

INTRODUCTION

WHY JAPAN MUST BE REIMAGINED

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EARTHQUAKES ARE A TERRIFYING reminder of human frailty. They strike without warning. They kill indiscriminately. They flatten cities. The Great Eastern Japan Earthquake of March 2011 brought all that, plus a devastating tsunami and a nuclear emergency the equivalent of Chernobyl.

And yet, as the people of Japan have shown, such tragedies can also illuminate the best of human nature. Within weeks of the crisis, it was clear that, although the chain of destruction had resulted in the deaths of tens of thousands and unalterably changed the lives of hundreds of thousands more, Japan would recover. Survivors were bearing their hardships with extraordinary dignity and courage. The nation had begun mobilizing to rebuild. Though battered by one of the most powerful seismic jolts in recorded history, Japan was unbowed.

This book was on its way to the publisher when the earthquake hit. We immediately commissioned new material; many authors recast their work. The ideas and insights assembled in this volume, therefore, explore the idea of restoring Japan in a much broader sense than mending the damage done by the disasters.

In fact, Japan faces two separate emergencies. The first is the urgent need to rebuild the Tohoku region. Kobe's eventual recovery following the earthquake that flattened much of that city in 1995 offers reason for optimism about Japan's capacity to recover from geological shocks.

The second emergency is less obvious because it is ubiquitous; it has to do with Japan's long-term social and economic trends. Well before March 2011, Japan's once-formidable economy had been sputtering. Growth was lackluster. Deflation persisted. Japan's workforce was shrinking at an alarming rate, and the nation's

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population, already the world's oldest, was also the fastest aging. The debt-to-GDP ratio was more than 200 percent, the highest in the developed world.

The country continued to excel at manufacturing; even so, many of its largest and best-known companies had lost market share to rivals from South Korea and China. Meanwhile, its service industries were global laggards. And despite a highly educated, technically savvy workforce, Japan had failed to create the sort of entrepreneurial culture that could compete with Silicon Valley. In sum, the economic model associated with Japan's rise, including such features as close collaboration between the public and private sectors and lifetime employment, had faltered. No robust new model had emerged to take its place.

When the earth moves, nothing can stop it; when a tsunami forms, it must crash to the shore. But Japan is not helpless when it comes to the social and economic factors that play a large part in determining long-run prosperity. Change is never easy, of course. As Takeda Pharmaceuticals CEO Yasuchika Hasegawa notes in his essay in this volume, "Despite our long record of withstanding sudden external shocks, we are less successful in combating gradual, long-term challenges, especially when the origins of those problems are homegrown." The important point, however, is that the future is not fated. Japan can shape its own destiny. The key variables are all within the control of the Japanese people themselves.

As McKinsey considered Japan's difficulties in addressing these long-term challenges, we decided to reach out to a distinguished group of business leaders, experts, and thinkers. We conceived *Reimagining Japan* as an effort to consider Japan's strengths and weaknesses along many dimensions, social and cultural as well as economic and political. To that end, we invited debate from an extraordinarily diverse mix of contributors; together, they bring a wealth of expertise without parallel in a single volume. These are independent voices. McKinsey did not tell them what to say or challenge their conclusions; we wanted their views to help Japan think through these difficulties.

Many of our contributors offer detailed (and sometimes contradictory) prescriptions. The head of McKinsey Japan, Heang Chhor, the driving force behind this project, suggests his own road map. But *Reimagining Japan* is meant as neither a "white paper" nor a precise policy plan. Rather, our hope is to provoke discussion and to contribute to debate about how Japan can define its future.

Naturally, this volume includes economists, academics, and CEOs (from Asia, Europe, and the United States). But it also includes contributions from a video-game designer and a *manga* artist. Baseball's Hideo Nomo and the man who saved the Akita dog breed are the subjects of other essays.

Despite the differences in the authors' backgrounds and perspectives, several themes surface repeatedly:

Openness: Again and again, authors noted that younger people seem increasingly unwilling to venture outside the safe cocoon of Japan, a symptom of a worrying insularity at a time of rapid global integration. Glen S. Fukushima of Airbus Japan

notes that the number of students going overseas to study has dropped dramatically. He is not the only author to compare the country's attitude today to the Tokugawa shogunate's policy of *sakoku* (or "closed country"), where no foreigners were permitted to enter Japan, and no Japanese were allowed to leave. And Takumi Shibata, deputy president and COO of Nomura Holdings, is not the only person to call for a new Meiji, the era that followed the shogunate's demise, in which Japan embraced the world: "We must try to rekindle that positive energy."

Openness matters because in an ever-more competitive world, the only way to compete is to test yourself against the best. That is the lesson that Takeshi Okada, the former coach of Japan's national soccer team, takes from his own difficult sojourn in Germany and the experience of other athletes who have played in Europe.

As a market, Japan is big enough to stand on its own. But that size can become a trap. Venture capitalist Allen Miner demonstrates that Japan does not lack entrepreneurial verve; what is missing is the ability, or perhaps the desire, to take great ideas global. *Nihon Keizai Shimbun* technology writer Waichi Sekiguchi dissects the "Galapagos Syndrome," a term that describes the tendency of Japanese companies to make wondrous products that can work only in Japan. This is no way to become a global leader.

Diversity: Japanese society, like the best varieties of Japanese rice, has a marvelous "stickiness." Japan's people feel bound to each other. They rally together in times of difficulty, and have developed elaborate social norms and codes of personal conduct to preserve harmony. That sense of mutual obligation governed the extraordinarily civilized manner in which Japan's citizens endured the terrible days and weeks after the Tohoku disasters.

Japan's cohesiveness is often ascribed to its ethnic and cultural homogeneity. But as David Sanger of *The New York Times* notes, homogeneity also can be a disadvantage. In a global economy where rewards increasingly accrue to creative "knowledge workers," it helps to have a feel for multiple perspectives.

One dimension of this problem is English, the language of global business. The standard of spoken English in Japan is comparatively poor; as a result, not only are Japanese often uncomfortable in international settings, but the country itself can be intimidating for foreigners to navigate. Japan's largest companies might consider following the example of some global competitors in adopting English as their corporate language. Even if they do not, they must do better in recruiting and retaining Japanese with international experience, as well as foreigners who understand how to operate in Japan.

A second way to diversify is to bring in more people. Cities like London and New York get much of their energy from their global orientation; almost four in ten New Yorkers were born overseas. Could Japan, or at least Tokyo, be like that? As Japan's own workforce contracts, and as its companies push into such high-growth emerging markets as China and India, Japanese employers must learn to compete for global talent. And yet the country retains an unusually strong aversion to outsiders

and immigration, an attitude reflected in the fact that it has a lower percentage of foreign-born residents than any other nation in the Organisation for Economic Co-operation and Development (OECD).

Even if Japan does not accept a large influx of immigrants in the near future, it could still bring in more points of view by taking advantage of its position as the region's most developed country. Author and former editor of *The Economist* Bill Emmott believes Japan should seek to become "Asia's hub for ideas, technology, culture." Infosys CEO Senapathy Gopalakrishnan suggests Japan create an independent global university specializing in technology and drawing in students from all over the world.

A final source of diversity could come from within: Japan's women. As a result of demographics, it is a mathematical certainty that Japan needs to expand its workforce. If the country will not accept immigrants, more Japanese need to get to work. And the largest untapped resource is women, whose attachment to the workforce is limited, with most quitting after giving birth and few building long-term careers.

Japanese businesses should diversify their boards by including more foreigners and more women. Instead, these corporations have taken the opposite approach to an extreme; the typical board member is Japanese and male, and has been working at the company his entire professional life. Boards thus composed are a closed circle that can keep out fresh ideas and new thinking. Shiseido's chairman Shinzo Maeda made it a priority to diversify the cosmetic company's board when he was CEO; among other advantages, he writes, meetings are more interesting than they used to be.

Innovation: The Japanese are rightly proud of their manufacturing expertise. And of course there is a place, and always will be, for high-value, high-quality manufacturing in Japan, just as there is in Germany and the United States. But with China (and other countries) climbing up the value ladder, mass manufacturing in Japan is the wave of the past. "No labor-intensive industry can revive Japan," SoftBank founder and CEO Masayoshi Son argues. "Knowledge-intensive industries are the only way forward." Tomoko Namba, the founder of DeNA, Japan's most successful mobile games operator, identifies a number of factors that prevent Japan from hatching successful start-ups, and hinder the ability of Japanese ventures to compete with rivals in Silicon Valley.

Japan is known for its service ethos. And yet the nation is a global laggard when it comes to such important service industries as aviation, financial services, accounting, insurance, law, and tourism. Gopalakrishnan describes Japan's service sector as "an island unto itself." In 2009, according to the OECD, Japan created only 67 percent as much economic value per hour as the United States—much of that gap came from its underperforming service industries. This is not a trivial issue, considering that services accounts for more than three-quarters of Japan's GDP. Such inefficiency saps competitiveness, economist Adam S. Posen concludes.

One problem is that Japan's education system, which served the country so well for so long in the postwar era, is not delivering as many of the flexible, creative thinkers as Japan needs for what best-selling management author Stephen R. Covey calls the "Knowledge Age." Rather than turning out clever crammers, Covey argues, Japan's educators must cultivate among students a sense of their own "primary greatness"—that is, future leaders who are self-sufficient, internally motivated, and accustomed to thinking for themselves. Keiji Inafune, a noted game creator and entrepreneur, notes that a salaryman ethos prevails in the sector, unlike the more decentralized, performance-driven US model—and Japan has gone from dominant to also-ran.

Leadership: Is Japan capable of fundamental change? Many authors—including celebrated Japan specialists Ezra F. Vogel and Gerald L. Curtis—note the shortcomings of Japan's political system, and the reluctance of the nation's political elites to abandon the entrenched factionalism and parochialism of the past. Tadashi Yanai, CEO of Fast Retailing, one of Japan's notable recent success stories, perceives a similar flat-footedness among Japan's business leaders. He worries that "other countries are growing, while we in Japan stick to our old ways."

Historians Ian Buruma and John W. Dower, however, take issue with the oft-heard assertion that Japan cannot change. Of course it can, they argue; the nation has done so many times before. Carlos Ghosn, the man who led the turnaround at Nissan, notes that "Japan doesn't always move fast, but it always catches up." And Henry Tricks, Tokyo bureau chief for *The Economist*, discerns the possible emergence of a new generation of bolder and more far-sighted Japanese leaders in both the political and corporate spheres.

Perhaps the single message that shines through most clearly in these pages is that Japan has a huge community of global friends and supporters. The world has an enormous stake in Japan's success.

To realize that hope, Japan must change. The country does not have to reject its traditional values; these can serve Japan well, as the world saw after the tsunami. But Japan must adapt those values to a changed world.

Japan balanced tradition and transformation successfully in the Meiji era, led by men of courage and vision like Ryoma Sakamoto. After World War II, a generation of entrepreneurs led by such iconic names as Honda and Matsushita helped reshape Japan's struggling postwar economy into an economic powerhouse. The Japan that emerged from those transitions was stronger, richer, and more confident.

Few of the issues the contributors to *Reimagining Japan* identify will be unfamiliar to the Japanese. Indeed, some of the essays could have been written five or even 15 years ago. The problem is that weak governments and Japan's very success has attenuated the sense of urgency.

For 20 years, Japan has drifted. To reimagine a brighter future, that must change.

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