Japan's Importance to the U.S. and Southeast Economies

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It's an honor for me to join you this evening as your speaker for the Japan-America Society of Georgia annual dinner.

I'm here tonight as both the president of the Federal Reserve Bank of Atlanta and a former banker and private citizen who is a longtime admirer of many things Japanese. Earlier in my career I had substantial experience with Japanese companies and visited Japan several times. My talk will represent both my perspective as a current Federal Reserve official and musings and remembrances from earlier experience.

Rise of China and India

I'd like to begin my remarks with a potentially controversial statement. Japan has receded in the consciousness of the American business community, and public attention in this country has turned away from the relationship between the United States and Japan. For the last few years, China has been top of mind. Americans have grown increasingly aware of the rise of China as a manufacturing powerhouse and destination for offshored American manufacturing jobs, as a consumer product exporter to our market, and, recently, as an important financial and industrial investor in U.S. assets. I could add to that the growing profile of India as a services provider.

But I don't need to tell this group that Japan still matters to the United States and especially to the economy of the Southeast region. And the Southeast is important to Japan. Let me flesh out the picture.

Japan's importance to the U.S. Southeast

For the purposes of my argument, I will define the Southeast as roughly the same geography as the Sixth Federal Reserve District, which includes all of Georgia, Florida, and Alabama and parts of Mississippi, Louisiana, and Tennessee. We could add other states to my definition of the Southeast, and that would only serve to strengthen the case.

This region is economically diverse, with a composition of industries similar to the nation as a whole. The population of the six states in this region is about 45 million, and the region's economic output last year was about $1.8 trillion. If the region were ranked as a nation, the Southeast's economy would rank eighth in the world, below Italy and above Canada. By comparison, Japan, the second-largest economy in the world, had a GDP in 2007 of $4.4 trillion.

For the past two decades, the Southeast has grown more rapidly than the United States as a whole. There are many reasons for this growth, but among them is the region's attractiveness to businesses, including foreign investment. Japan has been a very important source of investment throughout the United States and especially in the Southeast.

Japan is the second-largest investor in the United States (after the United Kingdom). Japanese companies in 2005 employed about 614,000 people in the United States, including more than 100,000 in the Southeast as defined by the Atlanta Fed's Sixth District states. That number is up from about 90,000 in 1995, which suggests Japan's economic commitment to the Southeast is ongoing.

Within this region, Georgia plays an important logistical role. This state offers excellent port and air transport facilities along with other essential commercial infrastructure. Between 2002 and 2005, Japanese firms increased their investment in commercial property in Georgia from $779 million to $859 million. Based on available data, employment at Japanese-affiliated companies in Georgia is about 25,000.

The Southeastern state where Japanese firms own the most real estate is Florida, which is the most populous state in our district and the state with the largest economic output. Japanese firms in 2005 owned $1.2 billion of commercial property in Florida. Also, about 19,000 Floridians are employed by Japanese companies.

Elsewhere in the Southeast—notably Alabama, Tennessee, and Mississippi—Japanese firms have led the development of highly efficient vehicle manufacturing and assembly facilities. Between 1995 and 2005—the most recent year for which data are available—Japanese firms in these three states increased hiring from about 38,000 to more than 54,000 jobs.

Vehicle assembly in this region has grown at a time when employment in the industry nationally has declined. But with weak economic and consumer spending growth in the United States during the past year, auto plants have cut back vehicle production. The reduced flow of auto imports from Japan and elsewhere has been reflected in lower import traffic at major ports in this region.

Of course, investment and trade go in both directions. Japan in 2007 accounted for 7 percent of all U.S. imports and 6 percent of U.S exports. From the reverse perspective, about 23 percent of Japan's exports went to the United States. Clearly, this country continues to be an important market for Japan.

Georgia's goods exports to Japan in 2007 amounted to $1.2 billion, including the shipment of transportation equipment, machinery, and chemicals.

With any economy, the financial sector is important. Japanese banks started building a presence in the Southeast when I lived in Atlanta back in the 1980s. By 1991, there were 11 Japanese banks with offices in Georgia and Florida with assets totaling $3.9 billion. By 1999, most of the Japanese banks had closed their Southeast offices. Today, I'm aware of only two Japanese bank offices that operate in Georgia.

Why the retreat? Much of this had to do with retrenchment in the Japanese banking industry as Japan dealt domestically with a decade of recession and slow growth. Japanese banks in the 1980s became overextended by making loans to businesses whose collateral later collapsed in value. Many borrowers struggled to make payments, and Japanese lenders had to take enormous losses on bad loans. This financial instability spilled over to the broader Japanese economy and led to an extended period of slow growth. Between 1989 and 2001 the wealth of the private sector in Japan declined by more than $10 trillion—two to three times the value of the economy's annual economic output. This period—sometimes called "the lost decade"—was characterized by very low interest rates calibrated to resist deflation and stimulate economic growth.

Expectations for a different experience

Some have argued that the United States is today in a similar position to that of Japan in 1989 and will suffer a similar prolonged period of economic weakness. I understand why this connection is being made as both episodes were preceded by rapid appreciation in asset prices—often called bubbles—followed by rapid depreciation, as we are experiencing today with house prices.

I do not expect this country to experience the same protracted economic weakness as Japan, in part because we can learn from Japan's experience in order to avoid something similar. Taking lessons from the Japanese experience, we here in the United States must come to grips with broad systemic inadequacies and make necessary changes. Affected financial companies are already well into the process of loss recognition and recapitalization. In the coming months and years we can expect substantial improvements in the area of risk management and liquidity management even to the extent of fundamental changes of their business models. Also, the debate on reform of the regulatory framework has already begun. Years of economic performance are at stake, and I'm confident we will muster the will to make the necessary changes.

Historical precedent supports my view. In the late 1980s, the United States went through the savings and loan crisis. Recognition of the scope of the problem took some time, but ultimately U.S. policymakers were able to respond aggressively with a comprehensive resolution of the problems of impaired assets, insolvent institutions, and weak management.

There is one similarity between the situation in Japan in the '90s and the reality today in the U.S. financial system that gives pause. One explanation for the slow response in Japan was the relatively more opaque nature of its banking system, reflecting the complex relationship culture of Japanese business. Much has been written recently about the so-called "shadow banking system" of hedge funds and complex securities in the United States that also renders much of our financial system opaque. Improved transparency must accompany other reforms as an early priority.

Cultural differences but mutual respect

Need I remind this group that our two countries differ profoundly culturally? A book that has influenced my thinking on our cultural differences is *The Seven Cultures of Capitalism* by Charles Hampden-Turner and Alfons Trompenaars. In surveys of businesspeople in a dozen or more countries asking them how they would resolve value dilemmas, American and Japanese businesspeople were often at opposite ends of the spectrum. Yet, during the last 60 years a symbiotic partnership has developed and matured, yielding great benefits to both countries. I would argue that the relationship between Japan and the United States stands as perhaps the world's most prominent example of pragmatic cooperation between peoples who, if not opposites culturally, are at least very, very different.

It hasn't always been so, but I believe the relationship works so well because of a high quotient of mutual respect. Let me share some personal remembrances in that vein.

From 1988 to 2001, I worked closely with a number of Japanese bankers from then Fuji Bank, now Mizuho. There was much I admired in my Japanese colleagues, and I learned a lot from them that I've taken to heart.

There are two allied notions in Japanese business culture—*seijitsu* (sincerity) and *wa* (harmony). In a few words, sincerity is the proper discharge of one's duties and obligations no matter what. It's about dedication to the interests of the company or team and the subordination of one's personal interests to the interests of the institution that employs you.

Wa, as I said, means harmony. It is the ideal that informs the teamwork culture in Japanese organizations. Two of my colleagues rose to become eventual presidents of Fuji Bank, and a number rose to become managing directors—the senior most position below president. I observed that the personality types that lead Japanese organizations are quite different than those we often reward with high positions in American business culture. Japanese leaders are skillful facilitators of organizational harmony and teamwork.

At a higher, less personal, level, I believe Japanese concepts have been internalized here in American business culture and have served to make the United States more competitive. *Kaizen*, continuous improvement, is widely practiced as a requirement of competitive survival. *Kanban*, just-in-time supply, with the commitment to absolute reliability it implies, is now an essential element of the sophisticated supply chains of American and global manufacturers and retailers.

There is irony in this assertion that Japanese ideas have become Americanized because the intellectual origins of *kaizen* and *kanban* techniques, and the encompassing concept of total quality management, are widely attributed to two Americans: Edwards Deming and Joseph Juran. Both were prophets ignored in their home countries, to paraphrase the old saying, so they took their ideas of statistical quality control in manufacturing processes to Japan after the Second World War. Their message, in a nutshell, was "do it right the first time." Six Sigma is a descendant of Deming and Juran.

I know from personal experience that Japanese executives working here have learned from their American colleagues. In my observation, my Japanese colleagues learned much about risk taking, risk management, and risk-reward calculation. They learned about rapid decision-making, competitive differentiation, and invention of contrarian business models. Speaking of his experience in an aggressive, risk-taking American financial company, one of my Japanese friends said, "You are hunters, and we are farmers."

There is one other Japanese concept I admire because it demonstrates the Japanese sense of humor. It is *chindogu*. I am a prospective member of the International Chindogu Society. For the Americans here tonight, *chindogu* is the Japanese word for the art of the "unuseless" invention. Unuseless here means almost completely useless, but with just a hint of serious purpose. Examples of *chindogu* inventions are eyelid clips to stay awake in boring meetings. Or bedroom slippers encased in dust mops to clean your floor while you shuffle around the house. I submitted the idea of advertising bibs for cows grazing beside highways, but this idea has actually been put into practice in Holland. A rule of the International Chindogu Society is, if you invent something that turns out to be so handy you actually use it, you have failed to make a *chindogu*. You should go to the patent office.

Loyalty and livelihood

I have a serious thought—related to *chindogu*—as I close. In an earlier speech some months ago, I argued that in this world of global commerce, global brands, international trade and cross-border investment, and complex international supply chains, our notion of product loyalty should be updated. I argued that in many product categories,

national identity is increasingly unuseless. I argued that there is a difference between national brand identity and the geographic origin of a product, and that, if at all, we as consumers owe loyalty to the products of companies that provide a livelihood to our people.

Foreign companies—including many represented here tonight—employ more than 170,000 people in Georgia. Your companies and your products are bedrock contributors to the national and southeastern economy.

Thank you.

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