# Notes

## Introduction

1. In this international economic environment, the ability of governments to manage their macroeconomic policies effectively is also constrained. For examples, see Keohane and Milner 1996; Cohen 1996; Andrews 1994.

2. For historical accounts of various financial crises, see Kindleberger 1989; Galbraith 1994. I acknowledge the general argument by economists that public intervention in the market has, in many cases, led to a moral hazard problem and thus may be more detrimental than a laissez-faire policy. However, the international financial market has also been known to be unstable. John Maynard Keynes, for example, advocated in the 1920s an international mechanism to provide a multilateral lender-of-last-resort function.

3. The recent financial crises include the Third World debt crisis of the 1980s (which continued for some countries into the 1990s), the 1987 Black Monday stock market crash, the 1992–93 EMS (European Monetary System) crises, and a major currency crisis in Mexico in 1994–95. Most recent has been the global crisis that began in several East and Southeast Asian (hereafter Asian) countries in 1997–98 and has since spread to Russia, Brazil, and elsewhere.

4. The basic definition of public goods has two parts: that they are jointly supplied and that exclusion is impossible. The first part means that one person's consumption of the good does not reduce the amount available for anyone else, and the second means that it is impossible to prevent relevant people from consuming it (see Hardin 1982, 17). On the international level, these goods are known to be the basis for the smooth operation of multilateralism and an open international economic order.

5. Charles Kindleberger (1989, 201) notes that in an international arena "with no government, no world central bank, and only weak international law, the question of where last-resort lending comes from is a crucial one."

6. Many scholars have tackled the question of peace and stability after the relative decline of the United States. Their explanations range from the formation of international regimes, to the role of privilege groups, to coerced cooperation.

7. This study focuses on the dynamics between Japan and the United States as an important component of international financial crisis management. However, the focus does not translate into the discussion on whose policy is right and whose policy is wrong. In addition, I have no intention of engaging myself in the polemic of keeping score as to which country is winning points and becoming the number one power in the world. From observing Japan's position in the world of international finance in recent decades, the study starts out defining Japan as a nonhegemonic supporting power in this issue area.

8. For discussion on Japan's role as a major economic power in the world, see Inoguchi 1988.

9. In a way, a major nonhegemonic power has strong relational power but not so strong structural power. See my discussion on this distinction in chapter 1.

10. Cooperation is generally defined as "when actors adjust their behavior to the actual or anticipated preferences of others, through a process of policy coordination" (Keohane 1984, 51–52). Cooperation also means something opposed to conflict.

11. For example, following requests from the Argentine government after it suffered from capital outflows and attack on its currency in the spring of 1995, the JEXIM Bank agreed to extend $0.8 billion in untied loans. In the summer of 1996, the JEXIM Bank signed an agreement for $0.5 billion in untied loans to Mexico at the time of the Japanese prime minister's visit to the country.

12. The New Miyazawa Initiative, announced in October 1998, would provide $30 billion in financial support to Asian countries in crisis. In December 1998, the revival of the AMF was once again suggested by Japan's finance minister (see *Financial Times,* December 16, 1998), and, finally, the regional fund scheme in the case of financial crises was officially agreed upon. The agreement on May 6, 2000 among the Association of Southeast Asian Nations (ASEAN) plus three members was called the Chiang Mai Initiative (see chap. 8).

13. In the 1994–95 Mexican peso crisis, the Europeans disagreed with the assertion by the Clinton administration that this crisis was systemic. This issue is discussed in chapter 6.

14. More theoretical discussion on this point is included in chapter 1.

15. Furthermore, although the nature of each crisis differs to some extent, the need for some kind of external intervention to contain and resolve the crisis remains the same.

16. Therefore, the distinction between public and private here does not correspond directly to the distinction between the state sector (public sector) and the private sector.

17. At the time of the Asian crisis, the United States enjoyed stability and growth in its own economy, but it had to respond to the fact that its major economic partner was hurt by the regional crisis, a factor that threatened the overall stability of the international economy.

18. For the first complete discussion of "complex interdependence," see Keohane and Nye 1977.

19. The first factor belongs to the hypothesis of joint product, and the remaining factors belong to the hypothesis of transnational linkages.

20. See King, Keohane, and Verba 1994, 3–7.

21. The typical example, particularly relevant to the issue of this study, is the sign of a coefficient. Suppose that Latin American country A received more foreign aid from Japan as its foreign aid receipts from the United States rose. The coefficient shows a positive sign. But does this mean that Japan is competing with the United States for influence in country A or that Japan is cooperating with the United States to help country A because it is considered important for the United States?

**Chapter 1**

1. Former managing director of the IMF Michel Camdessus also emphasized this notion of international public goods in his speech "International Financial and Monetary Stability: A Global Public Good" (IMF/Research Conference on Key Issue in Reform of the International Monetary and Financial System, Washington, D.C., May 28, 1999).

2. James Boughton (1997) discusses the historical role of the IMF as crisis manager. He argues that the IMF was only pulled in to deal with the crisis. The big turning point came at the time of the 1982 debt crisis, when the IMF was set in the center stage.

3. The problem associated with fungibility of economic resources is best described by David Baldwin in his discussion regarding foreign aid as a strategic good. When a good is fungible (freely exchangeable for or replaceable by another of like nature or kind in the satisfaction of an obligation), the good can contribute to something different from the intended use. For example, foreign aid disbursed by a donor to build a bridge in a developing country can be fungible. If there has already been some money set aside in that country for the construction of this bridge before the country receives aid, the economic resource provided from outside frees up the original budget, which would then be used for other purposes (see Baldwin 1985, 304). In the simplest case of bailout, funds provided by creditor government A can be used to pay back debts from private creditor B first. Thus, creditor B will benefit immediately while the benefit to creditor A is uncertain and probably less than that allocated to creditor B.

4. See Grieco 1988 on the theory of relative gains and international cooperation.

5. On the debtor side, the crisis management and bailout packages can often reward problem debtors. They mismanaged their economies, severely indebted themselves, and have not committed seriously to the country's economic reforms or its repayment obligations, both of which are often politically difficult. It is true that the rescue packages—above all, those implemented by the IMF—come with stringent conditionality and stabilization programs, but prolonged crises in relatively large countries, such as Brazil or Russia, give debtor countries much more leverage not to adjust. On the investors' side, such rescues may end up encouraging those investors and transnational banks to take repeatedly high risks in their investments and lending decisions. By creating the perception that they will be bailed out every time the financial crisis gets out of control, many critics argue, these bailout packages lower financial institutions' risk consciousness, thus increasing the likelihood and the magnitude of future financial crises. Incidentally, some argue that the action of creditors (particularly the U.S. government) in the 1995 Mexican peso rescue encouraged investors to be more aggressive in Asian investments and thus invited the 1997 Asian financial crisis. For further discussions of problems with rescue packages, see Goldstein and Calvo 1996.

6. See, for example, my discussion of the AMF scheme and of the criticism of the IMF in chapter 8.

7. For an excellent narrative of the negotiation on the form of new institutions, see Gardner 1980. See James 1996 on the evolution of the role of the Bretton Woods institutions from the time of their establishment through the present.

8. The Group of Ten (G-10: France, Germany, Japan, the United Kingdom, the United States, Canada, Italy, Belgium, the Netherlands, Sweden, and Switzerland) was actually the first group to form, in 1962, to organize an extraordinary lending system called General Arrangements to Borrow (GAB) via the IMF. The Group of Five (G-5: only the first five countries from G-10) came together in 1973 to provide a forum among the countries' finance ministers. G-7 (G-5 plus Canada and Italy) formed after the Tokyo Summit in 1986. From the Denver Summit (1997), Russia joined G-7 as a special member on political issues, leading some to address this group as the Group of Eight. The first summit among the heads of state was held in 1975. See Bergsten and Henning 1996, 18; James 1996.

9. For the classic texts on the hegemonic stability theory, see Kindleberger 1986b and Krasner 1976.

10. Robert Keohane's well-known discussion in *After Hegemony* (1984) emphasizes that international regimes play a key role in maintaining stability. Others attribute sta-

bility to collective action among major powers and to international cooperation; see, for example, Oye 1986.

11. Mancur Olson (1971, 35) notes that "there is accordingly a surprising tendency for the 'exploitation' of the great by the small." In addition, a hegemon can ensure that everyone plays by the rules.

12. See this point in Milner 1992, 480 and n. 26; Snidal 1985, 588–90. Also on the discussion of involuntary cooperation (coerced cooperation) involving economic sanctions, see Martin 1992.

13. Lisa Martin (1992, 15–45) provides a succinct contrast of the forms international cooperation take under different theoretical perspectives. The realist tends to see international cooperation as coercion by the strong, the liberal thinks cooperation occurs as a coincidence of interest, and the neoliberal institutionalist looks at cooperation as coadjustment arising from mutual policy adjustment.

14. This perspective originates in Keohane and Nye 1977. In contrast to "realist" ideal types, complex interdependence emphasizes the interaction of subnational actors and argues against the assumption of security supremacy.

15. Peter Haas (1990, 55) coined the term *epistemic community,* defining it as "a professional group that believes in the same cause-and-effect relationships, truth tests to assess them, and shares common values. As well as sharing an acceptance of a common body of facts, its members share a common interpretative framework, or 'consensual knowledge,' from which they convert such facts, or observations, to policy-relevant conclusions."

16. Grieco 1988, 499–500; 1990, 47.

17. Krasner 1985, 3.

18. Here I follow the criticisms of regime theory by Susan Strange (1983).

19. Snidal 1985.

20. This is not to contradict the assumption of the anarchic nature of international relations. All students of international relations learn in IR101 that anarchy is not the opposite of order and that anarchy in the international arena means the lack of an overseeing world government. Some, such as Helen Milner (1992), argue this point to be problematic. In the context of my analysis, I am merely pointing out that units (states) in international relations are neither equally powerful nor equally motivated.

21. Robert Keohane and Joseph Nye (1977, 15) define this distinction earlier as process-level and structural-level power of interdependence, and they discuss sensitivity and vulnerability in a country's interdependent relationship with others.

22. Strange 1994, 24–25.

23. See Cohen 1977, 56–57. This point is discussed further in the section on regionalism that follows.

24. See Stallings and Streek 1995.

25. Discussion on international sources of regionalism includes functionalism and neofunctionalism, emphasizing the role of expansion of economic activities in regional economic integration. International institutions and ideational change can explain regionalization. But domestic interest groups and societal pressures can also promote regionalization. For a summary, see Mansfield and Milner 1997, 4–14. For summaries of various theories on regionalism, see Hurrell 1995.

26. See Yarbrough and Yarbrough 1994, 108; 1987.

27. For an application of club theory on regional arrangement, see Padoan 1997.

28. There are various nonregional arrangements among G-10 countries in the form

of the General Arrangements to Borrow (GAB) (see James 1996, 161–65). Recently, the New Arrangements to Borrow (NAB) was established to deal with balance-of-payments problems of emerging market countries.

29. In the case of Asia, discussion of this type of arrangement was widespread in the aftermath of the 1994 Mexican peso crisis, and some achievements were made in this area (see chap. 8). The currency swap lines established were, however, not sufficient.

30. Risse-Kappen 1995, 15–16.

31. Milner and Keohane 1996b. Benjamin Cohen (1996) discusses the contrast between outside-in and inside-out perspectives regarding the rise of financial globalization.

32. See Calder 1988.

33. The early work of T. J. Pempel (1978) and a new contribution by Frances McCall Rosenbluth (1996) provide alternative explanations focusing more on the domestic sources of foreign policy.

34. Schoppa 1993, 383.

35. This study distinguishes the two, when necessary, by calling the former "transnational institutional linkages" and the latter "economic linkages."

36. Stephany Griffith-Jones (1991, 111) notes that "stable external financial flows to fund development and stability of the banking system are 'public goods' that cannot be provided by private market agents acting individually." Although funds themselves are excludable and thus are not pure public goods, one can use such financial flows as necessary costs in providing public goods (i.e., international financial stability).

37. As I discussed earlier, classic collective action literature suggests that financial stability will always be undersupplied when there are many actors involved. The larger a group is, the more motivated its members will be to free ride on the public goods without contributing. See Olson 1971, 9–16. Note the argument of relative gains by Grieco (1990), who disagrees that a larger number of group members could enhance cooperation.

38. Sandler 1992, 11.

39. Lawrence Broz uses this analysis to explain the formation of the Bank of England (1998) and the Federal Reserve Bank (1999), and Leonard Dudley and Claude Montmarquette (1976) analyze foreign aid in this light.

40. Broz (1999, 40) notes that "the crucial requirement of the model . . . is that the private and public goods in question cannot be disaggregated due to some prevailing supply constraints." Although I agree with the importance of the "joint" nature of the product, I argue that if private goods can, by the very nature of their connectedness to the public goods supply, be most effectively or cheaply supplied when tied to public goods provision, there is a clear reason why the suppliers prefer the joint product to a separate one.

41. Logically, one can also argue the reverse sequencing of public goods–private goods provision and that creditor governments are much more concerned about providing public goods in terms of international stability so that, as the externality, their own private financial sectors can be saved from financial collapse (I thank Benjamin Cohen for pointing this out). I argue, however, that as a single creditor government decides its policy regarding crisis management, there is enough uncertainty as to whether or not sufficient stability would be produced through its own actions so that the government would not be driven initially or solely by the production of public goods.

42. Kenichi Ohmae (1991, x) notes that "[the Interlinked Economy] is becoming so powerful that it has swallowed most consumers and corporations, made traditional na-

tional borders disappear, and pushed bureaucrats, politicians, and the military toward the status of declining industry." David Andrews (1994, 197–203) notes that capital mobility is becoming a systemic constraint in international relations.

43. For further discussions on the way in which these new inventions facilitated capital flows to developing countries and invited the collapse of the world of development finance, see Wood 1986.

44. See Lipson 1985.

45. Devlin 1989, 217–18.

46. The issue associated with asymmetry of power is relevant here. Even though this type of economic linkage binds two major economic powers, the negative impact of the U.S. economic downturn influences the Japanese economy much more than vice versa. This asymmetry arising from the powers' bilateral relations in both economic and security realms, therefore, leads the Japanese government to act more on behalf of U.S. economic recovery than the other way around.

47. See Gourevitch 1978.

48. For details on the history of the Japanese government's role in forming Japan's economy, see Johnson 1982 and Hollerman 1988a.

49. Henrik Schmiegelow and Michele Schmiegelow (1986, 582) note that "the government can use instruments of domestic policy to stimulate, control, guide, and promote autonomous households and firms to save, consume, invest, or undertake research and thereby become, through such private actions, factors of structural change on the global scale."

50. See Spindler 1984, 121. Koichi Hamada and Akiyoshi Horiuchi (1987, 260) argue that coordination by the authorities *(nemawashi)* has created a situation in which most participants are prepared to conform smoothly to the new rules. The relationship between the Ministry of Finance (MOF) and the banks in Japan is also known as the "convoy system" *(goso sendan hoshiki).*

51. See, for example, Pempel 1987.

52. Evans 1992, 165.

53. See Stallings 1990b.

54. See Yamamura 1994 and Rosenbluth 1996 on how internationalized private sectors, such as large manufacturing firms and commercial banks, gradually won the support of the Liberal Democratic Party (LDP) over the domestic sectors, such as farmers and small and medium-sized businesses.

## Chapter 2

1. There is some increase in the trend of Japan importing manufacturing goods from developing countries, particularly from Asia since the late 1980s. However, as Edward Lincoln argues (1993, 86), Japan's imports of manufacturing goods as a percentage of its gross domestic product (GDP) remains very low (3.8 percent in 1990) compared to other industrial countries, whose figures range from 7.8 percent (United States) to 50.8 percent (Belgium). In addition, the ratio of manufactured goods within the U.S. total imports (not GDP) have been higher (averaging 75 percent between 1990 and 1993) than that of Japan (averaging 46 percent between 1990 and 1991) (see OECD, *Handbook of International Trade and Development Statistics,* 1994).

2. See, for example, Rosecrance and Taw 1990; Helleiner 1989.

3. A comprehensive analysis of Japan's economic activities in developing countries is beyond the scope of this book. Recent books that focus on this issue include Koppel and Orr 1993; Nester 1992; Yasutomo 1995.

4. See Bergsten and Cline 1987; Bergsten and Noland 1993a.

5. Such a trade deficit is partly due to the increase of Japan's FDI in the region since the mid-1980s, through which the Japanese manufacturing firms overseas increased their imports of intermediate goods and inputs for production. Despite some increase in the amount of exports due to manufacturing production, the level of manufacturing exports from these Asian countries to Japan is still limited, particularly in comparison to that of the United States. See Bernard and Ravenhill 1995, 200–202; Naya 1990, 181.

6. See Lincoln 1993, 87–93.

7. See Pyle 1992 for detail. The gist of the so-called doctrine originated right after Japanese independence in 1952, when Japanese foreign policy rested on two pillars: (1) Japan will concentrate on its economic recovery and growth after World War II, and (2) Japan will minimize its military expenditure and resort to the U.S.-Japan security alliance for its defense needs.

8. See Teranishi 1986.

9. See Johnson 1995.

10. Historically, the Japanese government has preferred to refer to all of its financial flows to developing countries as "economic cooperation." This category includes funds from both the government and the private sector. In comparison to *foreign aid,* the term *economic cooperation* emphasizes Japan's comprehensive and multidimesional economic interaction with the recipient countries. Alan Rix (1980, 226) notes that the term *economic cooperation* constructs a program that would not be identified with the view of a single ministry and that it is more appropriate for the Japanese foreign aid administration, which is a consortium of several ministries. They include the four major ones (MOF, Ministry of Foreign Affairs, Ministry of International Trade and Industry, and Economic Planning Agency). In addition and as noted by Hanabusa (1991, 90), the government and private sector entities dealing with developing countries are considered "partners in development," as their interests have often converged.

11. Early writings include Rix 1980; Hasegawa 1975; Yasutomo 1986, 1995; Inada 1989; Orr 1990; Brook and Orr 1985. In the 1990s emerged a new generation, including Arase 1995; Ensign 1992; Katada 1997; Kato 1996, 1998; Miyashita 1999; Wan 1995.

12. Burma first reached an agreement on reparations with Japan in 1954; the agreement took effect in 1955. The Philippines (1956), Indonesia (1958), and South Vietnam (1959) followed. Additionally, Laos, Cambodia, Thailand, Burma (in addition to the previous agreement), and Korea received Japan's quasi-reparations grants during the 1960s. The last installment of reparations officially ended in 1977. See Hasegawa 1975 for accounts of Japanese foreign aid during these early years.

13. See Yanaga 1968.

14. Until 1961, Japanese foreign aid was implemented by the JEXIM Bank, which was set up in 1950 to encourage commercial banks to finance exports, imports, and overseas investment. In 1961, the OECF was established specifically to handle foreign aid loans. The two organizations merged in October 1999 and established the Japan Bank for International Cooperation (JBIC).

15. Throughout the 1970s, the OECD publication *Development Co-operation* kept mentioning that Japan's foreign aid failed to meet the terms recommended by the De-

velopment Assistance Committee (DAC), and the publication criticized that Japan's foreign aid had a very high concentration in Asia.

16. Brook and Orr (1985, 326) note that the concept of ODA was not firmly established until the early 1970s.

17. Aid-doubling plans were conducted in 1978–80, 1981–85, 1986–92, 1988–92, and 1993–97. See Arase 1995, 217.

18. However, due to Japan's high gross national product (GNP), the country has never met the UN target of ODA contribution relative to its GNP, 0.7 percent. Japan has always scored below average (0.3 percent) in this measurement.

19. Representative cases in the 1980s include Korea (1982), Egypt (1977–80, 1983), Jamaica (1980–83), Pakistan (1980, 1982, 1984), Sudan (1982, 1984), Ethiopia (1984), the Philippines (1984), China (1979, 1984), and some Central American countries (1985). See Orr 1988; Yasutomo 1986, 81–105.

20. See Brook and Orr 1985, 323.

21. MITI 1977, 123, my translation.

22. Yasutomo 1986, 5. The notion of comprehensive security has been best described by its advocate Prime Minister Ohira when he explained in July 1980 that the days were gone when Japan could count on an international system maintained single-handedly by the United States, either in the realm of military security, politics, and diplomacy or in that of the economy. He said that Japan must now contribute to the maintenance and management of the system as an influential member of the free world. There has been a shift from a world of "Pax Americana" to the world of "peace maintained by shared responsibilities" (cited in Pyle 1992, 206).

23. Japan-U.S. communiqué, May 8, 1981.

24. Inada 1989, 402.

25. See Kato 1996, 100–101.

26. OECF, *Nenji Hokoku Sho* (Annual Review) (1992), 13–14. In 1991, the only remaining tied loans are called "LDC tied," which means that only firms from the less developed countries (LDCs) or Japan can participate in the bidding. Some scholars argue, however, that there is still de facto tying of Japanese aid in many parts of Japan's development projects (see Ensign 1992). In addition, some Japanese industries pushed toward more "tied aid" in the late 1990s to increase their business opportunities (see chap. 8 in this book).

27. Japan became the top ODA donor for the first time in 1989. The United States apparently overtook Japan from 1990 through 1992, when Japan returned to the postition of number one aid donor. However, if you subtract the non-ODA debt forgiveness from U.S. ODA figures in these three years, Japan has kept its position as number one aid donor.

28. Another noteworthy issue in the first half of the 1990s is that in 1992, after facing long-standing criticism for not having a clear philosophy or guidelines for its foreign aid, the Japanese government announced its ODA Charter. The charter contains four pillars: (1) environmental protection and sustainable development; (2) no use of aid for military purposes; (3) diversion of ODA from countries that have excessive military expenditures, production of weapons of mass destruction, and arms trade; and (4) promotion of a market economy, democratization, and human rights.

29. For more on government-business relations in Japan's foreign direct investment in the Asia Pacific, see Hatch and Yamamura 1997.

30. The OECF has restrictions on its concessional loans to countries whose GNP per

capita is higher than an upper middle-income country as determined by the World Bank every year. In 1997, for example, the threshold for GNP per capita was $3,126.

31. Most of the JEXIM Bank's loan sources come from the Fiscal Investment and Loan Program (FILP). FILP consists of postal savings (which is 30 percent of Japan's savings deposits) and has traditionally been used to fund Japan's economic reconstruction. Due to Japan's economic recovery and the decreased need for infrastructure projects, the Japanese government was facing declining demands on this fund (sometimes called the Japanese government's shadow budget). During the mid-1980s, the MOF agreed to lend the excess liquidity of FILP to developing nations. Thus, the demand from indebted countries and the supply of JEXIM Bank untied loans happily met. See Calder 1997, 38.

32. For illustrations in various financial activities, see Schmiegelow and Schimiegelow 1986; Spindler 1984; Hatch and Yamamura 1997.

33. For discussion on the Japanese model of FDI in Asia, see Hatch and Yamamura 1997.

34. The compilation of FDI by notification to the MOF started in 1951. This statistic is the accumulation of 1951–80. See Jun et al. 1993, table A-4.

35. The aggregate amount of Japanese FDI in Latin America is quite deceiving: it is strongly dominated by Panama and other tax-haven countries where Japan has significant investment in finance and insurance as well as in flag-of-convenience ship registrations (see Jun et al. 1993, 17–19). In addition, a substantial amount of Japanese investment in Mexico has been made by Japanese subsidiaries in the United States and is not captured statistically as Japanese investment (interview with a Japanese businessman, Mexico City, December 1997).

36. One banker noted: "[the banks] felt that we were contributing to Japan's national interest by investing in these projects. We felt proud to work for the benefit of our country, since there was a sense of urgency to secure the source of minerals and oil through these projects" (interview with a Japanese banker, Tokyo, April 1993). Although bankers' feelings of patriotism spurred their involvement in these "national projects," the accompanying public financing also reduced their risk.

37. Akamatsu 1937.

38. Kojima 1978b; the definition of the "flying geese pattern" is from Bernard and Ravenhill 1995, 171. Bernard and Ravenhill argue that this pattern does not apply to Asian development.

39. Ozawa 1979.

40. See Encarnation 1992, 169.

41. See Encarnation 1992, 169–74; Yoon 1990, 13; Lincoln 1993.

42. See Yoon 1990, 12. In 1990, 41 percent of long-term debt to implement Japan's FDI in the manufacturing sector of Asia was financed by Japanese investors or Japanese banks, and the rate was 45 percent for Latin America (see MITI, *Kaigai jigyou katsudo kihon chosa* [1991], 33).

43. See Ozawa 1989.

44. See Frieden 1981.

45. The MOF officials thought that in comparison to FDI, capital flows in the form of bank lending were relatively free from potential friction and conflict in investment-receiving countries (or against other investors in these countries). See Fujioka 1979, 222, 248.

46. Fujioka 1979, 181, emphasis added.

47. See Spindler 1984, 182.

48. See Ozawa 1989, 41.

49. See Rosenbluth 1989, 52–95; Pauly 1988; Healey 1991, 131–34.

50. Nakao 1995, 63. This maturity transformation also enables banks to make financial profit from the difference between the short-term borrowing and long-term lending.

51. See MOF, "Wagakuni Shihon yushutsu wo meguru shomondai ni tsuite" (1990), 22. This was also pointed out by Healey (1991, 133–37).

52. See MOF, "Wagakuni Shihon yushutsu wo meguru shomondai ni tsuite" (1990), 51.

53. See Schadler et al. 1993. For discussions on push factors and pull factors of capital flows to developing countries, see Chuhan, Claessens, and Mamingi 1993; Fernandez-Arias 1996. Sylvia Maxfield (1998) contributes to the discussion of "push" and "pull" by adding the level of "patience" of different types of portfolio capital to developing countries.

54. For the conservative and illiquid characteristics of Japan's Samurai (yen-dominated) bond markets, see Shilling 1992, 98.

55. Chuhan and Jun (1995) list various explanations for why Japanese institutional investors were slow to tap into Latin American emerging markets, including Japan's administrative guidance that is conservative on political risk.

56. For example, Mike Mansfield, former ambassador to Japan, has repeatedly emphasized that the U.S.-Japanese relationship was the most important bilateral relationship in the world. See Mansfield 1989.

57. The two countries' combined economic weight in the world economy is significant, with the aggregate exports of the United States and Japan reaching over 20 percent of total world exports in the 1980s. These two countries have been the top two aid donors to developing countries since the mid-1980s. They also wield the top two voting positions in IFIs, such as the IMF, the World Bank, and the Asian Development Bank (ADB).

58. The well-cited literature on the U.S.-Japan relationship in the area of political economy includes Destler et al. 1976; Destler and Sato 1982; Bergsten and Cline 1987; Prestowitz 1988; Volcker and Gyohten 1992; Encarnation 1992; Bergsten and Noland 1993a; Iida 1993b; Schoppa 1997.

59. See H. Schmiegelow 1986, 222–38.

60. The emphasis of this book is more on the first and second dynamics and less on the third.

61. This study does not focus on the question of Japan's "leadership" role, and it assumes that there is a power asymmetry between the United States and Japan in the U.S. favor. Well-known scholars of Japan-U.S. relations have already produced a collective work on the analysis of U.S.-Japan leadership sharing (Sato and Destler 1996). In that volume, Sato defines leadership as "the initiative taking in leading or getting others to do what one wants them to do (or to move toward a certain goal)" (14). For further discussion on the different types of leadership, see Young 1991.

62. For a historical account of Japan's external economic policy from the 1950s through the mid-1970s, see Krause and Sekiguchi 1976, 411–40.

63. See Borden 1984; Schaller 1997.

64. Some have claimed that Japan is still a free rider, particularly in the field of international security, a trend well exemplified during the 1990–91 Persian Gulf crisis. For a discussion of the three scenarios of Japan's international role in relation to the United

States, in terms of Japan becoming a free rider, challenger, or supporter to the United States, see Inoguchi 1988.

65. Kindleberger 1986a, 9.

66. For example, see Nau 1990.

67. This was the time when Ezra F. Vogel's book *Japan as Number One* (1979) and his article "Pax Nipponica?" (1986) attracted the attention of the public from both the United States and Japan. Many anti-Japan campaigns emphasized the threat of Japan's economic dominance, see Fallows 1994.

68. The Japanese yen appreciated rapidly between 1985 and 1988, from ¥250 to ¥125 to a dollar; thus the relative strength of the yen against the U.S. dollar doubled within three years.

69. The information is compiled in Inada 1993.

70. See Ito 1993; Janow 1994. In this recent stage of U.S.-Japan trade negotiations, the revisionist perspective on the Japanese system is said to have influenced U.S. policymakers. The revisionists argue that Japan's unique domestic structure is maintained in such a way that it is difficult for any foreign goods to penetrate and reach its consumers; they thus argue that to change the trade imbalance, there has to be a clear target with which Japan must comply (see Ito 1993, 409; Uriu 2000). The revisionist perspective is best presented by Chalmers Johnson (1995).

71. Edward Lincoln (1993, 87–92) and others argue that Japan's lack of intra-industrial trade is making the "Japan problem" much worse than is indicated by the trade numbers themselves. Nevertheless, it is worth noting that thanks to a strong yen and to repeated trade negotiations, Japanese imports of U.S. manufacturing goods doubled between the mid-1980s and the mid-1990s.

72. For example, see Tyson 1992. David Richardson (1990) has a good overview of the main characteristics of strategic trade theory.

73. The U.S. trade dependence on Japan for certain goods like semiconductors has led to a serious discussion about the security threat this represents for the United States: Japan could potentially curtail this supply, affecting U.S. defense capabilities. See Morita and Ishihara 1989.

74. In terms of profitability per capital or asset, no Japanese banks rank high. Fukushima Bank is the only one that was ranked in the top ten (twice) around the mid-1990s.

75. Shigeo Nakao (1995) discusses two theories regarding the rise of Japanese banking in the 1980s: threat versus statistical exaggeration. The original argument on the "hegemonistic threat" comes from David Hale (1990). Others who discuss the threat of Japanese yen power in the late 1980s include Daniel Burstein (1988) and R. Taggart Murphy (1989).

76. Nakao 1995, 103.

77. Yamamura 1996, 29. Yamamura also continues to argue that the capital flow from Japan to the United States was further facilitated by Japan's developmentalist state policy to boost its economy with artificially low interest rates in the 1980s, a trend that led to its "bubble economy."

78. Interviews with Japanese bankers, Tokyo, June 1997.

79. For the details of the Yen-Dollar Agreement, see Frankel 1984.

80. For an excellent account of Japan's monetary policy, with strong emphasis on its exchange rate policy against the U.S. dollar from the 1970s through the early 1990s, see Henning 1994, 121–75.

81. For the details of the discussion, see Stallings and Streeck 1995, 85–87. See also World Bank 1993; Wade 1996b.

82. Rosecrance and Taw 1990, 208.

83. Helleiner 1989. Schmiegelow and Schmiegelow (1986) also note the importance of the dynamics between government and domestic actors in determining Japan's global power.

84. The original thesis is from Organski 1958, 300–316; the quote is from Chan 1993, 109.

85. For example, James Fallows (1989) calls for the need of "containing Japan."

86. See Calder 1988.

87. Asher 1996, 220.

88. The debate surrounds the "Japanese model of development" led by a strong bureaucracy. Many Japanese policymakers and scholars, such as Ryotaro Komiya (1996) and Eisuke Sakakibara (1997), as well as some American analysts, such as Peter Drucker (1993a, 1998), assert that Japanese fundamentals are still strong and that its bureaucracy can lead Japan, one way or the other, into future recovery. Also see a debate between Helweg (2000) and Mulgan (2000).

89. However, many American observers are attacking Japan's model as "what not to do" (Desmond 1997). The critiques include Posen 1998 and Lincoln 1998.

90. For an example of such criticism, see "Reviving Japan: Time to Wake Up," *Economist* 348, no. 8087 (September 26, 1998): 21–23.

91. See Kapstein 1989, particularly on the competitiveness of Japanese banks before the rule (327). Since this standard is not applied to those banks operating solely domestically (their capital-asset ratio guideline is 4 percent instead of 8), some banks, such as Nissaigin (Nippon Credit Bank), weakened by the recession and lack of profitability abroad, retreated from international operations.

92. The United States, however, started to pour its portfolio investments into the emerging Latin American markets, particularly in Mexico, where the United States was concluding NAFTA negotiations between 1992 and 1993 (they came into effect in January 1994).

93. The relationship is not merely one-sided. When the Daiwa Bank ran into problems due to its illegal dealing in 1995, the U.S. Federal Reserve offered to support the Bank of Japan in dealing with the financial sector problems.

94. See Padoan 1990.

95. For further bargaining analyses of debtor-creditor negotiations under the debt crisis, see Aggarwal 1996.

**Chapter 3**

1. See the discussion on public goods in chapter 1.

2. However, regression analysis involves costs, including difficulties in operationalizing concepts and data limitation.

3. The Third World debt crisis of the 1980s is not over for many severely indebted low-income countries, such as those in Africa. Hence, it makes more sense to limit the case to the Latin American region.

4. The definition and distinction between ODA and OOF did not become clear until the early 1970s. Currently the standard definition of ODA (or foreign aid) is the financial assistance provided by the public sector for development objectives and with higher

concessionality (25 percent of grant element or more). The official flows that lack the second and third components are considered OOF. In the case of the Latin American region, from 1975 to 1991, the proportion of ODA within the official financial flows has ranged between 40 and 60 percent. The source for these calculations is OECD, *Geographical Distribution of Financial Flows to Developing Countries* (various issues).

5. See Iyo Kunimoto, "Japanese Migration and Its Consequences in the Context of Modern Japanese-Latin American Relations" (paper presented at a conference "Agenda on the Pacific Rim" Northwestern University, October 16–18, 1997), 23, table 4.

6. A syndicated loan involves the combined activities of a number of banks (ranging from a few to 200) in the assembly of a relatively large loan to a single borrower under the direction of one or several banks serving as lead manager. See Smith and Walter 1997, 22.

7. Interviews with Japanese bankers, Tokyo, April 1993. Devlin (1989, 99–100) notes that the insertion of Japanese finance in Latin American lending since 1976 increased competition among lenders, lowering the loan spread.

8. The MOF seemed to be in favor of the Japanese banks becoming leading banks, since the banks could earn more commission fees this way, thus offsetting the low profit margin of overseas lending. In 1980, a qualitative guideline introduced by the MOF favored the banks' role as leading banks in syndicated loans.

9. Spindler 1984, 162.

10. Devlin 1989, 122.

11. Devlin 1989, 154, emphasis added. Devlin continues with an example: "Wells Fargo drew heavily on Japanese banks which contributed approximately one-third of the funds raised in syndication by this institution."

12. See appendix 1 for the list of Latin American countries included.

13. See the discussion in chapter 2. On the one hand, noticeable fungibility exists between ODA and OOF. They serve the same purpose when it comes to increasing Japan's financial flows to indebted countries. On the other hand, the stated purpose of and forces overseeing these respective flows are different, and thus they should be disaggregated.

14. Scrutiny on the use of FILP as well as its existence (which is argued to have crowded out private financing) has dramatically increased in the 1990s.

15. Due to the data constraints, I was not able to disaggregate flows of Japanese bank lending from OECD data or to find such data from Japanese sources. Therefore, the private capital flow variable includes any private capital flows except FDI.

16. The level of confidence at 2.5 percent for the two-tailed test changes from 1.96 (degrees of freedom higher than one hundred) to 2.228 (degrees of freedom of ten).

17. See Kennedy 1992, 247–67. See also Harvey 1990; Dickey and Fuller 1981; Engle and Granger 1987.

18. As noted in chapter 2, Richard Rosecrance and Jennifer Taw (1990) have argued the importance of Japan's increasing concerns for world affairs as the size of the Japanese economy has increased. Despite Japan's increasing economic power, however, the structure of the power hierarchy of international finance in the 1980s was not altered, with the United States remaining at the top.

19. However, OOF is financed largely by FILP. FILP was once added as a control variable in OOF regression, but due to its insignificance, it was dropped.

20. Jeffrey Sachs (1989b, 17) calculates that 25 percent of the deterioration in the U.S. trade balance in the 1980s was attributed to the collapse of international finance in Latin America.

21. The U.S. Congress urged Japan in 1987 to import more from Latin American countries to provide them with foreign exchange. The link between debt and trade increased the incentive for Capitol Hill to enact trade legislation against the Japanese. See *JEI Report* 29A (July 31, 1987).

22. For example, see Mototada Kikkawa, *Mane-i Haisen, Bhunshun Shinsho,* no. 2 (Tokyo: Bungei Shunju, 1998).

23. See, for example, Yamamura 1996.

24. See Mishkin 1992, 96–97. The expected return on portfolio investment (including bank lending) is determined by the interest rate differentials plus the spread to cover the risk factor and commissions that the financial institutions charge for these transactions. The ideal way to measure this interest rate differential is to compare the domestic discount rate, which is strongly related to the domestic interest rate for bank lending, to the international interest rate, usually represented by the LIBOR (London Interbank Offered Rate—the rate of interest offered on loans to first-class banks in the London Interbank Market for a specified period, usually three to six months) plus the specific margin. This is particularly relevant for the syndicated loans of the 1970s and early 1980s.

25. Additionally, Japanese banks' relations with Japanese multinational corporations might have influenced Japan's private capital flows to the region. Because of the "follow-the-customer" mentality of Japanese banks, Japanese corporations' overseas direct investment is thought to induce Japanese bank lending to a particular region or country (see Yoon 1990). The MITI reported in 1989 that in Latin America, $1 billion (45 percent) of $2.26 billion in long-term lending for Japanese direct investment to the region was financed directly by investors, while $0.7 billion (32.5 percent) was financed by the Japanese banks. Therefore, the hypothesis is that larger Japanese FDI in a particular region should lead Japanese banks to expand their financial activities in that region. This variable, however, had to be dropped from the regression due to a severe multicollinearity problem.

26. Interview with a Japanese banker, Tokyo, June 1997.

27. For a game theoretic analysis of bargaining dynamics among the debtors, the banks, and the governments, see Aggarwal 1996.

28. The $F$ ratio for ODA regression (Model 4B) is 7.501 (critical value at 0.5 percent, 1.88), and that for OOF regression (Model 5b) is 9.413 (critical value at 0.5 percent, 2.10). See Kennedy 1992, 108–9; Chow 1960; Greene 1990, 211–14.

29. See Beck and Katz 1995. I also run these TSCS data using TSCS regressions (the Park method) and the Weighted Least Square method (suggested by Greene [1990]). The results, particularly the signs and significance of the important coefficients, are almost the same.

30. See *Wall Street Journal,* March 18, 1992. Fujimori's presidency attracted a significant amount of Japanese ODA. Peru ranked as the tenth largest Japanese ODA recipient in 1992.

31. Arrangements include the issuing of work permits in Japan, scholarships, and training (interview with a MOFA official, Tokyo, April 1993).

32. This FDI variable had to be dropped from the model due to a severe multicollinearity problem.

33. See Brook and Orr 1985, 325; Nakai 1989.

34. Various discussions on this issue can be found in government publications on economic cooperation and from the ODA Charter (*Seifu Kaihatsu Enjo Taiko*), announced on June 30, 1992.

35. There is a vast literature on the development model that Latin America pursued prior to the debt crisis (especially in comparison to the East Asian model) in terms of trade and industrial policies. For example, see Haggard 1990; Gereffi 1989. Also note Frieden 1981.

36. Interviews with Japanese bankers, Tokyo, April 1993. This notion of economic structural change can also be measured by looking at whether or not a country agreed to follow orthodox economic prescriptions under structural adjustment policies designed by IFIs, such as an SAL (Structural Adjustment Loan by the World Bank) or an SAF/ESAF (Structural Adjustment Facility and Enhanced Structural Adjustment Facility by the IMF). But when I ran regressions using these variables, they came out insignificant, so they were dropped.

37. For example, see Chenery and Strout 1966.

38. Obtaining permanent membership in the UN Security Council is noted to be one of the most important foreign policy goals of the MOFA in recent years (interview with a MOFA official, Tokyo, April 1993). Because the General Assembly of the United Nations adopts a one country–one vote system, the greater the number of countries that the Japanese government can influence is, the better its chances are.

39. No significant relationship was found between Japan's ODA allocation and its total trade with a Latin American country (Model 4, TRADE).

40. Note that since the variable measures difference between the U.S. and Japanese trade shares, DIFEX will be smaller as the Japanese trade share increases relative to that of the United States. Thus, the expected relationship between DIFEX and the dependent variable is negative.

41. Like DIFEX, YVSUSD is denominated in such a way that the Japanese yen is counted per dollar. Thus, as the yen strengthens, there will be fewer yen per dollar, making the expected relationship between YVSUSD and the dependent variable negative.

42. For ODA allocation (Model 4), the negative relationship between JLOANO and ODA is more prominent during the predebt crisis (Model 4Bb). This indicates that before the crisis, there was a clear division of labor between Japan's capital flows; that is, Japan's ODA refrained from going to some rich Latin American countries (prone to have accumulated more debt exposure to Japanese banks), while poor countries with more aid from Japan did not get much private financing.

43. Japan's ODA allocation to the Latin American region could be influenced by its ODA allocation to other regions (particularly influential is Asia, where usually more than 60 percent of Japanese ODA is allocated). Model 1C includes the variable of Japanese foreign aid to Asia (ASIAID), but it did not produce any significant results.

**Chapter 4**

1. Throughout this chapter, I distinguish between these two crises as the "1982 crisis," or "debt crisis," and the "1994–95 crisis," or "peso crisis."

2. On the strength of the synergy between the variable-oriented approach and the case-oriented approach, see Ragin 1987, 69–84.

3. All three concerns could have been addressed individually, but that would have been more problematic: helping the private financial sector would be problematic due to the negative reaction of the public if the government had to blatantly bail out banks; assisting the U.S. economy would be considered a problematic use of national resources

if done directly, and other solutions (e.g., opening Japan's agricultural market to boost its imports from the United States) are politically difficult; enhancing Japan's status in the international financial world would be difficult without a "deal" that would convince major powers in the IFIs to change the status quo in Japan's favor.

**Chapter 5**

1. Economists writing on this topic include Jeffrey Sachs (1984, 1989a, 1989b and 1989c), Benjamin Cohen (1986a, 1986b, 1992), Daniel Cohen (1991), Robert Devlin (1989), Jonathan Eaton and Mark Gersovitz (1981), Jack Guttentag and Richard Herring (1983), Suel Özler (1989), Jeremy Bulow and Kenneth Rogoff (1989), and John Williamson (1990b). Political scientists addressing it include Miles Kahler (1986b), Stephan Haggard and Robert Kaufman (1992b), Charles Lipson (1985, 1986), and sociologist Robert Wood (1986).

2. An article by Barbara Stallings (1990b) and Kinoshita 1991 are one of the two written in English on this subject. There are a few materials written in Japanese, including Tokunaga 1988; Yanagihara 1989b; and various publications from the Japan Center for International Finance (JCIF).

3. Unlike many earlier financial crises in which core countries unilaterally affected those on the periphery, this crisis was triggered by the developing countries' debts, and it pulled in major creditor countries because of these creditors' loan exposure. For a comparison of this debt crisis with early periphery financial crises, see Maddison 1985.

4. See Kraft 1984, 18–19; Volcker and Gyohten 1992, 201.

5. This $8.25 billion consists of $3.625 billion from the United States, $925 million from the BIS, and an additional $3.7 billion from the IMF (see Lustig 1996, table 1).

6. When the letter of intent for the IMF loans arrived on his desk, de Larosière insisted that there would be no IMF loans to Mexico without the commercial banks' commitment to that amount. Although his strategy received an angry response from commercial banks, it helped bring the commercial banks into the debt solution. This constituted the beginning of "concerted lending" headed by the IMF, a dominant form of rescue package operations in the 1990s as well.

7. Volcker and Gyohten 1992, 201.

8. From Latin America and the Caribbean, Argentina, Brazil, Chile, Costa Rica, Cuba, the Dominican Republic, Ecuador, Jamaica, Mexico, Nicaragua, Panama, Peru, and Uruguay concluded multilateral debt relief agreements during 1983–84 (see World Bank, *World Debt Tables,* 1994–95, 78–82).

9. See *Yomiuri Shimbun,* June 23, 1984.

10. The formal name of the Baker Plan is Program for Sustained Growth. The fifteen countries in the plan are Argentina, Bolivia, Brazil, Chile, Colombia, Ecuador, Mexico, Peru, Uruguay, Venezuela, Cote d'Ivoire, Morocco, Nigeria, the Philippines, and Yugoslavia. The coverage of the countries labeled as heavily indebted was later expanded to seventeen, including Costa Rica and Jamaica.

11. Many European banks were actually openly hostile to the plan (see *Toronto Star,* December 19, 1985).

12. See *Asahi Shimbun,* December 13, 1985. The banks emphasized that their support should be accompanied by the same effort by the debtor governments, creditor governments, international organizations, and other financial institutions.

13. Cline 1989. See also Cohen 1992, 156.

14. Nevertheless, the idea of debt reduction resonated among some policymakers (see *JEI Report* 29A [July 31, 1987]: 4–5).

15. This option exempted banks from new money obligations when they converted certain amounts of their outstanding loans to debtor countries' government bonds. This scheme was implemented to convert some debt for Argentina in August 1987.

16. For a good summary of the details of the first two programs, see Fujikawa 1988a. Some of the additional $20 billion was already committed before the announcement of the expanded program.

17. See *Washington Post,* April 23, 1987.

18. There was a discussion on the "additionality," as some people questioned how much of the money promised through this program was in addition to the amount of foreign aid and OOF that the Japanese government would provide anyway. They never reached a closure on this discussion, but many speculated that a numerical target of the recycling packages did help intensify the efforts of implementing agencies to provide more economic assistance to the countries in financial trouble, and as a result, the Recycling Program increased the amount of money given to these countries (interview with a Japanese economist, Tokyo, July 1999).

19. The idea of debt reduction was included as part of the "menu approach" of the latter half of the Baker Plan, but what was new about the Miyazawa Plan was that it also included heavy involvement of the IFIs' guarantees supported by the financial contribution of major creditor countries, especially Japan.

20. See Kinoshita 1991, 70–71. See also *JEI Report* 38B (October 7, 1988): 3–4.

21. See Cline 1989, 186.

22. See *Mainichi Shimbun,* June 14, 1988.

23. See Cline 1989, 186.

24. *Wall Street Journal,* October 14, 1988.

25. The U.S. administration was also concerned about Japan's increased influence in the IMF. See *New York Times,* September 28, 1988. In addition, there was a suspicion that the reason the Japanese were pushing for this scheme was because they wanted to arrange the deals to be more favorable to the Japanese banks (interview with an IMF official, Washington, D.C., May 1998).

26. See Rosenbluth 1991, 679–80. Jeffrey Sachs (1989b, 29) also mentions the same idea in his book.

27. Interview with a Bank of Tokyo banker, Tokyo, June 1997.

28. *Asahi Shimbun,* February 3, 1989.

29. President-elect Bush's speech on the debt problems and strategies on December 19, 1988, cited in Fujikawa 1990a, 15.

30. *Nihon Keizai Shimbun,* March 11, 1989.

31. Quote from Japanese finance minister Murayama, cited in Fujikawa 1990a, 16, my translation.

32. European banks were ready to accept some debt reduction, thanks to their large reserves and national regulatory policies that would offset the losses from debt reduction (see Lehman 1994, 209).

33. At the same IMF meeting, the United States reversed its previous position regarding an increase in Japan's IMF quota. It supported such an increase, which would move Japan's position up from the fifth largest quota (see *JEI Report* 15B [April 14, 1989]).

34. See Kinoshita 1991, 72; *JEI Report* 28B (July 14, 1989).

35. See Kinoshita 1991, 73. See also Japan Center for International Finance 1990, 16–26. Included in the $48.5 billion were $9.7 billion of Japanese commercial bank debt, but Japanese banks overwhelmingly preferred principal reduction (83 percent) and took no new money options.

36. I have divided my hypotheses into two groups, joint product and transnational linkage, for the purpose of theoretical clarity. However, this "domestic concern" component of Japan's private returns overlaps significantly with my following discussion on the transnational linkage. I here divide my discussion so that this section includes the situation under which government is actively involved in gaining such private returns (i.e., domestic stability and protection of its financial sector), while the next section includes the case of the Japanese government influenced by the pressures and demands of the private sector.

37. The MOF's role of protector of the banks is much more pertinent in Japan than in many other countries in the industrial world. Until very recently, Japanese banks had an implicit guarantee from the MOF that they would not go bankrupt (see Rosenbluth 1989, 112). Japanese policymakers and bankers call the relationship between the Japanese government and the banks a "convoy system."

38. See *Nihon Keizai Shimbun,* July 18, 1979.

39. See *Nihon Keizai Shimbun,* April 30, May 26, and December 26, 1977.

40. See *Nihon Keizai Shimbun,* December 9, 1979.

41. See *Nihon Keizai Shimbun,* January 16, 1982. The statistics are from Capital Loan Data Service, Ltd., of England, cited in the article.

42. More commission fees could offset the low profit margin of overseas lending. In 1980, a qualitative guideline introduced by the MOF favored the banks' role as leading banks in syndicated loans.

43. See Cline 1984, table 2.2.

44. This is noted by Robert Devlin (1989, 122). Andrew Spindler (1984, 201) also discusses that U.S. banks are sensitive to U.S. foreign policy and always try to guess which foreign countries carry an official "U.S. umbrella." In that sense, many Latin American countries—in particular, Mexico—do carry such an umbrella.

45. See *Nihon Keizai Shimbun,* September 19, 1982. Barbara Stallings (1990b, 7) notes: "Latin American loans were more important to Japanese banks than generally assumed. . . . Japanese exposure to Latin America was slightly *higher* than that of the United States." However, one must note that in the early 1980s, Japanese banks had a significantly lower rate of self-capitalization relative to American counterparts.

46. See *Nihon Keizai Shimbun,* November 25, 1983.

47. The total debt in Latin America is composed of about 60 percent in U.S. dollars, around 6 percent in Japanese yen, and the rest in other European currencies.

48. Part of the concern of the MOF came from the fact that it has been the Japanese banks' implicit guarantor to oversee that none of the banks would go bankrupt. However, there were real concerns regarding the Japanese banks' health, because of (1) the concentration of Latin American debt in a very few major banks, such as the Bank of Tokyo; (2) high exposure and low profitability of some of the Japanese banks' foreign operations; and (3) the thin buffer that most of major Japanese banks had against losses (again due to implicit MOF guarantee).

49. Interviews with Japanese bankers, Tokyo, April 1993. Japanese private capital flows to Latin America were fairly steady and positive until 1989 (see fig. 3.1).

50. See Kapstein 1989, 327; Rosenbluth 1989, 91.

51. See *Nihon Keizai Shimbun,* July 9, 1989.

52. Rosenbluth 1991, 684.

53. As noted by Jeffry Sachs (1989b) and mentioned in my chapter 3, 25 percent of U.S. current account deterioration was attributed to the Latin American debt crisis.

54. Jeffrey Sachs's paper on the impact of Japan's Capital Recycling Program on the improvement of the U.S. trade deficit was cited in Fujikawa 1988b. Sachs's research was said to have a noticeable impact on Japanese policymakers (interview with a Japanese economist, Tokyo, June 1996).

55. Interviews with Japanese economists, Tokyo, April 1993.

56. Senate Subcommittee on International Debt of the Committee on Finance, *Impact of the Latin American Debt Crisis on the United States,* 100th Cong., 1st sess., March 9, 1987, 114.

57. House Subcommittee on International Economic Policy and Trade of the Committee on Foreign Affairs, *The International Debt Crisis: A Review of the Brady Plan,* 101st Cong., 1st sess., April 19, 1989, 26.

58. At the congressional hearing, Treasury Department official Charles Dallara responded: "They [the Japanese] have assured us that this will be untied, and I can assure you that we will work closely with them to in the end try to avoid any inappropriate linkages here that might be developing" (House Subcommittee on International Economic Policy and Trade of the Committee on Foreign Affairs, *The International Debt Crisis: A Review of the Brady Plan,* 101st Cong., 1st sess., April 19, 1989, 26). On the Japanese side, Fujikawa (an MOF official) explains this untied nature to be an essential component of the Capital Recycling Program, so that "Japan will not lose credibility from other countries" (Fujikawa 1988a, 58, my translation).

59. The OECF has restrictions on its concessional loans to the countries whose GNP per capita is higher than an upper middle-income country as determined by the World Bank every year. In 1997, for example, the threshold for GNP per capita was $3,126.

60. See Fujikawa 1988a, 52.

61. For the details of Japan's increased FDI in the United States, see Encarnation 1992, 97–146, particularly 101, fig. 3.1. Also note table 2.3 from chapter 2 of the present book, indicating a significant increase of Japanese FDI allocation to North America (over 45 percent) in fiscal year 1985 and fiscal year 1990.

62. This voting power is set through discussions of the IMF executive board, based on the capital subscriptions of each country. See IMF, *Annual Report,* various issues, appendix 7.

63. On the point about the gap between Japan's burden sharing and its power sharing in IFIs, see Islam 1991, 221; Ogata 1989.

64. Ryokichi Hirono (1991, 178) notes that such reluctance also comes from the distrust that many of these governments had regarding Japan's ability to cooperate with them on the international financial and developmental matters in the IFI arenas.

65. Rapkin and Elston 1995, 14.

66. See Hirono 1991, 176; Rapkin and Elston 1995, 10.

67. The 45 percent increase in the overall IMF quotas after the Mexican peso crisis changed this slightly and put Japan (6.279 percent) in the second voting position, leaving Germany (6.135 percent) in the third (see *IMF Press Release* 97/63 [December 23, 1997]).

68. Interview with a banker from the Bank of Tokyo, Tokyo, June 1997.

69. See Stallings 1990b, 19.

70. Robert Devlin (1989, 122, 154) notes that well-informed American banks relied increasingly on inexperienced Japanese banks for syndicated lending during the few years before the debt crisis, while well-informed American banks stayed away from new Latin American lending before the disaster struck. Many Japanese banks increased their amount of syndicated loans in 1981 and 1982 and increasingly served as the leading bank of syndication (see *Nihon Keizai Shimbun,* January 16, 1982).

71. See Putnam 1988, 430; Schoppa 1993.

72. Frieden 1984, 153.

73. See Stallings 1990b, 20–22; *Nihon Keizai Shimbun,* November 26, 1983.

74. See Stallings 1990b; Rosenbluth 1991.

75. See Ramseyer and Rosenbluth 1993.

76. Despite the yen power of Japanese banks, the MOF was concerned about the weakness of the Japanese financial sector and believed Japan was not in a position to accrue significant losses on developing country loans (interview with a Japanese banker, Tokyo, April 1993).

77. See *Nihon Keizai Shimbun,* November 26, 1983. Information was also obtained through interviews with Japanese bankers, Tokyo, April 1993.

78. See Stallings 1990b, 20–21.

79. See *Asahi Shimbun,* March 20, 1987. The newspaper reported that the banks would continue demanding a higher rate of tax deduction for the loan-loss reserves to the government. Furthermore, a banker noted that the fact that the Japanese banks were reducing their bad loans in developing countries did not mean that they would start new loan activities there any time soon.

80. See Stallings 1990b, 20. Information was also obtained through interviews with Japanese bankers, Tokyo, April 1993. One interviewee mentioned that the system became institutionalized, and this stringent regulation on lending to developing countries discouraged Japanese banks from extending new loans to Latin America even into the 1990s. See also Latin American Information Services 1989, 61–62. Stallings (1990b, 17) also notes that the internal conflict between the Tax Bureau and the International Finance Bureau within the MOF made it difficult for the banks to achieve a tax deduction on their loan-loss reserve. The banks' demands were supported by the International Finance Bureau, which also pushed for the Capital Recycling Program discussed shortly.

81. Another book proposing debt reduction is Tokunaga 1988.

82. See Japan Bond Research Institute, *Country Risk Information,* various issues.

83. The three Brady Plan options are (1) to exchange debt for thirty-year interest reduction bonds at par (with a World Bank/IMF guarantee for repayment); (2) to swap the debt for thirty-year principal reduction bonds with 35 percent reduction in principal; and (3) to make new money commitments equal to 25 percent of the outstanding debt with no collateral.

84. Rosenbluth 1991, 682.

85. See Japan Center for International Finance 1990, 18. See also *Wall Street Journal,* February 7, 1990.

**Chapter 6**

1. *Wall Street Journal,* August 21, 1992.

2. "The Brady gamblers win, for now," *Economist* 326, no. 7798 (February 13, 1993): 73.

3. For a detailed analysis of the origin of the Mexican peso crisis (1994–95), see Sachs, Tornell, and Velasco 1996; Roett 1996a. For the Mexican perspective on the crisis, see Castañeda 1995.

4. See Bankers Trust Research, "Mexico Floats the Peso," *Emerging Markets,* December 23, 1994. According to the official figure from the Bank of Mexico, Mexico's foreign exchange reserve dropped to around $11 billion by December 16, 1994 (see Lustig 1996, 19).

5. The *Wall Street Journal* (February 3, 1995) reported very low currency reserve.

6. For a good summary of, evaluation of, and discussion of lessons from this Mexican Peso crisis, see Truman 1996, 199–209.

7. After the assassination of Mexican presidential candidate Colosio in March 1994, and as pressure on the peso increased due to political instability, Secretary Bentsen of the U.S. Treasury and Chairman Greenspan of the U.S. Federal Reserve set up a swap line of $6 billion. In April, the three parties of NAFTA signed an agreement to make this swap agreement permanent in the form of the North American Framework Agreement (NAFA). See Lustig 1996, 21–22.

8. *Nihon Keizai Shimbun,* January 4, 1995.

9. For a good summary of the U.S. initiative in assembling the Mexican rescue package (in both 1982 and 1995), see Lustig 1996. The United States General Accounting Office (GAO) has an official record of the U.S. assistance (1996, especially chap. 4). Consult also *IMF Press Release* 95/10 (Febuary 1, 1995).

10. The European governments were more concerned about Eastern Europe and their own economies at that time (see *Daily Telegraph,* January 30, 1995).

11. See Lustig 1996, 34.

12. A high-ranking former MOF official noted that the Japanese government was very supportive of the U.S. initiatives throughout the management of the Mexican peso crisis and that frequent phone discussions took place between the U.S. Treasury and the MOF in the early months of 1995. He noted, however, that there was not a direct request from the U.S. government for Japan to become more involved in bilateral financing for Mexico using its official resources (interview with an MOF official, Tokyo, June 1998).

13. *Kyodo News,* February 1, 1995 (via Foreign Broadcast Information Service [FBIS]).

14. See *Nihon Keizai Shimbun,* July 13, 1995.

15. See *Nihon Keizai Shimbun,* April 19, 1995.

16. In addition, Japan's MOF informed Japanese banks in January 1995 that they had removed the reserve requirement for lending to Mexico, a move completely opposite of what would be expected when considering the safety of bank lending in the country, whose risk had just increased significantly. The move also indicates an encouragement by the Japanese government to increase (or at least not decrease) Japanese lending to Mexico at the time of crisis (interview with a field representative of a Japanese bank, Mexico City, December 1997).

17. See *Export-Import Bank of Japan Press Release* 97-11 (September 1, 1997).

18. For an explanation of the Tequila Effect, see Truman 1996; Calvo and Reinhart 1996.

19. The Convertibility Plan was the key component of President Menem's economic strategy, which was launched in March 1991. This plan pegged the Argentine currency to the dollar at a rate of one Argentine peso to one U.S. dollar, and Argentine money supply was determined by the amount of its dollar reserve (otherwise called "currency

board"). This powerful policy instrument proved effective in coping with inflation, improving expectations of international investors, and enforcing fiscal discipline in the public sector. The plan did not, however, prevent the currency traders from attacking the Argentine peso, thus affecting Argentina's stock market when the financial environment became less favorable.

20. The measures included an international public relations campaign applauding the economy's good health and reiterating a strong commitment to the Convertibility Plan and provision of various safety nets to prevent bank closures.

21. See *IMF Press Release* 95/18 (April 6, 1995).

22. See *Nihon Keizai Shimbun,* April 1, 1995.

23. See *Nihon Keizai Shimbun,* April 29, 1995.

24. The sentiment among Japanese policymakers and investors was that Gurría was quite arrogant in dealing with the Japanese investors even as Mexico faced this crisis. It seemed quite clear that Gurría was confident that the United States would take care of this crisis and that Mexico would not need Japan's help in this case (interviews with people from the commercial banks and the government, Tokyo, May 1996). However, Japan's foreign minister Yohei Kono was reported to have rejected the Mexican foreign minister's request to use governmental influence over private banks to extend additional credit to Mexico (*Kyodo News,* January 9, 1995).

25. See *Financial Times,* January 12, 1995. It is important to note that the Mexican Peso crisis also shook Asian economies. On January 12 and 13, the Hong Kong dollar, the Indonesian rupiah, and the Philippine peso also came under attack.

26. Although some would disagree on this prediction, and although it is counterfactual and cannot be proven, the Japanese officials whom I interviewed in Japan (May 1995) had the sense that this Mexican crisis had a potential to become systemic.

27. See *Nihon Keizai Shimbun,* January 25, 1995.

28. The European governments' resentments were also presented when Germany, the United Kingdom, Switzerland, the Netherlands, Belgium, and Denmark abstained from supporting the IMF's Mexican rescue package of $17.8 billion on January 31 (see *Nihon Keizai Shimbun,* February 4, 1995).

29. Interview with a Japanese official, Washington, D.C., October 1995.

30. For a discussion on the impact of NAFTA on Japanese exporters and manufacturers, see Tsunekawa 1994.

31. See IMF, *Direction of Trade Statistics Yearbook,* 1995. Mexico's total trade with Japan declined from 6.6 percent in 1987 to 4.2 percent in 1994. For the United States, trade with Mexico occupied just below 6 percent in 1989, which increased to 9 percent in 1996.

32. President Bill Clinton also showed strong support for the idea of hemispheric integration and the Free Trade Area of the Americas (FTAA) during the Summit of Americas held in Miami in December 1994, just a few days before the Mexican peso devaluation.

33. United States General Accounting Office 1996.

34. In addition, Mexico's very new administration, which came into power less than a month before the crisis, had no expertise in identifying the channels and procedures to deal with Japanese public institutions (interview with a Japanese official, Washington, D.C., October 1995).

35. See Bank for International Settlements, *The Maturity Distribution of International Bank Lending.* Japanese banks arranged only two major new loans to Mexico in the early

1990s, totaling $450 million, both for Petroleo Mexicano. In addition, in 1992 there was a syndicated loan of $800 million to Petroleo Mexicano, the totality of which is covered by MITI insurance.

36. Thomas Biersteker (1995) discusses such changes in ideas influencing the economic policies of developing countries.

37. Nevertheless, if one compares the situation of the 1990s with that of the positions of the major debtors of the 1980s debt crisis, it is apparent that the option of turning to the Eastern bloc (or seriously considering such an alternative) or collectively defending the debtors' interests through collective action among the debtors seemed hardly feasible or practical even in the 1980s, as shown in chapter 5.

38. See, for example, Mochizuki 1997.

39. Some changes in the institutionalization of Asian regionalism are discussed by Donald Crone (1993) and Yoichi Funabashi (1993).

40. See Stallings and Streeck 1995. They call this arrangement "nonhegemonic interdependence."

41. David Asher (1996, 221) notes that the price-keeping operation (PKO) of the early 1990s was implemented by the MOF to support stock and land prices, which also tapped the state-controlled funds invested in the national pension, postal saving, and postal life insurance scheme.

42. The budget item for economic cooperation (ODA budget from General Account sources) steadily increased to 3.7 percent (FY 1994) and 3.6 percent (FY 1995) in yen terms. Economic cooperation was one of the few budget items that showed measurable growth during these years.

43. See Rapkin and Elston, 1995, 2–3.

44. See IMF, *International Financial Statistics,* 1995.

45. The deadline for complying with BIS capital adequacy requirements coincided with an overall decline of Japanese stock prices in the early 1990s. To meet the BIS deadline (March 1993) under its low self-capitalization ratio, banks were forced to cut back on their lending and repatriate some of their investment from abroad.

46. See *JEI Report* 31B (August 15, 1997); *Export-Import Bank of Japan Press Release* 97-11 (September 1, 1997).

47. See Purrington and A. K. 1991.

48. *Washington Post,* March 1, 1995. This debate continued well into the summer of 1995.

49. Interviews with officials from the MOF and the JEIM Bank, Tokyo, December 1997 and June 1996, respectively.

50. See Camdessus's speech "Prospect and Challenges in Our Globalized World Economy," given at the Wharton School of Business, University of Pennsylvania, Philadelphia. April 4, 1995.

51. See IMF 1997, 234–51.

52. Charles Kindleberger (1989) discusses various historical cases of this dynamic.

53. In addition, the lending rate was variable. The interest rates on loans were adjusted every three or six months according to the movement of the LIBOR. For more on new financial innovations that enabled the banks to extend long-term lending to developing countries, see Devlin 1989, 25–35.

54. Many argue that the resolution of the debt crisis and the resurgence of capital flows to Latin America are well connected via the Brady Plan. The plan allowed many major Latin American debtors to convert their bank debt to Brady bonds collaterized

with U.S. Treasury zero coupon assets (see Cline 1995a; Culpeper 1995). In addition, the stabilization and structural adjustment that many of these countries went through under the IMF and the World Bank led the Latin American governments to privatize much of their public or semipublic sectors, leading to an investment boom in their stocks and asset purchases.

55. See Goldstein and Folkerts-Landau 1994.

56. Cline 1995a, 427–28. The term *emerging market* actually came into use in the mid-1980s, when the International Finance Corporation (IFC) of the World Bank was trying to beef up support by private investors for a Third World investment fund. The first emerging market fund came out in 1986 and quickly became a boom (see *New York Times,* February 15, 1999).

57. Herzog (then Mexican ambassador to the United States), speech at the Conference on Financial Globalization and Emerging Markets: Policy Autonomy, Democratization, and Lessons from the Mexican Crisis, Brown University, November 18, 1995.

58. See, for example, Calvo, Leiderman, and Reinhart 1993; Fernandez-Arias 1996.

59. See Cline 1995a, 424–30.

60. See Ramirez de la O 1996.

61. See World Bank, *World Debt Tables,* 1994–95, 10. From the level of capital inflows, these countries include China, Mexico, Argentina, Thailand, South Korea, Brazil, Portugal, Malaysia, Turkey, Greece, India, Indonesia, Chile, Hungary, Venezuela, the Czech Republic, Poland, the Philippines, Colombia, and Peru.

62. In addition, due to the structure of some mutual funds, such as the Latin American fund, mutual fund investors hit by a major loss in Mexico had to pull out money from other places that constituted the same fund to compensate for the losses. Thus, they took capital out of such countries as Argentina regardless of the countries' creditworthiness or economic fundamentals. See Truman 1996, 202.

63. See *Nihon Keizai Shimbun,* January 7, 1995. The amount of $3 billion was discussed in informal consultations, and later the amount was reduced to $0.8 billion, when the formal request came from Mexico (see *Nihon Keizai Shimbun,* January 11, 1995).

64. Interview with a Japanese banker, Tokyo, October 1995.

65. Interview with a JCIF researcher, Tokyo, June 1995.

66. Interviews with Japanese bankers, Tokyo, April 1993. Some note that the internal structure of banks changes to accommodate the amount of business. Hence, more sections are now devoted to Asian business and very few to Latin American. Most of the bankers stress recent memory and the repeated failure of their businesses in Latin America and hold out little possibility that they will expand their operations in that region any time soon.

67. See Chuhan and Jun 1995, 92–94.

68. Japanese investors began getting into the Mexican market in late 1994, when American investors became cautious and the market was at its highest level (see *JEI Report* 2B [January 20, 1995]: 7–8).

69. For discussion on the party politics after the 1993 shift, see Kohno 1997.

70. See Mabuchi 1997, 338. However, the MOF's friends in the LDP have helped the MOF protect its core base in the reform efforts (see Hartcher 1998, 244–46).

71. See Hollerman 1988a; Pempel 1997.

72. See Yamamura 1994; Pempel 1997; Daniel Okimoto, "The Japanese Financial Crisis: A Need to Search for a New Paradigm?" (paper presented at the University of Cali-

fornia Conference on the Political Economy of the Japanese Financial Crisis, Los Angeles, February 26, 1999).

73. Pempel 1997, 348.

**Chapter 7**

1. By mid-2000, there seems to be a consensus that the Asian financial crisis is over (see *New York Times,* May 27, 2000; *Los Angeles Times,* June 3, 2000). However, this study, focusing on the international aspects of the Asian financial crisis, considers that the height of the Asian crisis, requiring financial crisis management, was over by the end of 1998. Nevertheless, some discussion on the future plans are still being held into the year 2001.

2. Based on the contrast between the two regions in the 1980s, several well-informed books were published. They cover regional industrial policies (Deyo 1987; Haggard 1990); economic adjustment (Nelson 1990; Haggard and Kaufman 1992b); and financial policies (Haggard, Lee, and Maxfield 1993).

3. The difference between the regions comes from the difference in the problems facing their respective economies prior to the crisis. Latin American countries faced the problem of macroeconomic fundamentals, leading to the balance-of-payments crisis. In Asia, the sudden loss of confidence by the international capital market, which was triggered by bankruptcies of banks and corporations in the region, led to the crisis. See Palma 1998, 800–802.

4. Many books have been written on the subject of economic regionalization in Asia in the 1990s, including Lincoln 1993; Funabashi 1995; Katzenstein and Shiraishi 1997; Nishijima and Smith 1996; Frankel and Kahler 1993; Hatch and Yamamura 1997.

5. Japan also appeared to pursue its narrow economic self-interest through its exports to these countries until the 1970s, which caused nonpurchase movements of Japanese goods in various countries. To improve Japan's relationship with Asia, the Fukuda Doctrine toward Southeast Asian countries was announced in 1977, stressing the equal partnership and mutual understanding between Japan and ASEAN countries. The Japanese government also dramatically increased its foreign aid to these countries from 1978. See Sudo 1988.

6. Even in the context of the Asian crisis, the presence of China as a counterweight or rival to Japan is a critical factor. See, for example, Funabashi 1995, 162–65. The decision of the Chinese government not to devalue its currency in the aftermath of the Asian crisis has been praised by the United States and other countries, making the Japanese government very nervous about China's increased positive role in Asia. In addition, although it is not extensively covered in this study, chapter 8 notes that the opposition of the Chinese government to the wider use of the yen and to the idea of a strong financial mechanism in Asia under Japan's leadership has made a regional solution of the crisis much more complex.

7. The 1994–95 Mexican currency crisis does not provide a good comparison in this sense, because the U.S. economy was quite fully recovered then, and the United States had a higher economic capacity to deal with regional crisis then than during the debt crisis.

8. The U.S. president, Bill Clinton, was cited as saying, before the APEC meeting in Vancouver, Canada: "We just want to be in a position to be supportive when we can, but

I think Japan can lead Asia out of this difficulty with the strength of its economy" (*New York Times,* November 25, 1997).

9. *Nihon Keizai Shimbun* has several articles (see, e.g., January 17, 1998; February 5, 1998) criticizing Japan's lack of initiative and active commitment in early 1998.

**Chapter 8**

1. There has been a debate between prominent economists regarding the costs and benefits of financial globalization for emerging market countries and the causes of the "financial crises of the twenty-first century." For a cautious view on the financial liberalization and its impact on developing countries, see Joseph Stiglitz (the World Bank's former chief economist), "Boats, Planes, and Capital Flows," *Financial Times,* March 25, 1998.

2. There are several interrelated aspects of the Asian crisis; its degree of severity depends on the country considered. Problems ranged from currency crises (immense devaluation and volatility of currencies); financial crisis, both domestic (stock market volatility and vulnerability of banking sectors, leading to credit crunches) and international (capital flight and accumulation of external debt); and other economic and social crises (bankruptcies, unemployment, social instability, political instability). In this chapter, I focus on currency and international financial crises in Asia.

3. One of the earlier publications addressing these issues is by Morris Goldstein (1998). Later came a book by Haggard (2000), edited books by Pempel (1999b) and Noble and Ravenhill (2000), as well as various special journal issues on the Asian crisis (e.g., *World Development* 26, no. 7 [1998]; *Cambridge Journal of Economics* 22 [1998]; *Brookings Review* 15, no. 3 [summer 1998]). In addition, see Krugman 1998; Wade 1998a, 1998b; Feldstein 1998; Sachs 1998; Fischer 1998; Noland, Liu, Robinson, and Wang 1998; Mallaby 1998; Kawai 1998a, 1998c; Huang and Xu 1999. Lastly, there have been numerous publications from the World Bank and the IMF, such as *International Capital Markets.*

4. For a descriptive analysis in English of the Japanese government's actions in the Asian financial crisis from the AMF to the New Miyazawa Initiative, see Hamada 1999.

5. To prevent a replay of the Mexico-type currency crisis, which also shook some currencies in Asia in 1995, the chairman of the Australian Federal Reserve Bank, Bernie Fraser, advocated an Asian version of the BIS. He envisioned a strong coordination mechanism among the Asian central bankers, with a bridge loan facility in preparation for regional financial emergencies. By November 1995, the Asian countries Thailand, Indonesia, Malaysia, Hong Kong, and Singapore (in December) joined an agreement for mutual cooperation to cross-support their currencies (see *Nihon Keizai Shimbun,* May 15, 1997).

6. See "Just what the doctor ordered?" *Economist* 344, no. 8027 (July 26, 1997), 73.

7. See *IMF Press Release* 97/33 (July 18, 1997). This EFF credit came in the form of an extension of the ongoing three-year EFF initiative of June 24, 1994, which was due to expire on July 23, 1997.

8. The Thai government was reportedly hoping to receive significant financial support from Japan without resorting to the IMF, but the Japanese government was insistent on having an agreement with the IMF as a precondition for Japan's additional financial support (*Bangkok Business Day,* July 31, 1997 [FBIS]).

9. See *Nihon Keizai Shimbun,* August 12, 1997; *IMF Press Release* 97/37 (August 20,

1997). Asian contributors to the package were Australia, Malaysia, Singapore, and Hong Kong at $1 billion each; Korea, Brunei, and Indonesia at $0.5 billion each; and later China at $1 billion.

10. *New York Times,* October 31, 1997. This point was also noted by many IMF officials whom I interviewed in Washington, D.C., in May 1998.

11. The U.S. Senate came up with a resolution preventing Washington from committing more than $1 billion in aid in any one year without congressional approval, unless the administration could prove the commitment vital to U.S. national interests. This amendment expired on September 30, 1997. See "Pacific Divide," *Far Eastern Economic Review,* November 6, 1997; *Congressional Press Releases,* August 8, 1995.

12. Quote of Japanese IMF deputy managing director Shigemitsu Sugisaki in *Bangkok the Nation,* August 12, 1997 (FBIS). Camdessus's comment in February 1997 on the possible regional arrangement to solve the regionalized financial crises reportedly helped form such an idea (interview with an MOFA official, Tokyo, June 1998).

13. *Nihon Keizai Shimbun,* August 19, 1997.

14. See *Hong Kong AFP,* September 18, 1997 (FBIS); *Nihon Keizai Shimbun,* September 23, 1997.

15. See *Nihon Keizai Shimbun,* September 22, 1997; "Rumpus in Hong Kong," *Economist* 344, no. 8036 (September 27, 1997): 15; "An Asian IMF?" *Economist* 344: 15, 84. For an analysis of the Japanese government's engagement in this unusually active and controversial initiative, see *JEI Report* 47A (December 19, 1997).

16. See *Nihon Keizai Shimbun,* September 22 and 23, 1997. Some even note that the very reason why the Japanese government pushed for the AMF scheme was to maximize its leverage in seeking more influence within the IMF. See Rowley 1997.

17. The most vocal advocate of this view is Malaysian prime minister Mahathir Mohamad (see *Nihon Keizai Shimbun,* September 14, 1997).

18. See JEI Report 47A (December 18, 1997), 8–9.

19. Actually, Tokyo gave up the idea even before this meeting (see *Kyodo News,* November 10, 1997).

20. See Rowley 1997, 1. The Manila Framework, an agreement reached during the APEC financial ministers' meeting, includes (a) establishment of a regional financial surveillance mechanism to complement global surveillance, (b) technical support to strengthen the financial sectors in each of the participating countries, (c) a call for increased IMF responsiveness in preparation for new financial crises, and (d) regional supporting mechanisms to complement the crisis management by IFIs, including the IMF. These components of the Manila Framework incorporate many of the ideas from the AMF scheme. See "Ajia tsuka kiki ni manabu," report by the Committee on Foreign Exchange and Other Transactions under the MOF, May 19, 1998, 13–14.

21. *Hong Kong AFP,* November 30, 1997 (FBIS).

22. Ever since that crisis, Thailand has been a vocal critic of the U.S. lack of interest in helping resolve economic problems in Asia. For example, see the "The Generosity of the United States, Our Great Friend, Is Even More Scarce in Time of Crisis," *Bangkok Matichon,* January 15, 1998 (FBIS). The U.S. government later became quite supportive of Thailand, because the country implemented relatively smooth economic adjustment programs and followed the IMF rules obediently, particularly in comparison to Indonesia.

23. See *Nihon Keizai Shimbun,* November 1, 1997. The *New York Times* (November 1, 1997) reported that the Clinton administration justified the U.S. financial commitment to help resolve the Indonesian crisis as follows: (a) to stop market contagion, particularly

to emerging market countries in Latin America; (b) to use this opportunity to further open the world market; and (c) to prevent market instability from turning into something more ominous. In addition, a State Department official noted that the U.S. financial contribution was "an untenable policy"; that is, "If you want to deal the cards, you have to buy some chips" (*New York Times,* October 31, 1997).

24. The "second line of defense" is a promise in which a central bank of a country in balance-of-payments difficulty could request a loan in reserve currency (usually in U.S. dollars). The central banks of the participating countries then deposit into the central bank account of the country in difficulty the amount of reserve currency committed. This idea was convenient for both the United States and Japan: the U.S. executive branch could commit a certain amount of money to the financial crisis management of Indonesia and still avoid a major fight with Congress (see *JEI Report* 42B [November 7, 1997]), and the Japanese government did not have to resort to the usual JEXIM Bank untied loans, as the JEXIM Bank's budget was depleted due to its financial commitment of $4 billion for the Thai case (interview with an MOF official, Washington, D.C., May 1998).

25. The second line of defense was constructed by bilateral funds, including contributions from Japan and Singapore ($5 billion each), the United States ($3 billion), and Australia ($1.43 billion). Other contributors included China, Malaysia, and Brunei. See *New York Times,* October 31, 1997; *IMF Press Release* 97/50 (November 5, 1997).

26. Martin Feldstein (1998) notes that the Korean financial crisis did not share the same nature as other crises of Asia during the fall of 1997.

27. The various sources of this information include *Korean Times,* November 15, 1997 (FBIS).

28. Major creditor governments, such as the United States, Canada, and Japan, were consulted for their bilateral financial support, but all of them advised the Korean government that it had to involve the IMF first (see *Nihon Keizai Shimbun,* November 21 and 23, 1997).

29. See *Asahi Shimbun,* November 22, 1997.

30. *Asahi Shimbun,* November 29, 1997; *Korean Times,* November 30, 1997 (FBIS).

31. First, the sum of the package was announced as $55 billion, but some European countries, such as Italy, joined the package later, expanding the total amount to $57 billion.

32. See *IMF Press Release* 97/55 (December 4, 1997); *Financial Times,* December 4, 1997. Some OECD countries did not specify the exact amount of their financial commitment. No Asian country participated in the financial rescue package this time. It is also worth noting that a part of the Korean rescue package represents the first time that the IMF used the Supplemental Reserve Facility (SRF) approved by the IMF board on December 17, 1997 (see *IMF Press Release* 97/59 [December 17, 1997]).

33. See *New York Times,* December 30, 1997.

34. See *Nihon Keizai Shimbun,* January 29, 1998.

35. In this system, the country fixes its exchange rate per dollar and determines the country's domestic supply of rupiah based on the amount of foreign currency it holds. This system, in effect, makes the country abandon all flexibility on its monetary policy and provides a full commitment to its fixed exchange rate.

36. See *Nihon Keizai Shimbun,* March 14, 1998. Although Washington has reportedly feared Japan's "soft" stance vis-à-vis Indonesia, one newspaper also speculated the possibility of a consultation between the United States and Japan regarding their respective

negotiation strategies with Indonesia (i.e., playing "good cop" and "bad cop" roles) while U.S. envoy Mondale made a several-hour stopover in Tokyo on his way to Jakarta (*Nihon Keizai Shimbun,* March 3, 1998). Later, the Japanese government also pledged $1 billion in JEXIM Bank untied loans to Indonesia on April 6 to entice the Indonesian government to reach an agreement with the IMF, which was realized two days later (see *Nihon Keizai Shimbun,* April 7 and 8, 1998).

37. See *JEI Report* 22B (June 12, 1998); *New York Times,* June 5, 1998.

38. Nevertheless, Indonesia continues to suffer from economic, political, and social instability, which caused concern among major powers in the realms of both economics and security into 1999.

39. For examples of domestic criticisms about the Japanese government's unresponsiveness and its banks' passive attitude and lack of initiatives, see, respectively, *Nihon Keizai Shimbun,* January 17 and February 5, 1998. On this view, see also *JEI Report* 8A and 8B (February 27, 1998). From the United States, the *New York Times* (February 22, 1998) noted, "the United States and its European allies have identified a new villain in the Asian financial crisis: not currency market speculators, not the crony capitalists of Indonesia and Korea, but the paralyzed Japanese government."

40. See *Nihon Keizai Shimbun,* February 23, 1998. Also, the United States has been frustrated by its mounting trade deficit against Japan. Commerce Secretary William Daley noted, "Japan has to understand the political reality in Washington, [in which] a soaring trade deficit and an election year are not a good mix for them" (*New York Times,* February 22, 1998).

41. See *Nihon Keizai Shimbun,* February 21, 1998.

42. See *Nihon Keizai Shimbun,* April 25, 1998; *New York Times,* April 25, 1998; *JEI Report* 17B (May 1, 1998).

43. Ministry of Foreign Affairs, "Misperception and Truth about Economies of Asia and Japan" (April 17, 1998, mimeographed).

44. Some academic discussions and publications were circulating during this time and a few months later. For example, on Japan's role in East Asia, see Kunimune 1998 and Tamaki 1998. In addition, the Japanese official position on the issue is reflected in "Ajia tsuka kiki ni manabu," report by the Committee on Foreign Exchange and Other Transactions, May 19, 1998. A whole series of publication has come out in 1999 and 2000 on the Asian crisis including Aramaki (1999), Hirata et al. (1999), Ito (1999b), Kunimune (2000), Kwan (1998), Shimazaki (1999), and Yoshitomi and Shirai (2000).

45. A publication by the newly established Asian Development Bank Institute (Yoshitomi and Ohno 1999) called for an alternative to the IMF's approach to financial crisis management. Actually, the one public figure who consistently pursued Japan's independent initiative in the Asian crisis management was then (and is now) Eisuke Sakakibara, then the MOF's vice minister of finance for international affairs.

46. In addition, massive withdrawal of Korean investment from Russia and lowering of oil prices due to the declining oil demand from Asia negatively impacted the Russian economy in 1998.

47. See *IMF Press Release* 98/31 (July 20, 1998). The Japanese government was the only bilateral financial contributor to this additional rescue package promising $1.5 billion through JEXIM Bank untied loans. The loan had already been promised to Russia in April (see *Nihon Keizai Shimbun,* July 14, 1998). See also *New York Times,* July 17, 1998; *Los Angeles Times,* August 18, 1998.

48. On July 28, 1999, the IMF approved a standby credit of $4.5 billion to support its

1999–2000 economic program (see *IMF Press Release* 99/35 [July 28, 1999]). The new loan was extended, reportedly, in order for Russia to avoid defaulting on international loans (see *Financial Times,* March 30, 1999; *New York Times,* March 30, 1999).

49. *New York Times,* October 25, 1998.

50. The IMF standby credit of $18 billion was approved on December 2, 1998. Other financial contributors included the World Bank ($4.5 billion) and the IDB ($4.5 billion). In addition, twenty or so creditor governments (including the United States and Japan), through or in coordination with the BIS, committed the total of $14.5 billion. See *New York Times,* November 13 and 14, 1998; *IMF Press Release* 98/59 (December 2, 1998); *Asahi Shimbun,* November 14, 1998).

51. See *Financial Times,* January 14, 1999; *New York Times,* January 15, 1999. The first devaluation came in the form of widening the monetary unit's band by 8 percent, and complete floating of the real came on January 18, 1999.

52. The Brazilian government and the IMF renegotiated their November package in March 1999 and agreed that $9 billion of IMF and other funds would be released (see *Financial Times,* March 9, 1999).

53. *Asahi Shimbun,* September 25, 1998. However, at the time of the Brazilian crisis, the *New York Times* (October 25, 1998) reported a comment of a U.S. official claiming that the fact that Germany and Japan were reluctant to part in its financial rescue package suggested that Latin America was becoming chiefly Washington's problem.

54. See *Nihon Keizai Shimbun,* October 1, 1998; *Washington Post,* October 1, 1998; *JEI Report* 37B (October 2, 1998). For the details and content of the initiative, see the MOF's Web page, <http://www.mof.go.jp.>. The list of countries covered in the plan was later extended to include Vietnam.

55. For example, after the U.S. Congress and Senate passed the subscription of $18 billion in capital to the IMF at the end of October 1998, the United States proposed a precautionary credit line including a capital increase of $90 billion in the IMF. The G-7 countries supported this. See *Financial Times,* October 31, 1998.

56. *Nikkei Weekly,* November 16, 1998.

57. The total amount of this AGRI fund also included contributions from the World Bank and the ADB. The U.S. money would support trade and investment in these countries, and Japan would provide at least $3 billion in addition to the already announced aid package of $30 billion through the New Miyazawa Initiative. See *New York Times,* November 18, 1998; *Nihon Keizai Shimbun,* November 17, 1998; *JEI Report* 44B (November 20, 1998).

58. See *Asahi Shimbun,* December 17, 1998. The Japanese government also stated that this financial aid would be tied to the recipient countries' procurement from Japan, to help Japan's private sector and boost its economy. Some Asian countries named as beneficiaries of the New Miyazawa Initiative had already been supported. The major financial support already indicated as of February, 2000 are to countries such as Thailand ($2.9 billion), the Philippines ($2.5 billion), Malaysia ($4.35 billion), and Korea ($8.35 billion), and Indonesia ($2.9 billion). See <http://www.mof.80.jp/english/if/e1e042a.htm> (downloaded December 5, 2000).

59. This bond guarantee package is sometimes called a "second stage" of the New Miyazawa Initiative. Japan's announcement came on May 15 at the time of the APEC finance ministers' meeting in Langkawi, Malaysia (see *Nihon Keizai Shimbun,* May 15, 1999; *Financial Times,* May 17, 1999). The JBIC was to be established on October 1, 1999, by merging the JEXIM Bank and the OECF.

60. Notable comments by the Asian leaders include one from Korean prime minister Kim Jong Pil on November 30, 1998 (see *Korean Times,* November 30, 1998), and another repeated by the Malaysian prime minister Mahathir Mohamad (see *Nihon Keizai Shimbun,* September 20, 1997). Even very recently on November 4, 2000, Thailand's finance minister supported the plan (*Asahi Shimbun,* November 5, 2000).

61. The $3 billion came from the fund that the Japanese government earmarked for the bond guarantee facility announced in May 1999.

62. See *JEI Report* 13B (March 31, 2000).

63. See Council on Foreign Exchange and Other Transactions (Gaikoku Kawase tou Shingi Kai) 2000. Appendix, 80–86 on the details of the scheme.

64. The upper house of the Japanese Diet passed the Financial Function Early Restoration Law on October 12, 1998, to help the banks get bad loans off their books and to enable the government to deal with bank failures. Although financial problems in Japan continued after the passage of this law, it set up the needed framework for the Japanese government to tackle the domestic crisis actively and systematically. See Amyx 2000 for an analysis of how financial crises in Japan are closely connected to troubles in Asia.

65. The weakened Asian currency helped Japanese companies export their goods produced in these countries to third markets. The MITI's survey indicates that 60 percent of respondents would not even rethink their Asian strategies because of the crisis, while 82 percent reported high hopes for developing production bases in these countries (ASEAN plus Korea) in the near future (MITI 1999, 165–71). Hatch and Yamamura (1997) characterize the uniqueness of Japanese FDI in Asia through a complex web of integrated vertical production networks.

66. See, for example, *Korean Times,* April 20, 1998; *Maeil Kyongje Sinmun,* February 10, 1998.

67. There have been some worrisome declines in the U.S. stockmarkets including the NASDAQ in the fall of 2000 and it is likely to lead to a major slowdown of the U.S. economy.

68. This point is illustrated by the first meeting between President Clinton and Prime Minister Obuchi, in September 1998. The key issue of their discussion was macroeconomic policy, which reflected U.S. concern about Japan's role in the Asian financial crisis (see *Journal of Commerce,* November 18, 1998).

69. Japanese direct investment in the United States (accumulated assets at the end of 1996) was $100 billion, slightly more than one-third of Japan's accumulated FDI assets abroad (see Bank of Japan, *Balance of Payments Monthly,* April 1997, 161).

70. As I noted in chapter 5, the BIS came to an agreement in December 1987 that member country banks (including Japanese banks) operating overseas would adopt a bank capital-asset ratio of 8 percent. Because the level of Japanese banks' capital was declining due to their weaker stocks, the agreement discouraged Japanese banks' loan extension.

71. The amount of bad loans (both nonperforming and extremely risky) granted by Japanese commercial banks is now reported to be between $600 billion and $1 trillion. The recuperation of these bad loans has become much more difficult due to Japan's declining and very low land prices. Most Japanese banks took land as their only collateral during the 1980s, because of its high value and the belief that prices would continue to rise. Facing these challenges, internationally weak banks like Nissaigin (Nippon Credit Bank) decided to limit their financial operations to Japan so that they could cut back on their overseas expenses, would not have to comply with the 8 percent BIS capital-asset

ratio, and thus could concentrate on regaining strength domestically. Some banks decided to weather the financial storms by either creating (or attempting to create) an alliance or by merging in part with financial institutions from the United States or Europe (e.g., Sakura Bank and Deutsche Bank, the Long-Term Credit Bank and the United Bank of Switzerland, the Industrial Bank of Japan and Travelers).

72. Even though there is still a high Japanese trade surplus against the United States, and even with Japan's financial retreat from the United States, the booming U.S. economy, with higher interest rates, created an environment of a higher dollar and a weaker yen particularly in 1997 into mid-1998. The shift from this trend came as the Russian and Brazilian crises hit the United States, and the U.S. Federal Reserve Bank (and other central banks in various European countries) lowered their interest rates between the summer and fall of 1998. The Japanese yen has appreciated significantly since the fall of 1998, raising questions about what is driving the appreciation (see *Financial Times,* January 7, 1999). The strong yen phenomenon is considered good for the Asian countries in crisis, because they can compete with Japanese goods much better in third countries and can also penetrate the Japanese market much more easily. However, it is devastating for many Japanese firms that were counting on the strategy of "exporting their way out" from severe recession.

73. Interview with an MOF official, Tokyo, June 1998.

74. Interview with an MOF official, Tokyo, June 1998. Actually, this view contradicts a comment from a former manager of the Bank of Tokyo who conveyed that he had been a part of discussion on the AMF idea from the beginning to the end. I have no way of telling who is exaggerating his point. In any case, even the Bank of Tokyo manager mentioned that due to the limited participation of the Japanese banking sector in the formulation of the scheme, the MOF could not create a framework that rallied the private sector to support and participate "on a voluntary basis" (interview with a former manager from the Bank of Tokyo, Tokyo, June 1998).

75. See Wade's debate on the Asian and IMF solutions (Wade 1998b). A particularly strong initiative was also taken by Vice Minister Eisuke Sakakibara of the MOF.

76. Interviews with a few Japanese bankers (Tokyo, June 1998) revealed that even though most of them did not publicly convey this reaction, they welcomed the possibility of having a large fund available to "bail them out" of the crisis.

77. See the interview article with a former president of Nissho Iwai, a Japanese trading company, in *Asahi Shimbun,* November 6, 1997.

78. *Asahi Shimbun,* September 20, 1997.

79. A very similar debate took place more than twenty years ago between the IMF and the OECD, on the Financial Support Fund idea presented by the OECD. See Cohen 1997, especially 14.

80. See *JEI Report* 47A (December 19, 1997), 9–10.

81. An IMF official noted that the ideas from the AMF survived within the IMF's structural change mandated in the Manila Framework and that, in a sense, it was a progressive step taken through the AMF (interview with an IMF official, Tokyo, June 1998).

82. For an analysis regarding the perspective of Japan's finance minister Kiichi Miyazawa on the need of a new and different architecture, see Yanagihara 1999.

83. See Wade 1998b, 1545–47; *Financial Times,* February 26, 1998.

84. Wade (1998b, 1540) maintains that the main and economic reason why these countries established more leveraged economies was because of their high household savings. Since the only way these ordinary people channel their savings into investment

is via banks, banks tend to have a strong incentive to lend to companies for their returns. Thus, this creates a high debt ratio of firms. World Bank researchers pointed out the possible danger of Asian financial sector weakness before the outbreak of the Asian crisis; see Claessens and Glaessner 1997.

85. However, the bank lending of the 1990s has a higher weight of project lending than do syndicate loans, which might loosen transnational linkage due to the structure of the loans.

86. Obviously, this phenomenon is nested in a larger issue of how important the financial crisis was to the international financial community overall. The more widely spread the repercussion felt among various creditor countries was, the stronger the concerns of the systemic impact were.

87. Interviews with Japanese bankers, Tokyo, June 1998.

88. See, for example, Asher 1996, 218; Mabuchi 1997, 14.

89. This is called a price-keeping operation (PKO), as noted in chapter 6, footnote 41. For details, see Asher 1996, 221–22; Wood 1994, 103–6.

90. The MOF, which wanted to be freed from the LDP's reign, gained its power by dealing with and guiding the inexperienced Morihiro Hosokawa cabinet and allying with "reformer" Ichiro Ozawa's new party in 1993. Its bet of breaking loose from the LDP in 1993 turned around to haunt it within a year, as the LDP along with the Social Democratic Party and the Sakigake Party regained coalition majority and began "revenging" the MOF for betraying the LDP during its most trying times.

91. In 1995, the collapse of Hyogo Bank, the scandal surrounding Daiwa Bank, and corruption charges against MOF officials rocked Japan's financial sector. The major case of mismanagement came at the time of the Jusen (housing loan companies) rescue, which required ¥685 billion of taxpayers' money from fiscal year 1996. See Suzuki 1996, 21; Mabuchi 1997, 6–28.

92. See Hartcher 1998, 156–57.

93. Major corruption charges in early 1998 alleged that MOF officials were "treated" by bank employees in exchange for information about the MOF's bank inspection details (*JEI Report* 9A [March 6, 1998]).

94. An official "liaison conference" was set up by Prime Minister Hashimoto in early February 1998 so that financial firms and the MOF could have a new forum in which to exchange information and opinions on financial issues on a regular basis (*JEI Report* 9A [March 6, 1998]: 9–10). However, many bankers noted that such a formal setting would not allow them to convey the frank opinions or sensitive information that they used to discuss in the after-work "drinking" setting (interviews with Japanese bankers, Tokyo, June 1998).

95. Stallings 1990b, 18–19.

96. There have been some efforts by both the Japanese government and the Bank of Tokyo-Mitsubishi to preserve such a function. For example, a new research institution, the Institute for International Monetary Affairs (IIMA), was established in December 1995, fully funded by the Bank of Tokyo, with a prominent former MOF official as the president, to analyze international monetary and financial issues (interviews with former Bank of Tokyo managers, Tokyo, June 1998; see also the IIMA website, <http://www.fastnet.ne.jp/iima>, for its prospectus).

97. See *Washington Post,* December 28, 1997.

98. See *New York Times,* December 31, 1997.

99. See *Washington Post,* December 28, 1997.

100. Interview with a former manager from the Bank of Tokyo, Tokyo, June 1998. There was a meeting of an international bank consortium at the end of January 1998, when short-term loans amounting to $24 billion from foreign banks to Korea, due in 1998, were given extensions of one to three years (see *Nihon Keizai Shimbun,* January 29, 1998).

101. Interviews with Japanese bankers (especially the ex-manager of the Bank of Tokyo), Tokyo, June 1998.

102. Interviews with a Japanese financial journalist and bankers, Tokyo, June 1998. See also *Asahi Shimbun,* December 20, 1997.

**Conclusion**

1. See Keohane 1984.

2. As I discussed in chapter 1, a "k-group" is an intermediate group of major powers that engages in collective action to provide public goods in the absence of a clearly dominant single hegemon. See Snidal 1985.

3. Interestingly, though not analyzed in this study, more elements of competition (e.g., trade) occur in the Japanese relationship with Asia than in U.S.–Latin American relations.

4. As I discussed in chapter 5, the U.S. Congress grew concerned that by making a large financial commitment to Latin America, Japan might threaten U.S. economic interests in the region. From this discussion, it was clear that a sense of "territory" or turf exists for the United States in Latin America.

5. As in the case of earthquake insurance, when everyone in a region gets hit by a disaster at the same time and claims their payments, the insurance system does not work (interview with an IMF official, Mexico City, December 1997).

6. The Mexican peso crisis presents a clear opposite picture from the Latin American debt crisis, in which case the Japanese government did not see much, if any, private returns from active engagement and thus was very reluctant to act.

7. Wade (1998b, 1545–47) calls the agent of such scheme "the Wall Street–Treasury–IMF complex." See also Bhagwati 1998.

8. See, for example, *New York Times,* January 17, 1998. For a critique against such arguments, see Wade 1998b.

9. *International Herald Tribune,* January 20, 1998.

10. Fukuyama 1992. On the implication of this triumph and of the Washington consensus on developing countries, see Biersteker 1995.