Research Activities

Major Policy Research Domains

I. Maintaining Economic Dynamism under the Adverse Demographic Conditions of Low Fertility and Aging Population

II. Promoting Innovation and Strengthening International Competitiveness

III. Formulating Japan’s Strategy in Response to Globalization and Deepening Economic Interdependence in Asia

IV. Compilation of the History of Japan’s Trade and Industry Policy Primarily of the 1980s and 1990s

Adjacent Basic Research Areas

A. Institutions Related to Financial and Labor Markets, and New Corporate Law and Governance

B. Regulatory Reforms and Evaluation Frameworks for Deregulation

C. Compilation of Micro Panel Data on Firm Activities, Trade, Energy, and the Elderly; and Model Building and Operation

The Ministry of Economy, Trade and Industry (METI) has identified Major Policy Research Domains for which RIETI should continually carry out research through the second mid-term period (FY2006-2010). Furthermore, RIETI is conducting its research in the Adjacent Basic Research Areas in which RIETI can choose newly emerging relevant policy issues from a medium- to long-term perspective in a more timely and flexible manner by responding to changes in socioeconomic conditions.

Notes: The following pages list main research projects. Fellows’ titles are applicable for FY2006. Most research results shown in the following pages are downloadable from RIETI’s website. Abbreviations are on the reverse of the front cover.
Maintaining Economic Dynamism under the Adverse Demographic Conditions of Low Fertility and Aging Population

Japan is faced with a challenging task of achieving sustainable economic growth at a time of unparalleled declining fertility and aging population. In order to help policymakers meet this challenge, RIETI will undertake comprehensive and integrated research on means of promoting structural change in the economy; increasing labor force participation rates of women, the elderly, and young people; increasing productivity of both labor and capital; identifying a social security system that can secure an optimal intergenerational and intra-generational balance of benefits and contributions under the public pension system; and designing effective fiscal policy and restoring the nation's fiscal balance.

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<th>Introduction of Research Projects</th>
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| **I-1) Economic Growth under Conditions of Low Fertility and Aging Population**  
*Project Leader/Sub-Leader: Hiroshi YOSHIKAWA, FF/Kazuyuki MATSUMOTO, FF* |

**<Overview>**  
The Japanese economy has broken out of its prolonged recession and embarked upon a new phase of expansion. Looking ahead over the medium- to long-term, however, it will be characterized by the aging of society and declining population, and it will follow a new path of growth never experienced in modern times, making it necessary to have knowledge and policies that differ from those before. Given this situation, in our research we analyze the factors that have a significant impact on economic growth under conditions of low fertility and an aging population. Specifically, these include the microstructure of innovation, the impact of technological advances on capital investment, the land system and agricultural productivity, labor mobilization, and the determinants of the labor force participation rates of women. We will also undertake basic research relating to measurement derived from the aforementioned themes (including the reexamination of the operating ratio index and the services deflator). Through the aforementioned studies, the objective of our research project is to gain new knowledge and draw policy implications in order to develop a strategy for future growth.

**<Major Research Results>**

- **Discussion Papers**
  - Centralization or Decentralization of Decision Rights? Impact on IT Per formance of Firms (Takahito KANAMORI and Kazuyuki MOTOHASHI) (DP No.:06-E-021)
  - Licensing or Not Licensing?: Empirical Analysis on Strategic Use of Patent in Japanese Firms (Kazuyuki MOTOHASHI) (DP No.:06-E-021)
  - Information Technology and Economic Growth: Comparison between Japan and Korea (Takahito KANAMORI and Kazuyuki MOTOHASHI) (DP No.:07-E-009)

| **I-2) Building a New Macroeconomic Model: Focusing on the Financial System**  
*Project Leader: Keiichiro KOBAYASHI, F* |

**<Overview>**  
In order to analyze the macroeconomic policy issues facing the Japanese economy, it is essential to build a more policy-relevant macroeconomic model. The macro model currently in widespread use in academia is an approach to explain actual data from assumptions about sticky prices and habit formation in consumption. In our research we focus on addressing financial issues such as borrowing constraints on working capital financing (using land as collateral), in building a theoretical model to explain macroeconomic data. In addition, we analyze the relationship between changes in banks' equity capital and the productivity of the economy as a whole from both a theoretical and an empirical perspective. We also analyze themes derived from these themes (e.g. characteristics of medium to long-term economic fluctuations, the Ramsey tax problem in the event of hypothetical crises such as wars). The analytical method is primarily theoretical research, and whenever necessary we adopt such methods as (1) the building of theoretical models, (2) the use of data to conduct empirical research, and (3) case studies by such means as literature searches.

**<Major Research Results>**

- **Discussion Papers**
  - Bank Distress and Productivity of Borrowing Firms: Evidence from Japan (Preliminary and Incomplete) (Fumio AKIYOSHI and Keiichiro KOBAYASHI) (DP No.:07-E-014)

| **I-3) Empirical Analyses Relating to IT and Productivity**  
*Project Leader: Kazuyuki MOTOHASHI, FF* |

**<Overview>**  
Japanese companies have been investing actively in information technology (IT) since the second half of the 1990s, but it appears that the impact of this on their productivity has been limited. IT is used in a wide range of industries, and in nonmanufacturing industry in particular, it is an important complement technology for realizing business innovation. In view of this, we believe that fostering the effective use of IT will have a major impact on trends in total factor productivity at the macro level. In this research we make comparisons with the United States and certain Asian countries, making comprehensive empirical analyses from both macro and micro perspectives, including from an international standpoint, in order to address the questions of whether the use of IT by Japanese companies is being conducted effectively, what the causes are if that is not the case, and what policy methods are conceivable for promoting the effective use of IT in the future.

**<Major Research Results>**

- **Discussion Papers**
  - Licensing or Not Licensing?: Empirical Analysis on Strategic Use of Patent in Japanese Firms (Kazuyuki MOTOHASHI) (DP No.:06-E-021)
  - Centralization or Decentralization of Decision Rights? Impact on IT Performance of Firms (Takahito KANAMORI and Kazuyuki MOTOHASHI) (DP No.:06-E-032)
  - Information Technology and Economic Growth: Comparison between Japan and Korea (Takahito KANAMORI and Kazuyuki MOTOHASHI) (DP No.:07-E-009)
I-4) Economic Analysis of Countermeasures for Low Fertility
Project Leader: Yoshio HIGUCHI, FF

Overview
Declining fertility and aging of society in Japan are advancing at an unprecedentedly rapid pace in comparison with other countries, with the result that the country is clearly entering an era of labor shortages. As a measure to compensate for the shortage of labor, women’s entry into the labor force is being required to a greater extent than before. On the other hand it is believed by some that the increase in the female employment rate will cause the fertility rate to fall still further, and that the resultant population decline will impede economic growth in the long run. To counter that prospect, policies have been implemented to enable the fertility rate to rise and at the same time women to continue in employment, for example through the development of a system of child care leave. However, it is not yet safe to say that the results of these measures have been verified empirically. Accordingly, in our research we (1) analyze the factors behind the decline in the fertility rate, and study how great an impact institutional changes such as the introduction of the child care-leave and other such schemes has been having, and (2) analyze factors that impede the continuation of women’s participation in the work force, and study what kind of institutional design is required.

Major Research Results
Discussion Papers
- Empirical Analysis of Fertility Rates—Focus on its Relationship with the State of Economic Activity and Family Policy (Akihito TODA) (DP No.07-J-007)
- Impact of Regional Factors on Births and Wives’ Continuation in Employment—Panel Survey of Consumers by the Institute for Research on Household Economics (Yoshio HIGUCHI, Toshiyuki MATSUURA and Kazuma SATO) (DP No.07-J-012)

I-5) Toward a Comprehensive Resolution of Social Security Problems: A new Economics of Aging
Project Leader: Satoshi SHIMIZUTANI, FF

Overview
As Japan experiences the aging of its society at a pace unprecedented worldwide, it is essential to build a sustainable social security system that ensures that the elderly do not suffer a decline in quality of life. Our research transcends the bounds of the traditional field-specific approach that addresses the health care, long-term care, and pension fields separately, and of simulation analysis with the use of macro models, and instead adopts a “new” microscopic yet comprehensive, market-oriented approach that is premised on the diversity of the elderly. Based on pilot studies already conducted as a research project in fiscal 2005, and with the intellectual support of the analogous studies of the elderly (the U.S. HRS [Health and Retirement Study], ELSA [English Longitudinal Study of Ageing] in the UK, and SHARE [Survey of Health, Ageing and Retirement in Europe] in Continental Europe), our research has inaugurated a world-standard panel study on population aged over 50. We are gathering data that is both multi-faceted, covering such aspects as health condition, economic situation, family relationships, employment status, and social participation, and that is also capable of international comparison. Our intention in doing this is to help ensure that “evidence-based policy-making” based on an abundance of microdata becomes an established feature in the sphere of social security policy in Japan, and that Japan’s experience can be taken advantage of by other countries in their policy-making.

Major Research Results
Discussion Papers
- Analysis of the Survey Response Behavior: An Experience from a Pilot Survey of the Health and Living Status of the 50s and beyond in Japan (Hidehiko ICHIMURA, Daji KAWAGUCHI and Satoshi SHIMIZUTANI) (DP No.06-E-035) International Workshop

I-6) Study on Social Security: Development of a Simulation Model for Social Security Finance
Project Leader/Sub-Leader: Mitsuhiro FUKAO, FF/Daigo NAKATA, F

Overview
The rapid aging of the Japanese population will increase the burden of social security finance in the future, and this is a cause for concern with regard to the maintenance of Japan’s economic vitality. In order to forecast the future burden of social security finance and the future benefits, it is essential to build a simulation model for social security finance that accurately reflects Japan’s social security system. Accordingly, in our research we focus on pension finance analysis using a pension simulation model previously developed at RIETI, while also conducting analyses in other social security fields. In this way we will build a simulation model to make possible the comprehensive analysis of pension, health care, nursery care, and welfare finance, and study the desirable forms of the benefits and the burden of a social security system that is compatible with economic vitality in a society characterized by a declining fertility rate and aging population.

Other results in Domain I
Discussion Papers
- Roles of Regimes under the Gold Standard and Impact on Prices (Shumpei TAKEMORI and Liudmila SAVCHENKO)(DP No.06-J-029)
- Simulation Analysis of Debt Management Policies to Ensure the Sustainability of Japan’s Public Debt (Takeru DOI)(DP No.06-J-032)
- Analysis of the Impact of Pension System Reforms on the Labor Supply Behavior of Elderly Males (Yoshio HIGUCHI, Masako KUROSAWA, Kayoko ISHII and Toshiyuki MATSUURA)(DP No.06-J-033)
- Impact of Family Care Needs on Elderly Workers’ Decisions on Retirement (Yoshio HIGUCHI, Masako KUROSAWA, Tadashi SAKAI, Kazuma SATO and Emiko TAKEISHI)(DP No.06-J-036)
- Marital Satisfaction and Work-Life Balance: A Viewpoint Indispensable to Mitigating Fertility Decline (Kazuo YAMAGUCHI)(DP No.06-J-054)
- Aging Japan and the National Burden Rate (Akira OKAMOTO)(DP No.06-J-056)
- The Optimal Method for the Social Security System (Toshiaki TACHIBANAKI, Akira OKAMOTO, Masumi KAWADE, Toshiya HATANO, Naomi MIYAZATO, Yoshihiko SHIMA and Akifumi ISHIHARA)(DP No.06-J-057)
- Opinion Survey and Econometric Analysis of the Benefit of Public Spending and the National Burden (Toshiaki TACHIBANAKI, Akira OKAMOTO, Masumi KAWADE, Toshiya HATANO and Naomi MIYAZATO)(DP No.06-J-058)
- An Optimal Rate of the National Burden in an Aging Japan (Akira OKAMOTO) (DP No.06-E-036)
Promoting Innovation and Strengthening International Competitiveness

Continuous innovation is vital for strengthening the international competitiveness of Japanese companies. However, the effects of innovation and the policies that promote it are extremely difficult to quantify. In undertaking research in this field, it is vital to have an analytical framework, both theoretical and empirical, that clarifies the correlations between innovation at the corporate and industry levels and total factor productivity (TFP). RIETI will evaluate and analyze conditions surrounding Japanese industry and specific industrial and technological policies to provide findings that the government can utilize to promote innovation policies.

Introduction of Research Projects

II-1) The Structural Characteristics of Research and Development by Japanese Companies, and Issues for the Future
Project Leader: Sadao NAGAOKA, FF

<Overview>
Effective research and development (R&D) by Japanese companies is of the greatest importance to the future growth of the Japanese economy. However, social science knowledge with respect to the fundamental factors of research such as the source of knowledge, external collaboration, spillover, financial constraints, barriers for the commercialization of research results, and the motivation of inventors is extremely limited. In our research we conduct a comprehensive survey of Japanese inventors, for the purpose of collecting information on these matters systematically at the level of research projects being implemented within companies. This is the first survey of its kind to be conducted in Japan. By means of statistical analysis of a combination of the information gathered from the survey and existing statistics, we will elucidate the structural characteristics of Japanese companies’ R&D, and will analyze the determinants of R&D performance and future policy issues. In addition, we will make preparations with a view to conducting international comparative analysis from the next fiscal year onwards, including exchanging views with academics in Europe and the United States with regard to the questionnaires and research methods.

II-2) Productivity of Companies and Industries, and Japan's Economic Growth
Project Leader: Kyoji FUKAO, FF

<Overview>
In the Japan of the future in which the working population is declining, raising productivity will be the principal source of economic growth. In addition, total factor productivity (TFP) determines the rates of return of physical and human capital, and it is also an important determinant of capital and educational investment. In our research we will be able to analyze the latest productivity trends in the Japanese economy by updating the Japan Industrial Productivity (JIP) database annually. In fiscal 2006 we aim to cover the years from 1970-2004. In addition, by integrating microdata covering all economic activity in Japan with macro industry-level data we will analyze increases in TFP and labor productivity at macro industry level from the perspectives of increases in productivity within individual firms and factories, the reallocation of resources among firms and factories, and entry/exit behavior. At present, the work of creating productivity databases at the two-digit level (for the entire macroeconomy; 72 sectors) is being conducted through the KLEMS project led by the University of Groningen with regard to the core EU countries and the United States, and at Seoul National University with regard to South Korea. The JIP database is participating in the EU KLEMS project on behalf of Japan. By collaborating with these organizations and Dale W. Jorgenson (Samuel W. Morris University Professor, Department of Economics, Harvard University), we will make detailed international productivity comparisons at the industry level. In addition, in collaboration with various bureaux and divisions at METI, research will be conducted into such matters as the impact of internationalization on firm productivity (Policy Planning and Research Office, Trade Policy Bureau), estimation of stocks of intangible assets at the macro and industry level (Technology Promotion Division), and productivity in service industries.

<Major Research Results>

Discussion Papers

- Productivity and Financing of Start-ups (Tsutomu MIYAGAWA and Atsushi KAWAKAMI)(DP No.:06-J-027)
- The Quantitative Assessment of Organization Capital (Tsutomu MIYAGAWA and Young Gak KIM)(DP No.:06-J-048)
- The Shadow of Death: Pre-exit Performance of Firms in Japan (Kozo KIYOTA and Miho TAKIZAWA)(DP No.:06-E-033)
- Determinants of the Profitability of Japanese Manufacturing Affiliates in China and Other Regions: Does Localization of Procurement, Sales and Management Matter? (Keiko ITO and Kyoji FUKAO)(DP No.:07-E-001)
- Estimation Procedures and TFP Analysis of the JIP Database 2006 Provisional Version (Kyoji FUKAO, Sumio HAMAGATA, Tomohiko INUI, Keiko ITO, Hyeoq Ug KWON, Tatsuji MAKINO, Tsutomu MIYAGAWA, Yasuo NAKANISHI and Joji TOKUI)(DP No.:07-E-003)
- Does Off shoring Pay? Firm-Level Evidence from Japan (Alexander HIJZEN, Tomohiko INUI and Yasuyuki TODO)(DP No.:07-E-005)
- The Effects of Multinational Production on Domestic Performance: Evidence from Japanese Firms (Alexander HIJZEN, Tomohiko INUI and Yasuyuki TODO)(DP No.:07-E-006)
- Overseas R&D Activities and Home Productivity Growth: Evidence from Japanese Firm-Level Data (Yasuyuki TODO and Satoshi SHIMIZUTANI)(DP No.:07-E-008)
- What Determines Overseas R&D Activities? The Case of Japanese Multinational Firms (Satoshi SHIMIZUTANI and Yasuyuki TODO)(DP No.:07-E-010)

International Workshop

"A Comparison of the Productivity of Japanese, Chinese, Korean and European Firms"* (Mar 2, 2007)
RIETI Policy Symposium
"Determinants of Total Factor Productivity and Japan's Potential Growth: An International Perspective"* (Jul 25, 2006)
II-3) Regional Innovation and Corporate Management in East Asia
Project Leader/Sub-Leader: Kazuhiro ASAKAWA, FF/ Susumu SANBONMATSU, CF

<Overview>
In recent years importance has been placed on metanational management in which companies do not rely entirely on home country advantage but acquire and leverage management resources worldwide, building competitive advantage on a global scale. However, at present, the mainstream approach is, as in the past, one of global innovation in which large corporations in industrialized countries play the pivotal role. In view of this, the recent trends in the LCD industry in East Asia are worth noting. The process of industry creation based on innovation chains in the East Asian region, centered on Japan, South Korea, and Taiwan, can no longer work in conjunction with the supremacy of industrial countries or ethnocentrism. In our research we study new trends in this global innovation, focusing on (1) the LCD industry in East Asia and (2) the development of SMEs in East Asia, with the intention of analyzing the new evolution of global and regional innovation and of drawing implications for Japanese corporate management and industrial policy.

<Major Research Results>
Discussion Papers
➢ Issues for Japanese Firms from Metanational Management Perspective (Kazuhiro ASAKAWA) (DP No.:06-J-030)
➢ Innovation and East Asian and Global Management of Start-ups and SMEs (Susumu SANBONMATSU) (DP No.:06-J-061)
RIETI Policy Symposium
"Metanational Management and Global Innovation: The Case of the TFT-LCD Industry" (Mar 14, 2007)

II-4) An Integrated Approach to the Raising of Productivity at the Macro, Industry, and Company Levels
Project Leader: Yoshihiko NISHIYAMA, FF

<Overview>
Referred to by terms such as the “lost decade,” the 1990s are regarded as a period of declining productivity. However, it is not clear what really caused the decline in productivity at the macro level. A number of causes are conceivable, such as declines in the productivity at individual firms, the entry of firms with low productivity, and the exit of firms with high productivity, but finding the actual causes requires an empirical approach. That requires examination with a combination of an appropriate economic model and appropriate statistical methods, but among existing studies there is nothing suitable that can be applied directly in this regard. From the standpoint of sustainable growth that should be sought in the future, an important issue to address is that of gaining a unified understanding of changes in the substructure at the company and industry level, together with changes at the macro level. In our research we adopt a comprehensive approach to this issue from both theoretical and empirical perspectives.

II-5) Research into Joint Inventions by Universities and Public Research Institutions and Private-sector Companies
Project Leader: Schumpeter TAMADA, FF

<Overview>
If companies are unable to obtain from within their own organizations the scientific or technical knowledge necessary for the development of new products, the alternative is to collaborate with universities or public research institutions. However, collaboration with other organizations incurs costs for searches and contracts. The objective of our research is a survey of joint inventions by researchers at public research institutions and private-sector firms, and through this to elucidate the roles fulfilled by the universities, other independent administrative organizations and other public research institutions, and to identify the implications for policies to further strengthen Japan’s innovation system.

<Major Research Results>
Discussion Papers
➢ Importance of Regional Innovation Systems (Schumpeter TAMADA) (DP No.:07-J-002)
### II-6) Value Acquisition through Innovation: Japanese Companies' Competitiveness in Information Devices and Digital Home Electronic Products, and Value-added Creation

**Project Leader:** Kentaro NOBEOKA, FF

**<Overview>**
The most important issue for the Japanese economy is the creation of value-added by means of innovation. Research until now has been based on the hypothesis that if technical innovation can be achieved and used as the basis for developing products that meet market and customer needs, that will lead to greater international competitiveness and productivity. However, international competition has grown more complex in recent years, and in a rapidly increasing number of cases Japanese companies have been succeeding with technical innovation and developing excellent products as a result, but this has not led to value-added creation. In terms of technology management theory, this means that even if value creation is achieved, it is not possible to achieve value acquisition. This is particularly striking in the sphere of information devices and digital home electronic products that use semiconductors, digital technologies, and communications technologies. Many aspects of this failure to achieve value acquisition that Japanese companies are facing cannot be explained within the existing theoretical framework relating to innovation systems. Our research is being conducted for the purpose of clarifying, both theoretically and empirically, the desirable form of value acquisition, and of making recommendations that will enhance the international competitiveness of Japanese companies.

**<Major Research Results>**

- Discussion Papers
  - "Increasing Complexity of Artifacts and the Role of Product Architecture" (Masahiro OKUNO, Hirokazu TAKIZAWA and Yasunori WATANABE) (DP No.:06-J-038)

### II-7) Research into Japanese Companies' Architecture and Design Processes

**Project Leader:** Takahiro FUJIMOTO, FF

**<Overview>**
In the debate in economics about trade and industrial competitiveness, and in research into comparative advantage in particular, the tacit premise has been that within the entire process of producing goods, the importance of the physical production process, or, in other words, the efficient use of resources in that process, constitutes the foundation of a country's trade structure and industrial structure. However, in numerous tradable-goods industries, among which it is the rule rather than the exception today to be characterized by increasing returns to scale and product differentiation, the inference to be drawn is that rather than the efficient use of resources in the manufacturing process it is the efficient use of resources in the preceding process, namely the design process, that is regarded as important for analyzing any particular country's continuing industrial structure. Premised on the above, in our research we re-examine Japan's trade structure and industrial structure on the basis of industry theory based on a design theory in which the manufacture of goods (manmade goods) is considered from the viewpoint of creating design information, and "manufacturing" is taken as being the optimization of the flow of this to the market. Specifically, we will attempt to devise a framework for estimating industrial competitiveness from the compatibility of organizational capability (which, for historical reasons, is unevenly distributed in Japan) and the architecture of the relevant products.

**<Major Research Results>**

- Discussion Papers
  - "Increasing Complexity of Artifacts and the Role of Product Architecture" (Masahiro OKUNO, Hirokazu TAKIZAWA and Yasunori WATANABE) (DP No.:06-J-038)

### II-8) Research and Analysis Concerning the Innovation Process in Japan's Semiconductor Industry

**Project Leader:** Hiroyuki CHUMA, FF

**<Overview>**
To create an effective innovation process in science-based industries we believe that a prerequisite is to mobilize a broader range of wisdom and knowledge of diverse experts both from within and outside each relevant company. Unfortunately, however, in Japan such mobilization of wisdom and knowledge can hardly be said to be sufficiently broad in scope to be effective. In view of this, even in fields in which there have been large numbers of creative discoveries, inventions, and improvements there is no shortage of cases in which it has been difficult to use these in a way that enhances the competitiveness of the relevant science-based industries. The purpose of our research is to re-examine, based on this awareness of current realities, the characteristics of the innovation process in the semiconductor (devices, equipment, materials) industry, one of Japan's foremost science-based industries, in particular its strengths and its weaknesses, and to seek remedies.

**<Major Research Results>**

- Discussion Papers
  - "Exploring Factors Behind the Weakening Competitiveness of Japan's Semiconductor Production System: From the Viewpoint of Meta-Level Integration Capability" (Hiroyuki CHUMA) (DP No.:06-J-043)

### II-9) Empirical Research into Software Innovation

**Project Leader/Sub-Leader:** Tatsuo TANAKA, FF/Jun SUZUKI, FF

**<Overview>**
Japan's competitiveness in the software industry is perceived as being weak. In the software industry as a whole there is an overwhelming import surplus, while exports are less than 10% of the value of imports. Among high-value-added high-tech industries it is rare to find any in which Japanese competitiveness is so overwhelmingly lacking. Additionally, this fact may have a negative impact on innovation in business processes that use information technology (IT). Why is this? Why has such a disparity in competitiveness arisen? Is it possible to devise policy remedies that will enhance competitiveness? The objectives of our research are to empirically study various hypotheses that may answer these questions, and in so doing to identify the current state of software innovation in Japan, and to seek policies to enhance the competitiveness of software industries and promote business innovation through the use of software.
II-10) The Desirable Form of Future Pro-Patent Policy
Project Leader: Yutaka KIYOKAWA, SF

<Overview>
The promotion of innovation is indispensable to the survival of the Japanese economy. There is a system of intellectual property rights to support that, and pro-patent policies will enhance this. A milestone in the shift toward pro-patent policies was the establishment of the Strategy Headquarters to promote them under the Koizumi administration, but in fact its history stretches back to the mid-1990s. At that time, it was given to the spread of technologies and there was a lack of protection, as it was argued that such policies would not sit well with the promotion of innovation. In the research conducted last year, factors such as the changes to the system implemented up to that time were assessed, and it was concluded that Japan's pro-patent level had improved considerably. In the United States, which is Japan's model for pro-patent policies, such policies have been revised because protection had gone too far, and in view of the increasing complexity and sophistication of R&D, there are calls for it to be undertaken on a collaborative basis. Against this backdrop we will study desirable forms of a system of intellectual property rights of a kind that stimulates innovation. Specifically, while listening to the opinions of companies directly affected by this question, we will study issues such as the revision of the protection system (exclusivity) and the desirable form of management and business strategies of a kind that put intellectual property to good use.

<Major Research Results>
Discussion Papers
- Developments in and an Evaluation of Intellectual Property Rights in Japan (Evaluation of the pro-patent trend since the latter part of the 1990s, in particular the patent system) (Yutaka KIYOKAWA) (DP No.:06-J-060)

II-11) Study on Industrial Clusters (joint research with Kyoto University)
Project Leader: Toshihiro KODAMA, Professor, Institute of Economic Research, Kyoto University

<Overview>
For Japan's economic growth strategy the formation of industrial clusters is becoming increasingly important, both for enhancing innovation capabilities and for invigorating regional economies. In our research we will use prior research findings concerning the TAMA (Technology Advanced Metropolitan Area) project in the western part of the Tokyo metropolitan area, which is regarded as a model case in METI's Industrial Cluster Program, and will engage in activities such as research in the Kyoto region, where there is an industrial agglomeration of high-tech firms and leading universities, with the objective of putting forward suggestions concerning the desirable manner in which industrial clusters are formed. Specifically, by means of a questionnaire survey of manufacturing firms in the Keiji district, which stretches from Kyoto and its suburbs into the southern part of Shiga Prefecture, we will identify SMEs that excel in product development, and study the possibilities for the development of linkages between large enterprises and these product-developing SMEs. Based on this we will study measures and policy issues concerning the development of industrial clusters as effective regional innovation systems, including the implications for the country as a whole.

<Major Research Results>
Discussion Papers
- Product-Developing SMEs and State of Formation of an Industrial Cluster in the Keiji (Kyoto-Shiga) Area (Toshihiro KODAMA, Takashi SAIJO and Shinya KAWAMOTO) (DP No.:07-J-009)

Other research results in Domain II

Discussion Papers
- Integrating Modular Products beyond Industrial Boundary—Analysis of the Integration Process of a PC System and NC System (Tomoatsu SHIBATA and Fumio KODAMA)(DP No.: 06-J-040)
- Start-up Financing and Human Capital of Entrepreneurs (Yuji HONJO)(DP No.: 06-J-047)
- The Impact of Regional Factors on the Business Startup Ratio in the Japanese Manufacturing Sector: A Comparative Analysis of High-Tech and Low-Tech Industries (Hiroyuki OKAMURO)(DP No.: 06-J-049)
- Regional Knowledge Networks of Corporations, Universities and Public Institutions (Ichiro SAKATA, Yuya KAJIKAWA, Yoshiyuki TAKEDA, Naoki SHIBATA, Masahiro HASHIMOTO and Katsumori MATSUMI)(DP No.: 06-J-055)
Formulating Japan's Strategy in Response to Globalization and Deepening Economic Interdependence in Asia

As the world economy becomes increasingly globalized, and particularly as Asian countries rapidly grow more economically integrated, Japan needs to establish a comprehensive strategy for implementing policies that respond to international trade rules—such as those under the WTO and FTAs—and facilitate trade and investment. RIETI will contribute to the formulation of Japan’s strategy for trade and other policies by conducting analysis on the value chain of trade, direct investment, and technological development in Asia, as well as on the transformation of Asia’s monetary and foreign exchange systems, thereby presenting policy proposals for Asia and the world. RIETI will investigate and sort out cases of actual implementation of trade rules, analyze the economic conditions and trade strategies of Japan’s major economic partners, and conduct research on business environments and other factors that influence the successful operation of Japanese companies in the global arena.

III-1) Research on Changes in Multinational Corporations, Trade Structures, and Market Institutions

Project Leader/Sub-Leader: Ryuhei WAKASUGI, FF/ Eiichi TOMIURA, FF & Hiroshi OHASHI, FF

<Overview>
The globalization is bringing great changes to the international economic environment for Japan. We will review the current state of globalization in Japan from three perspectives: (1) market institutions, (2) international trade structures, and (3) trade policy. (1) Market conditions are major determinants of international trade, foreign direct investment, and technology transfers, but their quantitative analysis is inadequately developed. In our research we will study the importance of market conditions by developing indicators, and analyze the impact on trade, investment, and research and development (R&D). One topic includes the impact of cross-country differences in the intellectual property rights (IPR) protection on technology transfers. (2) Amid the globalization, the Japanese international division of labor is becoming more complex. By analyzing the split of manufacturing processes by Japanese firms and relating it with the firms' R&D and scale, we will cast light on the state of outsourcing, in particular the outsourcing of production. (3) The advance of economic globalization is making it increasingly important to seriously consider the costs and benefits of safeguard measures in trade policy. We take up the United States' experience as a case study, and re-examine the importance of these policies.

<Major Research Results>
Discussion Papers
➢ Factors Determining the Mode of Overseas R&D by Multinationals: Empirical Evidence (Banri ITO and Ryuhei WAKASUGI) (DP No.:07-E-004)
International Workshop
"Empirical Studies of Trade, FDI and Firms in East Asia" (Mar 16-17, 2007)

III-2) The Foreign Aid Governance

Project Leader/Sub-Leader: Yasuyuki SAWADA, FF/ Hidemi KIMURA, F

<Overview>
The core of the debate about foreign aid is reaching a major turning point characterized by shifts from projects to budget support, from financing to an emphasis on debt forgiveness and grants, and from bilateral to multilateral. However, the policy tools for achieving the Millennium Development Goals (MDGs: the international aid community’s fundamental development goals) are not particularly clear, and the debate continues as to the relative efficacy of direct poverty reduction and growth-mediated strategies. In addition, whereas the debate about the quantity of aid is unfolding, there has been no deepening of the debate about the quality of aid. In light of these various stances, the objective of this research is to elucidate systematically the foreign aid governance* based on the evidence. Specifically, based on this approach our research will include quantitative analysis using the "trinity model," which links foreign direct investment (FDI), trade, and aid, in regard to disparities in the impact of foreign aid in Asia and Africa, and the causes thereof.
* "The foreign aid governance " here refers to the governance structure of development assistance (foreign aid) in the form of public international funds flows, comprising the structure of decision-making by donors, the structure of decision-making by aid recipient countries, and the modality of aid.

<Major Research Results>
Discussion Papers
➢ Is Foreign Aid a Vanguard of FDI? A Gravity-Equation Approach (Hidemi KIMURA and Yasuyuki TODO) (DP No.: 07-J-003/07-E-007)
III-3) Legal Approach to Regional Economic Integration
Project Leader: Tsuyoshi KAWASE, FF

<Overview>
Amid the burgeoning of regional economic integration (FTAs, EPAs, customs unions) since the second half of the 1990s, there are some aspects that require scrutiny. This phenomenon has been arousing intense interest in many fields of the social sciences, but generally the analysis of its legal aspects has lagged behind. Similarly to the WTO, regional economic integration is conducted with large amounts of legal documentation, and this constitutes a trade "agreement" pursuant to GATT Article 24. Accordingly, legal analysis must be a core policy tool with regard to the design of the systems and to their operation after they have come into being. On this basis, in our research we make issue-specific comparative studies of the systems in the major cases of regional economic integration that have been in force up till now, and elucidate the classification of the designs of legal systems in regional economic integration, and their special characteristics. In this way we will show what options are possible for orderly integration from a legal perspective, and how these can aid the effectiveness of economic integration.

<Major Research Results>
Discussion Papers
- Treatment of Technical Standards in Regional Trade Agreements—Some Lessons for Mutual Recognition Arrangements (Yoshiko NAIKI) (DP No.: 06-J-042)
- Competition Policy and Law in Regional Economic Integration (Shingo SERYO) (DP No.: 06-J-052)
- Disciplines on the Application of Antidumping Measures in Regional Economic Integration: A Quest of Prerequisites for Introducing Disciplines through Horizontal Comparison (Fujio KAWASHIMA) (DP No.: 06-J-053)
- Liberalization of Movement of Natural Persons in Regional Trade Agreements: A Convenient Framework of International Cooperation for Managing Cross-Border Labor Mobility (Yoshizumi TOJO) (DP No.: 07-J-008)

III-4) The Resolution of Global Imbalances
Project Leader: Willem THORBECKE, SF

<Overview>
Our work this year involved seeking a deeper understanding of the characteristics of international production networks in Asia and of the effects of exchange rate changes on processing trade. In the paper with Dr. Masaru YOSHITOMI we presented a detailed analysis of Trade-FDI-Technology Linkages in East Asia. In the paper with Mizanur RAHMAN we investigated the effects of unilateral RMB appreciations and joint appreciations among countries supplying intermediate inputs on China’s processed exports. In both cases we also tried to draw relevant policy conclusions from our results.

<Major Research Results>
Discussion Papers
- How Would China’s Exports be Affected by a Unilateral Appreciation of the RMB and a Joint Appreciation of Countries Supplying Intermediate Imports? (Mizanur RAHMAN and Willem THORBECKE) (DP No.: 07-E-012)

III-5) Financial Cooperation in East Asia and the Optimal Currency Basket
Project Leader/Sub-Leader: Takatoshi ITO, FF/ Eiji OGAWA, FF

<Overview>
The U.S. current account deficit widened from 2004 through 2005, reaching as high as 7% of the GDP, while China’s current account surplus expanded, exceeding 5% of the GDP. If we combine China’s figures with those of Japan, South Korea, and the ASEAN countries it can be seen that East Asia is recording a very large trade surplus with the U.S. If the U.S. dollar were to fall during the course of resolving this imbalance, in the absence of a cooperative relationship in the currency system in East Asia a number of countries could have an excessive appreciation burden imposed upon them, or to avoid that would have to spend massively on market intervention. However, if East Asian countries could cooperate to build a joint float mechanism (e.g. a common currency basket), then any shocks felt by East Asia in the course of resolving global imbalances could be mitigated. This research considers a common currency basket to be a desirable long-term option, and our objective is to conduct research linked directly with policy, studying the management of monetary and exchange-rate policies up to the transition to a basket, and seeking the desirable configuration of a basket system.

<Major Research Results>
Discussion Papers
- Analysis of China’s Exchange Rate Reform (Takatoshi ITO) (DP No.: 06-J-028)
- Exchange Rate Changes and Inflation in Post-Crisis Asian Economies: VAR Analysis of the Exchange Rate Pass-Through (Takatoshi ITO and Kiyotaka SATO) (DP No.: 06-E-018)
- The Chinese Yuan after the Chinese Exchange Rate System Reform (Eiji OGAWA and Michiru SAKANE) (DP No.: 06-E-019)
- On Determinants of the Yen Weight in the Implicit Basket System in East Asia (Takatoshi ITO and Keisuke ORII) (DP No.: 06-E-020)
- Chinese Exchange Rate Regimes and the Optimal Basket Weights for the Rest of East Asia (Etsuro SHIOJI) (DP No.: 06-E-024)
- Adopting a Common Currency Basket Arrangement into the ’ASEAN Plus Three’ (Eiji OGAWA and Kentaro KAWASAKI) (DP No.: 06-E-028)
- Progress toward a Common Currency Basket System in East Asia (Eiji OGAWA and Junko SHIMIZU) (DP No.: 07-E-002)

#International Workshop
"Regional Monetary Coordination and Regional Monetary Unit" (Dec 23, 2006)
"RETI-TIER Workshop"
"Strengthening Asian Economic and Financial Integrations" (Dec 8, 2006)
III-6) FTA Study
Project Leader: Shujiro URATA, FF

<Overview>
Free trade agreements (FTAs) have assumed a dominant status within the global trading system, and the number of them involving East Asia and Japan is increasing. Given this situation, our research examines major FTAs worldwide and in East Asia including Japan, evaluating the content of the FTAs and analyzing their impact. The results of these analyses will provide valuable information for constructing desirable FTAs. The results of the analyses and evaluations will identify the aspects of the FTAs to be improved. In addition, the impact analysis will provide valuable information for the formulation of FTA strategies.

<Major Research Results>
Discussion Papers
- An Analysis of the Potential Economic Effects of Bilateral, Regional, and Multilateral Free Trade (Kozo KIYOTA) (DP No.: 06-E-027)
- Services in Free Trade Agreements (Ryo OCHIAI, Philippa DEE, and Christopher FINDLAY) (DP No.: 07-E-015)
- Market Access in FTAs: Assessment Based on Rules of Origin and Agricultural Trade Liberalization (Inkyo CHEONG and Jungran CHO) (DP No.: 07-E-016)
- An Analysis of the Restrictions on Foreign Direct Investment in Free Trade Agreements (Shujiro URATA and John SASUYA) (DP No.: 07-E-018)

International Workshop
"FTA Study Project" (Nov 10, 2006)
RIETI Policy Symposium
"Assessing Quality and Impacts of Major Free Trade Agreements" (Mar 22-23, 2007)

III-7) The Rise of China and the Transformation of the East Asian Regional Order
Project Leader: Takashi SHIRAISHI, FF

<Overview>
The emergence of China as an economic powerhouse has been transforming the regional order in East Asia, particularly in the areas of economy, politics, and security. The project will address the question of how to manage these transformations. Project members will examine Japan's and other countries' engagement with China from the so-called "realist" (which emphasizes balance of power politics) and "liberal" (which emphasizes economic interdependence and institution-building) perspectives. The project will underline the importance of balancing and regional cooperation for managing the regional transformations.

III-8) The Desirable Form of Legal Protection for Overseas Investments
Project Leader/Sub-Leader: Akira KOTERA, FF/ Kayo MATSUMOTO, F

<Overview>
Foreign investments are exposed to considerable risk, depending on factors such as the conditions in the recipient countries. Among these risks, those (political and social risks) that may cause business failure as a direct result of acts by the recipient country need to be addressed through a public framework, and in recent years investment agreements have been attracting attention as such frameworks. Of particular note is that the procedure for resolving disputes between investors and states (investment agreements arbitration) provided in investment agreements functions as real investor protection. In our research we will analyze the legal principles of arbitration awards and will study desirable forms of legal protection for overseas investment. The analysis of legal principles will have considerable implications for the drafting of the investment-related provisions in future investment agreements or economic partnership agreements that Japan concludes in the future. At the same time, it will serve as a reference for company management when choosing investment targets or investment methods. In addition, this will influence the design of investment insurance schemes offering similar functions.

<Major Research Results>
Discussion Papers
- Transparency and International Investment Treaties—Definition and Responses (Akira KOTERA) (DP No.: 06-J-026)
- Possibility of Inefficient Breaches under WTO Dispute Settlement Procedures: Analysis from the Viewpoint of Law and Economics (Takashi SHIMIZU) (DP No.: 07-J-001)
- On the Comparison of Safeguard Mechanisms of Free Trade Agreements (Akira KOTERA and Tomofumi KITAMURA) (DP No.: 07-E-017)
III-9) The Environment, Trade, and the WTO; Food, Agriculture, and WTO Laws  
Project Leader: Naoto JINJI, FF

**Overview**
With the progress of globalization, issues such as trade and the environment, and food, agriculture and the WTO have become major points of contention. We take a comprehensive and interdisciplinary approach to these issues from the standpoint of both economics and jurisprudence. In particular, our research project focuses primarily on (1) the effects of environmental policies in an open economy, (2) sustainable forest management policies, including illegal deforestation issues and related countermeasures, (3) the impact of trade liberalization on the environmental, and (4) legal analysis of consistency between multilateral environmental agreements (MEAs) and the GATT/WTO. Both theoretical and empirical studies are conducted, and case-study and historical research are also incorporated.

**Major Research Results**
Discussion Papers
- Illegal Extractions of Renewable Resources and International Trade with Costly Enforcement of Property Rights (Naoto JINJI) (DP No.: 07-E-011)

III-10) Empirical Analysis of Change in the Comparative Advantage Structure in Trade in East Asia under the Modularization of Product Architecture  
Project Leader: Satoshi KUWAHARA, SF

**Overview**
The phenomenon in which previously individual production processes are split up and dispersed geographically through the progress of modularization is, if seen from the supply side, the consequence of dealing with differences in inputs of factors of production or differences in production technologies in each process. In the East Asian region at present, industrial clusters have highly fragmented production processes, straddle national borders, and are spread among dispersed locations, resulting in considerable change in the structure of comparative advantage. Premised on this, our research will use relevant data to study the impact the progress of modularization is having on the trade structure of the East Asian region.

**Major Research Results**
Discussion Papers
- Empirical Analysis of the Trading Structure Changes in East Asia under the Modularization of Product Architecture (Satoshi KUWAHARA) (DP No.: 06-J-050)

III-11) Study on International Strategies for Improving Productivity in the Context of Economic Globalization  
Project Leader: Shigeaki SHIRAISHI, SF

**Overview**
Amid the advance of economic globalization, Japan and other industrialized countries are facing the issue of how to enhance productivity. With the intention of making effective policy proposals concerning this issue, by understanding and identifying companies' international business activities in the form of the cyclical model "resource and risk as a company's strategic base," and "redefinition and relocation as companies' strategic actions," (the "2R-2R" model, which cyclically amalgamates positioning theory and resource base theory relating to corporate strategy), we will extract the real facts and issues of economic globalization at the micro level, namely the company level. At the same time, from the perspective of enhancing productivity in the context of globalization, we will also study the relationship between the government (policies) and companies (business activities). This study will be conducted as a joint project with the Organisation for Economic Co-operation and Development (OECD).

**Other research results in Domain III**
Discussion Papers
- Changing Roles of Economic Technocrats in the “Small Country” Malaysia (Takashi TORII)(DP No.: 06-J-031)
Compilation of the History of Japan's Trade and Industry Policy Primarily of the 1980s and 1990s

Knowldege of the history of trade and industry policy provides the foundation for formulating future economic and industrial policy. RIETI is undertaking comprehensive, systematic research to compile Japan's history of trade and industry policy, seeking cooperation from external experts including economists and historians.

<Overview>
In 1984, the Ministry of International Trade and Industry (the former METI) began compiling a history of trade and industry policy spanning the period from the end of World War II through the second oil shock. By 1994, the work had culminated in the publication of a 17-volume history. More than 20 years have elapsed since the period covered in the previous work and calls have grown for an analytical review and evaluation of more recently implemented trade and industry policy. This new research project will compile the history of trade and industry policy in the late 20th century, with a particular focus on the period from 1980 to 2000, incorporating not only objective facts but also such areas as analytical and evaluative observations concerning the policy-making and implementation processes, effects on industrial and economic conditions that necessitated the formulation of certain policy, realization of intended policy goals, and industrial and economic conditions following policy implementation.

This history of trade and industry policy will consist of 12 volumes. Volume 1 will present a general overview with chapters dedicated to specific time periods, while the remaining 11 volumes (arranged similarly to the ministry's organizational structure) will provide detailed accounts of different policy fields with chapters organized by policy theme. The compilation is slated for completion by March 2011.

<Project Leadership and Staff>
The project will be carried out under the leadership of the Committee on the History of Japan’s Trade and Industry Policy (HJTIP Committee) set up within RIETI.

HJTIP Committee Organization
Chairman: Editor in Chief
Committee Members: Deputy Chief Editors; Coordinating Lead Authors; Representative from METI

List of HJTIP Committee Members
Editor in Chief
Konosuke ODAKA (Professor Emeritus, Hitotsubashi Univ./Professor Emeritus, Hosei Univ.)

Deputy Chief Editors
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Vol. 3 Industrial Policy
Tetsuji OKAZAKI (Professor, Graduate School of Economics, Univ. of Tokyo)
Vol. 4 Distribution Policy/Consumer Administration
Takemasa ISHIHARA (Professor, School of Business Administration, Kwansei Gakuin Univ.)
Vol. 5 Environment, Location, and Safety Policy
Haruhito TAKEDA (Professor, Graduate School of Economics, Univ. of Tokyo)
Vol. 6 Basic Industries
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Vol. 7 Machinery and Information Industries
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Vol. 8 Consumer Goods Industries
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Vol. 9 Industrial Science and Technology Policy
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Vol. 10 Natural Resources and Energy Policy
Takeo KIKAWA (Professor, Graduate School of Commerce and Management, Hitotsubashi Univ.)
Vol. 11 Intellectual Property Policy
Nobuhiro NAKAYAMA (Professor, Graduate School for Law and Politics, Univ. of Tokyo)
Vol. 12 Small- and Medium-sized Enterprise Policy
Tetsuo NAKATA (Professor, Graduate School of Business, Doshisha Univ.)

<Major Activities in Fiscal 2006>
- Preparatory meetings for the compilation of the history of Japan's trade and industry policy (prior to the establishment of the HJTIP Committee) and meetings of the HJTIP Committee.
- Manifesto (overall outline) drawn up by Editor in Chief.
- Formulation of basic guidelines for the compilation of the history of Japan's trade and industry policy.
- Decision on the organization of volumes and selection of coordinating lead authors and co-authors.
- Opinion exchange with those who were engaged in the planning and implementation of trade and industrial policy in the past.
Introduction of Research Projects

A-1) Study Group on Changes in Financial and Industrial Structures
Project Leader/Sub-Leader: Tsutomu WATANABE, FF/ Iichiro UESUGI, CF

<Overview>
While the Japanese economy has been emerging from a long period of economic stagnation and entering a phase of steady economic recovery, there has been considerable change in (1) funds procurement by firms, (2) networks between firms (interfirm relationships based on commercial and capital transactions), and (3) relationships between companies and financial institutions relating to financial and capital transactions. This study group will empirically elucidate this transformation by using micro-level data on large corporations, SMEs, and financial institutions, and also data on the transactional relationships between firms themselves and those between firms and financial institutions.

A-2) Empirical Analysis of Japan’s Labor Market
Project Leader: Daiji KAWAGUCHI, FF

<Overview>
While the Japanese economy has shown signs of recovery, labor market indicators have improved little: the average wage has not increased and the size of non-regular employment has significantly increased. Under this rather stagnated labor market environment, the issue of the wage gap has attracted public and academic interest, but little progress has been made in gaining an overall picture of the wage gap with the use of large-scale government statistics; consequently, very little is known about matters such as the causes of wage differentials between regular and non-regular workers, and how the workers’ wage mobility has changed over time. Our research aims to fill the gap between social interests and rigorous empirical analysis by using microdata from large-scale government statistics. The final goal is to derive labor market policy suggestions based on rigorous empirical analysis.

<Major Research Results>
Discussion Papers
• "Male-Female Wage and Productivity Differentials: A Structural Approach Using Japanese Firm-Level Panel Data" (Hirokatsu ASANO and Daiji KAWAGUCHI) (DP No.:07-E-020)

A-3) Economic Analysis of Organizations and Institutions: The Design of Organizations and Institutions to Enhance Corporate Performance and Growth
Project Leader: Kotaro TSURU, SF

<Overview>
Amid the global boom in corporate mergers, acquisitions, and consolidation since the 1990s, the number of such cases in Japan has been increasing rapidly since the latter half of the 1990s. In order to understand these developments, it is essential to investigate fully (1) the motivations and intentions, and (2) whether the initially expected effects have occurred, and company performance has improved since reorganization. First, we will build a comprehensive M&A database that integrates microdata from basic studies of company activity with M&A information, and then conduct quantitative analyses in order to verify the above, while examining characteristics by industry and type. Also, as part of the creation of new research fields, we will establish a study group on the reform of the labor market system, for which the task will be to conduct interdisciplinary analyses, from both a theoretical and an empirical perspective, of ways in which to implement labor market reform in the future.

<Major Research Results>
Discussion Papers
• Consolidation of Cooperative Banks (Shinkin) in Japan: Motives and Consequences (Kaoru HOSONO, Koji SAKAI and Kotaro TSURU) (DP No.:06-E-034)

A-4) Research into Measures to Provide Efficient Public Services by Means of Government and Private-sector Collaboration, Premised on Small Government
Project Leader/Sub-Leader: Naoto YAMAUCHI, FF/ Hiromichi MORIYAMA, CF

<Overview>
Given the advent of an aging society with a declining population, plus major structural changes in the form of globalization and the intensification of international competition, in order to maintain economic vitality and to keep the size of the public sector within a scope that is sustainable it is essential to implement reform toward establishing "small government." Our research activities will include the categorization of the forms of public-private partnership (PPP) such as private finance initiative (PFI), the designated administrator system, and market testing; the conduct of quantitative verification of the effects of reductions in fiscal expenditure; and the conduct of analyses of introduction incentives, including by means of surveys of local government bodies and non-profit organizations (NPOs). In this way we will put forward suggestions on how to shape policies for achieving efficient public services in Japan through PPP.
### A-5) Theoretical and Experimental Research into Communication, Coordination, and Collaboration Mechanisms
Project Leader: Hirokazu TAKIZAWA, FF

**<Overview>**
In today’s state-of-art, science-based industries, of which the semiconductor industry is a leading example, complex cooperative relationships at the research and development (R&D) stage have been observed between companies that compete in their product markets, owing to factors such as increases in the size of necessary investment and the enlargement of the scope, growing complexity, and acceleration of R&D. Of particular note is that there has been growing interest in collaboration mechanisms that have until now been treated as black boxes in conventional economic theory, the reason being that R&D processes have come to be conducted across firm boundaries rather than kept within a single company, and there is increasing recognition of the necessity of understanding what types of communication, coordination, and collaboration mechanism are effective as well as incentive-compatible. Our research aims to address these issues from the viewpoints of the economics of information, game theory, and behavioral economics.

**<Major Research Results>**

**Discussion Papers**
- Information Sharing in Joint Research and Development (Hiroyuki CHUMA, Shuzo FUJIMURA, Toshiji KAWAGOE, Taisuke MATSUBAE, Masahiro OKUNO-FUJIWARA, Hirokazu TAKIZAWA, Yasunori WATANABE and Izumi YOKOYAMA) (DP No.: 07-J-013/07-E-019)

### A-6) The Frontier of Corporate Governance Analysis: Economic Analysis of M&A and Corporate Governance
Project Leader: Hideaki MIYAJIMA, FF

**<Overview>**
There has been considerable progress in recent years in the analysis of the governance structure of Japanese companies, but, to date, aspects such as the discipline imposed by main banks, the role of the ownership structure, and reforms affecting directors have progressed independently, and their mutual relationships have not been grasped fully. Furthermore, as a result of the gradual progress of creative destruction (the reorganization of traditional companies and the increase in the number of newly listed companies) since the second half of the 1990s, new corporate governance problems have been emerging at Japanese companies. Accordingly, our research will address all important issues regarding corporate governance and more broadly with regard to corporate systems, both in terms of their significance for policy and from an academic perspective, opening up a new frontier in corporate governance analysis. Adding to the economic analysis of M&A that has been conducted since the previous fiscal year, specific issues we will research include governance issues affecting emerging companies and listed subsidiaries, internal governance, business portfolios, a comprehensive understanding of internal organizational structures, and clarification of the relationship between a competitive environment and corporate governance. Also, in order to elucidate these points, we will attempt questionnaire-based analyses of the business portfolios and organizational structures of first-section listed companies.

**<Major Research Results>**

**Discussion Papers**
- Economic Analysis of M&As: Why has the Number of M&As Increased? (Yasuhiro ARIKAWA and Hideaki MIYAJIMA) (DP No.: 06-J-034)
- Understanding the Rapid Increase of M&As: Historical Background and the Economic Role of M&As (Hideaki MIYAJIMA) (DP No.: 06-J-044)

Project Leader: Nobuo AKAI, FF

**<Overview>**
To meet the increasing diversity of needs arising as society matures, it is necessary for local governments to take responsibility for implementing reforms to create systems that will ensure efficient administrative and financial management. Until now, the improvement of public infrastructure has been conducted by means of redistribution policies implemented by the central government in the name of “well-balanced land development.” It is important that regional economies that have been engaging primarily in domestic interchange should in the future, in line with the trends toward globalization and free trade with other East Asian countries, deepen international exchanges, for which a prerequisite is to make efficient use of public infrastructure and administrative assets. This calls into question what form of administrative and financial systems will support efficient management and use under the auspices of the local authorities. In addressing this, the most important components of the infrastructure assets are roads, ports, and airports. However, in these business fields many policies are still concentrated on the central government; administrative and financial systems sufficiently flexible to invigorate local economies under independent local government management do not yet appear to have been developed. In our research we will focus in particular on the future form of governance of regional airports and national airports that are operated under a national pool system through the Airport Improvement Special Account, studying it from various angles through the analysis of the redistribution originating in the special account system, the problems that arise from airport development and regulations under the central government, and the operating efficiency of regional airports and efforts by local government bodies toward the future. We will also study, both theoretically and empirically, the desirable form of administrative and financial systems that will operate local airports efficiently and invigorate their local economies.

### A-8) Changes in the Socioeconomic Structure and Tax Reform
Project Leader/Sub-Leader: Yasushi IWAMOTO, FF/ Kyoji HASHIMOTO, FF

**<Overview>**
Japan is currently facing the problems of an aging society, globalization of the economy, the global environment, and inequality, and it is exposed to change in its socioeconomic structure. Since a fundamental reform is also necessary in the tax system to address these changes, this research focuses on the desirable tax system that will respond to the changes in the socioeconomic structure from a medium to long-term perspective, incorporating recent developments of tax theory. For this purpose we will build a dynamic stochastic general equilibrium model that makes possible the simulation of tax reform proposals in line with policy issues in Japan, and we will analyze the effects of fundamental tax reform on economic activity and people’s welfare, also discussing the direction of the reform.
A-9) Reform of Labor Market Institutions
Project Leader: Kotaro TSURU, SF

<Overview>
In order to study a new “form” for Japan’s labor market institutions, and types of reform, we will organize a study group that will conduct theoretical and empirical research from various perspectives such as law, economics, and management. While looking broadly at labor market institutions as a whole, we will also look into the interrelationships of each constituent part, and in particular will make suggestions regarding a comprehensive system of labor laws from a standpoint that transcends vertical segmentation and boundaries. When conducting our analysis we will fully embrace international viewpoints and methods of analysis, including experiences from Europe and elsewhere, and will attempt to elucidate the relationships between labor laws and institutions and the labor market and employment systems, and in turn the relationship (including the issue of non-regular employment) with economic performance.

Other research results in Adjacent Basic Research Area A

Discussion Papers
- Shareholder Sovereignty Versus Employee Sovereignty: A Dilemma as Seen in Listed Companies in Japan (Kazuhiro TANAKA) (DP No.: 06-J-035)
- Bank’s Exposure and Private Workout Negotiations between the Creditor Bank and the Debtor Company: An Empirical Study Using Event Study Methodology (Fumio AKIYOSHI and Sumio HIROSE) (DP No.: 06-J-037)
- Measurement of the Impact of Buyout Funds’ Initiative in Corporate Reorganizations on the Recovery Rate of Reorganization Claims (Hiroshi MARUYAMA) (DP No.: 06-J-039)
- Relatively High Interest Rates for Okinawa Companies: A Quantitative Analysis by Means of a Nationwide Comparison (Yuichi ABIKO) (DP No.: 06-J-041)
- Relationships between Locally-Oriented Corporate Reconstruction Funds and Local Financial Institutions (Junsuke MATSUO) (DP No.:06-J-045)
- Development of a Multi-Region CGE Model that Incorporates Monopolistic Competition and other Factors (Masato HISATAKE and Kiyoshi YAMASAKI) (DP No.: 06-J-046)
- Innovation and Financing Structure (Noriyuki YANAGAWA) (DP No.: 07-J-004)
- Risk Money and Corporate Growth: Roles of Financial Intermediation (Takao KOBAYASHI and Masato HISATAKE) (DP No.: 07-J-005)
- SME Financing and the Choice of Lending Technology (Hirofumi UCHIDA, Gregory F. UDELL and Nobuyoshi YAMORI) (DP No.:06-E-025)
- Are Trade Creditors Relationship Lenders? (Hirofumi UCHIDA, Gregory F. UDELL and Wako WATANABE) (DP No.:06-E-026)
- Bank Size and Lending Relationships in Japan (Hirofumi UCHIDA, Gregory F. UDELL and Wako WATANABE) (DP No.: 06-E-029)
- Empirical Determinants of Bargaining Power (Hirofumi UCHIDA) (DP No.: 06-E-031)
- Loan Officers and Relationship Lending (Hirofumi UCHIDA, Gregory F. UDELL and Nobuyoshi YAMORI) (DP No.: 06-E-031)

B-1) Economic Analysis of Markets and Networks in Electricity Power Reform
Project Leader/Sub-Leader: Tatsuo HATTA, FF/ Makoto TANAKA, FF

<Overview>
In order to assist system reform in the electricity industry in Japan we will conduct more realistic research than ever into the issues of performance evaluation and system design in regard to the electric power market and the electricity transmission network, primarily from an economic perspective. Based on the results of project research conducted up to fiscal 2005, we have completed a number of prototype models for conducting quantitative evaluation and analysis concerning the electric power market and the electricity transmission network. In the project from fiscal 2006 onward we will further refine and develop these prototype models in line with the realities of the situation. After that, we will assemble and arrange the actual transaction data from 2005 onwards, and carry out more realistic quantitative evaluation and analysis for the purpose of assisting the continuous monitoring of the wholesale electric power exchanges, and investigation of impacts of changes in the system. In addition, with regard to individual system design issues relating to the market and the network, with a view to assisting ongoing system reform we will conduct applied research focusing on the application of these to real situations.

<Major Research Results>
Discussion Papers
- A Spatial Equilibrium Analysis of Transmission Charge Reform in Japan’s Electric Power Industry (Shu-ichi AKIYAMA and Nobuhiro HOSOE) (DP No.:06-E-022)
### B-2) Simulation Models for Policy Evaluation

**Project Leader:** Yoshitsugu KANEMOTO, FF

**Overview**
Applied general equilibrium models have been put into use for policy evaluation in fields such as energy policy, but owing to the large scale of the models it has tended to be difficult to evaluate their reliability. In this research we aim to assess the benefits and costs of each policy option, by using small-scale microeconomic models that are understandable, actionable, and facilitate the policy making process. The primary targets of the policy simulation will be countermeasures for global warming and the Japanese-style liberalization of the electric power market. With regard to the countermeasures for global warming we will analyze the effects of policies in specific fields such as automobiles. As for the liberalization of the electric power market, we will analyze the characteristics of Japanese system designs compared with those of other countries, and evaluate the various policy options.

**Major Research Results**

<table>
<thead>
<tr>
<th>Discussion Papers</th>
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<tbody>
<tr>
<td>Quantitative Policy Evaluation of the Front Runner Method Household Appliance Efficiency Standards Regulations in Japan by Cost-Benefit Analysis (Kazunari KAINOU) (DP No.: 06-J-025)</td>
</tr>
<tr>
<td>Quantitative Policy Evaluation of the Front Runner Method Regulations for Fuel Consumption Standards for Passenger Cars in Japan by Cost-Benefit Analysis (Kazunari KAINOU) (DP No. 07-J-006)</td>
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### Other research results in Adjacent Basic Research Area B

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<th>Discussion Papers</th>
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### C-1) Research into the Enhancement of Historical Energy Statistics

**Project Leader:** Kazunari KAINOU, F

**Overview**
Knowledge of the history of energy policies constitutes the base on which future energy policies should stand. However, the lack of highly accurate energy statistics that enable chronological comparison has been hampering our research. We will conduct research into the development of accurate historical energy statistics which consequently will serve as the basic materials for energy policy research. Also, by applying these historical energy statistics, we will conduct research on the optimum modality of energy policies.

**Major Research Results**

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### C-2) Building of GCE Model for East Asia that Introduces Economies of Scale

**Project Leader/Sub-Leader:** Kanemi BAN, FF/ Masato HISATAKE, CF

**Overview**
Amid the rapid progression of economic globalization, geographical concentration of economic activity and agglomeration of industry are accelerating. The remarkable development of the East Asian economies and the trends of economic integration are in particular having major impacts on the Japanese economy. In this research, we will develop an applied general equilibrium model for East Asia which will serve as a base for quantitative evaluation of the changes in the economic position of each nation including Japan, in the course of economic integration. This model will focus on trends in industrial agglomerations that arise as a result of economic integration and will explicitly incorporate economies of scale, also making imperfect competition a target of analysis. It will provide a highly transparent framework that will promote consensus-building by clarifying how each country’s political responses during negotiation of economic integration could affect the economic structure of East Asia, and how that would change the welfare of each country.

**Major Research Results**

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*Building of GCE Model for East Asia that Introduces Economies of Scale* (Dec 15, 2006)
Discussion Papers

Discussion Papers are research results formed in the shape of treatise which principally went through an internal review process. To stimulate active debate, they are posted on our website (http://www.rieti.go.jp/en/publications/act_dp.html). Discussion Papers including "J" in DP No. are written in Japanese.

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