

On Japanese Scandals

Karel van Wolferen / Chuo Koron Sept. 1991

The study of Japanese political and economic affairs should be enriched with a special subcategory for scandals. Not because Japanese people produce more, or juicier, scandals than others. Some other countries are pretty good at it as well. But there is a need for systematic analysis of Japanese scandals because of their important function of keeping the Japanese power system running smoothly. The current security brokerage scandal is, again, a wonderful example of this.

The major, central, role of the Japanese scandal is to help curb excess. Excess in any kind of behaviour that is otherwise considered normal. For example, it is considered normal in Japan that the astronomical amounts of money politicians spend to get re-elected is provided by corporations. But there are limits to this normality. It is not considered a good thing that one politician gets ten times more than he needs to get re-elected. Conversely, it is not considered a good thing that one single company funds every well-known politician. In either case there is the risk of producing a threat to *the way things are done*. This threat may turn into an instrument causing the breakdown of *the way things are done*. Let us use the term "System" interchangeably with *the way things are done* to make it easier to talk about this phenomenon.

The most important characteristic of the System is that it is "extra-legal"; it operates outside the framework of what is permitted and not permitted as determined by law. Behaviour within the context of the System is sometimes illegal, sometimes not. It keeps to certain rules, to be sure. But these rules are informal rules; they are, to use a term commonly used in European languages, "unwritten rules". In other words, the System is not ultimately regulated by rules that all of us can appeal to. The rules were not made to protect or give advantage to ordinary people. They serve a minority -- the political elite. Let us call the people who decide *the way things are done* "the members of the System". They are the most active among the political elite.

Japanese scandals are more than useful in helping to prevent destructive excess. They are probably indispensable. It is not difficult to see why. Any system, whether informal or highly legal, transparent or opaque, must have some mechanism to keep members in line. In a system governed by laws, an outsider supervisory body is necessary to ensure that these laws are obeyed. In a system governed by *the way things are done* such a check cannot exist, which means that the chances are pretty good that occasionally things may get out of hand. The System is prone to excess for the very reason that it is not ultimately regulated by law. Because a trend in *the way things are done* that brings advantages to some members of the System is difficult to stop as long as it doesn't bring great disadvantage to other members of the System. In an informal political system with unwritten rules scandals must, at least to some extent, play the role that courts of law and supervisory agencies play in a system governed by the rule of law.

By preventing destructive excess, Japanese scandals make it possible for the

System to survive. This is where Japanese scandals differ most from normal scandals in the United States and in Europe, which tend to bring about a purge, a "cleansing" of practices to a point where the conditions that facilitated illegal or improper behavior no longer exist. Cozy, extralegal ways of doing things develop among political elites anywhere in the world. Scandals in Europe or the United States tend to destroy them. Scandals in Japan ensure the future of such informal relationships.

Besides protecting the System by curbing the threat of excess, Japanese scandals generally benefit private interests of powerful organizations within the System. Scandal time in Japan is a time during which various power groups try very hard to accomplish their own goals. Things are in a flux during scandal time, and many goals cannot be achieved when things are static.

Japanese scandals also teach us that whereas the members of the System often cannot control processes, they generally do control outcomes. (I think the same is the case with control over the Japanese economy: the focus of bureaucratic management is on outcomes; there is seldom an attempt to direct the details). Japanese scandals are managed to a high degree, but still a lot that is unexpected can happen, including developments unpleasant to those who participate in the managing of the scandal. Scandals may bring anguish and pain for important members of the elite. At times scandals may give the impression of not being under control. My favorite comparison is with a garden hose. If you turn on the water before you get hold of the nozzle, the hose may flap about and drench bystanders who were not expecting to get wet. The Recruit case was a good example. While it was being used by various groups like the Keidanren, the Ministry of Post and Telecommunications, the enemies of Nakasone, and by Takeshita, all for their own ends, the scandal went temporarily out of control and forced the resignation of Takeshita (largely because of the wrong choice for justice minister when he reshuffled his cabinet).

The security brokerage scandal began when the tax bureau of the Ministry of Finance, under a new administrator, decided that the securities industry should not be allowed to get away with subtracting the now infamous compensations from their taxes -- in the way they are allowed to subtract their entertainment expenses. The next phase is blurred, but once the scandal got going it became abundantly clear that it was providing wonderful opportunities for officials in the Ministry of Finance.- Their purposes have so far been well-served, because two elements were brought back to what is in their eyes "the right order". One is Nomura, and the other their own securities bureau.

In the past ten years or so Nomura has become extraordinarily powerful. In fact, there is nothing like Nomura in the world. It is roughly 25 times bigger than the biggest American securities firm. This segment of the Japanese financial industry is run by a *de facto* cartel, composed of the four big securities houses. All the smaller ones are, as it were, subcontractors operating under the protection and in accordance to the unwritten rules provided by the cartel. The undisputed leader of this entire apparatus is Nomura. Even though the three other big firms are powers in their own right, they take their cues from Nomura in important matters. This set

up is an excellent illustration of oligarchic power verging on monopolistic power. With the one important restriction that ultimately the whole arrangement can only function under the wings of the Ministry of Finance.

The incredibly fast development of Japan's financial institutions during the 1980s, along with the massive inflation in capital assets (real estate and stocks), produced major power re-alignments within Japanese business, which for example made Keidanren and the banks relatively less important vis-a-vis the securities industry, construction and real estate companies. And, as always with such rapid power re-alignments, this stimulated an uncomfortable sense among the members of the System that normalcy had been disturbed, requiring at least some adjustment. In the 1980s, the security houses gained a measure of influence and prestige they had never had before. And it was reasonable to expect that it would only be a matter of time before they would be forced to undergo an experience intended to cool down their zealously, restrain their arrogance, and remind them of the proper relationships within the Japanese System. This has just happened, and for Nomura, as the leader of the cartel, it has been, of course, the most unpleasant.

Similarly, Ministry of Finance officials appear to have decided that the time had come to cut the securities bureau within their own organization down to size. Until it began to reflect the new importance of the securities industry in the 1980s, this bureau had been relatively insignificant when compared with the tax, banking and budget bureaus. The old internal balance in the Ministry of Finance can, at least to some extent, now be restored.

But these forced adjustments among the components of the Japanese power system may even have been relatively minor goals of the Ministry of Finance. Something else has happened that has been critically important for the Japanese economy as a whole. Although the securities companies appear to be the main sufferers in the current scandal, they are, ironically also its main beneficiaries. One way to interpret recent events is to see them as one gigantic rescue operation for the securities industry cartel. And that can be considered part of an even larger operation that has been going on for over a year and a half: the restraining of the so-called "bubble economy".

I do not believe that there ever was a real bubble economy, in the sense of a speculative bubble that could burst. There was always too much control -- informal control -- for any "bursting" to be a likely result of the wild, but managed, inflation of capital assets that took place in the second half of the 1980s. But the absurd increase in the nominal value of Japanese real estate and stocks did create considerable distortions in the economy and, very worrisome to the Ministry of Finance, it had brought into being fairly strong and opportunistic "bubble companies" that were not part of the informal networks to which members of the System belong. The dramatic plunge of the stockmarket a year and a half ago may not have been started by the Ministry of Finance. But once the downturn began, the ministry monitored and controlled it, and was ultimately able to use it to accomplish its goal of reducing the excesses of the "bubble economy", and bring all elements of the financial system back in better order. Indeed it was able to use the downturn to ex-

pand its area of control to elements such as non-bank financial institutions.

But this stockmarket downturn created major losses for firms which had always played the game according to the unwritten rules blessed by the bureaucrats. And compensations for these losses seemed very appropriate if you look at it from the inside of Japan's "miraculous" financial system. The amounts that the big investors expected to be paid were, however, much larger than ever before. They were so huge that if the securities firms had continued paying them, they would probably have sunk into deep trouble. And this would also have caused a further depression of the stockmarket.

To recapitulate: the recent threat of excess to *the way things are done* consisted of excessively large amounts of money and the recently excessive prominence of the securities industry. Both have now been taken care of.

In the Recruit scandal the threat of excess also consisted of massive amounts of money as well as large-scale use of new and less easily controllable methods of securing protection and influencing bureaucratic decision-making. Again, in the scandals involving Tanaka Kakuei (his money making methods and Lockheed), excess consisted of the very systematic use of huge amounts. Other than that, Tanaka Kakuei and Ezoe Hiromasa did what others also did and still continue to do. Their sin was that they were better at it than other members of the System. They knew how to exploit the opportunities for self-advancement offered by System much more effectively. They were geniuses. And the members of the System are scared of geniuses of that kind, because the latter threaten to dominate *the way things are done*, thus endangering the internal balance.

The routine compensation payments by Nomura and the others has not come as a surprise to anyone who is familiar with the workings of Japan's financial system. It has not been much of a surprise, either, to those who may know little about the financial world, but who have a generally good idea of how Japan is run. The security houses were doing what they were expected to do. Just like, in the Recruit scandal, the other main victims Shinto Hisashi and Miyazawa Kiichi had been doing exactly what was expected of them. All of these organizations and persons have been conforming to *the way things are done*.

Even more than staying well within the conventions of the System, the security companies were helping to make the System run more smoothly. They were helping to sustain conditions ensuring the collaboration of big corporations in large-scale pool efforts for creating and controlling a vast expansion of Japan's asset base (stocks and real estate), allowing for vast increases in Japanese productive capacity. They were crucial in helping to reduce the cost of capital for Japan's large companies to almost nothing, thus enabling Japan's corporations to make the investments necessary to be competitive notwithstanding the high value of the Yen from the mid 1980s onward.

The most important question to ask therefore is why there is a scandal to begin with. What, actually, is the scandal all about?

As in the case of the Recruit scandal, nothing much illegal took place. The Ministry of Finance has confirmed that compensation is only illegal if it has been

previously promised. And even though the compensations were expected as a matter of course, everyone can easily say that such promises were never made. So, there is no legal case.

But after years of agreeing with the practice of compensations, the Ministry of Finance has now decided that what the security industry did was improper. If that is true, the next question we must ask is: improper by whose standards? Did the security houses violate, in a major way, the rules of Japanese social convention? This question brings us to a subtle, and most interesting point. For the answer is both yes and no. Yes, in the sense that many ordinary Japanese think that something is wrong and unfair if only large investors get guarantees in a market in which the public also participates. But the answer must be "no" if we measure the behaviour of the security houses by the conventions of the world in which they operate. After all, their behaviour lived up to *the way things are done*.

It is rather clear that the Japanese political elite and Japan's ordinary people use different standards for judging what is appropriate and inappropriate conduct. What is very special about this situation is that while the common people have a fairly good idea of their own standards, they really do not know much about the standards of the elite that maintains the Japanese System. And the members of the System are not at all honest about their own standards when they present their views to the public. Ordinary Japanese have but a vague idea of how their country is really governed. This difference between what the elite knows and what the ordinary Japanese know is a vital characteristic of the Japanese political system, and of Japanese society generally.

The division is traditional. In Tokugawa days the relevant phrase was: "people must not be informed, but made dependent upon the authority of the government" (*tami wa shirashimu bekarazu, yorashimu beshi*). And still today, there are two classes of Japanese: one small minority of "knowers", of people who are clued in, and the large mass of political innocents, of people who may suspect that there is a different *bonne* behind many a *tatema*, but who cannot quite put their fingers on it.

If I had to choose the biggest villain in the various Japanese scandals that I have looked at closely, I would take the press. This choice may sound strange, since the Japanese press normally receives a good amount of applause for the revelations it provides in times of scandal. But it doesn't deserve this applause. Japanese newspapers help perpetuate the division between the minority of "people in the know" and the majority of political innocents. They never consistently and seriously analyse *the way things are done* in Japan. They do not explain to the Japanese public what it ought to know about how the country is governed. They could make the point, but do not, that yes, it strikes one as improper that the securities houses lent 36 billion yen to a boss in the Inagawa-kai, but that Japanese big companies and politicians and the police have been doing business with the gangsters as a matter of routine. They could point out that... yes, protecting big investors at the expense of small investors is discriminatory, but that the Japanese financial system has a long history of discriminating against the small saver and the small borrower. Japanese have normally had meager returns on their savings (for long periods even less than

the inflation rate), which were channeled directly into big industry. And consumer credit remains, even now, fairly primitive. All this has been important to realize the "economic miracle".

The newspapers assume a critical attitude once in a while, especially during scandals, but this attitude is phony. Editors and journalists help the bureaucrats in what I call the "management of reality". Reality is generally an elusive thing in Japan because there are too few Japanese intellectuals or journalists who relentlessly separate fact from convenient and politically expedient fiction. Again, in the current security brokerage scandal the newspapers are not engaged in pointing out the contradictions.

Without the press there would not be Japanese scandals. And Japanese scandals help keep the Japanese press under control too. Big scandals generally cause a firestorm that rages through the media world. Almost nothing else seems to exist for the time that they last. Scandals are wonderful opportunities for the media to blow off steam, to become very indignant, and to give journalists and editors, all worked up by faked indignation, a sense that they are doing their duty of protecting Japanese society by exposing wrongdoing. But all they do is protect the System, of which they are, of course, a part.

The press helps the Ministry of Finance to accomplish its aims by upholding the fiction of public outrage. Without an impression of public outrage there would, of course, be no scandal. This is one of the most subtle forms of manipulation of the "innocents" in the Japanese political system. Editors along with the bureaucrats in Japan are not in the habit of reflecting, or responding to, public opinion. They manufacture public opinion, simply by repeatedly telling newspaper readers the same things about what they believe the public thinks or should think, after which the reader begins to believe that this is what his or her opinion ought to be.

The Japanese public of today is considerably less innocent than in the Tokugawa or Meiji periods. In my experience Japanese who use their heads have a pretty good idea about how power is exercised in their own immediate environment, and they display a healthy cynicism about what the authorities in the central government and the big business world are up to. But the public has too much good sense to become outraged. Lacking the means to throw out the government, to change the System, or to express themselves in any other way besides joining a few hundred likeminded people for a snakedance down the street, most intelligent Japanese know that what they think makes no difference in any way.

To portray Japanese scandals as signs of "Japanese democracy at work" is unwholesome and an insult to the dignity of the Japanese individual. Scandals help prevent the realization of Japanese democracy by protecting, and thus strengthening, the system of informal relationships ruled by *the way things are done* over which the public has no influence at all. To make it appear as if the current security brokerage scandal is going to change the way business is done in Japan demonstrates either dishonesty or ignorance. Only those who look at the world from an unhistorical perspective can believe that the current scandal is bringing Japan a step closer to genuine legal rather than bureaucratic control.

There is talk of new legislation, and it has been suggested that Japan create its own Securities and Exchange Commission (SEC) after the American example. But what significance can that possibly have? Any new or amended laws will be administered by the officials of the Ministry of Finance. And they are accountable to no one. They can enforce or refrain from applying the law as they themselves see fit. Such bureaucratic discretion is crucial to the survival of the Japanese System. As for a Japanese SEC, if it were to come into being it will be manned and directed by *amakudari* bureaucrats from the Ministry of Finance, and will have wonderful relations with the securities industry cartel.

There is a growing number of serious observers, here and abroad, who believe that the real rulers of Japan, the cockpit of the state as it were, is the Ministry of Finance. I do not think so, because I do not believe there is a cockpit. But the current security brokerage scandal demonstrates once again just how powerful the Ministry of Finance is compared with the other members of the System. And I think that although it does not constitute a center of political accountability, the Ministry of Finance may well be, for all practical purposes, the single most powerful among the groups that share power in Japan. It therefore deserves to be studied more.

Japan's Ministry of Finance is in many ways a good ministry, and a capable ministry. It certainly knows how to preside over economic expansion. But it does not represent the Japanese people. Whatever new regulations and legislation it may now introduce, none of it will be designed to protect the majority against behaviour serving the vested interests of a business minority. And none of it will be used for such a purpose.

There is an urgent need for the class of "people in the know" to expand. If the "knowers" included a growing multitude of serious and concerned citizens who are not part of the System, Japan would get the intelligent general political discourse it so desperately needs. The advantage of a systematic study of Japanese scandals, as part of such a discourse, is that it throws much light on the relations among the various groups that share power in Japan. There is another, more subtle, advantage of thoroughly analysing Japanese scandals. If a proper analysis became widely known among Japanese people, the scandals would perhaps no longer fulfill the function of protecting the structure of informal relationships and informal transactions. It might help to give Japanese democracy a chance.