OSAKA UNIVERSITY LAW REVIEW No. 57 (February 2010) 19-38

A Political Analysis of the Economic Bubbles in Japan and the U.S.: A Critical Examination of Comparative Political Economy Models*

Ryunoshin KAMIKAWA†

Abstract

This article critically examines comparative political economy models by analyzing cases of economic bubbles in Japan in the late 1980s and the U.S. in the late 1990s. In comparative political economy, it has been argued that both low inflation and low unemployment are accomplished in countries that have both an independent central bank that places top priority on price stability and a wage-bargaining system that leads to wage restraints. It is certain that the combination of anti-inflationary monetary policies and wage restraints led to low inflation and low unemployment both in Japan and the U.S. However, because of this combination, commodity prices were stable even though stock prices surged. Hence, monetary policies were not tightened and stock prices were inflated. Consequently, this combination can cause a massive bubble once asset-price inflation emerges. Also, the bursting of economic bubbles places deflationary pressures on the economy. In summary, this combination does not necessarily ensure good economic performance over the long term.

1. Introduction

An objective of this article is to examine the comparative political economy models critically through analyzing cases of economic bubbles in Japan in the late 1980s and the U.S. in the late 1990s. Comparative political economy appeared in the 1970s when industrialized countries experienced stagflation, or high unemployment and high inflation simultaneously. Some countries were able to overcome these early, but others were not. Comparative political economy have been used to try to explain these divergences in macroeconomic performance

---

* This work was supported by the Ministry of Education, Culture, Sports, Science and Technology, Grant-in-Aid for Science Research (15730074).

† Associate Professor of Political Science, Graduate School of Law and Politics, Osaka University, Japan.

between industrialized countries by using political factors. It has been argued that wage restraints are needed to control cost-push inflation. It has also been thought that wage restraints bring about recovery in corporate earnings and capital investment and that this corrects the economy again and decreases unemployment. Therefore, under what political conditions wages could be restrained also came to be discussed.

However, in this article, I point out that although wage restraints certainly lead to low inflation and low unemployment, simultaneously, they may inflate bubbles, or elevate asset prices beyond those supported by the fundamentals. I will cite two cases, viz., the stock price bubbles in Japan in the late 1980s and those in the U.S. in the late 1990s.[1)] Comparative political economy models assume that wage restraints result in good economic performance. By showing that stock price bubbles were inflated in Japan and the U.S. where these situations occurred, I maintain that comparative political economy models cannot fully explain the economic performance of today's industrialized countries. This is because they have been established on the premise of structural inflation.[2)]

Another objective of this article is to explain economic bubbles in Japan and the U.S. from the viewpoint of political analysis. According to one prevailing view, the bubble economy in Japan was caused by lax monetary policies over a prolonged time.[3)] Most political scientists and journalists and many economists asserted that these policies were accepted because of the domination of the Ministry of Finance (MOF) over the Bank of Japan (BOJ). They argued that the U.S. government requested domestic demand be expanded to reduce the imbalance of payments between the U.S. and Japan and that the MOF, which tried to avoid increasing public spending, forced the BOJ to loosen its monetary policies.[4)] However, as will be explained later, I do not think that the BOJ has depended on the MOF since the late 1970s. If a lack of independence by the central bank brought about the economic bubble, why did a stock-price bubble emerge in the U.S., where the central bank was seen to be independent of the government? Moreover, the stock price bubble in the U.S. can largely be explained by political factors, even though some economic factors that caused it have been pointed out.

This article explains economic bubbles in Japan and the U.S., focusing on two political factors, i.e., a system of wage bargaining and the independence of the central bank, which have been seen as important explanatory variables in economic performance. In both countries, commodity prices were stable, even though stock-price bubbles were inflated. This was both because workers' wages were restrained and because private economic agents firmly believed that adequate monetary policies to control inflation should be implemented. Thus, monetary policies were not tightened promptly and the bubbles were further inflated.[5)]

I will briefly explain why a wage-bargaining system and the independence of the central bank are seen as "political" factors. First, workers' wages are not only dependent on the balance of supply and demand but also affected by wage bargaining between trade unions and employers' associations in each country. The ways in which trade unions and employers' associations are organized (whether centralized or decentralized) and at which level (at national, industrial, or firm levels) wages are bargained differ between countries. Influential relations between trade unions and employers' associations, those within trade unions, and those within employers' associations are determined due to these differences. Thus, under diverse wage-bargaining systems, there are increasingly different rates of wages, even under the same economic conditions. In other words, a wage-bargaining system is an institution that affects the "political process" between trade unions and employers' associations during wage bargaining.

Second, monetary policy should be managed by a central bank whose only goal is price stability. However, governments generally tend to pressure central banks to loosen monetary policies excessively, as they want economic expansion along with political considerations. Therefore, monetary policies depend on whether central banks are highly dependent on or independent of the government. In other words, the independence of central banks is a concept that affects the "political process" in determining monetary policies.

This article is organized as follows. The second section summarizes the development of comparative political economy and explains that a wage-bargaining system and independent central banks are regarded as explanatory variables of economic performance. The third and fourth sections explain the stock price bubbles in Japan in the late 1980s and those in the U.S. in the late 1990s, focusing on wage restraints and monetary policies. The last section concludes the paper by critically examining the comparative political economy models.

2. Development of Comparative Political Economy

This section explains the development of comparative political economy, where both wage-bargaining systems that lead to wage restraints and independent central banks that implement monetary policies to stabilize inflation result in sound economic performance, even though the explanation will be brief and oversimplified.

Low real wages in comparative political economy are thought to lead to both low inflation and low unemployment. Hence, there has been some controversy on what type of wage-bargaining system can impose wage restraints.

In corporatist theory, it has been argued that if trade unions are centralized and wage bargaining is conducted at the national level (or under a collective wage-bargaining system), a peak trade union can have a peak employers' association secure employees' jobs in exchange for the former restraining its demand to increase wages.[6)] However, in both dualism theory and the hump-shaped model, it has been argued that if trade unions are decentralized and wage bargaining is conducted at the level of the firm, trade unions cannot negotiate wage increases since they are compelled to choose between wage increases and job security. Consequently, sound economic performance is achieved in countries where trade unions are weak and decentralized as well as in those that are corporatist.[7)]

In the 1990s, the view prevailed that if employers' associations were centralized, wage restraints could be accomplished through coordination within them, regardless of the degree of centralization of trade unions.[8)] Moreover, some studies have argued that even if wage bargaining is conducted at the industrial level, wages can be restrained under conditions where neither the protected sector nor the public sector, but the export sector acts as a pattern setter in wage bargaining. Both the employers and trade unions of the export sector are cautious about increasing wages because this is exposed to international competition.[9)]

Furthermore, the attention of research since the late 1990s has focused on the interaction between the independence of central banks and wage-bargaining systems. It has been argued in economics that a high degree of independence by central banks since the late 1980s has resulted in lower levels of inflation without negatively affecting employment or economic growth.[10)] Political scientists agree that highly independent central banks result in noticeably lower levels of inflation. However, trade unions negotiate excess wage increases under the wage-bargaining system, which cannot lead to wage restraints. When this occurs, an independent central bank tightens monetary policy to curb labor cost-push inflation and unemployment increases as a result, even though inflation is lowered. However, under the wage-bargaining system, which can lead to wage restraints, trade unions restrain wage demands voluntarily and secure workers' jobs. This is because they are certain that an independent central bank will tighten monetary policy if they are awarded excess wage increases. In this situation, an independent central bank does not need to tighten monetary policy too aggressively, and this is regulated to the degree necessary to control inflation as real wages are relatively low. Consequently, this results in both low inflation and low unemployment.[11)]

As previously stated, there has been no agreement on what type of wage-bargaining system may lead to wage restraints. However, it has generally been argued that both low inflation and low unemployment are achieved in countries that have both an independent central bank that tries to stabilize prices and a wage-bargaining system that leads to wage restraints.

3. The Bubble Economy in Japan in the late 1980s

This section explains why the stock-price bubble was inflated in the late 1980s in Japan where both low inflation and low unemployment had been accomplished from the late 1970s to the early 1980s within the framework of a comparative political economy.

3.1. Overcoming Stagflation

From the late 1970s to the early 1980s, Japan overcame stagflation better and earlier than other industrial countries. There are two main reasons for this. First, wage increases had been restrained since 1975 because the export sector had taken the initiative in the annual wage bargaining and its trade unions had cooperated with employers by restraining wage increases, even though public-sector trade unions had gained wage increases. Second, the BOJ had implemented monetary policy and placed top priority on the stability of prices.[12)]

It is generally believed that the BOJ was not very independent of the government before the Bank of Japan Act was revised in 1998. In fact, Prime Minister Kakuei Tanaka compelled the BOJ to implement an excessively lax monetary policy in 1972. This caused a vicious price spiral in 1973 with the first oil crisis. However, learning from this failure, the BOJ has placed the utmost priority on price stability since the late 1970s. It has tried to implement monetary policy to control inflation, resisting pressure from politicians within the Liberal Democratic Party (LDP) to ease monetary policy excessively.

The BOJ's responses to the second oil crisis in 1979 conclusively improved the BOJ's reputation as "an inflation fighter." From April 1979 to March 1980, the BOJ continued to raise the official discount rate from 3.5% to 9.0%. In particular, when the budget draft was deliberated at the Diet in February 1980, the BOJ raised this despite strong opposition from the MOF and the LDP. These timely increases in interest rates enabled the Japanese economy to overcome the second oil shock because inflation was controlled. Through this experience of forestalling inflation, the BOJ became highly credible from the viewpoint of private economic agents.[13)]

3.2. Rises in Stock Prices

Next, I will explain the reasons stock prices soared to such extremes in the 1980s. As previously stated, it is generally believed that Japan's economic bubble emerged because monetary policy had been eased for a long time. It is certain that the economic bubble was inflated because of the low interest-rate policy from 1986 to 1989. However, stock prices began rising in 1983.[14)] It should thus be interpreted that the easing of monetary policy since 1986 did not cause stock prices to increase. After other factors had already raised stock prices, monetary policy was eased and this drove up stock prices tremendously. In addition, various factors other than monetary relaxation contributed to driving up stock prices, which had already been on the rise.

There were five main factors that raised stock prices other than loosening monetary policy. First, investment in stocks increased. In December 1980, in order to prompt companies and banks to purchase the government bonds that had been issued on a massive scale, the MOF permitted them to adopt an accounting procedure of dividing the book prices of securities that they already held and those of securities that they had bought by using cash in trust (the so-called *Boka-Bunri*). Since companies were able to save on their corporate income tax, most companies adopted this accounting procedure and corporate investment funds (specified money trusts, the so-called *Tokkin*) became a trend. This gave rise to the boom in speculative investment on the stock exchange (the so-called *Zai-Tech* boom).[15)] Moreover, the stocks of Nippon Telegraph and Telephone Corporation (NTT), which had been privatized in 1985, were sold in 1987 and stock prices continued to increase. This triggered a *Zai-Tech* boom among ordinary people who had not invested in the stock market.

Second, the management of companies came to attach importance to the high prices of their shares. When they increased capital, they had long-term shareholders who kept cross-shareholding with them to purchase their shares in case their prices dropped.[16)] In fact, the MOF permitted securities companies to control the stock prices of their client companies for a given period before stocks were issued, if they called the ministry for permission in advance.[17)]

Third, the government pursued a policy of fiscal austerity to improve the budget balance in the 1980s. Because it limited the number of government bonds it issued, government bonds themselves could not absorb all surplus funds in the market and stocks were subsequently bought.[18)]

Fourth, the financial crisis in 1987 was quickly overcome. On October 19, 1987, the New York Stock Exchange collapsed. Stock prices also dropped on the Tokyo

Stock Exchange the following day. The executives of both the Securities Bureau of the MOF and the four major securities companies held a regular meeting that day. They decided by tacit agreement that fixed limits for proprietary trading would be eased and securities companies would prop up share prices. Also, the securities companies themselves arranged not to send selling orders to the stock market.[19)] Moreover, the MOF pressed investment companies to purchase shares.[20)] By doing so, the stock prices rallied.

However, at the end of December 1987, life insurance companies started to sell stocks in bulk to cover the loss in dollar earnings and corporate investment funds. In April 1987, the Banking Bureau of the MOF had already instructed firms to change the accounting standard from cost-purchase accounting to lower cost accounting in March 1988. The Securities Bureau of the MOF became concerned about the sell-off of shares and asked the Banking Bureau to again change the accounting standard. Thus, the Banking Bureau instructed firms to postpone the introduction of lower cost accounting until April 1, 1988. Because of this, companies did not need to write down the loss and life-insurance companies did not have to sell stocks in mass quantities.[21)]

In this way, the MOF succeeded in preventing share prices from declining. After that, stock prices surged remarkably. This was because these measures by the MOF to contain the markets made investors believe that the ministry would never let stock prices slump.

Fifth, an economic theory that justified high stock prices emerged. The Japan Securities Research Institute released a report in October 1988. This report argued that stock prices were not too high, taking into consideration the market value of the companies' assets. This was simply because the price of land that companies owned was excessively high.[22)]

The myth of "permanent low-interest rates" also prevailed in the markets. This was because the International Finance Bureau of the MOF supported the international opinion that Japan should retain its low interest rates for as long as possible in order to shore up the world economy.[23)]

3.3. Easing of Monetary Policy

I will now explain why the BOJ continued to loosen monetary policy in the late 1980s even though stock prices surged extraordinarily.

The yen rose steeply since the Plaza Accord in September 1985. The BOJ lowered its official discount rate five times, i.e., in January 1986, March 1986, April 1986, November 1986, and February 1987. During this period, it was certain that the U.S. and the MOF had requested the BOJ to cut interest rates. However, the sharp appreciation of the yen against the dollar had forced the economy into recession and raised unemployment until the beginning of 1987. In this situation, it was not so unreasonable to ease monetary policy.[24)]

The problem was why the BOJ had not raised its official discount rate until May 1989 despite economic recovery, the rapid expansion of the economy, and asset-price inflation. This can generally be explained by the behavior of the executive officials of the MOF and the caucus of the LDP who forced the BOJ not to raise interest rates. They remarked off-the-record that Vice-Governor Yasushi Mieno, who had repeated statements that increased interest rates were needed to prevent inflation, was ill-suited to be governor of the BOJ. As BOJ officials had supported Mieno's promotion to the governorship because he had built his career at the BOJ, they refrained from raising interest rates.[25)]

However, I previously clarified that the executives of the BOJ did not reach agreement on increasing its official discount rate and they could not make a decision to increase it for three main reasons.

First, the BOJ was afraid that interest rate hikes in Japan might cause the dollar to crash. Actually, in summer 1987, it considered increasing interest rates and directed short-term interest rates to climb higher in the market from the end of August. However, stock prices plunged on the New York Stock Exchange on October 19 (Black Monday) and the dollar continued to depreciate after that. This happened because the German Federal Bank (the central bank of the Federal Republic of Germany) was thought to have been responsible for increasing the short-term interest rates on the market. Therefore, it decided to stop directing short-term interest rates to climb higher and gave up on raising its official discount rate.

Second, it could not perceive that the inflated asset prices were a bubble (i.e., they did not reflect real demand) on the grounds that asset prices had increased before it had loosened monetary policy. Moreover, it did not perceive that asset-price inflation would cause problems that would be too serious in the future. Thus, it did not have a clear awareness of a need to burst the asset-price bubble through imposing a credit squeeze.

Third, despite the inflation of asset prices, commodity prices were stable. The inflation rate was about 0% from 1986 to 1988. It was common knowledge that central banks should not use monetary policy to stabilize asset prices since these were determined by various factors other than interest rates.

In fact in May 1989, when commodity prices rose slightly, the BOJ increased its official discount rate even though this was not then regarded as sufficiently urgent to be necessary. This seemed to indicate that the BOJ was not as dependent on the government as had generally been thought.[26)]

Of these three reasons, the most important is that commodity prices were stable during this period.[27)] If commodity prices had risen as asset prices surged, the BOJ, which placed top priority on the stability of prices, would have tightened monetary policy and thereby the inflation in asset prices would have been curbed. Consequently, stable prices for commodities were the main reason for excessively elevating asset prices. Why were commodity prices stable during this period?

3.4. Stable Commodity Prices

The three main reasons for stable commodity prices despite inflation in asset prices are discussed in what follows.

First, wages were held down relative to the buoyant economy. From 1984 to 1989, real wage increases averaged 1.9% per year, even though the average productivity growth (in all sectors) was 6.3% per year.[28)] Since 1975, wage increases had been restrained as the export sector had taken the initiative in the annual wage bargaining. Despite the overheating economy during the bubble period, wage increases were restrained in the same way.

Second, the inflation that was expected did not occur. This was because the BOJ had gained a great deal of credibility with private economic agents in preventing inflation.[29)] It had implemented monetary policy to control inflation and had stabilized prices since the late 1970s. Hence, it had built up an excellent reputation as a central bank that could stabilize prices. Due to this experience, the expected inflation rate among private economic agents remained low and Japan achieved the most stable prices of any other developed country through the 1980s.[30)]

Therefore, it seems that private economic agents regarded the easing of monetary policy after the Plaza Accord as a response to emergency situations and they thought that the BOJ would change this policy and avert inflation when prices started to rise.[31)] This is why expectations of inflation did not occur and commodity prices were stable despite the easing of monetary policy.

Third, the strong yen and declining oil prices brought prices down.[32)]

3.5. Concluding Remarks

Almost no one has argued that tight monetary policy should be implemented to control inflated stock prices. This is both because asset prices had increased before the BOJ loosened monetary policy and because commodity prices were stable. Hence, monetary policy continued to be eased and the bubble in asset prices was inflated.

From the viewpoint of a comparative political economy, wage restraints and the central bank's outstanding credibility in avoiding inflation are very important. These had contributed to low inflation and low unemployment from the late 1970s to the early 1980s. However, because of these, commodity prices did not increase even though asset prices surged in the late 1980s. As a result, monetary policy continued to be eased and the bubble in asset prices was inflated even further.

4. The Bubble Economy in the U.S. in the late 1990s

The process and mechanism for the stock-price bubble in the U.S. in the late 1990s were very similar to those in Japan in the late 1980s. Like Japan, stock prices in the U.S. surged for similar reasons and monetary policy was not tightened because commodity prices were stable despite the bubble in stock prices.

4.1. Revival of U.S. Economy

In the early 1990s, the U.S. economy slipped into a serious recession. However, thanks to adequate monetary policies, wage restraints, and efforts toward fiscal reconstruction, it recovered.

To begin with, I will explain what these adequate monetary policies were. In July 1992, the Federal Reserve lowered the target rate for federal funds to 3%. At that time, the inflation rate was about 3%. The Federal Reserve maintained this real zero-interest-rate policy until February 1994, stimulating the economy.[33)]

In February 1994, the Federal Reserve increased the rate of federal funds. This decision surprised the markets because the inflation rate had not increased very much and the unemployment rate still remained high, although the economy had started to recover and the unemployment rate was about to decrease. The Federal Reserve continued to increase interest rates until February 1995.[34)] During this period, the chairman of the Federal Reserve, Alan Greenspan did not aim to cool the economy down to below the level of full employment to reduce the inflation rate, but to achieve a so-called soft landing at about the level of full employment without overheating the economy. He succeeded in fine-tuning the economy and established a reputation as "the macroeconomic magician."[35)]

Next, I will discuss wage restraints. The bargaining power of trade unions was markedly reduced in the 1980s. There were two main reasons for this. First, the rate of unionization declined substantially as employment in manufacturing decreased and that in services increased. Second, the Reagan administration took tough action against strikes.[36)] In addition, many workers were retrenched in manufacturing and the financial industry at the beginning of the 1990s. This forced workers to acknowledge their jobs were insecure and this restrained their wage demands.[37)]

Finally, I will point out efforts that were made toward fiscal reconstruction. The Clinton administration gave maximum priority to reducing budget deficits and decided to cut fiscal expenditures and increase taxes beyond the expectations of markets. Consequently, market players expected reduced fiscal deficits and long-term interest rates fell rapidly. This strongly stimulated the economy and created a boom in business investments.[38)]

4.2. Rise in Stock Prices

Next, I will explain five of the main reasons stock prices soared in the 1990s. As in Japan, the easing of monetary policy did not seem to cause stock prices to rise in the U.S. After other factors had already raised stock prices, monetary policy was eased and this greatly drove up stock prices.

First, investment in stocks increased. In the 1990s, the number of companies that offered 401(k) plans, or defined contribution pension plans, to their employees increased. This provided opportunities for ordinary people who had previously not invested in the stock market to learn about investments and become familiar with it. They became more willing to invest in stocks.[39)]

Second, the management of companies came to attach great importance to the high prices of their shares. Most companies since the 1980s had adopted "maximizing shareholder value" as their management principle. This tendency was strengthened in the 1990s as the stock-option system was introduced to provide rewards to executives. Then, numerous companies purchased their own stocks and liquidated them. By decreasing the number of outstanding shares, they expected their share price would rise and their return on equity (ROE), which was seen as a critical indicator of stock investment, would also rise.[40)]

As a result, many companies committed accounting fraud to drive up the prices of their shares. These were successively revealed after the stock-price bubble collapsed.[41)]

Third, the government pursued a policy of fiscal austerity to balance the budget in the 1990s. Because this limited the number of government bonds issued, government bonds themselves could not absorb all surplus funds on the market. Then, funds flowed onto the stock market and stock prices were driven up.

Fourth, the financial crisis in 1998 was promptly overcome. On August 17, 1998, the Russian government devalued the ruble and declared a 90-day moratorium on its repayments of foreign debts. This dramatically devalued most foreign and corporate bond portfolios and Long-Term Capital Management (LTCM), a hedge fund specializing in large-scale speculation, suffered massive losses. If LTCM were allowed to fail and defaulted on its debts, a serious crisis in the financial system could have occurred. Then, at the instigation of the Federal Reserve Bank of New York, the 16 banks and securities and investment-banking firms that had money in LTCM rescued it by contributing $3.6 billion.[42] Moreover, the Federal Reserve reduced interest rates three times from September to November, trying to stabilize the international financial market.[43]

These responses to the financial crisis prevented it from becoming global and U.S. financial authorities became appreciated to a greater extent. However, as investors placed too much confidence in their ability to control the financial crisis, they estimated their investment risks to be much lower than they really were. Consequently, they became addicted to higher risk investments and the bubble expanded.

Fifth, an economic theory that justified high stock prices emerged. It was the theory of the New Economy that argued that there was a permanent structural change in the U.S. economy. New Economy theorists insisted that the utilization of IT had permanently improved the productivity of labor and that this had eliminated limits to potential economic growth and thus business cycles. They argued that rapidly increasing stock prices were reasonable, which simply reflected improvements in the real economy.[44]

4.3. Easing Monetary Policy

I will now explain why monetary policy was not tightened even though stock prices surged astonishingly in the late 1990s.

Most economists in the mid-1990s thought that the potential growth rate in the U.S. was around 2.5% and the non-accelerating inflation rate of unemployment (NAIRU) was around 6.0%. They believed that inflation would occur if economic growth above 2.5% continued and unemployment dipped below the NAIRU.

However, the inflation rate did not rise in the late of 1990s, even though the economic growth rate was above 2.5% and the unemployment rate was below 6.0%. At the time, Greenspan determined that this was because productivity had grown and the unit labor cost had fallen. He persuaded the Federal Open Market Committee not to attack inflation preemptively but rather to wait until they could see clear evidence that inflation was rising. The Federal Reserve did not raise interest rates in the face of this extraordinarily low unemployment.[45]

If the inflation rate had risen during this period with the expanding economy as was expected by most economists, Greenspan should have tightened monetary policy to curb inflation. Then, the economy would have been prevented from overheating and inflated stock prices would also have been curbed. Commodity prices in the U.S., as in Japan, were stable even though the economy expanded and stock prices surged sharply. Therefore, monetary policy continued to be eased and the bubble in asset prices was inflated.

Moreover, just as the BOJ had faced Black Monday in 1987, the Federal Reserve faced the Asian financial crisis in 1997 and the Russian default in 1998 and it missed opportunities of raising interest rates.[46)] This is one reason that the policy of low interest rates was extended.

4.4. Stable Commodity Prices

There were three main reasons for the stability in commodity prices despite the inflation of asset prices.

First, wages were held down relatively despite the buoyant economy. From 1995 to 2000, real wage increases averaged 1.3% per year, even though the growth in average productivity (in nonagricultural sectors) was 2.5% per year.[47)]

One of the reasons for this is the "traumatized worker hypothesis," which argues that workers who feel their jobs are insecure in changing economies will accept smaller wage increases. After having been menaced by corporate restructuring, experienced suffering due to the recession, and then struggling through the "jobless" recovery in 1990–1991, American workers became more concerned with job security than with real wage increases. Moreover, American labor was thought to have suffered not just temporary trauma, but to actually have seen its bargaining position eroded on a permanent (or at least long-lasting) basis.[48)]

There are two reasons the bargaining power of labor was reduced. The first is that the rate of unionization declined substantially as employment in manufacturing decreased and that in services increased. Due to this, the position and influence of trade unions slipped. This changed labor-management relations from hostile to cooperative.[49)] The second reason is that the number of irregular employees increased. Corporations in the 1990s increased the number of irregular employees to spare them the cost of having to provide employee benefits (e.g., medical- and retirement-benefit plans).[50)] An increasing number of irregular employees ceased union membership and this made regular employees feel added job insecurity. Management had strong bargaining power against irregular employees since they had no security of employment. Therefore, an increasing number of irregular employees led to wage restraints, compelling workers to place the highest priority on job security and restrain their wage demands. This was the very situation that dualism theory had predicted.

Second, Greenspan established the credibility of his anti-inflationary policies. In February 1994, the Federal Reserve raised the rate for federal funds, which surprised the market, as the inflation rate had not yet risen. This continued preemptive rate hikes until February 1995.[51)] Greenspan's contributions in preventing inflation were greatly appreciated.

Through this experience, private economic agents expected that he would be able to curb inflation in the future. As a result, inflationary expectations remained very low through the late 1990s, even though the economy was overheating.

Third, Robert Rubin, who took office as Treasury Secretary in 1995, aggressively supported a strong dollar.[52)] The appreciation of the dollar lowered import prices and oil prices. Hence, the inflation rate fell.[53)]

4.5. Concluding Remarks

As had not been done in Japan, monetary policy was not tightened to control rising stock prices. This was both because asset prices had increased before the Fed loosened monetary policy and because commodity prices were stable.

From the viewpoint of a comparative political economy, wage restraints and the high credibility of a central bank in controlling inflation are very important. These contributed to low inflation and low unemployment in the U.S. However, because of these, commodity prices did not increase even though asset prices surged. As a result, monetary policy continued to be eased and the bubble of asset prices was inflated further.

5. Conclusion

I have examined the stock-price bubbles in Japan and the U.S. in this article. As the theory of comparative political economy has argued, the combination of anti-inflationary monetary policy and wage restraints has certainly led to low inflation and low unemployment. However, this combination has brought about a situation where commodity prices do not increase despite the inflation of asset prices. It may thus cause a massive bubble once inflation in asset prices emerges.

Undeniably, there were some factors that drove up stock prices in both countries beyond those supported by the fundamentals. The inflation in stock prices was attributed to these. Then, because of both independent central banks that curbed inflation and wage-bargaining systems that led to wage restraints, inflation was overcome. Thus, commodity prices kept stable despite the sharp rises in stock prices. As a result, tight monetary policies were not eased and massive bubbles in stock prices were inflated.

Moreover, such situations are increasingly likely to occur in the future. There are three reasons for this. First, with the progress of globalization, international capital flows are increasing. Consequently, huge amounts of money are flowing into financial markets and stock-price bubbles are more likely to happen. Second, because globalization also intensifies international competition between enterprises, wage increases may be restrained. Third, due to the liberalization of capital movement, countries have to control inflation more stringently. If inflation emerges, capital rapidly flows abroad. For this reason, the governments have to make central banks independent of them.

To summarize, the progress in globalization has enhanced the possibility of stock-price bubbles emerging and has forced countries to implement monetary policies to rigorously curb inflation and impose rigid wage restraints.

Unemployment used to decrease and wages used to increase in industrial countries with improvements in the economy. This raised prices. The central bank then used to tighten monetary policy and cool the economy down. As a result, unemployment increased and this reduced wage pressure and inflation. In short, price rises through wage increases used to signal central banks that the economy was overheating.

However, with the growth in globalization, this mechanism has failed. Although the economy is overheating, wages and prices do not increase and inflationary expectations remain low in more countries. Because prices remain stable in this situation, it is difficult for the central bank to tighten monetary policies even if inflation in asset prices emerges. For that reason, once asset-price inflation has emerged, the possibility for it to become a massive bubble increases remarkably.

It has been argued in comparative political economy what kinds of political factors are required to overcome stagflation. The answer is a combination of monetary policy to curb inflation and a wage-bargaining system that leads to wage restraints. This is now an effective measure that results in low inflation and low unemployment. While unemployment is admittedly still a serious problem, as globalization continues to progress, the asset-price bubbles and deflation that may follow its collapse become more serious threats than inflation. As I clarified earlier in this article, the combination of monetary policy to curb inflation and a wage-bargaining system leading to wage restraints can cause a massive bubble once asset-price inflation emerges. Then, the bursting of the economic bubble places deflationary pressure on the economy. That is, at present, the combination of anti-inflationary monetary policies and wage restraints do not necessarily ensure sound economic performance for the long term. Therefore, comparative political economy will have to develop new analytical frameworks that can deal with not only inflation and unemployment but also bubbles and deflation.

Notes

1) In Japan, the land-price bubble was also inflated in the late 1980s. In the U.S., the stock-price bubble that had centered on the IT industry collapsed in 2001, but the housing bubble continued to inflate until 2006. In this article, I have only focused on stock-price bubbles to simplify the argument.
2) Until now, the researchers of comparative political economy had not sufficiently examined the U.S. or Japan. This is because most of them have specialized on European countries. Due to this "European Bias," its shortcomings, which this article points out, have not been called attention to.
3) Kazuo Ueda, *Kokusai Shushi Fu-Kinko ka no Kin-yu Seisaku* [Monetary Policy under Disequilibrium in Balance of Payments] (Tokyo: Toyo Keizai Shimposha, 1992), pp. 169–193.
4) C. Randall Henning, *Currencies and Politics in the United States, Germany, and Japan* (Washington, D.C.: Institute for International Economics, 1994); William W. Grimes, *Unmaking the Japanese Miracle: Macroeconomic Politics, 1985-2000* (Ithaca: Cornell University Press, 2001); Akira Sato, *Dokyumento Kin-yu Hatan* [A Document on Financial Meltdown] (Tokyo: Iwanami Shoten, 1998), pp. 326–363; Akihiro Kuroki, *Kin-yu Seisaku no Yukosei: 'Tekisetsu' katsu 'Kidoteki' na Un'ei wo Motomete* [Effectiveness of Monetary Policy: Seeking for 'Adequate' and 'Expeditious' Management] (Tokyo: Toyo Keizai Shimposha, 1999), pp. 177–205.
5) On the other hand, in Scandinavian countries in the late 1980s, asset-price bubbles were inflated because of dependent central banks. However, in these countries, not only asset prices but also commodity prices rose simultaneously. From 1986 to 1990, the average annual rate of increase in the consumer price index in Japan was 1.4%, that in Sweden was 6.3%, that in Finland was 5.0%, and that in Norway was 6.2%. *OECD Historical Statistics* (Paris: OECD, various years). From 1995 to 2000, that in the U.S. was 2.4%. Tetsuro Sugiura, *Amerika Keizai wa Shizumanai: Otoroenu Mikuro no Tsuyosa* [The U.S. Economy will not Go Down: The Strength of the Micro-Economy does not Decline] (Tokyo: Nihon Keizai Shimbunsha, 2003), p. 12.
6) David R. Cameron, "Social Democracy, Corporatism, Labour Quiescence, and the Representation of Economic Interest in Advanced Capitalist Society," in John H. Goldthorpe ed., *Order and Conflict in Contemporary Capitalism* (Oxford: Oxford University Press, 1984), pp. 143–178.
7) Peter Lange and Geoffrey Garrett, "The Politics of Growth: Strategic Interaction and Economic Performance in the Advanced Industrial Democracies, 1974-1980," *Journal of Politics* 47, 1985: 792–827; Lars Calmfors and John Driffill, "Bargaining Structure, Corporatism and Macroeconomic Performance," *Economic Policy* 6, 1988 (April) : 13–61.
8) David Soskice, "Wage Determination: The Changing Role of Institutions in Advanced Industrialized Countries," *Oxford Review of Economic Policy* 6, No. 4, 1990: 36–61.

9) Torben Iversen, *Contested Economic Institutions: The Politics of Macroeconomics and Wage Bargaining in Advanced Democracies* (New York: Cambridge University Press, 1999); Franz Traxler and Bernhard Kittel, "The Bargaining System and Performance: A Comparison of 18 OECD Countries," *Comparative Political Studies* 33, 2000: 1154–1190; Sofia A. Pérez, "From Decentralization to Reorganization: Explaining the Return to National Bargaining in Italy and Spain," *Comparative Politics* 32, 2000: 437–458.
10) Vittorio Grilli, Donato Masciandaro, and Guido Tabellini, "Political and Monetary Institutions and Public Financial Policies in the Industrial Countries," *Economic policy* 13, 1991: 341–392; Alex Cukierman, Steven B. Webb, and Bilin Neyapti, "Measuring the Independence of Central Banks and Its Effect on Policy Outcomes," *The World Bank Economic Review* 6, 1992: 353–398; Alberto Alesina and Lawrence H. Summers, "Central Bank Independence and Macroeconomic Performance: Some Comparative Evidence," *Journal of Money, Credit, and Banking* 25, 1993: 151–162.
11) Peter A. Hall, "Central Bank Independence and Coordinated Wage Bargaining: Their Interaction in Germany and Europe," *German Politics and Society* 31, 1994 (Spring): 1–23; Peter A. Hall and Robert J. Franzese, Jr., "Mixed Signals: Central Bank Independence, Coordinated Wage Bargaining, and European Monetary Union," *International Organization* 52, 1998: 505–535; Iversen, *Contested Economic Institutions*; Robert J. Franzese, Jr., "Institutional and Sectoral Interactions in Monetary Policy and Wage/Price-Bargaining," in Peter Hall and David Soskice eds., *Varieties of Capitalism: The Institutional Foundations of Comparative Advantage* (New York: Oxford University Press, 2001), pp. 104–144.
12) That is to say, in Japan, the combination of monetary policy to curb inflation and wage bargaining at the industrial level has led to low inflation and low unemployment. This case fits Iversen's model well. Ryunoshin Kamikawa, "Hikaku Seiji Keizaigaku no Hatten to Nihon no Seiji Keizai: Chingin Kosho, Kin-yu Seisaku to Makuro Keizai no Seijigaku" [The Development of Comparative Political Economy and Political Economy in Japan: A Political Analysis on Wage Bargaining, Monetary Policy and Macroeconomics], *Hogaku Ronso* 150, No.6 (2002): 110–129, 151, No. 5 (2002): 93–118.
13) Ryunoshin Kamikawa, *Keizai Seisaku no Seijigaku: 90 nendai Kin-yu Kiki wo Motarashita 'Seido Haichi' no Kaimei* [A Political Analysis of Economic Policies: A Clarification of 'Institutional Settings' which Caused Economic Crises in the 1990s] (Tokyo: Toyo Keizai Shimposha, 2005), ch.2.
14) Yasuhiro Yonezawa, *Kabusiki Sijo no Keizaigaku* [Economics of Stock Market] (Tokyo: Nihon Keizai Shimbunsha, 1995), pp. 65–66.
15) Richard C. Hanson, *Okura Erito Hokori to Guko* [The Pride and Folly of Japan's Finance Ministry Elite] (Tokyo: TBS Buritanika, 1996), pp. 87–89; Katsumi Kawano, *Kin-yu Jiyuka Senryaku no Kiketsu* [Consequence of Financial Liberalization Strategy] (Tokyo: Yuhikaku, 1995), pp. 125–126; Ushio Shiota, *Okurasho no Fukaku* [Blunder of the Ministry of Finance] (Tokyo: Nihon Keizai Shimbunsha, 1993), pp. 54–56; Yukihiro Asano, *Tohshika kara Mita Kabushiki Shijo: Baburu no Kozo to Shijo Saisei no Jouken* [Stock Market from the Viewpoint of Investors: Structure of Bubble and Conditions for Market Revitalization] (Tokyo: Chuo Koronsha, 1996), pp. 171–172.
16) Hiroshi Okumura, "Shoken" [Securities], in Heiwa Keizai Keikaku Kaigi, Dokusen Hakusho Iinkai, *Baburu Keizai to Ginko, Shoken* [Bubble Economy, Banks, and Securities] (Tokyo: Ochanomizu Shobo, 1993), pp. 105–109.
17) Nihon Keizai Shimbunsha, *Kabu wa Shindaka* [Did Stocks Die?] (Tokyo: Nihon Keizai

Shimbunsha, 1991), p. 109.

18) Yonezawa, *Kabusiki Sijo no Keizaigaku*, pp. 77–78.
19) Shiota, *Okurasho no Fukaku*, pp. 38–48; Takashi Tachibana, *Dojidai wo Utsu* [Criticizing the Contemporary Affairs] (Tokyo: Kodansha, 1988), p. 268.
20) Tachibana, *Dojidai wo Utsu*, pp. 269–274.
21) Shiota, *Okurasho no Fukaku*, pp. 49–61; Hanson, *Okura Erito Hokori to Guko*, pp. 107–117; Yasuharu Ishizawa, *Za MOF* [The Ministry of Finance] (Tokyo: Chuo Koronsha, 1995), pp. 276–278; Juzo Arihara, *Okurasho Yuragu Soshiki to Seisaku* [The Ministry of Finance: Its Institution and Policy Waver] (Tokyo: San-ichi Shobo, 1996), p. 112.
22) Asano, *Tohshika kara Mita Kabushiki Shijo*, pp. 10–11.
23) Hitoshi Noguchi, *Nichi-bei Tsuka Kosho 2000 Nichi* [Negotiations on Currency between Japan and the U.S. for 2000 days] (Tokyo: Nihon Keizai Shimbunsha, 1995), pp. 229–230.
24) Kamikawa, *Keizai Seisaku no Seijigaku*, Ch. 3.
25) Sato, *Dokyumento Kin-yu Hatan*, pp. 343–345.
26) Kamikawa, *Keizai Seisaku no Seijigaku*, Ch. 3.
27) Concerning the relation between asset-price bubbles and commodity prices, there is an opinion that massive bubbles require stability in commodity prices. This argument is structured as follows. That is, central banks tighten monetary policy as commodity prices rise. Thus, if commodity prices rise, monetary policy does not continue to be eased and asset prices do not continue to be inflated. Yutaka Kosai, Osamu Ito, and Ritsuko Arioka, "Baburu-ki no Kin-yu Seisaku to sono Hansei" [Monetary Policy in the Bubble Period and Reflection on it], in Yutaka Kosai, Masaaki Shirakawa, and Kunio Okina eds., *Baburu to Kin-yu Seisaku: Nihon no Keiken to Kyokun* [Bubble and Monetary Policy: Experiences and Lessons of Japan] (Tokyo: Nihon Keizai Shimbunsha, 2001), p. 133. This argument fits countries whose central banks are independent of their governments. In countries whose central banks are dependent on their governments, the governments may compel them not to tighten monetary policy even if commodity prices rise. This holds true with the economic bubbles experienced in the Scandinavian countries in the late 1980s
28) Hiroshi Yoshikawa ed., *Kin-yu Seisaku to Nihon Keizai* [Monetary Policy and the Japanese Economy] (Tokyo: Nihon Keizai Shimbunsha, 1996), pp. 143–144.
29) Kazuhide Uekusa, *Kinri Kawase Kabuka no Seiji Keizaigaku* [Political Economy of Interest Rates, Currency Exchange, and Stock Prices] (Tokyo: Iwanami Shoten, 1992), pp. 36–37, pp. 93–94.
30) Kamikawa, *Keizai Seisaku no Seijigaku*, Ch.2.
31) Tsutomu Watanabe, "Menseki Joko Tsuki Kin-yu Seisaku Ruru no Suikei" [An Estimation of a Monetary Policy Rule with Exclusion Clauses], in Honda Yuzo ed., *Nihon no Keiki* [Japanese Business Conditions] (Tokyo: Yuhikaku, 1995), pp. 195–217.
32) Ueda, *Kokusai Shushi Fu-Kinko ka no Kin-yu Seisaku*, pp. 186–187; Yoshikawa ed., *Kin-yu Seisaku to Nihon Keizai*, pp. 143–144.
33) Alan S. Blinder and Janet L. Yellen, *The Fabulous Decade: Macroeconomic Lessons from the 1990s* (New York: The Century Foundation Press, 2001), pp. 12–13.
34) Tokyo Mitsubishi Ginko Chosashitsu, *Beikoku Keizai no Shinjitsu: Seicho no Dainamizumu wa Kenzai ka* [The Truths of the U.S. Economy: Is the Growth Dynamism Maintained?] (Tokyo: Toyo Keizai Shimposha, 2002), p. 41; Akinori Marumo, *Amerika Keizai Shijo Shugi no Genkai* [The U.S. Economy, The Limit of the Market Principles] (Tokyo: Chuo Keizaisha, 2002), pp. 101–102.

35) Blinder and Yellen, *The Fabulous Decade*, pp. 25–43. See also, Tokyo Mitsubishi Ginko Chosashitsu, *Beikoku Keizai no Shinjitsu*, p. 41; Marumo, *Amerika Keizai Shijo Shugi no Genkai*, pp. 102–103.
36) Marumo, *Amerika Keizai Shijo Shugi no Genkai*, p. 24.
37) Blinder and Yellen, *The Fabulous Decade*, pp. 6–9. That is to say, in the U.S., wage restraints were accomplished since trade unions were weak. This fits dualism theory and the hump-shaped model extremely well.
38) Blinder and Yellen, *The Fabulous Decade*, pp. 15–24.
39) Robert J. Shiller, *Irrational Exuberance* (Princeton: Princeton University Press, 2000), pp. 32–36; Yuichi Sato and Yasutoshi Nagai, *Amerika Keizai no Han-ei wa Tsuduku ka* [Is the U.S. Economic Prosperity Kept?] (Tokyo: Toyo Keizai Shimposha, 1999), pp. 90–92.
40) Nihon Keizai Shimbunsha, *Beikoku Seicho Shinwa no Hokai: Nyu Ekonomi wa Shinda ka* [The Collapse of the Myth of Economic Growth in the U.S.: Is the New Economy Dead?] (Tokyo: Nihon Keizai Shimbunsha, 2002), pp. 248–249.
41) Nihon Keizai Shimbunsha, *Beikoku Seicho Shinwa no Hokai*; Yoichi Takita, *Nihon Keizai Fu-Sakui no Tsumi* [The Sin of Omission of the Japanese Economy] (Tokyo: Nihon Keizai Shimbunsha, 2002), pp. 163–174.
42) Bob Woodward, *Maestro: Greenspan's Fed and the American Boom* (New York: Simon & Schuster, 2000), pp. 197–206; Sato and Nagai, *Amerika Keizai no Han-ei wa Tsuduku ka*, pp.76-78; Eisuke Sakakibara, *Nihon to Sekai ga Furueta Hi: Saiba Shihon Shugi no Seiritsu* [The Days when Japan and the World Trembled: Establishment of Cyber-Capitalism] (Tokyo: Chuo Koron Shinsha, 2000), pp. 50–65, pp. 70–73; Yoshiko Mori, *Beikoku Tsuka Senryaku no Hatan: Tsuyoi Doru wa Itsu made Tsudukuno ka* [The Collapse of the U.S. Currency Strategy: How Long will the Strong Dollar Last?] (Tokyo: Toyo Keizai Shimposha, 2001), pp. 110–117.
43) Woodward, *Maestro*, pp. 206–212; Sato and Nagai, *Amerika Keizai no Han-ei wa Tsuduku ka*, p. 78, p. 220; Yoichi Ito, *Gurinsupan wa Kamisama ka* [Is Greenspan God?] (Tokyo: TBS Britanika, 2001), pp. 116–119; Takita, *Nihon Keizai Fu-Sakui no Tsumi*, pp. 153–154.
44) Kunio Miyamoto, "Josetsu: Nyu Ekonomi to Amerika Keizai" [Introduction: The New Economy and the U.S. Economy], in Miyohei Shinohara ed., *Keizai no Teitai to Saisei: Gyakuten no Keiki wo Saguru* [Stagnation and Revival of Economy: Exploring Reverse Business Conditions] (Tokyo: Toyo Keizai Shimposha, 2003), p. 5.
45) Woodward, *Maestro*, pp. 110–112, pp. 166–178. See also, Blinder and Yellen, *The Fabulous Decade*, pp. 51–53.
46) Blinder and Yellen, *The Fabulous Decade*, pp. 54–55. See also, Takita, *Nihon Keizai Fu-Sakui no Tsumi*, pp. 153–154.
47) Sugiura, *Amerika Keizai wa Shizumanai*, p. 12.
48) Blinder and Yellen, *The Fabulous Decade*, pp. 38–43.
49) Tokyo Mitsubishi Ginko Chosashitsu, *Beikoku Keizai no Shinjitsu*, pp. 35–36, p. 59.
50) Tokyo Mitsubishi Ginko Chosashitsu, *Beikoku Keizai no Shinjitsu*, p. 37.
51) Tokyo Mitsubishi Ginko Chosashitsu, *Beikoku Keizai no Shinjitsu*, p. 41.
52) Mori, *Beikoku Tsuka Senryaku no Hatan*.
53) Blinder and Yellen, *The Fabulous Decade*, pp. 43–46.