

# JAPAN ECONOMIC CURRENTS

A COMMENTARY ON ECONOMIC AND BUSINESS TRENDS

## Japan and the US: The Global Challenges Ahead

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Every period in history is defined by its principal challenges. The twentieth century was largely defined by great power competition. This resulted in three great international conflicts: the two world wars and then the Cold War. There was a competition among the major powers of the day, motivated by traditional interests or ideologies of states.

The twenty-first century promises to be something very different. There is a saying in the United States that it is always dangerous to make predictions, especially about the future, but let me do just that. The twenty-first century will not be a repetition of the twentieth century.

The principal dynamic of the twenty-first century as it is unfolding is not great-power competition. The principal challenges of the twenty-first century are not going to be a rising China, Brazil, or India or issues between the United States and Russia, Europe, or Japan; instead, the principal challenges

of the twenty-first century are going to be global challenges. This will be the cardinal characteristic of this era of history. The challenges will include the spread of nuclear and other weapons of mass destruction; the possibility of pandemic disease; threats to world economic openness and threats to the free flow of goods and services and currencies; the warming of the planet, or climate change; terrorism carried out mostly by nonstate actors; and shortages of energy. And what will ultimately determine the success of this century and the character of this era of history is how good the major powers are at managing and dealing with this vast array of global challenges. Essentially, history will give us a report card on our success in dealing with an extraordinary array of challenges.

What will make this somewhat more difficult, at least initially, is that we begin with a certain disadvantage, which is that we do not have in place the institutional machinery, the regional and global arrangements, that are needed to contend with these challenges. To the contrary, a lot of the international machinery we now have dates back fifty to sixty years, to the

aftermath of the Second World War, and to what people at the time thought was going to be necessary to help manage the post-World War II era. The result is that we now have something of a gap between the scale and the nature of the challenges and the composition and the capacities of existing institutions.

The task for people involved in foreign policy and diplomacy is to close this gap between regional and global challenges and regional and global arrangements. There are many examples of this mismatch. The most obvious is the United Nations Security Council. The composition of the Security Council is what people in the 1940s imagined would be something of a steering group for the world after World War II. It explains the heavy emphasis or overrepresentation of Europe and an underrepresentation of

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Asia. The fact that Japan and India are not on the Security Council is quite telling. The absence of any country from Latin America or Africa is again quite telling. Instead there is the United States, Britain, France, China, and Russia. This was before anyone even imagined the rise of the European Union. So obviously, adapting this institution is one part of the challenge.

The second example is the General Assembly. When people imagined the United Nations General Assembly, I doubt many people imagined it with a composition of more than 190 countries. Any time I find myself in a meeting with 190 people, I don't expect a lot to be accomplished, and it should therefore be no surprise that the United Nations General Assembly can accomplish very little.

We could also look at other challenges where few if any relevant institutions exist. Global climate change is a relatively new phenomenon in the sense of our awareness of it. It is not new in the scientific sense, but it is new in the diplomatic sense. We do not have in place arrangements for coping with it. As for the meeting held in Kyoto, if you are an optimist you would call it a limited success, and if you are a pessimist you would call it a partial failure. I would simply say that, again, we do not have in place

either the rules or the arrangements to monitor, mitigate, or adapt to global climate change and large-scale emissions of greenhouse gases.

In the realm of nuclear proliferation, we have the International Atomic Energy Agency. The problem is that the International Atomic Energy Agency works on a basis of cooperation and consent. Countries are obligated to be honest and to cooperate. They should declare and make available for inspection any relevant facilities. But as we have learned in the case of North Korea, or as the world recently learned in the case of Iran, we do not have a means for dealing with countries that are not openly declaring or making available for inspection their relevant facilities. So in this case we have a mismatch between the institution's capacity and the challenge.

In the area of trade, we have in place the World Trade Organization. The problem is, we do not have a consensus on further steps to build an open trading system. This is the reason we cannot move from where we are to completing the so-called Doha Round of trade negotiations. We do not have a consensus on what ought to be included in world trade talks.

I am simply making the point that the challenge for people in my business and

for many of you is to figure out how to develop new arrangements, or how to adapt existing arrangements to meet the existing and emerging problems that are so central to this era of history.

There are several options for doing so. Let me suggest that the least likely solution to this challenge is what I would call the model of the United Nations General Assembly, in which there is universal and equal membership. I do not believe this will be a model for dealing with most international challenges. Instead, we are going to have to think much more about selective memberships that will include the countries most able and willing to deal with a particular problem. I think that is one likely rule of thumb.

Secondly, we may not be in a situation where we have institutions that deal with all aspects of a problem. So-called comprehensive approaches, while desirable, may simply be too ambitious and we may have to think of arrangements that deal with only parts of a problem. Let me suggest, for example, on climate change, that although all the governments of the world are going to meet in Copenhagen and are going to try to agree on all aspects of dealing with global climate change, the chances of that happening are zero. It is simply not going to happen. So the question is, how can

one try to separate out certain aspects of the problem where it may be possible to build useful global responses so we can agree on something even if we cannot agree on everything?

Maybe one of the things we could agree on is to create a large fund of money to try to discourage the process of destroying forests or to try to encourage the process of recreating forests, since we now know that deforestation, the destruction and burning of forests, is responsible for as much as one-fifth, or 20 percent, of the global climate change problem. So again, even if we cannot agree on everything, maybe we could agree on that one thing, or maybe we could agree on something to do with clean-coal technology. If everybody cannot agree on it, maybe five or ten or fifteen countries can agree, and if it happens to be the five or ten or fifteen countries that are responsible for 80 or 90 percent of the emissions that cause the problem, that may be good enough. Sometimes in international relations, all you can hope for and realistically strive for is what is "good enough" as a first or even second step. Over time you can maybe strive for something that comes closer to perfection. But in my business, "good enough" makes for a pretty good day.

In some cases, we are already innovating new institutions to take

advantage of things. We saw this in Pittsburgh recently with the G20. After World War II, people created the United Nations Security Council with the idea that the five permanent members were going to help direct the world. By the 1970s, with the full emergence of Japan, it became obvious that the Security Council was an inadequate basis for global leadership, and thus was born the era of trilateralism, and, among other things, the G7. The idea was to give a country such as Japan a much larger say and also to bring in the European Union, or at that point the European Community.

The world has changed and the leadership of the world is adapting to that change. The rise of the G20 is a recognition that we now need to find a place at the table for other countries, including India, Brazil, South Korea, and others. As world economic power has changed, institutions need to keep up with that change. It will be very interesting to see whether, over time, the G20 takes on a political role as well as an economic role, in some ways analogous to how the G8 complemented the G7. It is quite possible we can move toward a G20 with a political role in addition to its economic role.

But we also see one other thing out of the G20 that is instructive: that in many areas we will not be able to

reach agreement, but instead we will have what I have started to describe as "informal multilateralism." By that I mean that countries, even if they cannot sign on to treaties or conventions, can commit themselves to a set of national policies and to a degree of transparency so their national efforts can be observed and measured by others. We may see this in the area of climate change. We may see this in the area of energy. We may see this in the area of, say, financial regulation. We will not be able to agree to a formal set of rules or some new institution to regulate global finance, but the major countries involved in global finance may agree to a common set of standards, whether to deal with accounting or capital requirements for financial institutions or what have you, and this might be the basis of a multilateral collaboration. Again, it is not formal. It does not include everyone. It does not resolve everything. But it might be a very practical approach to multilateralism in an era when that is the only way forward. So if I am right, we are entering a period of what you might call flexible multilateralism in order to deal with the signature challenges of this era.

What does this mean for the United States and Japan? What it suggests to me is that the alliance between the United States and Japan, while

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necessary, is no longer sufficient. Alliances tend to be formal relationships in which countries agree on what they are against and what they are going to do in certain contingencies. But the United States and Japan are going to have to forge cooperation and are going to have to work together in a large number of situations, some of which are imaginable, some of which are not; sometimes they are going to have to figure out what it is they are in favor of, in some other cases what it is they are going to try to oppose. Many of these situations will not be clear-cut. What is it the two countries are prepared to do, for example, to discourage young men and women from making the decision to become terrorists in the first place? This is not the narrow stuff of traditional alliances but obviously it is very important. What are the two countries going to do to prepare for an H1N1 pandemic? Again, this is not the normal stuff of alliances but it is very important.

What this suggests to me is that increasingly central to the US-Japan relationship will be consultation in the most creative sense of the word, where the countries will try to look at the full range of challenges and will begin to figure out what the two can do in their own respective national policies or what the two can bring together mutually to various international meetings so we

can advocate together. This is going to require on both of our parts a rethinking of the relationship, a willingness to expand what it is we talk about. It is also going to take some discipline. Quite honestly, we should not be spending the bulk of our time thinking about how many US soldiers are going to be located where on Okinawa; that should not be the centerpiece of conversations between the United States and Japan. But rather, we should be thinking about much bigger regional and global and much more important issues that affect us both.

We also need to make sure that domestically we are doing all that we can—this applies to the United States and Japan—so we have the potential to be effective partners. For the United States, this means getting our economic house in order. We have got to do something about the scale of our deficits, which are far too large. But for Japan I would suggest it also means building up relevant capabilities for involvement around the world, and also essentially stretching your politics so this government and future governments have the domestic political freedom for Japan to play a larger role. If challenges are going to be met around the world, it is important that Japan be able to participate, and ability is a function both of capacity

and of domestic political support. So this means Japan needs to build up capacities; but it also needs to condition its political system for Japan to play a larger role if the United States and Japan are going to be able to be partners in dealing with this range of global challenges, which is what is going to define the twenty-first century.

You have a new government that is several weeks old now. We have a new administration that is eight or nine months old. We're about to have some of the first formal, in-depth, high-level meetings between our respective leaderships. This is the first of many opportunities for the United States and Japan to begin to redirect and, in some ways, recreate their relationship to make it as relevant to the first half of the twenty-first century as it was to the last half of the twentieth century. That is a task that is in our collective self-interest to meet.

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# The U.S.-Japan Partnership in a New Era: Under Fire or Looking Forward?

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Most of us did not anticipate the level of excitement that we saw in Tokyo on August 30, 2009, or in the days and weeks in the aftermath of the election in Japan. I think none of us, even people like myself who have been looking at Japanese politics and foreign policy for some time, really understands the full implications of the broad transformation that Japan is undertaking. So I think we are all trying to connect the dots. When I sit in Washington, I get asked many questions, not only about the Democratic Party of Japan (DPJ), but also about the priorities of the Japanese people and public, in particular, Japan's foreign policy priorities.

Clearly, this is a new political party. This is the first time that the Japanese voters have had a realistic alternative to the Liberal Democratic Party (LDP). We have all been watching this process unfold now for some years. It didn't just change overnight on August 30. This is a process Japan has been engaged in for more than a decade. But it does suggest to us a new set of politics in Japan.

The DPJ has clearly identified the need for politicians to be more accountable to the public, to take more responsibility over the policymaking in Japan, both in domestic politics and

also in foreign policy. This is not new to the DPJ. Prime Minister Koizumi made much the same argument almost ten years ago. Clearly, the Japanese public is asking more of its politicians and its political leadership, and I think that is an exciting opportunity for policy and policy reevaluation.

There is a sense that the DPJ is undertaking some very significant policy reviews. I often get asked a lot of questions on the foreign policy dimension of these policy reviews: How are they happening? Who is responsible? Who are the personalities, the policy teams that are at work today? So I think you will hear a lot of questions from people outside Japan about how this review of past policy, particularly foreign policy, is being undertaken.

There is another institutional dimension, which is just starting and which we will be paying attention to in the years ahead. This is the effort starting with the National Strategy Council, the effort to reorganize the way in which policy is made. I think it is much too early for us to think that we know what is going to happen here, but it is something that we will be watching, the reorganization of the institutional capacity of the Japanese government to make broad policy changes.

I am not a policymaker and I am relatively new to Washington, DC, but I was fortunate to arrive at the Council on Foreign Relations in Washington, DC in January 2008. I got a very up-close view of our own process of transition. Now I'm trying to watch Japan's, and I think there are two things that strike me about the parallels.

For those of us in the U.S.-Japan policy world, there was a certain amount of nervousness last fall about what the DPJ would bring to the U.S.-Japan alliance relationship. That looks very familiar today as we sit and watch this transition here in Tokyo.

I sense in Tokyo that this broader structural change is very much at the heart of what the DPJ is trying to accomplish. You have a transition of power but also a redesign of your governance system, and therefore it makes it very hard to understand where policy priorities lie and how you are going to be able to affect the new conversation with the United States.

I would say there is a little bit of nervousness, but there is also an excitement, too, for those of us outside of Japan. I was very impressed when Prime Minister Hatoyama and Foreign Minister Okada came to New York. The first public speech the new leader

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made was in an international forum, in the United Nations. Despite the fact that there is a lot of concern about this party never having been in power, they addressed some very key issues in a very impressive way. They made a mark not only in the United Nations, but also in Pittsburgh. I think the new government made its first international journey very successfully.

The identification of climate change and nonproliferation and disarmament as the two policy priorities of the new government was very clearly articulated and the ideas were clearly well thought out in advance. We watched as Prime Minister Hatoyama met with Hu Jintao and with our president. The relationships that Japan has with China and the United States are the two critical relationships that the new government will face for some time now.

The other aspect of the new government's foreign policy was the visit to Seoul and Beijing. The ASEAN plus Three summit is also something that many of us in Washington, DC think is very constructive for Japan and we look forward to watching that develop as well.

Many of us want to see a dynamic U.S.-Japan relationship and I think this is a moment of opportunity for

the relationship. It is a time where we recognize that our relationship cannot be seen as static and it cannot be seen as being in isolation from regional and world events. Both of our publics want to see the problem-solving capacity of this relationship. It is important that we demonstrate that the United States and Japan can be effective problem-solving partners.

The G20 Copenhagen initiatives are new initiatives to be sustained for some time, but they are initiatives in which both the United States and Japan have deep stakes.

The issue with North Korea, the question of whether North Korea will come back to negotiations over denuclearization is very important for both of our countries. Assistant Secretary of State Kurt Campbell was in Beijing and outlined his hopes that Pyongyang will come back to the six-party conversation, but I am not overly optimistic nor do I think our government is optimistic that Pyongyang is ready to do that. I think Wen Jiabao's visit to Pyongyang and the subsequent missile tests by the North Koreans are reason for us to be quite skeptical about North Korea's engagement in multilateralism and a serious conversation over denuclearization. Nonetheless, it is an important

endeavor that the United States and Japan must support together.

On Afghanistan and Pakistan, I think Foreign Minister Okada's visit to the region was a very positive first step. His meetings with the leaders of both of these countries will give him a very clear understanding of the challenges, and I hope that that is a conversation that he will continue to have with our Secretary of State Hillary Clinton and that Prime Minister Hatoyama and President Obama will have next month.

If I may be a little blunt on one issue of the alliance, I think what we can't understand yet in Washington is the new government's strategic assessment of Japan's own defense needs and its security priorities. That is an important understanding for us to have. We have a number of procedural issues, issues related to basing, to the Status of Forces Agreement, and to other kinds of issues to which we must pay attention. But I think there is a certain absence of understanding of how the new government sees Japan's own strategic needs and the place of the alliance in that strategic concept.

So my suggestion simply is for the new government to help Washington understand that strategic vision as it

proceeds to talk about some of these aspects of the stationing of U.S. forces in Japan.

Let me conclude with some suggestions and perhaps identify some opportunities ahead.

Dr. Haass was very right that the United States and Japan have to set our sights quite high. I don't think we should set our sights low. This is a partnership that has tremendous capacity and the challenges are severe and will demand every part of that capacity, be it the government, private sector, NGO, academic, or intellectual world as well. We should set our sights high and not be limited by some of the issues and problems that are affecting our working day-to-day relationship.

There is a lot of expectation in anticipation of our president's visit to Japan next month. I think that is the moment to set our sights high. We should also remember that the president will be back next year, in 2010. So not everything has to be accomplished by November 12, but we have to think about where we would like to go and what that agenda might look like.

The second suggestion I would make is that the new government has put forward in its foreign policy manifesto two very important goals. The first

is to create a more equal U.S.-Japan partnership. I know most of us want that to be the way in which Japan proceeds to have its relationship with Washington, but we don't understand yet what that equality really means for the new government, so we are trying to understand a little bit better how that definition is going to be applied.

The other goal is for Japan to join and to strengthen its efforts in East Asian community building. This is something that Japan has been deeply engaged in now for some time. People ask me: Is Japan moving more toward Asia and less toward the United States? There is a little bit of a tinge of that kind of questioning about these two priorities of the Hatoyama government. I think on the side of Washington and most of the thinkers about Asia, neither of these goals is mutually exclusive. In fact, Japan's engagement with its neighbors is fundamentally important for a successful U.S.-Japan partnership, and there is a welcoming of this new focus in Japan's foreign policy. But I think the regional aspirations of the new government and the place of the U.S. partnership in those aspirations is something that our two leaders could clarify next month.

Finally, we need alliance-management practices that match Japan's new politics. We need to develop them

and talk about them. Japan has had a single-party-dominant system for fifty or so years. U.S.-alliance management has responded to the political realities of Tokyo. Now that Japan is moving in a different direction, our alliance-management policies will have to change. I don't foresee that as a great obstacle. It is a learning process. We have other allies that alternate parties in power quite regularly so I don't think it is a huge task. But I do think that in this relationship, we are going to have to do some learning about how to proceed. We need sustainable policy coordination, and the U.S.-Japan relationship has to be owned by both major political parties. It cannot be perceived as belonging to one.

Many of our policymakers in Washington today are hoping to work with the new government in Tokyo to understand how to better design our alliance management, to reflect the new realities, and to learn more about how the alliance can be the possession of not only one political party but of the Japanese people as a whole.

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## Comments

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The idealism of the United States, the goodwill of the United States, and the sense of optimism that things can only get better, really came across in the presentations by Dr. Haass and Dr. Smith.

Dr. Haass spoke about the United States and Japan from a global perspective. He noted that the twenty-first century is no longer a competition among powers; it is a matter of how we confront global challenges. It is a new era. Dr. Haass also spoke about climate change, the fight against terrorism, the shortage of energy, and various global issues. He pointed out the mismatch between the vast agenda of global issues and the capabilities and institutions to confront these issues.

I very much agree with Dr. Haass's remarks. If the global community is to confront these global challenges, we need further cooperation and new types of institution. This is a fairly given conclusion. At the same time, we need a greater sense of speed. In this era of globalization, all of us need to share an even greater sense of speed. That was my impression after hearing Dr. Haass's comments.

Japan is an island nation and we Japanese use the Japanese language. We live in this very unique culture of Japan, so our exchange with the outer

world has been contained within a certain extent. But the world outside has undergone a massive change very rapidly. As an island nation, Japan is a few years late in feeling these changes. That has been my experience in the last few decades. For example, why did the Gulf War have such global, significant implications? And why was involvement and engagement in the Gulf War so important? Why was it that Japan was so severely criticized? I think it was only a few years afterwards that Japan came to recognize these questions.

The Cold War ended as a result of the fall of the Berlin wall in 1989 and the breakdown of the Soviet Union in 1991, but as far as we Japanese are concerned, I think it took us a few years to fully understand the implications of these events.

The so-called IT revolution began around 1994. We didn't understand that it was not just a matter of technological convenience. The IT revolution really changed how people connected with one another. It was a totally revolutionary event. Again, it took us a few years here in Japan to really fully understand the meaning of the IT revolution. As for the fight against terrorism, it took a few years for the Japanese to understand to what

extent the global community fully placed an emphasis on these issues.

After 2000, when we take a look at the trends of the national defense budgets of Europe, the United States, Russia, and China, all of these nations increased their budgets by at least 30 percent, or more than 100 percent vis-à-vis 2000, without exception. Japan was an exception. Japan was actually reducing its national defense budget after 2000. In a sense, the global community might be heading towards a more risky trend. But that awareness did not reach the shores of Japan until a few years afterwards.

We are now witnessing the rise of globalism. Since the global financial crisis hit us, we now understand that we cannot confront global issues alone, nor can the United States. We cannot resolve the financial crisis without China. I think there is now a greater spread of awareness of globalism in our community today.

Environmental issues need to be approached urgently. At the upcoming COP15 in Copenhagen, the climate change issue is going to be discussed and this requires a very rapid response. Is it going to take the Japanese greater time to really fully understand the significance of these issues? There

should not be a time lag in confronting these issues.

Japan ran for a permanent seat in the United Nations Security Council. Up until now, the conventional feeling in Japan was that Japan should be the first country to join the five permanent members of the Security Council. Some even felt that a line can be drawn between Japan and the other candidate nations like Germany, Brazil, and India. However, the situation has changed. In terms of international presence, we would not be surprised if India or Brazil joined the Security Council before Japan. Japan has been losing its international presence. Japan is clean, safe, and one of the most convenient countries in the world. Therefore the Japanese don't even feel uneasy about losing importance in the international community. I am very concerned about this lack of awareness of the Japanese. Amid rapid globalization the Japanese should be more engaged in the international community than ever before.

I would now like to share my comments about the US-Japan relationship. Prime Minister Hatoyama has given a good performance at the United Nations and in Pittsburgh and left a very positive impression. If that is the case, then I think Prime Minister Hatoyama really needs to act on his

words. Prime Minister Hatoyama promised a 25 percent reduction in carbon dioxide emissions compared to 1990 levels by 2020. But when we fully give thought to this, this is a 30 percent reduction compared to 2005 levels, yet 2020 is only ten years ahead. How can we really cut back 30 percent? Japanese industries are all casting questions. No matter how much effort they make, objectively speaking, many analysts say that the maximum reduction possible is only 10 to 12 percent. That means that there has to be carbon trading and we have to give money so that we would be allowed to continue to emit CO<sub>2</sub>. If that is the case, then what good was this commitment? What purpose did this commitment serve? Or does it mean that Japanese industry will have to cut back on its production? If that is the case, then that would lead to a weakening of Japan's competitiveness. There have always been calls for Japan to strengthen its political presence, but Japan's political presence is based on its economic strength. We learned this very painful lesson in the 1990s, which are referred to as the lost decade in Japan. I hope that the Hatoyama government will draw up a growth strategy to enhance Japanese economic capability—inclusive of the commitment in relation to CO<sub>2</sub>

reduction—and we need to implement that strategy.

Dr. Smith stated that as far as the US-Japan alliance is concerned, we don't need to clear all the issues before President Obama's visit to Japan. What is required is to identify a clear direction. I believe that is very positive advice. We really need to come up with a practical strategy.

Dr. Smith was very moderate in her choice of words regarding the US-Japan relationship. "An equal partnership is good, but what is the meaning behind an equal partnership?" I think this is a very essential and fundamental question. When DPJ leaders talk about a partnership on equal footing between Japan and the United States, they are talking about too much dependence on the United States. The members of the government have used terms like maintaining an appropriate distance with the United States or that Japan has been overly dependent on the United States. That seems to be the DPJ's interpretation.

The United States protects the world. They provide security to Japan and would like to see even greater involvement from the Japanese. That would make a more equal partnership between the United States and Japan, and the United States would welcome

such an equal relationship. So there is a gap between the United States' and Japan's interpretation of an equal partnership. This gap needs to be overcome.

The common thread emerging from the two panelists is that there is going to be a need for even greater cooperation and discussion between the United States and Japan. The engagement and relationship needs to be sustainable. I am very much encouraged by this message.

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