

Why is Japan's unemployment so low?  
Social costs of "total employment"

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**1. Figure speaks**

Among the G-7 countries, the seven richest countries in the world, Euro-zone countries are suffering from high and persistent unemployment: 9.6% in Germany, 9.4% in France, 8.6% in Italy (according to the standardized unemployment rates of the OECD for 2003). Canada is following them with 7.6%. The US rate was 6.0% in 2003 and 5.4% in August 2004. President George W. Bush is claiming "the economy is strong and getting stronger," pointing to the employment situation. With 5.0% the UK is so proud that it asserts in official papers that "We now have one of the highest employment rates in our history and, for the first time in nearly half a century, the highest employment rate and lowest unemployment rate of the major industrialised countries."

Then, how bad is Japan's employment? In the 1980s, with the highest economic growth and the lowest jobless rate among the major industrial countries, Japan was shining, claiming "Japan as

Number One” or “Model Japan.” After the burst of the bubble boom in 1990, the era of “a lost decade” began, in which the growth rate was nearly zero and in some years below zero. In 1997, Japan was on the verge of a great depression, caused by financial crisis that led to a series of financial institutions’ bankruptcies, including a big city bank and one of the three biggest brokerage houses. Quite naturally, many Japanese were seriously afraid of losing jobs.

In 2002 and 2003 the labor market deteriorated further, recording the highest jobless rate after the war. How high was the worst jobless rate? It was 5.5%. Now reflecting a little bit the improving economy, it was 4.6% in June 2004. If George W. Bush can claim “the economy is strong and getting stronger” with a 5.4% jobless rate, Prime Minister of Japan, Junichiro Koizumi would claim “the economy is very strong and getting stronger,” though the Japan’s economy in reality is just going upward since January 2004 after the over-a-decade recession.

## **2. Features of Japan’s unemployment in historical perspective**

Historically, Japan’s unemployment was and, albeit to a lesser extent, unique. First, it was low, extremely low. In 1995, the jobless rate exceeded 3% for the first time after World War II. That is, it was always under 3% for a half century, including the era immediately after the war, in which the economy was totally destroyed and a huge number of demobilized soldiers and repatriates from the former colonies appeared on the labor market. Except for Germany in the 1960s, when it had to import laborers from within Europe and later from Turkey to solve a severe labor shortage, Japan’s unemployment was the lowest among the major industrial countries.

Second, Japan’s employment was not sensitive to the economic cycle. Hit by the first oil crisis in 1973 and the second one in 1979, German’s unemployment soared to 7.7% in 1983 from 0.8% in 1972. Not only Germany, but other major countries too, began to suffer from high unemployment in the stagnated world economy caused by the oil crises. The only exception was Japan. Japan’s unemployment increased slightly in the same period, from 1.4% to 2.7%. Despite the two oil crises and the high yen (*endaka*) in 1985, unemployment did not increase substantially. Japan’s economy was not vulnerable to external shocks.

## **3. Theories explaining low unemployment rates in Japan**

In the late 1940s and 1950s, a jobless rate lower than 2% was widely thought of as full employment, an ideal employment situation. But in Japan, seeing so many working poor, no one believed Japan’s lower-than-two-percent jobless rate meant full employment. To explain the low jobless rate, three main theories were presented.

### **The theory of “over-employment”**

An industry is defined as “over-employed” when its marginal productivity was always considerably lower than other industries in the economy were. The agricultural sector was regarded as a typical “over-employed” industry. Nearly half of the 16 million workers in the agricultural sector in 1950 was estimated as “over-employed.” This theory of “over-employment” was forgotten in the 1960s as Japan’s economy fueled high economic growth, reducing the employment share of the primary industry drastically, from 48% in 1950 to 17% in 1970. With rapidly declining agriculture, the theory of “over-employment” lost relevance.

### **The theory of “dualism”**

Japan's economy was characterized as a dual economic structure. On the upper level, there were big firms, offering stable employment and good working conditions. On the lower level, there were the self-employed and family workers, employees of Lilliputian firms, and temporary workers. For those workers, working conditions were miserable, with low income and very long working time. These people on the bottom were working poor, but not unemployed. The economic development in the 1950s benefited the upper level of the dual structure, but the sunlight could not penetrate the icy bottom of the dual structure.

This theory of "dualism" was questioned in the 1960s. Pointing out severe labor shortages during the period of high economic growth, critics insisted that wages increased so rapidly that low-wage small firms had to diminish because they were failing to recruit a workforce. Of course, there were still many small firms. But, there were no more traditional tiny firms, surviving only with low wages. Powerful medium-sized firms, critics insisted, grew up in the 1960s. The dual economic structure was replaced by a modern economic structure in the late 1960s and 1970s. Failing to counter this critique effectively, the theory of dual economic structure lost its influence in the 1970s.

### **The theory of "total employment"**

Very low unemployment can be interpreted either as full employment or as "total employment". While defining full employment as a state in which all job-seekers can find jobs suitable for them with fair wages, "total employment" is defined as a state in which all job-seekers can find jobs but not necessarily with fair wages nor suitable for them. Japan's low unemployment was "total employment," not full employment. A labor economist found that there were two types of workforces in Japan: a constant workforce and a peripheral workforce. Peripheral workforces move between being in the workforce and "not in labor force," instead of becoming unemployed. In an economic boom they have jobs. After leaving work in a recession, they do not seek new jobs and thus become discouraged workers, workers who are not classified as unemployed because they do not seek jobs voluntarily. Because of these peripheral workforces, Japan's unemployment has been kept low. Married women were the main peripheral workforce. The employment behavior of married women is strongly influenced by their families. For example, the employment behavior of a wife in a self-employed agricultural family cannot be the same as that of a wife whose husband is working in a big firm in a big city. The total employment argument hit the mark.

### **4. Three employment models and the peripheral workforce**

Among the working, married women, full-time workers account for one-third, part-timers for another one third, and self-employed and family workers for the remaining one third. Full-time working, married female employees are an expression of "individualism of the society". They tend to be unemployed, not discouraged workers, when they lose jobs. They are hardly peripheral workforce. From the viewpoint of supplying peripheral workforce, there are three employment models: the big-firm model, the self-employment model, and the small-and-medium-sized-enterprise (SME) model. Each model contributes to total employment in its own way.

#### **The Big-firm model**

Regardless whether it is a white-collar worker's family or a blue-collar worker's, when a husband is a regular employee in a big firm, normally he can get a "family wage," a wage sufficient to maintain the household of his family. In post-war Japan, to cover increasing

expenditures due to the aging of the population, big firms adopted the *nenko* wage system, combining a living wage and individual assessment. This *nenko* wage is a typical “family wage”. When the husband gets a “family wage,” his wife stays at home as a full-time housewife.

Even in a recession, big firms hesitate to downsize regular workers. They prefer labor hoarding to downsizing. Needless to say, it does not mean that big firms never fire employees. In companies severely hit by recession, the shipbuilding industry after the first oil crisis in 1973, for example, companies practiced “voluntary retirement.” In fact, “voluntary” meant half voluntary and half compulsory. Or in the protracted recession in the 1990s, many big firms implemented “early retirement” of employees, not only in their fifties but also in their forties or even thirties. Still, compared with Western companies, especially Anglo-Saxon companies, Japan’s big firms are reluctant to fire regular employees.

There are several historical reasons explaining the hesitant attitude of Japanese big firms to dismissals. First, many big firms, including very famous ones such as Toyota and Hitachi, experienced serious labor disputes in the late 1940s and the early 1950s. Nearly all issues were dismissals of regular employees. Experiencing these labor disputes, big firms realized dismissals as a highly sensitive issue in labor-management relations. Second, big firms did not feel a strong necessity to dismiss regular employees. Except for the longest-after-the-war recession in the 1990s, recessions ended in a short time. If the economy is expected to recover from recession in a short time, firms will hoard workers, because it is economical when hiring and training costs of new employees are taken into consideration. Third, big firms have employment buffers. Very long overtime is one of the buffers. By reducing overtime, firms can cut labor supply. Non-regular workers such as temporary, seasonal and part-time workers are buffers too. Fourth, judicial precedents have backed up long-term employment by restricting dismissals. Dismissals are legal only after all other measures to cope with a company’s slump are exhausted.

### **The Self-employment model**

Households of the self-employed are maintained by the total income gained by all family members, from husband and wife to grandfather and grandmother. Grown-up children often send money to support their self-employed parents. If a husband is self-employed, the wife works as a family worker, as seen typically in agriculture.

The self-employment model contributes to “total employment” by means of a flexible labor supply within family. In the self-employment model, the husband is not expected to be the sole breadwinner. The household should be sustained by mobilizing the whole family workforce, if possible. If business is good, the wife works with her husband. In an economic slump, the wife becomes a full-time housewife and waits at home until business recovers. As the wife does not want to find a job outside the home, she is not classified as unemployed. In fact, almost no one becomes unemployed after having lost a job

### **The SME model**

In the case of the SME model, the husband has a job in a small and medium-sized enterprise. In Japan, the wage difference between big firms and SMEs is much larger than in other industrial countries. Despite large wage differences, there is little difference in behavior as consumers between workers in big firms and in SMEs, investing much in education of their children and buying durable goods and real estate similarly. Therefore, families of SME workers need

additional income to maintain the household. So, wives work as part-timers.

The SME model contributes to “total employment” in two ways. First, in a recession, SMEs increase employment for two reasons. As working conditions are less favorable in SMEs than in big firms, they suffer from difficulties in hiring good employees. When big firms cut down new hiring in recessions, SMEs find relatively good chances to hire better employees.

Second, a more important contribution to the SME model is the employment behavior of married, female part-timers. After having lost jobs, most of them do not seek work and thus become discouraged workers. Because of housekeeping or taking care of children, the work time of married, female part-timers cannot be flexible. When they lose jobs, they become full-time housewives, waiting for suitable job news from friends or circulars.

In the self-employment model and the SME models, married women play a decisive role for keeping unemployment very low. They are marginalized as peripheral workforce, but they are essential for keeping men’s employment stable. Married women are a marginalized but key workforce.

## **5. Employment structure in history**

In Asia, Japan started industrialization earliest and became the only industrial country in this region. But, compared to Western countries, Japan was a latest-comer. Japan’s industrial revolution began after the major countries had already finished. In Japan’s economic development, as is common in other industrial countries, the employment structure shifted from primary industry to secondary industry, and later to tertiary industry. But, as the latest comer among the major industrial countries, Japan has had a very large number of self-employed and family workers. In 1920, the self-employed and family workers are estimated to have accounted for 70% of the total workforce, and in 1930 still 68%. In 1948, they accounted for 63% of the total workforce. The strongholds of the self-employed and family workers were agriculture and forestry. In the high economic growth from 1955 to 1973, the agricultural population decreased drastically due to the rural exodus of young people to urban areas. But this decrease was compensated to some extent by the increase of self-employed and family workers in cities. As a result, the proportion of the self-employed and family workers has been the highest among major industrial countries.

Self-employed and family workers declined in the high economic growth era. But since the late 1960s, female part-timers increased as if offsetting the declining self-employed and family workers. In Japan, to define who is a “part-timer” is nearly impossible. In Western countries, part-timers are those whose working time is shorter than regular employees. But in Japan, there are a considerable number of part-timers who are working as long as regular employees. There are also “part-timers” doing overtime. The “part-timer” is a person who is employed as a “part-timer.” This is the exact definition of the part-timer in Japan. However, there are no historical data based on this definition. In the Labor Force Survey conducted regularly by the Management and Coordination Agency, the number of employees whose weekly work hour is fewer than 35 hours is surveyed. Apparently, these data do not cover all part-timers, but no other data are available. Adding the female part-timers in this sense to the self-employed and family workers, since the early 1970s, the peripheral workforce is astonishingly stable at about 18 million. Japanese capitalism has had a stable peripheral workforce.

## **6. Downsizing in “a lost decade”**

Core workers in big firms, male, regular employees, have been decreasing since 1993. The number of male employees in firms with more than 1,000 employees and male civil servants fell to 9.3 million in 2003, from 10.2 million in 1993, a contraction of nearly one-million. Stable jobs are expected to decline further.

Japanese big firms are now downsizing their employment, but in a Japanese style. Big firms slim down regular employees mainly by reducing new hiring. In Japan, nearly all big firms have compulsory retirement systems, under which all employees have to quit their firms at 60 years old. As a certain number of old employees quit under this system automatically, big firms can reduce employment by limiting new hiring. Further, big firms offer an “early retirement scheme” to employees, not only in their fifties but also in their forties and thirties. If necessary, big firms take more drastic restructuring policies by separating unprofitable plants from their firms. The separated plants have to survive as independent firms.

With retirement of the managers and the labor union leaders who experienced severe labor disputes in the 1950s, downsizing of employees, once thought to be the most sensitive issue in Japanese industrial relations, is now becoming a less sensitive issue. But direct and massive dismissals are still avoided, fearing that corporate images would deteriorate among consumers. The reason is that Japanese companies that implement dismissals are regarded as bad and problematic ones that fail to maintain employment, and their stocks usually go down.

Self-employment is dwindling too. In 10 years, from 1980 to 1990, the self-employed and family workers declined 1.6 million to 14.0 million. From 1990 to 2003, they declined an additionally 4.4 million. The reduction is rapidly accelerating.

Self-employed agricultural workers are declining because of increasing competition from foreign agricultural products and weakening protection by the government. More important for waning “total employment” is the increasing shutdown of mom-and-pop retail shops. For many years, they had been protected by the Large-scale Retailer Law, which obliged large-scale retailers, before establishing large shops, to make an agreement on shop scale and operation time with small shopkeepers who might be strongly affected by a new large-scale retailer. The U.S. government criticized this law as a symbol of non-tariff barriers, blocking American large-scale retailers from entering into the Japanese market. Under strong pressure from the U.S., the law was revised with the intention of making the establishment of large stores easier. Due to the deregulation of large-scale retailers, small and tiny shops ceased their business, one after another. Hollowing-out of downtown is on the agenda all over Japan, especially in smaller cities.

Small shopkeepers are now aging. They are facing difficulties in finding successors. They gave higher education to their children, who tended to choose jobs as employees, not to be successors of their families’ shops or jobs. The protracted economic slump, competition-forcing deregulation and aging of the self-employed will further accelerate reduction of this sector.

In the past, SMEs had a dynamic development. Many SMEs retreated, but more SMEs launched their businesses. For example, in the period from 1981 to 1986, 216,548 companies died annually, and 230,967 were newly born, meaning an average increase of 14,419 firms every year. But from 1991 to 2001, fewer SMEs were launched than ceased to function, resulting in annual decrease of nearly 56,000 firms. As a whole, SMEs are contracting.

The protracted economic slump hit workers in the SMEs. Housewives need additional income

because their husbands' wages are stagnating or decreasing. Women part-timers tend to stay in the labor market as unemployed workers instead of leaving the labor force after they lose jobs. The mechanism of total employment based on discouraged workers becoming part-timers is weakening.

## **7. Concluding remarks**

Clearly, Japan's total employment is not desirable from the viewpoint of fairness, because it is possible at the cost of the marginalization of women workers. But, under severe economic conditions in the era of globalization, how is full employment possible? Japan is facing difficult and dismal options-- between total employment and high unemployment. Now the options given to us are between bad and worse, not between bad and good.

For Western countries, total employment cannot be a model for lowering unemployment. First, self-employment with family workers as employment buffers was already reduced to a minimum in the 1950s, only about 10% of the total workforce. Second, as a more important reason, discriminatory employment of women is already unacceptable. Using the female workforce as a buffer is not permitted, either legally or socially.

Some Western countries could increase employment mainly by creating low-wage jobs. They include the U.S., the UK and the Netherlands. Western countries that were reluctant to create low-wage jobs, such as Germany and France, are suffering from high unemployment. If this is true, how is full employment possible while avoiding low-wage jobs? In my view, Western countries too are faced with dismal options between bad and worse.

For developing countries, total employment can be a model for transition to industrial societies. It seems to me that the Asian NIEs - South Korea, Singapore, Taiwan and Hong Kong – experienced total employment. Recently, economists are focusing on BRICs – Brazil, Russia, India and China – as developing economies. They are vast in population and land. Income differences between the rich and the poor are also vast. Surely, size matters. Countries with over one billion population such as China and India have to have their own economic and social policies learning not much from the experiences of the industrial countries, instead of emulating the experience of the industrial countries.