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Striving to Make Japan a Nation of Innovation Chairman's Address at the Fiscal 2005 Annual Meeting

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Introduction: Looking Back on Fiscal 2004

Looking back on the past year, I truly feel that the Japanese economy has emerged from a long period of stagnation, and is finally recovering and moving from crisis to normalcy. Progress that has been made in disposing of non-performing loans held by financial institutions and the removal of bank deposit guarantees are symbols of this change.

However, since so much of this recovery is supported by forces in the external environment, such as the strength of the American and Chinese economies, we cannot take solace in the current upswing. In the present context, the underpinnings of Japan's growth might easily be shaken by factors that influence the global economy, such as political and economic conditions in the United States, China, and other countries, their relations with our country, and crude oil prices. To consolidate recent positive gains and ensure that these translate into self-sustaining growth, it is necessary for us to make further leap forward.

Considering our acute awareness of this state of affairs and our sense of crisis, we have no choice but to conclude that structural reforms in the public sector are still inadequate and constitute only a half step forward. Although work to tackle postal system reform, privatization of the Japan Highway Public Corporation, the "trinity" of reforms for local governments, and reform of the social security system demonstrates the will of the Koizumi Administration to promote change, this has not been sufficient to solve core problems and ensure that the Japanese people feel confident and secure about the future.

Also during the last fiscal year, corporations, which bear responsibility for the economy and society, were involved in scandals in which they betrayed the

public's trust. Along with this, a movement developed that newly questioned both the value of corporations and the very reason for their existence.

In view of this situation, I believe we are entering an age in which we must reject the past and pursue new challenges for the future. To achieve new growth, now is the time for us to work for bold, path-breaking change. In other words, we must pursue "innovation."

1. Striving to Make Japan a Nation of Innovation

(What is "Innovation"?)

I think that "innovation" has a definition that is much broader than can be fit into narrow categories such as science and technology or corporate management. It goes beyond past experience and produces something that is novel, original, and superior to what currently exists. It creates new value in the form of a revolutionary strategy, idea, technology, product, or service. Moreover, it uses this new value as a lever with which to bring great changes to society, and generates a driving force that produces dramatic development. "Innovation" can be said to be something that breaks with the past, challenges the status quo, and creates future value.

In terms of the changes it brings, which are discontinuous rather than continuous in nature, the progress it allows, which is not an extension of past, and the fact that it is accompanied by quantum leaps in development, I believe that "innovation" is unlike the process of "kaizen" (improvement) at which we have excelled in the past.

Of course, to bring forth Japan's competitiveness and energy, it is necessary to work to achieve continuous "kaizen" in all fields. However, to make bold policy shifts and resolve fundamental, systemic contradictions, it becomes necessary to combine "innovation" that rejects precedent and brings about discontinuous change with a strategy that ties this innovation to growth and development.

(The Source and Starting Point of Innovation)

The source of innovation consists, first of all, of a new technology or theoretical invention or discovery and the value creation that results from its application.

Looking back through history, it is clear in what form letterpress printing technology, the steam engine, electricity, and the Internet brought about dynamic changes in society.

In addition to tangible discoveries and inventions, the discovery of intangible value in the form of individual needs, demands, and values, also leads to innovation. Two good examples of this are the parcel delivery business, which developed from the new idea of “freight for individuals and homes” and the discovery of demand for this, and hybrid vehicles, which developed as a result of thorough consideration of the value of “coexistence between the environment and driving.”

New value can also be created through a combination of two heterogeneous things, or by introducing an unusual idea. In this way, the application of ideas for factory production to the food industry resulted in the emergence of a market for fast food, and a multiplier effect achieved through the combination of traditional shops and the Internet spawned a huge virtual market for online shopping.

The true essence of this type of innovation is not defined only by its ability to create new goods and services and make the impossible possible. I believe that it also lies in the fact that it works through the creation of new value to spread changes that affect individual values, relationships among people, and the framework of society, and then promote the next innovation.

(The Climate for Innovation)

Several essential factors are required for innovations to burst upon the scene and be promoted regardless of the country in which they emerge or differences in their historical or cultural contexts.

One of these is the need to establish the importance of innovation as a strategy to enhance a country’s competitiveness. It is also necessary to firmly entrench in society a shared awareness of the idea that in an age characterized by dramatic changes and unpredictability, meeting these changes head on and adapting to them are the very actions that create growth and energy.

In addition, it is essential to institutionalize this awareness, and work to transform the social system such that more emphasis is placed on promoting innovation.

When this transformation occurs, the idea at its core will be to construct a framework that supports efforts to engage in trial and error and explore the possibilities of the unknown, and rewards individuals who are successful in creating value. It will also entail the creation of a free and open society in which different or new things are accepted and diversity is fully exploited. In such a context, if one innovation emerges and produces benefits for society, new challenges and subsequent innovations that build on this will also likely emerge.

It is my firm belief that the future shape into which Japan must strive to transform itself is none other than that of a “nation of innovation,” where energy and allure are created through continuous innovation. The first step in this process is to produce a “chain of innovation” and reinvigorate the whole of society.

2. Three Innovations that Will Open a Pathway to Japan’s Future

To transform Japan into a “nation of innovation,” it is necessary to promote reforms throughout society. Of great importance in this endeavor is innovation in corporations and executives who have responsibilities for private sector-led society, in the social system and the public sector, and in the consciousness of individuals. The obstacles that must be overcome in each of these areas are likely different. In all of them, however, enthusiasm for innovation that explores new dimensions and efforts to deal with change are more important than anything else.

(Corporate Management Innovation)

A corporation’s primary mission is to provide “solutions” for the diverse needs of individual, ordinary people. To accomplish our most important mission as corporate executives to improve corporate valuation and innovation, we must foresee coming changes and put our corporations’ cultures, organizational structures, and systems of evaluation and compensation into perspective as we carry out our own reforms.

In addition, the role that business ventures have played in identifying new needs that often go unnoticed by existing markets and industries, and in applying innovative technologies and discoveries is extremely important. The

construction of a social environment that encourages the entrepreneurial efforts of individuals and the active creation of new businesses is also important for the promotion of corporate management innovation.

(Public Sector Innovation)

Of any part of Japanese society, it is the government and public sector where innovation is least accepted and reforms are making the slowest tangible progress. “Structural reform” that lacks real substance and is carried out only to preserve existing frameworks and interests does not merit being called “innovation.” The destruction of the biggest obstacle to change, vested interests, is a necessary first step in efforts to bring about bold innovation in the public sector.

The role for government bureaucrats to play from this point forward is to create an infrastructure and environment in which individuals and the private sector can pursue innovation. They must be conscious of the fact that their mission is to work diligently to build a system that will reward people who make efforts and take up new challenges.

To create a society in which individuals do not shrink back because of concerns about the future, but are instead able to energetically pursue new challenges, it is particularly important to immediately implement reforms of the financial and social security systems. In the sense that it will serve to promote diversity, self-reliant efforts, and ingenuity and creativity, all of which are sources of innovation, the entrusting of many of the central government’s financial resources and authority to local governments and the private sector is also an urgent task.

(Innovation of Individual Consciousness)

Unless we ensure that the vision of the society we hope to create and the significance of innovation penetrate the thoughts and consciousness of individuals, true social innovation will not occur. It is necessary to carry out bold reforms of our country’s education and human resource development system as well, and do so while remaining focused on the type of society we are striving to build – one in which diversity and differences are positively valued and self-reliant efforts and challenges to the status quo are rewarded.

3. Conclusion – What We Are Striving to Achieve

Faced with falling birth rates, rapid aging, a shrinking population, and limitations imposed on it by its lack of natural resources, Japan is working in difficult circumstances as it struggles to cope with the need to secure the sustainability of many of its domestic systems.

In such a situation, piecemeal “improvements” restricted by vested interests cannot provide an adequate response. Opening the door to Japan’s future requires that everyone, including those in government, in the private sector, and individuals in society, all keep the concept of “innovation” in mind and accelerate the pace of change.

Historically, we Japanese have displayed a talent for taking in new things and making them our own. The dogged pursuit of challenges and progress is a part of our society’s very genetic makeup. With this in mind, should we not now commit ourselves to proving that the past decade of economic stagnation was nothing but an aberration?

Our mission as corporate executives who have come together in the Keizai Doyukai is to work to achieve growth and development through innovation. However, we cannot hope to realize sustainable growth if social norms are violated and the public trust is betrayed. We want to continue to hold up the promotion of CSR management as a lofty ideal, and strive to carry out our own duties.

In addition, we want the membership of the Keizai Doyukai this year to share an awareness of what is required to bring forth innovation not only in corporate management, but in many different areas of society, including public finances, finance, politics, education, and diplomacy, while we work to expand our activities.

To increase the Doyukai’s cohesiveness and send an even stronger message, we intend to pursue innovations as well in our own organization and its operations.