

7 Neoliberal economic policy preferences of the 'New Left'

Home-grown or an
Anglo-American import?

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A political party supports the elimination of taxes on investment (such as the capital gains tax) and higher taxes on consumption. It favours aggressive deregulation aimed at introducing more competition into sheltered sectors of the economy. It supports free trade. It favors an aggressive approach to Japan's banking problems that would involve nationalizing most of the large banks, dividing them into 'good' and 'bad' parts, returning the good parts to the private sector, and disposing of the remaining assets at whatever price the market will bear. It favors the privatization of public corporations because of the role they play in propping up inefficient sectors of the economy. And it calls for the devolution of more powers to local governments, arguing that this will encourage localities to compete to make their communities attractive places to do business.

In any party system besides Japan's, a party that advocated positions like these would be considered a party of the Right. These are the policy positions of Thatcher, Reagan and Chirac. In Japan, however, they are advocated by the Democratic Party of Japan (DPJ), the leading opposition party competing with the long-ruling 'conservative' Liberal Democratic Party (LDP). Since the LDP is on the Right, the DPJ must be on the Left, right?

Once upon a time, during the extended period between 1955 and 1993 when the LDP faced the Japan Socialist Party (JSP) as its leading opponent, Left-Right labels based on economic policy made some sense. The LDP, like parties of the Right in most advanced industrialized countries, was in favor of capitalism and private ownership of the means of production. The JSP favored the nationalization of industry and redistribution of income from the rich to those in need. After the JSP imploded at the end of this period, however, Japan found itself with no party of significant size that fit the mould of a traditional party of the Left. After the Lower House election of 2000, the only parties that might have had a claim to this title, the Japan Communist Party (JCP) and Social Democratic Party of Japan (SDPJ), were left with only 20 and 19 seats, respectively. Only the DPJ, with 127 seats out of a total of 480 seats in the Lower House, was in any position to compete with the still-much-larger LDP. The Democrats were,

arguably, the 'New Left' of Japan, and yet they were advocating neoliberal prescriptions endorsed by parties of the Right in most other political systems.

How did this happen? How did Japan end up without a significant traditional party of the Left after delivering 30 per cent of its votes to the socialist and communist parties for 40 years? Everywhere, the collapse of the Soviet Union and the end of the Cold War delivered body blows to parties of the Left, but in most political systems the traditional parties of the Left emerged with only slightly diluted versions of their social-democratic platforms. The Italian Communist Party helped form several governments in the 1990s after re-labelling itself the Democratic Party of the Left; the Socialists in France stuck stubbornly to a traditional left-wing agenda and still managed to win some elections; and even in Britain and Germany, where the Labour and Social Democratic Parties declared themselves 'new' and more market-oriented, party leaders advocated what they called a 'Third Way' that continued to place social justice and social welfare near the top of their agendas. Why is it that Japan doesn't even have a Third Way? And what does this tell us about the state of Japanese democracy today?

This chapter takes a close look at the economic policy prescriptions of the DPJ and the process that produced them, seeking to explain why Japan's New Left has ended up embracing such a neoliberal economic reform agenda. As suggested by the title, I consider two possible explanations for this puzzling outcome. The first is the possibility that the Democrats' turn toward neoliberalism was caused by years of trade pressure and 'markets-are-best' lecturing by foreign (especially Anglo-American) economic officials. In a previous paper, I argued that such pressure has played an important role in causing economic elites (economic officials, opinion leaders, and some politicians) to focus on neoliberal economic reforms as the primary alternative to status quo policies blamed for the nation's prolonged period of economic stagnation.¹ It could be that this 'learning' process accounts for the Democrats' embrace of neoliberal economic reforms. The second possibility is that positions taken by the Democrats reflect a more 'home-grown' process, including the incentives of the party and electoral systems. My answer is that foreign pressure alone cannot explain what is going on. We also need to look at the political incentives motivating those joining and leading the DPJ.

The transition from the Old Left to the 'New Left'

The Japan Socialist Party is the focus of many other papers in this volume, so I do not need to dwell in detail on the decades it spent as leading opposition party to the LDP. While the party was most passionate about its views on security policy, supporting unarmed neutralism and opposing constitutional revision, it long subscribed to similarly radical views on economic policy.² 'The Road to Socialism' (*Nihon ni okeru shakaishugi e no michi*), its core

policy statement from 1964 to 1986, called for a 'peaceful revolution' and held up the Soviet model of socialism, rather than European social democracy, as its goal.³ Socialist leaders such as Itsurō Sakisaka (1897–1984) spoke of 'the desirability of continued class struggle, a democratic dictatorship of the proletariat, as well as the need for a centralized state that would own land and large industry'.⁴ On economic issues as well, therefore, the JSP was clearly a party of the Left.

While the party held tight to these views much longer than parties of the Left in most European countries, it began modifying its positions under Masashi Ishibashi in the mid-1980s and even enjoyed a brief renaissance under the leadership of Takako Doi later in that decade. The election of 1993 made it clear, however, that the JSP's best days were behind it. In that election, held after Kiichi Miyazawa's LDP cabinet collapsed over its failure to address public concerns over political corruption, the ruling party lost 52 seats, but the Socialists lost even more, falling from 136 to 70 (see Figure 1). The biggest beneficiaries of the LDP's troubles were a set of brand new centrist parties: the Japan New Party under Morihiro Hosokawa; Shinseitō under disgruntled LDP faction leader Ichirō Ozawa; and Shintō Sakigake, another LDP-breakaway group.

The election of 1993 ushered in a period of remarkable turmoil in the Japanese party system, with parties splitting, merging, and forming at a dizzying rate. For a brief period in the mid-1990s, it looked like Ozawa would succeed in welding together a disparate group of parties to make the New Frontier Party the new leading opposition party facing off against the LDP, but by the end of 1997 Ozawa's mega-party had collapsed, leaving another group of splinter parties in its wake. Shortly before the 1996 election a group of moderate Socialists joined a group of centrists from Shintō Sakigake to form the Democratic Party of Japan. This party was not big enough to contest elections in all parts of the country, but it came out of that election in a strong enough position to negotiate a merger with some of the NFP splinter groups in 1998, making the 'new' DPJ by far the largest opposition party. The party confirmed its claim to this role by winning 127 seats to the LDP's 233 in the 2000 election.

Because the Democrats were born out of this messy process, making sense of their strategies and public policy positions requires an understanding of where the disparate elements in the party came from. The original party, formed before the 1996 election, was made up of two distinct groups. The first was a group of young and urbane Diet members from Shintō Sakigake, led by Yukio Hatoyama and Naoto Kan. Sakigake had formed in 1993 around a nucleus of ten ex-LDP Diet members, including Hatoyama, who were later joined by various newcomers and party-switchers, including Kan (who came to the party from the small Social Democratic League). Relative to Ozawa and others who split from the LDP at the same time, this group of Diet members was moderate, especially on security issues, and derived much of their support from citizen activist groups. Kan, in particular, was

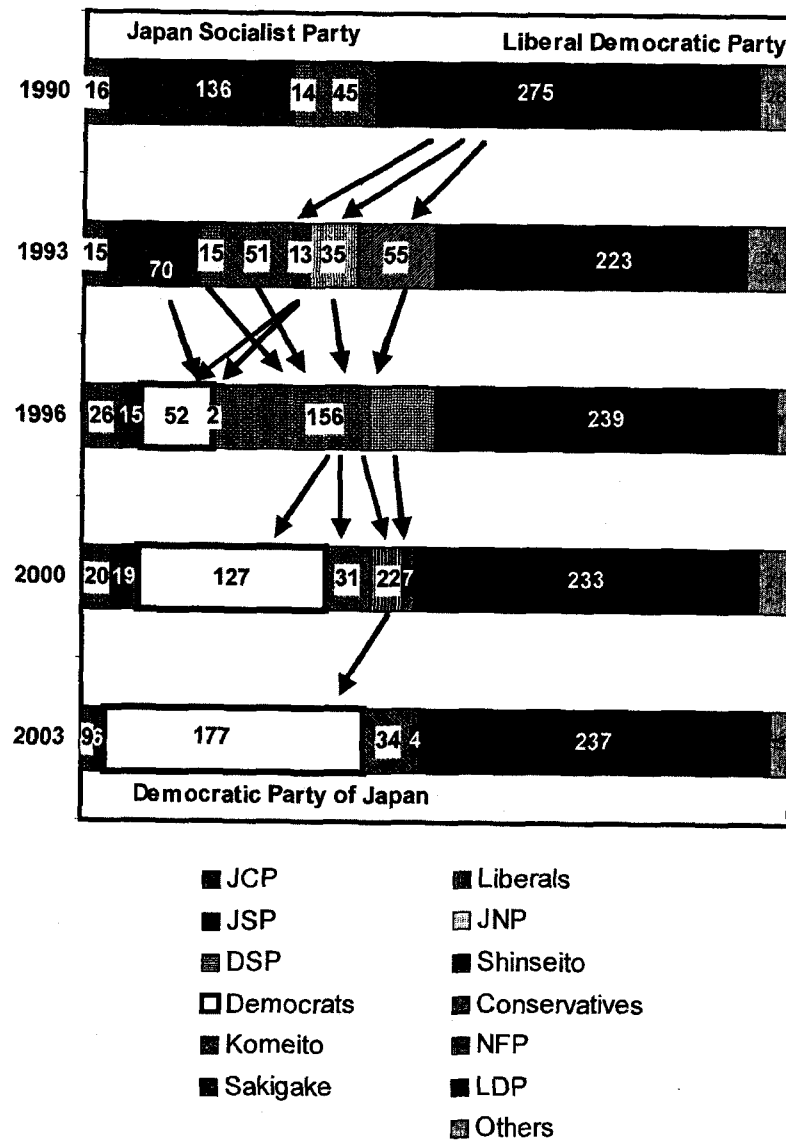


Figure 1 Lower House election results in seats, 1990–2003.

associated with this citizens' movement tradition and went on to make his name bucking Health Ministry bureaucrats who tried to cover up policy blunders that led to the spread of AIDS through blood transfusions. Hatoyama, the grandson of Ichirō Hatoyama, a former prime minister (1954–1956) and one of the founders of the LDP, brought a famous name and a large sum of money to the new party – which was known initially as the 'Hatoyama New Party'.⁵

The other component of the original DPJ was a group of moderate Socialists (the party was known by this time as the Social Democratic Party of Japan), led by former Hokkaidō governor Takahiro Yokomichi. The Socialists had entered a marriage-with-the-devil coalition with the LDP in 1994 under a deal that made their party leader Tomiichi Murayama prime minister (1994–1996) in exchange for his agreement to modify the party's long-standing opposition to the US-Japan alliance, the Self Defence Forces, and the use of the national flag and anthem in schools.⁶ By 1996, the party had alienated its base with these concessions while discrediting itself with urban swing voters by joining an LDP-dominated coalition. Facing the prospect of going into the 1996 Lower House election under these conditions, Yokomichi's group of moderate Socialists bolted from the party and helped form the brand new Democratic Party of Japan, hoping it would become a moderate Left party that could compete with the LDP for the new single member district plurality seats created under electoral reforms being used for the first time that year.

Despite the desperate conditions that surrounded its birth, the DPJ formed in 1996 was surprisingly coherent. Looking back on these early years of the party, Yokomichi claims that the original DPJ had 'quite a clear vision of what it wanted in the area of economic and social policy. It wanted a much less powerful central government. It wanted a shift of powers from the central government to localities, citizens' groups, and the market.'⁷ He explained that early priorities included decentralization of government functions, shifting more responsibilities to the local level, the privatization of some government activities, and social welfare reforms designed to draw on 'the vitality of the non-profit sector in the delivery of social services'. The agenda included elements that overlapped with neoliberal priorities, but its emphasis was on empowering *citizens*, not consumers or stockholders.

This original core of the DPJ was able to hold its own in the 1996 Lower House election, winning a total of 52 seats (20 seats for former socialists and 32 for centrists). That was not enough, however, to make the party the leading challenger to the LDP in the evolving party system. An opportunity to take up that role emerged only after Ozawa's New Frontier Party broke up at the end of 1997, leaving several splinter parties in its wake. DPJ co-leaders Hatoyama and Kan negotiated with leaders of these groups and relaunched the 'new' DPJ in 1998 with substantial additions that brought its seat totals in the Lower House to 95. The additions significantly changed the composition of the party, bringing in two more groups of politicians, some of them senior, and many of them with policy views quite different from those of the DPJ founders.

The first group was composed of relatively senior and conservative Diet members, led by former prime minister Tsutomu Hata, who had travelled a tortured path since 1993. Most had left the LDP that year with Ozawa, joining his Shinseitō and then following him into the NFP. Frustrated with Ozawa's personality and leadership style, however, a group of veteran politicians deserted him in late 1996 when they formed the Taiyōtō, which eventually combined with a larger group who left Ozawa when the NFP split in late 1997 to form a new party called Minseitō. Minseitō then merged with the Democrats in 1998. A measure of party system instability at the time was a campaign poster I saw in the Diet office of Tetsundo Iwakuni on a visit there in 2000. Iwakuni had been elected for the first time in 1996 as a member of Ozawa's NFP. After the NFP broke up, he could not leave up a campaign poster showing that party affiliation, so he placed a sticker over it showing his new party. By the time I saw it in 2000, the poster had four layers of stickers on it. Other new members of the DPJ who travelled similar routes had changed parties six times since 1993!

What distinguished this Minseitō group from the original DPJ were their more conservative views on security policy and economics. Some were strong supporters of constitutional revision and a larger security role for Japan. As we will see below, others were strongly committed to neoliberal economic reforms. Because of their seniority and willingness to leave the party if they did not get their way (these threats were quite credible since they had left so many already), they carried a great deal of weight in the 'new' DPJ.

The final faction joining the DPJ also came out of the NFP but was associated with the old Democratic Socialist Party (DSP) – the party long supported by private sector unions. Like Hata and his associates, the DSP had thrown their lot in with Ozawa, but after the NFP broke up they formed a separate group known as Shintō Yūai. Like the Minseitō group, these politicians tended to be more conservative on security issues than the original core of the DPJ. Their views on economics were mixed, favouring market forces in principle but frequently opposing liberalization measures that threatened the job security of their union member supporters.

Economic policy views of the Democrats

Not surprisingly given the diverse origins of the four DPJ factions, the party has not had an easy time coming to a consensus on its policy views. It has been plagued from the beginning, in particular, by public disagreements over the issue of constitutional revision and the deployment of Japanese troops overseas. In 2000, after party leader Hatoyama suggested the party might support constitutional revisions to make it clear that Japanese personnel could participate in United Nations 'peace-enforcement' activities, the leader of the ex-Socialist faction, Yokomichi, threatened to push for Hatoyama's resignation as party leader if he did not stop making such statements.⁸ In the fall of 2001, when party leader Hatoyama backed Prime Minister Koizumi's

plan to authorize the deployment of Japanese naval forces to the Indian Ocean, Yokomichi went even further. He and 27 DPJ compatriots voted against the Anti-Terrorism Law, abstained, or absented themselves from the vote, in open defiance of party discipline.⁹ Such battles have contributed to the DPJ's image as a divided party, a reputation that has cost it votes at election time.

Although DPJ internal battles over economic issues have not been so heated, the party has developed a reputation for being divided over these issues as well. Steven Vogel, for example, points to the different support bases of the DPJ factions and argues that 'the new Democratic Party is just as riddled with internal contradictions as the [New Frontier Party], and even more ambivalent about deregulation'.¹⁰ Citing DPJ leader Naoto Kan's assertion that his party needs to become 'the party of Thatcher and Blair', Gerald Curtis points out the contradictions inherent in such an undertaking.¹¹ I do not deny that such divisions exist, and I discuss some of them below. What I find more striking than the divisions, however, is the degree to which the party has staked out official party positions that are to the neoliberal *Right* of the LDP on a whole host of economic issues. That ex-Socialists sometimes object to these positions is not surprising. What is surprising is the degree to which they have ultimately gone along with a party strategy that has taken them not just closer to the LDP position (as is the case on security issues) but to the *other side* of the LDP on these economic issues.

The party has been most unified in its support for the neoliberal position on public spending. The DPJ opposes 'wasteful public spending' and favors measures to restore fiscal balance. Prior to the 2001 Upper House elections, for example, the party made 'reform of public finances' one of its top priorities in its manifesto, pledging to cut public works spending by 30 per cent and restore the budget to primary balance (no new borrowing beyond that needed to refinance old debt) in five years. It even went so far as to pledge to do away with the government tradition of adopting supplemental budgets whenever the economy showed signs of slowing. The DPJ would reserve such budgets, it said, for emergencies like natural disasters and financial crises.¹² The party had run on a similar promise prior to the 2000 Lower House election, when it pledged a 20 per cent reduction in public works and a reduction in the public debt to GDP ratio from 123 per cent to 60 per cent over the next decade.¹³

Needless to say, this policy is well to the right of the usual position of parties of the Left on fiscal policy. Rather than advocating the use of fiscal policy as a tool of Keynesian demand management, the DPJ has consistently argued that this tool needs to be discarded. Instead, it has called for the government to be put on strict timetables for public works spending cuts and debt reduction that virtually guarantee fiscal policy will exacerbate recessions and increase unemployment.

Closely related to the party's position on fiscal balance has been its support for a smaller central government, with its calls for the privatization of public

corporations and decentralization of government functions. Let us look at each of these positions in turn. In contrast to the mainstream of the LDP, which has defended public corporations and the fiscal investment and loan plan (FILP) that has channelled postal savings, postal life insurance, and public pension money to these politically-connected institutions, the DPJ has campaigned for a clean up of this system since its founding. It has argued for transparency in the accounting systems used by the public corporations to make it clear exactly how large the annual public subsidies are, and in its party manifesto issued before the 2001 Upper House elections called for the government to sell its remaining shares in NTT along with its stakes in public and special corporations.¹⁴ The following line from this manifesto is particularly striking: 'The DPJ will introduce appropriate private sector methodology and know-how to the public sector, to improve public sector efficiency and transparency, as was done successfully in the UK.' Margaret Thatcher's policies of the 1980s appear to be the model the DPJ has in mind!

Even where the public sector remains involved in providing services, the DPJ has argued, a much larger share of power should be devolved to regional and local levels of government. As discussed above, this emphasis on decentralization began with the original core of the party in 1996. Even Socialists like Yokomichi, who had experience dealing with heavy-handed central bureaucrats when he was governor of Hokkaido, were enthusiastic proponents of devolving power to the local level. By 2001, with the addition of the Minseitō and Shintō Yūai contingents to the party, views on this issue had coalesced to the point where the DPJ placed decentralization at the very top of its policy agenda. 'The DPJ believes that local services are best provided locally', the party manifesto reads. 'Issues that cannot be handled by individual prefectures are best handled at the regional level. Accordingly, a lean and more flexible central government should deal only with issues affecting Japan as a whole, such as diplomacy, defense, and monetary policy.'¹⁵

While decentralization advocated in these terms sounds admirably democratic, elaboration on the motives for this policy by Akira Nagatsuma, a newly elected DPJ member who was formerly a business journalist, makes it clear how it is connected to the neoliberal reform agenda:

One of the party's top priorities is decentralization by reorganizing government into eleven states. This was our number one promise in the last election. These units should have taxing power and the power to decide regulations. The central government would be radically shrunk. It would set a 'civil minimum' (doing some redistribution across regions and setting up a safety net below which no one would be allowed to fall), but the rest would be up to the states. If one of them wanted to lower wages, reduce regulations, and lower taxes to attract business, it could. It could compete with China for manufacturing business. The problem in Japan is that everything is made uniform across prefectures, so local areas cannot develop the means to compete and attract jobs and industry.¹⁶

Decentralization, Nagatsuma explains, will create structural incentives that encourage localities to cut taxes, lower wages, and relax regulations to attract jobs and business. It will no longer be necessary to fight these issues out at the national level, where interest groups and bureaucrats block moves to remove regulations. By devolving responsibility to local governments, reformers will be able to rely on regulatory competition between localities – described by public choice scholars as 'market-preserving federalism' – to accelerate the pace of liberalization.

If the DPJ's advocacy of small government is somewhat surprising in view of positions traditionally taken by parties of the Left, the positions the DPJ has taken on tax policy make one wonder if the world has turned upside down. Tax policy was one area of economic policy where the old Socialists actually had an impact. Throughout the period of LDP dominance, they defended the progressive structure of the income tax system tooth and nail. Taxes on capital were preferred to taxes on labour, and they fought pitched battles against LDP efforts to introduce the regressive consumption tax. Given this history, the positions the DPJ has taken on tax policy are positively baffling.

Prior to the Lower House election in 2000, DPJ leader Hatoyama made the party's plan to lower the minimum threshold above which residents are required to pay income tax one of its top priorities. The Japanese income tax system at the time was quite progressive by international standards because of the high level of income one needed to earn before one was required to pay the tax. Hatoyama proposed lowering the threshold as a way of broadening the tax base to produce revenue he argued was needed to shrink the government's massive fiscal deficit. His advocacy of this policy meant, however, that the party was proposing to raise the bulk of this new revenue from moderate-income citizens. In response, Shizuka Kamei, the chair of the LDP Policy Affairs Research Council, pointed out the regressive character of the proposal and claimed '[the LDP] will never hike taxes, targeting the socially weak alone'.¹⁷ Which of these parties is the party of the Left?

The party was more divided during the most recent debate over tax reform, begun after LDP Prime Minister Koizumi announced that this would be a priority of his administration. Because of these divisions, it failed to produce a coherent alternative package of reforms, but it nevertheless was able to come to an agreement on a set of tax cut proposals that were designed in a way that would have delivered most of their benefits to better-off segments of the Japanese citizenry. It proposed to eliminate the capital gains tax on stock dealings for a limited period of time and proposed to make interest payments on mortgage and educational loans deductible from income for the purposes of calculating income tax.¹⁸

Some of the tax reform plans backed by segments of the DPJ were even more regressive. The plan authored by Iwakuni called for a series of reductions in taxes collected primarily from wealthy citizens (the complete elimination of the capital gains tax; a reduction in the gift tax to 20 per cent for a period

of two years; and a reduction in the land-holding tax), to be offset by a gradual increase in the consumption tax up to the level of 10 per cent. Iwakuni's plan was backed by 44 DPJ members of the Lower House, including Yokomichi and several other ex-Socialists.¹⁹

On most of the economic policy issues discussed up to this point, the DPJ has been able to stake out positions without actually having to put them into practice. It has not yet participated in any ruling coalition or cabinet, and sceptics will no doubt question whether the party would be able to retain unified party support for its 'tough' neoliberal positions were it to be faced with the prospect of actually implementing policies opposed by redundant workers and firms threatened with bankruptcy. Therefore the DPJ's policy on how to deal with the Japanese banking crisis is probably the best test of where the party stands on economic issues, for this is one area where it actually helped decide government policy.

The highpoint in the DPJ's participation in economic policymaking came shortly after the party won an unexpectedly large victory in the 1998 Upper House elections. Party leader Naoto Kan was riding on a wave of popular support after this impressive showing, and he took the lead in coordinating opinions of a block of opposition parties (including Kōmeitō and Ozawa's Liberal Party) that held the votes needed to block passage of legislation in the Upper House. While the DPJ was not invited to join the LDP-only cabinet that was in place at the time, the party's control of votes in the Upper House and the LDP's need to pass legislation of some kind to deal with the impending collapse of the Long-Term Credit Bank gave Kan and the DPJ more policymaking power than they had ever enjoyed – or have enjoyed since.

The party used its power to block legislation the LDP had proposed to deal with the weak condition of the Long-Term Credit Bank (LTCB) and other large financial institutions. Convinced that a collapse of mega-banks like these could be avoided, the LDP was proposing that the government continue propping up weak institutions by helping to arrange for mergers with stronger institutions – rewarding banks willing to take on weak partners with capital injections financed with public funds. Legislators in the DPJ were convinced the LTCB was too big and too broke to be dealt with in this fashion, and they worried that with many other mega-banks in similar straits, a collapse of the LTCB could trigger a system-wide financial crisis with implications for global markets.²⁰

With these concerns in mind, they drafted an alternative non-cabinet bill that was designed to recapitalize the Japanese financial system with a massive sum of public money while imposing strict conditions on banks receiving this capital to assure that the problems in Japan's financial system would not reemerge at a later date. Strict audits were to be conducted to determine banks' actual capitalization levels after accounting for bad loans. Those institutions determined to have zero or negative capitalization levels were to be turned over to a Japanese equivalent of the American Resolution and Trust Corporation (RTC) – the body created to clean up the Savings and

Loans mess – which would dispose of bad loan assets and set up 'bridge banks' with the remaining assets that would be sold off to the highest bidder. Those banks in danger of failing, with low but positive capitalization levels, were to be forced to accept involuntary injections of capital through forced sales of bank shares to the government – 'temporary nationalization'. At that point, the government would again strip out the banks' bad loans before putting the now-healthy institution back on the market.²¹

DPJ leader Kan stood firm in his negotiations with the LDP and forced Prime Minister Obuchi to accept most of the terms of this bill, including agreement that the LTCB would be dealt with as a 'failed bank' with its assets sold off to another bank.²² This package of legislation, known as the Financial Revitalization Law, was passed with DPJ support on 2 October 1998. In a last-minute manoeuvre, however, Obuchi was able to undercut much of the purpose of the DPJ-backed legislation by passing a second set of laws two weeks later – with the support of Ozawa's Liberal Party and Kōmeitō who abandoned the opposition coalition Kan had created to make a deal with the LDP that would eventually bring both of them into the cabinet. Under this Early Strengthening Law, weak banks that had not fallen below key capitalization thresholds were allowed to opt for 'voluntary recapitalization', making available public subsidies without the strict conditions of the DPJ-backed legislation. A key concession by the DPJ on its own law, allowing banks to avoid strict audits, combined with the provisions of the LDP's second set of bills to allow banks to take public money without strict conditions – guaranteeing that the banking problems would resurface at a later date.²³

What is interesting about the position the DPJ took on banking legislation when it actually held the power to make policy is that it stuck to its guns and supported the neoliberal 'hard landing' approach to resolving the nation's financial problems. It was willing to force banks to write off bad loans even though it was clear this policy would lead to the bankruptcy of many firms and layoffs of workers. Alone among the major political parties, it opposed legislation designed to extend public money to banks in a way that would allow them to continue propping up struggling borrowers.

In the period since its brush with power, the DPJ has continued to call for this neoliberal solution to the nation's banking problems. In its 'Final Plan for Financial Reconstruction', issued in January 2002 after it became apparent the earlier rounds of recapitalization had not solved Japan's banking system troubles, the DPJ again calls for forced injections of public funds into weak banks to achieve temporary nationalization. It further proposes that 'big companies requiring monitoring and worse' be turned over to the Resolution and Collection Company (RCC), with the assets of the weakest of these firms sold off within a year.²⁴ These positions continue to put the DPJ to the neoliberal right of the LDP mainstream on banking reform, and probably to the right of Koizumi given his unwillingness to follow through on his rhetoric in this area.

While the party was united in 1998 when it pushed for a hard-landing approach to the nation's banking problems, the intervening years have revealed enough additional information about the likely impact of these policies to raise opposition within the party. The compromises the DPJ has had to make to accommodate these views can be seen in the provisions of the party's 'Final Plan' dealing with bad loans to small and medium-sized businesses. The RCC should distinguish between struggling large firms and struggling small ones, the DPJ advises, giving the smaller firms 'the opportunity for self-reconstruction, holding off on direct write-offs'.²⁵ Interviews with a number of DPJ Diet members in December 2002 confirmed that the party is split over how to deal with the nation's banking problems.

However, even those who oppose the hard-landing solution (such as Yokomichi and Iwakuni) support market-based solutions. The Iwakuni plan mentioned above calls for the banking problem to be dealt with through a system of convertible bonds designed to create a 'stockholder democracy'. They suggest that instead of recapitalizing banks with tax money and forcing them to write off bad loans immediately, the government should give banks cash in exchange for half of their holdings of stock (no picking and choosing, the government would take half of everything, at market prices). It would then raise this cash by turning around and selling principal-guaranteed convertible bonds to the public, including foreign investors. Five years later, investors could exchange these bonds for their face value, plus 1 per cent annual interest, or they could accept the underlying stock. The plan appeals to those worried about the hard-landing approach because it would give banks and firms five years to work things out, but its effectiveness rests on the hope that the bond sales would create a nascent 'stockholder democracy' that would demand that the banks and firms use this time to fix their problems: write off bad loans when this is necessary, forgive them when not.²⁶

That even this last plan, put forward by the wing of the DPJ opposed to a hard landing approach to banks, puts its faith in 'stockholder democracy' and relies on convertible bonds to raise funds from investors is a measure of how far the Left has come since the socialist days. When placed alongside the DPJ plans for tax reform, fiscal reconstruction, decentralization, and privatization of public corporations, the party's plans for the banking system reveal the degree to which neoliberal ideas have penetrated this 'New Left' party's thinking about how to fix Japan's economic problems. Let us now consider the question of why this perplexing turn of events has come about.

Home-grown or an Anglo-American import?

On first glance, the overlap between DPJ positions on economic issues and the positions taken by American economic officials over many years of bilateral economic discussions suggests that there is a cause and effect relationship between the two. The DPJ's 1998 proposals for addressing the nation's banking problems, for example, echoed the suggestions of US Deputy

Treasury Secretary Larry Summers, who in May and June of that year had urged Japan not to prop up its weak banks. These proposals were also applauded, and abetted, by foreign financial firms in Tokyo.²⁷ There is similar overlap between foreign demands and DPJ positions favouring selling the state's remaining shares in NTT and privatizing other public corporations. A few DPJ positions not discussed above, including the party's support for 'competition in the area of public utilities in order to rectify the high-cost structure ... and promoting more penetration of foreign capital into the Japanese market', are virtually verbatim repetitions of advice Japan has received from the OECD and US government officials.²⁸

Overlap of this kind, however, does not necessarily mean foreign demands are the direct cause of the DPJ's neoliberalism. One reason to be sceptical comes from repeated party statements emphasizing that the DPJ does not want to bring 'American-style capitalism' to Japan. In a 2002 *Ronza* article, for example, four young DPJ members begin an article in which they advocate aggressive bank reform and tax cuts of the types summarized above with the following statement:

The problems our nation faces today cannot be solved with a simple-minded notion of a 'small state'. We do not stand in favor of market fundamentalism, which says the state should do absolutely nothing. President Bush came to Japan and addressed the Diet by saying 'competition is fundamental', but this American-style market fundamentalism is exactly what we feel needs to be rethought.²⁹

The policies they support in the article are mostly consistent with Anglo-American neoliberalism, but the DPJ politicians nevertheless are repelled by the example of US capitalism and do not seem to have been attracted to these policies by their respect for George Bush's advice.

I heard similar comments from DPJ politicians I interviewed, often without any prompting from me. Akira Nagatsuma, for example, brought up the subject of American pressure in his very first comments after I began asking him about his economic policy preferences. He emphasized that Japan needed to 'break from its dependence on American pressure' and 'needed to think for itself, decide for itself'.³⁰ Other Diet members pointed out that it was American pressure that got Japan in the fiscal mess it was now in. In 1998 when Japan's financial crisis threatened to disrupt the global economy, the United States had urged Japan to use fiscal policy to stimulate its economy. The result was an orgy of public works spending by the LDP that put Japan deeper into debt without fixing its economic problems.

These last comments point to a crucial area in which the DPJ's policy preferences do *not* overlap with the demands they have been facing from the United States, the IMF, and foreign capital. Whereas the DPJ has advocated spending cuts, debt-reduction targets, and increased taxes on income and consumption in order to reconstruct Japan's public finances, foreign pressure

has consistently called on Japan to adopt stimulative fiscal policy, especially during its recent period of prolonged economic stagnation. Even the monetarist Reagan and Bush administrations have been surprisingly Keynesian when it comes to Japan's fiscal policy, urging tax cuts and public works spending increases on a regular basis since 1984. The fiscal conservatism of the DPJ, certainly, cannot have been caused by American pressure since the United States has been urging the opposite.

If we are to identify the roots of the New Left's neoliberalism, therefore, we need also to consider the domestic political context in which the DPJ has had to operate. The most fundamental feature of that context, which has shaped the way the DPJ was born and every move it has taken since, has been the dominance of the Liberal Democratic Party. The LDP was there first. It had superior numbers of incumbents, access to the resources that flow to the ruling party, and connections to many organized constituencies. The party had also staked out an established position in 'policy space', the terrain defined by the issues voters and politicians care about. The DPJ could not just move in and set up shop wherever it wanted. It had to work around this 800-pound gorilla.

Throughout the period of the '1955 Party System' (1955–1993), the policy space in which parties staked out positions was defined by the dominant cleavage over security policy. It was this issue that voters cared most about, and it was this one that defined the 'Left-Right' conflict between the Old Left and the LDP. Voters and politicians cared about economic issues as well, but over time the established parties of the Left and Right all came to support Japanese-style capitalism, with its extensive *informal* system of social protection. This system channelled public works spending to construction firms, which made sure contractors across the country stayed in business and provided jobs in job-poor rural areas. It propped up farm incomes through subsidies and protectionism. It upheld a lifetime employment system that protected a large proportion of workers, including many blue-collar workers, from the risk of layoffs. And it used regulations to manage supply and demand in industries ranging from retail to finance to provide firms with the support they needed to live up to their employment commitments and keep paying their small-business suppliers. Since this system was built under LDP rule, the party naturally supported it strongly. But the Old Left supported it too since it provided unionized workers with a fair measure of job protection and helped the small farmer and the small businessman. No party campaigned on a plan to dismantle this system.

This consensus on economic policy was disrupted by the collapse of the bubble, the banking crisis, and the government's deteriorating finances. Suddenly there was room to challenge the LDP on economic policy, and policy space was transformed into a two-dimensional arena. In this new policy space, the LDP maintained its position in support of Japanese-style capitalism, with its extensive system of informal social protection. Although few said it at the time, over the course of the decade more and more Japanese have

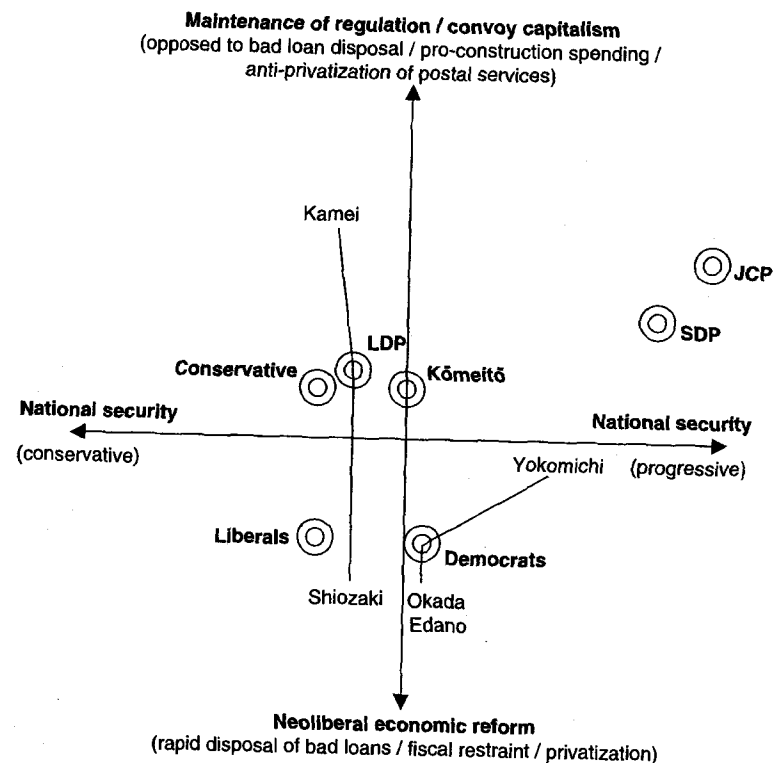
come to identify the LDP as 'the Communist Party of Japan' because of its support for the weak sectors of the economy.³¹ Since the dominant party had occupied this position in the debate, parties that wanted to take on the LDP had to stake out alternative positions from which to challenge it.

At this point the Japan Socialist Party was still the largest opposition party, and if it had been nimble enough, it might have been able to manoeuvre in such a way as to benefit from this opportunity. It could have defined the alternative to the LDP's Japanese-style capitalism as Swedish-style liberal social-democracy, with its *formal* system of social welfare programmes cushioning the impact of market forces that are allowed to operate much more freely than in Japan. Advocating this position would have required the JSP to support market-orientated liberalization (including labour market reform) along with a major expansion of social insurance programmes. Unfortunately, the JSP was not nimble enough to pull this off. It remained too obsessed with the security policy debate and too wedded to unions (that preferred lifetime employment to Swedish active labour market policies) to consider supporting this kind of programme. In 1992, as the economy began its long slide into stagnation, JSP legislators were taking a final stand against the LDP's *security* policy, cow-walking in futile protest against Miyazawa's plan to authorize sending Japanese personnel on United Nations peacekeeping missions.

The JSP's failure to redefine the economic policy debate in this way left the door open for new parties to step into the vacuum. Searching for a way to critique the LDP's economic policy, they naturally settled on the neoliberal line of argument, which had already established a track record in Japan under the patronage of LDP politicians who attempted to use it to advance their political careers. The ideology got its first tryout in the 1980s under Prime Minister Nakasone, who was impressed by the examples of Reagan and Thatcher and saw political opportunities in bringing this programme to Japan. Later in that decade, Ichirō Ozawa, then LDP Secretary General, again drew on this ideology when he wrote his 'Blueprint for a New Japan'. Both Nakasone and Ozawa were direct targets of many lectures by US economic negotiators, who counselled them on the virtues of competition and market forces. While this experience may have helped put neoliberal ideas in front of them, their decision to adopt this framework as a basis for critiquing the established political economy cannot be understood without appreciating how it fit into their political calculus. Both hoped to use it to appeal to urban salaried workers, the New Middle Mass.³²

By the time Sakigake, the Japan New Party, and later the Democrats set out to locate their own challenge to the LDP, therefore, the terrain had already been mapped and slogans tried out. With the LDP having resisted Nakasone's and Ozawa's attempts to shift the party's base, the party was more dependent than ever on its core constituencies – the farmers, the construction industry, and small businesses. Their example suggested that political opportunity lay in appealing to urban salaried votes with promises to cut pork barrel spending, clean up government finances, and make the economy

more efficient. Even the original core of the Democrats, the moderate socialists and Sakigake citizens' activists, were drawn into challenging the LDP with a promise to shift power from the central government to localities, citizens' groups, and the market. Once they did so, they attracted a host of eager young politicians who believed in this rhetoric and sought to make the party platform much more specific (see Figure 2 below).



Method: Security policy positions are based on chart in Ikuo Kabashima, 'An Ideological Survey of Japan's National Legislators', *Japan Echo*, August 1999, p. 14. Positions on neoliberal reform for parties based on surveys of Diet members reported in Ikuo Kabashima Zemi (ed.) *Gendai nihon no seijika zo*, Vol 1, Tokyo: Bokutakusha, 2000; and Junko Kato and Michael Laver, 'Research Note: Party Policy and Cabinet Portfolios in Japan, 1996', *Party Politics*, 4:2, 1998, 253-260, along with recent policy positions taken by parties and individual politicians, some of them discussed in this paper.

Figure 2 Two-dimensional positioning of parties and key politicians (2003).

The figure above shows how the LDP and DPJ have yet to develop unified positions on economic issues. The core of each party, however, has aligned on opposite sides of the 'economic reform' dimension, with the LDP (despite

Koizumi) continuing to delay banking reform, fiscal reconstruction, and privatization of the postal finance system. Meanwhile, the DPJ has settled (despite Yokomichi) on the neoliberal side of this divide. While the party system continues to evolve and may see more splits and mergers before this paper comes out in print, the processes set in motion by the decision of the DPJ to locate on the neoliberal side of the LDP is now self-reinforcing, virtually guaranteeing that the main party competing with the LDP for the foreseeable future will be attacking it from its right on economic issues.

The self-reinforcing process can be seen at work, first, in the DPJ's response to Koizumi's attempt to steal much of the DPJ's economic reform platform. When Koizumi upset the political world by openly campaigning against his own party in 2001, adopting many of the DPJ's reform proposals, the DPJ moved further in the neoliberal direction rather than attempting to stake out a new (social democratic?) position from which to challenge Koizumi. It went from calling for a 20 per cent reduction in public works to calling for a 30 per cent reduction. It attempted to put forward a tax reform plan that was more pro-business than Koizumi's. As Koizumi has compromised on many of his reform promises, the DPJ has called him on it, ridiculing him for his abandonment of his promise to limit deficit spending and criticizing his banking policies for being too lenient on banks and debtors. Once a new party stakes out a direction from which to challenge the established dominant party, it cannot easily change strategies.

Second, the self-reinforcing process can be seen in the way the DPJ has grown since it was founded. Having staked out a position as the neoliberal party relative to the LDP, it began attracting neoliberal candidates to run for open seats. This process began in 1996 when the original DPJ recruited a large class of new young Diet members to run for open seats and continued when the 'new' DPJ recruited another large class to run in the 2000 election. By 2001, there were a total of 66 DPJ Diet members in the Lower House (out of a total of 125) who had not run under any of the four parties that made up the original party union. This large contingent of newcomers, with few attachments to the founding parties, dwarfed all of these groups. By 2001, there were just 20 DPJ members of the Lower House who had originally been members of the Socialist Party, and just 14 who had run under the Sakigake banner. (See Table 1 for a complete list of members and groups.) When the DPJ held its leadership contest in 2002, the leader of the ex-Socialists, Yokomichi, came in fourth on the first ballot and was outpolled by Yoshihiko Noda, who came in third after stepping forward to represent the large bloc of newcomers.³³

What is interesting about the new faces recruited by the DPJ is how different they are from the types of individuals recruited by the Old Left parties. Six of them were former bureaucrats of the elite ministries, with two each from Finance, Foreign Affairs, and Trade and Industry. Three were bankers with the most elite Tokyo financial firms (see Table 2). Because of their elite backgrounds and rich experience, these new members were given policy influence way beyond their level of seniority. These were the men the party turned to in

Table 1 Democratic Party of Japan membership in the Lower House (total of 126 as of November 2001)

Former Social Democrats (20 members)	Former Minseitō (20 members)
Kanju Satō (10 terms)	Kōzō Watanabe (11 terms)*
Ichirō Hino (8)	Tsutomu Hata (11)
Takahiro Yokomichi (7)	Hajime Ishii (10)
Chūji Itō (5)	Michihiro Kano (9)
Hidenori Sasaki (4)	Hiroshi Kumagai (6)
Yoshino Hachiro (4)	Takao Satō (5)
Akihiro Ōhata (4)	Katsuya Okada (4)
Ritsuo Hosokawa (4)	Ikuo Horigome (4)
Taneaki Tanami (4)	Issei Koga (4)
Hirohata Akamatsu (4)	Kiyoshi Ueda (3)
Ryū Matsumoto (4)	Shigefumi Matsuzawa (3)
Kenji Nakazawa (4)	Kōichi Yoshida (3)
Mamoru Kobayashi (4)	Osamu Fujimura (3)
Tsutomu Yamamoto (4)	Shinji Tarutoko (3)
Masanori Gotō (4)	Eiji Nagai (3)
Motohisa Ikeda (3)	Masaru Nakagawa (2)
Yoshito Sengoku (3)	Kimiaki Matsuzaki (2)
Miyoko Hida (UH-1, LH-2)	Tetsundo Iwakuni (2)
Nobutaka Tsutsui (2)	Kazuhiro Haraguchi (2)
Yutaka Kuwabara (2)	Ban Kugimiya (UH-1, LH-1)
Former Sakigake (14 members)	Former Shintō Yūai (10 members)
Naoto Kan (7 terms)	Kansei Nakano (9)
Yukio Hatoyama (5)	Kazuya Tamaki (7)
Tadamasa Kodaira (4)	Eisei Itō (6)
Kenichirō Satō (4)	Tatsuo Kawabata (5)
Kōichirō Genba (3)	Keishū Tanaka (4)
Yukio Edano (3)	Yoshiaki Takaki (4)
Kō Tanaka (3)	Yasusuke Konta (2)
Sakihito Ozawa (3)	Masamitsu Jōjima (2)
Kōki Ishii (3)	Satoshi Shima (2)
Seiji Maehara (3)	Setsuya Kagita (2)
Seiichi Kaneta (3)	
Satoshi Arai (2)	
Fumihiko Igarashi (2)	
Hiroshi Kawauchi (2)	
Other (62 members)	
Masamitsu Ōishi (5)	Akira Nagatsuma (1)
Ryūichi Doi (4)	Kōichi Katō (1)
Kenji Kitabashi (4)	Ikuo Yamahana (1)
Banri Kaieda (3)	Yukihiko Akutsu (1)
Takashi Kawamura (3)	Shigeyuki Gotō (1)
Yoshihiko Noda (2)	Gōshi Hosono (1)
Yukio Ubukata (2)	Yasutomo Suzuki (1)
Hirofumi Hirano (2)	Yoshio Maki (1)
Yoshikatsu Nakayama (2)	Yūkichi Maeda (1)
Yoshinori Suematsu (2)	Kenji Kobayashi (1)

Shū Watanabe (2)	Hisako Ōtani (1)
Motohisa Furukawa (2)	Takeaki Matsumoto (1)
Shōichi Kondō (2)	Hideo Hiraoka (1)
Hirofumi Hirano (2)	Yorihisa Matsuno (1)
Jun Hayama (2)	Kakio Mitsui (1)
Muneaki Samejima (2)	Zenjirō Kaneko (1)
Eiko Ishige (2)	Toshiaki Koizumi (1)
Ken Okuda (2)	Hitoshi Gotō (1)
Seishū Makino (2)	Akira Ōide (1)
Satoru Ienishi (2)	Nobuhiko Sutō (1)
Azuma Konno (1)	Kazuo Inoue (1)
Sayuki Kamata (1)	Hirosato Nakatsugawa (1)
Hiroko Mizushima (1)	Eriko Yamatani (1)
Kōichi Takemasa (1)	Yutaka Banno (1)
Atsushi Ōshima (1)	Takeshi Yamamura (1)
Atsushi Kinoshita (1)	Shōgo Tsugawa (1)
Hisayasu Nagata (1)	Kazunori Yamanoi (1)
Hisako Ōishi (1)	Tetsuji Nakamura (1)
Yōichirō Esaki (1)	Osamu Yamauchi (1)
Jin Matsubara (1)	Toshimasa Yamada (1)
Yoshio Tezuka (1)	Kinya Narasaki (1)

* Watanabe Kōzō was nominally independent because he resigned from the party to serve in the Diet leadership

Source: Compiled by author based on data in Kokusei Jōhō Sentaa, *Shitte okitai kokkai giin no ugoki*, 2001. Thanks also for assistance from Diet Librarian Tarō Kawashima.

1998 when it needed to draft its own legislation to deal with the banking crisis, a team that included first-term member Furukawa, fresh from the Ministry of Finance. They were the ones who staffed the committees that drew up the party's new 'Final Plan' for the banking system, its Economic Revitalization Plan, and its New Strategy for Industrial Revitalization. Katsuya Okada, a former Trade and Industry official with just four terms in office, took over as Secretary General of the party in 2002 and was selected party leader in 2004.

Table 2 Recently elected DPJ members coming from financial sector and elite ministries

	<i>Background</i>
Motohisa Furukawa (2)	Ministry of Finance
Tetsundo Iwakuni (3)	Merrill Lynch (VP)
Takeaki Matsumoto (1)	Industrial Bank of Japan
Hisayasu Nagata (1)	Ministry of Finance
Akira Nagatsuma (1)	Nikkei Business
Katsuya Okada (4)	Ministry of International Trade and Industry
Sakihito Ozawa (3)	Bank of Tokyo
Yoshinori Suematsu (2)	Ministry of Foreign Affairs
Toshimasa Yamada (1)	Ministry of International Trade and Industry
Tsuyoshi Yamaguchi (1)	Ministry of Foreign Affairs

Source: Compiled by author using *japanesepoliticians.com* database (accessed 14 May 2003).

Iwakuni, a former Vice-President of Merrill Lynch, was made party vice-president after just two terms in office. Sakihito Ozawa, a three-term Diet member who was once with the Bank of Tokyo, was made shadow minister for Trade and Industry in 2002.

Another large contingent of newcomers came to the DPJ from the Matsushita Seikei Juku, a school for young people aspiring to enter politics that indoctrinates its graduates with views quite different from those of politicians who were attracted to the parties of the Old Left. The school was established by Kōnosuke Matsushita, the founder of Matsushita Electric, who is reported to have set up this operation in hopes of training a new generation of politicians who would bring business values and management training to government. *Asahi Shimbun* reporter Shinichi Yamada describes Matsushita graduates as advocates of smaller government, deregulation, and competition in an open market. They are committed to bolstering the power of politicians over the bureaucrats who have traditionally dominated the policymaking process in Japan.³⁴ As Table 3 shows, there were 11 Matsushita graduates among the DPJ's Lower House membership by 2003. Their similar age and common experience in the training school made them another coherent bloc reinforcing the DPJ's neoliberal orientation. These members have also been able to move quickly into leadership positions, with Noda challenging party veterans for the leadership of the party in 2002 and Maehara taking over as the shadow cabinet member for defense the same year.

In 2003, shortly before the most recent Lower House election, this process through which the neoliberal orientation of the party has attracted new members who share this perspective received its most recent reinforcement as the DPJ absorbed Ichirō Ozawa's Liberal Party and added 18 new members, many of them veteran Diet members and all of them to the neoliberal right of the LDP on most economic issues. It is difficult to predict how this

Table 3 Young DPJ members who are graduates of Matsushita Seikei Juku

	Age on 14 May 2003
Koichirō Genba (3)	38
Kazuhiro Haraguchi (2)	43
Seiji Maehara (3)	41
Jin Matsubara (1)	46
Shigefumi Matsuzawa (3)	45
Hiroyuki Nagahama (2)	44
Yoshihiko Noda (2)	45
Satoshi Shima (2)	45
Kōichi Takemasa (1)	42
Shinji Tarutoko (3)	43
Kazunori Yamanoi (1)	40

Source: Compiled by author using *japanesepoliticians.com* database (accessed 14 May 2003); and *Christian Science Monitor*, 15 August, 2002, p. 6.

process will play out in the coming years, but whether the DPJ grows slowly by adding new members over a series of elections or absorbs additional groups of Diet members who are cut loose in future rounds of party splits, the pattern we have observed up to this point suggests it will become more neoliberal over time.

Conclusion

Despite the diverse origins of the Democratic Party of Japan's membership and some disagreements over economic policy positions, the party is coalescing around an economic reform agenda that is distinctly neoliberal. In almost any other party system, a party like the DPJ that opposed the use of fiscal policy to fight recession, called for tax increases on moderate-income citizens while urging cuts in capital gains taxes, and pressed for a get-tough policy with banks that threatened to cause widespread corporate bankruptcy and a spike in the unemployment rate, would be regarded as a party of the Right.³⁵ Yet in Japan it represents the main alternative to the 'conservative' LDP.

The focus of the paper has been on the forces that lay behind the New Left's move to the neoliberal Right. While American trade pressure and lecturing by foreign officials, combined with the examples of Margaret Thatcher and Ronald Reagan, played a role in placing neoliberal ideas in front of party politicians, the structural context in which new parties had to operate also played a critical role. Faced with an '800-pound gorilla' in the form of the LDP defending a system of Japanese-style capitalism that provided a large measure of social protection for weak segments of the economy, the new parties that preceded the DPJ, and later the DPJ itself, all decided that neoliberal reform had the potential of attracting votes from disgruntled urban salaried workers. Once the party launched its challenge from the right of the LDP on economic issues, the trajectory of its rhetoric, its recruitment of new candidates, and its prospects for growth through party mergers all pushed it further toward the neoliberal Right.

The implications of the developments highlighted here for Japanese democracy are stark. Japanese voters face the prospect of having to vote in elections in which both of the largest parties, the only ones that can succeed under an electoral system that awards the bulk of its seats through first-past-the-post rules, are parties of the Right. The LDP may offer a measure of social protection, but the protection this system can provide is steadily eroding under the weight of mounting public debt and a fragile banking system. More and more workers face the prospect of unemployment even if they vote to keep the LDP in power because the system the LDP supports is unsustainable. Meanwhile, the only electorally-viable alternative Japanese voters are presented with on their ballots is a party that promises to *accelerate* the collapse of Japanese-style social protection, with only meagre and vague promises to replace this system with formal welfare programmes. Until Japanese voters are given the option of voting for a liberal social democratic

party that has prospects of actually winning some elections, Japanese democracy will be unable to remedy a situation in which 50 per cent of voting-age citizens report that they support *none* of the established political parties.

Notes

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- 33 *Yomiuri Shimbun*, 24 September 2002.
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- 35 The DPJ's positions supporting environmental regulation, fighting for freedom of information, defending human rights, and calling for an increase in spending on unemployment insurance are more consistent with positions taken by parties of the Left in other systems. I focus on its positions on fiscal policy, tax policy, public corporations, and banking because these are the issues at the top of the economic policy agenda in contemporary Japan. On all of them, the party comes down on the neoliberal Right of the LDP.

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