Columbia Business School
Center on Japanese Economy and Business

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State Intervention and Private Enterprise: Japan, the U.S., and China

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Columbia University

This conference addressed the topic of state intervention in private enterprise, comparing recent and historical trends in the United States, China, and Japan. Speakers and discussants addressed a broad range of topics relevant to the subject of intervention, from state-owned enterprises, to government buyouts of distressed firms, to regulation surrounding foreign direct investment. This event was co-hosted by the Center on Japanese Economy and Business (CJEB) at Columbia Business School (CBS), the Japan Economic Foundation (JEF), and the Center of Japanese Legal Studies (CJLS) at Columbia Law School (CLS).

Hugh Patrick, R.D. Calkins Professor of International Business Emeritus and director of CJEB, and Kazumasa Kusaka, chairman and CEO of the Japan Economic Foundation, welcomed participants to the event. Following the welcome, the event featured panels, one focused on the United States, another on China, and a third on Japan. The event concluded with a roundtable discussion with representatives from each panel and closing remarks by Curtis J. Milhaupt, Parker Professor of Comparative Corporate Law; director of the Parker School of Foreign and Comparative Law; Fuyo Professor of Japanese Law; and director of CJLS.

Welcoming Remarks

Hugh Patrick

Professor Patrick welcomed the audience and participants and emphasized the importance of the conference as an opportunity to discuss a wide range of extremely relevant and timely issues. He then introduced Mr. Kazumasa Kusaka, chairman and CEO of JEF, and described Mr. Kusaka's professional background in both the government and private companies as particularly well-suited for the conference topic.

Mr. Kusaka began his remarks by detailing the government's role in private enterprise as having two functions: 1) short-term risk abatement and response to crisis, and 2) as a part of a long-term growth strategy. Mr. Kusaka classified the U.S. government's response to the Lehman Brothers collapse and the ensuing financial sector crisis in September 2008 as an example of state intervention in the short term, explaining that this kind of response reflects traditional fiscal and monetary policy as well as being aimed to provide direct assistance to prominent private companies that act as backbones of the domestic economy. Mr. Kusaka added that this type of short term response is not limited to the financial sector, as other private enterprises, including General Motors, have been targets for government crisis management.

Kazumasa Kusaka

With regard to the second type of state intervention, Mr. Kusaka used the example of the debate surrounding China's state capitalism model, where the state intervenes in all aspects of the economy with goals of long-term economic growth. With so many global enterprises merging in China, Mr. Kusaka described a need to assess how government intervention into enterprise market access, finance, and technology development affects the competitiveness of global enterprises.

Panel I: United States

In the first panel, Gary Clyde Hufbauer, Reginald Jones Senior Fellow at the Peterson Institute for International Economics, gave a presentation on state intervention in the United States, followed by responses and further discussion with Christopher J. Mayer, Paul Milstein Professor of Real Estate at CBS, and Roger Kubarych, vice chairman of Craig Drill Capital and former national intelligence manager at the National Intelligence Council. Merit E. Janow, dean and professor of professional practice in international economic law & international affairs at SIPA, moderated the panel.

Panel I, from left to right: Roger Kubarych, Christopher J. Mayer, Gary Clyde Hufbauer, Merit E. Janow

Dean Janow opened the panel discussion by sharing a memory from the 1980s, when many in the United States were debating Japanese interventionist policies in the industrial sector, including direct subsidies, bailouts, and heavy import tariffs. Then, in the 1990s and early 2000s, the United States began to take a less interventionist role in the economy. However, this stance was reversed during the 2008 crisis, when Dean Janow noted that the U.S. government made several large-scale interventions, albeit generally followed by a rapid government exit. With all this in mind, she asked the panelists what they believe to be the nature and effectiveness of U.S. intervention in private enterprise.

Dr. Hufbauer responded by stating that every country has its national myths. In the case of the United States, the myth is that the government does not intervene in private enterprise. He asserted that, on the contrary, the United States has at least three distinct, regular forms of industrial intervention policy. The first is the tax code, which he contended is an illustration of interventionism favoring small enterprises. He asserted that this type of intervention strongly disfavors large firms, who pay the highest statutory rates. The second example of U.S. intervention is the provision of explicit and implicit loan guarantees; while Fannie Mae and Freddie Mac were not explicitly guaranteed before the Great Recession, they were implicitly supported, and since the Great Recession have been explicitly guaranteed. In addition, since the Great Depression, U.S. farmers have benefitted from favorable-rate and easy term agricultural loans. In general, the U.S. Congress favors loan guarantees for select frontier industries, and for the last decade, has

Merit E. Janow

Gary Clyde Hufbauer

strongly favored renewables. The third example Dr. Hufbauer cited was price and volume support for favored industries. While agricultural commodities are perhaps the most obvious example, he also addressed renewable energy and health policy. For example, the U.S. government guarantees prices for green energy, and Obamacare requires the compulsory purchase of insurance by individuals.

Dr. Hufbauer concluded by outlining three phases of robust U.S. interventionism: agricultural subsidies beginning in the Great Depression, support for the housing industry after the Great Depression, and the recent bailouts of large failing firms. The continuation of these policies is evidence that the United States is an interventionist state, even though mythology claims otherwise.

Professor Mayer, an expert on the housing and financial service credit markets, agreed with Dr. Hufbauer's remarks that the housing industry is a favored industry. The fact that implicit rent is non-taxable is one clear piece of evidence for this assertion. Professor Mayer added to this idea, explaining that housing is the most significantly subsidized sector worldwide because the largest financial return to owner-occupied housing is that "you get to live in the home." He stated that, as far as he knows, virtually no country has a wealth tax specific to housing.

With regard to the 2008 economic crisis, Professor Mayer differentiated Freddie Mac and Fannie Mae from other "bailed out" companies, such as American International Group (AIG) and General Motors (GM). Freddie Mac and Fannie Mae, he explained, were purchased by the U.S. government without an exit plan. However, the government did not purchase every share of the two entities and left many private stakes outstanding, which have since been picked up by private equity. Now, the government cannot buy them out. Professor Mayer contended that this lack of exit planning confuses investors and taxpayers alike. Investors need more information to make good decisions, and taxpayers need to maintain realistic expectations of their government.

Christopher Mayer

Professor Mayer concluded by referencing Dr. Hufbauer's comments on the corporate tax code, arguing that the discussion is about "tradeable" versus "non-tradeable" goods. When tradeable goods are taxed, they move to other markets. When non-tradeable goods are taxed, they stay in their current markets. He explained that, in this context, tradeable goods include those provided by large, economy-dependent firms, and non-tradeable goods include real estate. He argued that tradeable goods should have a lower tax rate.

Mr. Kubarych focused his comments on the restrictions that the U.S. government has placed on the ability of foreign companies to invest in the U.S. market. The United States is not unique in that every country has foreign direct investment (FDI) restrictions; many of these regulations are defense-related, but they also apply to aircraft and airlines, infrastructure, and broadcasting.

Mr. Kubarych explained that state intervention in this realm is coordinated by the Committee on Foreign Investment in the United States (CFIUS), part of the international office at the U.S. Department of Treasury. This inter-agency committee, which assesses the national security risk of FDI transactions, came into being in the mid-2000s to toughen FDI restrictions. About 100 "covered" cases that are being considered by an acquiring company are brought to CFIUS yearly. CFIUS operates on tight deadlines so as to not hold up clear transactions. For the transactions that raise national security issues, the Committee can ask for modifications or simply discourage the transaction in its entirety. Mr. Kubarych asserted that the vast majority of the cases are amicable and CFIUS does not represent a significant barrier to FDI.

Roger Kubarych

Dean Janow then opened up the discussion by asking the group if they believe that cases of recent U.S. intervention have been successful, and if so, why. The first response came from Dr. Hufbauer, who asserted that the success of Freddie Mac and Fannie Mae is yet to be seen. Professor Mayer agreed with Dr. Hufbauer, but went further to say that government intervention in this case should be a model of "what not to do." Professor Mayer asserted that part of the reason the housing market has not fully recovered is that Freddie Mac and Fannie Mae have acted neither in the market interest nor in their own financial interest. Mr. Kubarych expressed a slightly different view, recalling the history of Freddie Mac and Fannie Mae. He contended they did indeed misbehave, but that they did not misbehave like economists thought they would. He also argued that it was the private sector that truly got the housing market into trouble by creating collateralized mortgage obligations based on subprime mortgages.

Dr. Hufbauer pointed out that the case of General Motors was a successful example of U.S. government intervention. The government effectively prioritized stakeholders' interests while maintaining investor confidence and not deriding legal protections.

Dean Janow posed additional questions to the speaker and discussants: how do you think the rest of the world should react to U.S. intervention? Is it a violation of the subsidies code or was

government intervention absolutely necessary during such a crisis? Should states be allowed to intervene during crises, and how does this affect how we think about actions of other states?

In response, Dr. Hufbauer stated that, should other countries wish to continue as democratic, middle-class countries, they should follow the example of the United States and prevent the financial sector from complete collapse during a crisis. Complete collapse ensures fire sale conditions which are terrible for middle class families. He cited Greece as an example.

Mr. Kubarych answered the question of how other states should react by asserting that high-level policy dialogues such as the G-20 should facilitate extended dialogues on excesses, and countries should be prepared to augment their own misdeeds in intervention when their actions create negative externalities on the global economy. Mr. Kubarych maintained that this is the reason he is supportive of multilateral trade pacts such as the Trans-Pacific Partnership (TPP) and the Transatlantic Trade and Investment Partnership (TTIP); these are atmospheres where countries can achieve mutual beneficial results.

Panel II: China

Panel II, from left to right: Long Ke, Yasheng Huang, Curtis Milhaupt

Yasheng Huang, international program professor in Chinese economy and business and professor of global economics and management at MIT Sloan School of Management, gave a presentation on state intervention in China, and Long Ke, senior fellow at the Economic Research Center of Fujitsu Research Institute served as discussant. Professor Milhaupt moderated the panel.

Professor Milhaupt opened the session by remarking on the open seat on the panel: Claire Reade, assistant U.S. trade representative for China Affairs, was unable to attend due to the U.S. government shutdown.

Curtis Milhaupt

Professor Huang refuted any argument claiming equivalence between the United States bank bailout and the type of intervention China has long been engaging in with its economy. He pointed out three critical dimensions to assess differences in the way each country has handled state intervention. First is the rationale for state intervention, which has two parts: 1) response to a market failure; and 2) acting as substitute for the private sector. In the case of China, the state intervenes as a private sector substitute. The second dimension is whether or not the state intervenes with a social or an economic purpose. For example, he explained that Obamacare is designed to deal with a market failure as well as to promote a social objective. The third dimension is the institutional setting in which the interventions are deliberated – in short, whether or not the intervention is deliberated in a democratic setting will determine the level of transparency.

Professor Huang presented his summary of the three key characteristics of state capitalism: 1) intervention in the economy is performed in a one-party system; 2) the government acts as a substitute for the private sector; and 3) government intervention into private enterprise is not done for social purposes, but instead performed for economic, even political-economic, purposes. Professor Huang criticized this model, arguing that social performance is sacrificed within state capitalism.

By dissecting China's model and current status, Professor Huang challenged the assertion that China is the "new magic for economic development." He recalled the importance of maintaining a historical perspective: state capitalism spurs the economy to grow quickly, but it in turn compresses and causes a long lag in growth. Professor Huang drew on examples of Brazil in the 1960s and the Soviet Union to support his analysis.

Yasheng Huang

Professor Huang addressed the argument that became popular after the 2008 global recession that democracy is "bad" for economic growth. He stressed the importance of using relevant benchmarks when comparing economic growth. If one compares India and China, for example, then India's growth looks quite small. However, if one then compares India and Pakistan, one could conclude that GDP grows faster within a democracy than under an authoritarian regime.

Comparing democracies to one-party systems, Professor Huang stated that one-party systems either do extremely well or extremely poorly. He argued that a country's political system is a

reflection of how risk tolerant they are; one-party systems have higher economic growth potential but are much more volatile.

Professor Huang asserted that there are many challenges facing the Chinese economy today, chiefly the unbalanced nature of the country's economic growth. While state capitalism is good at encouraging GDP, it is not good at encouraging personal income. He explained that the personal income as a share of GDP started out in the early 1990s in China at about 45-47%, which was already low among countries in its income range. Currently, personal income to GDP is around 35-37%, by far the lowest among any major economies of which there is data available. In addition, labor's share of GDP has come down significantly; consumption share of GDP is destined to decline further as a result.

Professor Huang concluded by noting that very few countries have been able to graduate from the middle income trap after World War II. The countries that were able to graduate in the 1970s and 1980s had low income inequality. Therefore, China's high level of inequality will most likely prevent it from graduating. However, he noted that the current administration of Xi Jinping is more interested than previous administrations in correcting income inequality.

Mr. Ke expressed agreement with Professor Huang's analysis, asserting that due to the policies of the Hu Jintao administration, the current Xi Jinping administration faces many difficulties, such as how to approach government reform, sustain economic development, and stabilize growth. Mr. Ke agreed with Professor Huang, particularly regarding the serious problem of income inequality, with 3% of the population owning 75% of the country's assets.

Long Ke

Mr. Ke concluded by stating that China's problem is to maintain its progress in economic development. In order to succeed, the Xi Jinping administration must reform the economic system and strengthen the rule of law to realize that goal in the long term.

Professor Milhaupt stated that while both Professor Huang and Mr. Ke alluded to the propensity of the Xi Jinping administration toward reform, he finds it unlikely that the political system will be fundamentally overhauled any time soon. He asked Professor Huang and Mr. Ke what kinds of reform they believe are feasible, which specific reforms are most important in the next few years, and whether or not we can gauge the seriousness of the government to generate any sort of real reform.

Mr. Ke responded by contending that the current Chinese administration is concerned about social stability, but is also concerned about slowing economic growth, and as such, is finding it hard politically to advocate for reform. Professor Huang responded by explaining that, before 2008, Chinese private entrepreneurs were largely supportive of the government. Since then, there has been a shift in opinion, which has only been exacerbated by arrests of those who speak up against the government. By and large, members of the private sector are disappointed

with Xi Jinping's leadership, Professor Huang claimed. He concluded by stating that, while capitalism may be associated with income inequality, it is not the reason for Chinese inequality; state control is the ultimate cause.

Panel III: Japan

Panel III, from left to right: Edward Lincoln, Sota Kato, Kazuhiko Toyama, Alicia Ogawa

Kazuhiko Toyama, representative director and CEO of Industrial Growth Platform, Inc., gave a presentation on state intervention in Japan, followed by responses and further discussion with Sota Kato, professor at the International University of Japan and senior fellow at the Tokyo Foundation, and Edward Lincoln, professorial lecturer at George Washington University and adjunct professor of economics at Columbia's Department of Economics. The panel was moderated by Alicia Ogawa, senior advisor at CJEB and adjunct associate professor at SIPA.

Professor Ogawa commenced the session by framing industrial policy as either reactive or proactive. Proactive economic policy is what Japan is famous for – from managing the decline of industries that are overly mature to supporting new industries that the government foresees to be winners, both domestically and in export markets. However, this policy has resulted in the government intervening to fill voids the private sector is reluctant to fill. The private sector is thus disinclined to take any risks, illustrated by its hesitancy to supply risk capital, manage its own consolidation of excess capacity, and pay wage increases.

Mr. Toyama commenced by explaining that the majority of his remarks were based on his experience as chief operating officer of the Industrial Revitalization Corporation of Japan (IRCJ) from 2003 until 2007. The IRCJ was a government-owned fund that bought failing companies' debt and equities, restructured the firms, and then sold the companies back to the market

through a control-share auction. The IRCJ assessed more than 200 companies and intervened in 41 during its time of operation (April 2003 – March 2007).

Alicia Ogawa

Mr. Toyama classified two main challenges with his work at the IRCJ: 1) determining the criteria for intervention; and 2) being conscious of the public interest. Both challenges were complicated by political and media pressures, leading to market distortion. Mr. Toyama used the bankruptcy of Japan Air Lines (JAL) as an example to explain these challenges. Specifically, when JAL ran into trouble, the government provided so much assistance that it was unfair to JAL's competitors. Mr. Toyama argued that it was necessary for the government to step in to protect the domestic economy – allowing JAL to go under would have created a domestic shock. However, since JAL did not go through the typical control-auction and the government allowed JAL to re-list its stocks, this hampered the market power of All Nippon Airlines (ANA), JAL's main competitor; if JAL had been brought to control-auction, ANA would have had the chance to buy in.

Mr. Toyama concluded by saying that once a government chooses to intervene in private enterprise, the government itself becomes a market player and runs the risk of distorting the market through government influence. Intervention can be justified, but the government should not manipulate the competition and should be careful in implementation. In this sense, the IRCJ is viewed as a successful venture in Japan. However, Mr. Toyama argued, "the reality of intervention is that human beings don't have invisible hands."

Professor Kato generally agreed with Mr. Toyama's comments, but said they brought up a key question: can the guidelines on these public-private funds be implemented? More specifically, can market incentives prevail despite heavy Japanese government intervention? He also pointed out that there is a high level of political involvement in these funds, further restricting market forces.

Kazuhiko Toyama

Professor Kato illustrated this dynamic with an example regarding these public-private funds and their administrator, the Ministry of Economy and Industry (METI), an agency which also creates and implements industrial policy. Historically, METI was insulated from politics, even during Japan's high-growth era. It lacked the authority of the Ministry of Finance and had little influence on the banking sector. Without having financial tools, METI was only able to act as a weak

coordinator of the private sector during the high-growth era. Because of this weakness, METI often had to succumb to the market incentives of the private sector. However, METI's portfolio now includes these public-private funds that provide long-awaited financial tools for METI bureaucrats. METI is also more susceptible to political influence; recently, PM Abe convened a Cabinet meeting regarding these funds, exemplifying the politicization of industrial policy. In turn, METI's influence on the private sector is also enhanced.

Sota Kato

Given the politicization of METI and these funds, Professor Kato said he finds the political, bureaucratic, and economic motivations of all different parties involved hard to reconcile. He concluded that one of the key success factors for public-private funds is to allow market incentives to prevail. Therefore, it would be necessary to develop a long-term strategy for governing these funds, with careful designs for incentive mechanisms.

Professor Lincoln initiated his comments with a broad observation: Japan resembles neither the United States nor China with regard to state intervention in the private market. Looking back to the late 1930s and 1980s in Japan, there was a deep mistrust of markets on the part of government officials, academics, and the private sector. They did not trust the market to allocate resources in the correct direction to enable the economy to grow faster. Therefore, Japan initiated an active industrial policy including state financing through the Japan Development Bank, some state ownerships (but not to the extent of China-style SOEs), very specific tax breaks, and subsidies to the agricultural sector.

Professor Lincoln stated that, since these industrial policies of the 1980s were implemented, there has been a reversal trend: some tax breaks have been removed, Japan National Railways and Nippon Telegraph & Telephone Corporation (NTT) have been privatized, and even agricultural subsidies have been somewhat relaxed. Additionally, the Japanese market is more open to imports, which in turn creates more domestic competition, and makes it difficult to run an industrial policy "behind the closed door of protectionism."

Edward Lincoln

Professor Lincoln addressed Mr. Toyama's argument that, while there are arguments in favor of government intervention and bailouts, the government must be very careful in which circumstances to act. Building upon this, Professor Lincoln argued that perhaps the IRCJ was not being careful enough when deciding which companies to bail out; referring back to a list Mr.

Toyama provided detailing the 41 companies that the IRCJ bailed out, he said some of those businesses deserved to fail.

Professor Lincoln said he was disturbed by the addition of many more Japanese public-private funds similar to the IRCJ, calling them reminiscent of an old-fashioned industrial policy rather than crisis response mechanisms. He was concerned that PM Shinzo Abe was trending toward renewed government involvement in the economy, and questioned if this move was political in nature. Professor Lincoln expressed concern about Japanese government intervention moving forward, saying that the ultimate justification for intervention is market failure, which occurs much less in modern times than it did in previous decades such as the 1950s and 1960s. He contended that today, Japan has a harder case to make for intervention.

Professor Ogawa asked the panelists if they believed that the absence of risk and venture capital is a market failure, and why the IRCJ and the similar private-public funds have not jump-started the venture capital industry in Japan. Professor Kato explained that he considered the funds to be the transition step in the creation of a new, alternative private-led financial system that will someday include risk capital. Professor Lincoln claimed that these funds will not fix the problem of lack of risk capital, but this issue can instead be resolved by providing incentives for Japanese companies to be more accepting of foreign firms and capital, which, in turn, would change the risk environment.

<u>Roundtable</u>

Roundtable, from left to right: Gary Clyde Hufbauer, Christopher Mayer, Yasheng Huang, Long Ke, Kazuhiko Toyama, Kazumasa Kusaka, Hugh Patrick

After the three individual country panels, several speakers and discussants participated in an informal roundtable moderated by Professor Patrick. Participants included Dr. Hufbauer, Professor Mayer, Professor Huang, Mr. Ke, Mr. Toyama, and Mr. Kusaka.

Professor Patrick first asked Mr. Kusaka, as a co-host of the event, to share his observations. Mr. Kusaka stated that, as the panelists had discussed, in a market economy, state intervention into private enterprise can take various forms, from response to market failure to preservation of national security. He also explained that he remains cautious of Japan's new trend of enhanced intervention, asserting that this could lead to further government failures. With regard to the Chinese economy, he stated that it has been dynamically changing, especially under the leadership of Xi Jinping; therefore, it is increasingly important to carefully interpret the catalysts behind China's success as well as the government objectives for state intervention. Mr. Kusaka explained that this conference was an important opportunity to revisit industrial policy discussions and stated that the fundamental question is whether state interventions have been successful, and if such interventions have had a major role in the global competiveness of private enterprises.

Mr. Kusaka concluded by stating that he is optimistic; in Japan, the U.S., and China, we have common interests and should be prepared to form common guidelines on state intervention into private enterprise.

<u>Question and Answer session</u>

Professor Patrick then opened the roundtable to questions from the audience.

Q: Professor Takeo Hoshi from Stanford University had two questions, one China-related and one Japan-related. His China question addressed Mr. Ke's remark that reform in China has been talked about both during the Hu Jintao administration and now in the Xi Jinping administration. He asked the panelists whether, based on the lack of progress with reform, they believe the government is actually serious about reform.

His Japan-related question referred to Professor Ogawa's point regarding the lack of private risk capital. He wondered whether a reason why the private sector is reluctant to provide risk capital is due to the potential for government intervention. In other

From left to right: Gary Clyde Hufbauer, Christopher Mayer, Yasheng Huang, Long Ke, Kazuhiko Toyama, Kazumasa Kusaka, Hugh Patrick

words, does the government willingness to supply risk capital draw down the demand for the private sector to supply it.

A: Regarding the China-related question, Mr. Ke asserted that Japan acts in a more socialist way than China. The difference between Japan and China is transparency; in China, there is an enormous lack of transparency while Japan is very transparent. With regard to reform, strengthening transparency is politically very tough for the Xi Jinping administration. Mr. Ke said he did not know of an adequate solution to address the issue of transparency within a one-party system.

Regarding the Japan-related question, Mr. Toyama said that when the IRCJ came into being, some in the private sector were against it, while others were supportive. He contended that public-private funds can encourage private sector venture capitalists to get more involved, as these public-private funds have been very successful. However, when there is no economic crisis, the public-private funds do less work, and therefore don't provide examples of success to private sector venture capitalists. As such, he encouraged the government to come up with an adequate policy to encourage venture capitalists in times of economic stability.

Q: Professor Kay Shimizu from Columbia's Department of Political Science asked why the discussion focused mostly on domestic reforms rather on international objections to state intervention. She asked presenters if domestic concerns about income redistribution, rather than fairness within sectors internationally, were at the forefront of politicians' minds today in Japan, the United States and China.

A: Mr. Toyama responded that one of the concerns he and his colleagues had when assessing whether or not the IRCJ should intervene in companies was whether other countries – for example, Korea and the United States – would object if they saw what they perceived as an un-level playing field due to their intervention. Mr. Toyama contended that after the 2008 crisis – the Lehman shock and bailout of GM – foreign countries understood the role of state intervention in crisis response.

Dr. Hufbauer also replied to this question, referring to the attention that is paid to SOEs in the TPP and TTIP. He stated that he looks forward to seeing the final SOE Chapter in the TPP and is curious on how much compromise ("carve outs") there will be between the United States and Japan. In addition, he said he looks forward to seeing if the rules will encourage discipline of U.S. SOEs, such as the U.S. Postal Service, the Tennessee Valley Authority, and enterprises owned by individual states.

Professor Mayer brought up Basel III and its delayed implementation, and expressed doubt over how many countries will actually enforce it as written.

Long Ke

Professor Patrick said that there is a lot of rhetoric, but a lack of action regarding Chinese willingness toward reform, including the privatization of SOEs. This rhetoric-to-action ratio has historically been low, and therefore, there must be a distinction between two types of reform. The first happens when the government identifies the reform in great detail. The second is when the government remains vague by leaving the question of reform to the private and social sectors for their experimentation. Professor Patrick explained that the second type has typically produced the best results, as it requires the government to give space to others and to constrain itself ideologically and rhetorically. Right now, the Chinese government is restricting the political space, and even arresting people, including scholars.

Q: A member of the board of directors of TransEnergy Group stated that, since the Fukushima nuclear disaster, the domestic energy market has shifted, and Japan now lacks natural gas. He asked the participants whether they foresee the Japanese government intervening in this area or not.

A: Mr. Kusaka answered by affirming that the Abe government is currently in the middle of reviewing its energy policy. He asserted that the Japanese government would not intervene

directly in the choice of fuels. Mr. Toyama referenced the current political reality, stating that the equation is complicated. He does not think PM Abe is going to challenge Japan's fundamental energy policy in the short term due to the multitude of other challenges his government is facing. The timing for this kind of intervention may be right in two to four years.

Q: The next question, asked by a visiting scholar at Columbia Law School, addressed U.S. regulation on Chinese FDI, specifically referencing the Oregon wind farm and Smithfield cases. She stated that it appears as if Chinese FDI is getting greater attention in the United States compared to FDI from OECD countries. She agreed that the CFIUS review process is as transparent as it can be with the idea of national security not being properly defined by law. She asked for additional comments on state intervention of this sort.

Gary Clyde Hufbauer

A: Dr. Hufbauer responded by saying that, in the context of the Smithfield case, there were calls for introducing an "economic interest test" in U.S. law. Currently, FDI is evaluated by a "national security" test. Every transaction where an SOE buys into a domestic M&A automatically goes to review, but the ultimate test is national security. Adding an "economic interest" will ultimately depend on China's willingness to open up its investment rules and whether it seems to be playing fair with U.S. companies.

Professor Huang added that it remains important not to be influenced by media coverage. He noted that Chinese investments in developed economies are mostly M&A, while in developing countries Chinese FDI takes the form of Greenfield investments. The media typically has the perspective that M&A is bad and Greenfield is good. He drew upon the example of Honda and Toyota; when they originally expanded to the United States, they were considered Greenfield investments. He also explained that while China reviews every investment case, CFIUS only reviews about 100 per year. Chinese companies now are investing in the United States three times as much as U.S. companies are investing in China; U.S. investment has reduced substantially in the last 10 years.

Q: The final question from the audience called for comments from the participants on the impact of tax income deficit in the context of state intervention, specifically, what is the impact of state intervention from a growth perspective?

A: Dr. Hufbauer replied that Reinhart and Rogoff's "tipping point" is really more of a slide and that there is only a small tendency for a deficit to affect growth. In the case of Japan, its debt level is always stated as 200%, but in actuality, 60 percentage points are owned by the Bank of Japan and other government entities. As debt creeps up, sometimes there is a lag in growth, but it cannot always be attributed to the deficit; there is no universal percentage which a government has to reduce in order to spur economic growth.

Professor Patrick brought up the debate in Japan over whether the continued large deficits and increasing government debt ratio would lead to a crisis. He claimed that what has been impressive about Japan is that so many Japanese are willing to have their savings be invested domestically in government bonds. However, Japanese investors are taking risks on Japanese government bonds even though they may not think they are.

Curtis Milhaupt

Professor Patrick concluded the roundtable by mentioning that, when he and Mr. Kusaka had discussed the range of topics for this conference, they tried to make it as narrow as possible, knowing that it was impossible to achieve an overarching analysis of state intervention. Professor Patrick stated that the wide-ranging discussions and presentations at the conference provided an excellent start for what would surely be an ongoing discussion.

Professor Milhaupt gave closing remarks for the conference, stating that the panels and roundtable had covered a huge range of topics. He said he was struck by the different mechanisms, motivations, and constraints there are within government intervention, and how this mixture has changed over time in the three countries discussed. The United States used to be more interventionist and now is more crisis-driven. Japan shifted from old-fashioned industrial policy to a more market-confirming model, though perhaps it continues to vacillate between those two poles. China has changed its mode of intervention, and will hopefully continue to change.

From left to right: Alicia Ogawa, Kazumasa Kusaka, Hugh Patrick, Curtis Milhaupt, Merit E. Janow