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THE POLITICS OF POSTAL SAVINGS REFORM IN JAPAN

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The article provides an overview of the politics of postal savings reform in Japan. Although reform of the system has been a subject of debate over the last twenty years, the ascension of Koizumi Jun'ichiro to the prime minister's post in 2001 raised the issue to the forefront of Japanese politics. However, in the course of the past two decades the terms of debate have radically shifted. The key consideration that we analyze is how the nature of political conflict over privatizing the postal savings system has changed over time. Forces opposing reform are at their weakest level in the postwar period while forces in favor of reform are clearly stronger. Yet, particular economic impediments to full-blown privatization are greater than ever. The path to reforming the system is mined with political and financial hazards.

Key words: postal savings, privatization, LDP (Liberal Democratic Party), banking, Japan, economy

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Introduction

The privatization of postal services has been the focus of a major political battle playing out in Japan since Koizumi Jun'ichiro took over as prime minister in 2001. Postal services in Japan are comprised primarily of mail delivery, postal savings, and postal insurance. While the privatization of each of these three components has been contentious, the privatization of postal savings (*yūbin chokin*, or *yūcho*) is of particular interest to outside observers. Foremost among the reasons for this is perhaps that Japan's postal savings system represents the largest financial institution in the world in terms of asset size. Its deposits total 230 trillion yen, almost half of the total amount held in Japan's savings accounts. Privatization of this system would have a significant impact on the flow of funds within Japan. By subjecting the system to market forces and removing blanket deposit guarantees, we expect privatization to affect the calculations and behavior both of depositors and of those entrusted with investing these deposits, leading to the significant reallocation of funds. Most postal deposits are currently invested automatically in central and local government bonds, and in bonds issued by government-owned corporations. Many private financial institutions—domestic and foreign alike—are eager to lure some of those funds into other financial instruments, primarily in the private sector.

In this article, we provide an overview of the politics of postal savings reform in Japan. While reform of the system has only become part of the daily headlines since Koizumi became prime minister, the issue of postal savings has been an important one for Japan's financial sector for at least the last two decades. Important changes have been taking place in Japan across numerous dimensions for some time, affecting the performance and relevance of the system, as well as weakening the political forces opposed to change in this system.

The article proceeds as follows. The first section provides background on why significant reforms in the postal savings system took so long to emerge in Japan. In numerous other advanced industrial countries, significant reforms of postal savings/banking systems commenced in the 1980s. We delve into the reason behind the relative inertia in Japan. The second section highlights changes in many of the conditions that promoted

the status quo, and how system reform eventually emerged as a salient political issue. The third section examines the motivations behind Koizumi's push to *privatize* the postal savings system, and why this particularly extreme route of reform was pursued over alternative measures. The fourth section explores the government strategy to achieve the objectives of privatization and highlights remaining obstacles.

A key theme that emerges from our analysis is that the nature of political conflict surrounding postal savings reform and the constellation of interests around this issue today differ significantly from the past. While forces opposing reform are weaker today than ever before in the postwar period and forces in favor of reform are clearly stronger, the concrete economic impediments to full-blown privatization have never been higher.

Background

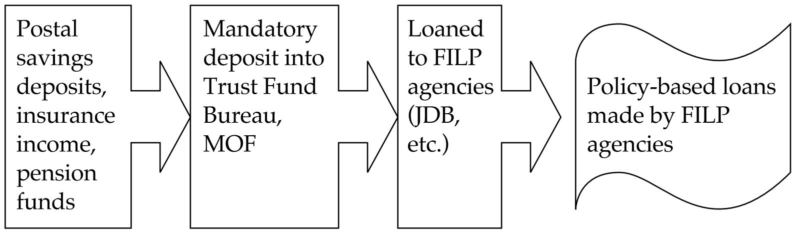
In many countries, an intermediate or precursor step to establishing a private banking sector is a state-owned banking sector. Postal savings/banking systems are technically the equivalent of a state-owned bank, but compared with other types of state-owned banks, they tend to have further-reaching political entanglements. There are at least five reasons why. First, postal networks are ubiquitous, reaching into the most remote, most rural areas. They are highly susceptible, therefore, to entrenchment in local politics. Second, the mail delivery business is often cross-subsidized by postal savings/banking, with personnel and locational synergies. Accordingly, the maintenance of universal mail delivery tends to become linked to the continued existence of postal financial services.[1] Third, postal savings systems and affiliated agencies funded by postal savings often receive government subsidies in the form of guarantees and tax breaks. This leads to lower costs of doing business, with savings often passed on to the saver in the form of higher interest rates, making postal savings accounts more attractive than accounts elsewhere. Fourth, personal relationships

1. A forceful argument for this linkage is made by Mark Scher and Naoyuki Yoshino, eds., *Small Savings Mobilization and Asian Economic Development* (Armonk, N.Y.: M.E. Sharpe, 2004). See, especially, chapter 2.

—particularly in rural areas—tend to develop among postmasters, workers, and customers. Fifth, postal workers tend to be unionized, and therefore will be crucial actors in any reform movement. Typically, they rally in opposition to reforms likely to weaken job security.

In Japan, these general tendencies were heightened by the structure of public finance, party and electoral politics, and the nature of bureaucratic incentives. The postal savings system (as well as the postal insurance system) served for decades to gather funds from individual depositors all around the country. These funds were then funneled through the government's Fiscal Investment and Loan Program (FILP), a type of "second budget," to government corporations established for public purposes. (*Figure 1* illustrates the general flow of capital through the FILP system prior to 2001.) For example, postal savings funds provided capital for the state-backed Japan Development Bank (JDB, now known as the Development Bank of Japan or DBJ). The JDB, in turn, invested in projects to strengthen the nation's physical infrastructure. The JDB also invested in industries designated by government industrial policies as priority industries.[2]

Figure 1. Basic Scheme of FILP Funding Prior to the 2001 Reforms



2. For more on the concept and practice of industrial policy in Japan, see Chalmers Johnson, *MITI and the Japanese Miracle: The Growth of Industrial Policy, 1925-1975* (Tokyo: Charles E. Tuttle, 1982); Daniel Okimoto, *Between MITI and the Market: Japanese Industrial Policy for High Technology* (Stanford, Calif.: Stanford University Press, 1989); and Scott Callon, *Divided Sun: MITI and the Breakdown of Japanese High-Tech Industrial Policy, 1975-1993* (Stanford, Calif.: Stanford University Press, 1995).

Political Uses of Funds Deposited in Postal Savings Accounts

Postal savings deposits played an important role in financing Japan's postwar economic development and rapid growth. At the same time, however, these funds also became a source of pork barrel goods under the near-exclusive domain of the Liberal Democratic Party (LDP) and were therefore linked to electoral politics.

For Japanese politicians, FILP, which was primarily funded by postal savings, was a main formal institution for distributing material benefits to their supporters. Though FILP is formally a supplement to the General Account budget, it is distinguished from other types of budgetary supplements by some unique features. First, compared to what observers know about General Account budgeting, far less is known about how FILP funds are allocated. FILP budgets are neither subject to legislative approval nor up for debate. Rather, they are worked out through an intensive consultation process between Ministry of Finance (MOF) officials and LDP politicians. The political use of FILP is evident when one compares spending patterns of FILP to those in the General Account budget (which is more transparent and openly debated). While increases in the General Account were largely guided over the high growth period by a principle of incrementalism,[3] the FILP budget tended to increase after elections in which the LDP suffered a loss of electoral support.[4]

3. See John C. Campbell, *Contemporary Japanese Budget Politics* (Berkeley, Calif.: University of California Press, 1977). Some later works find greater fluctuation in spending patterns in the General Budget and relate these to politics but few disagree that the decision-making process surrounding FILP spending permitted relatively greater political discretion over the use of these funds.
4. Patterson finds evidence that FILP lending to SMEs follows a pattern of increases after LDP electoral losses during the period between 1960-1981 (Dennis Patterson, "Electoral Influence and Economic Policy: the Origins of Financial Aid to Small Business in Japan," *Comparative Political Studies*, vol. 273 (1994), pp. 425-47). Toyoda finds that the picture is greatly complicated by financial liberalization, though the results for the high growth period prior to 1973 supports the argument that FILP allocations for constituent groups increase after loss of support for the LDP (measured through periodic polls by Jijitsu-shinsha). A. Maria Toyoda, "Why Thinking Globally Makes It Difficult to Act Locally

Second, although FILP spending, like that in the General Account, can be channeled through central disbursements to local governments, most FILP resources are disbursed through specially created channels, including Special Accounts and "FILP agencies." The latter are government-affiliated agencies and public corporations (*tokushu hōjin*), including government financial institutions.[5] These FILP agencies are highly compartmentalized and specialized niche lenders, with separate corporations targeting small business, large industry, agriculture, housing and road construction, and waste disposal industries. By funneling postal savings funds to FILP agencies that in turn directed money to local areas, the LDP tried to bolster its electoral support. Calder[6] and Patterson,[7] for instance, note a pattern of compensation in the form of financial assistance to key voting groups whenever a political or economic crisis arose that affected them. Frequently, that compensation came in the form of easily accessed credit through government financial institutions funded by postal savings deposits.

As a consequence of its uninterrupted rule between 1955 and 1993, the LDP was the only party in a position to influence the direction of policy-based financing over most of the postwar period. It is no surprise, therefore, that the institution of policy-based financing became integrated into the LDP's political machinery and became a device wielded to satisfy the party's particularistic electoral strategies. Particularly instructive is the example of the Tanaka faction (now known as the Hashimoto faction) and politicians who belong to the "postal tribe" (*zoku giin or yūsei zoku*) who forged especially close ties to the Ministry of Posts and Telecommunications (MPT), which oversaw the

(And Vice Versa): The Political Economics of Financial Liberalization and National Elections in Japan," Ph.D. diss., Georgetown University, 1998).

5. For a comprehensive list of these special corporations, please see Susan Carpenter, *Special Corporations and the Bureaucracy: Why Japan Can't Reform* (New York: Palgrave McMillan, 2003).
6. Kent Calder, *Crisis and Compensation* (Princeton, N.J.: Princeton University Press, 1988) and *Strategic Capitalism: Private Business and Public Purpose in Japanese Industrial Finance* (Princeton, N.J.: Princeton University Press, 1993).
7. Patterson, "Electoral Influence and Economic Policy."

postal system, and to the three postal-related services.[8]

Former Prime Minister Tanaka Kakuei's power in his district and in his party was in no small way built on his legendary ability to direct public works to his constituents. Not coincidentally, many construction tribe politicians also belonged to the Tanaka-related factions. Ties to construction companies were bolstered by the considerable flow of capital into construction projects through FILP. To put it simplistically, the postal tribe protects the inflow of financial resources into FILP, while the construction tribe channels the outflow of financial resources from FILP. Both groups were harbored in the powerful Tanaka family of factions.

Political Connections to Postmasters

A further political connection to the postal savings system comes through the dense personal networks cultivated by the LDP with local elites. Postmasters, especially those in rural Japan, were long a vital part of the LDP's networks, helping to mobilize votes for the party at election time. Unusually, while postmasters were classified as public servants, they were politically appointed in rural areas and could even inherit their positions from relatives. The political influence of Japanese postmasters is particularly striking given that some 19,000 of Japan's approximately 24,000 postal offices do not engage in parcel or mail delivery at all.[9] Virtually all post offices offer postal savings services, however.

The power of the LDP *yūsei zoku* and their links to postmasters played a big role in influencing what types of reform measures could be considered in the Diet. Members of the postal tribe typically headed committees on the LDP's Policy Research Council (formerly Policy Affairs Research Council), where legislation is introduced and where it must typically gain approval before being submitted to the Diet.

8. In 2001 MPT was merged into the Ministry of Public Management, Home Affairs, Posts and Telecommunications.
9. See Patricia L. Maclachlan, "Post Office Politics in Modern Japan: The Postmasters, Iron Triangles, and the Limits of Reform" *The Journal of Japanese Studies*, vol. 30, No. 2, (Summer, 2004), pp. 281-313 for a detailed analysis of the political role of postmasters in Japan.

Bureaucratic Inertia

No single government ministry or agency was keen to call for postal savings reform, for the simple reason that any reform of the postal savings system would be expected to entail the scrutiny and reform of FILP as a whole. Nearly every ministry, even ones such as the Ministry of Health and Welfare, benefited from FILP.[10] These benefits are in personnel. First, *amakudari* or post-retirement positions were available to bureaucrats in quasi-government corporations (*tokushu hōjin*) through which FILP money was allocated. Second, quasi-government corporations also relieved some of the labor burden from the ministries with which they were affiliated. Many of these were established, in fact, in the midst of freezes on the hiring of central government personnel. Ministries could "outsource" or delegate research and other responsibilities to these entities when personnel were insufficient within the ministry to carry out tasks.[11] In this way, while politicians had little incentive to do away with the discretionary funds FILP represented, bureaucrats were also reluctant to take the lead in suggesting reform.

Weak Position of Private Banks in Arguing for Reform

In the early stages of financial development, postal banking, or other state-owned banks, can play a complementary rather than competing role vis-à-vis private sector financial institutions, filling niches private banks are unwilling or unable to fill. Generally as the private financial sector matures, however, it becomes more difficult to maintain a wholly government-owned postal savings institution that receives special public support without its competing head to head with private banks. The nature of private sector financial regulation in Japan and the impact this had on the provision of retail financial services by private banks meant that the public harbored little sympathy for private banks, however. Instead, the public remained strongly supportive of maintenance of the government-owned postal savings system.

The convoy approach to financial regulation, in which no actor was allowed to move forward so fast as to leave the weakest actor behind, meant that Japanese banks never focused on retail banking operations: The post offices did a much better job in meeting the needs of financial consumers. A common slogan was "*Yūbinkyoku wa kokumin ni shinsetsu*" or "post offices are kind to the people."[12] If the debate over rationalizing or privatizing postal savings could be depicted as one pitting efficient banks versus inefficient postal savings institutions, the public would probably have been more sympathetic to the needs of reform. After all, this is the most typical reform rationale propelling privatization or rationalization movements in countries elsewhere in the world. To the contrary, private banks were viewed, correctly, as inefficient, paying lower rates of interest on deposits and charging higher service charges than the post offices.[13] The distance that developed between individual citizens and private banks is an important part of the story of reform inertia.

In 1969, when Japan's high-speed economic growth had been achieved, the banking industry association, *Zenginkyō*, argued within a government deliberation council that the postal savings system had begun to compete with rather than complement or supplement private banking operations. Such complaints elicited little support for private banks, however. In response to growing criticism from the banking industry in successive decades, the MPT issued a statement in 1981 that postal savings continued to meet the needs of individual savers in a way that banks did not and that the exclusive focus by the postal savings system on individuals distinguished it from the banks.

10. Amyx interview with Ministry of Health, Labor and Welfare official in February 2002.
11. Amyx interview with Ministry of Finance official, March 2002.
12. Amyx interview with long-time Japan Federation of Bankers Association official, Satoru Yoshida, 2003.
13. Even over the past four years, the difference in attention to retail financial services has been stark. For example, in contrast to the private bank automatic teller machines (ATMs), the post office ATMs made no service charges for early morning or late night usage. From January 2000, postal ATMs extended their hours of service fee-excluded usage times to span from 7 A.M. to 11 P.M. In contrast, Japan's large city banks were only expanding their similar usage- without-service-charge period in 2003 to go until 9 P.M.

MPT concluded that it was only natural for the government to continue to provide services where the private sector remained underdeveloped and that no private sector financial institutions had been nurtured to focus exclusively on individuals.[14] As a result of the protest from the banking industry, however, the government did respond by allowing banks to diversify the offering of their financial products and to introduce fixed-term savings instruments. Postal savings retained its comparative price advantage, however, offering higher interest rates on deposits.

When MPT and MOF finally decided to liberalize postal savings interest rates, they did so incrementally from 1985 and only completed the process at the end of 1992. By 1992, banks were on equal footing in terms of the financial products they offered; but by then, private banks were also experiencing the aftermath of the bubble's collapse. The ensuing instability in the banking sector contributed to greater relative confidence in the postal savings system over banks. According to a public opinion poll in the Tokyo metropolitan area conducted by the *Tokyo Shimbun* at the end of 1995, one in eight citizens expressed anxiety at this time about the stability of the city banks.[15] From 1994 to 1999, the number of post offices grew from 297 to 24,690 and amounts held in postal savings increased accordingly.[16] With the banking system enshrouded in scandal, *Zenginkyō's* appeal for more transparency in the management of postal savings fell on deaf ears.

Changing Conditions and the Emergence of Reform as a Salient Political Issue

Changes over time in a number of dimensions described in the previous two sections serve as the backdrop for the emergence of significant reform discussions for the first time in the

14. *Yūbin Chokin in Kan suru Chōsa Kenkyūkai* (Study Group on Postal Savings), Ministry of Posts and Telecommunications, March 1981, cited in Hiromitsu Ishii, *Making Fiscal Policy in Japan: Economic Effects and Institutional Settings* (Oxford: Oxford University Press, 2000), p. 176.
15. Poll results cited in Ishii, *Making Fiscal Policy in Japan*, p. 172.
16. Ibid., p. 171.

latter 1990s. Demographics and economics began working against the LDP's former strategies of using postal savings and FILP for electoral gain. For example, the number of independent voters climbed in the 1990s, making it more difficult to target specific groups via FILP spending.

Other factors such as the depopulation of rural areas and the greater accessibility to many different sources of information also worked to decrease the postmasters' political influence and ability to mobilize the special postmasters association on behalf of the LDP. Once closely woven into the social and economic fabric of the local community, postmasters were able to act as effective vote-gatherers.[17] Over time, however, distance emerged in social relations. One postmaster who ran the village post office out of her home in rural Gifu Prefecture commented: "These days, young people would rather drive to a bank in a nearby town and do their transactions more anonymously than keep their money in this post office; doing the latter means that I have personal knowledge of their financial situation and this is annoying (*iya*) in their minds."[18]

A 91-year old retired commissioned postmaster also noted that when he served as a special postmaster decades ago, people in the village often looked to him for guidance on whom to vote for. "But, that was in the days when there weren't many sources of information about candidates and politics and things," he noted. "These days, people have many different sources of information on which to base their voting decision."[19]

Additional evidence suggests that postmasters in rural areas were aware of their weakening political clout as early as 1993. In that year, the postmasters association published a booklet (for internal distribution) that expressed a clear concern that the pressures on them would only increase in the future. This booklet reviewed the history of the commissioned post office system and the battles it had fought up to that time. It also expressed anxiety about the future of the postal business: "On the surface, there is the sense that things are stable but internally (*naiyō-teki ni*) there are many problems . . . " The foreword then goes on to

17. Maclachlan, "Post Office Politics in Modern Japan."
18. Amyx interview, May 16, 2004.
19. Amyx interview, May 16, 2004.

express the hope that the booklet will enable each commissioned postmaster to come to a unified consciousness about the organization's history, role, and future visions which will, in turn, lead to united actions.[20]

Administrative Reform Initiative Under the Hashimoto Cabinet

In the latter part of the 1990s, significant developments related to the Japanese bureaucracy and to national economic performance also facilitated reforms that would affect the status of the postal savings system—and the official flow of its funds, in particular. In 1996, in the face of a public uproar over a series of scandals and policy failures involving key government ministries such as finance, welfare, and foreign affairs, the Hashimoto cabinet launched a major initiative for administrative reform.[21] All major political parties expressed their support for the move.

While a number of cabinets in the postwar era carried out administrative reforms, the Hashimoto cabinet was the most ambitious in that it tried to reshuffle and redesign the entire structure of the central government. Among these organizations was the Ministry of Posts and Telecommunications, which was responsible up to this point for formulating policies for the three postal related services and for the telecommunication and broadcasting industries. Ironically, Hashimoto was a leader of the Obuchi faction at the time, a successor faction to the Tanaka faction. Yet, it was under his watch as prime minister and in the midst of the battle over administrative reforms that reform of the three postal related services would first emerge as an issue seriously debated within the government and ruling party.

Shortly after the Administrative Reform Council was convened to discuss the reorganization, it placed the privatization of the three postal related services on the agenda.[22] In August 1997, the Council announced its Interim Report, which presented a preliminary plan on how to restructure the administrative organizations. The plan was particularly unfavorable to MPT, as it proposed dividing the ministry into three different entities and privatizing postal insurance and postal savings.[23] Faced with such a severe plan, the MPT launched a series of efforts to change the Interim Report. It mobilized the heads of the special post offices and the unions to increase pressure on politicians.[24] LDP politicians, in particular those from the "postal tribes," responded quickly and mobilized to strongly oppose privatization. For example, on August 27, right after the Council had announced the Interim Report, the LDP held a joint meeting of the Division of Communication of the Policy and Research Council and the Research Committee of Telecommunications of the Policy and Research Council in which 120 LDP politicians gathered to express their opposition to the privatization. Even LDP leaders revealed their opposition to the privatization.

On October 5, the chairman of the LDP Policy and Research Council, Taku Yamazaki, made it clear that the three postal ser-

20. Zenkoku Tokutei Yūbinkyokucho-kai (All-Japan Association of Special Postmasters), *Tokutei Yūbinkyokuchō* (1993).
21. For a comprehensive list of post-bubble scandals surrounding central government ministries and agencies, see the appendix in Jennifer Amyx, *Japan's Financial Crisis: Institutional Rigidity and Reluctant Change* (Princeton, N.J.: Princeton University Press, 2004).
22. *Sankei Shimbun*, April 17, 1997. Although Koizumi Jun'ichiro served in the cabinet at this time as minister of health and welfare, articles from major newspapers from this period provide no clear evidence that he played a central role in the placement of privatization on the agenda. Numerous interpretations exist concerning how the issue emerged, with most suggesting that the topic of privatization arose as a byproduct of discussions over introducing Incorporated Administrative Agencies (IAAs) in Japan as part of the government reorganization. IAAs, common in the United Kingdom, are established as bodies external to a government ministry or agency and implement but do not formulate policy. Some thought that an entity carrying out mail delivery, postal savings, and postal insurance functions would be an appropriate candidate for IAA status.
23. Eda Kenji argues that the mass media picked up the issue of privatization, making it a major agenda item for administrative reform and leading the Administrative Reform Council to agree suddenly to include it in the August 1997 Interim Report. See Kenji and Tomohiko Nishino, *Kaikaku Seiken ga Kowareru Toki* (When a Reform Administration Falls Apart) (Tokyo: Nikkei Bijinesu, 2002), pp. 184-85. Other newspapers such as the *Asahi Shimbun* and the *Sankei Shimbun* claim, however, that the inclusion of privatization was due to the strong leadership of Hashimoto. See *Asahi Shimbun*, November 9, 1997 and *Sankei Shimbun*, December 26, 1997.
24. *Asahi Shimbun*, November 10, 1997.

vices had to remain under the management of the state. At the same time, LDP politicians strongly opposed the allocation of responsibilities for licensing and formulating industrial policy for telecommunication and broadcasting industries to different organizations. Instead, they proposed the merger of the Ministry of Posts and Telecommunication with the Ministry of Transportation.

In the face of strong opposition from LDP politicians against the Interim Report plan, the Administrative Reform Council lost control over the allocation of responsibilities to the new ministry, of which the former MPT was to be a part. As a result, when the Council drafted in November 1997 the Final Report on Administrative Reform, which was to set the final plan on how to reorganize administrative organizations, it completely deferred to the LDP's decision on how to restructure the Ministry of Posts and Telecommunications. The LDP decided that the state would continue to manage the three postal related services. It also decided that the government would not divide the oversight of the telecommunication and broadcasting industries into two separate organizations. Instead, it would merge the Ministry of Posts and Telecommunications with the Ministry of Home Affairs and the Management and Coordination Agency. The newly formed ministry would include a Postal Services Agency to manage postal services, postal savings and postal insurance in 2001, when a comprehensive reorganization of national administrative organizations would take place. The Postal Services Agency would then be transformed into a new public corporation (Japan Post) in 2003. In its new form, the corporation would be subject to inspections and regulation by the Financial Services Agency and subject to management principles in line with those observed in the private sector. Another important outcome from this period of political wrangling was reform in the FILP system itself. The requirement that postal savings or insurance income be invested in government bonds was considerably loosened.

It is important to note here that the bureaucracy was in a particularly weak position in this period when the aforementioned changes were made. In the latter half of the 1990s, nearly every government ministry or agency became enshrouded in scandal and / or was blamed for major policy failures. Accordingly, many bureaucratic agencies lacked sufficient political leverage to block those FILP reforms that they might otherwise

have successfully resisted.

As planned in January 2001, the Ministry of Public Management, Home Affairs, Posts and Telecommunications was established as part of the reorganization of national administrative organs. The new Postal Services Agency was placed within this new ministry.[25] Soon thereafter, another event that would have a significant effect on the three postal related services took place within the LDP: the rise of Koizumi to the prime minister's post.

The Push to Privatize

Koizumi and LDP Party Politics

In April 2001, following the resignation of the unpopular Prime Minister Mori, the LDP held an election to nominate the succeeding president. Koizumi won a landslide victory in the party election on his pledge to privatize the three postal related services. More specifically, he pledged to consider the privatization of the three postal services once the new public corporation was established in 2003. Immediately after becoming prime minister, Koizumi appointed a private advisory council to discuss the future of the three postal related services and the privatization of these services was put on the political agenda once again.

What motivated Koizumi's persistent advocacy for privatization? He may be a genuine believer in its efficiency benefits. But the boldness of his stance may be attributed to his unusual position within the LDP, and his populist appeal in an era when corporatist forms of mobilization are proving increasingly ineffective. As some observers point out, Koizumi's political strategy has long been one in which he suggests dramatic measures and conveys ideas to the public in an easy to understand manner. As one bureaucrat notes, "*kaikaku*" or "reform" is a frequently intoned word in the political world, so few take it seriously. Often, a politician's declaration of "reform" is usually a very vague and empty notion. The term "privatization," on the other hand, is attention-grabbing, and its meaning is much clearer

25. In September 2004, the ministry's English name was changed to the Ministry of Internal Affairs and Communication.

and focused than reform.[26]

Moreover, adopting this stance does not hurt him from an electoral or factional standpoint. Kōizumi is the first individual in more than twenty years—since Ōhira Masayoshi—to become prime minister without obtaining support from the Tanaka faction or one of its successor factions. The Tanaka faction and its successors have dominated the LDP for most of the period since the 1970s. Thus, while past prime ministers who relied on support from these factions found it very difficult to put privatization on the agenda, Koizumi is not similarly constrained. In fact, Koizumi played a role in the split within the Hashimoto faction (successor to the Tanaka faction), having assiduously courted some members of the faction while being attacked by its old guard.

Indeed, since he took office in April 2001, Koizumi has publicly stated that LDP candidates should try to appeal more to individual voters and move away from heavy dependence on organized sources of votes. Perhaps this is a far-sighted piece of advice. The postmasters' association readily admits that their ability to gather votes is much diminished:

> "We have been instructed [unofficially by the association] to gather at least 50 votes each" in the upcoming election, said a post office chief who asked not to be named. "But we probably will not be able to gather as many votes we did in the in the last election [in 2001]."[27]

A 2001 election scandal involving postal workers, the weakening of the Hashimoto faction—now enshrouded in a bribery scandal and with many of its heavyweights now retired—and Koizumi's strategy of circumventing the traditional policymaking mechanisms of the LDP, have also weakened anti-privatization forces. In 2001, sixteen individuals—including elite postal bureaucrats and postmaster association members—were arrested for violating the Public Offices Election Law that bans public servants such as postmasters from campaigning for a specific candidate. LDP representative Kōso Kenji, whom the special commissioned postmasters association backed, was forced to resign from the Diet to accept responsibility for these breaches of the law. This incident is clearly in the minds of current postmasters and means that as a group, they are maintaining a noticeably lower profile this time around to avoid the recurrence of similar problems.[28]

26. Amyx interview with central government bureaucrat, February 2004.
27. *Japan Times*, June 7, 2004.

The launch of Japan Post in April 2003 as a state corporation affiliated with the Ministry of Public Management and the preparations leading up to its launch have also weakened the potential clout of postmasters. Since the establishment of Japan Post, postal savings and postal insurance have come under the jurisdiction of the Financial Services Agency, which now carries out regular inspections.[29] This means that even the commissioned post offices are subject to inspections. Moreover, rural postmasters report that the management of finances has become much stricter. A number of special postmasters in one village in rural Gifu Prefecture noted, for example, that prior to the past few years, numerous customers had more than the legal limit of 10 million yen deposited in their respective accounts and the excess was literally ignored. Over the past couple of years, however, the management of account transactions has all become computerized, enabling the immediate detection of such over-deposit incidents, and special postmasters have been strictly ordered not to accept deposit amounts over the legal limit. "I feel badly," one commissioned postmaster said, "but I must make the rounds in the village and return excess deposit amounts to customers these days."[30]

Among the ramifications related to the new salience of postal

28. As a result, the postmasters' OB (alumni) group is the focus of political activities, as retired postmasters are no longer public servants. The sensitivity of the issue of political campaigning was clear in interviews with postmasters in rural Gifu Prefecture. When questions were posed to current postmasters about their political activities, they refrained from replying, simply noting, "well, there was the incident three years ago, so . . . " Amyx interviews as noted above.
29. Financial *supervision*, however, remains with the Ministry of Finance, as is the case with all government-backed financial institutions. The FSA reports its inspection results to both the MOF and to the Ministry of Public Management.
30. Amyx interviews with commissioned postmasters (current and retired) in rural Gifu Prefecture, May 2004.

savings reform are also the decline of the Hashimoto faction and attempts by younger LDP members to increasingly draw in public opinion as a relatively new factor in support of certain policies, or in support of their own political and party careers.

Privatization Hurdles

The strength of the argument for reform of the postal savings system is undeniable. Today it is seen as a symbol of "bloated public finance." In 2004, articles focused on inefficiency in postal savings operations were cited repeatedly in *Japan's Wall Street Journal* equivalent, *Nihon Keizai Shimbun*.[31] For example, in April, it was revealed after an inspection by tax authorities that Japan Post and its predecessor had failed to collect 15.16 billion yen in withholding taxes on postal savings interest from fiscal years 2001-2003 because of the erroneous application of tax exemption extended to the elderly and disabled to non-eligible customers. Moreover, as a public entity, Japan Post is not required to pay taxes. Once privatized, however, Japan Post will need to pay 533 billion yen a year in national and local taxes, according to its own internal estimate. The projected tax payment is expected to contribute to the government's fiscal reform efforts. Japan Post also estimates that, upon privatization, it would likely need to pay 200 billion yen in premiums to the government-backed Deposit Insurance Corporation (DIC). Clearly, this would be a boon to the finances of the DIC, which required an injection of public funds in the late 1990s to deal with the nonperforming loan problem in the banking system.

Furthermore, while the Postal Savings Law stipulates that postal savings should be provided universally, a 2003 report by *Zenginkō* shows that out of the 3,247 cities, towns, and villages in Japan, only ten lacked any type of private financial institution in 2001.[32] The number of individuals left without any financial institution in their immediate locality if postal savings institutions disappear would total a mere 6,769 nationwide (2,747 households), undermining a well-worn argument that privatization would lead to a large public-goods loss by increasing the number of those who were under- or un-banked. Nevertheless, major hurdles to the realization of postal savings system privatization remain.

The biggest hurdle continues to be the strong political opposition from influential lawmakers in the LDP. In early September 2004, the government's Council on Economic and Fiscal Policy agreed that postal operations would be divided up into a mail delivery company, a postal savings firm, an insurance firm, and a company overseeing over-the-counter services, beginning in April 2007 but done in stages so that complete privatization is achieved by 2017. This announcement led dozens of LDP lawmakers to rally in opposition, claiming that they would try to block the legislation aimed at privatizing Japan Post.[33] In the past, government-sponsored bills submitted to the Diet were always vetted first through the LDP's Policy Affairs Research Council (PARC) and the party's Executive Council. Yet, this has not been done with the postal privatization legislation and for this reason, numerous LDP members (numbering approximately 250, according to news reports) claim they are under no obligation to support the bills.

A second class of impediments to privatization has to do with more concrete economic problems to realizing this objective. Since the announcement by the Koizumi administration that postal services would be privatized in April 2007, a committee under the umbrella of the Council for Economic and Fiscal Policy (CEFP) has convened to discuss privatization scenarios. Despite Koizumi's personal enthusiasm for privatization (he went so far

31. Such articles were especially numerous in the May 26, 2004 issue. One article, for example, emphasized the massive size of postal savings assets but then noted the abysmal returns on capital, even in comparison with Japan's private "megabanks" that have been struggling with eliminating massive amounts of nonperforming loans.
32. Private financial institutions are defined here as city banks, regional banks, trust banks, agricultural cooperative banks, long-term credit banks, and second tier regional banks (*shinyō kinko, shōko chūkin, shinyō kumiai, nōkyo, ryūkyō, and rōdo kinko*). *Zenginkyo* (Japan Bankers Federation), "*Yūbin Chokin Jigyō ni Tsuite*," May 12, 2003, p. 3. In the smallest villages that have only a single private sector financial institution, this entity is almost always the financial arm of the agricultural cooperative (*nōkyo*). As with postal savings accounts, deposits into *nōkyo* accounts are limited to 10 million yen. Amyx, 2004 interviews.
33. Reiji Yoshida, "LDP Lawmakers Pledge to Block Postal Reform" *Japan Times*, September 9, 2004.

as to do the calligraphy on the signboard for the Preparatory Office for Postal Privatization[34]), the further discussion proceeds within the committee, the more evident it becomes that the implementation of Koizumi's privatization objectives face numerous impediments. Importantly, these impediments differ significantly from those in previous decades, underscoring that the timing and nature of reform path are of critical importance. It is worth noting that numerous countries have successfully carried out reforms of their postal savings systems without resorting to full-blown privatization.

The Condition of the Private Sector Banking System

When inefficient services are privatized, their exposure to the competitive pressures of the market often presents a challenge to the survival of these services and emerges as a major political issue. While a successful long-term business model for a privatized postal bank is missing from current government plans and is one of the many issues under examination within the Preparatory Office for Privatization of Postal Services, it is notable that privatization could also pose a competitive *threat* to many private banks. Some regional banks, in particular, may find their profitability jeopardized as a result of privatization, depending on how the process is carried out.

If postal savings operations shrink, which they are expected to do after privatization (primarily because the most popular "*teigaku choking*" product cannot be continued with the same attractive interest rate conditions attached to it as in the past), then existing private banks will have an opportunity to attract those funds. Because of stagnant loan demand and the public's seeming resistance to alternative investment instruments accompanied by greater risk, however, these banks have had weak incentives to compete for the public's deposits. For banks, the spread between deposits and loans is a key profit source. Unless a flow of additional funds into banks in the form of savings deposits is accompanied by additional lending opportunities,

34. *Kantei*, "Prime Minister Delivers Address on the Launching of the Preparatory Office for Privatization of Postal Services," April 26, 2004, online at www.kantei.go.jp.

costs will rise and profitability will be negatively affected. In recent years, many banks have also been forced to rationalize operations in the face of heightened competitive pressures and stricter regulatory oversight. Rationalization, in turn, has often led to the closing of bank branches. Such actions make these banks less rather than more attractive to many financial consumers. At the same time, many of the banks that once opposed the existence of postal savings have become integrated into the postal savings system's ATM network, as a means to expand their capacity to compete for retail business.[35] For these reasons, it is unclear that all banks will be able to seize the potential business opportunities presented by the shrinking of postal savings.

At present, regional banks have the advantage of offering foreign currency denominated deposits and trusts, as well as other products not currently offered by post offices such as pension insurance and life insurance. However, if the post office expands its fee-based distribution business, selling financial products, then such operations will directly compete with the regional banks. Because the strength of regional banks varies considerably from one prefecture to another, the competitive threats posed by postal savings privatization loom large to some and weaker to others.[36]

One proposed solution to the problem of how postal financial operations can run profitably without overwhelming private financial institutions is for post offices to sell products of private-sector insurers, asset managers, securities companies, and the like.

35. Citicorp, a foreign bank, was the first to approach MPT to pursue the possibility of joining the postal savings system ATM network (the idea of doing so had been considered taboo among Japanese banks). Once Citicorp became integrated into this network (as the first private-sector financial institution to do so), Japanese banks felt pressure to join as well. Failing to do so would have left them at a comparative disadvantage. In effect, this move represented the first instance of cooperative business relations with the postal savings system.

36. While the balance in postal savings accounts nationwide exceeds the balance in all regional banks combined, the picture looks differently if we examine the breakdown across each of the forty-seven prefectures. In fifteen prefectures, regional banks hold a higher percentage of total deposits than do postal savings. "Yūbin Chokin vs Chigin Jyoiko Shaaru Bunseki" (Analysis of the Share of Postal Savings Versus the Top Regional Banks), *Kinyū Bijinesu* (June 2004), pp. 12-19.

Some question the ability of postal workers to act as agents for a wide variety of financial products, given their lack of specialized training. A recent government decision represents one attempt to address this and other potential problems by using post offices as platforms for the delivery of financial products developed by the private sector. Beginning in 2006, the government will allow the post office to distribute private-sector investment trusts but will permit only 500 of the largest post office branches to handle the new products. Moreover, the employees responsible for selling those products are to be licensed, the product selection process is to be transparent, and the post offices will be required to set commissions in line with current private sector standards. If these sales actually expand in the future, then technology such as video kiosks might also be used to enable private-sector providers to have equal access to this distribution channel and to allow interested customers to communicate directly with product specialists at those private-sector providers.[37]

Japanese Government Bonds (JGBs)

A second and perhaps even important impediment to privatization relates to its potential impact on public finances. While the fiscal role of yūcho was always an important supplementary feature of Japanese economic policy and budget politics, it is perhaps even more important in the present situation of deflation, near-stagnant growth rates, weak political and bureaucratic actors, and weak banks. Reforms implemented in 2001 mean that it is no longer compulsory for postal savings to be directly deposited into the Trust Fund Bureau Fund for loans to the FILP agencies. Postal savings are now invested on a discretionary basis. In this respect, the link between postal savings and FILP has ostensibly been severed. In reality, however, most postal savings funds continue to be invested in Japanese government bonds, municipal bonds, or bonds issued by FILP agencies.

The postal savings and postal insurance systems today hold over 20 percent of the total balance of JGBs.[38] Given the low

37. Amyx interview with Jonathan Schuman, co-chair of the Financial Services Committee, the American Chamber of Commerce in Japan, June 2, 2004.

returns on JGBs, a privatized company might be expected to seek better investment opportunities and decrease its holdings accordingly. The result could be a decline in the predictability and stability of the JGB market, leading to a rise in the long-term interest rate. The damage inflicted on the Japanese government bond market could be huge. This is of concern not only to the finance ministry but also to *Zenginkyō*, which fears that private banks might come under pressure to purchase more bonds in such a situation.

Ironically, however, exposure of the postal savings system to government debt is *growing* at a time when these agencies' freedom to invest in the market is expanding. In fiscal year 2004, the postal savings system is expected to absorb 19.7 trillion yen of Japanese government bond issues, compared with 9.9 trillion yen in fiscal year 2003.[39] Even while the finance ministry scrambles to market JGBs to individuals and other investors to limit the concentration of holdings (diversification limits the likelihood of a shock to the market arising from economic difficulties faced by institutional investors), the simple jump in the amount of government and government-guaranteed bonds limits the impact of such efforts. With an approximate doubling of Japanese government indebtedness over the past decade, the size of the JGB market now exceeds that of the U.S. Treasury market. This comes at a time when market actors have become increasingly reluctant to absorb more JGBs, given their negative experience in June 2003 when a sudden, sharp surge in yields left holders with substantial paper losses on their portfolios. Consequently, public institutions such as postal savings are more important than ever to the government in absorbing JGB issues.

38. Zaimushō Rizaikyoku, "Waga Kuni no Kokusai Kanri Seisaku" (Policy for Managing Our Country's Government Bonds), April 8, 2003, p. 19. All government-backed financial institutions together held 41.1 percent in 2003. By comparison, the equivalent figures for the United States, Great Britain, Germany, and France are 12.8 percent, 3.9 percent, 0 percent, and 15.7 percent, respectively.
39. Oxford Analytica Daily Brief, January 2004.

Conclusion

Many changes have taken place in Japan's political economic landscape over the past decades, and particularly in the past decade and a half. These have included demographic changes, financial liberalization, the emergence of scandals and policy failures in the bureaucracy, instability in private sector finance, changes in the party system, and changes in electoral rules. Together these have helped spur a shift from inertia to more proactive reform of the nation's postal savings system. As noted above, however, the current blueprint for reform that centers on privatization may not be the best one for Japan. Clearly, the timing and character of reform are critical and the delay of real reform of the nation's postal savings system until the twenty-first century has brought with it numerous problems.

The political dynamics surrounding liberalization and reform of the postal savings system differ significantly today from political dynamics surrounding this issue in earlier periods. Japan's banking industry organization, *Zenginkyō*, once spoke in a unified (albeit ineffective) voice for all banks in seeking the privatization or dismantlement of postal savings. Today, however, interests across the banking sector are more diverse. While virtually all banks seek reform of the current system, particular forms of privatization present opportunities to some private actors and threats to others. Indeed, until more details of the privatization process are worked out, it is unclear who will "win" and who will "lose" as a result of the reforms. As the article has shown, many private regional banks may face heightened competitive pressures as a result of privatization. At the same time, there is a serious concern that the Bank of Japan may be called upon to purchase large amounts of Japanese government bonds if the privatization of postal savings and insurance triggers a crisis in the government bond market.

The privatization of postal savings represents both a threat to some actors and an opportunity to others. How the process plays out hereafter—in particular, decisions made in the 2005 ordinary Diet session regarding the government's legislative proposals for privatization—will have a major long-term impact on the functioning of Japan's financial system. The ongoing political battle is thus worthy of our continued attention.

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