PART I REPORT BY THE JAPAN TEAM

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Privatization and Deregulation: The Case of Japan

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1. INTRODUCTION

Deregulation and opening-up is in full swing in developing countries, particularly, the privatization of state-owned enterprises, firstly for fiscal deficit and secondly for free-market economy reasons. Furthermore, deregulation of many business activities is occurring thereby creating many benefits. However, several negative effects on society such as unemployment, foreign capital dominance, oligopoly, and an increase in the income gap can be observed.

This brief paper examines merits and demerits of privatization and deregulation. The first section describes the pros and cons of these policies. The second section surveys privatization and deregulation processes in Japan. Especially, privatization of the railways and telecommunications sectors are illustrated. Finally, some suggestions for developing countries are drawn from Japanese experiences in the third section.

2. PROS AND CONS OF PRIVATIZATION AND DEREGULATION

Market mechanism with less intervention from state or government has been pursued in every corner of the globe during the 1990s. Efficiency and transparency led by markets are better than inefficiency and opaque systems led by government. Under these circumstances, state-owned enterprises (SOEs) have been privatized and deregulation in social and economic activities has been going on in developing countries as well as advanced countries. This market-oriented approach has become the main economic philosophy in the contemporary world. However, there are, in fact, some serious problems related to this exercise.

2.1. Merits of Privatization and Deregulation

It is usually said that privatization of SOEs and deregulation of economic activities bring about (a) free entry and competition, (b) cost and price reduction, (c) improved services, (d) increased efficiency and efficient resource allocation, and (e) temporary asset sales income to the government (which helps reducing fiscal deficits). Privatization of SOEs in public works destroys monopoly or oligopoly of their activities. Their stocks are sold to the private sector. Combined with deregulation, free entry produces competition. Intermediate goods and raw materials relating to these public utilities are also influenced by such privatization. Price mechanism turns to work in every domain. Costs are reduced and hence prices go down.

Competition also yields better and increased services for consumers. For example, privatization of telecommunications and succeeding deregulation in several advanced countries has brought about lower telephone charges, better services and increased opportunities to enjoy various cellular phone services.

In developing countries, asset sales of SOEs boosted government revenue which could be channeled to external as well as internal debt repayments. New investments attached to such privatization also helped initiate new recovery for developing countries.

2.2. Demerits of Privatization and Deregulation

Demerits of privatization and deregulation include (a) unemployment and reduced labor union power, (b) reduced service in remote areas (i.e., universal services), (c) declined supply stability or reliability, (d) foreign capital dominance (the so-called 'Wimbledon effect'), (e) bad debt problems, (f) survival of the fittest, and (g) disorder or crises in certain sectors.

It is well recognized that privatization of SOEs produces unemployment. If there is no provision to reallocate fired laborers, unemployment increases. Recent Latin American figures show that increases in the unemployment rate definitely reflect privatization rushes and the free market business philosophy practiced in the region (urban unemployment rate: 5.8% in 1990, 7.2% in 1995, and 7.5% in 1997).

Labor unions of SOEs are often considered to be strong (for example, the labor union of the Japan National Railways was traditionally one of the toughest unions in Japan). However privatization greatly reduced the power of such unions and deregulation in the labor sector certainly weakened labor union power, too. The appearance and expansion of various types of non-permanent employment (part-time, dispatched, and temporary) is unfamiliar with labor union tradition.

Privatized concerns often ignore unprofitable areas which were previously subsidized by state-owned monopolies. Services to remote areas tend to be shutdown or cutback. For example, US airline companies are said to have greatly curtailed services to remote areas after liberalization. Nonetheless, regardless of the above trend, it is generally accepted that services such as gas, electricity, water and mail collection/delivery are necessary for daily life. Therefore, some long-term political strategy regarding accountability and performance of such universal services is required.

Price competition sometimes produces negative effects such as supply instability. The occurrence of blackouts in the UK electricity industry after liberalization is a point in case (Ishida [1998]). Security and reliability of supply must be maintained.

Privatization and liberalization invite foreign capital. As has happened in the City of London, liberalization of the financial sector during the 1980s resulted in the dominance of foreign banks, what we call 'Wimbledon effects.' Privatization of SOEs in developing countries has attracted the attention of many multinational enterprises. However, if market conditions in those countries are not yet fully developed, this may cause uncomfortable frictions.

Generally, SOEs have huge debts. That is why SOEs are criticized for their inefficiency and face constant pressure to be privatized, especially, in developing countries. If SOEs are privatized, each new company's profit will increase but the original debts owed by the SOEs are not so easily repaid. This is a headache for the state. For example, the problems surrounding the huge debts of the Japan National Railways have not yet been solved and remain an immense burden on the national treasury and the people of Japan.

Liberalization and deregulation tend to foster and encourage purely capitalistic values in society where the stronger become stronger and the richer become richer while the poor become poorer. There is a tendency for big companies to marginalize small companies by providing new services or discount prices which the small companies are unable to compete with. If network effects work, those companies with larger networks tend to attract more and more customers, thereby strengthening oligopoly. It is said that US airline companies became oligopolistic by providing better mileage services and temporary discount prices thereby marginalizing smaller competitors. Another concern is distribution. Market mechanism does not guarantee fair income distribution. Therefore a system of safety nets or social development planning is necessary to protect the weak, especially, in developing countries.

Hasty liberalization and deregulation create turmoil, particularly when markets are not ready for global opening-up. Such a situation developed in Thailand, Indonesia and Korea in 1997, sparking the so-called Asian monetary crisis. Hence, the speed, sequence, and timing of deregulation or liberalization are important factors that must be considered. Furthermore, monitoring systems to guard against unexpected turmoil, for example, monitoring institutions, or at least information disclosure, for short-term capital movements in the case of global money markets, are urgently required.

3. PRIVATIZATION AND DEREGULATION: JAPAN'S EXPERIENCE

3.1. Government Reform

The government of Japan has made enormous efforts to reform government and bureaucracy departments as well as economic and social systems for many years. The first Provisional Committee on Administrative Reform was organized under the Ikeda cabinet and its recommendation on efficient administration was made in 1964. However, no fundamental changes had taken place up to the 1980s.

In 1981, the second Provisional Committee on Administrative Reform was established under the Suzuki cabinet. Mr. Toshio Doko, honorary chairman of the Federation of Economic Organizations (Keidanren), was nominated as the head of the Committee. Stronglybacked by the Nakasone cabinet (1982-87), Mr. Doko, an honest and plain life-style person, deliberately promoted administrative reforms, particularly, privatization of SOEs. The Doko reform recommended the privatization of three giant SOEs, the Japan National Railways (JNR), the Nippon Telegraph and Telephone Public Corporation (NTTPC), and the Japan Monopoly Corporation (JMC, tobacco and salt). Consequently, NTTPC and JMC were privatized in 1985 and JNR followed in 1987 (see Table 1.1).

Between 1983 and 1993 three Promotion Councils for Government Reform were formed. Their emphasis was slightly different but their fundamental objectives were to seek efficient government as well as social systems geared toward upgrading the quality of life of the citizenry. Market-oriented economies with 'small government' were the basic ideology which underpinned the councils. Their recommendations covered such issues as deregulation, privatization, decentralization, fiscal reforms, restructuring of ministries and agencies, and information disclosure. Issues which particularly caught the public's imagination were the power of the ministry of finance (separation of budget and banking supervision), the postal savings system, the so-called 'big bang' in the banking sector, and social welfare systems (aging population).

Japan's current systems are basically built on the war-time system (the so-called '1940s regime') which aimed at mobilizing all resources into the war effort. Therefore, even today the government retains strong power and everything is centralized. For example, bureaucratic systems, government budgets, land systems, indirect financing and the main bank system, as well as Japanese enterprise behavior (so-called 'Japan Inc.') have their roots in the 1940s' regime (Noguchi [1995]). Drastic reforms are thus needed in every field to harmonize with the modern global society.

A mid-term action plan on deregulation was announced in 1995 according to the third Council's recommendation. From then on, annually revised Three-Year Plans for the Promotion of Deregulation (PPD) got underway. To support and monitor the execution of the reform process, the Committee for Government Reform (chairman, Mr. Yotaro Iida, former president of Mitsubishi Heavy Industry Co.) was established in December 1994 for three years. As far as market access is concerned, there is the Office of Market Access which has a grievance arm, the Market Access Ombudsman Council, consisting of fifteen members including three foreigners.

Table 1.1: Process of Deregulation in Japan

Year	Main Movements	Explanation
Up to 1980	Minor changes	Law for the Lump-sum Reduction of Permissions /Approvals Between 1967 and 1979 hundred-and-eighty-one laws and regulations were amended and 337 items were reduced.
1981 | 1983	Second Provisional Committee on Administration Reform (Mr. Doko)	The Committee investigated the role of the public sector from the stand point of reduction of people's burden, simplification of public procedures, and assistance for private activities. It made three recommendations which pointed out 253 items regarding permissions/approvals.
1983 | 1986	First Promotion Council for Government Reform (Mr. Doko)	Its proposal nominated 258 items for the promotion of private initiatives.
1987 | 1990	Second Promotion Council for Government Reform (Mr. Otsuki)	Deregulation was recommended taking the following points into consideration: (a) to upgrade quality of life; (b) to transform industrial structure to more market-oriented one; and (c) to improve market access to Japan.
1990 | 1993	Third Promotion Council for Government Reform (Mr. Suzuki)	Deregulation in the field of (a) internationalization of systems and institutions and (b) consumer sovereignty.
1993	Overall Economic Measures (April)	Speed-up of deregulation in permissions/approvals.
	Emergency Economic Measures (September)	Ninety-four specific items were determined to be deregulated in order to mitigate exchange gains due to highly appreciated yen against the US dollar.
	Final Report by the Third Promotion Council for Government Reform (October)	In order to establish new order, rule, and systems for enjoying private initiatives, mid-term action plan, institutional arrangements, and realignment of government mechanisms were recommended.
1994	Great Charter for Government Reform (February)	To realize a society which is based on individual responsibility and market principles, 781 public regulation items should be eased (250 permissions/approvals and 531 reports/notices were to be eased.) Also the establishment of a plan for the promotion of deregulation was recommended.
	Outline of the Promotion of Deregulation (July)	Such fields as (a) land and housing, (b) information and telecommunications, (c) market access and distribution, and (d) finance, securities, and insurance were specified for the promotion of deregulation including 279 items.
	Establishment of the Committee for Government Reform (Mr. Iida) (December)	Five private-person committee for monitoring the deregulation processes for three years.

Table 1.1 (continued)

Year	Main Movements	Explanation
1995	Plan for the Promotion of Deregulation (PPD) (March)	Objective fields include (a) land and housing, (b) information and telecommunications, (c) commercial distribution, (d) transportation, (e) norms/standards and imports, (f) finance, securities and insurance, (g) energy, (h) employment and labor, (i) public nuisance, industrial waste and environment, (j) dangerous goods, disaster protection and security, and (k) others. 1091 items were addressed. The original five-year plan (PPD) was revised as a three-year plan (1995-97) and its realization was advanced in April. PPD is a rolling plan so at the end of every budgetary year it is checked and revised.
1996 | 1998	Revised Three-year Plan for the Promotion of Deregulation PPD 1996-98, PPD 1997-99, and PPD 1998-2000. Establishment of the Committee on Deregulation (Mr. Miyauchi) (January 98)	PPD 1997-99 added education to the above-mentioned eleven fields. PPD 1998-2000 emphasizes accountability of the government.

Source: Management and Coordination Agency [1998], *White Paper on Deregulation.*

Prime Minister Hashimoto (1996-98) announced in 1997 six key reforms in the following areas: (i) administration and bureaucracy, (ii) fiscal structure, (iii) monetary system, (iv) economic structure, (v) social welfare, and (vi) education. Accordingly, for example, one office twenty-one ministries/agencies will be reduced to one office twelve ministries/agencies in government institutions.[1]

The most recent plan, PPD 1998-2000, aims at the realization of a rich and diversified life, activation of business activities, internationalization (global standards), and a reduction of the people's burden. It also aims to change administrative controls from ex-ante regulation (or direct control) to ex-post check (or indirect control) systems. The plan includes 624 deregulation items in 15 fields.

In order to promote deregulation smoothly, a new committee was organized in January 1998. This new Committee on Deregulation (chairman, Mr. Yoshihiko Miyauchi, president of Orix Co.) is a watch dog for the PPD.

3.2. Deregulation Processes

Regulatory reform has two aspects: one, deregulation or relieving regulations, controls, and rules; the other, improvements in the quality of existing regulations or sometimes making new regulations. In this paper we focus on deregulation. As pointed out, privatization and deregulation had not been active up to the beginning of the 1980s. The law for the Lump-sum Reduction (or makeup) of Permissions/Approvals was the only device in operation in the pre-1980s period. One-hundred-and-eighty-one laws and regulations were amended and 337 items were put in order between 1967 and 1979. This law continued to work and 148 laws and regulations were revised including 333 items reduced between 1982 and 1994.

The first major push for deregulation came from the Doko Reform Committee which proposed privatization of three important SOEs, NTTPC, JMC, and JNR. Japan has made great strides since then due to the successful privatization of these enterprises, combined with mounting pressures for trade opening-up from outside (mainly the US). However, full-scale progress toward deregulation had to wait to the mid-1990s.

Particularly, the establishment of the World Trade Organization (WTO) in 1995 required Japan to make rapid adjustments for globalization and international harmonization. Technological innovations in the information and telecommunications sectors and globalization of capital markets also forced Japan to move quickly toward deregulation of the economy. Deregulation measures have advanced especially since 1996 (see Table 1.2).

The coverage of deregulation has also widened. The Outline of the Promotion of Deregulation in 1994 put emphasis on four fields while the Plan for the Promotion of Deregulation (PPD) 1998-2000 covers 15 fields containing 624 deregulation items. The 15 fields are as follows: (i) competition policies, (ii) housing, land, and public works, (iii) information and telecommunications, (iv) commercial distribution, (v) transportation, (vi) norm, standards, certification, and imports, (vii) banking, securities, and insurance, (viii) energy, (ix) employment and labor, (x) public hazard, industrial waste, and environmental conservation, (xi) dangerous items, disaster protection, and securities, (xii) education, (xiii) health care and welfare, (xiv) legal systems, and (xv) others.

For instance, permission to form a cartel in times of recession will be

Table 1.2: Main Deregulation Items 1982-1998

Year	Deregulation Items
1982	• Modified from permission to notice systems on changes of bus stops.
1983	• The period of automobile check for new cars was prolonged from two to three years.
1985	• Abolition of the Rent Control.
	• Privatization of the Nippon Telegraph and Telephone Public Corporation (NTTPC) and the promulgation of the Telecommunications Business Law.
	• The Japan Monopoly Corporation (JMC, tobacco and salt) became a joint-stock company.
1986	• Established standards for double/triple trucks in domestic airlines.
1987	• Permitted the issue of commercial papers.
	• Privatization of the Japan Airlines (JAL).
	• The Japan National Railways (JNR) became joint-stock companies.
1989	• Liberalized interest rates for large-scale fixed deposits.
1990	• Eased land transport regulations (the Truck Transportation Business Law and the Truck Transportation Handling Law).
1992	• Modification of the Law for Large Retail Stores.
	• Establishment of fixed rented-land right.
	• Modification of the Law for Construction Standards.
1993	• Total weight of automobiles was changed from 20 to 25 tons.
	• Easing construction regulations (building volume rate and designs).
	• Permission of alcohol sales at large retail stores.
	• Easing taxi fare regulations.
1994	• Annual minimum beer production was reduced from 2,000 kl to 60 kl.
	• Liberalized stock sales fee beyond 1 billion yen.
	• Introduction of sell-out methods for cellular phones.
	• Eased opening hours and closing days for large retail stores.
	• Modification of the Law for Construction Standards (use of basements).
	• Liberalized deposit rates except current account deposit.
1995	• Began to make JIS to world standards.
	• Effective period of a passport was prolonged from five to ten years.
	• Six-month regular check-up of cars was abolished.
	• Introduction of tenders for electricity wholesalers.
	• Abolished the period control for fixed-rate time deposits.
1996	• Introduction of yardstick methods for electricity and gas charges.
	• Permitted subcontract of hospital food supply.
	• Abolished temporary measures for imports of specific petroleum products.
	• Introduction of insurance brokers.
	• Abolished asset operation controls on trust banks regarding the Social Insurance Fund.
	• Cross-entry by subsidiaries of insurance companies.
	• Abolished some obligatory measures relating to the issue of corporate bonds.
	• Registration of rice sales.
	• Liberalized domestic interconnections between public networks and special lines.
	• Eased sales of sweet sake brandy.
	• Notice systems of charges for mobile telecommunications.

Table 1.2 (continued)

Year	Deregulation Items
1997	· Quality control on construction structure (wall frame construction).
	· Report of the Council for Construction Standards.
	· Amended the Law for Town Planning and the Law for Construction Standards.
	· Rechecking of designated plumber systems.
	· Abolished salt monopoly sales.
	· Amended Industrial Standards Law.
	· Negative list for paid replacement centers.
	· Amended the Telecommunications Business Law.
	· Amended the NTT Corporation Law.
	· Amended the Electric Wave Law.
	· Amended the Foreign Exchange Law (abolished permitted foreign exchange sellers).
	· Liberalized international internet phones.
	· Liberalized international interconnection between public networks and special lines.
	· Abolished asset operation controls (allocation) on the Fund for Social Welfare.
	· Amended the Anti-trust Law (permission of the establishment of holding companies).
	· Abolished double-triple trucks for domestic airlines.
1998	· Amended the Commodity Exchange Law (liberalized commissions).
	· Amended the Lawyer Examination Rule and the Court Law.
	· Revised social worker regulations.
	· Amended the Telecommunications Business Law (prior notice of charges from permissions).
	· Abolished the International Telegraph and Telephone Company (KDD) Law and KDD was fully privatized.
	· Measures for foreign lawyers.
	· Amended the Law for Land Transport Vehicles.
	· Amended the Anti-trust Law.
	· Amended the Law for Land Utilization Plan.
	· Abolished the Law for Large Retail Stores and enacted the new Law for Establishment of Large Retail Stores.
	· Amended the Broadcasting Law (charges for satellite use)
	· Amended the National Highway Law.
	· Amended the Teacher License Act.
	· Enacted the Law for Financial System Reform (liberalized commission for stock sales, etc.)
	· Amended the School Education Law (permitted enrollment of special school students to universities.)
	· Amended the Law for Construction Standards.

Source: Same as Table 1.1.

abolished in the field of competition policies. The reorganization of NTT is planned in the field of information and telecommunications. The Intelligent Transportation System (ITS) will be promoted in the field of transportation. The possibility of encouraging retail supply of electricity will be examined and self-service gas stations will be permitted in the field of energy. The number of lawyers who pass the national examination will be increased in the field of legal systems.

Deregulation and privatization processes in certain sectors have not yet advanced, for instance, electricity, gas, water, mail services and banking. In the case of electricity, regional monopolies remain with 10 companies according to the country's regional division (Hokkaido, Tohoku, Tokyo, Chubu, Hokuriku, Kansai, Chugoku, Shikoku, Kyushu and Okinawa). Slow change, however, can be seen. In 1995, new entry was at first admitted in the electricity wholesale business. The so-called independent power producers (IPPs) were able to participate in electricity supply by tender. Part of the tariff system was also modified from an approval to a report bases and yardstick pricing was introduced. The Council for Electricity Business recommended to MITI in May 1998 the liberalization of electricity retail but only for large-scale users (above 2,000kW using 20,000 volts) from the year 2000 on. Discussion is now going on regarding retail liberalization for small users including households.

In the financial industry the situation is slow and acute. The banking sector has long been protected by the ministry of finance (MOF). The basic policy of MOF has been not to bankrupt major banks therefore they have been equally treated in financial policy matters regardless of performance, the so-called 'convoy-guard' method. Information was not disclosed to the public about the financial condition of banks but only between the banks themselves and MOF. Moreover foreign banks have not been permitted to operate in Japan for a long time. Consequently, markets also developed in a very distorted way. Bank lending heavily based on land collateral and not on business opportunities or performance became widespread. Therefore, banks faced enormous accumulated bad debts after land prices fell sharply and the economic bubble burst in the mid-1990s.

Over-loans (too much lending) dependent on high domestic savings through post office saving accounts as well as bank savings became a common phenomenon of corporate finance. Thus, direct finance was ignored and securities markets left underdeveloped. In particular, the cross-holding of stocks by conglomerates of big companies and banks slowed the development of individual stock holdings. Still at present, Japan's personal financial assets (approximately US$8,900 billion) are mainly held in the form of deposits/savings (53%), while the share held as securities represents a mere 12%. Such a low percentage of holdings in securities basically means that the development of the stock and equity markets has been left behind. For example, in the US the figure is almost exactly the opposite, securities (54%) and deposits/savings (12%). The coming financial reform, the so-called big bang, is aimed at liberalizing the sector and correcting the skewed financial markets in Japan. And, indeed, it is urgently needed, especially after several bankruptcies and failures of large security companies and banks (Yamaichi Securities, Hokkaido Takushoku Bank, and Japan Long-term Credit Bank).

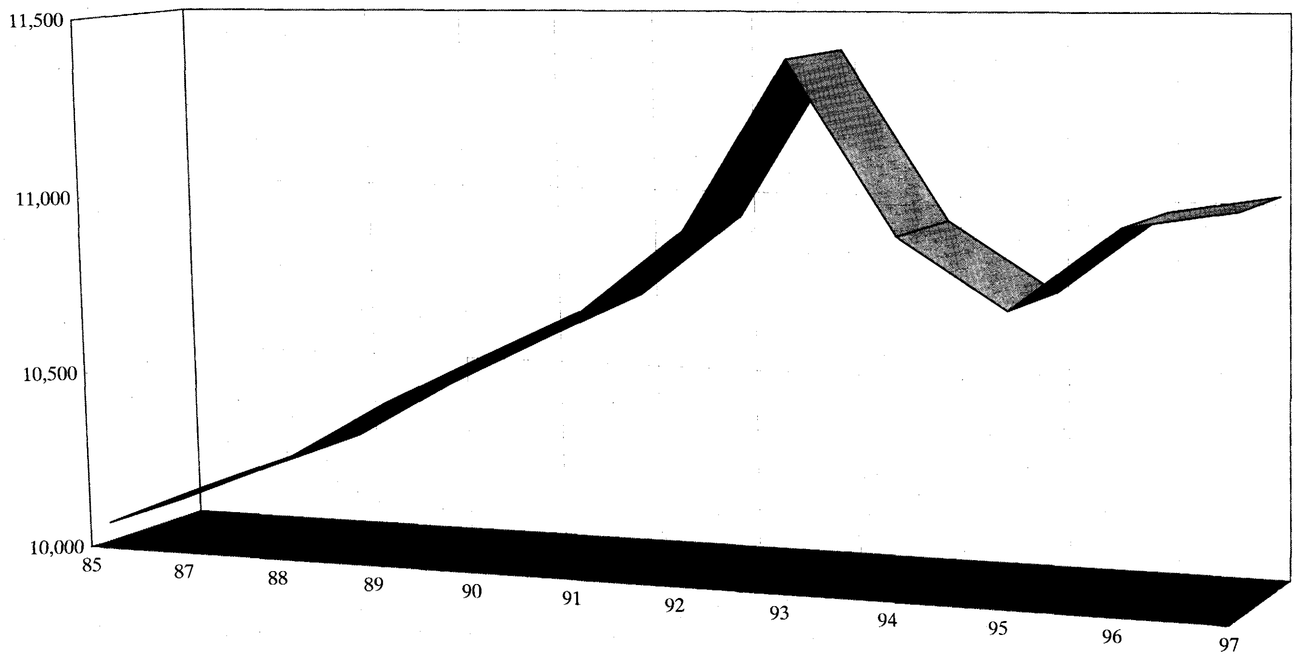
3.2.1. Present State of Permissions/Approvals

In Japan deregulation is occasionally considered as the reduction of the number of public permissions and approvals which laws[2] stipulate. Japan's efforts at reducing them are not good as far as the number is concerned. There were 10,054 permissions/approvals in 1985 but 11,032 in 1997, a net increase of 978. The number peaked at 11,402 in 1993 (see Figure 1.1).

Although such an increase is basically considered as reflecting social and economic needs (new diseases, environmental concerns, technological changes, etc.), it remains out-of-step with the world tendency toward market-oriented economies and global harmonization.

Ministerial distribution of permissions/approvals in 1996 showed that the ministry of international trade and industry (MITI) had the largest number 1,842, followed by the ministry of transport (MOT) 1,551, the ministry of finance (MOF) 1,469, and the ministry of agriculture, forestry, and fishery (MAFF) 1,405. Compared with 1985, only two ministries reduced their number (MOT 466 and MITI 28) while MOF and the ministry of health and welfare (MHW) were largely responsible for the increase in the number of regulations (MOF 353 and MHW 340) (see Table 1.3).

Figure 1.1: Evolution of the Number of Permissions/Approvals



Source: Management and Coordination Agency [1998], *White Paper on Deregulation.*

Table 1.3: Number of Permissions and Approvals by Ministry /Agency

	1997	1985	Increase/ decrease(−)
Prime Minister's Office	32	27	5
Fair Trade Commission	26	26	0
National Public Safety Commission	149	81	68
Management and Coordination Agency	35	29	6
Hokkaido Development Agency	31	26	5
Defense Agency	31	26	5
Economic Planning Agency	31	26	5
Science and Technology Agency	307	218	89
Environment Agency	210	149	61
Okinawa Development Agency	32	27	5
National Land Agency	87	81	6
Ministry of Justice	180	146	34
Ministry of Foreign Affairs	48	37	11
Ministry of Finance	1,469	1,116	353
Ministry of Education	345	310	35
Ministry of Health and Welfare	1,276	936	340
Ministry of Agriculture, Forestry and Fisheries	1,405	1,263	142
Ministry of International Trade and Industry	1,842	1,870	−28
Ministry of Transport	1,551	2,017	−466
Ministry of Posts and Telecommunications	303	265	38
Ministry of Labor	654	532	122
Ministry of Construction	863	742	121
Ministry of Home Affairs	125	104	21
TOTAL	11,032	10,054	978

Source: Same as Table 1.1.

3.3. Case Study: Privatization of State Enterprises

3.3.1. Japan National Railways (JNR)

According to the recommendation of the Doko Committee, Japan National Railways (JNR), the largest state enterprise in Japan, was divided into seven joint-stock companies in 1987, considering localities. Those were (i) the Hokkaido Passenger Railway Company (JR-Hokkaido), (ii) the East Japan Passenger Railway Company (JR-East Japan), (iii) the Central Japan Passenger Railway Company (JR-Tokai), (iv) the West Japan Passenger Railway Company (JR-West Japan), (v) the Shikoku Passenger Railway Company (JR-Shikoku), (vi) the Kyushu

Passenger Railway Company (JR-Kyushu), and (vii) the Japan Freight Railway Company (JR-Freight). The last one covers nationwide freight transportation while the others serve their own region (Fukui [1992]).

In addition, the Shinkansen Holding Corporation (which owns the Shinkansen bullet train properties and leases them to the three passenger railway companies in the mainland Honshu area), and the JNR Settlement Corporation were set up.

The JNR Settlement Corporation was established for management of debts, asset sales, and personnel handling. JNR's debt reached US$286 billion by 1986, of which US$197 billion in debt was inherited by the JNR Settlement Corporation, US$43 billion by the Shinkansen Holding Corporation, and US$46 billion by the three major JR passenger companies and JR-Freight. The JNR Settlement Corporation planned to repay US$91 billion by selling JNR's real estate and stocks while the outstanding US$106 billion was to be paid by the government (i.e., tax payers' burden).

In 1980 there were 414,000 employees in JNR. The number was reduced to 277,020 by April 1986 due to JNR's efforts at rationalization. Out of this total (277,020 employees), 6,300 retired and 46,410 found new jobs by April 1987. New JR passenger and freight companies absorbed 199,200 employees and other JR related companies 1,450. The remaining 23,660 persons were received by the JNR Settlement Corporation.

The JNR Settlement Corporation actually employed 2,510 and 21,150 workers needed re-employment. By April 1990, 20,100 had found alternative work and only 1,050 were dismissed because they refused to accept jobs introduced by the corporation. The great success of re-employment occurred at a time of expansive economic activity during the late 1980s and business as well as government support was forthcoming in efforts to employ them. Railway-related private companies employed JNR relocated workers, while central and local governments received them by providing special quotas.

JR stocks were not sold to the public at the beginning because new JR companies seemed not too profitable as well as being burdened with enormous debts. Listing on the Tokyo Stock Exchange needs certain requirements with respect to profits, dividends, and assets and some of the JR companies could not meet these requirements at first. Another factor which tallied against their listing was a stock price rhapsody. NTT stock, for example, was sold in 1986 but it turned out to be a nightmare for many share holders due to ups and downs of the stock price (from a peak of 3,180,000 yen per share in April 1987 to a trough of 453,000 yen in August 1992). Moreover, the government worried about criticism that JR would profit from its stock sale. Ultimately, JR-East Japan was listed on the Tokyo Stock Exchange in 1993 and sold firstly its government-owned stocks totaling 2,500,000 out of 4,000,000 stocks in October.[3] JR-West Japan was listed in October 1996 (sold 1,366,000 out of 2,000,000 stocks) and JR-Tokai in October 1997 (sold 1,354,000 out of 2,240,000 stocks) (see Table 1.4). It is estimated that the government got US$8.6 billion for the stock sale of JR-East Japan and US$3.8 billion for JR-West Japan.

Before privatization, there were three main labor unions in JNR: the National Railway Worker's Union (NRWU, 70% of JNR union members and under the General Council of Trade Unions of Japan or Sohyo); the National Motive Power Union (NMPU, 10% and under Sohyo and the Japan Socialist Party); and the Japan Railway Worker's Union (JRWU, 10% and under Domei and the Democratic Socialist Party). After privatization, NRWU continued to exist but its numbers dwindled while NMPU and JRWU formed a coalition called the Japan Confederation of Railway Worker's Union (called JR Soren) whose membership was around 135,000 or 74% of union members of the new six passenger and one freight railway companies. However, JRWU-affiliated members separated from JR Soren later. Coupled with the weakening of socialist political influence, the power of labor unions gradually declined.

Table 1.4: JR Stocks Held by the Government

(Thousands of stocks)

	When privatized 1987	First Sale		Present* (January 99)
JR-EAST JAPAN	4,000	Oct. 93	2,500	1,500
JR-TOKAI	2,240	Oct. 97	1,354	886
JR-WEST JAPAN	2,000	Oct. 96	1,366	634
JR-HOKKAIDO	180	-	-	180
JR-SHIKOKU	70	-	-	70
JR-KYUSHU	320	-	-	320
JR-FREIGHT	380	-	-	380
TOTAL	9,190		5,220	3,970

Note: * Japan's government holds JR stocks through the Japan Railway Construction Corporation.

Source: *The Nihon Keizai Shimbun* (The Nikkei Journal News), January 8, 1999.

3.3.2. Results of the JNR Privatization

After more than 10 years of experience, it is generally recognized that the privatization of JNR was a success. Services improved, facilities renewed, and train schedules became more reliable. Fares for the main Honshu Island companies were not raised except for some adjustments in line with the introduction of a national consumer tax (the fares for JR-Hokkaido, JR-Shikoku, and JR-Kyushu were raised in 1996).

As business corporations, the JRs became profitable, reduced costs and increased efficiency. It is also said that transport volume in terms of both passenger and freight augmented and labor productivity improved. Furthermore, public subsidies for the JRs decreased while corporate tax revenues from them increased and hence greatly contributed to government coffers.

The negative side of the story remains the heavy debt problem. The JNR Settlement Corporation has outstanding debt of US$224 billion as of March 1997. In particular, the sale of real estate was unsuccessful due to the land price deflation which followed the end of the so-called bubble economy. The corporation was dissolved in 1998 and the majority of its debt was transferred to the government. The burden (or misfortune) then fell on smokers. The government raised the cigarette tax (one yen for one cigarette) from December 1998 to repay the debt.

3.3.3. Nippon Telegraph and Telephone Public Corporation (NTTPC)

The Nippon Telegraph and Telephone Public Corporation (NTTPC) was privatized in 1985 and became the Nippon Telegraph and Telephone Corporation (NTT). NTT was listed on the Tokyo Stock Exchange in February 1986. NTT stock price soared to 3,180,000 yen per share in April 1987 but has declined since then. It is estimated that the government received approximately US$78.6 billion from the sale of NTT stock. The amount was mainly utilized for the redemption of government bonds (Takano [1992]). At the same time deregulation in telecommunications was carried out and private companies entered into this market. However, unlike the JRs, the new NTT was not split, thereby retaining a Gulliver-type monopoly in the sector.

There were about 310,000 employees in NTTPC in 1984. After privatization, competition forced NTT to seek efficiency and, as a result, more than 50,000 employees were fired by 1990.

The privatization of NTTPC and the subsequent deregulation in the telecommunications sector brought about drastic price reductions especially for long-distance and international calls. New common carriers (NCCs) participated in the long-distance call market such as DDI, TWJ, and JT. Subsequently, NTT had to reduce call rates per subscriber by approximately US$92 by 1990. Local call tariffs have not been changed due to the monopolistic nature of NTT. Because of rebalancing or cross-subsidization, low local call tariffs have been covered by high long-distance and international call tariffs. Local call tariffs in Japan are notably low by international standards. This is the main reason that NCCs can not enter the domestic local call market. On the other hand, long-distance and international call tariffs are still high even though there are new entrants. Introduction of the so-called price-cap system is planned for local calls, long-distance calls, ISDN and leased circuits in 1998 (Tsuji [1999]).

The ministry of posts and telecommunications (MPT) still wields strong control over NTT such as share holding (more than one-third), appointments of directors, approval of business plans, etc. This is an obstacle to the NCCs and restricts the development of a more competitive telecommunications markets.

The Committee for Government Reform recommended the division of NTT in 1995 and the related laws were amended in 1997. According to the restructuring plan, NTT will be transformed into a holding company under which two corporations (NTT East Japan and NTT West Japan) and five private companies are to be established (NTT Long Distance and International Calls, NTT Data, NTT DoCoMo Group, NTT Personal Group, and NTT Comware). NTT Data undertakes data transmission. NTT DoCoMo carries out cellular phone services while NTT Personal sells PHS-type phones. NTT Comware is a software company for the development of information and telecommunication software (Namikawa [1997]).

3.4. Features of Japanese Privatization and Deregulation

Fundamental changes in privatization took place in the middle of the 1980s. Four big SOEs were privatized (NTTPC, Japan Monopoly Co., Japan Airlines, and JNR). At the same time deregulation accelerated. Some features can be drawn from these experiences:

(a) Japan's privatization of public utilities such as NTTPC and JNR is incomplete. The government still has controlling power in terms of share holding, appointments of directors, price setting, and business activities.

(b) Privatization and deregulation processes are also at the half-way stage. The processes with regard to public utilities recognized as natural monopolies such as electricity, gas, water, and the Post Office have been delayed or even left untouched. The number of permissions/approvals by public authorities have not decreased. Generally speaking, there is agreement on safety and environmental regulations but not on business and commercial ones.

(c) The sales of SOEs directly helped government revenues. The government received US$78.6 billion for NTT, US$4.5 billion for Japan Tobacco Inc., US$8.6 billion for JR-East Japan, and US$3.8 billion for JR-West Japan sales. Corporate tax revenues also increased as privatized companies generally make profits.

(d) Long-term liabilities of SOEs have not been solved. For example, the JNR Settlement Corporation has left debts of US$224 billion which remains a huge burden for tax payers.

(e) Labor union power was greatly reduced. And, in the post-bubble period, a time of recession, its power has withered. The appearance of flexible employment systems has also weakened its power. This tendency has been further strengthened by the decline of political influence of the Japan Socialist Party as well as a global decline of socialism and communism.

4. SUGGESTIONS FOR DEVELOPING COUNTRIES

Merits of privatization and deregulation include cost and price reduction, increased efficiency with better business performance, improved services, increased customer satisfaction, and augmented government revenues.

Demerits comprise unemployment, reduced labor union power, the appearance of oligopoly or monopoly, foreign capital dominance, a threat to the existence of universal services, and bad debt problems.

Some lessons can be derived from the Japanese experience of privatization and deregulation for developing countries:

(a) Results of these policies (privatization and deregulation) depend on business cycles. During a boom period, dismissal of employees by privatized SOEs is easy and does not create serious social or political fallout because restructured companies can easily relocate or find alternative employment for workers who are made redundant. Stocks can also be sold at higher prices to repay SOEs' debts. However, the opposite happens during periods of recession. Thus, timing of these policies is of the utmost importance.

(b) Foreign capital dominance, the so-called Wimbledon effect, has not yet taken place in the case of Japan. When NTT was privatized, the NTT Corporation Law prohibited foreign ownership of shares. It was amended in 1992 and foreigners can now buy up to 20% of NTT shares. Japan's opening up is slow in this context. It is expected that the so-called big bang in the financial market will invite foreign capital into Japan. However, it has to be remembered, that hasty liberalization in East Asian financial markets created turmoil for those developing economies. The speed of deregulation is hence another issue to be considered. Gradualism with clear time schedules may be the best solution for certain developing countries.

(c) Technology advances very rapidly and global standards come from advanced countries. It is vital for developing countries to enhance absorptive or learning capacity to catch up with advanced technologies (In this context, see, for example, Kagami, Humphrey, and Piore [1998]).

(d) Firm but fair institution building for new liberalized systems is required and must be substantial. Especially, independent monitoring and controlling institutions such as fair trade commissions and banking supervisory authorities are necessary. In the case of Japan, vertically-split ministerial vested interests remain a hindrance to fair institution building. Nepotism, political influence as well as corruption should be avoided in developing countries.

Notes

1 In the program of the special corporations reform, our institute (IDE), was merged to the Japan External Trade Organization (JETRO) under MITI in July 1998. The Export-Import Bank of Japan is expected to merge with the Overseas Economic Cooperation Fund (OECF) in 1999.

2 Regulations are stipulated in the form of laws, acts, government decrees, ministry codes, and announcements.

3 In the case of JR-East Japan, its stock price hit the peak of 746,000 yen in September 1998 but has decreased since then to below 600,000 yen in January 1999. The government plans to do the second sale (the remaining 1,500,000

stocks) in 1999 but its sale may be delayed due to stagnant stock markets and recession.

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