

CIRJE-F-1

**'Market' and 'Marketization':
From the Japanese Experience**

Yoshiro Miwa
Faculty of Economics
The University of Tokyo

May 1998

Discussion Papers are a series of manuscripts in their draft form. They are not intended for circulation or distribution except as indicated by the author. For that reason Discussion Papers may not be reproduced or distributed without the written consent of the author.

'Market' and 'Marketization': From the Japanese Experience

Yoshiro Miwa

At least until very recently, with various reasons, many, particularly those in and around the governments both in developing economies and former socialist economies, have studied the past history of Japan to draw lessons for development strategies and/or the 'marketization' of a command economy to a market economy. Talk about Japan's economy, however, is full of misconceptions, and this movement, often emphasized with a phrase 'East Asian Miracle', is based upon false ideas: at least before the 1970s the Japanese economy was a command economy, undeveloped market economy directed from the top (MITI and Ministry of Finance); the role of the government has been great in recovering from the war destruction and in promoting her economic growth. Japan is well known for a vast number of active small business, the creation and development of which many economies recognize as critical for economic development and 'marketization'. Focusing upon small businesses and the government policies for them during Japan's Transition Period, 1945-1955, the period between the war destruction and the 'high growth era', this paper describes in detail the past history of small business, the environment conditioned them, and the role of small business policies. A special focus is placed upon the machine tools industry, which suffered from the transition the most seriously and also has been the basis for the Japan's postwar industrial success. This paper concludes that the most important lesson the governments of the developing economies and/or transition economies should learn from the Japanese experience is that imposing inappropriate restrictions on the market mechanism and using it inexhaustively, whatever may be the reason, will incur tremendous cost to consumers over a long time.

*'Market' and 'Marketization': From the Japanese Experience*¹

Yoshiro Miwa

(The University of Tokyo, Faculty of economics)

Address: 7-3-1, Hongo, Bunkyo-ku, Tokyo, 113-0033, Japan

Tel: (81)-3-3812-2111, ex.5622

Fax: (81)-3-3818-7082

E-mail: miwa @e.u-tokyo.ac.jp

CONTENT:

- [I]. Preface and Introduction
- [II]. Historical Background and Description of the Problem
- [III]. The Role of the Government in Creating and Supporting Small Businesses
- [IV]. Machine Tool Industry
- [V]. Policies for Small Business
- [VI]. Conclusion

[I]. Preface and Introduction

If we can agree that the economic problem of society is mainly one of rapid adaptation to changes in the particular circumstances of time and place, it would seem to follow that the ultimate decisions must be left to people who are familiar with these circumstances, who know directly of the relevant changes and of the resources immediately available to meet them... We must solve it by some form of decentralization. But this answers only part of our problem. We need decentralization because only thus can we ensure that the knowledge of the particular circumstances of time and place will be promptly used. But the 'man on the spot' cannot decide solely on the basis of his limited but intimate knowledge of the facts of his immediate surroundings. There still remains the problem of communicating to him such further information as he needs to fit his decisions into the whole pattern of changes of the larger economic system. (Hayek, 1945, pp.524-25)

Preface

This statement, which Friedreich von Hayek wrote several years before the birth of the People's Republic of China, came to my mind when I was requested to present a paper on "market" and "marketization" at this Japan-China Joint Research Conference. Over the past several decades, the world has witnessed a wide variety of experiments in solving the Hayek's 'economic problem of society,' from which we have much learned. The focus of our discussion has moved much toward decentralization and the market. Today it is placed upon the "market" and "marketization", more specifically, how to 'introduce' and 'control' the functioning of

¹ Revised version of the paper presented at the Japan-China Joint Research Conferences, 29-30 November 1996 in Tokyo and 10-11 November 1997 in Beijing, on 'Market' and 'Marketization' jointly-organized by the Research Institute of Industry and Economics of the Department of Economics, The University of Tokyo, and Chinese Academy of Social Sciences, which again is based on Miwa[1996c] prepared for the Conference on the 'Marketization' of East European Countries sponsored by European Bank for Reconstruction and Development. The author gratefully acknowledges the conferences participants for their helpful comments and suggestions, particularly Dr. Robin Burgess and Professor Katsuji Nakagane for their strong and constructive instructions on the organization and direction of the present paper. The Japanese version is also available as Miwa [1998b].

markets and how to 'manage' the transition process from a command economy to a market economy, instead of the classical one, 'the superiority of socialism or communism over capitalism'. It applies not only to former socialist economies but also to many market or 'capitalist' economies, for instance, the UK which experienced a series of privatization and dramatic deregulation of the former nationalized enterprises² and the USA with drastic deregulation in many industries over two decades. Of course, Japan is no exception.

'Administration reform' and 'deregulation' were the most favored political slogans in Japan in the 1996 October election for the national Diet, symbolizing that they are the agenda in politics the people recognize as the most urgent and important for their life. Throughout the postwar period, the role of the government has been one of the central issues in the political debate in Japan. As is the case everywhere, in Japan the centralized power, particularly that of the government, has ill-performed so much in adapting rapidly and smoothly to changes in the circumstances over time and place than the market would have been, quite often backed by specific vested interest groups, sacrificing the consumers' interest. With time people has become keenly aware that more deregulation and/or 'marketization' is essential for their standard of living, the delay of which costs huge, resulting in a strong demand for 'administration reform and deregulation'.³

We learn much from the history. With various reasons, some of which are totally false, many, particularly those in and around the governments in former socialist economies, study the past history of Japan to draw lessons for the 'marketization', or the transition and the transformation, of a command or a government-led economy to a market economy. My recent experiences, particularly those in joining two such research projects, lead me to a conclusion that the most productive contribution of mine to this conference is to discuss Japan's past history, placing focus upon the functioning of the markets with special reference to the position of small businesses and the government policies for them. The World Bank research project was organized and designed on a false presumption that the Japanese government has had strong power to intervene into the private sector and has actually intervened continuously, which was one of the main engines of Japan's industrial success. Upon request, I contributed a paper on Japan's small business policies, Miwa [1995a], with the following conclusion: Although the scope of Japanese policies for small businesses is extensive, they have not effectively supported small businesses. Neither, therefore, have they stimulated Japan's overall economic growth.⁴ Any lessons to be learned from the Japanese experience are therefore negative: it is of no use to imitate Japanese policies for small businesses. To learn why so many small businesses now exist in Japan, we should search for causes and mechanisms other than government polices.⁵

For the conference in 1996 on 'Policy Studies to Promote Private Sector Development', the European Bank for Reconstruction and Development (EBRD) asked me to write a paper on 'Small Business in Japan During the Transition Decade, 1945-1955: Lessons for Eastern Europe', Miwa [1996c], on which the present paper heavily depends, focusing on the government policies in creating a huge number of vital small businesses, particularly within the manufacturing sector. This request comes from two types of recognition. First, the transition

² For privatization and deregulation in the UK, see Vickers and Yarrow [1988], Foster [1992], Armstrong, Cowan, and Vickers [1994], and Bishop, Kay, and Mayer eds. [1995].

³ For the details of the recent deregulation and related controversy, see Miwa[1997b].

⁴ For the clearer statement of the view, although in Japanese, see Miwa[1998a, Chapter 3].

⁵ The final report, Kim et als. eds. [1995], separated my paper in a part with a title 'The View of A Pessimist', which includes no other paper.

toward a market economy is to be realized with entry and growth of a huge number of small businesses, which compete with large 'nationalized' enterprises, forcing them to adapt to changing circumstances, and providing newly born unemployed with workplaces. Thus, the creation of small businesses, particularly in the manufacturing sector, and the support of their activities is vital for the success of the transition. Many observe that, although so many small businesses have appeared in the distribution sector, the number of small businesses in the manufacturing sector has been so small. Second, every developed economy is dominated by small businesses, and Japan and Italy, above all, are well-known for their vital small businesses. Moreover, Japan is famous for its effective 'industrial policies,' and many believe that at least before the 1970s the Japanese system was heavily directed from the top. This recognition naturally leads to a question that how so many vital small businesses were created in Japan by the government policies. My argument again shocked and disappointed the conference organizer. Symbolically, the central slogan of Japan's small business policies over several decades has been the struggle against the 'excessive competition' in small business sectors, where most recognized that there have been too many small businesses. Thus, instead of creating new small businesses, in Japan how to handle with their 'excessive' existence has been the central policy issue.

In this paper, I deal directly neither with 'market' nor 'marketization.' I am deeply interested in the functioning of the markets and the role of the government in China and its relations to the markets. However, I have an interest neither in the definition itself of China's 'market socialism' nor in whether it is still a 'socialism.' I deal only with the Japanese experience, focusing on the behavior of small businesses, with special reference to their surroundings which were for or against their behavior, their responsiveness to changing environments, and the government policies for them. As false information often leads us to false policy lessons, like a recent introduction of 'mainbank system' to China,⁶ this paper will provide a sound ground for the future research on 'marketization.'

Introduction

Every economy is worth a close study to draw lessons for economies in transition from a centrally-controlled toward a de-centrally market-led; so is the Japanese economy. Japan's economy deserves a special attention for five reasons. First, it realized a rapid and long-lasting economic growth, over several decades from an underdeveloped stage to an economy with one of the highest per capita income. Second, prior to the well-known 'high growth era' since the latter half of the 1950s, it experienced both a decade since the second half of the 1930s of wartime control and destruction and that of hard days of transition between 1945 and 1955.

⁶ Taking Japan's 'mainbank system' as a reference, People's Bank of China, the Central Bank of China, issued in June 1996 the 'Basic Rule for Loans,' which stipulates that a company receiving loans has to establish 'mainbank' relationship with a bank in the district where the company has the basic registration, requested by the Commercial Bank Act. For this purpose the Bank issued in August the 'Mainbank Regulation Rule'. Under a 'Bank-Company Cooperation Agreement' between a bank and a company, the mainbank is obliged to provide the borrower with financial services concerning with settlement and liquid money, technology improvement funds, and so forth. The scheme started in the middle of 1996 with 300 companies among 1,000 companies the State selected for their strong support. The Bank appointed the mainbank to each company, referring to the past loan and settlement history. The Industry and Commerce Bank was appointed as the mainbank to 240 companies among 300. The author thanks Mr. Ken'ichi Imai of the Asian Research Institute for the information in this note. Many literature suggest that 'Japan's mainbank system' would be a useful reference for developing economies, among which Aoki and Patrick eds. [1994] is a representative. On Japan's mainbank system, see Chapter 6 of Miwa [1996a].

Third, through the growth it achieved a complete transformation of industrial structure, from an economy of agriculture and textile manufacturing to that of machinery manufacturing and services. Fourth, throughout the transformation process, it has been dominated by small businesses, rather than now internationally famous big companies such as Toyota, Nissan, Honda, Hitachi, Toshiba, Panasonic, and Sony. Now the recognition that a huge number of small businesses supported and made Japan's industrial success possible gained a worldwide attention. Fifth, as many argue that the government has controlled the economy and led the growth, its role and policy tools for the transformation and growth gather a wide attention, often with a phrase: 'East Asian Miracle', or simply, 'Asian Miracle.'

As briefly mentioned below, talk about Japan's economy is full of misconceptions. Worldwide attention on Japan's economy and related issues asked for this paper, therefore, are basically ill-defined and wrongly-directed, and Japan's economy in the following discussion is different from a generally understood and expected picture. In reading what follows, note two points which are mutually dependent. First, basically Japan has been a market economy for a long time, of course since the prewar days. Even under the wartime control, Japan's economy was a market economy, rather than a command economy similar to those we observed until very recently in the former socialist economies. Second, the role of the government has been by far smaller than is generally understood. These points are crucial particularly in understanding both how the economy was run during the transition period and how such a huge number of active small businesses were born and supported and made the rapid growth possible. Even at the first stage of the 'high growth era', industries were equipped mostly with very old machine tools with low quality, and with the industry expansion they improved the quality by introducing new machines. Quite often readers suffer from a vague belief like Krugman [1994, p.142] that: 'There is no question that before the early 1970s the Japanese system was heavily directed from the top, with the MITI and the Ministry of Finance influencing the allocation of credit and foreign exchange in an effort to push the economy where they liked.'⁷ We are now observing a new product or idea, a development model, exported from Japan, particularly by those who are in and around the Japanese government, that for the economies in transition the Japanese postwar experience must be very instructive and we should draw lessons from it, suggesting a strongly interventionist role of the government, with a phrase '(East) Asian Miracle.'⁸ As readers learn below, those views are totally false, and drawing lessons from Japan's experience could be harmful when it is done on those grounds.

The central questions are, first, how well the market has worked in Japan, and, second, what was the role played by the government during the time of transition and growth. For this, focus is placed upon two sectors of the economy during the transition period of 1945-1955, the small business sector in general for their crucial role in the economy, and the machine tool industry for two reasons: first, the machine tool is basic to the machinery industry development;

⁷ Many Japanese as well share the view, like Okazaki and Okuno-Fujiwara [1993, p.12] who argue, referring to The Industry Stabilization Act (*tokuan-ho*) of 1978 and The Structural Improvement Act (*sanko-ho*) of 1983, as follows: "Those policies for "competition control" and "planned resource allocation" are what the government inherited from the wartime plan-and-control system. The postwar industrial policy differs from the wartime control merely in the objective, economic independence and economic growth instead of wartime mobilization, and in the policy implementation system, decentralized inducing system with diversified soft-type methods instead of command-control system, making excessive competition visible.'

⁸ World Bank [1992] and a series of World Bank Research projects on the Japanese experiences, resulting in Aoki and Patrick eds. [1994] and Kim et als. eds. [1995] and etc., are the representative.

second, the transition period was the severest for this industry, and their experience must be most informative for economies in transition. As everybody understands, these are hard questions to answer. Three observations should be noted: (a) the high profitability of small business must have induced many to begin new operations; (b) there were little expectation of government's support and high rewards from old jobs and positions, and many people by themselves searched for a new way of living; (c) after a decade of transition hard days many launched into the venturous high growth process only with old equipment. Fortunately, the government was unreliable enough to let people look to the market for solution, but reliable enough to maintain the social stability. Thus it was not too weak, but not too strong.

Section II provides preparatory information for the discussion in the order of high growth in the prewar and in the postwar period, transformation in industrial structure and dominance of machinery industries, the transition decade: 1945-1955, dominance of small businesses, how the market worked in the prewar Japan, and the role of the government and industrial policy. Section III discusses the role of the government in creating and supporting small businesses. Section IV places focus on the machine tool industry, as an example for illustration. Section V is a brief description of the content of small business policies and their implementation process, referring to one specific local government, Hyogo Prefecture. Section VI is a brief summary and concluding remarks.

[III]. Historical Background and Description of the Problem

Studies of the Japanese economy abound, but few provide a good introductory overview, letting talks about it full of misconceptions, upon which not only political debates but also academic works heavily depends. This is partly because interest in Japan's economy has intensified as its industrial success has become well-known since the 1970s and especially in the 1980s. Interest in Japan is predicated upon a taste for the exotic and the expectation at home and abroad that Japan is and should be different from Western countries. The strong demand for the Japan-is-different-view has been satisfied by those with similar beliefs. To perform the assigned task, I have to begin with providing minimum information in order to clarify what are the real agenda.

High growth both in the prewar and in the postwar period

Japan's 1990 GDP was more than half that of the USA and was larger than the remaining Group of Seven industrialized nations.' As shown in Table 1 Japan's per capita GDP was this year the highest of the Group with Germany. In 1980 the situation was almost the same. Even in 1970, at the mid-way point between 1945 and today, Japan's per capita GDP was catching up with that of Europe. In 1960, however, Japan's per capita GDP was the smallest of all the G7 countries, only a third of the UK, Germany and France.

----- Table 1 -----

Although Japan's per capita GDP grew the fastest among the G7 countries from 1973, its growth rates was even higher in the 'high growth era' of 1951-73. Table 2 shows the five year average real growth rate of GNP between 1945 and 1980.

----- Table 2 -----

The Japanese economy has grown at a remarkably rapid speed, not only since the war but also before. Between 1913 and 1929, for example, Japan's real per capita income increased 46%, compared with the 36% growth over the same time period in France, the second fastest-growing country among today's G7 members.

Transformation in industrial structure and dominance of machinery industries

As symbolically shown in Table 3, postwar Japan's industrial success can be characterized by the machinery industries, whose ratio of exports to total exports of all industries in 1970 was 46.3%, almost double the 25.3% of 1960, and four times the 10.5% of 1950. In the prewar Japan, textile products such as cotton yarn, cotton fabric, silk yarn, and silk fabric, with agricultural and mining products, were the main export items. Thus Japan's long-lasting rapid growth was achieved over the complete transformation in industrial structure.

----- Table 3 -----

Rapid growth of machinery industries began in the prewar period; the ratio of machinery exports to total exports was already 13.0% in 1940. As shown in Table 4 production of machinery items reached its peak before the Second World War and rose rapidly again after a wartime lull. Different products emerged successively, starting with electric fans, sewing machines and binoculars, followed by cameras, radio receivers, monochrome televisions, bicycles, clock and watches, and then motorcycles, three-wheeled trucks, ships, cars and various other kinds of electrical and industrial machinery including machine tools.

----- Table 4 -----

The transition decade: 1945-1955

For Japan the first postwar decade was a difficult transition due to materially and politically unstable circumstances, where the policy effort of the newly established government was devoted exclusively to securing social stability, including safety and stability of life, and secure supply of basic materials such as food and energy, and it could not be active in developing specific sectors of the economy, like the small business sector. As shown in Figure 1 only in 1957 did real per capita income exceed the 1939 prewar peak. Total GNP topped the prewar level in 1954. It was the 1956 *Economic White Paper* that solemnly declared: 'No longer are we in the postwar age. We are now facing a new, different situation.'

----- Figure 1 -----

From 1945 to 1952, Japan was under occupation. The Potsdam Declaration which Japan accepted was announced as the result of the Allied summit conference held at Potsdam in July 1945. It stated that:

'There must be eliminated for all time the authority and influence of those who have deceived and misled the people of Japan into embarking on world conquest, for we insist that a new order of peace, security and justice will be impossible until irresponsible militarism is driven from the world./ Until such a new order is established *and* until there is convincing proof that Japan's war-

making power is destroyed, points in Japanese territory to be designated by the Allies shall be occupied to secure the achievement to the basic objectives we are here setting forth./ Japan shall be permitted to maintain such industries as will sustain her economy and permit the exaction of just reparations in kind, but not those which would enable her to rearm for war. To this end, access to, as distinguished from control of, raw materials shall be permitted. Eventual Japanese participation in world trade relations shall be permitted.' (Paragraphs 6, 7, and 11)

Particularly in the first few years of the occupation, the policy was hostile to the established business firms. A special emphasis was placed on eliminating the concentration of economic power, so-called *zaibatsu*.⁹ Also in many sectors, a large amount of the production capacity, (such as shipbuilding, machine tool production, iron and steel, and bearing manufacturing), was designated as means for reparation payments, and could not be used for production purpose. The Interim Reparations Policy (Pauley Report, 6 December 1945) revealed the objective and size of reparations policy, which, being considered to be too severe, strongly shocked both the government and the business people. It included the following statement:¹⁰

'The fact is that Japan's industrial equipment was overwhelmingly designed for war. Despite all the destruction, Japan still retains, in workable condition, more plant and equipment than its rulers ever allowed to be used for civilian supply and consumption even in peaceful years. That surplus must be taken out. ... In steel, and in machine tools and other machinery made from steel, Japan's own figures show that she still has, in workable condition, more than twice the facilities that she had when she invaded Manchuria in 1931.'

International trade, of both imports and exports, was restricted, which is part of the reason, and Japan had a foreign currency shortage and could not import basic materials for production expansion.

Dominance of small businesses

⁹ At the beginning of the Occupation, General MacArthur was instructed that, under the US policy, 'you will require... to submit, for approval by you, plans for dissolving large Japanese industrial and banking combines or other large concentrations of private business control.' A series of deconcentration policies, such as the Zaibatsu Dissolution, the Elimination of Excessive Concentration of Economic Power Act, the Antimonopoly Act, and the Economic Purge, was introduced and planned to implement in a massive scale. The Holding Company Liquidation Commission, for instance, first designated 'Big Four' *zaibatsu* and Fuji Industries, and the number of the companies on the target list amounted to 83 by July 1947. The Elimination of Excessive Concentration of Economic Power Act enacted in December 1947 designated 325 companies as the target by February 1948. With the development of Cold War, however, they were implemented in a drastically reduced scale. Only 18 companies, of the 325 companies previously designated as the target, remained at the last stage on the list of the Excessive Concentration Elimination Act, of which 11 companies were ordered to split. It took almost twenty years when the Antimonopoly Act was accepted by the Japanese people and became effective. There is a popular understanding that these deconcentration policies contributed much to Japan's postwar growth, which however extremely overestimates their policy effects. See Miwa [1993].

¹⁰ Ministry of Finance [1982, p.442]. For the description of the situation and the circumstances, see Ministry of Finance [1984] and Ministry of International Trade and Industry [1992].

The Japanese economy has been dominated by small businesses¹¹ throughout the postwar period. In 1991, 99.1% of the 6.5 million private sector establishments in Japan were small businesses.¹² 79.2% of the 55 million people employed in the private sector were employed by small businesses. Limiting our attention to the manufacturing sector, we find almost the same picture. In 1991, 99.4% of the 857 thousand establishments were small businesses. 73.8% of the 14.1 million people employed in manufacturing were employed by small businesses. The corresponding figures for the manufacturing sector in 1957 were 99.6% and 72.3%, respectively, which suggests the stable predominance of small business. Throughout these 30-40 years, more than 55% of the Japanese economy's value added has been produced in the small business sector. As shown in Figures 2 and 3, both the number of firms and employees in each size category grew constantly at almost the same speed as the total.

----- Figures 2 and 3 -----

Even in the first postwar decade, the number of small business increased and they rapidly began exporting some of their products, such as textiles, sewing machines, binoculars, and cameras. In some cases, Japanese small business were so competitive that foreign governments requested the Japanese government to force a floor price so that export prices would not drop too low.

The two decades since the second half of 1950s were the high-growth era of Japan's economy, which was led by the growth of machinery industries, such as shipbuilding, automobile, and electric and electronic products. In these industries, a well-developed division of labor among firms contributed much to the success. There was a vast number of small businesses actively playing central roles in the development process, by cooperating both among themselves and with large firms.

How the market worked in the prewar Japan?

Thus we reached our central questions: how did the market work? and what role did the government play within the market? For answering these questions in the following sections, we have to add two points. One of the popular misconceptions about Japan's economy is that before a certain time period, for example 1970, it was a command economy where the government controlled every side of business decisions, including new entries and investment expansion. This is a totally false idea, which make it impossible to understand Japan's economy in the transition period.¹³ I show here only Figures 4 and 5 with brief description of the state,

¹¹ The definition of small businesses depends on the type of industry. In manufacturing, mining, etc., small businesses include enterprises with ¥100 million or less in paid-in capital, or 300 or fewer employees. It is a traditional custom in Japan to use 'medium and small-sized' businesses instead of small businesses, but I choose 'small business' in order to eliminate misunderstanding and confusion.

¹² Establishments in agriculture and fishery are excluded. Those figures are from *Establishment Census*, and therefore, to be exact, they are different from the number of firms. For instance, a firm with five plants and a head office is counted as six establishments in this statistics. Most small firms, however, have only one establishment.

¹³ In postwar Japan Economic Planning Agency has always prepared medium-term plans for the national economy, on average a five-years-plan in every two to three years. Many argue that it is a symbol of Japan's command-economy-type character. 'Plans' have existed, those who were directly concerned with 'plans' tend to emphasize their importance by far than the actual, and official documents provided by them have the same tendency, with which so many directly draw conclusions, some totally depending on official documents and statement. As Komiya [1990, p.284] points, 'Japan's national economic plan should be interpreted as a long-term forecast, with some flavor of wishful thinking by the plan-makers,' and 'nobody considers the national economic

expecting interested readers to read Miwa [1996b] or Miwa [1998a, Part I]. Figure 4 shows the volume of annual machine tool production during 1930-1968, both in the number of units and in the total weight of machines produced. Figure 5 shows the number of plants in each employees size category during 1930-1942. With the explosion of weapon procurement, between 1931-1938 machine tool production grew thirty times in terms of number of machines produced and almost fifty times in terms of the total weight of machines produced, and the number of plants in each size category also increased dramatically at almost the same pace. The production increase was particularly impressive between 1936-1938. It was only in July 1938 when the government enacted a special law to support machine tool production and designated 6 firms as the direct objectives for policy support, whose number increased to 21 in May 1941. Thus most firms were outside the government support, making their entry and investment decisions independently, and even in Fiscal Year 1941 (April 1941 - March 1942), 21 designated firms' total share in machine tool production was only 23.0% in terms of the number of machine produced and 41.4% in terms of value.¹⁴ Note that in 1939 there were 2,730 plants over with ten employees in metalworking machinery manufacturing industry, including machine tool manufacturing industry.¹⁵

----- Figures 4 and 5 -----

plan as a rigid, binding plan with which must be followed by the government...There is not much substance in the national plan which can be usefully referred to which government ministries and agencies make important policy decisions in their respective fields....This is similar to a long-range (one to three months) weather forecast announced once or twice a month.'

For some time after the publication of Income Doubling ten-year plan in December 1960 'it became fashionable among larger companies to publish their own overall long-term management plan for a five- or ten-year period. When making company's plans, the national or sectoral rate of growth was taken for granted...and each company added a plus factor to the industry average rate of growth, hoping for an increasing market share for itself. But here again in practice few companies paid much attention to their long-term plan in making actual investment decisions, since most such plans turned out to underestimate growth potentials' (*ibid*, p.286). Before the Oil Crisis, the government plans consistently underestimated the growth potentials, however, as I concluded in Miwa [1996a, Chapter 9], MITI's investment coordination program, in the steel industry for instance, based on long-term plans prepared for their 'Long-term Credit Plan' had only a negligible impact, if any, on individual company's investment behavior.

Okazaki and Okuno-Fujiwara [1993, p.18], referring to the wartime control, argues as follows and emphasizes its continuity to the postwar economic system, which, however, is based on an misunderstanding about the basic character of postwar economic planning: 'The economy was covered with the control web based on those laws and ordinances mentioned above, which implies that resource allocation function of the market was restricted. A variety of economic plans of the government were the basis of the control, substituting the market's resource allocation function. The Material Mobilization Plan (*bussshi doin keikaku*, or *butsudo*) began to work in January 1938, and other plans also began in Fiscal Year 1939 such as Trade Plan, Credit Control Plan, Labor Mobilization Plan, Transportation and Electricity Mobilization Plan, and Production Capacity Expansion Plan.' It is another empirical question, which should be studied elsewhere, how far those wartime plans effectively influenced the behavior of individual industries and firms. Miwa [1996b] (or Miwa [1998a, Part I]) concludes that the impact of the government plans and controls during the wartime control period through the control association (*tosei-kai*) on the machine tool industry with the highest policy priority was miserably limited. Okazaki and Okuno-Fujiwara [1993, pp.24-25] describe the organization and function of control associations, taking the Steel Control Association as an example, which, however, would be a source of misunderstanding, overestimating their role and effectiveness, because of the Association's peculiarities such as the particular importance of steel rationing during this period, the key position the Association occupied in the whole wartime control system, and the product characteristics of steel as a raw material suitable for rationing.

¹⁴ For the details see Miwa [1996b] or Miwa [1998a, Part I].

¹⁵ Besides, there were 2,029 plants with 5-9 employees in the industry.

The government and industrial policy in Japan

Another popular misconception about the Japanese economy is the existence of strong government and its continuous and effective intervention into the private sector, called 'industrial policy', which is one of the main engines of industrial success. As I argued elsewhere, the strength of powers of intervention is a matter of definition. Outside regulated industries, the government rarely intervenes, however, and the net contribution of industrial policy to Japan's industrial success is negligible. This misconception is composed of five parts: a big government, a government organization suitable for 'targeting policy', a strong government like those in former socialist countries, a magnificent capability on the part of the government to beat the market,¹⁶ and a big contribution to Japan's industrial success. Although the effectiveness of

¹⁶ The same applies also to the 'priming-water (*yobimizu*) effect,' the 'signaling effect,' and the 'cowbell effect' which appear later concerning with small business policies. So does to the 'main bank' argument, too. Many argue in essence that an institution like the government or a main bank with a predetermined role as a representative or as a leader of a group of relevant economic agents in selecting their policy objects or in monitoring their borrowers would both save the aggregate of individual agent's direct resource inputs as a whole and improve the group's overall performance, which, however, contradicts a standard commonsense view that a decentralized market economy rather than a government or a main bank enjoying a stable monopolistic position, providing appropriate incentives for information gathering activities, would select better agents. This popular argument implicitly relies upon an idiosyncratic assumption on the ability of the government or a main bank that it has a capability magnificent enough to beat the market in pursuing better performance.

Emphasizing the role of industrial policy in "discovering" promising industries with growth potentials through forecasting future technology and demand', Okazaki and Okuno-Fujiwara [1993, pp.11-12] argue that a variety of information collection and exchange schemes, such as government councils, unofficial study meetings, and private networks for information exchange, worked so well. It is, however, free riding that seems to be a rational reaction to these schemes, and it is against the best interest of a really important information holder to join the circle actively. If the schemes nevertheless had functioned effectively, here again we would have to rely on the idiosyncratic assumption. In my view, such a case, if any, rarely exists, and it is so rare that nobody has ever officially documented it. Here main bank system is defined as 'a system under which a main bank monitors individual borrower's operation and management as a representative of other lending banks, saving their monitoring costs' (Okuno-Fujiwara [1993, p.286]).

In today's Japan, Okazaki and Okuno-Fujiwara [1993, p.9] insist, bank monitoring disciplines individual firm's management, the function of which is based on 'magnificent monitoring capability of banks and an efficient monitoring scheme called main bank system.' They refer to Ueda [1993], suggesting that he shares the same view, and introduce as his statement that present Japanese 'banks' magnificent monitoring capability is indebted much both to monitoring skills developed and improved in the prewar period mainly by Industrial Bank of Japan (IBJ) and their diffusion during and after the war to other financial institutions, particularly, government-affiliated ones.' Ueda[1993, p.55], however, simply argues that after the War some IBJ's monitoring capability in long-term financing remained and used within the bank and the other flew out to government financial institutions like Japan Development Bank (JDB) to be the basis of their financial activities (p.55).

Have Japanese banks, recently suffering from a flood of bad loans which threatens both individual banks existence and the stability of Japan's overall financial system, 'magnificent monitoring capability'? At least have they ever had it? My view and explanation of the flood is as follows. Since the financial crisis in the 1920's (*Kin'yu Kyoko*) in particular, Japanese banks have adopted as a common principle in making loans and purchasing corporate bonds, particularly in making long-term loans, to take security (and/or a guarantor). This caused a shift of focus in bank's examination and monitoring for making loans, from the proposed project's profitability and borrower's management to value and safety of the security and guarantor. No change in this principle has occurred at least until very recently. During the 'Japan's Bubble Years' in the second half of the 1980s', most loan security (and guarantor in substance, too) was land, which, with a collapse of land market, 'a land-bubble crash' since 1990, resulted straight in the flood of bad loans. Many argue that at the final stage of the Bubble banks were 'bubbly' enough to overvalue securities, making their damages bigger. Thus Japanese banks

industrial policy is not a black-and-white affair, but a 'gray' matter to varying degree, all of five parts are more or less incorrect and exaggerated.¹⁷

Even when the law empowers the government to intervene in the private sector, it is often reluctant in using it.¹⁸ For instance, the Petroleum Industry Act, enacted in 1962, permits the government to intervene in individual refiners' decisions on production levels, pricing, and investment. In the Idemitsu Incident of 1963, Ministry of International Trade and Industry (MITI) officials and the Chairman of the MITI's Petroleum Council tried without success to elicit Idemitsu's cooperation in output coordination. The case suggests four points: (1) even when the government has strong powers, 'self-coordination (coordination by themselves)' is normally chosen by the government as the basic approach to conflict resolution; (2) only when self-coordination fails does government intervene; (3) for government participation to achieve its goals, the active cooperation of the relevant firms is essential; (4) even when the government

magnificent monitoring capability, if any, is to examine the value and safety of security and guarantor, not to examine and evaluate the project's profitability and borrower's management. On these points, see Miwa[1996a, pp.120-22]. A misunderstanding on JDB's role and activities is also popular, which results in an extreme overvaluation of JDB's monitoring capability and their loan's 'priming-water effect.' See Miwa[1997a, (2), pp.46-47] or Miwa[1998a, Part III.III-12].

¹⁷ For the details of Japan's industrial policy, see Part III of Miwa [1996a]. On this misconception see Miwa [1996a, pp.13-15] or Miwa [1995b] which is a reproduction of part of Introduction and Summary chapter of the former.

¹⁸ *Tatewari*, vertically integrated divisions (with poor mutual coordination), has been probably the most popular expression to characterize Japan's politics and administration. Many argue that because of this Japan has been so slow in making decisions, particularly in need of drastic structural change. *Tatewari*-type image applies particularly to industries under individual industry acts (*gyo-ho*), such as Banking Act, Securities and Security Exchange Act, Insurance Industry Act, Loan Regulation Act, Investment Advising Act, Freight Transportation Act, Electricity Utilities Act, Telecommunication Act. Most such industries are within three major regulated industries, that is, energy, financial services, and transportation, or four with telecommunication. In the manufacturing sector, however, almost no such industry act has ever existed since the end of the war, and Petroleum Industry Act of 1962 is almost the only exception. Starting with Petroleum Industry Act of 1934, many manufacturing industries, such as steel, aircraft, automobile, shipbuilding, machine tool, and etc., fell under individual industry acts, and the power and scope of government control over industries was strengthened with the establishment of control associations with The Imperial Order for Key Industry Associations (*Juyo Sangyo Dantai Rei*) based on The National General Mobilization Act (*Kokka So-Doin-ho*). With the end of the war, both of all those control associations and industry acts were abolished. For details, see Miwa[1997a, (1), pp.74-76] or Miwa[1998a, Part II.III-6 and III-7].

Noguchi[1995], famous for the title, 'The Year 1940 Regime,' describes that under the 'New Economic Order' of the Second Konoe Cabinet the government enacted many industry acts, issued the Key Industrial Associations Order, and 'organized industry associations called "control associations", which were the instruments for economic control by bureaucrats.' He concludes as follows: "Those trade associations, government corporations (*eidan*), and government funds (*kinko*), with slight changes in shape and style, still remain, increasing the number in some sectors, and play important roles both as instruments for bureaucratic control and informal regulation (*gyosei shido*) on economic activities and as seats for former higher bureaucrats (*amakudari-saki*)" (p.9). Noguchi insists that 'the economic system underlying and supporting Japan's high growth was basically the continuation of the Wartime General Mobilization Regime (*senji soryoku-sen taisei*)'. However, what he argues to be maintained without any essential change from the wartime economic regime is 'the economic regime -- particularly the institutional foundations for financial control' (p.12) and he stands against the so-called 'Japan Inc.' view, suggesting that at least he does not consider the industries in the manufacturing sector as typical industries under the Year 1940 Regime. Anyway, 'The Year 1940 Regime' is an ill-defined catch word, like 'the dual structure,' '*keiretsu* loan,' '*shitauke* (subcontracting) system,' and 'main bank system,' rather than a well-defined analytical concept, and therefore, readers have to define by themselves the substance of argument with those words or to shelve and neglect them.

uses its power to coordinate private sector activity, it is not easy to actually attain its goals.¹⁹

Facing with the hyper-inflation due to severe supply shortage during the Transition Decade, described soon, the Japanese government was reluctant to introduce a direct control on commodity prices and wages, which was strongly suggested by the Supreme Commander for the Allied Powers (SCAP), who, based on ideas of regulation and planning, reflecting in part the influence of the New Dealers in the Occupation, insisted on their strong regulation. Even during the War, these regulations under the rationing systems set up by the Goods and Materials Control Ordinance (*Busshi Tosei-rei*) had not succeeded. This lack of success was particularly noticeable just before the end of the War, when huge differences between controlled and market prices together with a complex regulatory system dramatically undermined the government's ability to regulate prices and ration goods. Because of this failure, the Japanese government intended to decontrol almost all goods and services in postwar Japan, excepting necessities, favoring liberalization by market forces. In February 1946 the government issued a program on Emergency Measures for the Economic Crisis, which included a new system of official prices, so-called 3.3 system, where all official prices were decided according to linkages with the basic prices of rice, wages and coal products. Note two points: first, there was a big uncontrolled market, called free- or black market, where on average 20% of products in quantity consumed by urban residents were purchased and even the actual price data were continually collected and published by the government; second, such strong regulation of price and quantity did not much contribute to the stabilization of prices, and the overall economy.²⁰ Following much higher free market prices, the official prices were frequently revised. The market price index for consumer products (50 items: in Tokyo) was 40.1 times higher than the official price index in January 1946. This ratio decreased to 9.3 in January 1947, 5.4 in January 1948, 2.7 in January 1949, 1.7 in January 1950, 1.3 in January 1951, and finally 1.1 in December 1951 (Source: Bank of Japan).

[III]. The Role of the Government in Creating and Supporting Small Businesses

Thus, the focus of our study is on the period between 1945 and 1955. The central question is what made such a large number of small businesses emerge, and what happened to them. This section's focus is placed upon small businesses in general, and the next section on machinery industries, particularly the machine tool industry.

Unfortunately, however, it is difficult to answer these questions for the following three reasons: (a) we lack well-organized data and detailed information on the behavior of individual firms and their employees, particularly for the new entrants; (b) until now there has been little significant research in this area; (c) we were in confusion particularly in the second half of the 1940s, the period just after the War.

We lack well-organized data for two reasons. First, under the Occupation Japan adopted the Census Survey data collection system, but before that time there was no well organized collection of data, except in very limited areas such as population, establishments like plants and offices, and employment. Second, for the last stage of the wartime economy, we have only relatively poor data due to wartime secrecy and confusion.²¹ We lack precise and well-organized

¹⁹ For the Idemitsu Incident, see Miwa [1996a, Chapter 10].

²⁰ See Kosai [1986], and Kuroda [1993].

²¹ For this reason, we have no data on establishments and employment for 1943 and 1944, for instance, as shown above in Figure 5.

information on the individual behavior of new entrants, which applies particularly to this transition period.

We lack well directed previous studies, partly because of an intellectual tradition which until very recently has dominated discussion of Japan's economy. This tradition is based on dogmatic Germanic theory or Marxian economics, and does not explain economic phenomena as the actions and reactions of individuals, nor does it address questions concerning the decisions of micro-economic actors.

The Difficulties during the Transition Decade: 1945-1955

As shown above, only in 1957 did Japan's real per capita income exceed the 1939 prewar peak. Total GNP topped the prewar level in 1954. Those ten years were long enough. At the end of the decade, as mentioned above, 1956 *Economic White Paper* declared: 'No longer are we in the postwar age. We are now facing a new, different situation.' Most Japanese, however, thought at that moment that the economy could have grown fairly rapidly in the past decade as a recovery from the destruction which would end with the Transition Decade. They were pessimistic about the future development of the Japanese economy and received the declaration as an empty encouragement from the government.

During the Transition Decade, Japan experienced almost every kind of difficulty which any economy now in transition is facing with.²² First, the total economic system collapsed with

²² Okazaki and Okuno-Fujiwara [1993, p.31] argue that 'Japan's postwar economic recovery at the initial stage was carried out upon the continued plan-and-control system established during the war.' They also argue as follows: 'the scheme underlying industrial policy was also maintained from that during the war and the beginning of the postwar. Trade associations descended from control associations during the war were approved (*shonin*) by the Trade Associations Act of 1948, promoting the formation of widely expanded web of trade associations.' The Trade Associations Act, however, was enacted in order to supplement the Antimonopoly Act, preventing trade association's controlling activities, which was clearly declared in Section: the objective of the Act is 'to clearly define the legal bounds of due activities for trade associations, and to enforce their notification to Fair Trade Commission.' The Act also declared in Section 17 that the provisions in the Antimonopoly Act and 'the authority of Fair Trade Commission based on the Antimonopoly Act should not be interpreted as influenced in any sense by the provisions in this Act.' Thus the Act simply clarified the limits of trade association's activities accepted as not prohibited by the Antimonopoly Act, and therefore the intent and implication of their statement that 'trade associations ... were approved by the Trade Association Act' is incomprehensible. Nothing prohibited formation or existence of trade associations, even just after the war. See Office of FTC [1997, I, pp.37-39]. Every control association, established with the Key Industry Associations Order to supplement the administration capability of the government section in charge of the industry as its affiliate, was abolished just after the end of war, following the abolition both of the Order and related laws like relevant industry acts. Obviously, the strength of continuity from the wartime regime to the postwar one is a matter of definition. For another view, see Miwa [1997a, (1), pp.74-76] or Miwa [1998a, Part II.III-6, III-7]. Even if strong 'continuation' exists between the wartime regime and postwar one in the appearance such as the organizational form and the association membership, no such strong 'continuation' never existed in substance such as what the government was allowed and obliged with the highest policy priority to pursue. Here again Okazaki and Okuno-Fujiwara present their view taking the steel industry as an example, which, as shown above in note 13, would cause serious misunderstanding. Arguing in Miwa [1996a] (or in Miwa [1998a, Part I]) that wartime control was by far less effective than is usually believed, I conclude that the 'discontinuity' in substance is not so obvious as is often believed, either.

'The Year 1940 Regime established for the wartime general mobilization' was kept untouched in postwar Japan, argued Noguchi [1995, p.12], and 'the economic system underlying and supporting the high growth was basically the continuation of the wartime general mobilization regime.' Noguchi concludes as follows. 'The continuation in the government's institutional structure from the prewar Japan was strong enough to surprise us. Only the military authorities disappeared, and all the ministries except for the Ministry of the Interior

the end of the War, at the final stage of which the system was almost paralyzed and the bombing cities, particularly on production plants, accelerated it. Moreover, the production capacity had been forcefully reorganized for wartime production, most unsuitable for peacetime use. As a result, total production level fell to a miserably low level at the start of the Decade: the production index for all manufacturing in January 1946 was only 7.6 compared with the peak of 1944 as 100, which rose to 16.6 in January 1948, and 33.8 in January 1950. Second, as mentioned above, under the Occupation 'Japan shall be permitted to maintain such industries as will sustain her economy and permit the exaction of just reparation in kind, but not those which would enable her to rearm for war.' This basic policy was clearly revealed as the reparation policy which designated so much production facilities as the objects. Third, Japan suffered from hyper-inflation during the first half of the Decade: the overall wholesale price index in August 1945 was 3.36 (1934-36 average = 1) jumped to 18.19 in August 1946, which again jumped to 59.75 in August 1947 and rose up to 157.5 in August 1948. The corresponding figures for August 1949, 1950, and 1951 were 213.1, 254.9, and 348.2, respectively. Thus the price rose in fifty times in three years and more than a hundred times in six years (Source: Bank of Japan).

Fourth, the government was under a strong pressure or a strict control of the SCAP. Besides its weak and unstable position, the government's decision making was strictly restricted, and moreover strongly influenced by changes and confusion in the SCAP's policy due partly to the Cold War development and partly to the conflict of opinions both between Washington and Tokyo and within the SCAP. Fifth, although Japan's governing system was maintained even after the War, purging military men from the government, the political system suffered from the instability over the decade, symbolized by the birth of the Japan Socialist Party cabinet in 1947. Japan's famous political stability emerged after the birth of Liberal Democratic Party in 1955, whose dominance lasted for the next forty years. Sixth, during the War two million houses were burnt down, depriving nine million people from their place to live. With the end of the War, seven million people, both civilians and military men, were forced to come back to Japan from abroad. Providing those people with food, houses, and jobs was a hard task. Seventh, coupled with the confusion after the War, the decrease in food production due to the bad weather in the summer 1945 caused a serious food (rice) shortage, particularly in the urban areas, which aroused a rumor that with a famine over ten million people would starve to death by the next summer. Eighth, in the first few years of the Occupation Japan experienced drastic social and economic reforms on almost every side of the society, including deconcentration policies like *zaibatsu* dissolution, the enactment of Act for the Elimination of Excessive Concentration of

remained almost unchanged. ...Perfect continuation from the wartime regime even of seniority rule in promotion was maintained' (p.76). For this conclusion he takes the Ministry of Finance as an example, arguing that even each bureau (*kyoku*) never changed at all. The picture seems to be completely different when we take government policy toward the manufacturing sector by the Ministry of Commerce and Industry (later, Ministry of International Trade and Industry), instead of financial administration or control by the Ministry of Finance upon which Noguchi's argument mostly depends. In the Commerce Ministry, there existed strong continuation in human resources, but in other respects the continuation is less obvious. First, the basic objective and role of the Ministry completely changed, from industry development and control to export promotion. Second, bureaus changed drastically and repeatedly in number, the organizational structure, their names, and the roles. As mentioned above in note 18, all industry acts and control associations were abolished, and trade associations, when survived, were obliged to change radically their role, character, and leaders. Moreover, the administration's essential role and function has also changed drastically, on the process of which no remarkable change occurred in human resources and seniority rule in promotion. For the details on these points, see Miwa[1997a, (1), pp.68-76] or Miwa[1998a, Part II, from III-3 to III-7].

Economic Power, the Economic Purge, and the introduction of Antimonopoly Act,²³ and a series of 'liberalization' of land ownership, labor unions, and women's political participation. Coupled with the confusion due to the end of the War and the transition to a peacetime economy, these radical changes made the society at least potentially unstable.

Ninth, firms, particularly large corporations suffered seriously from the wartime damages: their production facilities were organized for wartime production; the Japanese Diet passed in October 1946 the Act on Special Measures for Wartime Compensation, which in effect canceled war-related debts owned by the government and puts almost all major corporations in Japan into a state of insolvency or near-insolvency²⁴; many big firms made every effort in establishing stable relationship with labor unions, in Japan most of which are company unions and whose formation was prohibited before and during the War. Liberalization of labor unions' activities, particularly under the strong influence of Japan Communist Party, intensified the tension in industrial relations, which needed a decade to stabilize.²⁵

The Central Message on Small Businesses and Small Business Policies

The central message of this section, and therefore the central message of this paper on small business and small business policies, is the following two points. First, there were no basic restrictions peculiar to small businesses, and, compared with large firms, small businesses were not seriously handicapped. Being flexible in character, small businesses were more suited for radical adjustment for the completely changed environment. Large firms were more seriously damaged both during the War and by the postwar government policies. They had to spend much energy in establishing a stable industrial relations. Second, during and after the transition period the government did not play any crucial role, at least in direct means, in creating small business and supporting their activities.

Note four points. First, the first postwar decade was a difficult transition period, during which the government, being unstable and not so strong, was busy in maintaining social stability. The basic factor which obviously contributed much to the development of this process is the social stability maintained during this period. Thus the government, under the supervision of the SCAP, played an essential role in providing a favorable environment for smooth transition and development in the next stage. What the government did for specific sectors of the economy, particularly for small business, is negligible. Although the government's policy began to focus on small business in the second half of the 1950s, in the first postwar decade the policy effort was devoted exclusively to securing social stability which included safety of life, price stability, and secure supply of basic materials such as food and energy.

Second, since the turn of the century, at least over the political debate with popular phrases such as the dual-structure and small business exploitation, it has been small businesses rather than large firms which were to be supported by the government policy. Even when the government decided to enact a special law to support machine tool production in 1938, as mentioned in the previous section, by selecting small number of large producers, the Diet, referring to its potential bad influence on small businesses, strongly demanded not to focus too much upon them. The same discipline applied to the policy debate throughout the postwar

²³ See Miwa [1993] for the assessment of the effectiveness of these policies, which is quite often overestimated.

²⁴ To prevent bankruptcies, at the same time the Enterprise Reconstruction and Reorganization Act and the Financial Institutions Reconstruction and Reorganization Act were enacted.

²⁵ The industrial relation conflict was the most serious in automobile industry, particularly Nissan, the second largest automobile manufacturer in Japan, which suffered from a serious 'struggle' over four months in 1953.

period, where small businesses came first and large firms received lesser attention, at most.

Third, however, as shown above, most firms have been small businesses, which have provided most of employment. Nobody can subsidize everybody, and no government has effective policy weapons to create such a mass of small businesses predominating the whole economy. Only 'the market' could have done the task given Japan's postwar environment, only part of which was provided by the government. There was no policy magic, by the so-called 'industrial policy.'

Fourth, through the postwar period, the central policy objective, or the policy slogan, of government intervention into the private sector was to avoid 'excessive competition,' by establishing and maintaining 'the industrial order,' for which new entries were argued to be restricted and mergers among incumbent firms to be subsidized. This suggests a common understanding at least among policy makers that in many sectors there were too many firms and too many entries, both actual and potential. This applied also to sectors dominated by small businesses. The Japanese government has never worried about obstacles discouraging entry of small businesses.²⁶

The Textile Industry

The textile industry was the most important export industry during this period. In 1953 and 1954 the ratio of textile exports to Japan's total exports was 36.1% and 40.5%, respectively. Small businesses, which dominated this sector, suffered from the wartime controls because they were small business and because the textile industry was not designated as the one for the wartime urgent need. In the last stage of the war, many textile factories were forced to switch production to goods deemed more urgent for the wartime effort and textile production machines were ordered to be scrapped so that they could be used as basic materials in machine production. With the exception of import restriction of cotton through foreign currency rationing, the end of the War brought about an end of textile production restrictions. Simple observations show that there was a huge stock of unfilled demand accumulated during the War both at home and abroad, and textile production and exports increased. The ratio of textile exports to Japan's total exports in 1934-36, on average, was 52.1%, and presumably this rapid postwar production and export expansion was the revival of the past prosperity based upon the experience and memory of old days.

As shown in Table 5, in 1935 there were about 30 thousands textile mills with over 5 persons engaged, where in total 1,135 thousands were engaged.²⁷ 25,983 mills, 88.4% of the total, were with 5-49 persons engaged, where 337,030, 29.7% of the total, were engaged. In 1946, corresponding numbers in total were 11 thousands and 513 thousands, respectively, of which 86.8% were with 5-49 persons engaged, where 34.0% of the total were engaged. In 1953, there were about 30 thousands textile mills with over 4 persons engaged, where 930 thousands were engaged. 28,849 mills, 96.5% of the total, were with 4-49 persons engaged, where 353,852, 38.0% of the total were engaged.²⁸ The ratio of small business to the total is much higher when

²⁶ In the 1980s, however, with a slowdown of the increase in the number of the smallest firms which finally began to decrease, the government started policies to promote small business entry, as policies against 'industry hollowing-out [*sangyo kuhdo-ka*].'

²⁷ Figures are from *Plant Census* before 1947, and *Manufacturing Census* after 1948. Figures are at the end of the year, 31 December, and for instance figures for 1935 are those on 31 December 1935.

²⁸ Note that before 1947 figures are for plants with over 5 persons, and after 1948 for plants over 4 persons. Besides, in 1953, there were 47,464 textile mills with below 3 persons engaged, where in total 109 thousands

its definition follows the standard usage, with below 200 or 300 persons engaged. Thus, in Japan both before and after the War small businesses have dominated the textile industry.

----- Table 5 -----

Small Business Policies

In the second decade, the government organized, or systematized, policies for small business, symbolized by the enactment of the Small and Medium-sized Enterprise Basic Act of 1963. These policies were designed to eliminate the 'dual structure' under which a vast majority of small businesses were 'exploited' by large firms. The majority of the dual-structure view's supporters argued that there were too many small businesses, which, lead to 'excessive competition' among them. As the result of this basic view, elimination of obstacles to small business's entry was not included among policy objectives.

As I have already discussed elsewhere, Miwa [1995a, and 1996a], the dual-structure view underlying Japan's small business policy is totally wrong. Four points emerge. First, the Japanese economy grew rapidly even before the 'dual structure' was 'dissolved' by 1970. Within this environment, both small businesses and large firms grew steadily. This implies that large firms provided a stable demand for the products of rapidly growing small businesses. Such a fact is not consistent with the exploitation of small businesses. Second, as shown in Table 6 and Figure 6, the profit rate for small businesses has been much higher than that for large firms. This too is not consistent with the argument that small businesses were exploited by large firms.²⁹ Third, consistent increases have been observed in the number of small businesses. As shown in Figure 2, between 1954 and 1991, before and after the time of the 'structural changes,' the number of establishments of every size increased constantly. This too is inconsistent with the argument that small businesses were exploited, as rational entrepreneurs would not enter markets in which they would be exploited. Fourth, although it is widely argued that a 'loan-concentrating mechanism' in the financial sector targeted loans to large firms rather than small businesses—perpetuating the notion of 'dual structure'—such a mechanism in fact never existed, as shown below. From these four points (or even just one or two), three propositions follow: the assertion that a large majority of small businesses were 'exploited' before the early 1960s is inconsistent with reality; the assertion that they have been exploited in more recent years is likewise inconsistent with reality; and 'structural change,' in the sense of a drastic reduction in the proportion of small businesses being 'exploited,' never occurred. In short, the problem that

persons were engaged. Corresponding numbers in 1949 were 23,624 and 70 thousands, however, no corresponding data are available for the prewar period.

²⁹ Readers may comment that small business profit rate is higher than that of large firms simply because the hazard rate of the former is much higher and their profit includes a big risk premium. Note, however, that the issue here is whether small business profit rate was much lower than was expected due to the dual structure disadvantage, and I am arguing that on the contrary the profit rate was rather higher than was expected. As for the hazard rate, at least in Japan it was not so high as is usually imagined. So far as I know, no systematic data is available for small business hazard rate. In Japan as a byproduct of a large sample survey, *Basic Survey on the Reality of Manufacturing [Kigyō jittai kihon chosa hokoku-sho]*, 4th in 1971 and 7th in 1987, Statistics Bureau, Ministry of International Trade and Industry, we have two years survival rate data for 1969-71, at the final stage of Japan's high-growth era, and 1985-87. The former says that two years hazard rate (= 1 - survival rate) for all manufacturing firms was 6.6%, for firms with 1-3 persons engaged was 10.2%, for firms with 4-9 persons was 5.4%, and for firms with 10-19 persons was 3.7%. The corresponding numbers for 1985-87 were much lower than those for 1969-71.

small business policies were ostensibly designed to address did not exist. In addition, the scale of these policies has been so small and their targets so indiscriminate that they could have no remarkable effects on small business situation.³⁰

----- Table 6, Figure 6 -----

Several important events in small business policy occurred even before the 1963 Small and Medium-sized Enterprise Act. The Small and Medium-sized Enterprise Agency (SMEA) was created in 1948 as an extra-ministerial bureau of MITI (the Ministry of International Trade and Industry). The People's Finance Corporation was founded in 1949, and the Small Business Finance Corporation was founded in 1953. Together with the Central Cooperative Bank for Commerce and Industry founded in 1936, the latter two corporations became the principal means by which the government channeled loans to small firms.

Those events in small business policies, however, had only negligible effects.³¹ Before a detailed description of Japan's small business policies in Section V below, I explain here why they had only negligible effects. I take financial policies as an example, as there is wide agreement that the most important policy measures for small businesses are financial. (a) Small business financed from above mentioned three governmental financial institutions only about 10 percent of their total borrowing. 8.7% in 1960, 8.8% in 1965, 9.3% in 1970, 12.8% in 1975, and 12.6% in 1980. (b) In most cases the lending rate is the designated 'base rate,' which is equal to the 'long-term prime rate,' and is only slightly, 0.5% - 1%, lower than the market rate with which small businesses borrow. (c) Moreover, the supporters who emphasize the effectiveness of this lending policy assume the existence of 'dual-structure' in Japan's financial market, which severely handicaps small business. This view is totally wrong, too.³² As shown in Figure 7, it was large firms, rather than small businesses, that increased borrowing while the financial markets were developing, which runs counter to the traditional view.

----- Figure 7 -----

The Market Mechanism rather than the Government Policy

Why the market worked so well in Japan in this transition period is the central question. As everybody understands, this is a hard question to answer. It is hard to ask right questions for this purpose, too. Two observations should be noted: (a) The high profitability of small business must have acted as an incentive to begin new operations. (b) There was little expectation of the government's support and high rewards from old jobs, which made many people search for new way of living. Fortunately, the government was unreliable enough to let people look to the market for solution but reliable enough to maintain the social stability. Thus it was not too weak, but not too strong.³³

³⁰ For a more detailed analysis of Japan's small business policies in recent 30-40 years, see Miwa [1995a].

³¹ For the details see Miwa [1995a].

³² See Miwa [1996a, Chapters 3 and 5].

³³ Those who are familiar with Japanese supplier-assembler relationships, particularly those in the automobile industry symbolically called 'Toyota production system,' may argue that it is those assemblers rather than the government that played the central role in creating and supporting the development of small business in Japan. This is, however, another popular misconception about the Japanese economy. Note a basic fact that, even if those assemblers might be more well-qualified than the government in playing the role, nobody could easily earn

The market rather than the government policy was the basic determinant of the pattern of Japan's postwar economic transition and development. As a result, the development in individual districts was quite unbalanced, more developed districts accelerating their development and vice versa. As shown in Figure 8, Kanto District including Tokyo and Yokohama, Kansai District with Osaka, Kyoto and Kobe, and Tokai District with Nagoya, in total the Central Japan, have gathered much larger shares in economic activity and population than the prewar days. For instance, Kanto more than doubled the number of manufacturing plants, increasing the share from 26% in 1951 to 31% in 1981, while Kyushu and Shikoku, the southern part of Japan, did not much increased the number, decreasing the total share from 15% in 1951 to 9% in 1981. Although the government adopted policy for well-balanced overall development, the market dominated.

----- Figure 8 -----

[IV]. Machine Tool Industry

Among machinery industries the automobile industry represents Japan's postwar economy both during the hard days of the transition period and during the explosive development process since the second half of the 1950s. As shown in Table 7, Japan's total car production in 1955 was only 20,000 when Toyota launched its first true car, the Crown. By 1965 production grew to approximately 700,000 cars. In 1970 production was at 3,000,000 cars, and in 1971 more than 1,000,000 cars were exported. In this explosive development process, the cooperation between suppliers and assemblers played a central role. Those supplier-assembler relationships were organized through exchanges by agreement among participants, presumably under the assemblers' leadership.³⁴ Toyota and Nissan began truck production in the 1930s, but with the end of the War they lost their biggest customer, the government, making the next 10 years very difficult to survive.

----- Table 7 -----

For some industries which grew notably with the war, the end of the war and the following transition period was a difficult challenge. Machine tool industry is one example. As shown above in Figure 4, between 1931-38 machine tool industry production grew thirty times in terms of the number of machines produced and almost fifty times in terms of the total weight of machines produced. Only in 1960 was the prewar peak topped in terms of the number, and in 1967 in terms of the weight. The wartime government particularly at the last stage directed materials toward large firms in this industry. Many of them survived the transition period and could support Japan's explosive growth in the next 'high growth era,' supplying mother machines to industries, particularly to machinery industries.³⁵ Lessons from the observations

profits by persuading entrepreneurs to enter the market and commit their resources, particularly in such an unstable transition period. Toyota, for instance, began their explosive growth after 1955, after this transition period, and most Japanese thought at this moment their business so risky and unpromising. See Miwa [1996a] for the details of the argument, Chapter 4 for supplier-assembler relationships in the automobile industry, and Part IV for interfirm relationships in general.

³⁴ On this point, see Miwa [1996a, Chapter 4].

³⁵ The above mentioned Pauley Report (1945) on Japan's reparation recommended first of all machine tools to

related to this industry are that the transition period was hard and long, individual firms and often individual employees survived by themselves, and the government could play only a basic role and could not pursue any policy directed to particular individuals.³⁷

The automobile industry has been the largest user of machine tools. With the high growth of the economy after the short recession in 1954-1955, symbolized by the dramatic growth of passenger car production, over eight times in five years (1955-1960) and 35 times in ten years (1955-1965), machine tool production increased rapidly, in five years (1955-1960) 4.4 times in terms of the number of machines produced and 9.0 times in terms of the total weight. The production volume in 1955, after a decade of hard days of transition, however, was by far below the prewar peak, 27 % in terms of the number of the prewar peak and only less than 5% in the total weight of 1943 level.

We have only a collection of fragmentary information on what happened to each individual firm just after the end of the War. In general the number of employees in each firm

make available under a program of interim deliveries. (1) Half of the capacity for the manufacture of machine tools. (2) All tools and equipment as follows: In army and navy arsenals, except for equipment useful solely for making arms, ammunition, and implements of war, which will be destroyed. It is estimated that these seizures should bring in not less than 70,000 machine tools; in the entire aircraft industry of Japan, It is estimated that this should bring in 220,000 machine tools; in all plants manufacturing ball and roller bearings; in all plants manufacturing aircraft engines.

³⁶ Note that in the 1980s Japan has become the world largest machine tool manufacturing country.

³⁷ Many industries, particularly those heavily involved in military supplies like the machine tool manufacturing industry, were strongly influenced by the wartime control. The issue here is the seriousness and the direction of influence. The machine tool industry, for instance, obviously and seriously suffered above all from huge demand-supply imbalance due to expanded production capacity, machine tool stocks in operation, and drastically reduced demand with the disappearance of the military authorities. But I do not agree with Okazaki and Okuno-Fujiwara[1993, p.8] and Okazaki[1993, pp.116-17]. "The characteristic feature of corporate organization in the present Japan that shareholders' influence on corporate management is minimal' is a direct result of the wartime control, where 'the roles and rights of shareholders were restricted, the position of managers and employees was much improved, and a main bank became in place of shareholders the principal monitor of a company as a manager of fund suppliers' group, typically a group of cooperative lenders' produced by 'the corporate system re-examination movement resulting in the Munitions Company Act (*Gunju kaisha-ho*)' effective in December 1943.

'Friendly shareholders (*antei-kabunushi*)', shareholders considered by the present directors and managers to be friendly to them, choose voluntarily to be friendly to the present management, and nothing has happened to their right as shareholders. The management is strongly influenced by shareholders, including friendly shareholders, since it has to keep the support of friendly shareholders, charming enough to keep them on the present position. On this point, see Miwa[1996a, Chapter 11]. If they suggest with the 'characteristic feature' that management in Japanese firms, particularly the roles and rights of shareholders, much differs from those in foreign firms, particularly those in American firms, here again many do not agree. Clark[1985, p.56], for instance, comments as follows: '[t]o an experienced corporate lawyer who has studied primary legal materials, the assertion that corporate managers are agents of investors, whether debtholders or stockholders, will seem odd and loose.' See also Mace[1971].

Moreover, as mentioned elsewhere in Miwa[1996b, (1), pp.81-82]or Miwa[1998a, Part I.II-12], although a munitions company had to appoint 'a responsible person' who as a representative of the company bore the responsibility to the government, 'a responsible person' could not be dismissed without government's approval and the government could dismiss him when he was not the right person, both the military authorities and the Munitions Ministry could not contribute through active intervention much to their objective of production expansion as they lacked in production management capability. If active intervention of the authorities into private sector were to be so effective, centralized ex-socialist economies would not have collapsed. If it were effective, the period till the collapse of wartime economy and the end of the war was too short. Even if the government could have much influenced the production system by forceful intervention, it is implausible that such influence survived after the war, when the power enabling intervention disappeared, and it been effective for a long time in the postwar Japan.

decreased drastically just after the end of the War. In 1942 there were 3,213 machine tool manufacturing plants with over 5 persons engaged, where 203,331 were engaged. The corresponding figures in 1947 were 1,885 and 49,089. Limiting attention to metal machine tool manufacturing, the decrease was more drastic, the number of plant from 815 to 191, the number of persons engaged from 118,441 to 7,805.

An owner-manager of a small business once told me that at the beginning of the transition period most employees decided to ask for firm's retirement payments and therefore he had no trouble in decreasing the employment size. As shown below, we find the same picture with some of the large companies, drastic decrease in the number of workers. This happened because most people were shocked by the end of the War and the war destruction, and many of them thought it better to quit the company. Presumably this is one source of the expansion of new small businesses operations. This suggests that, with little hope of help coming from the firms actually employed or the government, many were forced or induced to begin their own business.

Hitachi Seiki, the largest machine tool builder during the War with over 10,000 employees at the peak, decreased the employees number soon after the War to one tenth. Toyoda Machine Works, established in 1941 by splitting off from Toyota Motors and ranked as one of the Big Five machine tool builders in the 1960s, describes in the company history that in 1953, when their machine tool sales were still far below 20 % of the total revenue, they had to make every effort in reorganizing the company from textile machinery manufacturing toward machine tool manufacturing. After the War, with drastically decreasing the employees number they had to survive with manufacturing every kind of metal products including cooking pots and pans, and farm plows. With the expansion of textile production in Japan it found a new rich market and became one of the biggest suppliers of textile machinery. Then in 1953, Toyota Motors, still holding over 20% of stocks in 1955, asked whether it would take part also in making automobile parts, to which after a long discussion the board of directors of Toyoda Machine Works finally answered in the affirmative. Note that in 1953 almost all Japanese people, except some challenging ones, recognized that manufacturing passenger cars in Japan was a venturesome business. People remembered the famous statement in 1950 of Mr. Ichimanda, the Chairman of the Bank of Japan, which has come to be known as 'no-passenger-car argument': 'It is useless to develop the car industry in Japan. Now is the time of international division of labor, and we can buy it from the USA.'³⁸

At the start of the postwar expansion of the industry, not only the production volume but also their quality, user's trust and the reputation were all very low, and most found the prospectus unpromising. For example, in 1955 the total value of imported machine tools exceeded that produced in Japan, which occurred even under the strict import control by MITI due to serious foreign currency shortage. MITI enacted in 1956 the Act on Temporary Measures for the Promotion of the Machinery Industries (*kishin-ho*) which placed among many designated industries a special focus upon the machine tools- and the auto parts manufacturing industries. Whether the Act was effective is another question, however.³⁹ The corresponding prewar law mentioned above was not so effective, even when attached the highest policy priority and carried out by much stronger government. Like the prewar industry expansion process, as

³⁸ For the historical background of the industry, see Miwa [1996a, Chapter 4].

³⁹ I closely examined the effectiveness of the policies based of this Act and concluded that it could not have been effective and actually had negligible effect, if any. See Miwa [1997a] or Miwa [1998a, Part II].

shown in Figure 9, a huge number of new firms in every size category entered the market. The figure is quite similar to that for prewar development shown in Figure 5.

----- Figure 9 -----

Another point worth attention is that both the automobile industry and the machine tool manufacturing industry started their rapid expansion process basically with very old equipment, and modernized them through investment for expansion. As shown in Figures 10 and 11, even in 1958 most machine tool equipment vintage in these industries were over ten years, implying machine tools manufactured during and before the War. As no technological and product information on new machine tools were available from abroad during the War, this means that they started the industry expansion with the prewar technology.

----- Figures 10, and 11 -----

[V]. Policies for Small Business⁴⁰

Government policies for small business began in prewar Japan as social policies, not as economic policies. The government imposed them, in other words, for reasons of 'equity' rather than 'efficiency.' At least until the beginning of the 1970s, postwar policies strongly reflected this character. The policies for small business during this period were designed to solve the 'medium and small enterprise problem.' This term is closely related to 'dual structure,' discussed above, and suggests that large firms in the modernized industrial sector subordinate, control, and exploit small businesses in the traditional sector. This view implicitly assumes that large firms have and can exercise power to exploit small businesses, whose freedom of choice is tightly restricted and likened to a 'hold-up' situation. Many Japanese have recognized this situation as a 'social problem' to be solved by government intervention.⁴¹

Several important events in small business policy occurred in the early postwar period, such as the creation of the Small and Medium-sized Enterprise Agency (SEMA) in 1948, the foundation of People's Finance Corporation in 1949, and that of the Small Business Finance Cooperation in 1953. It was not until the late 1950s, however, that policies for small business drew public attention. The *1957 Economic White Paper*, next to the already mentioned *1956 Economic White Paper*, asserted the existence and emphasized the seriousness of the 'dual structure' of the Japanese economy. This argument, apparently striking a responsive chord in the public, gained immediate acceptance and 'dual structure' became one of the most popular phrases of the time. In 1963, 15 years after the establishment of SEMA, the Small and Medium-sized Enterprise Basic Act was enacted with broad public support and enthusiastic political backing. It ordered the government to conduct fact-finding survey on small business and to submit to the Diet an annual report (the so-called *White Paper on Small and Medium-sized Enterprises in Japan, or Small Business White Paper*, first published for fiscal year 1963) on trends among small business and measures taken to assist them. From this date, policies for small business began to be carried out systematically.

Ironically, with rapid economic growth in the 1960s, support for the dual structure view

⁴⁰ This section is a brief summary of Miwa [1995a].

⁴¹ As mentioned above and discussed in detail in Miwa [1996a], however, this view is totally wrong.

weakened rapidly. By 1970, the *Small Business White Paper* had a subtitle: 'The Transformation of the Dual Structure and the Increasing Variety of Small and Medium-sized Enterprise Problems.' Either the situation surrounding small business or the public's image of small business had changed. I concluded that a wide gap has existed between the image and the reality of small business and that the image of small business has changed more radically than the reality. In short, the problem that small business policies were ostensibly designed to address did not exist. If the elimination of the 'dual structure' is the standard for measuring the effectiveness of small business policies, those policies could not have been 'effective.'

Overview of Small Business Policies

Although many studies of small business policies address 'policy ideas,' 'policy targets,' and 'policy measures,' few consider 'policy effects.' Among those who do, Hajime Takaki, former chairman of the Central Cooperative Bank for Commerce and Industry, observed soon after the depression of the early 1970s⁴²:

"There are so many different policy measures for small business policies that most of us would be amazed to discover how tiny the scale of each policy is. Policy efforts have been wide but thin. It is as though the government waters large flower pots with small sprinkling cans ... In the present severe depression, there is a strong demand for such policies for small business in order to encourage their owners and managers ... Each policy is well designed and sensitive; however, the scale of government's policies is too small to have any effects."⁴³

A more standard view, however, would be similar to that expressed by Yokokura [1988]. First, small business policies until the 1950s were but one facet of social policy and consisted of financial and cartel policies. In the 1960s, policies to assist the modernization of small business facilities were but one facet of industrial policy. In the 1970s and 1980s, modernization policies emphasized human resources (people), technology (information), and industrial adjustment policies such as assistance for firms to change their line of business. Second, small business policies tended to be indiscriminate in focus and in the policy instrument they used. This was in part because of the great variety of disadvantages faced by small business, but was also due to the operation of political-economic mechanisms.⁴⁴ Nonetheless, the indiscriminate use of small business policies, such as in the designation of industries under the Modernization Promotion Act of 1963,⁴⁵ inevitably weakened their collective impact (effectiveness). Third, small business policies relied primarily on the use of financing, operating through the market mechanism, rather than competition-restricting measures and direct subsidies, which eliminated the use of small business policies as protective policy.⁴⁶ This contrasts sharply with agricultural policies,

⁴² For the details see Miwa [1996a, Chapter 3].

⁴³ *Nihon Keizai Shimbun (Japan Economic Journal)*, 12 January 1975, cited in Miwa [1996a, p. 53].

⁴⁴ See Miwa [1996a, Chapter 8] for a brief description of industrial policy formation process.

⁴⁵ This Act was enacted as the embodiment of the Small and Medium-sized Enterprise Basic Act of 1963 and in order to modernize small business in each industry. The number of industries designated in the five years ending in fiscal year 1967 was 137. By 1975 the number had increased to 232.

⁴⁶ 'In the case of financing, it differed from a direct subsidy in that firms had to repay the principal and pay interest, while the market mechanism was utilized so that financing was not provided to firms without the ability to repay' (Yokokura [1988, p.532]).

which depended on the use of import restrictions and direct subsidies.⁴⁷

Financing Policies for Small Business

As mentioned above, there is wide agreement that the most important policy measures for small business were financial, which, however, were not effective. In short, during 1960-80 the three government-affiliated financial institutions provided only 10% of the total amount of funds small business borrowed from all financial institutions. Therefore, when policy loans are provided at 1% below the market rate, the average rate of funds for small business can be lowered only 0.1%, which cannot be considered very significant.⁴⁸

There is a widely held view that those lending policies have strong 'priming-water (*yobimizu*) effects,' 'signaling effects,' or 'cowbell effects' (that is, policy lending has an effect of attracting private bank loans to its borrowing firms) which refutes above evaluation. It is often asserted - and in most cases orally - that even if the ratio of the actual loans had been less than 10%, their effects have been far greater than this figure suggests. However, I cannot agree with this view with three reasons. First, most of the policy loans are provided under the general loan system at the 'base rate' and the doors are open to any small business. For instance, the Small Business Finance Corporation (SBFC) provides its loans directly through its approximately 60 offices and indirectly through private financial institutions, which number 846 (15,131 branches). SBFC offices and agents are open to any small business and borrowers may negotiate with them directly. They need not, in other word, acquire recommendations form third party such as local government, Boards of Commerce and Industry, Chambers of Commerce and Industry, or other financial institutions. Second, the SBFC and its agents check the loan applications and security presented by their borrowers so rigorously that it is sometimes said their requirements are more severe than those of private institutions. If a default occurs on an indirect loan, the agent bears 80% of the loss. Coupled with a low default rate of their loans, the observation suggests that their lower interest rate loans are directed to riskless small borrowers through rationing with strict standard, subsidizing those which could have borrowed from private banks. Third, even if the government selects firms with their own standards, why and how can they promote economic growth? An underlying, seemingly tautological, assumption of belief is that in Japan, the government always has the ability to beat the market, which is, at least, still open to careful investigation.⁴⁹

⁴⁷ Yokokura [1988, p.524] has commented that:

'If ... one compares the amount and content of the budget for small business policies with that of agriculture and fisheries, the other sector that along with small business has been labeled "pre-modern," then the following differential can be observed. Subsidies for agriculture, forestry, and fisheries in the 1980 General Budget came to 1.9 trillion yen (including funds for land improvement and other activities to improve the infrastructure), while 1980 Fiscal and Investment and Loan Program (FILP) investments came to 890 billion yen. In contrast, 1980 General Budget subsidies for small business policies came to 61 billion yen, while 1980 FILP investments came to 3.4 trillion yen. In contrast to the huge subsidies expended on agriculture, those for small business are small, and the dependence is on FILP investments.'

⁴⁸ The effectiveness of the financing policies for small business depends of the state of the capital- and product market and the relation between small business and large firms. In many cases, small business sectors are so competitive that lower interest rate loans to small business benefit only the buyers of their products, such as consumers and large firms. This suggests that this 0.1% reduction is an overestimate as its policy effect.

⁴⁹ As discussed above in note 16, a similar assumption underlies as common views peculiar to the Japanese economy, emphasizing the singularity of the Japanese economy and the Japanese firms. See Miwa[1996a] for

Menu of Small Business Policies in Japan

Let me here catalogue, for readers' convenience, the 'basic measures' of small business policies in Japan. These are the 'basic measures' for small business policies found in SMEA, *Outline of Small Business Policies (Chusho Kigyo Shisaku no Aramshi)*(Tokyo: SMEA, 1992). Readers should keep in mind two points. First, I refer here to many Japanese 'policies' and 'policy measures.' Their titles often make little sense even in Japanese and therefore are hard to translate into English. Many of these policies are simply new versions of older ones and contain new phrases with only nominal differences in meaning. This proliferation of policies with slight variations has resulted from political and administrative conditions in Japan. Second, although SMEA was established to promote small businesses, it is not the only government institution to do so. The Ministries of Labor and Construction, the Fair Trade Commission, MITI, and local governments all have small business policies.

- (1) *Finance*: financial assistance by three government-affiliated institutions - the Small Business Finance Corporation, the People's Finance Corporation, and the Central Cooperative Bank of Commerce and.
- (2) *Credit supplements* (financial reinforcement by means of credit supplement): to receive a loan from a financial institution, a small firm must have its loan guaranteed by a credit guarantee association (CGA); CGAs in turn apply to the Small Business Credit Corporation to insure the guarantee.
- (3) *Small business taxation*: reduction of the corporate income tax; preferential tax treatment to promote investment by small businesses.
- (4) *Cooperatives*: aid for the joint business activities (such as joint production, joint processing, joint sales, etc.) of about 50,000 cooperatives.
- (5) *Consulting and finance*: provision of management consulting and guidance by specialized personnel in the prefectural government.
- (6) *Personnel training* (for human resource development): a variety of training programs at government institutions for small business and basic training courses at the prefectural government level.
- (7) *Technological development*: technical training courses at institutions for small business and technical assistance by prefectural and other public research institutions.
- (8) *Promotion of small enterprises*: personnel at the Board of Commerce and Industry and the Chamber of Commerce and Industry; special loans for management improvement; special loans for equipment modernization.

Implementation of Policies for Small Businesses and the Role of Local Government

critical comments on those views. Most those views simply 'interpret' and 'theoretically explain' the phenomena, assuming an argument as obvious and firmly proved, without careful examination by himself, that the policy of the system was effective. I have never seen a research which empirically proved that a 'main bank system' performs much better than decentralized monitoring through the market. I show in Miwa[1996a] that 'main banks' of firms experiencing financing trouble tends to change more frequently than 'main banks' of ordinary firms, and draws a negative conclusion on the existence of the 'lender of the last resort' function. Thus, often 'main banks' run away before the borrowers fell into financial trouble. Before this observation, it is irrational for non-main-bank lenders to save monitoring cost by 'delegating' monitoring function to main bank. Even if 'main bank' both has magnificent monitoring capability and possesses borrower's information better than other banks, my observation is consistent with a plausible rational choice to use it for itself.

Compared with financing policies, it is more difficult to evaluate the effectiveness of other policies, such as technical assistance by prefectural and other public research institutions, management guidance by specialized personnel, provision of management consulting and guidance by specialized personnel. Coupled with the following two points, however, what I have heard on various occasions and scattered materials do suggest that the overall effectiveness is no different than the effectiveness of the financing policies: (1) there is wide agreement that the most important policy measures for small businesses were financial; (2) as shown below, the number of persons engaged in those activities has been so small to be effective.

Most of the policies of the central government are implemented through or with the assistance of local government. In most cases, however, the central government decides the general scheme of each policy. Those local governments that consider the scheme useful then develop more detailed plans and compete to have the central government adapt their specific plan.⁵⁰ The policy then implemented by the central government is a collection of policies from the local governments. This division of labor reflects the recognition that the effectiveness of such policies depends on the circumstances surrounding them, and that these circumstances greatly differ in each area. Each local government also has its own policies for small businesses. As a result, there are a wide variety of objectives, the weight of which are also different, and forms among the actual policies of local governments.

To better understand the implementation and effect of policies, let us focus upon a specific prefecture, Hyogo Prefecture, in which Kobe is the largest city. Its population is 5.4 million, 4.4% of the total Japanese population. Several indicators show that its economic power is 4-5% that of the whole country. The prefecture is located in the Kinki district, which is located in the central western part of Japan and is made up of seven prefectures, and has both densely populated, highly industrialized urban areas and sparsely populated areas that have agricultural bases or are located in mountainous regions. The number of establishments (excluding agriculture and fisheries) was 274,000 in 1986 and 99.1% were small businesses. Of these establishments, 47.9% were in wholesaling and retailing, 23.9% in the service sector, and 12.6% in manufacturing. Of total employees, 77.75% were in small businesses. The manufacturing sector employed 27.5%, and 69.6% of those were in small businesses.

The Bureau of Commerce and Industry (BCI) within the prefectural government is in charge of policies for small businesses. It has 360, or 4.2%, of the approximately 8,500 prefectural employees (in 1967, the corresponding numbers were 404, 8,000, and 5.0%). BCI is divided into seven divisions (five in 1967), and the Industry Policy Division, the New Industry Location Division, the Finance Division, and the Industry Division are directly involved in small business policies. In addition, the General Coordination Division had indirect involvement in small business policies. Of the 360 BCI employees, 166 are in the central office, and 75 of those are in one of the small-business-related divisions. In additions to the divisions in the central office, two subordinate institutions deal with policies for small businesses. The institute for General Guidance for small businesses, subordinate to the general Coordination Division, employs 19, and the Hyogo Prefecture Institute for Industrial Research, subordinate to the Industry Division, employs 118.

Three groups of policy measures were at the core of 1992 BCI policies: measures for upgrading industrial structure, measures for stimulating regional economies, and measures for

⁵⁰ The selections of proposal often appears to be very politicized, which may be the reason for the indeterminacy of the focus of those policies.

promoting successful small businesses. The budgets for each group reveal the predominance for the last, which included two significant items: ¥57.6 billion for financial assistance and ¥14.4 billion for assisting the growth for small businesses. The policies for small businesses are the core of local government policies for commerce and industry, and at the center of these policies are the financing policies. There is thus no significant difference between the small business policy priorities of the central and local government.

The Finance Division of BCI contains four subdivisions, three (14 employees and 3 managers) of which implement policies directly related to small businesses. The Finance Subdivision (4 employees) is responsible for a wide variety of tasks such as providing information on government loan systems and assorted financial guidance. The Credit and Cooperative Subdivision (7 employees) is in charge of financing through cooperatives and tasks related to the credit guarantee system. The Equipment Modernization Subdivision (3 employees) is in charge of tasks related to loans for modernizing equipment.

Let us consider the policies for modernizing small policy equipment as an example to illustrate the division of roles between the central and local governments. Of these four measures, the budgetary burden for 1 and 3 is equally divided, and that for 2 and 4 is wholly on Hyogo Prefecture:

1. *Loans for modernizing equipment:* ¥1.6 billion. In line with the Small and Medium-sized Enterprise Modernization Promotion Act.
2. *Expansion of funds for loans for the promotion and modernization of local industries:* ¥550 million.
3. *Equipment-leasing system.* In line with the Equipment Leasing System established in 1966, the central and prefectural governments provide loans to an equipment-leasing agency (a public service corporation). The equipment-leasing company then purchases machinery and leases it to small enterprises. Total loans for leasing are ¥1.65 billion.
4. *System for leasing high technology and energy-saving equipment.* The Hyogo Prefecture equipment-leasing agency purchases equipment and leases it. Total purchases for leasing are ¥700 million.

Besides financing policies, the most conspicuous measures among the policies for small businesses in Japan are the various activities called consultation, diagnosis, guidance, advice, and assistance. Here I explain the scope of the 'technical assistance' granted though the Hyogo Prefecture Institute of Industrial Research, of which the Industry Division is in charge of. The Industry Division of BCI, with 17 employees and 6 managers, consists of two subdivisions, the Manufacturing and Mining Promotion Subdivision with 4 employees and the Local Industry Areas Promotion Subdivision with 4 employees, and two offices. Three technical centers (TCs), each with a special purpose, are subordinate to the Institute of Industrial Research: the TC for machinery and metals (16 employees), the TC for textiles (15 employees), and the TC for leather (13 employees). The institute has 74 employees for its own, and therefore employs 118 people in total. The origin of the institute was the establishment by the prefectural government of an Industrial Experiment Station in 1917. The newest technical center (the TC for leather) was established in 1948, just after the War. In 1967, the allocated number of total employees was 126, and the TCs had 20, 21, and 7 employees, respectively, suggesting little changes in 25 years.

These types of institutions and TCs are not peculiar to Hyogo Prefecture. Every

prefecture has its own institutions, whose origins, and roles are quite similar. As in the case of Hyogo Prefecture, which has special interests in specific industries such as textiles and leather and has established TCs for them, each prefectural government has institutions for specific industries (usually local industries). The effectiveness of those technical assistance policies can be evaluated in part by the ratio of the total number of technical personnel to the number of small businesses. In the case of Hyogo Prefecture, there were 188 technical personnel for 272,000 establishments (34,000 in manufacturing alone). Even if these policy measures were effective, their overall impact could not have been great.

An Overall Evaluation of Small Business Policies

Although the scope of Japanese policies for small businesses is extensive, they have not effectively supported small businesses. Neither, therefore, have they stimulated overall economic growth. Any lessons to be learned from the Japanese experience are therefore negative: it is of no use to imitate Japanese policies for small businesses. To learn why so many small businesses now exist in Japan, we should search for causes and mechanisms other than government policies.

Some observers, especially non-Japanese, have been impressed by the existence of SMEA and the wide variety of its policy measures.⁵¹ However, this ignores the basic nature of the Japanese administration system. In Japan, almost every industry has a counterpart in government - such as the Steel Industry Section of MITI and the Securities Bureau in Ministry of Finance - which devotes all its efforts to protecting, encouraging, and supporting the firms in that industry. Therefore, almost all industries are systematically and continuously protected and supported by the government. The case of small businesses is no exception. The problem comes from the simple fact that nobody can protect and subsidize everybody.⁵²

Readers may wonder why the government's policy menu has been so extensive, why small businesses have been so enthusiastic about those policies, and what the basic characteristics of those policies are. Although this paper has not considered these questions, I will close this section with a brief response.⁵³

1. The basic and common character of the policies for small businesses has been 'social,' and not 'economic.'
2. Although the policies have not been effective in improving consumer welfare, each policy worked as a subsidy for some small businesses and had redistributive effects. The enthusiastic response from some political groups follows from this fact.⁵⁴
3. Almost always, a new policy requires a new law and a new organization with employees. These employees will then resist any attempt later to reduce the size of government. As a result, in Japan as everywhere else, it tends to be easy to expand government organization but difficult to reorganize it and almost impossible to shrink it. The

⁵¹ Calder [1988, pp. 312-13], for example, observed that: 'While the Reagan administration in the mid-1980s was attempting to disband the U.S. Small Business Administration and end its meager and declining volume of subsidized loans, the small business-oriented People's Finance Corporation in Japan disbursed nearly the volume of subsidized loans annually of the vaunted Japan Export-Import Bank.'

⁵² For the details on this point, see Miwa [1996a, Chapter 8].

⁵³ For the details see Miwa [1998a, Section V of Chapter 3].

⁵⁴ Sometimes such enthusiastic movements demanding 'new' policies for small businesses appear to be for the sake of professionals in the movements, nor for small businesses, as is often the case for political movements.

expansion trend and the extensive menu of policies is a direct reflection of this logic of government organization.

[VI]. Conclusion

During the Transition Decade, small businesses, revealing their superior flexibility, rapidly adapted to changes in the circumstances of time and place. The same applies to the machine tool manufacturing industry both during the next decade and under the preceding wartime control. It occurred under the circumstances where small businesses were strictly handicapped under 'the dual-structure' on every side, from the labor market and the financial market to the product market and the market for material procurement. Whether the Japanese economy of this time was not a market economy is not an issue, either. Simply, in Japan once demand for a product appeared or was expected to appear with a profitable business opportunity, a flood of new entrants appeared. Procuring resources such as capital, labor, and production materials, and cultivating distribution channels for their products, they made profits. On the process the role of the government was negligible, if any. Whether Japan's economy of this period was a market economy is a matter of definition. Such a responsiveness of individual participants in a decentralized manner, however, is one of the key characteristics of well-developed market economies, most agree, I believe, that the market worked so well in Japan even during these periods, before the 1970s.⁵⁵

⁵⁵ To those readers still holding a sense of closeness to conventional wisdom and popular view on these points, such as Okazaki and Okuno-Fujiwara[1993] and Noguchi[1995], it is my advice to examine carefully whether they are based and presented with well-examined empirical foundation, whether they draw the conclusion, not directly from the description, particularly reports and documents of the government, on the appearance of institutions and systems such as laws, rules, plans, control associations, and trade associations, but from any research to examine their actual function, and what is the substance of such impressive but vague expressions as 'Japanese economic system', 'the origin (*genryu*)', 'The year 1940 regime', and 'the general mobilization regime'. The next two comments on government regulation apply also to the whole of government activities including 'planning': 'Innumerable regulatory actions are conclusive proof, not of effective regulation, but of the desire to regulate' (Stigler and Friedland [1962, p.1]) . 'What the regulatory commissions are trying to do is difficult to discover; what effect these commissions actually have is, to a large extent, unknown; when it can be discovered, it is often absurd' (Coase [1964, p.194]) . Any 'plan' prepared by the Power, backed by his instructions, will not materialize automatically. If 'plans' and 'instructions' were so effective as once widely believed, ex-socialists economies would not have collapsed in such miserable performance.

Many readers both at home and abroad would reply that where there is smoke, there is fire. Most non-Japanese Japanologists love this reply, since they first were interested in Japan because of her 'singularities.' Here I quote two parts from a section entitled 'A Prior Rejoinder' in the 'Introduction and Summary' Chapter of Miwa[1996a]. 'I would like to mention a Japanese proverb coming originally from China: "One dog barks at a shadow, and a hundred dogs at the voice" (an approximate equivalent in English may be "Much ado about nothing") and ask them to recall what the wrong dual-structure view was and what the fire was. My work on the corporate group model...is analogous to examine the validity of the existence of UFOs' (pp.27-28). 'Readers may comment, 'why so much discussion and new literature on Japan's main banks and industrial policy?' My answer is threefold. First, many ignore the *post hoc, ergo propter hoc* fallacy. Second, strong demand for the discussion and literature exists among politicians, government officials, journalists and academics, particularly in the former socialist economies. It creates the supply, which the politicians and government officials in Japan support enthusiastically both on the belief of the effectiveness of government policy and for their own self-justification. Third, as is usually the case, the authors of the literature on main banks, for example, are only those who are interested in them. Thus, there now exist the "main bank literature industry" and the "Japan's industrial policy literature industry"' (p.28).

I take the view of Stigler [1988, pp. 111-12], concerning with Gardiner Means's doctrines, that: 'It is fair

The central question essential for drawing lessons from the Japanese experience for countries in transition from centrally-controlled economies toward decentrally, market-led ones is why the market worked so well in Japan during this transition period, rather than what was the government's role in managing the transition and promoting the high growth. As everybody understands, this is a hard question to answer. Three observations should be noted: (a) The high profitability of small business must have induced many to begin new operations. (b) There was little expectation of government's support and high rewards from old jobs, and many people by themselves searched for new way of living. (c) After a decade of transition hard days many launched into the venturesome high growth process only with old equipment. Japan has been, like other industrialized countries, a country dominated by small businesses. As nobody can subsidize everybody, no government has effective policy weapons to create such a mass of small businesses. Only 'the market' could have done the task given Japan's postwar environment, only part of which was provided by the government. As a result, Japan's recovery and development process was strictly market-driven and therefore unbalanced.

Like Japan under transition in the first postwar decade, most people, perhaps people in the government particularly, are pessimistic about the future during the transition period, with a low demand pressure and wide and drastic change both in social- and industrial structure. Only people in the market, particularly small business entrepreneurs, can be vital and optimistic enough to look and go forward. What the government can do is at most to provide stable social environment, having the market work smoothly. Fortunately, the Japanese government was unreliable so people looked to the market for solution but reliable enough to maintain the social stability. Thus it was not too weak, but not too strong. With this government the market worked so well, creating many vital small businesses, for which demand shortage was the most serious restriction.

In order to draw lessons from the above discussion, we have to pay attention to the difference of environmental conditions, including initial conditions at the beginning of the transition period, in Japan from those in East European countries. It is again a hard task for me having almost no knowledge about the latter, which, in my view, should be carried out carefully as the next stage of research, cooperating with those who have ample information on these points and are able to discuss the difference. However, at least the importance of the following five points is obvious: (1) Even the prewar Japan was dominated by small businesses, and the government has never made an effort in increasing the number of small businesses. Instead they have been always complaining of an 'excessive competition' due to their abundance; (2) The government has never been strong enough to intervene into the private sector and change their basic industrial structure, unable to strongly control the economy like a command economy even under the War. As a result, the policies for industries have been always indiscriminate and almost always ineffective; (3) Coupled with (1) and (2), a long history since the feudal Japan maintained well-organized distribution networks, coordinated typically by wholesalers, were available even at the start of the Transition Decade; (4) Japan at the start of the Transition maintained also well-developed markets for inputs, such as labor, materials, and capital and credit; (5) With the above four points, people were well aware of the unreliability of the government, and they looked to the market for their survival and improvement of life.

to say that Mean's doctrines are much less widely held in economics than they were in the Great Depression, but their persistence is a remarkable tribute to their palatability to ruling political thought. Once an idea is widely accepted, it is guaranteed a measure of immortality. Its decline in popularity is more often due to changing interests than to contrary evidence, no matter how powerful that evidence may be.'

I close this paper, making reference to the fact that in today's Japan, in the mid-1990s, 50 years after the War and 40 years after the transition decade, 'deregulation and administration reform' is the political issue of the highest priority. Just after the transition decade Japan witnessed a hot economic-order-controversy in and around the government (MITI), called the 'Industrial Order Controversy [*sangyo taisei ronso*],' in which people discussed to what extent and in what form the government should intervene into the market, particularly into the manufacturing sector. MITI strongly asserted in vain for the government's intervention, or 'participation,' into the market, emphasizing the 'government-private sector cooperation [*kan-min kyochō*],' otherwise the market would result in 'excessive competition.' In consequence of MITI's failure in enacting a new law allowing their intervention, MITI's argument, for the need of the government intervention into the market, received a full empirical test. So did the assertion that the free market would work also in Japan.⁵⁶ What the world observed is an obvious result, perceived by everybody as the glorious industrial success of the Japanese economy, particularly in the manufacturing sector, to which the market free from the government's active participation contributed much. No serious sign realized of what the government asserted for justifying their intervention such as 'going too far of the market mechanism,' 'excessive competition,' and 'chaos in the market order.' Thus, in almost every manufacturing industry, without individual industry act, before and after 1960 there was neither drastic deregulation nor clear change in the government policies toward the industry.

I refer to the public's strong attention on 'deregulation and administration reform' in recent Japan in order to emphasize what follows below. Japan's recent deregulation and administration reform focuses, intending to let the market work more freely, particularly upon the sectors where the government has actively intervened into the private enterprise's activities through such instruments as individual industry acts and subsidies and the sectors where the government has done the business by themselves. Until very recently, at least, in those sectors the work of the market has been totally eliminated or strictly restricted and all the circumstances are against the market mechanism. Therefore, without the government's overt declaration of the policy change, introducing the market mechanism into those sectors and making it work well would be almost impossible. Before the recent success in deregulation,⁵⁷ in many regulated sectors, such as financial service, transportation, energy, communication, health and welfare service, labor market related service, legal service, education, broadcasting, publishing, and newspapers, people had never discussed seriously how the market would have worked there and what the role of the market should have been. As the result, in those sectors the work of the market has been remarkably weaker than that in the manufacturing sector. The recent focus upon deregulation and administration reform in those sectors reflects the public's clear recognition that the traditional government's role in those sectors have been against their interests. The Japanese people are now paying an expensive bill due to the inappropriate decision made 40 years ago concerning with the work and the role of the market in those sectors. In my view, the most important lesson the governments of the transition economies should learn from the Japanese experience is that imposing inappropriate restrictions on the market mechanism and using it inexhaustively,

⁵⁶ For the details of the controversy see Miwa [1996a, Chapter 8].

⁵⁷ It may sound odd to hear that in the past three years, 1995-1997, Japan made a big success in deregulating the economy, however, it is an obvious fact. For the details of the facts and the process see Administration Reform Committee [*Gosei Kaikaku Inikai*] [1998], and for the details of Japan's recent deregulation and related issues, see Miwa [1997b].

whatever may be the reason,⁵⁸ will incur tremendous cost to consumers over a long period.

Reference:

- Administration Reform Committee [*Gosei Kaikaku Inkai*] [1998] *Soui heno Zen-teigen [All the Recommendations to the Prime Minister]*. Tokyo: Gyosei Kanri Senta [Administration Management Center].
- Aoki, Masahiko and Hugh Patrick [1994] *The Japanese Main Bank System: Its Relevance for Developing and Transforming Economies*. Oxford: Clarendon Press.
- Armstrong, Mark, Simon Cowan, and John Vickers [1994] *Regulatory Reform: Economic Analysis and British Experience*. Cambridge: MIT Press.
- Bishop, Matthew, John Kay and Colin Mayer eds. [1995] *The Regulatory Challenge*. Oxford: Oxford University Press.
- Calder, Kent E. [1988] *Crisis and Competition: Public Policy and Political Stability in Japan. 1949-1986*. Princeton: Princeton University Press.
- Clark, Robert [1985] 'Agency Costs versus Fiduciary Duties', in Pratt and Zeckhauser eds. *Principals and Agents: The Structure of Business*. Cambridge, Mass: Harvard Business School Press.
- Coase, Ronald H. [1964] 'Comment', *American Economic Review*, May.
- Fair Trade Commission, Office of [*Kosei Torihiki Inkai*] [1997] *Fifty Years of Antimonopoly Policies (I and II)*. Tokyo: *Kosei Torihiki Kyokai* [Fair Trade Association].
- Foster, C.D. [1992] *Privatization, Public Ownership and the Regulation of Natural Monopoly*. Oxford: Blackwell.
- Hayek, Friedrich von [1945] 'The Use of Knowledge in Society', *American Economic Review*, September, pp.519-30.
- Kim, Hyung-Ki, Michio Muramatsu, T.J. Pempel, and Kozo Yamamura eds. [1995] *The Japanese Civil Service and Economic Development: Catalysts of Change*. Oxford: Clarendon Press.
- Komiya, Ryutaro [1990] *The Japanese Economy: Trade, Industry, and Government*. Tokyo: University of Tokyo Press.
- Kosai, Yutaka [1986] *The Era of High-Speed Growth*. Tokyo: University of Tokyo Press.
- Krugman, Paul [1994] *The Age of Diminishing Expectations: U.S. Economic Policy in the 1990s*, revised and updated edition. Cambridge: MIT Press.
- Kuroda, Masahiro [1993] 'Price and Goods Control in the Japanese Postwar Inflationary Period,' in Juro Teranishi and Yutaka Kosai eds., *The Japanese Experience of Economic Reforms*. London: Macmillan.
- Mace, Myles L. [1971] *Directors: Myth and Reality*. Cambridge, Mass: Harvard Business School Press.
- Ministry of Finance [*Ohkura-sho Zaisei Shiryo-shitsu*] [1982] *Showa Zaisei-shi [Fiscal History of Showa] Vol. 20: Materials in English*. Tokyo: Tokyo Keizai Shimpo-sha.
- Ministry of Finance [*Ohkura-sho Zaisei Shiryo-shitsu*] [1984] *Showa Zaisei-shi [Fiscal History of Showa] Vol. 1: Sohsetsu, Baisho, Sengo-shori [General Remarks, Reparations, and*

⁵⁸ For instance, such 'reasons' as follow: a vague unrest on the market mechanism due to lack of experience; overconfidence on the competence and function of the State; overvaluation of the 'equity' value and underestimation of the cost to achieve it; the expected effect on the role and position of the people now in power; and the expected influence on the present overall political- and economic system.

- Postwar Management*]. Tokyo: Tokyo Keizai Shimpō-sha.
- Ministry of International Trade and Industry [*Tsusan-sho*][1992] *Tsūsyō Sangyō Seisaku-shi* [*History of Trade and Industry Policies*] Vol.3: *The First Stage. Postwar Recovery* (2). Tokyo: Tsusho Sangyō Chōsa-kai.
- Miwa, Yoshiro [1993] 'Economic Effects of the Anti-Monopoly and Other Deconcentration Policies in Postwar Japan,' in Juro Teranishi and Yutaka Kosai eds., *The Japanese Experience of Economic Reforms*. London: Macmillan.
- Miwa, Yoshiro [1995a] 'Policies for Small Business in Japan,' in Hyung-Ki Kim et al. eds., [1995].
- Miwa, Yoshiro [1995b] 'Five Misconceptions about the Japanese Economy', *Economic Notes* (by Monte dei Paschi di Siena), Vol.24, no.1.
- Miwa, Yoshiro [1996a] *Firms and Industrial Organization in Japan*. London: Macmillan.
- Miwa, Yoshiro [1996b] '*Seifu no Noryoku, Kodo to Kino: (1) Senji Tosei-ka no Kosaku Kikai Sangyō* [The Competence, Behavior, and Function of the State: (1) Machine Tool Industry under the Wartime Control],' *Keizaigaku Ronshū* [*Economic Review*] (University of Tokyo), Vol. 61, no. 4, and Vol. 62, no. 1.
- Miwa, Yoshiro [1996c] 'Small Business in Japan During the Transition Decade, 1945-1955: Lessons for Eastern Europe,' paper presented at the Two Day Conference on Policy Studies to Promote Private Sector Development, 26-27 April 1996, London organized by the European Bank for Reconstruction and Development.
- Miwa, Yoshiro [1997a] '*Seifu no Noryoku, Kodo to Kino: (2) Kikai Kogyō Shinkō Rinji Sochiho kano Kikai Kogyō* [The Competence, Behavior, and Function of the State: (2) Machinery Industry under the Act on Temporary Measure for the Promotion of the Machinery Industry],' *Keizaigaku Ronshū* [*Economic Review*] (University of Tokyo), Vol. 63, no. 1, and no. 3.
- Miwa, Yoshiro [1997b] *Kiseikanwa ha Akumu desuka? [Is Deregulation a Nightmare?]*. Tokyo: Toyo Keizai Shimpō-sha.
- Miwa, Yoshiro [1998a] *Sefu no Noryoku, Kohdo to Kino* [*The Competence, Behavior, and Function of the State*]. Tokyo: Yūhi-kaku.
- Miwa, Yoshiro [1998b] "'Shijō" to "Shijō-ka": Nihon no Kkeiken yori ["Market" and "Marketization": From the Japanese Experience],' in Nakagane, forthcoming
- Nakamura, Takafusa [1993] *Nihon Keizai (The Japanese Economy)*, 3rd. Tokyo: University of Tokyo Press.
- Noguchi, Yukio [1995] *1940-nen Taisei: Saraba 'Senji Keizai'* [*The Year 1940 Regime: Farewell to 'Wartime Economy'*]. Tokyo: Toyo Keizai Shimpō-sha.
- Okazaki, Tetsuji [1993] '*Kigyō Shisutemu* [Corporate System],' in Okazaki and Okuno-Fujiwara eds. [1993].
- Okazaki, Tetsuji and Masahiro Okuno-Fujiwara [1993] '*Gendai Nihon no Keizai Shisutemu to sono Rekishireki Genryū* [Economic System in Today's Japan and the Historical Origin],' in Okazaki and Okuno-Fujiwara eds. [1993].
- Okazaki, Tetsuji and Masahiro Okuno-Fujiwara eds. [1993] *Gendai Nihon Keizai Shisutemu no Genryū* [*The Origin of Economic System in Today's Japan*]. Tokyo: Nihon Keizai Shimbun-sha.
- Okuno-Fujiwara, Masahiro [1993] '*Gendai Nihon no Keizai Shisutemu: sono Kozo to Henkaku no Kanosei* [Economic System in Today's Japan: its Structure and Reformability], in Okazaki and Okuno-Fujiwara eds. [1993].

- SMEA (Small and Medium-sized Enterprise Agency [Chusho Kigyo-cho]) [1992] *Outline of Small Business Policies [Chusho kigyo shisaku no aramashi]*. Tokyo: SMEA.
- Stigler, George J. [1988] *Memories of an Unregulated Economist*. New York: Basic Books.
- Stigler, George J. and Claire Friedland [1962] 'What Can Regulators Regulate? The Case of Electricity', *The Journal of Law and Economics*, Oct.
- Ueda, Kazuo [1993] 'Kinyu Shisutemu, Kisei [Financial System and Regulation],' in Okazaki and Okuno-Fujiwara eds. [1993].
- Vickers, John and George Yarrow [1988] *Privatization: An Economic Analysis*. Cambridge: MIT Press.
- World Bank [1992] *The East Asian Miracle: Economic Growth and Public Policy*, Oxford University Press.
- Yokokura, Takashi [1988] 'Small and Medium Enterprises', in Ryutaro Komiya, Masahiro Okuno, and Kotaro Suzumura eds., *Industrial Policy of Japan*. Tokyo: Academic Press.

Table 1. Per capita GDP in Group 7 countries (US\$ 100)

| | <i>Japan</i> | <i>USA</i> | <i>UK</i> | <i>Germany</i> | <i>France</i> | <i>Italy</i> | <i>Canada</i> |
|------|--------------|------------|-----------|----------------|---------------|--------------|---------------|
| 1990 | 237 | 221 | 171 | 237 | 211 | 190 | 215 |
| 1980 | 89 | 115 | 94 | 133 | 122 | 70 | 106 |
| 1970 | 19 | 47 | 22 | 31 | 29 | 17 | 39 |
| 1960 | 5 | 28 | 14 | 14 | 14 | 7 | 21 |

Source: Bank of Japan, *Comparative Economic and Financial Statistics*.

Miwa [1996a, p. 4, Table 1.2]

Table 2. Real GNP growth rate in Japan, 1945–80 (five-year average, per cent)

| <i>1945–50</i> | <i>1950–55</i> | <i>1955–60</i> | <i>1960–65</i> | <i>1965–70</i> | <i>1970–75</i> | <i>1975–80</i> |
|----------------|----------------|----------------|----------------|----------------|----------------|----------------|
| 9.4 | 10.9 | 8.7 | 9.7 | 12.2 | 5.1 | 5.6 |

Source: Adapted from Kosai (1981, p. 2, Table 1).

Miwa [1996a, p. 4, Table 1.3]

Table 3. Export component ratios of Japan, 1900–1990 (per cent)

| | <i>1900</i> | <i>1910</i> | <i>1920</i> | <i>1930</i> | <i>1940</i> | <i>1950</i> | <i>1960</i> | <i>1970</i> | <i>1980</i> | <i>1990</i> |
|-----------------------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|
| Marine products | 1.8 | 1.6 | 0.9 | 2.6 | 2.9 | 3.6 | 3.2 | 1.6 | 0.5 | 0.3 |
| Tea | 4.4 | 3.3 | 0.9 | 0.5 | 0.7 | 0.6 | 0.2 | 0.0 | 0.0 | 0.0 |
| Coal | 9.8 | 3.4 | 2.3 | 1.5 | 0.2 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Copper | 6.3 | 4.6 | 0.7 | 1.5 | 0.3 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Cotton yarn | 10.3 | 9.8 | 7.8 | 1.0 | 1.6 | 2.1 | 1.3 | 0.1 | 0.0 | 0.0 |
| Cotton fabric | 2.8 | 4.5 | 17.2 | 18.5 | 10.9 | 24.8 | 8.6 | 1.0 | 0.3 | 0.0 |
| Silk yarn | 21.8 | 28.4 | 19.6 | 28.4 | 12.2 | 4.7 | 2.2 | 0.0 | 0.0 | 0.0 |
| Silk fabric | 9.1 | 7.2 | 8.1 | 4.5 | 1.0 | 2.7 | 1.3 | 0.1 | 0.0 | 0.0 |
| Non-cellulosic fibre fabric | — | — | — | 2.4 | 3.6 | 6.0 | 5.3 | 3.5 | 1.4 | 0.7 |
| Pottery | 1.2 | 1.2 | 1.6 | 1.8 | 1.7 | 2.2 | 1.7 | 0.7 | 0.3 | 0.2 |
| Cement | 0.1 | 0.3 | 0.5 | 0.7 | 0.4 | 0.7 | 0.6 | 0.2 | 0.2 | 0.1 |
| Machinery | 0.0 | 0.9 | 2.6 | 1.4 | 13.0 | 10.5 | 25.3 | 46.3 | 46.4 | 75.0 |
| (Ships) | 0.1 | 0.1 | 0.8 | 0.4 | 1.0 | 3.2 | 7.1 | 7.3 | 2.7 | 1.9 |
| Steel | — | — | 0.7 | 0.6 | — | 8.7 | 9.6 | 14.7 | 8.8 | 4.4 |
| Others | 32.4 | 34.8 | 37.1 | 34.6 | 51.5 | 33.4 | 40.7 | 31.8 | 42.1 | 19.3 |

Source: Adapted from T. Nakamura (1993, p. 43, Table 16).

Miwa [1996a, p. 5, Table 1.4]

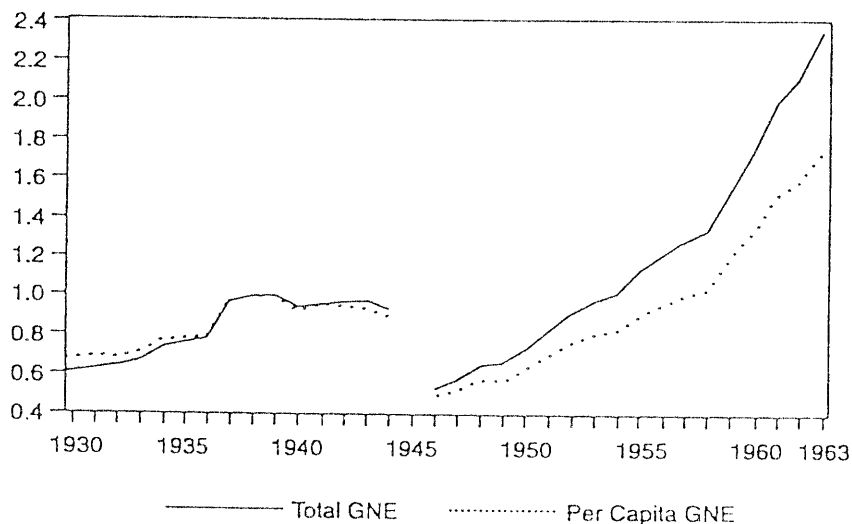
Table 4. Production of selected goods, 1935–53

| | <i>Sewing machines</i> | <i>Electric fans</i> | <i>Radios</i> | <i>Ships (tons)</i> | <i>Three-wheeled trucks</i> | <i>Binoculars</i> | <i>Bicycles</i> | <i>Cameras</i> | <i>Clocks and watches</i> |
|------|------------------------|----------------------|---------------|---------------------|-----------------------------|-------------------|-----------------|----------------|---------------------------|
| 1935 | 12 301 | 43 562 | 153 974 | 174 067 | 9 837 | 81 700 | 903 000 | 95 326 | 4 183 000 |
| 1936 | 40 924 | 42 228 | 427 287 | 274 784 | 12 557 | 79 200 | 1 055 000 | 154 648 | 4 864 000 |
| 1937 | 53 133 | 46 918 | 406 753 | 483 548 | 15 233 | 99 500 | 1 090 000 | 178 321 | 5 114 000 |
| 1938 | 104 204 | 43 575 | 604 463 | 464 679 | 10 450 | 45 600 | 1 080 000 | 187 569 | 3 814 000 |
| 1939 | 132 997 | 58 302 | 740 356 | 391 679 | 7 953 | 62 500 | 950 000 | 205 522 | 3 384 000 |
| 1940 | 154 402 | 64 780 | 852 903 | 401 866 | 8 113 | 60 000 | 1 245 000 | 218 659 | 3 424 000 |
| 1941 | 142 317 | 55 828 | 917 001 | 466 249 | 4 503 | 56 400 | 185 000 | 203 011 | 2 935 000 |
| 1942 | 51 129 | 41 200 | 841 301 | 547 051 | 3 721 | 35 200 | 181 000 | 133 854 | 1 582 000 |
| 1943 | 25 573 | 45 240 | 741 816 | 1 030 601 | 2 259 | 36 100 | 70 000 | 57 588 | 808 000 |
| 1944 | 16 047 | 2 360 | 262 372 | 2 198 790 | 1 338 | 60 000 | 65 000 | 29 548 | 413 000 |
| 1945 | 2 150 | 1 240 | 87 529 | 632 005 | 686 | 14 400 | 20 000 | 13 082 | 98 000 |
| 1946 | 36 912 | 66 282 | 672 676 | 143 860 | 3 647 | 37 836 | — | 24 145 | 714 000 |
| 1947 | 133 949 | 74 329 | 772 428 | 83 565 | 7 432 | 31 158 | — | 51 772 | 1 599 000 |
| 1948 | 165 726 | 72 167 | 769 730 | 162 898 | 16 852 | 47 623 | 337 000 | 53 016 | 2 404 000 |
| 1949 | 274 468 | 95 703 | 702 327 | 163 980 | 26 727 | 97 356 | 552 000 | 83 243 | 3 051 000 |
| 1950 | 493 038 | 118 804 | 281 602 | 229 761 | 35 503 | 115 970 | 981 000 | 117 481 | 2 331 000 |
| 1951 | 1 030 289 | 173 903 | 399 943 | 454 149 | 43 717 | 176 180 | 987 000 | 213 840 | 3 050 000 |
| 1952 | 1 260 293 | 290 879 | 929 126 | 627 064 | 62 262 | 179 510 | 1 019 000 | 357 918 | 3 803 000 |
| 1953 | 1 318 059 | 434 585 | 1 391 031 | 521 759 | 98 405 | 212 704 | 1 184 000 | 663 484 | 4 673 000 |

Source: Ministry of International Trade and Industry, *Kokogyo Seisan Shisu [Production Indexes of Mining and Manufacturing Industries]* (1955); Adapted from Miwa(1993a, p.137).

Miwa [1996a, p. 6, Table 1.5]

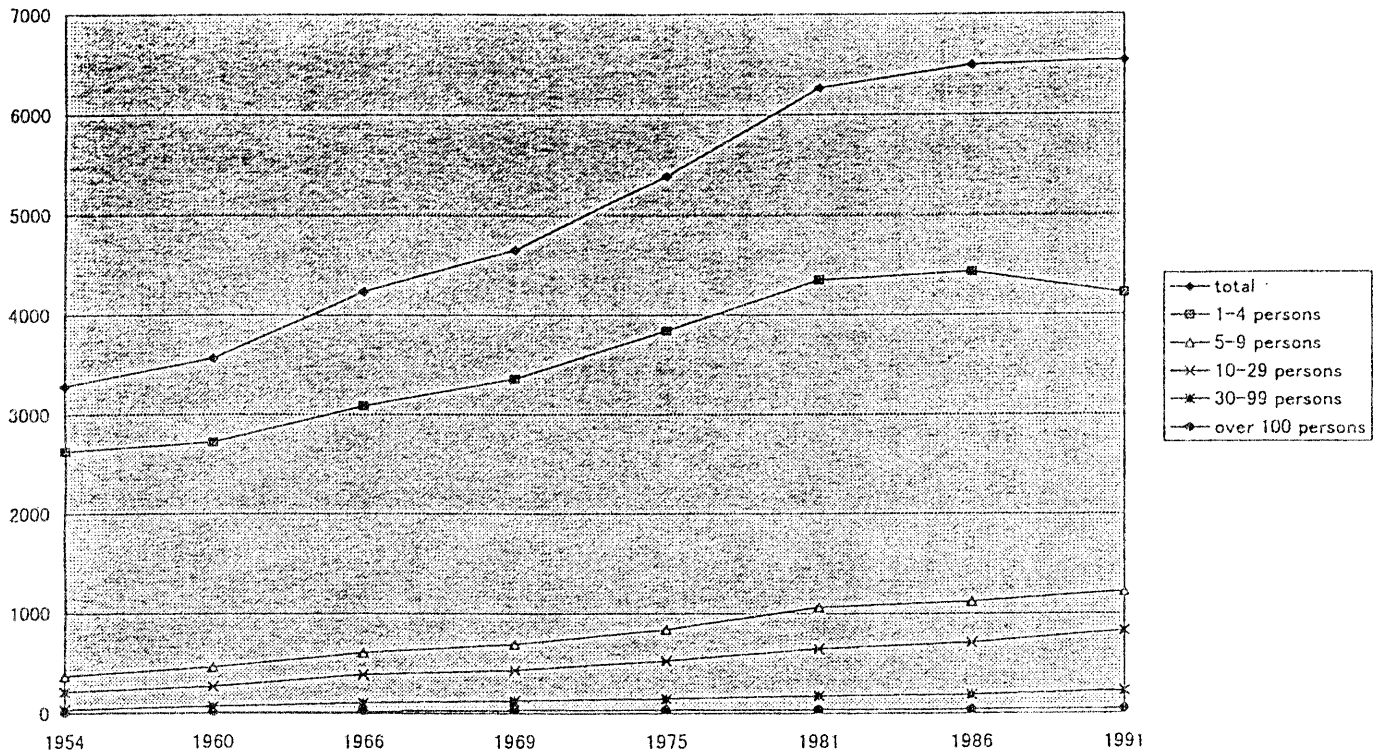
Figure 1. Total and per capita Gross National Expenditure (GNE) at current prices in 1934–6 (1939 = 1)



Source: *Kokumin Shotoku Tokei Nenpo (National Income Statistics Yearbook)*, Economic Planning Agency, 1963.

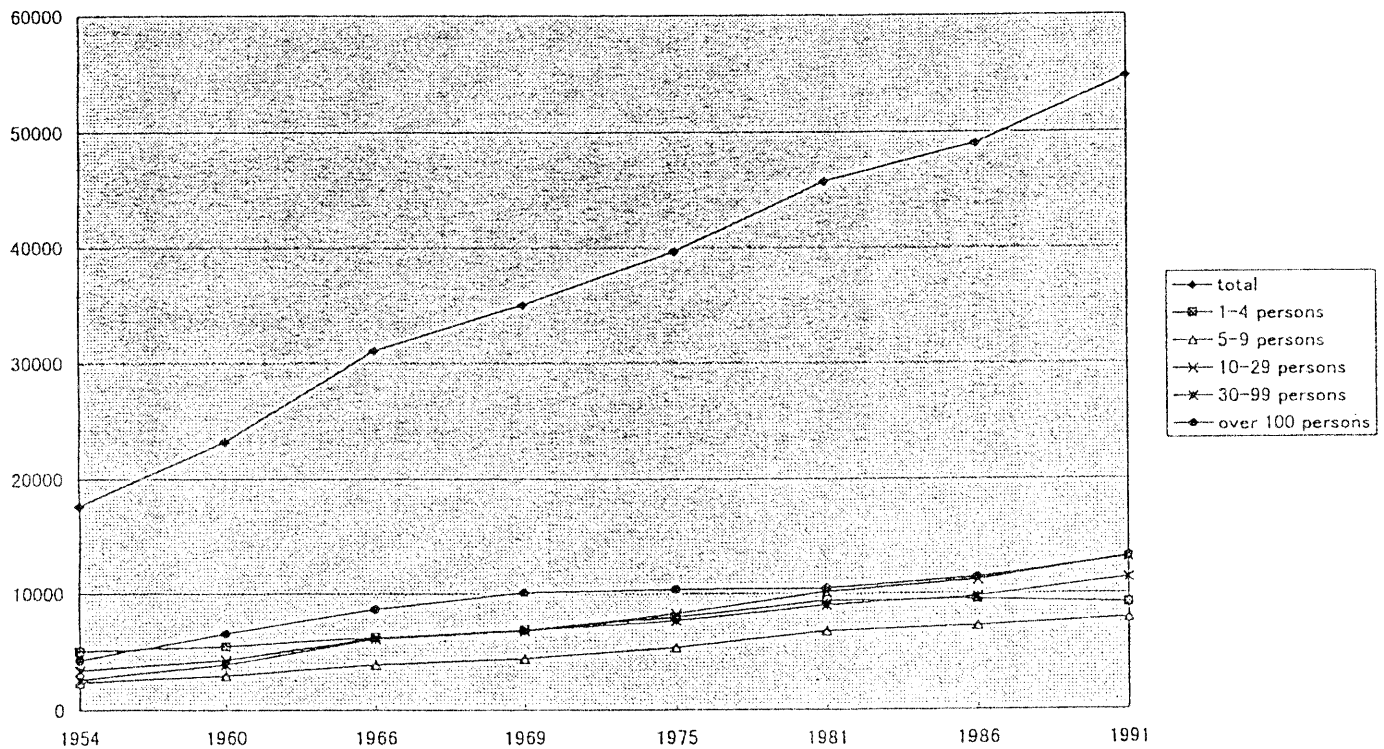
Miwa [1996a, p. 7, Figure 1.1]

Figure 2. The Number of Firms in Each Employment Size Category: Non-agriculture, 1954-1991, unit=1,000

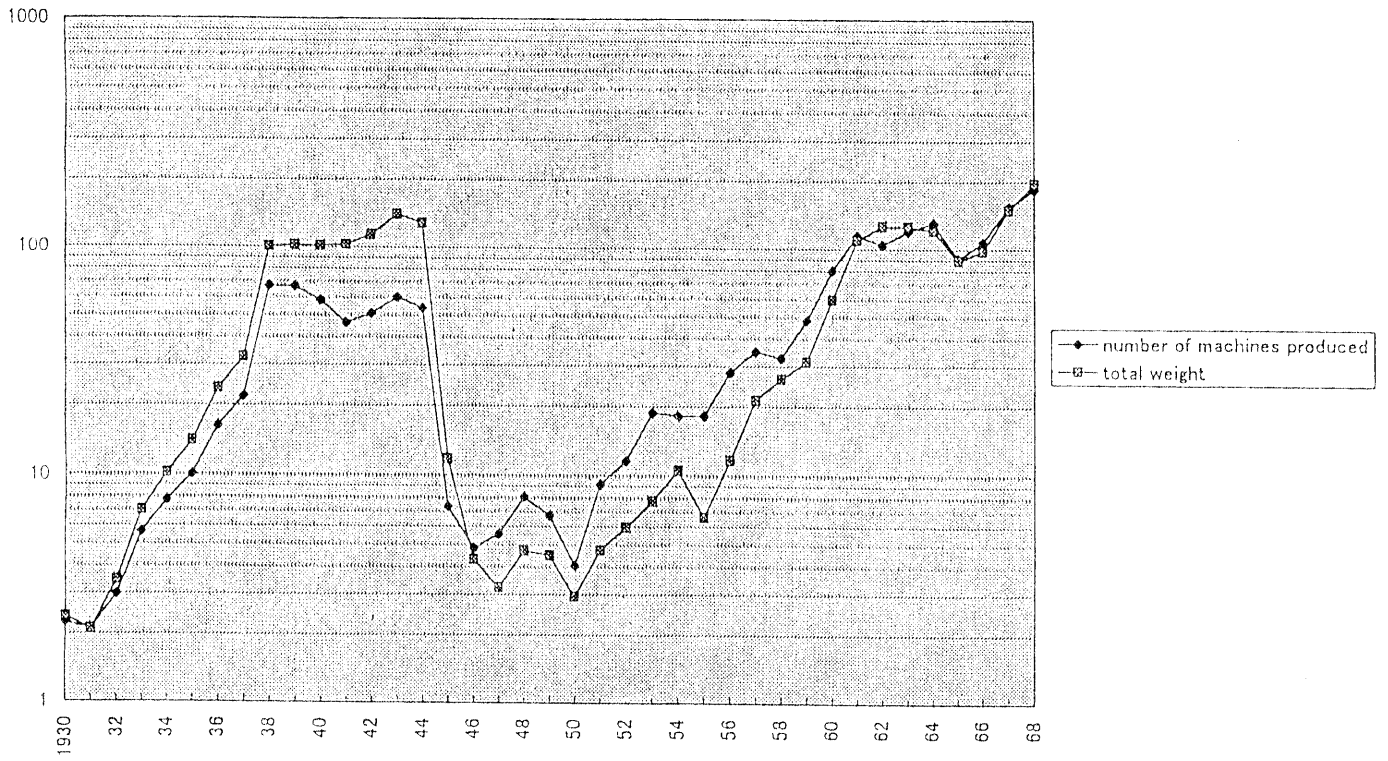


Source: Administration Management Agency, *Census of Establishment*.

Figure 3. The Number of Persons Engaged in Firms in Each Employment Size Category: Non-agriculture, 1954-1991, unit=1,000



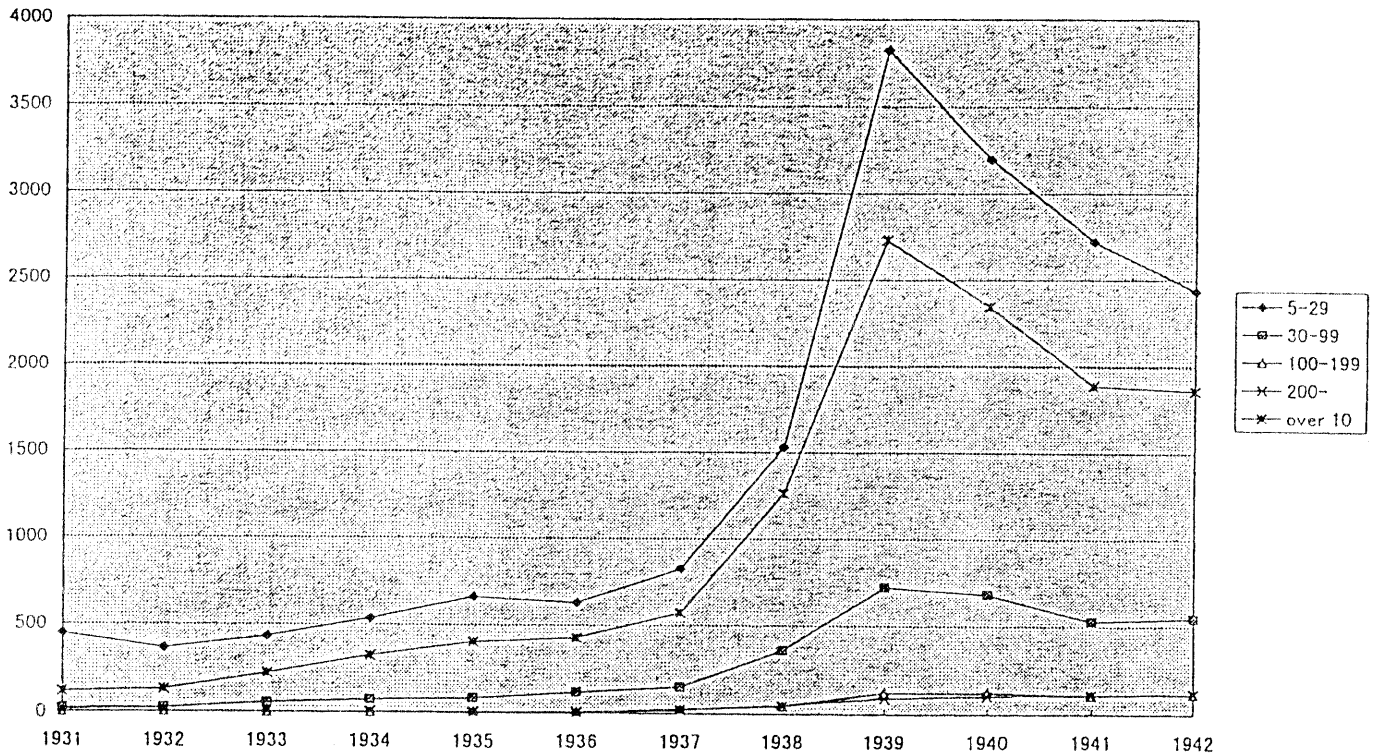
Source: Administration Management Agency, *Census of Establishment*.



Source: Miwa [1996b].

Figure 7.5

The Number of Establishments in Metalworking Machinery Mfg: 1931-1942



Source: MITI, *Census of Plants*.

Table 5. The Number of Establishments and Persons Engaged in the Textile Manufacturing Industry, in Each Size Category, 1909 - 1958
Size in the Number of Persons Engaged.

| | Total(1) | | 5-9 (2) | | 10-29 | | 30-49 | | 50-99 | | 100- | |
|------|----------|---------|----------|-----------|-------|---------|-------|---------|---------|-----------|------|---------|
| | Est. | Persons | Est. | Persons | Est. | Persons | Est. | Persons | Est. | Persons | Est. | Persons |
| 1909 | 15574 | 516190 | 6958 | 49055 | 5602 | 93220 | 1320 | 51469 | 979 | 67556 | 715 | 254880 |
| 1914 | 14081 | 600299 | 5152 | 35726 | 5416 | 91932 | 1399 | 55039 | 1190 | 82005 | 924 | 335597 |
| 1919 | 18800 | 990012 | 7270 | 55291 | 6880 | 126736 | 1903 | 82205 | 1388 | 112590 | 1359 | 613190 |
| 1924 | 18511 | 1032553 | 7502 | 52709 | 6406 | 111084 | 1701 | 68567 | 1412 | 100934 | 1490 | 699259 |
| 1929 | 21532 | 1121781 | 10085 | 67877 | 6325 | 112509 | 1789 | 72838 | 1614 | 118377 | 1719 | 750180 |
| 1934 | 27988 | 1089321 | 13891 | 87090 | 8631 | 150152 | 2141 | 85672 | 1630 | 117132 | 1695 | 649275 |
| 1935 | 29378 | 1135933 | 14311 | 86675 | 9341 | 156881 | 2331 | 93474 | 1666 | 122191 | 1729 | 676712 |
| 1936 | 30506 | 1164924 | 14388 | 86310 | 10154 | 176396 | 2570 | 101804 | 1675 | 122441 | 1719 | 677973 |
| 1937 | 33192 | 1185333 | 17170 | 99810 | 10412 | 176652 | 2404 | 95383 | 1491 | 110248 | 1715 | 703240 |
| 1938 | 33773 | 1137260 | 18179 | 99060 | 10140 | 172759 | 2356 | 94074 | 1424 | 105578 | 1674 | 665789 |
| 1939 | 38272 | 1188897 | 20045 | 138258 | 12743 | 219241 | 2475 | 100558 | 1423 | 106542 | 1586 | 624298 |
| 1940 | 35966 | 1091862 | 19666 | 133671 | 11376 | 195715 | 2131 | 87297 | 1328 | 99964 | 1465 | 575215 |
| 1941 | 33691 | 994478 | 18474 | 129443 | 10717 | 190274 | 1969 | 81584 | 1245 | 95110 | 1286 | 498067 |
| 1942 | 28251 | 840657 | 15411 | 102745 | 8959 | 157035 | 1651 | 68403 | 1117 | 88211 | 1113 | 424263 |
| 1946 | 11860 | 512583 | (3)10295 | (3)174081 | -- | -- | -- | -- | (4)1245 | (4)129323 | 320 | 209179 |
| 1947 | 16484 | 627931 | (3)14875 | (3)235421 | -- | -- | -- | -- | (4)1206 | (4)122519 | 403 | 269991 |
| 1948 | 13732 | 633545 | (3)12119 | (3)199293 | -- | -- | -- | -- | 790 | 62884 | 823 | 371368 |
| 1949 | 15509 | 639545 | 6444 | 48321 | 5785 | 100518 | 1359 | 51933 | 913 | 63608 | 1008 | 375165 |
| 1950 | 26997 | 811847 | 14322 | 86411 | 8703 | 140068 | 1753 | 66713 | 1033 | 70683 | 1186 | 447972 |
| 1951 | 28287 | 908426 | 13984 | 86389 | 9836 | 136659 | 1915 | 72447 | 1254 | 85381 | 1298 | 505782 |
| 1952 | 28886 | 872537 | 13861 | 86781 | 10476 | 168270 | 2037 | 76776 | 1250 | 85576 | 1262 | 455134 |
| 1953 | 29896 | 930178 | 13519 | 85855 | 11358 | 182979 | 2256 | 85018 | 1359 | 92163 | 1404 | 484163 |
| 1954 | 30866 | 915709 | 14139 | 89791 | 11850 | 191072 | 2222 | 83925 | 1292 | 87744 | 1363 | 463177 |
| 1955 | 32404 | 964011 | 13804 | 89701 | 13167 | 213301 | 2486 | 93639 | 1530 | 104393 | 1417 | 462977 |
| 1956 | 33738 | 1038289 | 13919 | 90996 | 13896 | 226290 | 2715 | 102068 | 1672 | 113690 | 1536 | 505245 |
| 1957 | 36176 | 1092854 | 15337 | 99102 | 14536 | 236125 | 2896 | 108959 | 1791 | 121719 | 1616 | 526949 |
| 1958 | 34996 | 1032426 | 14714 | 95302 | 14155 | 231128 | 2813 | 105859 | 1761 | 120052 | 1553 | 480085 |

Est.: the number of establishments. Persons: total number of persons engaged in the establishments in each category.

(1): before 1947 over 5 persons engaged, :

(2) before 1947 5-9 persons engaged, and after 1948 4-9 persons engaged.

(3) 5-49 persons engaged for 1946 and 1947, and 4-49 for 1948.

(4) 50-199 persons engaged.

Source: Plant Census for the period before 1947, and Manufacturing Census for the period after 1948.

Table 6

Rate of profit on equity (paid-in capital) of corporate enterprises in Japan, before tax, all industries

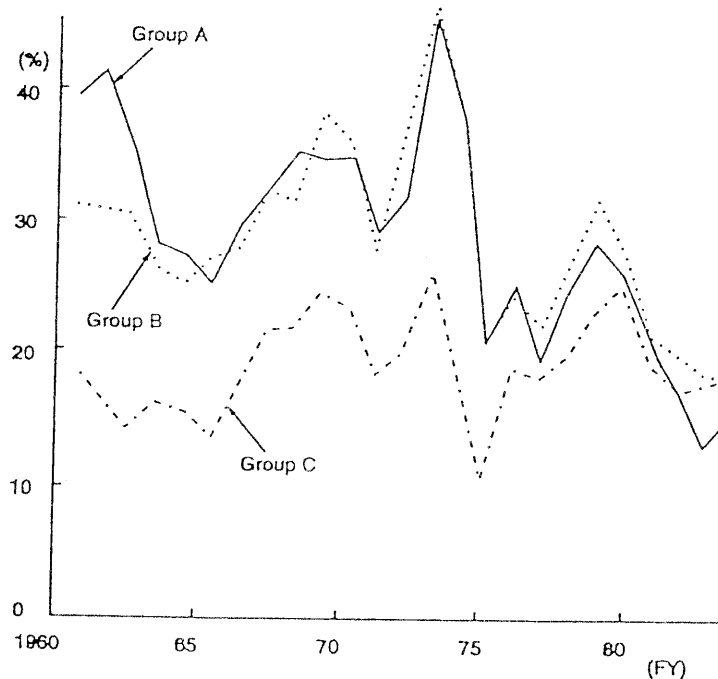
| Firm size by equity (¥million) | Profit rate (5-year running average) | | | | | | Number of years below average profit rate | | |
|-----------------------------------|---|---------|---------|---------|---------|---------|--|---------|---------|
| | 1953-59 | 1960-64 | 1965-69 | 1970-74 | 1975-79 | 1980-84 | 1960-84 | 1960-74 | 1975-84 |
| 2-5 | 22.4 | 32.4 | 30.7 | 34.6 | 22.2 | 16.1 | 7 | 0 | 7 |
| 5-10 | 20.9 | 34.1 | 31.4 | 35.4 | 23.0 | 17.8 | 6 | 0 | 6 |
| 10-50 | 21.2 | 28.7 | 31.2 | 35.5 | 24.4 | 20.9 | 1 | 0 | 1 |
| 150-100 | 18.7 | 25.3 | 26.7 | 30.4 | 23.1 | 24.4 | 2 | 0 | 2 |
| 100-1000 | } 13.1 | 20.5 | 23.3 | 25.6 | 22.0 | 22.3 | 12 | 10 | 2 |
| 1000+ | | 16.2 | 19.8 | 21.3 | 17.8 | 19.5 | 23 | 15 | 8 |

Note: Figures for 1953-59 are adapted from Ryutaro Komiya (1962, Supplemental Table A).

Source: Ministry of Finance, *Hojin Kigyo Tokei Nenpo (Financial Statement of Incorporated Business)* (Tokyo: Ministry of Finance, annual); adapted from Miwa (1990a, p.13, Table 1.1).

Miwa [1996a, p. 38, Table 2.1]

Figure 6 Rate of profit on equity (paid-in capital) of corporate enterprises in Japan, before tax, all industries (per cent)

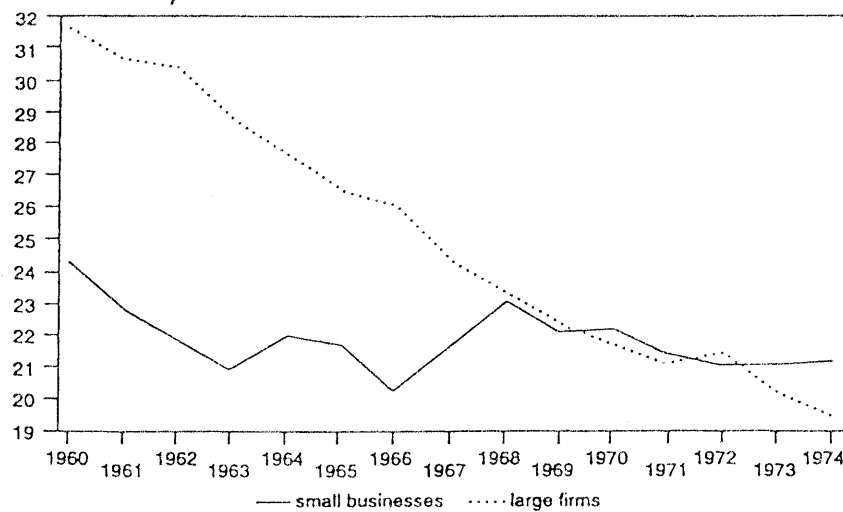


Group A: Enterprises with 5-10 million yen in capital
 Group B: Enterprises with 10-50 million yen in capital
 Group C: Enterprises with more than 1 billion yen in capital

Source: Adapted from Miwa (1990a, p. 13, Figure 1.1).

Miwa [1996a, p. 37, Figure 2.1]

Figure 10. The equity-total capitalization ratio, 1960-74 (per cent)



Sources: Bank of Japan, *Financial Statement of Small Business in Japan* for small businesses and *Financial Statement of Principal Enterprises in Japan* for large firms.

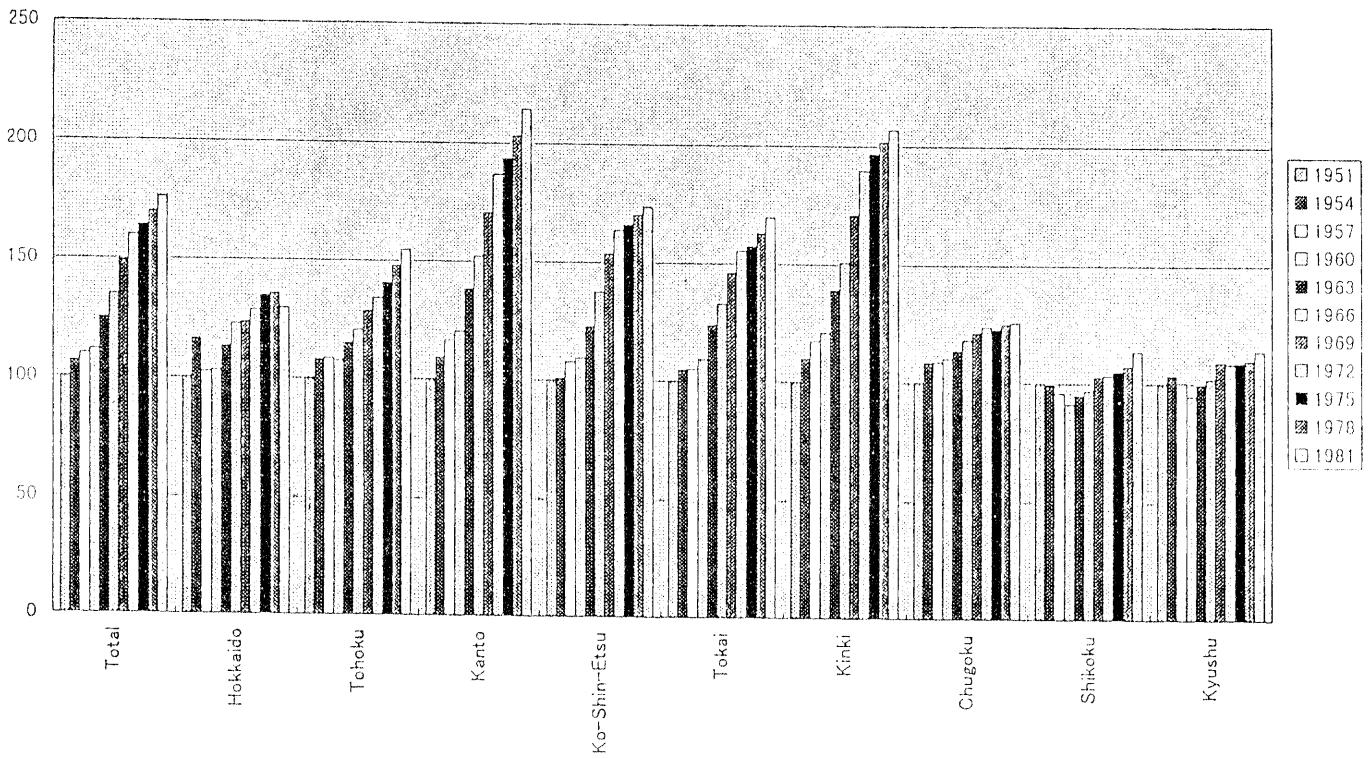
Miwa [1996a, p. 87, Figure 5.1]

Table 7 Japanese car production and exports

| Year | Production | Exported (%) |
|------|------------|--------------|
| 1947 | 110 | 0.0 |
| 1948 | 381 | 0.0 |
| 1949 | 1 070 | 0.0 |
| 1950 | 1 594 | 0.0 |
| 1951 | 3 611 | 0.0 |
| 1952 | 4 837 | 0.0 |
| 1953 | 8 789 | 0.0 |
| 1954 | 14 472 | 0.0 |
| 1955 | 20 268 | 0.0 |
| 1956 | 32 056 | 0.1 |
| 1957 | 47 121 | 0.9 |
| 1958 | 50 643 | 4.7 |
| 1959 | 78 598 | 6.2 |
| 1960 | 165 094 | 4.2 |
| 1961 | 249 508 | 4.6 |
| 1962 | 268 784 | 6.0 |
| 1963 | 407 830 | 7.7 |
| 1964 | 579 660 | 11.6 |
| 1965 | 696 176 | 14.5 |
| 1966 | 877 656 | 17.4 |
| 1967 | 1 375 755 | 16.2 |
| 1968 | 2 055 821 | 19.8 |
| 1969 | 2 611 499 | 21.5 |
| 1970 | 3 178 708 | 22.8 |
| 1971 | 3 717 858 | 34.9 |
| 1972 | 4 022 289 | 35.0 |
| 1973 | 4 470 550 | 32.5 |
| 1974 | 3 931 842 | 43.9 |
| 1975 | 4 567 854 | 40.0 |
| 1980 | 7 038 108 | 56.1 |
| 1985 | 7 646 816 | 57.9 |

Source: Nihon Jidosha Kogyokai (Japan Automobile Manufacturer's Association), *Jidosha Tokei Nenpo*;

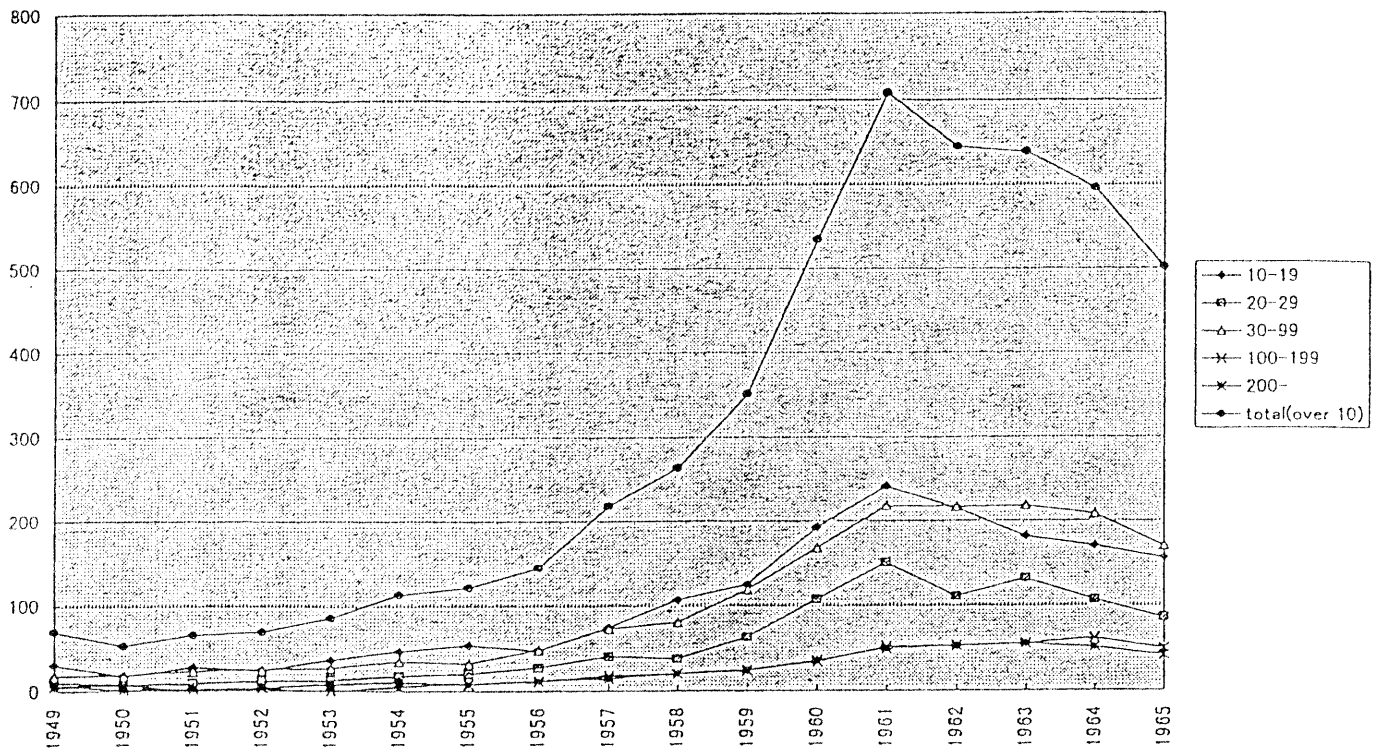
Miwa [1996a, p. 8, Table 1.6]



Source: Administration Management Agency, Census of Establishments.

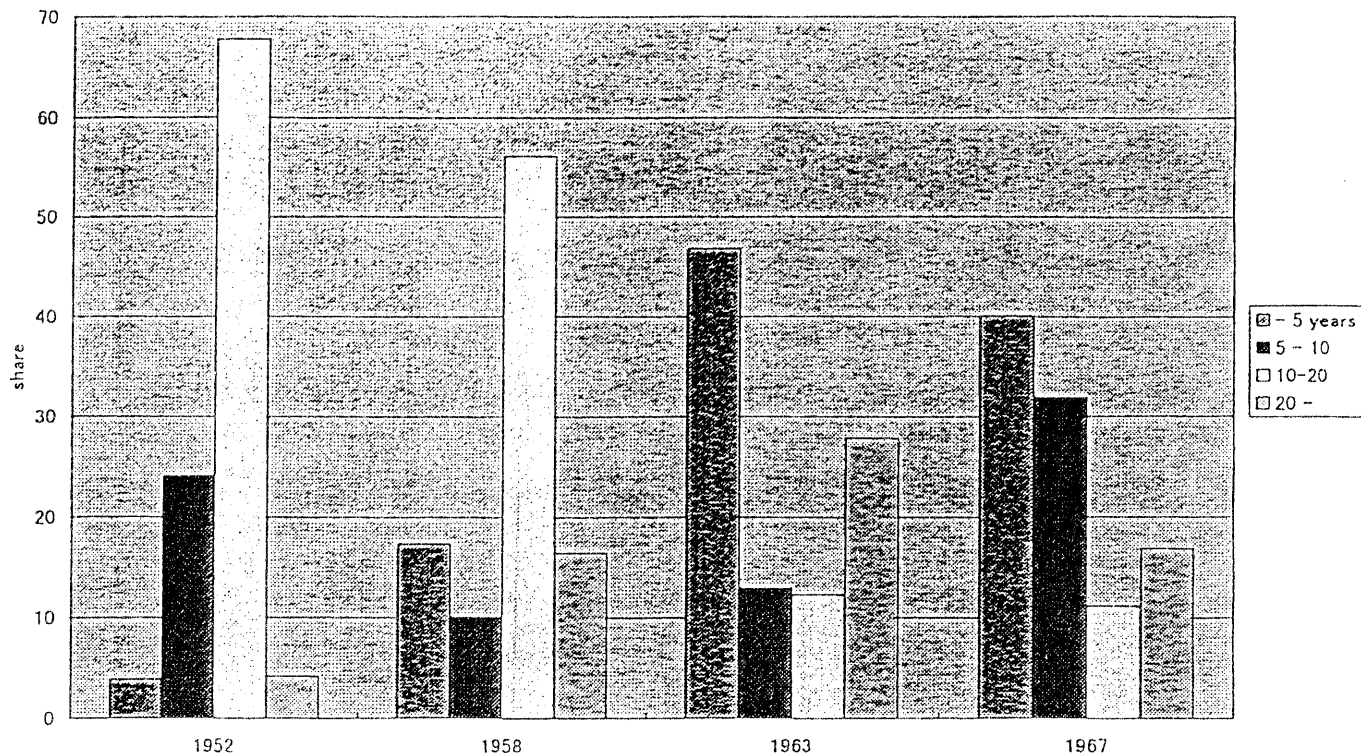
Figure 9

The number of Establishments in Machine Tool Industry: 1949-1965, employees size category



Source: MITI, Census of Manufacturing.

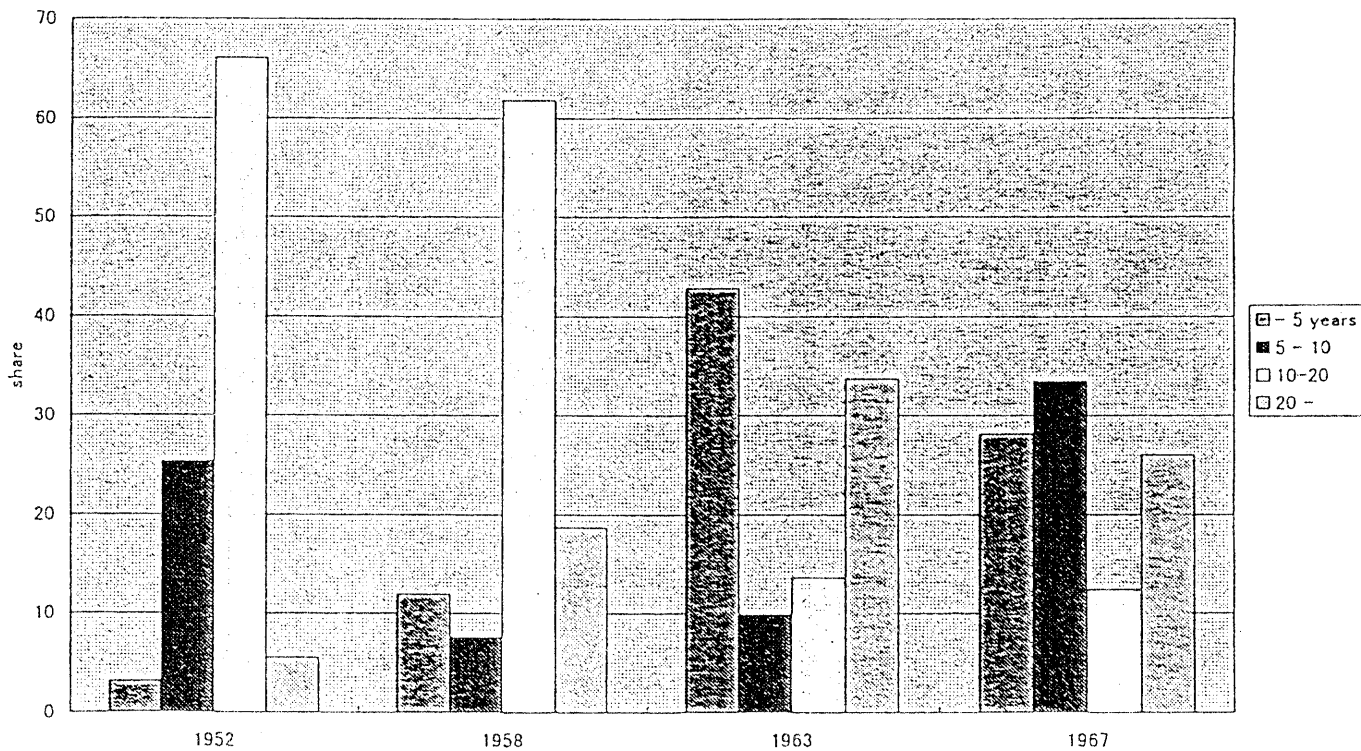
Machine Tool Equipment Vintage (%). Automobile and Auto Parts Mfg.



Source: MITI, Report of the Census of Machine Tool Equipment, 1st - 4th.

Figure 11

Machine Tool Equipment Vintage (%). Metalworking Machinery Mfg. Industry



Source: MITI, Report of the Census of Machine Tool Equipment, 1st - 4th.