CHAPTER 1

The Motivation to Cooperate, Lead, and Follow

Financial crisis management comes in various forms, including emergency financial resources (rescue packages) and intervention of public institutions (the IMF or creditor governments) to influence the behavior of the market one way or another and restore international financial stability. Globally, such crisis management is important to avoid further repercussions and international financial disasters. It may thus be considered an international public good.[1] In the last two decades, the IMF has usually been in the forefront of international financial crisis management, but the IMF lacks coercive power, particularly against private creditors, and it fails to maintain sufficient funds to deal with crises on its own.[2] Thus, the active involvement of various financial actors, especially major creditor governments, becomes imperative. Several factors, however, make state actors reluctant to take up this role.

The first disincentive discouraging collective action in crisis management comes from the very nature of a public good and the problem of funding supply, considering that some entity or entities have to shoulder the costs of public goods. A public good is a good that cannot exclude noncontributors from enjoying the benefit of added funds. In these circumstances, the incentives to free ride are high; so are the disincentives to contribute. Although crisis containment aims to provide international financial stability at critical moments, the fungibility of added liquidity through bailout operations makes creditors reluctant to commit their funds.[3] In addition, uncertainty regarding the payoff from crisis management leads to noncontribution. Major creditor governments that want to stabilize debtor economies and improve their external balance might emphasize the global repercussions and systemic risks arising from a crisis. However, there is always the suspicion that a creditor government may be promoting the "public good" of international financial stability while actually trying to secure its own "private goods" in the forms of direct economic payoffs and political gains. This suspicion is even stronger when creditor governments are concerned about their relative gains vis-à-vis other governments, which discourages active involvement.[4]

The second factor that discourages state actors from becoming involved in active cooperative management are the uncertainties and criticisms associated with the impact of financial crisis management involving rescue packages. Some conservative critics of financial rescues argue that rescue operations by public institutions (creditor governments and the IFIs) create a typical moral hazard problem. Bailouts invite moral hazard problems for debtors as well as for lenders and investors.[5] Uneasiness and uncertainty also arise because of multiple perspectives on the desired modality of financial crisis management and crisis solutions.[6]

The third and quite obvious factor discouraging involvement is that government actions might invite taxpayer resistance. Financial rescue packages or extensions of loan repayments provided by governments require additional financial commitments to countries with financial problems. Rescue packages are provided either in the form of direct participation using the country's official funds (bilateral) or in the form of increased capital contributions to IFIs, such as the IMF and the World Bank (multilateral). In many countries, taxpayers in general object to financial bailout packages designed to help debtors, especially when taxpayers have no strong affinity or commitments to the debtors. They also object to assisting investors from their home country who, in the taxpayers' view, misjudged their investments. In turn, when asked to increase their financial commitment to problem debtors, private financial institutions wanting to exit promptly and with as little loss as possible from bad loans and risky investments also resist cooperating with creditor governments.

Finally, because of the tendency toward regional concentration of various economic activities, such as trade and foreign direct investment (FDI), the major regional power usually becomes the first candidate to take the lead in a rescue plan and to commit the largest amount of its own funds. But regional economic crises are usually closely connected to the economic conditions of the regional power, and those regional powers that are most motivated to take initiative might be in an economically weak position to proceed in this manner. This has commonly occurred when financial crises have originated in emerging market countries like Latin America and Asia. For example, the United States was constrained by its budget and trade deficits in the 1980s, when Latin America was in a desperate need for financial assistance. Japan, meanwhile, was criticized for not doing enough for Asia due to Japan's own economic problems at the time of the 1997–98 Asian crisis. As a regional crisis begins to affect global financial activities, the critical question becomes, who else—if anyone—will participate in the collective management of the crisis? Under these circumstances, tensions can occur between the regional power, which is more interested in its private returns, and other participants of the collective action, hindering successful crisis management.

Besides the production of international financial stability through the containment of panic and the provision of financial support to countries in crisis, collective action among creditors can be effective in urging "discipline" on debtors. Creditors, both public and private, have an ultimate interest in making debtors pay back what they owe. Creditors are at a disadvantage if they negotiate separately with various debtors, because that allows debtors to play one creditor against the other. This can create a typical case of a prisoner's dilemma among creditors. In a prisoner's dilemma situation, the creditors' best solution is to cooperate among themselves to impose stricter adjustment and payment conditions on a debtor, but creditors wanting to extract better repayment from the debtor might allow more lenient conditions without knowing what others are doing simultaneously. A simple bidding war might take place, thus enabling the debtor to extract favorable deals. Because they are concerned about international financial stability and with making the debtors follow the established rules of the game, creditor governments have every interest in preventing such a scenario.

One way of getting around the difficulties of establishing a unified front for collective action in financial crisis is through institutionalization. In the 1940s, having regretted that World War II resulted from a failure to adequately respond to the financial and economic crises after the Great Depression, the major economic powers, led by the United States, installed a new design of international cooperation for trade liberalization and balance-of-payments support under a fixed exchange rate regime. The latter was represented by the Bretton Woods system, which involved new international financial institutions, such as the IMF and the International Bank for Reconstruction and Development (IBRD), otherwise called the World Bank.[7] In addition, since the 1960s, countries with strong financial interests have established various forums for similar goals, including the Group of Seven (G-7), through which the political and financial leaders of the major powers can join together to discuss matters important to their economic growth and stability.[8] These institutions have helped establish in the global economy a certain level of consensus and a moral code, guiding the actors' behavior.

Although these institutional arrangements have facilitated crisis management on the international level, still state actors have to agree on the implementation of crisis management and on increased funding for countries in crisis. The importance of such agreements is obvious in the case of the G-7, but it is also critical for the IMF, where the members of the executive board—delegates from member countries who hold different shares of voting power generally based on the amount of a country's capital subscriptions to the institution—discuss and vote on important decisions. Furthermore, the commitments of major creditor governments vary significantly depending on the government's positions on respective financial crises. Because the institutions (especially the IMF and the World Bank) represent a disproportionately large influence of the U.S. government, the motivation of major supporting governments to follow (or not to follow) the U.S. lead becomes even more important. Scholars of international relations thus have to start with an analysis of the motivations that bring state actors to decide to cooperate (or not) in financial crisis management.

Various strands of explanation for states' cooperative behavior already exist, ranging from international systemic accounts to unit-level analysis. However, each cluster of explanation manifests some weakness logically and empirically as it tries to account for the behavior of nonhegemonic major powers, particularly Japan, in international financial crisis management. In the following sections of this chapter, I outline the challenges facing existing explanations and then pose the two core hypotheses in this study: the importance, in international financial crisis management, of the "joint product" nature of public goods and of transnational linkages motivating state actors. These hypotheses constitute encompassing categories under which various specific dynamics and factors are organized. They thus provide clues regarding the analysis of international public goods supply.

Existing Explanations

Regarding international cooperation and provision of international public goods, three types of arguments have been developed in the literature to explain the behavior of either nonhegemonic powers in general or Japan in particular. These include a systemic explanation; an explanation based on the power of regionalism; and an outside-in explanation of foreign policy formation, including Japan's "reactive state" thesis. These explanations, it appears, help account for the general tendency of these powers to act in some kind of concert. When it comes to the powers' variant behavior in financial crisis management, however, these explanations leave a theoretical gap.

The Systemic Explanation

A hegemon provides international public goods to help maintain world stability that benefits all states, including the hegemon.[9] The theory of hegemonic stability was empirically challenged when it became increasingly clear that despite the decline in the early 1970s of the dominant and unchallenged post–World War II hegemony of the United States, the world was not facing major economic collapse. On the contrary, a certain level of international economic stability persisted. Various scholars have explained this continuing relative stability by analyzing how the anarchic nature of international relations has been overcome or modified by collective action.[10]

The analysis of hegemonic behavior in the provision of public goods splits into two camps. On one hand, the "benevolent" version of hegemonic stability theory argues that there is usually an exploitation of a large player by small players, in which the hegemon contributes a disproportionately large share of public goods provision.[11] On the other hand, the larger country, which is assuming the leadership role, can become a "predatory" hegemon and manipulate or coerce the smaller countries to cooperate.[12] Intellectual neglect still exists in the analyses of why nonhegemonic countries sometimes support and other times do not support the hegemon.

Many scholars consider cooperation among major powers as a key explanation for the stability and maintenance of a certain level of public goods supply. It is clear that scholars' views on the world and on the fundamental logic of state actions largely determine their judgment of the origin of international cooperation.[13] Some scholars from a liberal tradition note that the reciprocal effects emerging from various transnational institutional linkages and issue linkages in the world under "complex interdependence" can provide grounds for international cooperation.[14] Such conditions as a small number of actors, long-term reciprocal relationships, and the existence of "epistemic communities"[15] increase these possibilities. Scholars from the realist and neorealist perspective claim that international cooperation of a liberal institutionalist style would be largely impeded even with the existence of international economic exchanges, because states desire to obtain "relative gains" in relation to other countries, particularly rivals. Grieco emphasizes that unless there is a balanced distribution of gains, states have a hard time achieving international cooperation.[16]

Scholars looking at the systemic structure of international relations emphasize the existence of international regimes or of a set of "implicit or explicit principles, norms, rules, and decision-making procedures around which actors' expectations converge in a given area."[17] However, despite efforts made in the past to set up arrangements to secure international financial crisis management, power relations and interests of creditor governments still dominate decision making, leading to case-by-case responses. Thus, the international regime argument falls somewhat short of explaining cooperation in the issue area of crisis management.[18]

Scholars focusing on the motivations of major powers emphasize the possibility of collective action among an intermediate group in the absence of a clearly dominant single hegemon. Snidal argues that if the size distribution among a few subhegemons (e.g., Japan and Germany) is arranged in such a way that these countries find it beneficial to collaborate with the declining but still most powerful hegemon (the United States), a "k-group" can form to provide the public goods needed in the world.[19] The question is, however, whether we can always count on these major powers to agree with each other when the real or expected benefits accrued through collaboration are either unclear or very one-sided. Moreover, how could one account for the variance in a "k-group" member's behavior when the costs arising from a systemic collapse would be the same?

Furthermore, the power relations within the "k-group" are not uniform. Asymmetry of power determines, in part, the willingness of major powers to cooperate in crisis management.[20] This power asymmetry in the world and the influence (or power) of each state are channeled through two somewhat distinctive conjunctures: the country's structural powers and its relational powers.[21] The advocates of this distinction define relational power as "the power of A to get B to do something they would not otherwise do," and they maintain that structural power "confers the power to decide how things shall be done, the power to shape frameworks within which states relate to each other, relate to people, and relate to corporate enterprises."[22] Consequently, asymmetry of power means not only that a superpower larger and more powerful than others can coerce smaller countries to do what it wants them to do but also that international structures and institutions in different issue areas can be set up in a way that significantly benefits the large and powerful. This point is relevant in discussing the dynamics in the IMF at times of international financial crisis. Moreover, the type of power that a state possesses could vary depending on issue areas or geographic regions.[23]

In sum, the systemic explanation of international cooperation falls short of satisfactorily explaining the collective action outcome and behavior of state actors involved. It is thus important to analyze specific cases of cooperation and noncooperation to determine which factors go into a state's logic and how they translate into its actions.

Regionalism

Regionally based financial crisis management, in which a regionally dominant power commits exclusively or most actively to the crisis solution, is an alternative to a global or a multilateral arrangement. It would increase the motivation of a creditor government in the region, as the government's interests in stabilizing the economy are often greater and better-defined in the regional economy than in the global one. Regional interests in the face of financial crisis may lead to an arrangement of less collaboration or to some kind of geographical division of labor among major powers seeking to secure financial stability.

From the 1960s until the 1980s, theories on regionalism were limited to empirical cases from Western Europe, but they expanded globally in the 1990s, as the cold war ended and various regional integration efforts began to materialize in regions beyond Europe (e.g., the North American Free Trade Agreement [NAFTA], the Asia Pacific Economic Cooperation [APEC], and Mercosur). Furthermore, the regionalism of the 1990s not only involved integrationist movements among the industrial countries but also the north-south linkage of three major economic areas—the United States with Latin America, Japan with Asia (particularly Northeast and Southeast Asia), and recently Western Europe with Central/Eastern Europe and Russia.[24] Scholars began to examine why it is arguably more desirable to arrange international economic matters (and security matters) on regional bases rather than on a global basis. These discussions might be relevant to the analysis of major powers' response to financial crises emerging in their respective backyards.[25]

Regionalism is considered a conflict-minimizing way to organize state relations, particularly in trade. Trade arrangements in the form of "minilateralism" (within a small group of countries, as in the case of the post-1985 European Community) should facilitate careful allocation of costs and benefits arising from trade and thus should benefit participating states more, particularly when a hegemon, the main supporter of multilateral trade, is experiencing decline.[26] Due to lower transaction costs derived from close distance and already existing economic, political, and social ties, regional grouping is the most appropriate structure for this minilateralism, in which cooperation is more likely to take place. Moreover, if public goods produced through regional arrangements are excludable (against extraregional countries), a regional hegemon can emerge to supply such regional public goods.[27]

The logic of regionalism does not, however, fit well when explaining international financial relations and thus does not seem to satisfactorily explain the behavior of creditor governments in financial crisis management. The relatively more global (rather than regional) nature of financial transactions compared to trade makes the argument of regionalism much less effective. Evidence from recent international financial crises arising in developing countries shows that formal and regionally based crisis management in the form of lender-of-last-resort arrangements are still incomplete.[28] The most advanced case of such an arrangement is the North American Framework Agreement (NAFA), signed (after the conclusion of NAFTA) among the United States, Canada, and Mexico and providing a $6 billion swap arrangement among the three countries.[29] Some relatively small financial crises might be contained within a region. However, any large crisis with potential extraregional contagion effects (as observed in many of those major financial crises in the past two decades) would require a global solution. Thus far, empirical evidence indicates that creditor governments have been involved in extraregional crisis management despite high transaction costs and limited economic, political, and social ties. Specific to this study, Japan's active involvement at the final stage of the Latin American debt crisis and its passive position vis-à-vis the U.S. active initiative during the second phase of the Asian financial crisis (the Indonesian and Korean crises) requires a more appropriate explanation than regionalism.

The Outside-In View of Foreign Policy Formation on the Unit Level

In examining motivations that lead governments to act in the international arena, analyses of domestic or unit-level factors are considered fundamental. However, Risse-Kappen correctly points out,

> Empirical research in comparative foreign policy has established that domestic politics accounts alone are as insufficient as international level explanations and that they have to be complemented by [the] "second image reversed" concept.[30]

International dynamics and transnational relations influence how respective governments respond to external shocks and demands from outside. Even as we focus on dynamics among major powers, which are not merely "policy takers" but also "policy setters," external influence becomes a critical component of their foreign policy formation. In their discussion on the impact of economic globalization, Milner and Keohane summarize that internationalization changes the policy preferences of domestic actors and that domestic institutions intervene to determine the domestic response of each country to the same external shocks.[31] The impact of and the response to international financial crises would be considered corollaries to this analysis. External shocks are transmitted through transnational channels and form policy preferences of important domestic actors, particularly in the financial sector, and then the domestic institutional arrangements and domestic politics create various layers of intervening variables, shaping the policy outcome. This perspective is thus quite pertinent.

Looking more specifically at Japan, however, the existing theory is quite limited. Japanese foreign policy behavior (and Japan as a country overall) is often labeled "unique" as a major power because Japanese foreign policy has been characterized by a readiness to cooperate with the United States, with the Japanese government frequently reacting favorably to U.S. demands. The theory of a "reactive state," as it is called, suggests that strong cooperation arises from a special U.S.-Japanese bilateral relationship that includes Japan's high dependence on the U.S. market and on America's diplomatic and military support, as well as Japan's unique and fragmented structure of foreign policy decision making.[32] The theme of reactive or passive Japanese foreign policy-making has dominated the theoretical understanding and perception of Japanese external behavior.[33] This theory fails, however, to account for the condition in which Japan's actions vary despite the same high level of U.S. pressure. Moreover, Japanese domestic institutions and domestic politics influence policy outcomes by aggregating and transmitting the policy preferences of major actors. When is the Japanese government more willing or less willing to support the United States in providing public goods in the international economic arena? How do Japan's domestic politics influence the outcome?

To answer these questions, both domestic- and international-level analyses are important. Schoppa, responding to the challenge by examining the effects of foreign pressure under the Structural Impediments Initiative (SII) negotiations between the United States and Japan, notes that the "key to understanding why *gaiatsu* (foreign pressure) succeeds in Japan in some cases but not others lies in an appreciation of how domestic and international politics interact during the course of international negotiations."[34] This interaction between domestic and international politics requires careful attention.

As is discussed later in this chapter, it was inevitable that external pressure would be brought to bear on the Japanese government's calculations, due to the rapid internationalization of Japanese private financial institutions in the 1980s and to their strong domestic ties with the Japanese government. These institutions created a solid channel for the transmission of external pressure on the Japanese government from abroad. A task of this study is to examine the impact of external forces on Japanese governmental decision making at the time when some strong domestic actors began playing "external pressure" and "exit option" cards as international linkages solidified. To clarify the links and dynamics between a country's domestic politics and international influences, it is important to analyze precisely how a "second image reversed" view becomes incorporated in a country's policy formation.

The Argument: Sources of Japan's Actions in International Financial Crisis Management

How can we account for the Japanese government's varying level of engagement in international financial crisis management since the 1980s? More generally, how can we explain the level to which a major (but nonhegemonic) state contributes to the provision of international public goods in cooperation with other major powers? Two interrelated arguments account for the important variation in creditor governments' behavior. Although this study specifies these two arguments as hypotheses for the sake of clarity, these arguments are rather encompassing categories, within which the empirically specific factors detailed hereafter are subsumed.

The first argument notes that cooperation occurs because successful crisis management not only produces a public good but simultaneously promises a significant amount of private goods to the contributors. Thus, a creditor government will naturally be more willing to engage in collective crisis management as private returns from its action increase. The public good in this case comes in the form of the stability of the international financial system, which benefits everyone without discriminating either against or in favor of a particular actor. Private returns, in contrast, manifest themselves in products that give direct and exclusive returns to a clearly defined beneficiary regardless of supply efforts by others. We can thus consider that collective action in international financial crisis management leads to a "joint product" that produces both public and private goods. Active involvement by a creditor government in collective financial crisis management is most probable when the government can expect to gain greater private returns.

The second argument, closely related to the first, arises from strong economic and financial linkages among creditor countries. The stronger such linkages are, the more active a creditor government becomes in financial crisis management. Transnational linkages are characterized in two ways in the context of this study. On one hand, linkages come in the form of formal and informal institutional ties among major private financial institutions from various creditor countries. These ties become channels through which the demands of financial sectors are transmitted from one creditor country to another and from private creditors to creditor governments. On the other hand, economic interdependence in general establishes transnational linkages among countries whose economic activities are closely associated with each other. These highly interdependent economies thrive on many transnational linkages created through trade, investment, and loans and through other macroeconomic ties, such as interest rates and exchange rates.[35] These linkages among creditor countries also generate a mutual dependence or symbiosis that has lasting effects on the behavior of respective governments. These transnational linkages also create a powerful domestic force that can transmit pressures from abroad and demands on its home government, increasing, in turn, the stake (private returns) that a government can acquire from financial crisis management.

Financial Crisis Management as a Joint Product

> Hypothesis: A creditor government's motivation and efforts in managing international financial crises increase as the private returns that it can reap from this effort increase.

Financial crisis management involving relatively large developing economies will lead to the production of "public goods" in the form of international financial stability. Such stability, which is enjoyed by each and all without depriving others, could, in the absence of adequate management, be disrupted by the external economic problems of the debtor countries. In most cases, financial crisis management includes a rescue package to calm the market and lead to financial stability.[36] This calls, first of all, for leading creditor governments to commit themselves to financial rescue packages—in addition to guiding their respective private financial sectors to slow amortizations and roll over existing debt—and/or to increase capital flows to the problem countries. However, even public agents may have a difficult time providing stability, due to collective action problems.[37] Nonetheless, historical evidence points to the fact that major debtors in the series of financial crises analyzed in this study received rescue packages within a reasonably short time, despite collective action problems. From analysis of the financial crises in the 1980s and the 1990s, it is also apparent that Japan was often willing to collaborate with the United States, either bilaterally or through the IFIs, to provide critical management. Where does the discrepancy between logic and reality emerge?

A better explanation of cooperative crisis management among creditor governments, particularly the supporting behavior of nonhegemonic major powers, emerges when such management is thought of as a "joint product." Sandler explains this notion as "collective activity yield[ing] multiple outputs that vary in their degree of publicness," adding, "Some output may be private, while others may be purely or impurely public."[38] Many seemingly "public goods" are produced because they include some elements of private returns for the suppliers.[39] In addition, private goods can be supplied most effectively as a joint product with the public goods, rather than separately.[40]

International financial crisis management demonstrates the nature of a joint product. In most cases when crisis management has been conducted with each creditor's private interests in mind, it has also provided public goods along the way. As the amount of private return increases, a creditor government begins to see that engaging actively in internationally collaborative crisis management efforts offers an attractive option. In general, major creditors want to protect their own financial institutions and investors exposed to outstanding loans to debtors. Because it is difficult for any major creditor government to solely bailout the private investors with public money, and because of the fungibility of such money provided to the economies in crisis, these governments prefer collaborative financial crisis management to unilateral actions. As a consequence, public goods are provided that minimize the negative repercussion of such crises and enhance financial stability on the international level.[41]

In the context of this study, the private returns that the Japanese government has expected from active involvement in financial crisis management have two dimensions: domestic and international. Within the domestic dimension, the Japanese government has sought to support its own financial sectors facing problems stemming from financial crises and to increase its domestic political support from specific domestic sectors as well as from the public. In the international dimension, Japan's relationship with the United States and with the regions in distress becomes critical. By contributing actively to financial crisis management, the Japanese government has improved and consolidated its bilateral relationship with the United States (in terms of both economics and security) and with the countries in crisis. The Japanese government has also demonstrated its leadership ability with some alternative ideas and initiatives regarding financial crisis management, both regionally and multilaterally. The Japanese government also tries to satisfy transnational demands transmitted to Japan through domestic actors. The following empirical chapters discuss how all these factors have influenced the Japanese government's behavior in three sets of international financial crises.

Transnational Linkages and Financial Crisis Management

> Hypothesis: The stronger the transnational linkages between a creditor country and other countries are, the greater the creditor government's effort in managing international financial crisis is.

An in-depth analysis of international financial crisis management renders support to arguments emphasizing political factors—the liberal economic order—and to complex interdependence perspectives. Economic interdependence among countries has created multiple channels through which influence is transmitted, raising the stakes in successful cooperation as negotiations take place among creditor governments. Influence and pressures passed on through transnational linkages can often become domestic pressures from private sectors to governments. While "borderlessness" in the world of finance is allegedly becoming more of a norm,[42] it does not mean that the relationship between private actors and governments is losing its importance. In this study, the term *transnational linkages* refers to two kinds of linkages, both resulting from increased economic interdependence. The stronger both linkages are, the hypothesis states, the greater their influence is in inducing creditor governments' involvement in collective actions in international financial crisis management.

The first type of transnational linkages, institutional linkages, arises among internationalized financial sectors from different countries, establishing cross-border institutional links. Strong transnational coalitions among financial sectors from different countries increase respective home governments' commitment to financial crisis management. Interaction among transnational financial sectors is a major component of institutional linkages that influence financial crisis management. In the deals involving sovereign lending and syndicated loans in the late 1970s, transnational coalitions among international banks from different creditor countries were strengthened in part by their financial activities and risk-hedging mechanisms.[43] Even after the onset of the debt crisis in 1982, the institutionalization of committees (e.g., the BACs) among the affected banks established moral and legal mechanisms to strengthen (sometimes voluntarily and other times coercively) ties within the coalition.[44] This process, put into motion to deal with major debtor countries, is described by Devlin.

> . . . private banks had at their disposal the coordinating mechanism of an "advisory committee" with a track record of success in dealing with problem debtor countries. . . . in unregulated international markets there is unbridled communication. . . . Also facilitating communication and coordination among the banks are the legal incentives deriving from cross-default clauses that accompany almost all international loan agreements. . . . it can facilitate collusion and the formation of an effective cartel geared to skewing the distribution of the costs of a problem.[45]

The power of this kind of transnational coalition among different actors in the financial sector, particularly at the time of a crisis, establishes a strong cross-border link that transmits pressures and demands from one creditor country to another. Furthermore, such institutions as the London Club and the BACs provide international forums within which cross-national peer pressure is applied among transnational banks, making it more likely for banks themselves to act in concert.

The second type of transnational linkages, understood generally as economic linkages, increases as a country's economic stake in another country expands with an intensification of trade and investment activities by the former in the latter. As economic integration among major creditor countries deepens, their vested interest in each other's financial and economic health becomes a major focus of foreign financial institutions heavily invested in the countries. Furthermore, such economic linkages tend to be correlated with bilateral political and security ties that make one of the countries even more sensitive to the other's actions.

These economic linkages, in turn, bind two major economic powers when they deal with financial crises of third (i.e., not their own) countries, creating a triangular relation. The negative economic impact of a financial crisis in a distant region is transmitted to a creditor country not so much directly but through the negative economic consequences the crisis has on the economy of the major regional power, whose conditions influence other industrial countries via economic linkages.[46] Particularly relevant to this study are crises occurring in regions whose economic turmoil affects one major creditor country more severely than it affects another. In the case of the U.S.–Japan–Latin American debtor triangle in the 1980s, for example, the Japanese government considered both Japan's overall economic relationship with the United States and the restoration of U.S. economic health imperative at a time when intraregional economic ties in the Americas detrimentally affected the U.S. economy.

Strong transnational linkages therefore prompt creditor governments to become involved in financial crisis management. These dynamics provide good examples of the "second image reversed" analysis discussed earlier in this chapter.[47] Importantly, though, how such international forces influence the final decisions of a government depends on the nature of each state. Japan is commonly described as a typical developmental state in which the government plays a vital role in every area of economic activity, domestic and international.[48] Claims are made that Japan has been most successful in the area of controlling the external behavior of its private sectors.[49] Japanese banks have traditionally been willing to engage in international business in accordance with official state objectives because of a convergence of interests between Japanese banks and the government in the international sphere and because of the banks' deferential attitudes toward the home government.[50]

Although understanding the nature of the developmental state is important in correctly examining Japanese behavior, the country has gradually transformed itself into a more pluralist system with societal pressure influencing the government's behavior. This is increasingly true as Japan becomes exposed to international pressure. Some argue, correctly, that the nature of the autonomous Japanese state has changed since the mid-1970s.[51] There are two major reasons for this: (1) exposure to the international system has introduced various external pressures and uncertainties; and (2) the development of the private sector has undermined the power and autonomy of the government by changing the domestic power balance. Under conditions where deregulation and internationalization have enhanced the institutional linkages of Japan's financial sector, the sector has gained a stronger voice from its financial integration with the rest of the world as well as from its increased capital mobility. The power relationship between the two actors has shifted gradually in favor of the financial sector, particularly in the case of the sector's influence on the government's behavior in financial management abroad. These external factors and foreign pressures (*gaiatsu*), channeled through various paths, influence the government's foreign policy decision making. Japan's private sector has also severely undermined the state's power: "as private capital has become less dependent on the resources provided by the state, the state's relative dominance has diminished."[52]

As financial crises abroad accentuate tensions in the relationship between the Japanese government and its financial sector, Japan's banks have exerted significant pressure on the government to minimize losses, regardless of the government's positions. In exchange, they have collaborated with the government in financial crisis management.[53] The health of its own financial sector in the face of crisis and the likely repercussions that a financial sector problem might have on the economy concerns the Japanese government. These factors have thus motivated the government to accommodate the sector's demands as much as possible, increasing the likelihood that transnational linkage pressure would prevail in the Japanese government's decision-making process.

The domestic politics that translate greater economic linkages in general into the Japanese government's actions in financial crisis management are less straightforward. Of course, larger direct investment, higher trade dependence, and increasing trade tensions have prompted various agents in the internationalized Japanese private sector to push for greater accommodation of demands by the United States, so that Japan could support the U.S. economy and avoid its economic retaliation.[54] Furthermore, Japan's financial sector, which has a high stake in the U.S. economy as well as in the countries experiencing financial crisis, has added incentives to engage the Japanese government in crisis management.

In sum, the strength of transnational linkages matters to creditor governments involved in international crisis management. On one hand, the willingness of major powers to engage in collective action in financial crisis management lies in the degree to which institutional ties among transnational financial sectors can lead home governments to engage in financial crisis management on their behalf. Particularly in the case of Japan, where the government-bank relation is known to be symbiotic, the Japanese government's external behavior and the crisis solutions provided by the public sector are strongly influenced by the bargaining and quid pro quo between the financial sector and the government. On the other hand, economic interdependence among major creditor countries creates general economic linkages that urge increased collective action as one of these countries becomes greatly affected by a financial crisis in its region. These economic linkages induce increased private returns to a government engaging in financial crisis management via support to its closest economic partner. This study therefore places the impact of economic linkages on the behavior of creditor governments as an important component of joint product.

Finally, the outcome of this process presents itself in the international arena as the Japanese government's foreign policy behavior. In some cases, Japan cooperated fully and actively with the United States and helped solve crises; in other cases, it avoided deep involvement.

Summary

International financial stability is a public good that requires continual attention. The question of collaborative management in a world lacking a single dominant hegemon becomes critical when a financial crisis that has the potential to bring major international financial disaster occurs. The existing literature and theories on international cooperation in general or on Japanese foreign policy behavior in particular fall short in accounting for Japan's varying involvement in cases of international financial crisis management. Hence, we still need to seek pertinent explanations of the actions taken by the Japanese government that have shaped the solutions to some of the largest financial crises of recent years.

This chapter emphasizes the joint product nature of the process by which international crisis management aiming for financial stability brings about both private and public benefits to the creditor governments involved in the solution. In this context, joint products motivate a major creditor government, such as that of Japan, to actively engage in collective action among potentially adversarial governments that are otherwise reluctant to become involved. Related to this point, transnational linkages have, in the past, successfully transmitted influence from one creditor country to another, both through institutional channels and through the power of economic interdependence.