Toyoo Gyohten: The Responsibility for Recovery Lies in the Hands of Business People

Toyoo Gyohten is president of the Institute for International Monetary Affairs and senior adviser to the Bank of Tokyo-Mitsubishi, Japan’s prime financial institution. Formerly he was chairman of the Bank of Tokyo and for many years he served the Japanese government as Vice Minister of Finance and was special adviser to the prime minister.

His unique perspectives on international monetary affairs spanning four decades are documented in Changing Fortunes, a book he co-authored with former U.S. Federal Reserve Chairman, Paul Volcker.

In April 2009, he visited IESE Barcelona to participate in a meeting of the school’s International Advisory Board of which he is a member. During his visit, he was interviewed by Alfredo Pastor, professor in the Department of Economics, whose areas of specialization include the European Union, Spanish economic policy, the role of the State in a market economy and the Chinese economy.

Here follows a full transcript of their conversation.

TOYOO GYOHTEN: Good morning, Prof. Pastor.

ALFREDO PASTOR: I would like to thank you, on behalf of IESE, for giving us this interview, because our audience is made up mostly of business people, executives and so on, and whatever comments you have will be of great interest.

GYOHTEN: Very good. I am very much honored and pleased to have this opportunity.

PASTOR: I will make the mistake of quoting you. This is something we always dread, when you say, “A few years ago you said…” You think, “Oh, gosh, what did I say on that?” Well, in 1992, you said that we needed a change of paradigm in the way the financial world and the economic world operated. Do you still think so? Do you think the change has happened or is bound to happen shortly?

GYOHTEN: I still strongly believe that. I think actual change really took place, particularly during the 1990s and early part of the 21st century. That was a great change.

PASTOR: For the good, or not?

GYOHTEN: Well, it is we who can change it either for good or for bad. At this moment, I have to say that we are still unable to ascertain whether we are on the right path or the wrong path.

PASTOR: With the experience that you have in your long life as a professional economist and a civil servant, and especially as vice minister for finance in Japan, how do you see the measures that different governments are taking to face the current crisis?

GYOHTEN: First of all, I have to confess that we did make a serious mistake when this current crisis started in the early part of 2007. None of us realized the depth and implications of the crisis properly, so our early response to the crisis, in my view, was very clumsy. The measures were taken too little, too late. We wasted time, and the situation was aggravated considerably.
After the so-called Lehman shock in September 2008, we all came to realize the real meaning of the crisis, and I think the policies we have been taking after that were, all in all, in a good direction. The problem is the speed and the amount of resources we are putting into that.

PASTOR: Are you thinking mostly of the fiscal stimulus or of the bank stimulus?

GYOHTEN: Both. Certainly we have started our policy responses in the right direction, in my view. But we are just at the very beginning. We don’t see how those measures will work. In the case of the financial measures – that is, the provision of liquidity into the market or clearing toxic assets and replenishing the banks’ capital – all these measures are necessary and the right ones. But we have just started.

PASTOR: But have we started?

GYOHTEN: Well, these areas are planned. For instance, in the U.S., which is the epicenter of the crisis, they just published the plan [March 2009], the so-called Geithner toxic asset plan. So there is a plan. Also, in the replenishment of capital, they have pledged to the public that they will start doing operations once they have collected and analyzed the actual, real situations of major banks. Well, plans are there. In that sense, steps have been taken. But we are still to see what will be coming out of these plans.

PASTOR: I think the U.S. has left aside the possibility of creating these so-called bad banks, which is a solution that has been adopted on other occasions. For instance, this was the strategy adopted in China, cleaning up the bad assets of the banks, so that they could operate normally. Do you think the bad bank is a necessity?

GYOHTEN: Well, what is necessary is to separate those bad assets from banks and somehow clear them, either by putting them in a new institution – you may call it a bad bank…

PASTOR: Which is not a bank, by the way.

GYOHTEN: …or you just sell it, liquidate it at market price. So I don’t think the structure of a bad bank itself is an absolute necessity, because there are other means of liquidating or clearing bad assets. The important point is to just clear those bad assets from banks. That’s a must.

There are piles of very difficult problems before we can get the right solution. First of all, to decide which asset is bad and which is good. Then, what should be the price of the asset? And thirdly, who is going to finance that transaction?

All these problems need to be solved before the transaction or operation can be a success. And the American plan is certainly one way of dealing with the problem – that is, to try to activate and encourage private sector participation in the whole process while the public sector, Treasury, or the Fed, is prepared to provide very significant financial support; to guarantee support, very significant support.

So this is one way of trying to solve that. But as you said, there are other ways, for instance, other countries did it in different ways. I think the Chinese are doing it a different way. I don’t think the bad bank per se is an absolute necessity.

PASTOR: But it may be very convenient in some cases.

GYOHTEN: Oh, yes, of course.

PASTOR: Is Japan adopting anything like it? Are toxic assets a big problem in Japan?

GYOHTEN: It was a big problem in the late 1990s.

PASTOR: In the previous crisis.

GYOHTEN: It is no longer a major problem. I think after spending almost, let me see, 5 percent of the total GDP in that operation, at the worst period, Japanese banks’ ratio of bad assets was
almost 20 percent of loan assets, and it was reduced to just above 1 percent or so. That was a very heavy burden on public money.

**PASTOR:** And your prime minister was very insistent before the G20 meeting that other countries had to adopt very substantial fiscal stimulus. Do you agree with that view?

**GYOHTEN:** I have to agree with you. Because, you know, in this current crisis, two major problems are there. One is in the financial sector — that is, the problem of the credit crunch — and the other problem is within the real economy sector, which is the collapse of demand. I suspect that most countries around the world have started, or are in the process of providing, very ample liquidity into the market. So the remaining problem is, how can you really start stimulating the demand, not simply by providing easy credit?

In that sense, fiscal policy, whether you like it or not, has to play a major role, because fiscal policy, either through tax measures or expenditure measures, can have direct impact on people’s consumption or corporate capital spending. So I think fiscal policy has to play a major role.

Of course, activation of fiscal policy may be accompanied by very grave risks in the future: inflation, default, deterioration of the balance sheet. You have to be really, really careful, and you have to be very determined to avoid the future deterioration of your public policy situation.

This is a very serious political issue, which must have support from every sector in society, not only from politicians or from business, but also from taxpayers and private citizens, who have a great stake in this.

Having said that, I think, at least at present, we need very active fiscal policy to save this situation of the collapse of demand.

**PASTOR:** I think your prime minister thought that measures adopted in some European countries were insufficient.

**GYOHTEN:** Did he say that? I didn’t hear that!

**PASTOR:** I think so, because he was immediately answered by German Chancellor Angela Merkel saying that they did not want that; they could rely on exports.

**GYOHTEN:** Well, I cannot agree with him so easily, because I know the European situation pretty well, and I know how European policy makers and taxpayers do feel about very active utilization of fiscal policy. You have much more serious experiences of inflation than people in America, for instance; than in the case with Japan. It is quite understandable that European people, as a whole, are more cautious about fiscal stimulus in fear of possible inflation in the future.

Having said that, I also sympathize with my prime minister, because he believes that fiscal stimulus is now an absolute necessity for the world, and in Japan, he is starting to take that very active fiscal stimulus in the face of public concern. In order to convince his own people, he needs global support, so that he can tell his own people that, look, this is a thing: global citizens are doing the same.

**PASTOR:** Everybody’s doing it.

**GYOHTEN:** That’s right.

**PASTOR:** Some time ago, you said that during a time of crisis, the responsibility for recovery lies in the hands of business people, essentially, CEOs and business leaders. Most of our audience are either CEOs or business leaders or future business leaders. What recommendations would you have? What does it mean to act like a CEO in a time of crisis?

**GYOHTEN:** Well, I remember I said that when the Japanese economy was in serious crisis in the late 1990s. At that time, bluntly speaking, we ran out of fiscal policies, monetary policies. Macroeconomic policies were all exhausted. Still, the economy remained very sluggish.
What I thought was, look, it is, after all, the corporate sector that can really revive the economy, by leading the economic opportunities in the country. Also, it was quite obvious, at that time, that the Japanese corporate sector was not really very forthcoming in that leadership role, because they themselves were burdened by excessive debt, excessive employment and excessive capacity. So they had to introduce major, major restructuring of their own. Otherwise, the corporate sector would not revive, and the economy would not revive.

I have to say, some of our business leaders, at that time, were still rather complacent, hoping that, “Well, we are in bad times, but good times will come sooner or later, so just wait.” There was lack of strong initiative and willingness to sacrifice or take pain in demonstrating that leadership.

I am not in a position to give any lectures to business leaders. But I think, first of all, they should feel a strong sense of responsibility, both as leader of the company – they have their own employees, hundreds, thousands, some tens of thousands of employees, whose lives are depending on this leadership – and they have customers and community surroundings. They should have the sense of responsibility to put the role of the corporate sector in a right position, because, after all, a country’s economy will be supported by three players: the corporate sector, the household sector and the public sector.

The corporate sector always has very serious leadership responsibilities. I do believe it is very important for every CEO to entertain this multiple sense of leadership role, as a head of a corporation, but at the same time the leader of the sector, a very important sector in the economy. Particularly in this world of globalization, the role of a big company’s CEO is almost global. Your company’s performance can affect the far corners of the world. This sense of responsibility is really crucial.

PASTOR: Would you also have some words of encouragement for them? Because many of them feel very disoriented. This crisis is so big, it is difficult to understand, and for many business leaders, sometimes they do not see how to handle it.

GYOHTEN: There will be no eternal darkness. The night will end sometime. And it is often said that when you feel it is the darkest, that is the time when maybe the dawn is approaching. This is not very pragmatic encouragement, but I think it’s true.

Of course, before they start enjoying some encouragement, they have to go through a period of reflection and probably self-condemnation. They have to graduate from that process, anyway.

And after graduating from that process, I am sure they can find encouragement, or a glimmer of hope, or bright sunshine at the end of the tunnel. I am a strong believer in that. And you can look back at history. Optimism always pays. It is better paid than pessimism. Don’t you think so?

PASTOR: It makes you feel better.

GYOHTEN: Right.

PASTOR: Thank you very much.

GYOHTEN: You are most welcome.

PASTOR: It’s been a very pleasant conversation.

GYOHTEN: Thank you very much, Alfredo.

* Note: The above text was lightly edited for grammar and factual accuracy. Please check against actual delivery on video.