

Japan in crisis: How serious is the problem?

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A recent cover story in the Economist magazine (February 16-22, 2002), "The sadness of Japan," has given a detailed account of the problems the country is currently facing. It has described without mincing words the dismal scenario in Japan, "There is no single solution to Japan's ills: neither a depreciating yen, nor monetary expansion by Bank of Japan, nor fiscal reform, nor nationalisation of the banks, nor privatisation, nor deregulation, nor mass bankruptcies of zombie companies will bring Japan's economy back to productive life. The government needs to do all these over a period of years, in order to reflate demand as well as reinvigorating private enterprise and restoring consumer confidence."

So, how serious is the problem in Japan? As always, the markets are a reliable judge of the state of affairs. During the period 1/1/1999 to 31/12/2001, the Dollar appreciated from Euro 0.8422 to 1.2274 (33.31%) and from Yen 113.33 to 127.42 (12.4%). This is a clear evidence, that the performance of Japan is not all that bad, when compared to the Eurozone.

While there are some macro economic problems that Japan has not been able to resolve satisfactorily, corporate sector reforms are on in full swing. In 2001, more than 19,000 companies went bankrupt. This is a sure sign that reforms are gaining momentum. Many Japanese companies have been cutting flab and rationalising their operations. Nissan's dramatic restructuring and turnaround is of course well known. Corporate giants like Fujitsu, Hitachi and Toshiba have announced job cuts. Many less known Japanese firms have also been declaring lay-offs.

Japan's banking system, though currently in a big mess, is being revamped. From April, 2002, Japanese banks will mark their equity holdings to market. This means losses, which have been conveniently hidden under the carpet for so long, will come to surface. A blanket deposit insurance introduced in 1998 will also be repealed gradually. This will go a long way in minimising the moral hazard problem and improving accountability of banks.

The Japanese economy seems to be gradually evolving from a manufacturing-oriented, high investment economy, into a service-oriented consumer economy. Employment is shifting from large manufacturing companies to small service firms. The proportion of part-time workers is increasing. These are all clear signs that the Japanese corporate sector is prepared to change to become more flexible and nimble. Moreover, Japanese companies like NTT DoCoMo are demonstrating their capabilities in developing innovative Internet technologies.

As Japan restructures, a level playing field is also being created for the smaller companies. A good example is the success of the Uniqlo apparel chain (also known as Fast Retailing). In about three years, the chain has become Japan's most successful retailer. According to Tadashi Yanai, CEO (Fortune, January 14, 2002), "Anyone who looks at our company should not think we are a typical Japanese corporation. I take my inspiration from the US high-tech industry." Many of Yanai's business practices, including generous stock options, a young management team and a lean organization are modelled on Silicon Valley. In fact, Yanai has tried to benchmark his company against the famous retail chain, the Gap. The increasing presence of foreign retail chains like The Gap, Carrefour and Starbucks is a clear indication that the Japan's notoriously complicated distribution system is changing. Domestic and foreign retail chains now do not hesitate to source goods from overseas markets. When the Japan Towel Industrial Association launched a campaign to curb imports of cheap Chinese textiles, Uniqlo was singled out as the major culprit. Yanai responded, "I think Japan must undergo major changes. We are showing Japanese companies what they should look like in the future."

As Peter Tasker, an expert on the Japanese financial markets puts it (The Economist World in 2002), "2002 will be a constructive year for Japan. As usual, the conventional wisdom about the country makes a poor pointer to the future. A learner, tougher and once again dynamic, Japan stands, surprisingly on the threshold." He argues

that the current deflation is the result of cuts in capital spending and a new emphasis on profitability in Japan’s private sector. This combined with a weak and poorly supervised banking system has created a climate of doom. But Tasker feels that this is a temporary phase and a turnaround is only a matter of time.

In short, Japan is slowly but quietly and surely changing. It will take sometime before the transformation is complete. Once that happens, Japan may well emerge a revitalised player, with a leaner, stronger economy. The country might well be approaching the end of the long dark tunnel it has been going through for the past several years. And a resurgent Japan is badly needed to prevent a global economic slowdown.

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