

London takes aim at Japan, Inc.

Will Japan abandon the policies that made it an economic miracle? Second in a two-part series by Kathy Wolfe.

The stock market scandals which hit Japan's Nomura Securities in June have now escalated to threaten Japanese industry and banks. Japan's largest banks are about to be charged with making payoffs to customers, *Business Week* reported on July 22. Tokyo Sagawa Co., a major trucking company, fired its president, Hiroyasu Watanabe, on July 12. He was accused of financial deals with gangster Susumu Ishii, the same charges originally made against Nomura by British banker Robert Zielinski at Jardine Fleming.

Large Japanese investors now so fear a Tokyo market crash, that Japanese industrial corporations are being forced in a panic onto the London Eurodollar market to borrow money in order to produce. More than \$1 billion in Japanese corporate "equity-linked bonds" were floated in London in a single week, the London *Financial Times* bragged July 15. Nikon Corp. was forced to cancel plans to issue new stock in Tokyo on July 15. Japanese companies fear that less than half of the \$8 billion in stock issues they had planned for July and August can now be sold.

"For American investment bankers, the crackdown in Japan is welcome," *Business Week* gloated July 22. "For years they struggled to break into the Japanese banking business. Now the playing field for U.S. bankers and brokers in Tokyo is leveling. . . . U.S. brokers are upbeat about making inroads into the Japanese corporate market."

Behind the headlines, however, recent policy pronouncements by the Anglo-American elite show that Japan's financial system is under fire not for what it has done wrong, but for what it has done right: help create a productive *physical economy*.

On May 28, former Lehmann Bros. bank chairman Peter Peterson warned Wall Street that Japan will soon become to the United States, as the U.S. was to decaying Great Britain after World War II. Peterson, now chairman of the New York Council on Foreign Relations, said that something drastic must be done to stop Japan from continuing to produce and invest, while the U.S. becomes a scrap heap.

He recalled that by 1956, when Great Britain invaded Suez, U.S. President Eisenhower demonstrated that the U.S. was "top dog" by forcing the British to retreat militarily, or face a U.S.-run crash of the British pound. Japan, Peterson warned, precisely because of its industrial superiority, is now positioned to do this to the United States. (For his speech,

see *EIR*, June 28, 1991.)

Paul Summerville, chief economist for Britain's Jardine, Fleming office in Tokyo, told the *New York Times* of June 14 that the West should be particularly alarmed about the fact that during the 1980s, Japanese corporations poured "unprecedented sums of money into research, new technologies, and new factories." Now Japan is about to reap the benefits, with an entire new generation of technologies and cheaper, better products.

"The wave of Japanese exports that will come from that 1980s investment, will likely dwarf anything we've seen so far," warned Wall Street economist Jeffrey Garten of The Blackstone Group in June. Peter Peterson is chairman of The Blackstone Group.

'Window guidance' national banking

The heart of Japan's economic miracle is an "American System" of national banking, which *directs credit* toward investment in science, technology, and industrial production. These policies, such as "window guidance" by the Japanese central bank, were imported from the United States and Germany in the 19th-century Meiji Restoration. The concept of window guidance derives from Alexander Hamilton's credit program in his 1790 *Report on Manufactures*. Under it, the Bank of Japan encourages banks to make a certain proportion of total loans to production and science.

"American System" directed credit is emphatically not socialism. The key distinction is the freedom of the *individual producer*. Under the 18th-century British System, London merchant banks were "free" to buy tea from colonies, speculate up prices, and sell it back, because the British fleet backed them up with guns.

After the Revolution, Hamilton created the Bank of the United States, to ensure that *producers* got low interest rates on credit. Those producers, farmers and industrialists, were never told what to produce, or how. Speculators could get credit, too, but at higher interest.

While the U.S. abandoned directed credit long ago, the Japanese stuck with it until very recently.

Starting in 1978, however, when London's Hong Kong and Shanghai Bank demanded access to purchase U.S. banks, the Bank of England and its Washington branch, the Federal Reserve, invented "financial deregulation." The

Brits and the Fed drummed out a press campaign that all protective national bank laws in the United States, Japan, Germany, and especially in developing nations such as Mexico, Brazil, and India, were outmoded and restrictive. Elected officials who protected national banking were labeled "corrupt." Scandals such as the Lockheed affair were orchestrated to dump them.

In the United States, this resulted in the International Banking Act of 1978, the Omnibus Bank Bills of 1980 and 1982, and worse. Usury restrictions were removed, allowing interest rates to zoom from 5% to 20%. Americans now enjoy the results: the savings and loan crisis, 18% credit card debt, balloon mortgages, and a vast national debt.

Deregulation: 'financial AIDS'

In Japan, the Finance Ministry and central bank held to some Hamiltonian programs, but after 1980, they bent the rules enough to permit an influx of British and U.S. financiers into Tokyo. Led by Hong Kong and London's Jardine and New York's Salomon Brothers, they brought to Tokyo what Japanese officials call "financial AIDS."

The newcomers created new speculative vehicles such as short selling, new varieties of futures, real estate junk bonds, and other perversions popular in London and New York. Japanese brokers and banks jumped stupidly into the swim. Since Japan's central bank interest rates were incredibly low by U.S. standards—still only 2.5% in 1989—once the speculation virus got to Tokyo, it took over. Stock speculation zoomed.

Tokyo and Osaka real estate speculation rocketed too, driving land and housing prices out of sight. Japanese financiers had been content to get central bank money at 2.5% and make industrial loans at 5%, but with real estate loans paying 10%, productive lending fell behind.

In May 1989, Minister of Finance Ryutaro Hashimoto grew properly concerned. His reaction, however, fell right into the Anglo-American game: The Finance Ministry and Bank of Japan (central bank) began to *deregulate interest rates*. Hoping to deflate Japan's real estate and stock market bubble, by making money more expensive to speculators, they more than doubled the central bank's discount rate to 6%.

This, however, has hurt the Japanese host far more than the Anglo-American disease. Japanese brokers and banks, in a panic for profit, only went further into speculative stock issues, cutting back stock sale funds for industry. This bred fierce competition for clients, and backroom payoffs.

The problem is that interest rate deregulation is *usury*. Whereas under a Hamiltonian system, only speculators get hit with high interest rates, the Bank of Japan has hit everyone with high interest rates. This is precisely how Federal Reserve chairman Paul Volcker bankrupted the U.S. savings and loans in 1980: Suddenly, instead of paying 5% for money, S&Ls were paying 20%, but could not earn half that on loans.

Now Japan's commercial banks, the world's largest, are in the same boat and losing billions. The London *Economist*

reported June 15 that Japanese banks are now having to pay 8% to depositors because of high central bank rates for banks, but earning much less than that on industrial loans. The *Economist* added that the Japan stock market could collapse again soon, which will knock Japanese bank shares down below bankruptcy level. The *Economist* advised readers to dump Japanese bank stocks.

Falling into the trap?

The *Wall Street Journal* noted gleefully on June 26 that the Finance Ministry and Bank of Japan are continuing to fall into the *gaijin* (foreign) trap. To prove that his ministry has not been "colluding" with Japan's financiers, Finance Minister Hashimoto is removing the ministry from the markets by allowing further steps in deregulation:

- more interest rate decontrols;
- decontrol on bank lending;
- decontrol of foreign exchange markets;
- deregulation of "Article 65" (modeled on the American Glass-Steagall Act) which prevents cartelization of banks and brokerages.

Jardine Fleming's Robert Zielinski in the *Journal* that day demanded an increased "climate of deregulation, disclosure, and increased accountability."

The most foolish action of all, however, is the Bank of Japan's announcement June 27 that it plans to halt its "window guidance" program, and move to U.S. Fed-style "open market" operations. This will in fact have the opposite effect of what Hashimoto intends, and will lead to a major rise in interest rates and speculative lending.

The action is praised by bankers from Union Bank of Switzerland, Swiss Bank Corp, S.G. Warburg, and Phillips and Drew of London. "It's the logical end of the ambitious deregulation begun in 1984," says Jesper Koll of Warburg's Tokyo office. "They've almost fully completed deregulation of interest rates, so the next step, is that window guidance be abolished."

British and U.S. bankers are delighted that this will cut Japanese bank lending, especially since the Japanese banks are already being forced to curb lending to meet the Bank for International Settlements' tough capital-to-loan ratio regulations this year.

This is the wrong way to go. Japan had better think twice before it lets its economic miracle explode in a stock market bubble. Jacking interest rates up and down has never stopped speculation in any economy.

The only rational course is the one which has brought Japan to industrial growth in the first place: directed credit. The appropriate response would be to withdraw the June 27 plans to remove window guidance, and instead, to increase it, penalizing loans to speculation in particular, while lowering interest rates to industrial production. If London and Washington scream, they should be told to do the same and foster some useful production for a change.