

**June 9, 1996**

## **Riches to Rags**

**By Jeffrey E. Garten**

THE WEIGHT OF THE YEN How Denial Imperils America's Future and Ruins an Alliance. By R. Taggart Murphy. 352 pp. New York: W. W. Norton & Company. \$25.

One day in 1985, when I was living in Tokyo and running the Asian investment banking operations of Shearson Lehman Brothers, I was visited by James D. Robinson 3d, the chairman of American Express, our high-flying parent company. Mr. Robinson asked us to figure out how high up in the rankings of Japanese corporations -- as measured by size -- Amex could get if we had a virtually limitless budget and bought whatever financial companies could conceivably be for sale. Three months later, after feverish research on our part, Mr. Robinson returned for the answer. Making wildly optimistic assumptions, I said, we could be the 47th largest financial company in Japan. My boss was not happy.

Those were the days when the value of the land in Tokyo and its three surrounding prefectures was estimated to exceed the value of all the property of the United States. The Industrial Bank of Japan -- the country's classiest bank -- was valued at 18 times that of J. P. Morgan, its closest American counterpart. Japan was becoming the largest lender to the world, and its stock market value was approaching 40 percent of the combined value of all stock markets around the world.

Today, of course, the landscape looks a lot different. The Japanese economy has been on the ropes for most of the 1990's. The banking system is in shambles, mired in bad loans and scandals and requiring a bailout on the order of \$400 billion. Many of Japan's trophy investments, like the purchase of Rockefeller Center, have turned sour. The once-revered civil service mandarins who directed Japan's amazing rise to power are demoralized and in disarray. Not long ago, the riot police were seen in the halls of Japan's Ministry of Finance protecting employees from an angry public.

This riches-to-rags story is the subject of "The Weight of the Yen," by R. Taggart Murphy, an investment banker living in Japan. He starts with a description of the unique features of the Japanese political and economic system that created such enormous surpluses of money for Japan to lend or invest abroad. Mr. Murphy reports, as one example, how the Government discouraged consumer purchases at home with high prices and strangling regulations. At the same time, it pushed companies to make up for lack of Japanese demand by exploiting markets overseas. The combination resulted in anemic levels of imports, enormous amounts of exports and mountains of cash to lend to other countries.

The most interesting part of the story, however, is why the Japanese economy tanked. Mr. Murphy's central point is that Tokyo's civil service drove the country into crisis out of an unwillingness to recognize that the Government's ability to control the economy was no

longer feasible in a world where Japan's international trade and financial links had grown so extensive. When Japan's economy began to sag, Mr. Murphy says, the bureaucrats propped up the stock market by ordering Japanese companies to increase purchases of shares. Such purchases were made easier because the Bank of Japan -- Tokyo's Federal Reserve -- flooded the economy with low-cost money. Then the Government allowed banks to cook their books to avoid huge write-offs on old debts gone bad. It all worked for a while, but, under the glare of international scrutiny, especially from nervous investors around the globe, the house of cards collapsed. A far better course, Mr. Murphy implies, would have been to change Japanese economic fundamentals by, for example, deregulating the economy and releasing consumer demand, and by disclosing the banking crisis earlier and addressing it before the pressures became so severe.

Mr. Murphy's single biggest culprit in this sad story is Japan's civil service, particularly the Ministry of Finance. He explains how this unbelievably powerful department -- combining as it does the functions of our Treasury Department, Securities and Exchange Commission and Office of Management and Budget, and often having a

de facto veto over even the prime minister's decisions -- arrogantly misused its clout. The author is quite emotional on the subject, with descriptions of "rampaging bureaucrats" and analogies between the Ministry of Finance and the uncontrollable Japanese military of the 1930's. One of his policy prescriptions is a dismantling of the ministry itself, a highly prescient recommendation given that serious high-level debate on this very course of action has begun in Tokyo in recent months.

For the most part, "The Weight of the Yen" is a fast-paced account of an important part of the late 20th century. While its cursory advice for everything that ails Japan and America, thrown in at the end, detracts from the story, the book does provoke the question "What happens now?"

Mr. Murphy implies that current problems notwithstanding, Japan is still a powerhouse. In this he is dead right. These islands still account for two-thirds of East Asia's economic activity. Economic growth is stirring again. Companies like Toyota and Fujitsu are strategically investing outside of Japan, particularly in the highly dynamic emerging markets from Seoul to Jakarta. And a new prime minister has recently been put at the helm, one whose vast experience and powerful personality could well provide the leadership for Tokyo to turn the corner fast.

The challenges to America are every bit as daunting as they were in the 1980's, and they will continue to center on finance and commerce. Japan will still be a major lender to us and to the world. Confrontations over trade are sure to continue into the next century, about everything from intellectual property rights to aircraft landing rights. But compared with the last decade, Japan will be more preoccupied with its own internal affairs than with Japan-United States relations. It will focus on modernizing its political system, on deregulating its economy and on defining its interests without its traditional deference to American views. It will loom very large in our foreign policy because of its global importance, but also because of its lack of responsiveness to American goals. On several

occasions, Mr. Murphy bemoans the way Tokyo and Washington mishandled their alliance these past 10 years. His account is likely to be a prologue to the even greater turbulence in the Washington-Tokyo alliance in the years ahead.