Japan's industrial policy: made in the U.S.A.

by Richard Katz

In 1868 Japan was a poor, relatively barren set of islands, whose harsh land yielded food only to those willing to stand in the wet rice paddies, arduously planting and transplanting the seedlings. Its people eked out a living standard lower than Indonesia's today.

Suddenly everything changed: that year, a group of officials, *samurai*, and literati inspired by Western progress, but fearful of Western imperialism, took over Japan, determined to remove the fetters of 200 years of Confucian ideological dominance, to industrialize a land without raw materials, and above all to "catch up" to the West. Within less than four decades they had succeeded so well that, to the astonishment of the world, they defeated Russia in modern warfare. Two decades later, Japan's exports competed on the world stage.

All of this appeared to have come to naught in August of 1945. Japan lay in ashes—not only Hiroshima and Nagasaki, but even Tokyo, a victim of continuous firebombing. By 1946 Japan could produce at only 1/6 of prewar levels. Tokyo informed the U.S. Occupation that, without emergency measures, by March 1947 Japan would no longer be able to produce anything, "due to an exhaustion of stockpiles, a lack of imports, and an acute coal shortage." Faced with food riots by Japanese barely surviving on rations of 1,300-1,700 calories per day, Gen. Douglas MacArthur sent an urgent appeal to President Truman: "Send me bread, or send me bullets!"

Today, these images of Japan's past are hardly remembered. They are replaced with the silhouette of an "economic miracle," of a technological giant whose practices Americans are now asked to copy, lest the oriental nation overtake the United States.

Stunning as Japan's success may seem, its transition from feudal backwater to economic superpower was no unforseeable "miracle." This miracle was planned, the product of what is now called *sangyo seisaku*, or industrial policy. In other times and other lands it has been called by different names, including American System economics, dirigism, and cameralism. But the content remains the same: people, not invisible hands, determining the march forward of the nation.

Members of the 1872-73 Iwakura Mission, which sent 40 Japanese leaders to the United States and Europe to study modern ways. Second from left is Toshimichi Okubo, the architect of the 1868 Meiji Restoration and of Japan's rapid industrialization. Seated is Prince Iwakura, a noble in the court of Emperor Meiji and the new regime's prime minister.

What is Japan's industrial policy?

Many Americans, seeing Japan's success, are now debating whether the United States too should adopt industrial policy. In the course of this debate, at least three distinct, equally wrong, images of Japan's practice are generated, sometimes by the same economists who smugly proclaimed—or even welcomed—Japan's 1964-65 recession as the long-predicted end of its "impossible" effort to sustain double-digit growth.

One image, presented by Democratic Party economists like Robert Reich or Lester Thurow, projects onto Japan what they propose here: phasing out alleged "sunset" basic industries, such as steel, through "depressed industry cartels"; and phasing in "sunrise" electronics-computer industries through R&D subsidies and tax incentives. In the second image, Japan Inc. uses government subsidy to build up export-oriented growth industries, giving these sectors a competitive advantage they would not otherwise enjoy. The third, equally misleading, portrayal is often presented by the Japanese themselves to avoid the "unfairness" charges. The claim is Japan really does nothing different; some ads and government statements imply they are even more obedient to "free enterprise" than America since the ratio of state-funded R&D is so much less in Japan.

To help set the record straight, in order to provide the background for a real debate on proposals for an American industrial policy, this *EIR* special report will examine three topics:

1) What Japan's industrial policy is;

2) How Japan learned it from America in the 19th century;

3) The "nitty-gritty" of industrial policy tools: how Japan was transformed into an economic superpower.

The basic principle of Japanese industrial policy is quite straightforward: It is *maximum leverage*. Through government-banking-industry cooperation, resources are allocated to frontier, growth industries—industries whose development over a 10- to 20-year period propels the entire economy forward technologically; industries which increase the ability of each worker to develop greater skill and produce greater output. Sectors are chosen for development, not for their own productivity, but for their ramifications for the entire economy.

Through the Industrial Structure Council of the Ministry of International Trade and Industry (MITI), Japanese officials and industrialists decide jointly what kind of industrial/technological/labor structure Japan needs on a 10-, 20-, or even 30-year horizon. They then choose key leveraging industries because the *process of developing those sectors* is the most effective way to transform Japan in the desired direction. Those sectors get special investment tax benefits, low-interest credit from government agencies, priority for private bank credit, and government/industry funds for research and development. Special aids are applied particularly to sectors in which it takes years to recover investment, and where short-term "market forces" alone might not dictate a large enough allocation of resources.

Early in the postwar period, Japan's leaders decided to