



CSIS-JICC Conference

U.S.-Japan Alliance: A Sustainable Relationship?

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Japan Information & Culture Center

Opening Remarks by His Excellency Shunji Yanai, Ambassador of Japan

I am delighted to have the opportunity to give some opening remarks. Speaking of opening remarks, I had a very bad experience in Moscow during the Cold War time. Even in those days, we had annual consultations between Japan and the Soviet Union. In one of those sessions, my counterpart started talking at nine o'clock and he went on and on. He spoke for three hours without interruption. Finally he looked at his wristwatch and said, 'Gee, it's almost lunchtime.' He went on to say, 'I wish to finish my opening remarks.' But please don't worry, I shall be very brief.

This conference was the brainchild of Prime Minister Keizo Obuchi. When he visited Chicago this April, Prime Minister Obuchi announced his intention to dispatch Japanese intellectual leaders to the United States to bring together American and Japanese experts and the public with the aim of deepening mutual understanding and promoting dialogue. Professor Kanda and Mr. Morimoto form one of these groups. I am hopeful that today's dialogue will not only be thought-provoking for us but that it will make a valuable and fresh contribution to the ongoing public policy debates that are taking place here inside the beltway.

As you may recall, Prime Minister Obuchi and President Clinton agreed that our relationship is in the best shape ever. And, Ambassador Foley also remarked recently that our relationship is flourishing. I too believe that our relationship is on sound footing. But at the same time I think it is important that we do not forget that our alliance has neither been easily attained nor easily maintained. We should not take it for granted. If I may use a metaphor, I liken our relationship to the United States and Japan jointly pushing a cart up a slope to attain ever higher vistas with the scope of this effort serving the national interests of both countries. However, we must be ever vigilant against the cart rolling backward as it surely will when either side of the alliance becomes too complacent. Thanks to the efforts of people from all walks of life in both countries, I am happy to note that the scope of our collaboration continues to expand daily. Indeed, this is the very process envisaged by the U.S.-Japan security treaty. That treaty provides the foundation for our alliance but it also provides clear guidance under which both the United States and Japan mutually commit themselves to work closely to seek to eliminate conflict in their international economic policies and to encourage economic collaboration between them.

Ladies and gentlemen, I arrived here just two weeks ago. This is my very first opportunity to speak to an audience like you here in Washington. It is my intention to do my part to make our alliance one that is truly enduring and steadfast. Over my tenure as ambassador, I look forward to getting to know many of you personally. I would like to thank you all for coming today.

Panel I: “The Future of the U.S.-Japan Alliance: Changing Asian Security Realities”

Satoshi Morimoto, Chief Researcher, Nomura Research Institute, Ltd.

The U.S.-Japan security alliance and the Atlantic alliance are the most successful international relationships in this century and both alliances are still in the process of rehabilitation or revitalization. We have to explore and make efforts to make them more effective and efficient, otherwise both will face a very serious crisis in the future. Especially the U.S.-Japan security alliance, which has not been tested yet or experienced real trials. Today I would like to suggest some thoughts on how to survive in the future.

As all of you know, our government established three pillars of security policy in the mid-1970s including the U.S.-Japan security arrangement, effective defense capability, and diplomatic efforts as a member of the western alliance. However, our security deeply depends on the U.S.-Japan security alliance, which was extremely successful in containing the former Soviet Union in the Far East. In this sense, the U.S.-Japan security arrangement has contributed significantly to the security of the western alliance. You may recall that we have shared the same perception with European allies that the western alliance is indivisible in the context of dealing with INF or SS20 in the political declaration of the Williamsburg summit. Japan modernized its Self-defense Forces to bolster the U.S. military presence in Asia through purchase of highly sophisticated U.S. military equipment, defense cooperation, host nation support, and improving interoperability. I think it was also extremely successful. The good shape of our security relationship has helped compensate the difficulties in our economic relationship.

Now, the Soviet Union has collapsed. We reviewed our security policy to meet the changing security environment, including not only reduction of the Soviet military threat, but also some indications of new destabilizing factors in the region. We have concluded that we don't have to change the three pillars, but in fact the nature of each pillar has changed significantly. We have explored the new rationale of the alliance since the end of the Cold War. We concluded in 1995 that we should strengthen the alliance until a new world order is structured. If you look at Europe, NATO is expanding to the east in order to reinforce its role in the security of the European continent, and the U.S.-Japan alliance will be reinforced through redefinition. The U.S.-Japan security declaration issued in April 1996 was the outcome of the review. Under this declaration, we have set up some issues such as new defense guidelines, reliable use of U.S. bases in Okinawa, and TMD cooperation. Our Diet passed Guideline-related legislation last May. We are encouraging local governments to follow the legislation in order to implement the Guidelines. The government is now drafting an emergency law covering cooperation with U.S. military forces within our territory in an emergency.

As for Okinawa, our government is encouraging the Okinawa government to find an alternative heliport to relocate the U.S. Marine corps from Futenma airfield. As for the TMD, we already began some technical research programs from this fiscal year.

The nature of the U.S.-Japan security alliance in the post Cold War period is changing. The first factor in the change is that the purpose of the alliance has become not simply to meet a common enemy, but to reinforce the common cultural affinity or national values, which both countries share. The second factor is that our security policy is now exploring the broader dimensions including our international security contributions. For example, Japan has sent Self-Defense Forces to the Golan Heights under the legislation for international cooperation, to Cambodia and Mozambique as a part of PKO, and to Zaire for humanitarian relief activities. We intend to send our Air Self-Defense Forces to West Timor for transportation of humanitarian aid. The ruling parties already agreed to relax PKF restrictions, which are suspended by the current legislation. We don't know yet whether this modification of the legislation will be realized in a special session of the Diet or the normal session of the Diet, which begins next January, in order to participate in the UN transition activity in East Timor.

As for Asian Pacific security, we have significantly developed dialogue and cooperation in the Asia Pacific region since the ASEAN Regional Forum (ARF) was established in 1994. But due to the economic crisis in Asia, momentum and the capability of Asian nations to deal with political instability and security problems in the region have been decreasing. With that, it seems to me that the first stage of regional security cooperation in Asia is finishing. Now the second stage is coming up. Most of the countries are currently putting their highest priority on how to overcome the economic crisis, and some countries have recovered more than we expected. South Korea, Singapore, Malaysia, and Thailand have become very confident about managing their economy in recent months. Indonesia and China are different stories, but we expect the dynamism of multilateralism or regional security cooperation and dialogue to emerge in the next century for promotion of preventive diplomacy as well as confidence in the region.

I would like to talk about some security issues in East Asia, which we have to manage through the U.S.-Japan alliance. One is the Korean peninsula. I think the Korean peninsula is in the process of reunification. *The U.S. Commission on the National Security in the 21st Century* report indicates that Korean reunification could be delayed for another 20 years or more. I don't think so. I wouldn't be surprised if something happened on the Korean peninsula next week. We have to think about a security structure in Northeast Asia after the reunification. We don't know what the nature of a unified Korea will be. I have two scenarios for reunification of the Korean peninsula. One is that the North Korea leadership collapses – political leaders will defect, or be killed in a coup. The other is large-scale social confusion or disorder that will cause the complete collapse of North Korea. The most important security issue is that we must encourage unified Korea to join the community of nations, which share the same values as ours.

As for Taiwan, I think that China will never give up its quest to unify with Taiwan. The security of the Taiwan Strait depends on three factors. One is China—which direction China will go and how well Chinese political leaders can manage their relationship with the PLA. The second is domestic politics in Taiwan. The third is the U.S. engagement policy. I am personally afraid that China may take some action against Taiwan at the time of the Taiwanese election next year if candidates provoke China in order to get support from the public. We have the Okinawa Summit next July and China has already expressed serious concerns that Japan might toward support of Taiwan's participation in the summit, although our Prime Minister has no such intention.

The U.S.-Japan alliance is the most significant factor for peace and stability in the region. However, the problem is that this alliance has not been tested yet. We had several crises in the U.S.-Japan alliance just after the Iranian revolution, during the Gulf War and the 1994 North Korean crisis. Future crises in the Korean peninsula and the Taiwan Strait may again test our alliance. In order to prepare for this Japan has to think seriously about constitutional issues. I'm not saying that we have to modify the constitution itself. I think this is a waste of energy and time. I prefer to pass some sort of national security legislation to allow Japan to have the right of collective self-defense, at least in the region, in order to support U.S. activities. Both the Upper and Lower Houses have set up constitution research committees which will produce a conclusion in three to five years, but I think this is a waste of time.

As for the Korean peninsula, we have to expand the U.S.-Japan defense guidelines to include the ROK to promote deterrence against North Korea. The problem is how to deal with North Korean missiles, especially their launching, testing, deployment, and development. We have no legal framework. It seems to me that we should explore a framework for midrange missile arms control talks in Northeast Asia. Before that, we have to make a political decision on TMD procurement and deployment in order to use the TMD card for a deal with North Korea. In addition, we have to encourage North Korea to participate in the ARF and upgrade Northeast Asia cooperation dialogues. We must reinforce both deterrence and dialogue.

China still is the key to security in the next century. We have no objection to that. But we don't know which direction China is moving toward. The *U.S. Commission on National Security in the 21st Century Report* indicates two possibilities for the future prospects of China. The first is that China continues to get rich, but Chinese authoritarianism remains. The second is that China collapses politically and violence erupts. No one knows what China will look like in 25 years. The only thing that seems truly clear is that the status quo cannot persist. I have two scenarios in my mind. One is political and economic collapse, but the survival of a single China, which attains power through a strong military. The second scenario is that China will divide, I don't know into how many. But the most important security agenda is how to encourage China to be a stabilizing factor rather than a destabilizing factor in the Asia Pacific region. We cannot and should not contain China.

My conclusion on the future prospects of the U.S.-Japan security arrangement is that a new world order will be constituted of national values and national interests. History shows that alliances cannot survive forever. However, foreign relations seem to be developed through same values and common interests. In other words, countries that share the same values and interests, react to a conflict for the same political will rather than an alliance. If so, the United States and Japan have to expand the bilateral relationship to multilateral with members that can share similar values and cultural affinities. The U.S. Commission Report indicates that 21st century will be characterized more by the shared willingness than traditional alliances. I absolutely agree. If the United States and Japan can make a loose group, with their willingness as a core of the U.S.-Japan alliance, with such countries as Australia, New Zealand, ASEAN, or a unified Korea after the unification process, I think the U.S.-Japan alliance will be more meaningful in the next century. Japan's role for the peace and stability of the region is to encourage the United States to pay more attention to Asia and engage in Asian business. I believe that the U.S.-Japan alliance will sustain the key role as the lynchpin of U.S. policy and approach to the region.

Michael Green, Olin Fellow, Council on Foreign Relations

In the mid-1980s I was working in the Japanese Diet for a politician named Motoo Shiina who was very active in foreign policy and defense. One of my jobs was to be a *kabanmochi*--to carry papers back and forth between the Diet and Mr. Morimoto in the Foreign Ministry. I am very honored to have this promotion and actually sit next to him. This was about 1987, 1988 and I continued to work in the Diet until 1989. The Cold War was winding down, FSX was troubling the alliance relationship, trade problems were intense, particularly in the wake of the Toshiba incident and semi-conductor fights. I was doing my dissertation on the U.S.-Japan alliance and a lot of my Ph.D. colleagues told me that I was out of my mind and that I should be studying economics or at the very least Japan's economic security policy. But I soldiered on.

Of course predictions of the demise of the U.S.-Japan alliance were, as Mark Twain might have said, somewhat premature. The alliance is actually doing quite well. I think to answer the question in this conference that the U.S.-Japan alliance, looking at it structurally and at the nature of international relations is very sustainable. In the early 1990s there was some doubt, but I think it's becoming clear now that there is a strategic convergence in Japanese and U.S. views of the critical security problems in the world and in the region.

Particularly, as Mr. Morimoto said with regard to China and North Korea, where, if you follow Japanese policy toward these countries, Japan is not moving away from the U.S. view, but in my argument, is moving closer. There is broader support now for the alliance in Japan than at any point in its history. That was evident in things like the March 1997 vote on the extension of U.S. base leases on Okinawa when nearly 80 percent of Diet members in the Lower House voted to support this very controversial legislation in order to sustain the alliance and avoid a crisis. And, Japan's other foreign policy pillars, multilateralism--the United Nations, and integration of Asia--are all in some flux and in some ways are not terribly strong tools for Japan compared to the tool represented by the U.S.-Japan alliance. So I am fairly optimistic at the structural level. And when I hear talk suggesting the alliance could fail in a Korea crisis or the alliance could collapse in a Taiwan crisis, I tend not to think that's the case. I think there could be some big, big problems and some very very late nights for alliance managers in both countries. But, I don't see a scenario where the alliance just completely collapses. Several crises, the failure of the alliance over several events perhaps, but I don't see an absolute plummet in the event of a North Korea, or Taiwan or other crisis.

However, having said that, while there is broad support for the alliance, while structurally there are strong trends for strategic convergence between the United States and Japan, we have what the Japanese might call a '*soron sansei kakuron hantai*,' a general agreement that the alliance is good, broader than ever in both countries, according to public opinion polls, but on the specifics of how you manage the alliance--where you take the alliance, how equal you distribute the burdens and so forth--there are more and more tactical disagreements, which are going to present some very new and very big management challenges. If we mismanage them, we will be much less prepared for whatever crises come in the future.

I had a list of ten of these management problems, but in the interest of time, I've reduced them to nine. Let me go through them briefly. The first management problem for the alliance is the changing Japanese strategic culture, which is becoming out of sync with the U.S. view of Japan. Some call it Japanese nationalism; some call it Japanese aspiration; let's just call it a changing Japanese strategic culture. I think public opinion polls, newspaper and journal articles, and statements by politicians pretty clearly indicate that the Japanese elite and public are taking a

different view of security, of northeast Asia, of China and of Korea, and are ready to step up to the plate and do more in the area of security. Part of this is because of the threats in the region, and part of this is the search for an identity that's been an issue for Japan's foreign policy.

At the popular level this was revealed in the Asahi Shimbun/Harris poll taken about a year ago--I think it was in March--where a large number of Americans said the purpose of the U.S.-Japan alliance is to contain Japan. I think the exact language was "to prevent Japanese remilitarization." What was really striking about this was when you look at the ages, the younger you got in the United States, the more prevalent this view was, which really surprised me. I teach at the School of Advanced International Studies and I thought that younger Americans had a very different view of Japan. But there is at the popular level in the United States, I don't think this is a strongly held view, but a sort of a complacency or an ambivalence that continues from the Cold War and it's completely out of sync with Japanese changing aspirations, particularly among younger Japanese and especially among younger Japanese politicians. But even in the elites of the United States, in the halls of the State Department, Pentagon, and the White House, I think there is at best an ambivalence about Japan playing a larger role, particularly in security. And these two views are becoming out of sync.

The second management problem is how the two countries define the American unipolar moment. In the early 90s in Japanese academic literature there was a fascination with the idea of multipolarity because it appeared that Japan might be one of the poles. The rise of Chinese power and influence has somewhat changed that view. I don't see in Asia or in the world Japan as a challenger of the status quo or of the American unipolar moment. In fact, in many ways Japan is the best ally we have at this unique point where American power is unparalleled. But what the United States should do with that power creates a different set of arguments in the two countries. The congressional position on the United Nations, on CTBT and so forth in my view, is not isolationism. It's a different definition of American primacy and preserving American unipolar power. But it's one that is growing and that is not consistent with the Japanese view of how American power should be used. And this particularly is a problem when it comes to the United Nations and nuclear arms control. The Kosovo case is one case in point where, although the United States and Japan were not at odds, there was subtle body language from the Japanese government expressing dissatisfaction and concern that the UN Security Council was bypassed in the case of Kosovo. The Japanese government sent Madeleine Albright's star student, Yamamoto Ichita, to lecture her about international relations. A really classic vignette.

If this trend continues in the United States, and this is not isolationism in my view, it's a different view of primacy and of how U.S. power should be sustained, it could create some tensions, in the UN and possibly even in the management of nuclear issues. If nuclear arms control is now stalled, I think the United States is going to come under increasing pressure from Japan, particularly from politicians, to do something. And Japan has certain cards it can play. It could insist on no first use policies from the United States and could play with NPT. I don't think these are near-term issues. I don't think that the Japanese government is contemplating these. I think there are rumblings in academia and the Diet that could become more potent if the United States doesn't keep moving forward with arms control.

This brings me to the third challenge that isn't necessarily bad, but actually quite good. That is the growing pluralism in Japanese foreign and security policy. When I worked in the Diet and Morimoto-san was in the Foreign Ministry, very few Japanese were interested in security policy, politicians or the public. There was recently a poll that showed 70 percent of the Japanese public is actively interested or following security policy issues. This is really

surprising to me. Among Diet members, particularly younger ones, it's almost universal that they are interested in security and many are starting to play a role. The changes in the Japanese political system since 1993 mean that the old factions and *zoku*, or policy caucuses, which had a much more disciplined policy-making system for security and foreign policy, now face a little bit less discipline and predictability and more pluralism. Local governments are playing more of a role as we see when U.S. carriers try to visit local ports, and the Guidelines are being resisted by some local assemblies. On the whole this is a good thing. This is civil society and transparency. But in terms of managing the alliance, it makes things much less predictable, much more difficult for a small group of gurus in the two countries to manage the security relationship. Somehow we have to reach out and educate and incorporate this broader constituency.

The fourth challenge or management issue we are going to face, particularly for the United States, is how to deal with Japan as it becomes a more efficient ally. Morimoto-san mentioned the passage of the Defense Guidelines in the next Diet session, and maybe in the one after that, '*yuji hosei*,' crisis management legislation, will pass. I suspect that in a few years collective defense will be recognized. When I was in the Diet in the 80s, it took considerable U.S. pressure to have any forward movement in Japanese defense policy. You don't need very much U.S. pressure now as there is a momentum on its own. The Japanese side recognizes the need for these things and this consensus is growing. Where you had a significant step forward in defense policy every five or six years in the 70s and 80s, now it seems every five or six months a significant new stage is reached, whether it's the Defense Guidelines or decisions about the use of force with North Korean ships or about collective defense in the Constitution.

This is what the United States has wanted for decades—a more efficient ally. Now I think within some parts of the United States, the fact that this is moving on its own and not because of U.S. pressure, is causing some concern. I think that there is ambivalence about Japan becoming a more efficient ally precisely because, and this is unavoidable, a more efficient ally potentially is a more independent ally. Crisis management and centralization of authority in a crisis are going to make Japan potentially a more independent actor in crises, but also a much more efficient and faster acting ally of the United States. The Self-Defense Forces, which for years had problems with “jointness” and interoperability (they couldn't fight or train together), have begun training together. This is a long overdue development, but one which the U.S. side is not fully sure how to judge. I think that a more efficient ally is a good ally and the U.S. ambivalence or concern is misplaced, but it does point to an area where we have to have richer dialogue about how the two countries manage crises in the future. Again, this is a trend that the United States has been pressing Japan on for some time, so it's long overdue.

The fifth, and in some contradiction to this, is that Japan is going to come under increasing pressure to have a more joint and combined crisis management, decision making, and security policy making structure with the United States. Sometimes people forget that, unlike NATO and the U.S.-ROK alliance, there is no joint and combined command structure with Japan. It is two separate systems that interact primarily through policymakers and political structures such as the SSC. This is a much more political and policy managed alliance than the U.S.-ROK alliance, NATO, or more traditional military alliances. But, with the introduction of Theater Missile Defense and more high-tech information systems in the United States, and with Japan playing more of a role in the Guidelines, I think there will be pressure on Japan to have something close to a joint and combined command with the United States. When missiles fly, you have a minute or two to fire off missile defenses and you have to make sure that U.S. and Japanese missile defenses are not duplicating each other, which is wasteful if you have incoming

missiles, or shooting down each others planes. When you have to have this kind of real time response and interoperability, it places a lot of pressure on a system that politically, from a Japanese perspective, has been designed to keep Japan from being trapped in U.S. security policy.

The sixth problem, or challenge, is going to be that in spite of Japan's changing strategic culture and changing views of security policy, in many ways the rhetoric is ahead of the reality. In this last Diet session, there have been unprecedented debates about whether Japan can preemptively use force in the case of a missile threat, whether or not Japan could undertake certain missions, and whether or not it could fire the next time on North Korean ships and sink them.

Viewed from China, this is revolutionary change and it's only a matter of days before the Kanto army is reestablished and we're back in the 1930s. But the rhetoric, especially the politician's rhetoric, is way ahead of the political and operational reality in Japan. In some ways it's happening because taboos have fallen and the old left has fallen, but it is a real contrast, for example, to East Timor. Now there are a lot of voices in Japan saying slow down, we're not ready to take on this risk and put the Constitution at risk. So there continues to be a risk aversion in the Japanese body politic that is out of sync with some of the rhetoric. That could cause some real problems because I think many in the United States would like to see a more pro-active Japanese role in East Timor and expected it, given all of the rhetoric coming out of the Diet this past year. Expectations, if they are not met by implementation, are going to lead many in the U.S. to dismiss Japan's evolving view of strategy.

Mr. Morimoto has articulated the challenges we face. In terms of bilateral policy coordination, I think we are better off than we were five or six years ago. Throughout the Cold War the Japanese government tried very hard not to be entrapped in U.S. China policy, not to get caught up in U.S. confrontation with the mainland. After 1972, the Japanese side rushed in to normalize relations with China and tried to play a bridging role between Beijing and Washington. Some in Japan, Kato Koichi being the most prominent, would still like to play this sort of trilateral bridging role. I think the prevailing view in the Japanese political body is very suspicious and nervous about China and not that different from the prevailing view in the United States. Primarily because Japan is so close and has such different history of relations with China and has so many limitations about what it can do about China. In terms of concern about which way China might go in the future, there is probably a convergence and not a divergence in American and Japanese views. Having said that, there is, as far as I can tell, not a real convergence in terms of coordinating those policies or views. Certainly, we don't want to contain China as Mr. Morimoto said, and it is very difficult to structure the alliance to deal with China without making it look like we're containing China. But compared with the dialogue and coordination that took place between the United States and Japan on the Soviet Union in the late 1980s there's a real paucity of interchange on China policy.

And that doesn't have to do only with the darker sides of dealing with the Chinese security problem, it has to do with WTO and policies for integrating, opening, and engaging China, as well. I've pondered why this is the case and Professor Reinhart Drifter, who is doing a major project on this, and I think there are several reasons. One is that the Japanese side is still reluctant to give up that bridging role between the United States and China. Given limited tools, Japan has to deal with the Chinese reluctance to be trapped in U.S. China policy. That is somewhat understandable because U.S. China policy is fickle, unpredictable, and inconsistent.

The Chinese, when I was in Beijing, were arguing that Japan is becoming more pro-Taiwan than the United States. This was think tanks mostly, but they pointed to several things: the Japanese government didn't issue a "three-no" statement like the U.S. and the Japanese government after Lee Tenghui's "state-to-state" announcement in July didn't do what the United States did, which was to pressure publicly Lee Tenghui. All Japan did was, according to the Chinese, restate their one-China policy. They didn't do what the United States, the United Kingdom and other countries did in the UN, which was for the first time to come out against movements for Taiwanese membership. Every year there's this pro-forum introduction of a proposal by some countries Taiwan has bought for Taiwanese membership, and the United States usually sits passively and doesn't object. This year for the first time the United States came out in opposition. The Chinese are tallying these things and saying Japan is doing none of this to. When I was in Tokyo, someone in the Foreign Ministry, said 'look, our Taiwan policy never changed, it is the U.S.-Taiwan policy that keeps changing.' I think sentimentally and politically, the Chinese are right. Japan is drifting in a more pro-Taiwan direction. But operationally, there isn't much of a change. There is no consensus to put Taiwan in the Guidelines, for example. This is a potential management problem because, if the Taiwan Security Enhancement act passes or if the United States were to move toward a more obvious defense relationship with Taiwan, in spite of growing pro-Taiwan sentiments in Japan, I don't think the Japanese would be willing to follow that course. Certainly when it comes to Taiwanese independence, there is an awful lot more hesitation in Tokyo than in Washington. So, although there is a convergence of views on China, we are not coordinating our policies or managing these problems as well as we might.

After the North Korean *Taepodong* missile launch in August 1998, North Korea loomed as one of the big management nightmares in U.S.-Japan relations because the Japanese prevailing view was that the U.S. response to the *Taepodong* launch was tepid and not really looking out for legitimate Japanese security interests. One reason the controversy over the satellite became so contentious was because it reflected some mistrust between the two countries that came out of this somewhat divergent response to the *Taepodong* missile launch. Today, however, after the Perry Review and the establishment of the trilateral mechanism with South Korea for coordinating policy toward the North, I think the Korea issue is not such a big problem. In the Guidelines process, it's pretty clear that the threat from North Korea legitimize U.S. and Japanese defense planning. Diplomatically, the Perry Process has established a very good working relationship trilaterally.

I was in South Korea with the Council on Foreign Relations several times these past few years and met with President Kim Dae Jung three of these times. The first time and the third time were interesting contrasts because when we asked him questions about North Korea, the first time he always said "I will do this, we will do this, or we will consult with the U.S. on this." By the third time in June, almost every question he answered with, "consulting with Japan and the United States, we would ...". So it has really entered the Korean psyche that Japan is an active and positive player on the peninsula, and this trilateral coordination is going quite well.

The problem is going to be, as Mr. Morimoto said, the collapse of stability in the North which could come tomorrow or in twenty years. As we saw in *Taepodong*, which was a fairly finite episode compared to what would happen in the event North Korea starts unwinding, if the United States doesn't act to address Japanese security interests, there's going to be some tension. If Japan doesn't coordinate with the United States fully and, as in the case of *Taepodong*, suspends funding for KEDO, there's going to be suspicion on the U.S. side. But that was just one finite episode. It had a happy ending because of the Perry Review, but I think that in

August, September, and into October of 1998 there was a lot of tension on this issue. You can imagine what would happen if North Korea starts to go belly up. This is a difficult problem, and I think that we need to start anticipating and working on it ahead of time. Trilateral coordination with the South Koreans is absolutely critical. There are two problems. One is that you can't engage North Korea when it's obvious that you're planning for their collapse. The other problem is that the Chinese view of trilateral coordination is that it's aimed at containing China.

Finally, bases and host nation support--a big challenge. The Special Measures Agreement, the five year agreement that covers funding for the bases, is going to be negotiated again soon. I think there will be a lot of pressure for the U.S. side to take a symbolic decrease in funding. This pressure will come from the politicians and will intensify if the Okinawa G-8 summit is not a success. I suspect that the United States could do with less. But, there is a certain amount of bureaucratic inertia on both sides that gets in the way of this if you could let Japan pay for upgrades more and if the United States could do with fewer new facilities. There are ways to buy more with less if we have a more creative and flexible accounting system.

I also think that over the long term there's obviously going to be pressure on U.S. bases. The majority of Japanese politicians and public opinion polls say they expect bases to be reduced over time. I think that expectation should be met, but not at the expense of stability and not at the expense of operational needs. Therefore, I would argue against cutting the U.S. Marines in Okinawa in the near future. But we should be looking at creative ways to integrate our forces with the Self-Defense Forces. There's a lot of attention to civil-military dual use. The Koreans, for example, have a lot of harbors that are civil-military dual use. I think in Japan that's going to be harder, the more I think about it. The U.S. military will find it very hard to get the access they need if it's a dual use base with civilians until a crisis, because the Japanese side is going to resist defining something as a crisis if it gets in the way of normal civilian use. So the real opportunity is in the integration of Self-Defense Forces in U.S. bases which could allow us to reduce our footprint.

In conclusion, the way we may be able to get at all of this is to rethink or to have a sort of bottom view of the division of roles and missions, which was how we split up what the U.S. and Japanese forces would do in the 1980s. I don't think those divisions of roles and missions should be changed. Basically, for those of you unfamiliar with this, the metaphor is that the United States is the spear and Japan is the shield—the United States does offensive missions and power projections, Japan does defensive. That still basically makes sense. But it's worth reviewing in the context of peacekeeping and new missions.

It's especially worth doing on the diplomatic side. The United States could be giving Japan much more of a lead much more running room on certain diplomatic issues. I won't go into detail now, but it seems to me that the Japanese proposal for an Asian monetary fund had many flaws. But it also had much merit, including a check for fifty billion dollars. The U.S. side should have, instead of shooting it down, worked quietly behind the scenes to make it a Japanese initiative that fit U.S. and IMF objectives, which was very doable. In fact, the Miyazawa Plan, which it became, was precisely that. We lost valuable time because we were suspicious of Japan's motives.

On other diplomatic things, six party talks, which Mr. Morimoto mentioned, Japan's position is better than the United States to push those if we support Japan. There are certain areas where, diplomatically, we should think about division of roles and missions, not an ATM machine where we push a button and get Japanese cash for U.S. shopping but where we actually encourage Japan to take a lead in certain areas. That's where we were heading in the late 80s

and early 90s when we in the United States were sure Japan was going to be an economic superpower. There's no less of a need for it now that Japan's economy is restructuring and it's the kind of thing that I hope a new administration would look at. Thank you.

Q & A

Q: (To Green) How seriously do you think we should take this changing strategic culture on Japan's side and where is it going to materialize in terms of forming a specific culture? What should both countries do? Should we do it again with the Nye Initiative or what?

GREEN: I would recast your question a little bit. I wouldn't say that Japan is out of sync with U.S. expectations, I would say that the United States is out of sync with the trends in Japan which are a mix of realism, a certain anxiety about China and about the future of the Japanese economy, frustration with the United States and therefore some level of nationalism is always an element here. This is, for the most part, a positive trend where a broader percentage of the public and especially younger Diet members, are eager to play a larger role. Among some of the older politicians there is an old-fashioned view of the U.S.-Japan alliance and much of this new role is defined in terms of not the U.S.-Japan alliance, but a more independent Japan. I think that the younger politicians have a different view, you might call it a cosmopolitan view, which is supportive of the U.S.-Japan alliance but aiming to play a more valued and equal role; not only do things that are important for the U.S.-Japan alliance, like the defense guidelines, but also to look out for Japanese security.

This is a real opportunity for the United States. If these aspirations are encouraged, I think that the Japanese people will support a much more activist foreign policy. If they are discouraged, I think the Japanese public might begin to turn against internationalism in the same way some in the United States and Europe have. There are now Diet resolutions to cut dues for the United Nations, for example, that don't go very far, but they're new. It's in the U.S. interest that Japan has idealism about the UN and an activism about multilateral policy. There is a danger that if the United States keeps knocking down the little heads when they pop up, that the idealism of the Japanese public can turn toward a more selfish view of international relations which would not be in the U.S. interest. A little bit less sentimentality or idealism about international relations is good if it's unrealistic. If we don't encourage Japan to play a larger diplomatic role, it can cause an inward-looking trend. I don't think that the United States alone has the key to the future of Japanese foreign policy. Because the U.S.-Japan alliance is such a central part of Japanese diplomacy, however, the United States really does have an important role. The other important role obviously is for Japanese political leadership.

Q: About U.S. policy toward North Korea. Since 1994 when the Framework Agreement was reached, the United States has taken a very concessionary policy toward North Korea when you compare it to other nuclear capable or near-nuclear capable countries like India, Pakistan, Iran or Iraq. Why?

Based upon the U.S. behavior, I am afraid that the North Korean leadership has been convinced that the best way for North Korea--a small, non-oil producing, non-Islamic little known country—to attract attention and to get concessions from the United States will be to have a nuclear missile capability. The moment the United States loses its strategic interest in North

Korea, the United States may withdraw all kinds of concessions and aid like it did to Pakistan after the Soviet withdrawal from Afghanistan. What is your opinion?

GREEN: The pattern you describe is a fair criticism. North Korea doesn't manufacture much—mushrooms and tension. They use that tension very effectively to get concessions from the United States and the outside world. That is a fair criticism. However, the question I would ask back is what better option the United States has.

North Korea is different from Iraq and India. It has the ability to do immense damage to South Korea. Eleven thousand artillery tubes could devastate Seoul. But if the peninsula becomes in any way violent, it could quickly lead to tens or hundreds of thousands of casualties. North Korea is also isolated from the international system, so there is very little to take away to punish them. So the merits of the Perry approach are that first, it creates some dialogue, which helps to mitigate against an unraveling of the situation. Second, you give something to the North Koreans, not a lot, the lifting of sanctions and food aid, rather small potatoes. In the case of food aid, literally potato seeds. In the case of sanctions, very few U.S. businesses are going to rush in now and establish Food Lions in Pyongyang, but it's symbolic and it opens up dialogue.

But you have something to take away, and there are two things about North Korea we know, I think, in retrospect. One is they respond to threats, and the second is they respond when you threaten to take away something that they've gotten used to. So we have several things now that they've gotten used to--KEDO, food aid and other things. And over the long term that offers some prospect that we might gradually increase interaction and decrease tension. Having said that, if I had to bet, I would say that the odds are that North Korea will collapse violently, not that this would lead to peaceful unification. But, I still think it's still worth doing. Finally, it's worth doing because that's South Korean policy and it is after all their country and no matter what happens in the North, the number one priority for the U.S. has to be a solid security relationship with South Korea and of course with Japan.

MORIMOTO: If I think about the U.S. approach toward North Korea compared with U.S. approach to other countries, there are at least three factors to take into consideration. One is that, for the first Clinton administration, North Korea's attempt to withdraw from the NPT had a very serious implication for non-nuclear proliferation policy because North Korea was already a member of the NPT, although India and Pakistan were not. So I think the U.S. government put the highest priority on non-nuclear proliferation policy to deal with North Korea at that time. But, it seems to me that the U.S. lost some enthusiasm under the second Clinton administration, unfortunately.

The second is that the North Korea leadership is very "unprecedented," very "unmanageable." In another words, U.S. cannot manage North Korea leadership and also we don't know how the North Korea political leadership may manage nuclear weapons and systems or some sort of mass destruction weapon system. In any case, I think the political leadership of North Korea has a very unpredictable capability. I think this is another concern.

Third, the U.S. has a military presence in the Korean peninsula. I think this is quite different with another region or area.

Q: (To Morimoto) It seems to me that Theater Missile Defense and Ballistic Missile Defense could pose one of the problems that would be a true crisis not only for the alliance but in particular for Japan. It's unlikely to be very effective and is certainly easy to overcome because

as you pointed out, it is ballistic missile defense and it does not deal with cruise missiles which could take out guidance radar, early warning radar, interceptors, and so forth. The problem hasn't been solved just like ballistic missile problem is still basically unresolved. But it seems to me that it continues to put Japan in a very difficult regional spot, especially if deployment is pursued. Could you comment on the possibility of Theater Ballistic Missile Defense and what it might create in the way of problems for Japan?

MORIMOTO: First of all, both governments began a joint technical research project on TMD at the beginning of this fiscal year. I don't know how long it will take, maybe a several years. During that time, I strongly expect our government to make a final decision on the procurement and deployment of the TMD system. I don't know which exact system will be under the TMD project. But in a political sense, procurement and deployment of TMD is a true testament for the alliance.

On the other hand, we have some problems to overcome for the procurement as we have to sort out some legal restraints on TMD issues. We also have at least three or four criteria to make a final decision, including cost-effectiveness. Which direction, not only from China and North Korea but also Russia, the new serious threat is coming from and how to persuade ordinary people, that is the first criteria. The second is how many we need. The cost is a very crucial political issue. The third is how much challenge we can meet, even if we equip with TMD in the future. Anyway, China is seriously concerned about our TMD system. I think China strongly worries that if Japan is successful in deploying the TMD, then Taiwan may acquire. That means that U.S. satellite and Japan/Taiwan TMD defense system will be associated to deter Chinese medium range ballistic missiles in the future. China seems to be already applying a strong pressure to Japan on TMD issues. Maybe China intends to acquire cruise missiles. But as you said, we cannot meet the cruise missile threat through TMD.

We have to make a final decision on BMD in the foreseeable future. But we have to overcome some obstacle in a legal, political, economical and technical sense as well. It depends on security environment in Northeast Asia. Whether we can persuade ordinary people to accept the TMD in the future is also very important factor to think about.

Q: Pressures have been increasing in Japan to reduce host nation support for the United States. What would constitute a symbolic cut and what would be the reaction be in the Congress?

GREEN: I actually don't have a number in mind. I think an increase would not be a symbolic cut. I'm not an expert on accounting, I've tried to figure it out and it's complex. But as I understand that there are facility improvement budgets and new facilities budgets. And it's very hard to move from one to the next. When you start getting into facility upgrades you get into the operational side and it becomes a little bit mushier. But that side of the budget, in other words, improvements to existing facilities could be increased and then new facilities could be decreased and the overall amount would be somewhat less. I don't know what the percentage would be.

I do know from talking to Japanese politicians that there is a pretty universal view on the political side in Japan that there should be some decrease. Usually this game starts with the Finance Ministry saying, 'We're going to give you 10 percent less,' then the U.S. says we need 10 percent more, and then we come in somewhere around the amount. That's how budget bureaucratic politics in Japan are usually played. But the danger of getting into that tit-for-tat is

that we might lose sight of more creative solutions to revamp. They're creative but they're tough because there are bureaucratic interests—labor unions in Japan, and a lot of people who have a stake in the way the system works now—and it would mean reapportioning some power among ministries even. But I think it's worth trying proactively before we get to the end of this macho game about increases or decreases.

In terms of the congressional reaction, my answer would be that it depends on what the Marine Corps wants the congressional reaction to be. My father was a Marine, and so was my grandfather, so I know of what I speak. I don't see the Congress watching this with an eagle eye right now. I don't think that the members of Foreign Affairs or Defense or Appropriations Committees are especially focused on this and if the U.S. military came in and said, 'This works for us,' then it wouldn't be a problem. The problem would be if we come down to the wire and there's a cut, and then quietly or not so quietly the uniform military makes it clear that this has an operational effect, then there would definitely be a response. One more reason I think to start trying to put things together early.

COMMENT: I am the Defense Attache at the Embassy of Japan, and would like to make a small footnote to the question raised on Ballistic Missile Defense. What we have done is that the government of Japan last December decided to go ahead with the research phase of the naval theater-wide, which is upper tier defense on the sea. This is a very limited decision in terms of phases; we have a research phase, development phase, and deployment phase. What we have decided is to research the naval upper tier. In terms of the system, the government of Japan's decision is just on one of the interceptors. We have not come up with the whole picture of missile defense for Japan. Also, since 1994 we have been working quite hard on how our air defense system should be, not only ballistic missile defense, but also cruise missile and the conventional air defense. Before we came up with this decision to research TMD with the naval upper tier, we have covered all the three threats, conventional aircraft, cruise missile aircraft, and ballistic missiles. The whole picture has to be drawn in the next several years.

Q: What was your tenth point? How do you characterize new nationalism and how does it play on the alliance?

GREEN: The tenth one was nuclear by the way, and I tried to sort of fold it in without getting into detail.

When Ishihara Shintaro won the Tokyo governors election, the exit polls showed that only around 15 percent or less that voted for him agreed with his ideology, but over 50 percent voted for him because of his *ketsudanryoku*, or *jitsugenryoku*, his ability to get things done. I think that is a useful division of numbers. I would say the Japanese view on UN, U.S. and China and all these other things, probably about 10-15 percent nationalism and 50 or 60 percent, is ready for a new approach, where Japan, as I suggested earlier, is given weight and responsibility and a voice comparable with its economic power. This is not very scientific, but I have a feeling that the trend certainly in U.S. foreign policy and worldview of Japan, rose with the Nikkei. There was more and more understanding that Japan should play a larger role. When the Nikkei started to collapse, so did the worldview and even the U.S. view that Japan should play an increasing world role. But in Japan it didn't stop, it kept going. That's where much of this frustration comes from. As I said, it's a mix of frustration and some anxiety about the future of Japan's identity vis-a-vis Asia where China is on a roll, and North Korean missiles are flying. A

continuation of this trend that really took off in the 1980s that Japan should play a larger. Opinion polls still show very high support for Japan becoming a permanent member of the UN. So the public is still ready to keep going where the trend lines were, and that perhaps is where it comes from.

MORIMOTO: Japan has had no systematic education on national security for half a century. For example we have no national security courses even in university, especially public universities. I started a security class at Keio University five years ago. Almost 1600 people take this course every year. Unfortunately I could not manage, and I terminated my undergraduate course at Keio and opened up another in Keio's graduate school and at Chuo University. At Keio University one very junior associate professor began a national security class following me. As there is no systematic national security education in Japan, people are very flexible in accepting one. On the other hand Nishimura sensei resigned because of his very careless remarks on the nuclear issue.

I think nuclear weapons are extreme weapons. But Japanese people regard nuclear weapons in a context of morals and ethics rather than international power politics. So, even if Nishimura or other people wish to discuss the nuclear arms, military, or defense issue in a context of political science, ordinary people, especially elderly people, cannot deal with such issues that are regarded as "immoral." On the contrary, young people tend not to have a taboo or allergy toward discussing military issues. For example I joined "Asamade TV," an all night debate program, three times this year. Almost 4.5 or 5.5 percent of the people were watching the program. 1 percent is six hundred thousand people, so almost three million young people were watching TV. Participants received opinions by fax from all over the country. The number one opinion was 'We should be militarily built up.' This is not nationalism. I think young people are very frank in discussing military issues.

This big gap between older and young Japanese is making it quite difficult to encourage the people to understand what national security is. American people are frustrated because Japanese bureaucracy is very slow. On the other hand, Asian people are frustrated as they think Japanese move too fast. Currently, Japan is undergoing many reforms: economic reform, financial reform, educational reform, and bureaucratic reform, but we have no national security reform. I think the constitution issue will be a top priority next year. Already, Hatoyama raised the issue, not as the head of the Democratic Party, but to encourage the people to discuss the issue. Otherwise, we cannot make a true reform, not only security but also for the future direction of the country. This is a key factor to think about.

Q: Dr. Green mentioned that one of the problems is that you might have only 30 seconds to a minute to make a decision and today, it might take six hours to a day to make that same type of decision. This slow reaction seems somewhat cultural. At one time this was okay, but under a Missile threat from North Korea or China, can this process change before a catastrophic event takes place? If so, how would you go about changing that so the commander on the ship has the ability to react quickly rather than having to get permission to engage?

GREEN: The problem culturally or constitutionally is the issue of the right of collective self-defense, whether or not Japan has the right to use force against a third country in defense of its ally, the United States, which is different from exclusively defensive defense, where Japan

only has the right to use force against an attack on itself. That little technicality I think is getting in the way of TMD.

There are two pieces to collective defense. One piece is part of Article 9, one of the pillars of pacifism. But I also think it's one of the pillars against being entrapped by the United States. It has been a useful way for the Japanese side to avoid being too integrated. It's going to have to be dealt with to move forward. I have my own solution. There are several interpretations of what constitutes collective defense. One of them is the so-called '*buryoku koshi no ittaika*,' the idea that if you are involved in the use of force by the United States, it is not in strict self defense, but collective defense. And that particular branch of this debate is what really gets in the way of missile defense. For example, you have to have the ability to cue off U.S. intelligence or to provide information to the U.S. when you have only 30 seconds or a minute and a half because you don't want all the U.S. or all the Japanese shooting at the time incoming missile while the next one gets by. So, my elegant solution to that problem is to deal with this question of '*buryoku koshi no ittaika*,' the idea that Japan cannot get involved in U.S. use of force, and make exceptions for TMD. In other words, you can sort of nibble away at this. And I think there is support in Japan to do that. I don't know if that was clear.

The other thing is that TMD moved forward primarily as a technology issue in the early 1990s, driven by the acquisitions part of the Pentagon; then the policy side got involved. But for the most part, the driver in bilateral dialogue on TMD has been technology cooperation, exchange and development issues. The policy side has lagged behind on the political and strategic implications. What also has lagged behind is what you might call the "interoperability side," how we would actually use these things in a real shooting situation. There are reasons for that. One is, the most interested parties in the U.S. were the ones who wanted access to Japanese technology and do research. We are still, of course, in the research and development stage here. So those guys have most of the momentum. And I think on the Japanese side, especially in industry, interoperability, the ability to operate together with the United States, is a 'Trojan horse' for 'buy American.' In fact I've heard the Japanese industrialists working on TMD say, 'When you say interoperability, we hear "buy USA, buy American."' So those are two obstacles that have to be overcome and what's long overdue is a real dialogue on how these things will work. Such a dialogue will help propel forward solutions to the problems in your question.

Q: Mr. Morimoto talked about the importance of cultural affinities for a sustainable relationship between U.S. and Japan. Would you expand on this subject and how we can promote better cultural affinity between the two countries?

MORIMOTO: It's a very difficult and hypothetical question. Political scientists in the post World War have been seeking the basic theory or principle for a new world order. Although we have the X article in the Cold War period, many people are trying to challenge that. Especially Samuel Huntington's *Clash of Civilizations* is one of the challenges which many people paid attention to. But unfortunately, this did not necessarily define the post-X article period. It seems to me that cultural affinity and values are the key factors for a new world order. The problem is that even if we discuss human rights, democracy, freedom, or market economy, each country or person has a different definition. I think there is sometimes a misinterpretation of NATO operations in Kosovo, East Timor activities and also operations to Somalia and Bosnia. I think we have to discuss frankly how to interpret a definition of cultural affinity or values in

order to sustain the peace and stability of not only the international community but also of the region. This is one of the future agenda items for both countries.

“U.S.-Japan Economic Relations: Implications of the ‘Big Bang’”

Hideki Kanda, Faculty of Law, The University of Tokyo

I'd like to describe four things and make one inquiry. The first two things are about financial sector reform and deregulation, Japan's "Big Bang," and the second is cleanup of the banking crisis. Then I will talk about their implications for the financial sector and the Japanese economy in general and the legal system a little bit. The two other issues are the economic outlook in general and the U.S.-Japan economic relationship. Finally I will make one inquiry.

In today's Japan there are two things taking place simultaneously: the Big Bang program and cleaning up of the banking mess. Former Prime Minister Hashimoto Ryutaro initiated the Big Bang program in 1996. It is a five-year program and should be completed by 2001. The Big Bang is a drastic reform of the financial sector and has two characteristics different from past reforms in Japan. Number one the scope is extensive and drastic, at least by Japanese standards. The second is that the timetable is very specific. With these two characteristics the contents of the financial Big Bang are very extensive. Let me give an example. Foreign exchange control is gone, generally speaking, and therefore, the currency exchange business is not regulated any longer. It used to be that you had to go to a bank to buy U.S. dollars. Now you can purchase U.S. dollars anywhere—at the counter of Japan Airlines or at some convenience stores like Seven-Eleven. In other words, the currency exchange business is no longer a licensed business. Similarly, any Japanese can have a deposit outside Japan without permission from the government. Also, from October, the so-called "fixed commission system of security brokerage" was eliminated. There is already a major competition in this brokerage sector.

Now, what is the Big Bang's impact on the economy? I will focus on three things. First, Japan may move from a bank-centered system to a capital market-centered system. That means that banks will be less important in the Japanese financial sector. I am not saying banks are becoming unimportant, but that traditional banking service will become unimportant. Traditional banking service means deposit taking and commercial lending, but from now on the capital market activities will become more important. The very purpose of Big Bang is to encourage broader capital markets.

Second, Japan may move from a "stability-based" society to "adaptability-based" society. One of Japan's highest priorities was stability, especially employment stability. Japan is very poor in adapting to changing economic and other environments. The other extreme is of course the United States. The U.S. is very good at adapting to changing environments where things are sometimes not stable. So there may be a trade-off. But the financial Big Bang in Japan means that Japan will move to an adaptability-oriented system.

Finally, who will be the major players in Japanese financial markets, once the Big Bang picks up steam? Some say that Japan's Big Bang program is a "Wimbledon style" reform—Wimbledon is located in the UK, but all major players are non-UK players. And if that happens in the future, in Tokyo market most players will be non-Japanese players. There are already many institutions including American financial institutions, which are being very active in the Japanese markets. Others say that Japan is becoming the "J-League" style, not the "Wimbledon"

style.” J-League is a pro-soccer league. The J-League is owned by Japanese, but they hire non-Japanese players. I’m not sure which is true. I believe that there may be some Wimbledon style that will take place in the Japanese markets. Is that good for Japan? I think it’s good. In London, there are lots of players from outside, but the market is very active and it greatly contributes to the British economy.

The second item is the banking crisis. Japan suffered from a bursting of the bubble in the stock and real estate markets, causing the banking crisis. Many things have happened including nationalization of banks. Some major banks are beginning to see daylight. Big banks are recovering, and small and mid-size banks and other credit union type institutions are being taken care of. It may take another year but more or less, the crisis is ending.

What is the nature of this banking crisis? There are three things. One is the asset bubble—or the bursting of the bubble—which means that it’s not just some banks’ mismanagement or fraud, but a problem facing all banks. By the way, the financial crises in other Asian countries more or less follow this pattern. All banks suffered because the banks held huge equity shares of other companies and land. And big long portfolio turned to be bad ones, which means that this may not happen again. In other words, once this problem is resolved, I think the financial sector will be okay. Also, a huge amount of taxpayers’ money has been injected, so the entire area has been taken care of. Finally, very low interest rates have helped those banks recover. The banking sector has made great progress in cleaning up their mess in the past few years.

So, with these two items, financial Big Bang on one hand, and the banking crisis solution on the other, what are their implications for the more structural side of the Japanese system? Number one, legal change. Number two, corporate governance. Number three, the style of regulation.

The Big Bang is encouraging a much deeper change in the legal system. There are three characteristics about the Japanese legal system after World War II, especially during the high economic growth period. Number one, the basic statutes. Japan imported basic statutes including savior code, commercial code, procedures, and court systems from the West about 100 years ago. The transplantation was very smooth. But these codes and written statutes, were not really used. They’re okay, but not very useful. Number two, the bureaucracy is very strong. My university, the University of Tokyo has been known as the bureaucrat-making machine since the Meiji Era. The strong bureaucracy played a very major role in Japanese economic development. Number three, the judiciary system, on the other hand, has been kept very small. The national budget spent on the judiciary is very small, less than 0.1percent. I’m not saying small is bad. The court system is solid, the judges are highly respected, but the judicial sector itself is very, very small for the size of the economy.

Now, these three things are changing. Put things in reverse order. First, the judicial system has become larger and the number of attorneys and judges is increasing. There is a big debate on further changes in the judicial sector, court system and private attorneys. It may not mean that Japan will become a more litigious society, but the judicial system is becoming larger.

Second, bureaucracy. The style of regulation is changing. In the financial sector, as you may know, the Ministry of Finance lost its power to regulate banks, securities and insurance companies and a new agency called the Financial Supervisory Agency was established last year. This restructure of regulators changed the style of regulation, from consensus-based regulation to a more rule-based regulation. This means that the role of politicians became more important as

the Diet passes the law. Diet members are more active in discussing specific legal or regulatory changes than before.

A couple words on corporate governance. Three things are happening now. First, the banks' power is declining, and mutual stock holdings are disappearing. And finally, the size of boards of directors of major companies is shrinking.

I will stop here and move on the two other issues: the economic outlook and U.S.-Japan economic relations. Professor Saxonhouse will talk about the economic outlook more in detail later, but the Japanese economy is recovering. The economies in Asia are recovering. That's what statistics indicate and why the stock markets are rising. Economic recovery may mean that the speed of structural change will become slower, because crises stimulate structural change. In Japan there remain two big issues. One is public debt, and the other is our aging society, including pension system and social welfare.

Finally, on U.S.-Japan economic relationship. There are many things to say, and it is difficult to focus on specific issues. In Washington, the U.S.-Japan economic relationship means U.S.-Japan economic talks. There are three stages in the talks, but these stages do not necessarily move in order from number one to number three. Number one is the world trade balance, number two is market access, and number three is more structural reform or convergence of systems. This means that the three key notions in U.S.-Japan talks are deregulation, transparency, and shareholder-oriented corporate governance so to speak. My focus will be on the third stage that is deeper structural reform or the convergence of systems. U.S.-Japan relations will continue to be important, but even more complex, I think with no clear focus on specific methods. But rather these three things are co-mingled so there are more things to talk about.

Now, I would like to make one inquiry. That is, "What is the relationship between structural changes and economic recovery?" Historical experience suggests that you cannot prove with any evidence that structural change *per se* leads to economic recovery. Nor you can say that any economic recovery leads to structural change. What we observe is that a crisis or some drastic event often brings structural change. I will present an academic hypothesis and a theoretical hypothesis about when structural change occurs. One well known economic theory in Japan was invented by an American economist. It is the theory of complementarities. While this theory is well known and well accepted in Japan, it has never been accepted in the United States as far as I know. The theory basically says that any system consists of a subsystem of parts that are complementary to each other. Therefore, it is difficult for any single part of the system to change unless other parts change. That is to say, more parts of the system, or many parts of the system must change simultaneously, otherwise the system will tend to remain the same. The question is how that will happen. Generally speaking, the theory says, we need a big shock or crisis for that to happen.

Gary Saxonhouse, Professor of Economics, University of Michigan

This conference is about the U.S.-Japanese alliance and asks whether this relationship is sustainable. In this regard, I'd like to look first at the long history of U.S.-Japanese trade disputes and observe that while U.S. and Japanese policy makers have thus far been successful in preventing these disputes from significantly disrupting the U.S.-Japanese Security Alliance—they have been unsuccessful in preventing them from putting a serious strain on Japan's macro economic performance. Indeed, I believe a significant share of the blame for the difficulties that

Japanese policy makers have faced in responding aggressively to the macro economic challenges of the 1990s can be attributed to this source. With this in mind, I'd like to take a look at the macro-economic policies currently being pursued in Japan and recommend new policies. U.S.-Japanese economic relations are far from the only problem that has complicated macro-economic management in Japan in the 1990s.

I would like to look also at how the structure of the Japanese economy has complicated the cyclical shocks it has received and has made the process of economic recovery more difficult. Ironically, structural reform, however beneficial it may be for the Japanese economy in the long run, may actually retard its near term recovery. Because our discussions this morning are at least partially about the economic consequences of Japan's financial Big Bang, I also want to look, or at least allude, to how Japan's financial liberalization promotes structural change. Finally, I will conclude my presentation by arguing that Japan's ongoing structural changes will facilitate the accelerating multilateralization of U.S.-Japanese economic relations. This is a worthy end, in and of itself, but this multilateralization can have very positive macro economic consequences. In concluding this overview, I should note that I hope to do all of this in the remaining 21 minutes of the time that has been allotted to me.

One of the simplest, but little publicized explanations of what went wrong in the 1990s stresses the deflationary bias imposed on the Japanese economy by continued U.S. government demands that Japan pare its large trade surplus by encouraging the yen to appreciate. These demands, which have been with us for much of the past three decades, have resulted in a trebling of the yen's value in relationship to the dollar, without necessarily having much long-term impact on Japan's trade surplus. Efficacious or not, this secular appreciation of the yen has been going on for so long, that it is now embedded in the expectations of global financial markets. If the financial markets expect that the long-term trend of the yen is to become more valuable in terms of dollars, interest rates will inevitably be lower in Tokyo than in New York. This difference in nominal interest rates between Tokyo and New York, posed no problem for Japan until the 1990s, by which time the Fed had finally rung most of the inflation out of the American economy. American interest rates are now in mid-single digits and with continued appreciation of the yen, expected and indeed cheered on by American policy makers, it's hardly surprising that nominal interest rates in Japan are now near zero.

Why are zero rates a problem rather than an opportunity for Japan? To put it quite simply, with zero interest rates, monetary policy ceases to be an effective instrument for dealing with negative economic shocks. In this environment, increasing bank reserves does not translate into increased economic activity. Inevitably, fiscal policy becomes the counter cyclical tool of choice, and in recent years the Japanese government has relied increasingly on it, as the only effective means to promote economic recovery.

Has the enormous expenditure of resources by the Japanese government in the interest of promoting economic recovery paid off? I, like so many in this room, am regularly asked, "Will Japan grow again?" The answer to this question is easy. Japan is already growing again. Of course, that this is happening, is a surprise to many. As recently as five months ago, the consensus forecasts on both sides of the Pacific, was for a continued slump in Japanese gross domestic product for this calendar year, nearly as bad as the 2.8 percent slump of last year. Instead, the first six months of this year have seen Japan growing at an annualized rate of 4.4 percent. Even if there is no further growth this year, Japan could record for the entire year a growth rate of 2.2 percent. In fact, I expect that when official estimates for growth in the third quarter are released early next month, the number once again will be positive. This means that

with the exception of 1996, in 1999 the Japanese economy is likely to turn in its best overall performance in the last eight years.

How has this unexpectedly good performance been achieved? Can it be attributed to the Japanese government's fiscal policy? While much has been made of the role played by the massive public works program initiated by the Japanese government, in fact, 85 percent of the growth in GDP so far this year, can be attributed directly to household spending. The propensity for households to consume rose markedly from 68 percent in February to 74 percent in July of this year. It seems regardless of the enormous government spending that the key ingredient in Japanese economic recovery is private sector participation. The major difference between the last six months of 1998 and the first six months of 1999, and again remember we don't get the third quarter GDP results until early next month, is household sector spending. During both periods there was a substantial increase in public spending. Indeed, the increase in public spending in the second half of 1998 was larger by more than a trillion yen, than the increase in public spending in the first half of 1999. In 1998, unlike 1999 however, the increase in public spending was undone by retrenchment in the private sector.

However surprising the past six months have been, significant storm clouds do remain. Given the current state of Japanese public finances, expansionary government budgets cannot be the key to eliciting the private sector spending necessary to Japan's economic recovery. In this connection I want to emphasize that it is difficult to be too alarmist about the state to which public finances have been reduced by Japan's fiscal policies of the 1990s. To be sure, at 22% of gross domestic product, Japan's net public debt is by far the lowest among the G7 countries. This figure, however, is wildly misleading. As is well known, it is so low largely because Japan's huge public debts are balanced by the assets of its social security system. Such a consolidation may be appropriate for some G7 countries, but it does not make sense at all for Japan.

Japan will soon have the oldest population among the G7 countries. The social security system assets are already spoken for. As Japan makes the transition from having the youngest population among the advanced industrialized countries to having the very oldest, these assets will soon be claimed. Far from being able to shore up the rest of Japan's public finances, its pension system is grossly underfunded by any reasonable actuarial standard. To make matters worse, many of the assets held by Japan's public pension system are suspect. Much of the revenue received by Japan's public pension system winds up being lent to special accounts, public corporations, and other public institutions, which do the bidding of the Japanese government. While many of these entities may once have played an important role in promoting Japan's economic development, today, too many of the projects and activities they have undertaken are of uncertain value. For example, the assets of Japan's public pension system directly or indirectly are being used for activities such as propping up Japan's small and medium size enterprises and for bailing out the corporate shell of what was once the Japan National Railway. But for these loans being government guaranteed, Japan's public pension system, together with Japan's enormous postal saving system, whose funds are invested in exactly the same way, might well be facing a bad loan problem, far exceeding that currently crippling Japan's banking system.

There is nothing unusual in loans of this type being made or guaranteed by government. What is unusual is the extent to which these liabilities are being kept outside Japan's public accounts. It is precisely for this reason that official net debt figures mask the crisis in Japan's public finances. Once such off budget liabilities are brought back on budget, the Japanese

government's financial obligations soar far above 100 percent of GDP, becoming significantly greater than any of the other G7 countries. This continuing extraordinary deterioration in the state of Japan's public finances can depress household spending behavior. This is not only because households necessarily expect future tax increases to pay for current deficits, but rather because this deterioration further undermines the already tattered credibility of Japan's pension system. Households increasingly expect that a substantial across the board cut in social security benefits will be necessary. Facing this prospect and recognizing that a reform in the way pension and social security funds are handled will take a very long time to make a significant impact, it is probable that households will soon be adjusting their savings and spending plans accordingly. The recent unexpectedly high propensity to consume of Japanese households, which has driven this year's recovery, cannot be counted upon to continue for very long.

For the past year there had been increasingly insistent calls for the Bank of Japan to commit not to price stability, but to a substantial positive rate of inflation. Such calls have been renewed recently by the worrisome appreciation of the yen. By making it costly to defer consumption, central bank targeting of the positive rate of inflation can create new incentives for private sector spending. This approach to resolving Japan's macro economic malaise, has much to recommend it. But it remains hard to say with any confidence, how the Bank of Japan can actually create such inflationary expectations in a deflationary environment where monetary policy has previously been ineffective. The Japanese financial system is awash with liquidity. It is not surprising that the Bank of Japan policy board finds it pointless or worse, to change its current policies.

To my mind, there is a way out of this conundrum. The government of Japan can join a credible commitment to the fiscal equivalent of inflation with a resolution of the crisis in Japan's public finances, at the same time that it allows the Bank of Japan and the Ministry of Finance to adopt mutually supportive and what I believe can be politically feasible policies. There has been a steady stream of proposals by some prominent Japanese politicians for lowering Japan's much maligned 5 percent consumption tax in order to re-ignite aggregate demand. This year's temporary incentives to stimulate Japanese housing construction are a cousin of this policy proposal.

Actually, I believe it would be better not to lower but to raise the consumption tax and to raise it substantially and permanently. Of course, this tax increase should not take place any time soon. But, it should be legislated very soon with the intention, for example, that a graduated increase in consumption tax commence at the start of the Japanese fiscal year 2001 with an initial 1 percent increase and with additional increases of 2 percent for each of the next three years. This would add 2 and a half trillion yen in the first year to the government's revenue base and 5 trillion yen increments for each of the three years thereafter, and will leave Japan in 2004, with a consumption tax of 12 percent. Such legislated inflationary expectations can have a powerful effect on the timing of consumer expenditures, moving forward expenditures that might otherwise have been delayed. By credibly committing now to consumption tax increases in the future, and repairing the state of Japanese public finances, the Obuchi government would become free to provide still more short-term stimulus to the economy right now, without fear of being undercut by the actions of the private sector. The anticipation of the consumption tax increase will encourage households to spend before it comes into effect. But of course, it also means there will be less spending once the tax is actually imposed. The year and a half before Japan increased its consumption tax from 3 percent to 5 percent on April 1, 1997, saw its economy expand at a rate exceeding that of any other OECD country. This expansion came at

the cost of later consumption, and it helped push the Japanese economy into seven quarters of mostly negative growth.

Am I proposing that once again Japan trade a future recession for a short-term recovery? I don't think so. In the next five years, the consumption expenditures that are moved forward, together with the new fiscal stimulus, permitted by the commitment to future tax increases, can be expected to generate the kind of demand pressure which fosters inflation. Given that such inflation has been generated as the ironic byproduct of a more fiscal responsibility, it should be politically feasible for the Bank of Japan to adopt an accommodating monetary policy. In the resulting environment it may finally be possible for the Bank of Japan to credibly commit to inflation targets that can maintain inflationary expectations and higher levels of private demand in the critical period after the transition to a much higher rate of consumption taxation is completed.

Now, it is not enough to think about more fiscal stimulus in Japan without attention to the crisis in Japan's public finances. At the same time, inflationary expectations that might stimulate private sector demand are unlikely to be generated by the Bank of Japan in the current deflationary environment. The long standing Japanese government interest in relying more heavily in the future on expenditure taxes rather than income taxes should be acted upon now. By committing to a timetable for increases in the consumption tax, the efficacy of Japan's traditional macro-economic tools and the health of the Japanese economy can be restored. The macro-economic fix I have proposed will leave the Japanese economy with a significant inflationary bias. This bias in all likelihood will undo the financial market expectations about perpetual yen appreciation that have made Japanese macro-economic policy sometime an unwilling hostage to U.S.-Japan trade diplomacy.

But does this mean that Japan will become less recession prone in the future than it has been in the past decade? Restoring monetary policy as an effective counter-cyclical measure should do just that. Over the next few years however, monetary policy will be challenged by the fallout from accelerating structural change within the Japanese economy. Rarely a day goes by when the Japanese newspapers do not announce some new corporate merger or some new corporate plans whose purpose is to reduce the burden of redundant capital and labor. These changes in the way Japanese firms operate in the future, can only be good news for the long run health of the Japanese economy. In the near term however, this means a continual shrinkage in the rate of investment in Japan will cast a pall over consumer confidence. Uncertainties arising from this source may pose a still greater challenge to macro-economic policies. While 1999 is likely to be a good year for the Japanese economy, the first year of the new millennium may not be nearly so good in the absence of a restyled macro-economic policy.

The ongoing structural change in Japan is being accelerated by an increased corporate concern with return on assets. This concern is being driven not just by the slump in return on assets during the 1990s but also by the increasing pace of financial deregulation in Japan. A financial system that finds it increasingly easy to move resources to sectors and firms that yield the highest rate of return is forcing change on the rest of the Japanese economy. In the presence of great uncertainties about the future character and direction of technological change, the more diverse sources of finance now available may lead Japanese firms to have more idiosyncratic portfolios of products and processes. The extreme degrees of export specialization and meager intra-industry trade so characteristic of Japan's past will be even less a part of Japan's future than they are today. In this fashion, the same structural change and institutional adaptation that is restoring the health of the Japanese economy is undercutting the basis for trade disputes between

United States and Japan. This process has been ongoing for some time and it augurs well for sustainable U.S.-Japanese alliance in the 21st century for both the direct and indirect reasons already outlined.

Q & A

Q: (To Saxonhouse) Back in 1986 when “*endaka*” came along, there was quite a restructuring of the Japanese manufacturing economy. A lot of companies suddenly started moving overseas. I think there has been a feeling more recently that some of the strengthening of the yen and the other pressures on the Japanese economy would again force Japan to continue restructuring and to cut back on investments or manufacturing that don’t make sense under the current environment. If you put your proposal into effect when the yen is not strengthening, what impact would this have on the pressures for faster restructuring of the Japanese economy?

SAXONHOUSE: I tend to be of the opinion that more important than the yen, changes of the value of the yen are driving structural change. I think the changes, the ongoing need to readapt to a very, very different global economy, are being forced upon Japan. Yen appreciation, to the extent that it drives structural change, drives an old-fashioned kind of structural change, the movement in the locations of where Japanese firms produce. I think the structural change that is really necessary is the change in Japanese domestic economic institutions. And the slump in the economy has forced an increase in the pace of deregulation, which has changed the character of the financial system and is driving a lot of other kinds of changes within the economy. I think that’s much more important. I would never rely on an appreciation of the yen to force a significant long-term change in the Japanese economy.

Q: Could Dr. Saxonhouse comment briefly on Dr. Kanda’s analysis of the cleaning up of the banking mess in Japan? It’s one thing to suggest that maybe recapitalization of the banks has been pretty much completed because of the massive amount of public funds. But I don’t see any evidence that there have been much asset sales yet. All of these assets are still on the books of one entity or another and are not being put back in the private sector use. Can this transformation, the banking system mess, really be cleaned up until these assets are disposed of?

SAXONHOUSE: I think the most significant fact is that these assets are not on the books of the banks. And that has prevented the banks from playing, if not their accustomed role in the Japanese economy, a more significant role in the next few years than they’ve played in the last few years. I think that is tremendously significant. I agree with you that the disposal of assets has been slower than one would like, but to say the least, I don’t think that has handicapped the banks. I once again would emphasize the institutional changes within the financial system that are increasingly changing the way finance occurs in Japan. And I think that’s probably what one should keep one’s eye on.

Q: (To Saxonhouse) Why would not your proposal of a shift towards an inflationary bias run directly counter to your expression of the importance of accelerating, pursuing, continuing, structural change in Japanese economic institution?

SAXONHOUSE: I think you have to make a distinction between the cyclical problems and secular problems. Japan faces a severe cyclical problem, which it now may be coming out of. And it has faced those cyclical problems primarily with one effective tool, fiscal policy. This tool has been used to excess, and we cannot expect that the Japanese government can run up debts that it has been running up for the last few years into the foreseeable future. At the same time there is no guarantee that the current recovery will be sustainable. With fiscal policy not able to play an important role in the future, given the current state of public finances, one has to think about what other mechanisms we can develop to get spending to occur within the Japanese economy. One way to do that is for people to believe that prices will be higher in a few years than they are presently. We want to get the psychology back among Japanese households. It's difficult to convince Japanese households simply by the Bank of Japan announcing that there's going to be inflation in the future. The only possible way this could be done, at least from my point of view, is to start talking about jacking up the consumption tax.

Now, we know from past experience that Japanese households respond very positively to the anticipation of future increases in the consumption tax. We know also, that the Japanese government, for reasons of social security and welfare, is going to have to increase the consumption tax in the future. Some of the more courageous Japanese politicians, such as Kato Koichi, have actually said as much. So if this is likely to happen in the future, my feeling is the government should take advantage of this and be specific about when it's going to happen, in the interest of inducing some short-run spending.

The problem with that is that we can't increase the consumption tax indefinitely and we don't want to. So, what happens when that period's over and the consumption tax stops increasing? Well, the way you can keep spending, is by having some inflation in the economy, which has been absent in the last decade or so. Get Japanese households thinking that in the period after there is a consumption tax increase, there's still going to be inflation in the future. This again will perhaps encourage still more spending in the transition period after the consumption tax has finally achieved its new level. Anyway, I view these all as short-run fixes. I think it'll have a long-term benefit in removing the expectation that the yen will always increase relative to the dollar. I think this complicates Japanese monetary policy.

But I think this is all very, very separate from the kinds of institutional changes that both Professor Kanda and I are extremely interested in, and which I think may well be very useful in raising the long-term growth rate of the economy, well above the 2 percent that is now anticipated. As recently as five years ago, it was conventional to assume a rate of increase of 3.5 percent. I think it has very little connection with the short-term policies that I'm talking about. Except, I don't believe that a depression in the Japanese economy is the best way to get structural change. Creative destruction is a good thing, but not that much destruction.

Q: Somehow the U.S.-Japan trade deficit, or trade surplus, looks to me as less relevant to the management of Japan-U.S. economic relations for the time being. This might have happened partly because since the two governments solved the very thorny issue of auto talks there have been now very few difficult sectoral issues. Maybe the focus has shifted to, as Professor Kanda mentioned, the issue of transparency or deregulation. Inside beltway, there is always a school of thought that once the U.S. economy tumbles the trade deficit will become a very hot issue. I would like your view.

KANDA: I have both theoretical and political answers. The theoretical answer would be that structure is more important than the trade balance. Which means that the longer-term talk will be more on structure rather than a sectoral trade issue, whatever happens to the U.S. economy. The political answer is that people don't pay attention when they are busy with other issues, but once they are gone, they look back and talk about them.

SAXONHOUSE: I agree with Professor Kanda. It's certainly possible that there could be a renewed interest in trade problems and the size of the bilateral imbalance. But I suspect that the character of the Japanese economy has changed so much. These changes have been very well publicized in the United States including the participation of GE Capital and Merrill Lynch in the Japanese economy, and the Ripplewood takeover of the Long-term Credit Bank, and possibly the Nippon Credit Bank. This is really a chain, the fact that a Brazilian is running Nissan, and a Scot is running Mazda. The face of the Japanese economy is changing. The kind of deregulation that has occurred in the last two years really should augur well for the future. Now, this doesn't mean that we won't have trade disputes between the United States and Japan. The bilateral imbalance makes it a little bit easier for the Congress to focus on a trade dispute with Japan than it is for the Congress to focus on a trade dispute with Europe although I think we're all aware that we have very, very significant trade disputes with Europe. But increasingly, the United States has a large number of hostages within the Japanese economy. And that changes the character of U.S.-Japanese economic relations. And I do see a change in the 21st century.

Also, some of these structural factors that have driven the bilateral imbalance may change. The Japanese population is aging. An aging population should change the character, the scope and size of household saving. That in turn should be reflected in the size of the Japanese current account surplus. Household savings will be less positive.

Q: (To Kanda) Regarding the theory of complementarity, how close is Japan to the point where all of the parts of the system are moving in the direction of complete systemic change? How important is it for the government to get those assets into the market?

KANDA: It is true that the government holds huge bad assets after cleaning up the banking mess. The question is how important it is to the Japanese economy. It's much easier to say that it takes time to find potential buyers for the remaining "better assets." The amount of the bad debts is much bigger in Japan than in the United States during the S&L crisis. However, in the relative size of the Japanese economy, I think the amount is not that big. I'm not saying that the entire problem with the banking mess is not important. But the size of the assets that the government holds is not as big as it should be in terms of affecting the Japanese economy in any way. So, I think the real question is how quick in the government can sell off or find their potential purchasers in the private sector. I think it may take three years or so. The U.S. experience showed that indeed speed is important. The U.S. enacted special laws back in 1991 to clean up this banking mess. It took two years for the U.S. banking industry to begin to recover.

Q: On the subject of public sector finance, the problem of the government held special corporations lending and bad assets in the public sector motivated the Hashimoto government to consider financial reconstruction of the public sector, but it was completely abandoned when the economy went south. It seems that, in fact, the government is going the other direction with the

expansion of very large lending and guarantee programs for small and medium enterprises. These programs are now being expanded and extended in their duration and the Diet session will be considering additional programs for small business, reflecting both the severe conditions and the political influence of small business. Do you think that this will be a political and economic problem in the future? Or do you think that your solution, perhaps raising the consumption tax in a graduated manner, will exert sufficient pressure and provide the sufficient resources to deal with this problem?

SAXOHNOUSE: I think it's apparent that it will be an economic problem. I'm well aware that what I'm proposing is not, either the policy of the Obuchi government or likely to be adopted by the present government. I do think that the current loan guarantees that are being considered during this Diet session are of such a scope that they really will significantly add to what is already a very, very serious problem. On top of that, the supplementary budget is being passed. Now, will there be a political problem? Certainly, there are lots of commentators in Japan, who point to the dire state of public finances, the waste in some of the government programs and how some of these loan guarantees may actually be counter productive. But I can't say with any assurance that this will be a major political problem, until it becomes an economic problem.

KANDA: I agree. In my personal opinion, financing by the public sector is a mistake. But why is the current Diet session focusing on small business? Two reasons. Number one, most small businesses are powerful politically. Two, MITI is trying to boost this area. These bureaucrats are surprisingly powerful. MITI, for example, is also just looking for something to do in each Diet session. I'm not saying that MITI is doing bad, but just acting improperly. For these two reasons, this Diet is focusing on small businesses. In my personal judgement, it will aggravate the public debt problem. The public debt problem, however, will not become a political issue unless it becomes an economic issue. The government announced a plan to protect bank deposits in full until March of 2001, but it is not free of charge. Full protection of deposits means spending more taxpayers' money. This, of course, will become a political issue, I think if it first becomes an economic issue.