

# The Great Transformation of Japanese Capitalism (1980-2010)

By Sébastien LECHEVALIER



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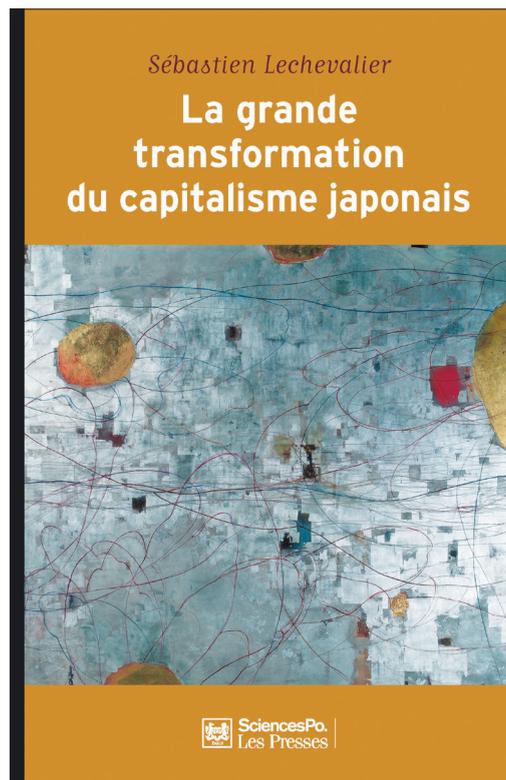
Although Japan attracted much attention from around the world up until the early 1990s, it has almost disappeared from discussions in Europe today. In the 1970s and the 1980s, economists competed in proposing interpretations of the Japanese model of capitalism and explaining its extraordinary performances. Among experts outside Japan, the dominant explanation for the poor performance of the Japanese economy since the early 1990s is maladjustment to a new environment. More precisely, according to most analyses, an absence of reforms in a new environment characterized by globalization and technological progress caused the “decay” of Japan. This is, for example, what Edward J. Lincoln argued in an article published in 2001, “Arthritic Japan: The Slow Pace of Economic Reform.” (JPRI Working Paper No. 81.) This image of Japan is similar to the way Europe in general (and France in particular) was characterized in the 1990s by the expression “eurosclerosis”.

In this article, I adopt a European perspective on the Japanese trajectory since the early 1980s and argue that the previous explanation is misleading. Japanese capitalism has in fact changed substantially as a result of a set of structural reforms. This change is underestimated because it has been gradual. Moreover, it is difficult to perceive this change for those who define the change – at least implicitly – as a convergence towards the Anglo-Saxon type of capitalism. In fact, in the course of this change, Japan has followed its own way, without convergence towards the Anglo-Saxon type of capitalism or towards the European types of capitalism. To understand this change, which is irreversible, we need to take a fresh look at the trajectory of Japanese capitalism since the early 1980s.

## How Did Japan Change? The Role of Neoliberal Transition

To have a fresh look at the trajectory of Japan since the early 1980s, we must adopt an alternative understanding of “change” by focusing more on its institutional and organizational dimensions. First, we have to recognize that gradual but nonetheless substantial change is possible. Second, we have to move away from the previous focus on change that is purely functional, for example a set of reforms resulting in increased efficiency. In the case of Japan, reforms were initiated before the so-called “Lost Decade” (1992-2004) when the economic system was at its peak, not for functional but for political reasons. This highlights the importance of neoliberal policies for the process of institutional change in Japan.

The neoliberal experience in Japan is not limited to the structural reforms



Sébastien Lechevalier, *La grande transformation du capitalisme japonais*, Presses de Science Po, 2011

introduced by two prime ministers, Yasuhiro Nakasone (1982-1987) and Junichiro Koizumi (2001-2006). First, it is important to include the contribution of two other prime ministers, Ryutaro Hashimoto and Keizo Obuchi. Second, the influence of neoliberal policies has been broader and deeper than usually thought, although the chronology has been non-linear.

In order to avoid any ambiguity, it is important to define neoliberalism. My approach has two characteristics. First, I focus on the bureaucratic dimension of neoliberalism rather than the intellectual and political dimensions (see “What is Neoliberalism?” by S. L. Mudge, *Socio-Economic Review* No. 6, 2008). I am interested in the implementation of neoliberal policies. We should not limit our focus to “structural reform” but examine various policies. For example, in the case of Japan, they also concern the structure of families (see H. Takeda, *The Political Economy of Reproduction in Japan*, Routledge, 2005).

Second, I am interested in the implementation and diffusion of neoliberalism in a coordinated environment, and in its power to generate institutional change. Therefore, I adopt the institutional definition proposed by Campbell & Pedersen (*The Rise of Neoliberalism and Institutional Analysis*, Princeton University Press, 2001): “The last two decades of the 20th century (...) have been described as the ones of rising neoliberalism – that is, a time of market deregulation, state decentralization, and reduced state intervention into economic affairs in general. Cast in these terms, neoliberalism has been a political project concerned with institutional changes on a scale not seen since the immediate aftermath of World War II and a project that attempted to transform some of the most basic political and economic settlements of the postwar era, including labor markets accords, industrial relation systems, redistributive tax structures, and social welfare programs.”

How should we characterize neoliberal policies in Japan? They have been progressively introduced, have included deregulation of markets (finance, goods, labor), privatization (e.g., JR, NTT, Japan Post), fiscal reform (though to a lesser extent than in the United States), changes in industrial relations, and downsizing of the public sector, in a context of rising public debt. They touched almost all dimensions of the postwar social compromise. These policies have also shaken the ideological bases of institutions such as firms, families and schools.

Although the content of these reforms is not unique, the process has some peculiarities. It has been strongly non-linear and discontinuous. Reforms have not been implemented quickly within a time frame. On the contrary, they were slowly introduced by waves until the first half of the 2000s. Therefore, it is better to characterize the process as a neoliberal *transition* rather than as a neoliberal *revolution*.

Why did Japan introduce neoliberal policies despite the absence of significant public support and the logic of the comparative advantages residing in non-market mechanisms such as *keiretsu*, long-term subcontracting relations or industrial policy? To put this question — formulated initially by Y. Tiberghien (*Entrepreneurial States: Reforming Corporate Governance in France, Japan, and Korea*, Cornell University Press, 2007) — differently, the issue at stake is to understand why and how neoliberalism was successfully diffused in Japan despite the apparently unfavourable environment of a successfully coordinated capitalism. The debate on this important issue is not over. The explanation that focuses on American pressure seems too simplistic, because domestic actors played an important part as well. For example, domestic players such as large banks and Japanese multinationals have called for financial deregulation, while various groups in Japanese society that would benefit from the reforms also supported them. The idea that some political entrepreneurs like Koizumi initiated the reforms in order to promote their own careers is also worth considering.

CHART 1

## Increasing productivity dispersion in the manufacturing sector



Source: K. Ito & S. Lechevalier (2009), *The Evolution of the Productivity Dispersion of Firms - A Reevaluation of its Determinants in the Case of Japan*, *Review of World Economics*, 145 (3).

### Changing Japan: Firms, Coordination & Social Compromise

Whatever the causes of the neoliberal transition in Japan, I argue that it has substantially changed Japanese capitalism. The change was in directions that its promoters neither desired nor planned. After years of (apparently) minor changes, Japanese capitalism finally achieved its transition by the mid-2000s. This change is now irreversible. Japanese capitalism today is significantly different from the “classical” model of the 1970s. Moreover, although the implicit or explicit aim of neoliberal policies has been to promote a convergence towards the liberal type of capitalism, they have not led to this expected outcome.

In order to assess this point, it is important to consider various levels: the firm level, the coordination level, and the social compromise level.

At the firm level, it is impossible to conclude that the “J model” — defined by relational employment and finance, and by opposition to market-style arrangements — has come to an end. As shown by Aoki, Jackson & Miyajima (*Corporate Governance in Japan. Institutional Change and Organizational Diversity*, Oxford University Press, 2007), it is now one option among others with the emergence of “hybrid” models (different logic for employment and finance spheres). This is symbolic of the increasing heterogeneity of Japanese firms since the mid-1990s. What is striking is not that Japanese firms are diverse in their organization and performance but that this heterogeneity has increased and exists among firms of similar size belonging to the same narrowly defined sector (*Chart 1*). Although the reasons behind this increasing heterogeneity are complex and deserve an analysis that goes beyond the scope of this article, it is worth mentioning the role of deregulation that has created a range of possibilities.

As for coordination forms — a set of non-market institutional arrangements that create complementarities and solidarity among heterogeneous actors — we have observed, in a first step, the decay of most of them including the *keiretsu* structure, long-term

CHART 2

## The re-segmentation of the Japanese economy

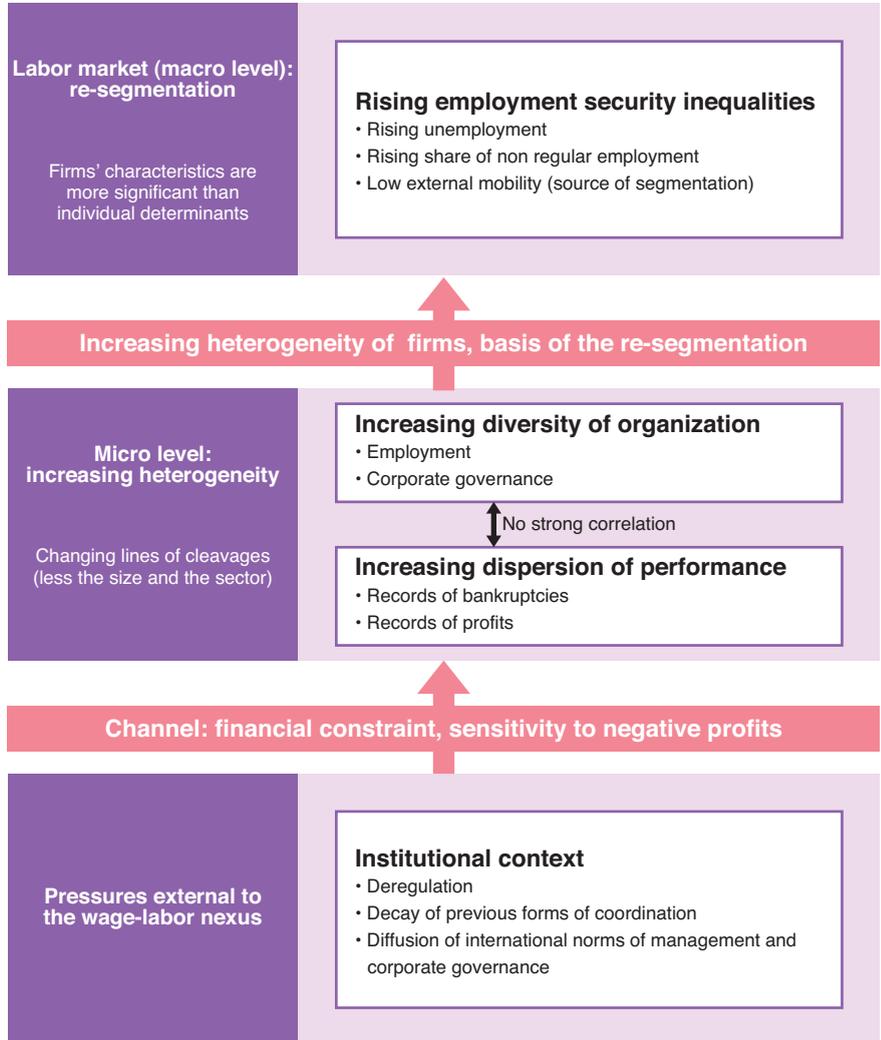
subcontracting, *shunto*, industrial policy, and “bureaupluralism” (representation of various and potentially conflicting interests within an administration). However, in a second step, we observed a revival of these coordination forms that have evolved over time, *shunto* being an exception. For example, fragmentation of production led by Japanese multinationals in Asia has functionally replaced the former type of subcontracting, while a new type of industrial policy called “innovation policy” has emerged with the clear aim of coordination. In this context, it is possible to argue that Japanese capitalism is still coordinated (unlike liberal capitalism in the United Kingdom and the United States) but its forms of coordination have changed.

Another important evolution, which reveals how Japanese capitalism has drastically changed during the last 30 years, is rising inequalities. Although there has been a lively academic debate on the extent and causes of this trend, most recent papers (e.g., R. Kambayashi et al., “Wage Distribution in Japan, 1989-2003”, *Canadian Journal of Economics*, 41 (4), 2008) have shown that rising inequalities are observed within a group (such as the younger generation) and are directly linked to the dynamics of the labor market. Besides the rise of irregular employment, a key factor is the heterogeneity of firms (D. Gatti et al., “Wage and Productivity Differentials in Japan. The Role of Labor Market Mechanisms”, *Global COE Hi-Stat DP Series 127*, Hitotsubashi University, 2010), which has led to a re-segmentation of the Japanese labor market (Chart 2). Rising inequalities reveal a drastic change in the egalitarian postwar social compromise.

In sum, instead of a rise of market-type coordination, there is an increasing heterogeneity of firms, a weakening of previous complementarities, and more generally a decay of institutional compatibilities. These trends suggest that the new Japanese capitalism lacks coherence. These trends, however, are irreversible (S. Lechevalier, *La grande transformation du capitalisme japonais*, Presses de Sciences Po, 2011).

### Lessons for Japan & the Rest of the World

An important lesson from an analysis of the Japanese trajectory over the last 30 years is that there can be many forms of contemporary capitalism. Globalization and technological environment certainly constitute constraints that should be taken into account by policy makers. However, they do not determine everything. Instead of emphasizing only these two constraints,



Source: S. Lechevalier (2011), *La grande transformation du capitalisme japonais*, Presses de Sciences Po.

- reformers should take into account three additional constraints:
- history or “path dependence” that makes any *tabula rasa* strategy impossible;
  - institutional complementarities that define the comparative advantage of a given form of capitalism and make it impossible to change one institution such as the financial market without changing other institutions;
  - the ability of politics to present a goal to society as a whole, beyond any conflict of interests.

If this analysis is correct, it should lead to a recommendation to the Japanese people to develop a more critical view of the idea that only one type of policy is possible. Moreover, the Japanese people need more self-confidence because “arthritic” Japan is a myth. Japan has changed and is still able to change further, if there is an agreement on a desired form of society and the goals to be achieved. **JS**

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Some parts of this article are inspired by his latest book, *La grande transformation du capitalisme japonais* (Presses de Sciences Po, 2011).