech branches and restructuring the ineffective parts of the economy.

Within the Japanese pension system, a range of problems and inconsistencies can be spotted. There are at least four issues that are worth raising. Firstly, although the average life expectancy of the Japanese population is the longest in the world, many firms still stick to the statutory retirement age of 60 years. The regulations introduced in 2006 obligated the employers to keep their workforce until 63 years of age, with the law becoming effective as of April 2007, when a large number of baby boomers were to turn 60 years old. This solution was a provisional remedial measure and most firms kept the age limit of 60 years, allowing only the interested persons to extend their employment contracts every year.

Secondly, the young Japanese are losing their trust in the public social security system. Almost half of persons older than 29 years usually build their retirement plans on personal savings and not on public mechanisms. Around 36 % of the citizens running their own firms and students aged 20+ do not contribute to the pension system at all<sup>66</sup>.

With the longest life expectancy among the developed countries of the world, the Japanese also have the lowest old-age pensions. Besides, most citizens still want to work in their middle adulthood – 70% of males aged 60-65 years are economically active or seek employment. In the USA the rate is below 60% and for Germany it is only 30%. Thirdly, measures aimed at reducing youth unemployment are still relatively rare, because many enterprises have kept the

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<sup>65</sup> See A. Kojima, *A New Development Model for Japan. Selected Essays, 2000-2008*, 2008.

<sup>66</sup> *Ibidem*.

lifetime employment approach despite the amended laws, and the financial crisis of 1997 limited the recruitment of graduates. Fourthly, the Japanese corporations have substantially extended their use of temporary workforce at the expense of workers with employment contracts, thus deteriorating the situation of young persons again.

Natural increase is still another problem – the 2005 fertility rate in Japan was only 1.25. To maintain the present size of population at least, the rate should be 2.07. The following measures are therefore necessary to induce the required change:

1. friendly economic and social solutions addressed to the fertile-age population,
2. a reform of the pension and social security system, allowing older persons to work longer and thus reducing the burden carried by the younger generation,
3. better conditions for mothers raising children.

The detailed solutions in the state pension system decide about the credibility of the whole decision-making mechanism and about its daily management. Regarding the latter aspect, the large number of deficiencies, or even scandals, that were discovered recently in SIA functioning (Social Insurance Agency) made the public distrustful in the actions devised by the officials. The situation is aggravated by a much more serious issue – the possible inefficiency of the whole system resulting directly from the rapid aging of the Japanese population and indirectly from the fact that Japanese pensions are paid out “on a current basis”, which means that their source is contributions submitted by the economically active population. Another important factor is that many firms still exercise the retirement age limit of 60 years.

The authorities have launched many measures to alleviate the present situation; for instance, higher contributions and lower old-age pensions were enacted, and the employers are encouraged to raise the retirement age significantly, or to conclude three years' contracts with older workers. Notwithstanding, as mentioned, the number of persons, especially the young ones, who completely withdraw from the government system has been growing. Unlike the older generation that will recover the amounts it has paid to the system during the entire period of economic activity, the younger people cannot be sure of that. This situation has given rise to the problem of social injustice embedded in the intergenerational context. So it cannot be surprising that although all Japanese turning 21 years are expected to contribute to the pension fund, a growing percentage of such persons refuse to do so.

Each time the demographic projections overshoot the actual rate of natural increase, the government tries to fix the situation by increasing the level of



insurance contributions and reducing the amounts of the benefits. It is being proposed now that the entire amount of an old-age pension (a so-called base pension) be funded from taxes, instead of the present solution where two thirds of the pension comes from the obligatory contributions and one third from taxes<sup>67</sup>. If this variant were to be implemented, then the present VAT rate of 5% would have to be increased by as many as five percentage points. A monthly pension would remain at the level of ¥ 66,000 (ca US\$ 600), but only in the case of those retirees who have contributed to the system for 40 years. Contributions paid regularly for the whole period of 25 years would entitle to a reduced old-age pension and any negligence (e.g. a month contribution missing) would deprive the potential beneficiary of any equivalent!

The government pension is now granted to persons reaching the age of 65 years, but raising the limit to 67 years is proposed, so that considerable VAT increases can be avoided. Consequently, private entrepreneurs are also expected raise the retirement age. In the transition period, the beneficiaries covered by the old system would draw their old age pensions in proportion to the number of pensionable years. Such persons would be included in both the new and the existing system. There are also plans to limit the income tax exemptions in the case of persons drawing old age pensions so as to decrease government's net subsidies to the well-off seniors. Today, employers are obligated to finance half of the obligatory workers' contributions to the base pensions. The proposed modification of the system for financing pensions, where tax revenues replace enterprise resources would considerably reduce employers' liabilities. The Nikkei Inc. Panel suggests that some of the savings thus obtained could be used to extend the pension system over the temporary and seasonal workers. The Panel's report also proposes to replace the term „a base pension” with „a universal pension” to accentuate the direction of the changes.

#### **4. The competitiveness of the Japanese economy – a definitional change. The Japanese FDI as illustrated by the case of Poland**

Globalization preferences successively reshape the character of a competitive advantage. Competitiveness depends today on having a knowledge-based economy with flexible modes of operation and structures. In the past, Japan paid special attention to the cultural factors and the role played

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<sup>67</sup> Proposed by the so-called Nikkei group associating scientists, journalists and other experts; Nikkei Inc. is the publisher of the Nihon Keizai Shimbun (Japan's Economy Daily).

by institutions. Why has Japan lost so much of its competitiveness in the last two decades?

Competitiveness seems to have much deeper roots than culture and tradition alone, and **the export of capital services and technologies outweighs low manufacturing costs**. Notwithstanding, contemporary Japan concentrates on routine operations, unlike the other developed economies that build strategies and oversee institutional changes. The real challenge is investment-driven development, but in Japan the number of investments has been falling alongside the declining rate of savings.

„The World Competitiveness Yearbook” of 2002 recognized the USA as the most competitive economy in the world and Finland was ranked second<sup>68</sup>. Japan, ranked 26<sup>th</sup> in 2002, slid into the 30<sup>th</sup> position a year later (Poland oscillates around the 45<sup>th</sup> position). It is worth mentioning that in 1991 Japan was the leader in the same ranking, with the USA and Germany being second and third, respectively. The year 1991 marked a watershed in the speculative growth of the Japanese economy, opening at the same time the longest period of US expansion after World War II.

Dynamically growing FDI is believed to have a strong, spurring effect on country's competitive advantage. The incoming and outgoing investments in Japan are imbalanced, as the outgoing FDI largely exceeds its inflow<sup>69</sup>. In 1996, the incoming and outgoing flows of investments accounted for US\$ 23.4 bn and only US\$ 200 million, respectively, growing in 2000 to US\$ 31.5 bn and US\$ 8.2 bn. The White Paper on International Trade of 2001<sup>70</sup> presents “shocking” comparative data. In 1998, the received FDI's share in gross capital assets averaged 11.1% in the world, 10.9% in the developed countries and 15.3% in the EU (see table 2). Regarding the particular countries, the rate was 12.8% in the USA, 12.9% in China and 5.5% in Korea. Among the European countries, Sweden had the rate at the level of 59.8%, in the Netherlands it was 55.2%,

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<sup>68</sup> See The World Competitiveness Yearbook 2002, International Institute for Management Development, 2002.

<sup>69</sup> The literature treats the outgoing FDI more at length, perhaps not only because their value is higher, but also because of their larger (compared with the incoming investments) importance in the past. For instance, A. Drzymala examines in his article: „Wybrane aspekty oddziaływania japońskich bezpośrednich inwestycji zagranicznych na japońską gospodarkę”, *Gospodarka w praktyce i teorii*, no. 2, 2008, the traditionally understood benefits offered by the outgoing FDI with respect to the following areas: trade, technology, manufacture and employment.

<sup>70</sup> The White Paper on International Trade 2001, METI (Ministry of Economy, Trade and Industry), 2001.

51.3% in Finland, and 25.7% in the UK. In Japan the rate was extremely low – 0.3%!

Japan's focus on boosting the outbound FDI and her underestimation of the inbound FDI separate the country from the world trends and make it less appealing to foreign firms. Perhaps this situation should entail an adjustment of the country's broadly understood investment environment and infrastructure? However, this course of action is inseparable from launching a fully fledged structural reform.

**Table 2. The incoming FDI values (in US\$ billions)**

| Ranked (1999) | Country            | 1990 | 1995 | 1996 | 1997 | 1998 | 1999 |
|---------------|--------------------|------|------|------|------|------|------|
| 1             | USA                | 479  | 675  | 770  | 1060 | 1863 | 2755 |
| 2             | UK                 | 324  | 225  | 324  | 370  | 637  | 848  |
| 3             | Sweden             | 20   | 149  | 55   | 103  | 194  | 594  |
| 4             | Germany            |      | 120  | 32   | 117  | 201  | 522  |
| 5             | France             | 132  | 237  | 220  | 231  | 295  | 388  |
| 6             | China              | 35   | 359  | 402  | 442  | 438  | 388  |
| 7             | Belgium/Luxembourg | 81   | 105  | 147  | 120  | 227  | 384  |
| 8             | Netherlands        | 123  | 115  | 78   | 118  | 372  | 342  |
| 9             | Brazil             | 10   | 49   | 99   | 197  | 319  | 327  |
| 10            | Canada             | 76   | 108  | 64   | 118  | 217  | 251  |
| 11            | Argentina          | 18   | 42   | 43   | 88   | 67   | 236  |
| 12            | Hong Kong          |      |      |      |      | 148  | 231  |
| 13            | Ireland            | 6    | 15   | 25   | 27   | 110  | 191  |
| 14            | Japan              | 18   | 0    | 2    | 32   | 33   | 123  |

Source: IMF data, International Financial Statistics.

Japan's current account balance still shows the largest surplus in the world that reached ¥ 18 trillion (around US\$ 150 bn) in 2005. However, its structure has been changing in time. The capital incomes, i.e. capital gains and dividends, exceeded the incomes derived from foreign trade for the first time in 2005

(¥ 11.4 trillion and ¥ 10.4 trillion, respectively). The current account surplus represented around 4% of the Japanese GDP. However, the growing investment incomes were still accompanied by small amounts of the incoming FDI. The amounts of the received FDI are very important for Japan's further economic growth, considering that its population is aging and the natural increase is falling.

Japan's weak interest in the outgoing FDI can be illustrated with the magnitudes and structure of the Japanese FDI in Central and Eastern Europe, particularly in Poland. The national characteristics of the Japanese and their patterns of behaviour largely determine their business attitudes: they tend to take group actions, revealing a sort of a „herd instinct”. They have difficulty launching overseas projects on their own account but willingly join other initiatives, such direct investments, portfolio investments or strategic alliances.

Some of the reasons encouraging Japanese businesses to invest in the CEE countries are the following<sup>71</sup>: 1) attractive markets; 2) lower labour costs compared with Western Europe – although Poland cannot compete against China or the former USSR countries as far as the low-skilled labour costs are concerned, the professional bearing and the language skills of the Polish „white collars” are ranked high among other nationalities; 3) the possibility of acquiring production facilities that allow the Japanese firms to make and sale their products (e.g. Magyar Suzuki in Hungary and NSK, the producer of ball bearings and spark plugs, in Poland).

The incoming investments substantially increased across Central Europe following the admission of the regional states to the European Union. The investments almost doubled in 2004 compared with the previous year, reaching the level of US\$ 16.3 bn. A year later, their maximal value went up to US\$ 28 bn<sup>72</sup>. Although the absolute numbers may show Poland as the largest beneficiary among the CEE countries, her relatively large population makes the Polish FDI *per capita* vary from one third to one fourth of its value in Hungary, the Czech Republic or Estonia. The inflow of investments in relation to Polish GDP is around 25% and it does not compare, for instance, with the Estonian 78.6%<sup>73</sup>.

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<sup>71</sup> From the discussion with Yoji Koyama, a professor emeritus of the university in Niigata, Japan.

<sup>72</sup> See G. Kozuń-Cieślak, „Kapitał zagraniczny w Specjalnych Strefach Ekonomicznych”, in: *Kapitał zagranicznych w Polsce w dobie globalizacji*, E. Freitag-Mika (ed.), Wydawnictwo Instytutu Technologii Eksploatacji, Radom, 2006.

<sup>73</sup> See Y. Koyama, *Direct Investment of Japanese Companies in Poland and Other Countries in Central and Eastern Europe and Their Strategies*, proceedings of the conference *Corporate Culture. Universality and Differences*, L. Koźmiński Academy -14 May 2009.

At the end of 2004, the Polish investments of 15 foreign firms were estimated to exceed US\$ 1 bn, the largest investors being, by their size, France Telecom, EBRD and Fiat. The main type of business in the group was financial intermediation. The Japanese were almost imperceptible in the CEE region, with their turnover with the CEE countries estimated at only 0.2% in the early 1990s, i.e. 0.4% of the value of the Japanese trade with abroad. In this decade, the Japanese FDI (excluding few firms such as Suzuki) were mainly represented by the wholesaling and retail business, as well as exports of the Japanese manufacturing industry, predominantly the machine-building industry (Japanese manufacturers operating through their EU branches).

In the mid-1990s, the Japanese boosted their investment activity in this part of the world, focusing their attention on the manufacturing industry, but even then, the Japanese FDI in the CEE region was estimated at only US\$ 2.8 bn as of the end of 2000. Because of the forthcoming admission of 12 new countries to the European Union in 2004, the Japanese raised their CEE investments to US\$ 24.4 bn in 2002, but this number still accounted for only 0.5% of their outgoing FDI. Most of the investments were made in the Czech Republic, Hungary, and Poland<sup>74</sup>. This policy intended to secure the potential markets and export opportunities for the mother companies in Japan. The Japanese investments in CEE were “narrowly” channelled into two favoured branches of industry: automotive and electromechanical engineering, as it was expected that the more restrictive environmental laws specific to the European Union would boost the demand for new cars in the recently admitted countries and that the better-off citizens would choose to have a second car in the family. At first, the Polish government promoted capital privatisation with the participation of foreign investors (mergers and acquisitions), but with legislation amendments in the second half of the 1990s that „warmed up” the investment climate in Poland the major types of the incoming FDI changed.

The relaxation of the tax rules applying to foreign firms and the abandonment of regulations limiting the ownership of stocks, the values of new issues, or employment, etc., increased the number of investments with foreign-owned majority stake, mainly of the greenfield projects. At the end of 2006, over 150 Japanese corporations traded and manufactured in the territory of Poland. Between 2000 and 2007, the number of the manufacturing enterprises grew from 14 to 58. Poland probably ranks fifth as the European recipient of the Japanese investments, after the UK, France, Germany and the Czech Republic<sup>75</sup>.

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<sup>74</sup> Ibidem.

<sup>75</sup> JETRO's internal documents (Japan External Trade Research Organization), 2007.

The major Japanese projects in Poland include the Toyota Motor Poland plants in Wałbrzych that manufacture gear boxes and low-compression engines and the so-called Crystal Park near Toruń where the production of plasma TV sets started in 2006; the major player in the Crystal Park is Sharp. Unfortunately, the Japanese invariably underline several disadvantages that make our country less attractive as a destination for investments: 1) a very low share of R+D outlays in GDP (0.58% in 2006) compared with the EU average of 1.9%<sup>76</sup>; 2) some shortage of highly-qualified labour (the middle-level management); 3) the slow implementation of investment incentives that are applied in the EU; 4) the poor condition of roads.

### 5. The microeconomic operational effectiveness *versus* strategic effectiveness

Japan's problems with economic growth are due to the errors in macroeconomic policy, but primarily to the low microeconomic effectiveness of many branches of industry, services and agriculture. This is not to mean that the government's measures aimed at stimulating growth and restoring banking sector's liquidity are unimportant; yet, the macroeconomic policy tools alone cannot bring the expected results. The Bank of Japan followed the policy of a short-term zero discount rate for a long time; public works, tax cuts, subsidies for the „lame” banks, and even food vouchers consumed almost US\$ 1.5 bn. All the extraordinary measures failed the hopes that were vested in them.

As regards the operational competitiveness, many Japanese firms still adhere to the cost minimization principle while lacking distinct long-term strategies. Naturally, there are some positive exceptions in their group, but these are **not** the powerful, well-established corporations, but the relatively new firms that started up in the 1980s or 1990s and are “infected” by the traditional model of a Japanese enterprise to a rather low degree. Unable to use the resources and power arising from the connections with the industrial-financial groups „*keiretsu*”, they had to specialise themselves and fill in the identified production niches that were rejected by the dominating investors<sup>77</sup>. The group of the global market leaders comprises today organizations with **definite** strategies, such as Nintendo, Sega and Sony – video games; Toray – carbon fibres, or Juki with its

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<sup>76</sup> See Y. Koyama, *Direct Investment of....*, op.cit.

<sup>77</sup> This is how individual entrepreneurship developed in the Kyoto region, far away from the industrial centres of Tokyo and Osaka.

industrial sewing machines. Toray decided to meet the needs of a selected group of sports equipment manufacturers, giving up orders from the defence and space sectors. Regarding sewing machines, Juki chose the industrial segment, abandoning household sewing machines.

Developing a programme where the products and the buyers are clearly differentiated is a necessity today, also for the Japanese giants. For instance, in the industry producing fax machines, the leading manufacturers undermined the profitability of the business by not selecting the distribution channels and by introducing standard products unattached to a specific producer to the market. As a result, rather indistinguishable advertising campaigns launched by behemoths such as Matsushita, Canon, Toshiba, Ricoh, NEC, Sharp, Mitsubishi, Fujitsu, Hitachi, Murata and Minolta did not emphasise specialization and diversification. The large corporations usually favoured price competition, which reduced the average price of a fax machine in Japan from ¥ 78,717 to ¥ 42,498 yens between 1992 and 1998<sup>78</sup>.

Replacing the focus on the present, on the volume of production, with a strategic approach emphasising originality and ensuring expected revenues involves appropriate readjustment of the corporate governance system, the enterprise model and the role of the government<sup>79</sup>. In Japan, around 60% of the large firms' stocks are held by stable, long term shareholders (banks, insurance institutions, and cooperating enterprises). They do not demand particularly high returns and resale their holdings quite rarely, tending to treat the assets as a secure deposit rather than an investment. The main advantage of the cross-shareholding system is a stable and expanding network of contacts within the capital group. It is not surprising therefore, that with this ownership structure firm expansion (sales boosting) and job creation in the cooperating organizations motivate the managers more strongly than the short-term profitability.

Japan certainly needs a new **corporate governance model**, because its economy shall not be able to solve the competitiveness problem without placing a stronger emphasis on a more effective use of capital and satisfying profits. Increased transparency and openness of the decision-making processes are necessary, likewise more independent boards of directors and shareholders with a true influence over the companies' strategies.

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<sup>78</sup> See Asahi Shimbun, (Asahi Daily) 29 July, 1999.

<sup>79</sup> More on the theory of changes in the continental-Japanese corporate governance system can be sought in J. Młodawska's „Tradycja i współczesność-model nadzoru korporacyjnego” in: Meandry japońskiej polityki, J. Marszałek-Kawa (ed.), Toruń, 2008.

To build a new **model of the Japanese enterprise** a different system of accountability is needed. In the post-war period, firms were controlled by the government ministers and banks. The cross-shareholding mechanism existing within the powerful financial-industrial groups promoted friendly terms between their participants rather than economic responsibility for the corporation. The risk of bankruptcy or hostile takeover actually did not exist and the nature of corporate governance frequently encouraged overinvestment, careless approach to profitability and never-ending support for the profitless products and enterprises running at a loss. However, it has been found recently that the system of traditional ties is changing – the numerous scandals and the resistance to the proliferation of the laws has eroded the power of bureaucracy and, additionally, the commercial banks have lost their substantial power over enterprises that radically reduced their debts originating in the „bubble economy” period.

At the same time, **new priorities for the government role have appeared**, particularly in the field of innovation. The Japanese economic policy traditionally favoured large-sized enterprises and powerful *keiretsu*. As mentioned earlier, in the past the Japanese government actively participated in identifying modern products and technologies and created the R+D cartels responsible for distributing the government funding. At present, the Ministry of Economy, Trade and Industry (METI) has shifted its operational focus and works on providing conditions conducive to the development of an innovative economy, improving the scientific and technical staff's skills (human resources), removing the various barriers impeding economic growth and on withdrawing the protection of the unprofitable sectors.

## 6. Conclusion

As indicated in the main theme of the article, to build her new competitive advantage and spur growth, Japan will have to harness her potential reserves hidden in the components of the socio-economic system by<sup>80</sup>:

- 1.organizing the state universities as the centres where new ideas and new products are created (knowledge and basic research),
- 2.recognizing that the small and medium-sized enterprises are as important for economic progress as the large firms are,
- 3.following an innovation strategy based on rivalry rather than cooperation,

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<sup>80</sup> See M. Porter, H. Takeuchi, M. Sakakibara, Can Japan Compete?, London 2000.



4. increasing the number of the small-sized enterprises through the improvement of their access to the nominal capital in the form of guaranteed bank credits, as well as making it easier for them to raise funds on the stock exchange,
5. initiating clusters that stimulate economic growth, containing both the cooperating and competing organizations, and abandoning the “large-firm obsession”, with the consequent departure from the maximisation of shares in the domestic sales towards the participation in the global competition in selected products.

Summing up, in the past the Japanese government performed the allocation, control and domestic competition **restraining** functions, in line with the orderly growth theory that promotes equal opportunities for particular organizations and branches in the economy. To enterprises and economic segments being especially promising exporters the theory of infant industry protectionism was applied. The existing economic growth determinants call for the radical reworking of the practical goals and their theoretical context. The formation of a competitive business environment, stronger competition among the micro firms and modern understanding of the term ‘innovation’ turn out to be as precious as gold.

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## Streszczenie

### NOWA PRZEWAGA KONKURENCYJNA JAPONII: ARGUMENTY I PROPOZYCJE NA RZECZ PRZEORIENTOWANIA STRUKTUR

*Zgodnie z prognozami rządowymi gospodarka Japonii będzie dźwigać się w górę, chociaż w powolnym tempie. Istnieje bowiem niebezpieczeństwo dalszego pogarszania się sytuacji w sferze zatrudnienia i koniunktury na rynkach zagranicznych. Panuje przekonanie, że nie należy się spodziewać pobudzenia gospodarki wskutek wzrostu eksportu, będącego z kolei efektem ożywienia w skali międzynarodowej, a raczej w wyniku kolejnych pakietów stabilizacyjnych i stopniowego wzrostu popytu wewnętrznego. Te prognozy należy traktować z dużą ostrożnością ze względu na znaczną nieprzewidywalność co do wysokości stopy bezrobocia, obawy odnośnie deflacji oraz prawdopodobieństwo, że recesja światowa może się okazać głębsza, niż się przypuszcza.*

*Jak podaje agencja AFP (Gazeta Wyborcza z 08.12.2009) japońska gospodarka wreszcie ożywiła się w trzecim kwartale bieżącego roku, wychodząc na wielkość dodatnie, spadło też bezrobocie z 5,3% we wrześniu do 5,1% w październiku. Przeważają głosy że ożywienie jest bardzo kruche. Mogą o tym świadczyć wciąż spadające ceny, deflacja, a także rosnący kurs jena (najwyższy od 14 lat w stosunku do dolara: 84 jeny na 1 dolara), co zagraża japońskiemu eksportowi.*