

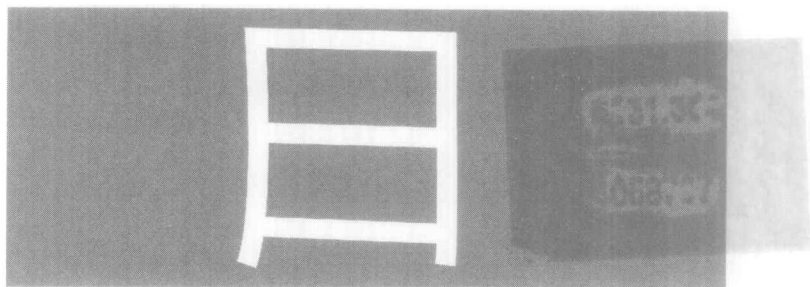
# THE SUN **ALSO** SETS

THE LIMITS TO JAPAN'S  
ECONOMIC POWER

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BILL EMMOTT



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THE SUN  
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THE LIMITS TO JAPAN'S ECONOMIC POWER

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FOR MY MOTHER AND MY LATE FATHER

## P R E F A C E

“Money can’t buy you friends,” wrote the British comedian Spike Milligan, “but it can get you a better class of enemy.” It also brings power, which is why, as Japan has become richer, it has also become more influential in world affairs. As Japan’s wealth has grown, Japanese and Japan-watchers alike have quite naturally begun to wonder when and how Japan will begin to flex its muscles. Will it buy up the world? Will it dominate financial markets? Will it take on more international responsibilities? Will it become a superpower? How long will its strength last? How will wealth change Japan? Will it take over leadership from a declining America? Will it, above all, become a military force once again?

This book is, at its most ambitious, an attempt to answer these questions. It seeks to show where Japan is heading and how it is changing, in economic, financial, social, and political affairs. It is thus not intended as a snapshot of Japan, nor as a static description of how Japan works and why. There are already plenty of books that do that more effectively and with far greater expertise than this author could achieve. Instead, *The Sun Also Sets* is offered as an analysis of an ever-changing subject, an attempt to show the direction in which Japan is moving as well as to measure its speed.

Such an effort is fraught with dangers since it implies, at least in part, an exercise in prediction. As Sam Goldwyn warned, “Never prophesy, especially about the future.” In its humbler moments, however, the book is also an attempt to show how to think about Japanese power. To that end, it seeks to identify those factors that will determine how powerful Japan will become, how long its strength will last, and

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in what sort of circumstances Japan's potential power might be unleashed in military or political form. Then, anyone who agrees with Sidney Webb that "economists are generally right in their predictions but generally a good deal out in their dates," can come up with their own timetable for Japan.

These tasks cannot be achieved by viewing Japan in glorious isolation. National power and influence, whether political or economic, are always relative to those of other countries, not absolute. In plain language, the book's questions must not just be about Japan but rather must also be about the United States and, to a lesser extent, about Europe. Crucially, the book must concern itself with such issues as whether America is a spent force and how its power and influence compare with those of Japan. Some of that is attempted *en passant* in chapters principally concerning Japan, in particular in Part Three. But also the final chapter is almost entirely devoted to the United States.

That chapter is not offered as a rigorous and definitive study of America's past and future, since such a task would require not only a book of its own but also an author more expert on and immersed in matters American than is this writer. Nevertheless, the chapter is offered as an essay on the state of America in the late 1980s, as it appears to an outsider seated in London who is employed to write and think about finance and business and who previously spent several years immersed in matters Japanese. The chapter seeks to place America in the context of Japan's strength, as well as to place Japan in the context of America's.

Like America, this author is now a net debtor, although fortunately in terms of gratitude for help and advice rather than trillions of dollars. At the top of my list of creditors must stand *The Economist*, and in particular Andrew Knight, its editor until 1986, for having given me the chance to learn about Japan as the paper's Tokyo correspondent. Rupert Pennant-Rea, Andrew's successor and an earlier co-author of mine, then generously offered a sabbatical in 1988, without which this book would never have appeared. And Vince McCullough made it possible for me actually to accept that time off by standing in (and eventually succeeding me) as financial editor.

The list of those who helped through interviews, either knowingly for this book or unknowingly during my time as Tokyo correspon-

## PREFACE

dent, is far too long for this space. Thanks are due to all of them. Special thanks must, however, go to Kiichi Kawamura, Toru Nagatsuka, and Junichi Yano of the Foreign Press Center for help in setting up interviews during a lengthy return visit to Tokyo in mid-1988. That visit was also made easier by help from Geoffrey Tudor and Martin Sillwood of Japan Air Lines, for which many thanks. Particularly heavy debts for advice, assistance, and nourishment during that visit are owed to Paul Maidment, Lisa Martineau, Taeko Kawamura, and Akio Mikuni.

Whatever the book's deficiencies, they would undoubtedly have been far worse had not the patient and ever-supportive Gordon Lee read the entire manuscript in several drafts, providing suggestions and criticisms galore, as well as boundless enthusiasm. Chapters were also read by Clive Crook and Steve Reilly, both of whom pointed out errors and were responsible for many improvements. Hiroko Asami, my former assistant at *The Economist* in Tokyo, helped with some of the research and Ritsu Suzuki with some of the trickier interpretation. Some of the ideas in the book were also contained in an essay entitled "The Limits to Japanese Power" that I submitted to the 1988 American Express Bank Review competition held in memory of Robert Marjolin. I am grateful, therefore, to AMEX not only for awarding me the first prize but also for tolerating the fact that my essay was, in effect, an early draft of chapter 11.

To my editors, Jonathan Segal and Ruth Fecych in New York and Nicholas Brealey in London, thanks are due not only for their interest and enthusiasm but also for their ideas in evolving the book's structure and content. Dasha Shenkman, my literary agent, helped to turn the book from a vague and abstract notion into a concrete, publishable project as well as providing constant encouragement. Delightful and secluded cottages in which to write were provided by Charles Ware and Helena Harding, as well as by John and Hilary Andrews. While credit is due to all of these and more, blame for any errors, omissions, or infelicities in the book remain, of course, entirely my own.

Bill Emmott  
London, January 1989

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PART

ONE

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POWER AND PARANOIA

パラノイア



# CHAPTER ONE



## THE JAPANESE CHALLENGE

*Prosperity is the surest breeder of insolence I know.*

—MARK TWAIN

FOUR DECADES AGO, Japan was written off as a contender for political and economic power; two decades ago, it was no more than a voice offstage; now it is a leading player in virtually every arena of international endeavor. Its companies are impossible to ignore, at home or abroad; so, still, are its exports; so, increasingly, is the capital it is sending overseas in truckloads; and so, at last, are beginning to be its politicians and diplomats. The Japanese are no longer coming. They have arrived.

Contrary to what was once a common assumption, Japan's growing influence on the world is by no means limited to strictly economic affairs. The country that for centuries deliberately isolated itself is now reaching out and, one way or another, is affecting everybody's lives. Japanese fashions, for instance, draw whistles in Paris; amid the fads and fancies typical of haute couture, the Japanese have had their moments as trendsetters. Names such as Kenzo, Comme des Garçons, Issey Miyake, and Rei Kawakubo can be seen on clothes or shops in all the world's major capitals. After buying a Japanese outfit, you can have a healthy Japanese lunch to ensure that when you get home you will still be the same size as the garment. New York, Los Angeles, and, increasingly, London are packed with sushi bars and other Japanese

restaurants, and not merely for the tens of thousands of expatriate Japanese who live in those cities.

All over Asia, Japanese department stores are coming to dominate retailing. Japanese banks can be seen everywhere all around the world, on street corners, in financial districts, in league tables, and on "tombstone" advertisements in newspapers and magazines. Japanese honeymooners dominate the Pacific islands. Groups of camera-toting Japanese tourists have taken the place in traveling stereotypes that was once occupied by tartan-trousered Americans. Teenagers in Hong Kong, Seoul, and Singapore listen to Japanese pop music on their Sony Walkmans (or, more likely, on locally made copies). Asian youth looking for the latest in style and popular culture no longer look merely to America but also to Japan.

By the same token, Japan is becoming, superficially at least, more international in character. Tokyo, in particular, has become agreeably cosmopolitan in appearance. There and in other big Japanese cities even the most traditional neighborhood feels incomplete without a French restaurant next to the noodle shop, a European-style bakery opposite the rice merchant. It is hard to eat badly in Tokyo, in whichever cuisine you choose. Ten years ago, that would not have been so, nor would the choice have been terribly wide. But Japan's ever-growing affluence and its taste for the new and exotic (although only mildly spiced, if you please) have lured foods, arts, and styles from everywhere.

Even modern architecture in Tokyo is more imaginative and attractive than much of what appears in London and is on a par with the best new structures in Manhattan, despite the fact that older Tokyo buildings are mostly hideous. Prince Charles would probably agree that, unlike in London, modern architecture is generally improving Tokyo rather than destroying it. Want to attend a Mick Jagger concert, look at impressionist art, or see the latest Hollywood movie? Come to Tokyo.

#### FROM SKEPTICISM TO TERROR

Just as Japan has changed, so has the outside world's attitude to this Asian upstart. Views of Japan have turned rapidly from a sort of skeptical admiration into awe.

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In the not-so-distant past, Japan's economic progress was often described (by some Japanese, as well as by Westerners) as being impressive but surely too fragile to last. One argument along these lines was that Japan's economy is vulnerable because it is dependent on imports for its supply of raw materials. Interrupt that supply, or raise prices sharply, and Japan will be crippled. Another theory held that Japan is like a bicycle: fine when it is moving fast, but when the pedaling stops it will topple over. Most recently, it was assumed that Japan's strength depended crucially on a currency that was artificially undervalued. If market prices were to prevail, ran the argument, Japan would surely be put in its place.

The 1970s and 1980s destroyed, one after another, these notions of Japan's fragility. First, President Richard Nixon abruptly devalued the dollar against the yen. Then the price of oil rose by ten times inside six years. What happens? While the rest of the industrial world suffered in post-oil-shock stagflation, Japan became the world's most efficient user of energy and cut its imports of other raw materials from 3 percent of gross national product (GNP) in the 1960s to 1.6 percent by 1984. It recovered from a severe but brief period of inflation in 1974-75 to resume its lead of the world's growth rankings.

Between February 1985 and February 1988 the value of the yen more than doubled against that of the dollar. For a while, the economy seemed to be slipping into a recession. Even Japanese pundits warned of a coming *endaka fukyo*, or high-yen slump. Yet suddenly Japan's domestic demand boomed and, far from collapsing, the economy grew at its fastest rate in six years. Unemployment rose a bit, but then fell back again. Not even the world stock market crash of October 1987 could derail Japan, even though Westerners had queued up to predict that Japan's financial markets would plunge first and farthest. With this sort of record, it is little wonder that, through many Western eyes, Japan has become akin to an economic Superman, able, apparently, to achieve anything once he has popped into a telephone booth to remove his disguise.

In foreign policy, by contrast, Japan has more often been under- than overestimated. It has long been common to sneer at Japan's low profile and apparent insignificance: meager military spending, a "free ride" on American defense, a mealy-mouthed foreign policy, almost

comically evasive prime ministers. Attitudes have changed since the early 1960s, when France's President Charles de Gaulle referred to a visiting Japanese prime minister as "a transistor salesman," but not by much. There is still, in fact, some truth to the sneer. But compare Japan's behavior in 1988 to that typical even a decade earlier, and things will look rather different.

For instance, anyone would have been called mad who, in the mid-1970s, predicted that a Japanese foreign minister would visit Israel and demand that his hosts withdraw from the West Bank and Gaza; or that a Japanese prime minister would arrive at a World Economic Summit (in Toronto) and announce plans to double Japan's overseas aid within five years as well as proposals to ease the Third World debt problem; or that Japan's defense agency would be buying and installing some of the world's most advanced weapons and radar systems. All of these happened during 1988. Ignore, for the moment, the more common and justifiably unfavorable static comparison of Japan's political profile and foreign policy with those of others. Look instead at the dynamics; the change in Japan's profile begins to appear impressive.

The underestimation of Japan's political position has, nevertheless, done little to calm attitudes to its economy. So remorseless has been Japan's economic rise that other countries now cower before actual and potential Japanese competition in virtually any area that Japanese firms might choose to enter. Think of a business in which Westerners have, so far, remained dominant—aerospace, biotechnology, supercomputers, luxury cars, design, retail financial services, computer software, and many more—and you will find someone, somewhere, who is forecasting a Japanese takeover of that market. Most likely, too, they will be lobbying for protective measures against such an event.

In addition, the awe inspired by Japan is now heavily laden with fear. The Japanese investments and loans that have flowed abroad since 1983 ought, in theory, to lessen such worries, since they spread finance, jobs, wealth, and technology more widely and evenly than does domestic Japanese production. On the contrary, this has prompted recipients to fear even more for the future. Japanese buying power (and actual buying) has grown so rapidly in the past five years that many American and European writers and pundits are wondering aloud what will be

## THE JAPANESE CHALLENGE

the consequences of being owned by Japan. Thanks to its trade and budget deficits, America has become the world's largest net debtor; thanks to its surpluses, Japan has become America's, and the world's, largest net creditor.

If that state of affairs persists for long, it is unlikely to remain happy and harmonious. As John Maynard Keynes wrote in his "Economic Consequences of the Peace" in 1919, "A debtor nation does not love its creditor."

Keynes was then referring to the likely feelings of a defeated Germany toward Great Britain and the United States. Thirty years previously, the same could have been said of America's feelings toward its chief creditor, Great Britain. In a most intelligent and perceptive paper in September 1987, David Hale, chief economist at Kemper Financial Services in Chicago, compared Japan's likely position in 1988 with the position of Britain as the financial bogeyman of American politics during the presidential election of 1896. In the 1880s and 1890s, Britain was far and away America's biggest creditor, with a portfolio of American investments equal to 20 percent of America's GNP (far bigger, proportionately, than Japan's current portfolio). The Democratic party platform in 1896 described the dollar's link to the pound as "a form of financial servitude." Hale cites an influential American monogram of the period, *Coin's Financial School* by William Harvey, that argued that the continuation of present policies would end

in England owning us body and soul. She is making a peaceable conquest of the United States. What she failed to do with shot and shell in the 18th century, she is doing with the gold standard in the 19th century.

It is not hard to find similar words being used for Japan in the late twentieth century. Having failed, it might be said, to beat the United States after Pearl Harbor in 1941, Japan is now making a peaceable conquest. Several books have already made similar assertions, including Marvin Wolf's rather hysterical *The Japanese Conspiracy* (how Japan is plotting to take over Western industry) and Russell Braddon's calmer *The Other Hundred Years War* (a former prisoner



of war about Japan's long-term struggle to get on terms with the West). On present trends, it may be feared, Japan will soon own America body and soul.

### **JAPAN UNLIMITED, AMERICA ENFEEBLED?**

This sense that Japan is buying up the world is beginning to alter expectations about Japan's political importance and role. The country's resilience, economic invincibility, and buying power have become so convincing that it is now common to read and hear forecasts that Japan could ultimately achieve some sort of supremacy in world affairs, despite all its present frailties and reluctance. At first it would merely take more "responsibilities" and share America's burdens. But that is only the beginning. Later it would take more power and would eventually rearm. The view is, in short, that extrapolating from present trends Japan is bound eventually to take over from America as the front-runner for the non-Communist world. Some clairvoyants see Japan taking the lead in partnership with China as a formidable Asian duo; more see Japan taking it alone, since China's economic development remains at such an early and uncertain stage.

In 1985, for instance, Kenjiro Hayashi, an economist at Nomura Research Institute, wrote of "Passing the Torch of World Leadership." In early 1986, Professor Ezra Vogel, a Harvard sociologist and author of a celebrated work in praise of the land of the rising sun, *Japan as Number One*, discussed the possibility of a "Pax Nipponica" in an article in *Foreign Affairs*. Although his conclusion was skeptical, he evidently took the idea seriously enough to examine it. Norman Macrae, then deputy editor of *The Economist*, wrote anonymously in October 1987 of "The Post-Hirohito Century" and about what Japan was going to do with all its money. Every risen economic power, he asserted, seeks eventually to mold its era. And in early 1988 a prominent American fund manager, George Soros, went further by writing, in an afterword to his book *The Alchemy of Finance*, that

The historic significance of the stock market crash lies in the fact that it marks the transfer of economic and financial power from the United States to Japan.