hence undermines his own claims at generality. Furthermore, he does not
discuss examples of powerful unions. Nowhere does the conservative Nis-
san union garner attention, despite its incontrovertible power.3 Public en-
terprise unions receive little mention. In fact, his example of a successful
minority union at Hiroshima Railway comes from a sector where members
paid dues directly to the regional union organization, not to its constituent
enterprise unions. That the strongest part of the book is a study of an
industrial union is ironic, given the book’s title. It is, however, sympto-
matic of an overall difficulty in extending any of Kawanishi’s findings be-
yond the confines of his specific examples.

Japanese Financial Markets and the Role of the Yen. Edited by Colin
McKenzie and Michael Stutchbury. Allen & Unwin and The Australia-
Japan Research Centre, Australian National University, North Sydney
Unequal Equities: Power and Risk in Japan’s Stock Market. By Robert
246 pages. $21.95.

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McKenzie and Stutchbury’s Japanese Financial Markets and the Role
of the Yen and Zielinski and Holloway’s Unequal Equities analyze the origins
and consequences of the dramatic changes in Japan’s financial markets dur-
ding the 1980s. The former is an edited series of conference papers pre-
sented in Australia in 1987. It gives a succinct yet relatively detailed his-
tory of the restrictions imposed on Japanese financial institutions and
markets and how they were liberalized under external and internal pres-
sures. The focus is on the international effects of Japan’s economic poli-
cies, capital flows, and the yen’s internationalization. The chapters are
rather technical since the papers were written by economists and regulators
for other experts. Nevertheless, several important unifying themes emerge
based on expectations that Japan’s liberalization will continue, its financial

delightful account of the pyrrhic victory management obtained when it replaced its radical
union with a conservative one. See also the account in Michael Cusumano, The Japanese
Automobile Industry: Technology and Management at Nissan and Toyota (Cambridge, Mass.:
markets and institutions will become closely tied to global markets, and traditional differences are eroding. The papers are well researched and contain useful data on changes in capital flows, global finance, and the liberalization chronology.

The Zielinski and Holloway book, also well researched and a good source of data on stocks, stock issuance, stock holdings, shareholder relationships, and the securities industry, offers an interesting contrast because it is an integrated work written for a popular audience. It is complementary, dealing with the same period and many similar themes. Further, its perspective is the stock market and equity investors as opposed to government policy and international economists. By reading Unequal Equities, one can fully appreciate the origins and extent of Japan's stable shareholding system under which almost 70 per cent of shares is now held by corporations of which over 40 per cent are owned by financial institutions. In addition to interlocking ownership, these companies have numerous other business relations. Thus low stock dividends cannot be viewed as these shareholders' total return. Particularly, it gives an excellent explanation of the main bank's role as a shareholder and investor. This neatly supplements Sheard's conference paper analysis in the McKenzie and Stuchbury volume of the main bank as insurer and monitor of the financial system. However, the authors' purpose is to show the Japanese stock market's irrationality compared to the United States and the benefits bestowed on special business and political interests. Also, the high price/earnings ratios (P/Es) resulting from the restricted supply of stock because stable shareholders do not sell have hurt the individual investor and give Japanese companies an unfair advantage because U.S. companies must raise capital at market rates, i.e., lower P/Es.

The first volume presents the larger institutional and policy framework within which the shareholder system, the stock market, and equity-linked financing operate. From this perspective, the conference papers agree that Japan in the 1980s moved from a heavily restricted environment to an increasingly more liberal system. Key changes involved the Foreign Exchange Law's "permitted in principle" basis followed by the Yen-Dollar Accord and a liberalization in interest rates. These changes allowed companies to raise funds abroad and banks and insurance companies to become major international lenders, enabling Japan to become the world's leading creditor while the United States became its major debtor. Because of Japan's large savings relative to investment, surpluses and capital exports were expected to continue, confirming Tokyo as the third major center in the global financial market after London and New York. Hong Kong and Singapore would also benefit as regional extensions given the growing presence of Japanese banks and the region's economic expansion. The yen would evolve as a more widely held international currency at least for
investment and financing purposes. The book thus tracks the accepted wisdom of the time.

Within this context Japanese banks appeared very powerful, and yen assets were in great demand, especially after the 1985 Plaza Accord. Rapid yen appreciation caused large losses for Japanese holding dollar securities. Since Japan's bond market was not fully liberalized and available financial assets remained limited, Unequal Equities notes surplus money migrated into stocks and land. Since the supply of land and stock was restricted, prices rose dramatically, fueling each other as shares were valued for hidden stock and land values, and stock profits were invested in land. Banks expanded loans based on land and equities as collateral while their capital bases increased as well based on their 'hidden' appreciated stock. Companies and banks not making operating profits reported securities gains and issued new capital or equity-linked debt to raise investment funds. This upwardly spiraling market finally ended abruptly in January 1990 as the Bank of Japan tightened interest rates and squeezed real estate loan limits.

Unfortunately, the Zielinski and Holloway story stops here, and the conference papers never anticipated this crash as they were prepared prior to even the October 1987 crash. Thus, both books have been overtaken by events which in their magnitude and import seriously alter many of the authors' assumptions. At the same time, several issues either not addressed or downplayed have emerged as being quite significant. Three seem especially noteworthy for the 1990s. First, as noted in the Bank of New Zealand's paper in the McKenzie and Stutchbury collection, Japanese imports have traditionally been dollar-denominated, and there appears no tendency for this to change since importers expect a stronger yen. Foreigners then cannot earn yen and are reluctant to create yen liabilities. So Japanese lenders must generate yen foreign assets via the exchange markets, contributing to more upward pressure on the yen. For this situation to reverse, Japan must open its markets to more imports, reducing appreciation expectations. This does not appear likely to happen soon, restricting development of a yen block similar to NAFTA or the EEC. Rather, most Asian countries complain about market access to Japan and sell in dollars. Further, since the region runs a surplus with the United States, these countries feel comfortable creating dollar liabilities. Yen will therefore be held mostly as exchange assets rather than for intervention. The small, short-term yen government bill market only strengthens this scenario.

Second, the collapse of the stock market has forced Japanese banks to retreat as global lenders, and Hong Kong has emerged as the main Asian center of the global financial market since the dollar remains the transaction and lending medium of choice. Japanese financial institutions appear to be just another source of funds. In addition, Hong Kong, because of its favorable regulatory, logistical, and tax environment, has turned out to be
the best place to do third-party business, an essential ingredient in developing an international financial center. The Ministry of Finance has also become disenchanted with liberalization as it has realized the consequences of losing control over financial markets or the yen. It has thus substantially slowed the process and in some cases, such as the futures market, has moved backward. Meanwhile the U.S. bond market has not collapsed as the Federal Reserve has been able to more than replace departing Japanese investors. The Fed has even expanded the U.S. money supply and lowered interest rates with little or no inflation. In sum, the inevitable internationalization and liberalization of Japan's financial markets as well as several underlying political economic assumptions are now in question.

Third, the rapid development of the futures markets, and especially the role of stock index futures in both accelerating the "bubble's" collapse and in destabilizing the stable shareholder system, was completely ignored. Stock index futures, once introduced in 1987, could be created in any volume and could be bought and sold by stable shareholders to hedge their positions without selling any underlying shares. Those who created the futures would offset their exposures in the market. The net result was the potential supply of an unlimited amount of stock that undermined the critical demand/supply equation so carefully documented by Zielinski and Holloway. If the stable shareholder system no longer restricted supply due to the ability to buy and sell the index, then prices would drop accordingly. Further, prices would not return to previous levels even with restored demand. While the addition of equity-linked bonds with warrants and convertible bonds affected the demand-supply equation, it was futures that undermined traditional shareholder stability. Finally, because it was the foreign subsidiaries of Japanese financial institutions that bought many of the bonds and equities issued abroad by Japanese corporations, the end of the main bank and stable shareholder systems documented by Sheard was somewhat overstated. It would appear that financial relations have been exported via foreign direct investment in the same way firms have exported other keiretsu relationships.

I was also struck by one other aspect common to both books which, given the authors' expertise, is puzzling. In both cases, they generally expect Japanese financial institutions and regulations to become more like those in the West, especially the United States. The convergence theory remains strong even among such knowledgeable analysts. However, given Japan's economic success, including its ability to weather the recent crash with little or no international repercussions, why should one expect Japan to follow our lead? The U.S. stock market is no more rational than theirs. We have themes where all companies in a sector go up or down in response to some event like Clinton's remarks relative to health care and pharmaceutical stocks. The leaders in some industries also sell at lower multiples than
the laggards. J P Morgan is currently at 9 compared to First Interstate's 14. There are wild gyrations in value within a few months even among established companies—witness Chrysler's move from $8 to over $40 in less than a year. Further, even allowing for the recent crash, the Japanese market has created much greater shareholder value for individual investors as well as for the stable shareholders who gain from other business relations. Similarly, its higher investment rate, higher growth rate, and appreciating currency have enabled Japan to undertake a massive public improvements program at a time when U.S. federal, state, and local governments are all under severe fiscal pressure, and the highway program and schools face serious financial difficulties.

These books are well researched and give a cogent well-reasoned analysis from an international perspective of the events leading up to and through the financial liberalization of the 1980s as well as the emergence of the "bubble." However, both reflect accepted ideas at the time they were written and especially concepts of international institutional and market convergence. Subsequent events of historical importance, though, have changed the business, political, and economic context. Therefore, other factors may now be more important for predicting the future evolution of Japan's markets, financial institutions, the yen, economic policy, and most importantly, major corporations. As such, despite their recent publication, they represent economic history more than a compass for the future.