

MITI and Industrial Policy of Japan*

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1. MITI is short for the Ministry of International Trade and Industry. As its name implies, MITI is the government office responsible for the management of Japanese international trade and industry. Energy and natural resources, industrial science and technology, and patent are also responsibility of MITI. So, we can say MITI is a counterpart of three ministries of your government : namely Ministry of Commerce, Ministry of Industry and Ministry of Science, Technology and Energy.

2. The policy that is conducted by MITI is industrial policy. The interest and concern on industrial policy and MITI in foreign countries started to appear about ten years ago, and it is growing recently, especially in the U.S. American people used the words "Japan Inc." or "Notorious MITI" at the initial stages, and now they are using "targeting policy".

When I was in New York City that is from 1978 to 1981, I watched, with my own eyes, that not only scholars and students but also so many Congress members, government officials and businessmen were discussing on Japanese industrial policy and roles of MITI. I was asked to talk on this subject many times like today. Some discussion there on industrial policy and MITI's role were negative ones : that is for the purpose to blame Japanese so-called unfair attitude. And other discussion on industrial policy and MITI's role were positive one : that is there may have some good lessons that they can learn from it. Either negative or positive, both discussion assumed that industrial policy and MITI has contributed greatly to the success of Japanese economy after the Second World War period.

It seems to me that the positive discussions on industrial policy and MITI's role are growing than the negative one, and positive interest on industrial policy is growing not only in U.S. but also in other countries such as E.C., Singapore, Malaysia, Republic of Korea etc. I believe this tendency will grow if many people have the correct perception of Japanese industrial policy. Last year, for that purpose, even the formal government base forum was established between Japan and U.S. as Joint Japan-U.S. Committee on industry-related policies and their effect on trade.

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3. Under these situation, I recall with some deep emotion an episode of about twenty years ago. One prominent professor of Economics of Tokyo University declared that there is no economic policy like industrial policy. This professor said, "Economic Policies are composed of only three policies : namely fiscal policy, monetary policy and anti-trust policy. We cannot find any text book on industrial policy in U.S. and he has never heard the words like "industrial policy" in U.S. while he had studied in universities in U.S. There is no room for industrial policy to stand as economic policy. If macro economic policy, namely, fiscal policy and monetary policy, and anti-trust policy are carried out properly, then, all other thing will be done automatically in best way only by market mechanism. So-called industrial policy is just a fake".

To hear that, all our MITI young officials got angry, and we argued like this : "Yes, it may be true that there is no text book on industrial policy in U.S., and it must be true this professor had never heard the words like "Industrial Policy" when he was in the university in U.S. But industrial policy no doubt exists. It is an important part of economic policy and it is necessary for the healthy development of Japanese economy to carry out industrial policy". And we defined industrial policy as "all policies that are conducted by MITI".

Fairly speaking, this definition seems to be a little bit tautology. But essence of this arguement are now accepted by many people not only in Japan but also in many countries. Now our definition of industrial policy is more sophisticated that can be accepted more easily even in the academic circle in Japan. Our definition of industrial policy is as follows :

"Industrial policy is government activities that directly related to the development and adjustment of various industries", whereas macro economic policy has rather indirect relation to them.

4. This definition of Industrial Policy is very broad one.

In reality, there are many types of Industrial Policy.

First : there is *Industrial structure policy*. This is the policy to aim the best industrial structure in the economy. Heavy and chemical industrialization, knowledge-intensive industrialization, high-technology type of industrialization or adjustment of declining industries are the examples of this type of policy.

Second : there is *Industrial Organization Policy*. This is the policy to aim to keep the market mechanism in each industries most efficient and to make each industries use economy of scale. Competition, marger, business tie-up, cartel are the main tools of this type of policy.

Third : there is *Entreprise Behaviour Policy*. This is the policy to aim to make each enterprises activities most efficient and to make them most desirable from various point of view. Introduction of modern or scientific management skill, rationalization of production, quality control, to secure the safety of products or production are the examples of this policy.

Forth : there is *International trade Policy*. To have the better international economic relation is the aim of this policy promotion of import, restrain of export of some products, removing of trade barriers, promotion of overseas investment are the examples of today's Japanese international trade policy.

Fifth : there is *Energy Policy*. This policy aims to have the best mix of energies in the economy. Conservation of energy, development of alternative energy, securing the stable supply of energy, stockpile of oil are the examples of this policy.

Sixth : there is *Medium and Small Enterprise Policy*. This policy aims to keep and strengthen the small business's vitality.

Seventh : there is *Industrial Location Policy*. This policy aims to provide industries better location and to promote regional economic development.

Eight : There is *Industrial Environment Policy*. This policy aims to keep industrial environment clean and safe.

Ninth : there is *Industrial Science and Technology Policy*. This policy aims to develop industrial science and technology in order to enlarge the new frontier of the economy.

Those are the concrete industrial policy. The general name of these various policies is the Industrial policy.

5. Industrial policy and macro economic policy are closely inter-related and both are complementary. For example, adjustment for the business cycle by macro economic policy sets conditions for the application of industrial policy. On the other hand, industrial development and adjustment by means of industrial policy supports macro economic policy through, for example, stable expansion of tax revenues.

But compared to macro economic policy, namely fiscal and monetary policy, industrial policy has three distinctive features.

One : Industrial Policy is sectoral or a *sector base policy*, whereas macro economic policy is (as its name shows) the policy towards Japanese economy as a whole. The policy object of industrial policy is also Japanese economy, but it is sector by sector base : like policy towards iron and steel industry, automobile industry, chemical industry, textile industry, coal mining industry or international trade, energy, medium and small enterprises, industrial location, industrial technology.

Two : Industrial policy is *the supply side economic policy*, while macro economic policy is demand-side economic policy. Main objective of fiscal policy and monetary policy is to control business climate, namely whether to make the economy recover from depression in order to reduce the unemployment or to cool off the boom in order to avoid the inflation. They do it by stimulating or tightening the demand side of economy. On the contrary, industrial policy pays most of its attention to the supply side of economy. In what kind of industrial structure, in what kind of industrial organization and in what each enterprises behaviour, we can produce various goods the most, the cheapest and the best to meet the people's demand? This is one of the important objective of industrial policy.

I recall one impressive speech made by Senator Bentzen, then the chairman of Economic Policy Committee of U.S. Congress about 5 years ago in New York City. He said "We have heard many proposals from Keynesian professors and also from Monetarist professors how to cope with the problem that America faces today. All are very excellent, but I'm sure those menu cannot solve the present problems. Because they all focus on demand side. In order to revitalize American economy again, we have to produce more goods and we have to produce them in more efficient way. For that, supply side of economy is very important. We have neglected so long time supply-side of economy. Now it is the time to do something and to have a policy in supply-side of economy".

Hearing that impressive speech, I said with some proud to one of my German friend who sat next to me that in Japan for long time we had a policy for supply-side of economy. Anyway it is since then in U.S. many people talk about supply-side of economy, and it is since then that in U.S. positive interest on Japanese industrial policy grows in a substantial way.

Three : Industrial policy is the *long term policy*, whereas macro economic policy is rather short term policy. Macro economic policy is often called fine-tuning policy. Its target period is usually three months or six months and at the longest one or two years. You can easily know this when you notice how often interest rate are raised or cut by Bank of Thailand in order to prevent the inflation or in order to boost the economy.

Industrial policy has much longer policy perspective.

Promotion of export cannot be achieved in three months or one year. So do the strengthening of competitiveness of specific industry. The development of alternative energy is a many years task. So is the change of the industrial structure. Most of the objectives of the industrial policy need the efforts of five years, ten years or more than that.

It is in these nature of industrial policy, namely supply-side economic policy and long-term perspectiveness that I feel industrial policy is more important in the developing countries like yours than in advanced economy like U.S.

6. I will mention briefly on the relation between industrial policy and anti-trust policy or anti-monopoly policy.

As in the case of the relation with macro economic policy, industrial policy and anti-trust policy are closely inter-related and both are complementary.

The competitive market that is secured by anti-trust policy set the condition and is the premis for the application of industrial policy. But, at the same time, the anti-trust policy should be complemented by industrial policy. Because, firstly, in the real market which is imperfect competition prevails, effective competition is secured only with the complementation of industrial organization policy. Secondly, from the view point of longterm and dynamism of economic development, anti-trust policy which assumes in their nature static market is not sufficient. Thirdly, in order to maintain effective competition we have to take into consideration not only domestic market but also international market.

7. Not a few people think that Japan's industrial policy is something very special and peculiar. But they are wrong. The government of any country has the responsibility of developing its economy and thereby promoting the economic well-being of its people. Since industrial activity provides the basis for national economic development, it is quite natural that government should be concerned and should conduct various policies related to industrial activities. In fact, industrial policy are practiced in all countries under different names and forms. Japanese industrial policy is only one form of such universal involvement in industrial activity, or just one type of industrial-related policy.

Then why Japanese industrial policy? I feel Japanese industrial policy is one of the best type of industrial related policy in the world, (i) because of its comprehensiveness, (ii) because of its clear self consciousness, (iii) by its for sightedness, (iv) from the view point of its dynamism, (v) because of its effectiveness and (vi) above all because of its success.

8. To see Japan's industrial policy, it is very important to realize that Japan's industrial policy has been changed greatly, in its aims, in its scope and in its tools, during the various stages of economic development. We can say roughly that there are "old industrial policy" and "new industrial policy" which are clearly different in its aim, scope and tools. The industrial policy that was practiced before the middle of 1960's is "old industrial policy". The industrial policy that has been practiced after 1970's is "new industrial policy". They are drastically different in many way. Even today, quite many people discuss and criticize present Japanese industrial policy based on the images of old industrial policy, without paying any attention to its difference. Many books and articles on Japanese industrial policy deal with only old industrial policy. One of the best book

Some industries were selected as industry for nurturing by Industrial Rationalization Council, and various measures were used to commercialize the products of these chosen industries. Allocation of foreign exchange by foreign currency law, control of import of foreign technology and control of investment of foreign capital by foreign capital law, direct government financing through Japan Development Bank and other government financing institution, orientation of the private financing through guideline, various tax benefit, providing industrial estate and regulation of cut throat competition by forming cartels through various special laws or administrative guidances. These are the main tools for those purpose.

(II) the Period of Rapid Growth (1960–1969)

During this period, Japan actively sought to open its economy to foreign competition by liberalization trade and the flow of international capital, and in the process, achieved rapid economic growth.

In 1960 when I joined MITI, Japan's trade liberalization was still low at about 40%. In this year, government adopted "Foreign Exchange and trade liberalization Plan" and started to open Japanese economy. By 1964, the rate of liberalization of trade has reached 93%. The first step towards capital liberalization were taken in 1967, and almost complete liberalization was effected by 1973.

During this period of transition, the primary task was to *strengthen industries international competitiveness* in order to overcome international balance of payments constraints on economic growth and catch up with the developed nation as quick as possible.

As far as policy measures are concerned, the transition to an open economy also meant a transition from direct and regulatory measures to indirect and indicative one. Under such circumstances, a long term vision for the industrial structure was elaborated. This vision was finalized in 1963 after three years investigation and discussion on the present and future state of Japanese industry.

In this vision, the path toward *heavy and chemical industries* development was chosen as most desirable. Accordingly, throughout the decade, and especially the late 1960's, plant and equipment investment, mainly in the heavy and chemical industries, grew more than 20% per year.

To support structural development, various tax measures and finance measures were adopted. But, it is important to know the fact that the real driving force was the active entrepreneurship of the private sector, the government support was only one of support. At the same time, a so-called "energy revolution" was rapidly taking place in this period, with petroleum replacing coal as the chief source of energy. This necessitated structural adjustment in the coal mining industry to deal with the problems of mine closures.

on Japan's industrial policy that I have read is Professor Chalmers Johnson's "MITI and the Japanese Miracle" published in 1982. It is an excellent book, but even this excellent book covers mostly old industrial policy and reference to new industrial policy is rather limited.

9. Then what is the present Japan's industrial policy? What are the aim, scope and tools of new industrial policy?

But before answering these question, let me talk about the brief history of Japan industrial policy. I'll do it because I feel, even in old industrial policy, or more in Japan's old industrial policy, there may be some point to be useful, particularly to your country which are now showing dynamic development and entering into so-called take-off stage.

10. The Japan's economic development during the post war period can be divided largely in three Periods, namely :

- (I) Reconstruction Period (1945-1959)
- (II) Period of Rapid Growth (1960's)
- (III) Period of Qualitative Consolidation (1970's)
- (I) Reconstruction Period (1945-1959)**

During this time, Japan reconstructed its war ravaged economy and laid the ground for viable economic growth. At the end of World War II, Japanese industrial facilities were almost completely destroyed and the condition for production were in terrible disarray. Production of consumer goods had fallen to 30 percent of prewar levels and that for producer goods was only 10%. In such an environment, the rapid recovery of key industries such as electric power, coal, iron and steel and chemical fertilizer was essential to rebuild the economy and to ensure even a minimum standard of living. To this end, a "*priority production system*" was adopted, and the limited raw materials, capital and foreign exchange resources were allocated to such key industries. At this initial stages (latter part of 1940's), allocation and direct control were the main tools of industrial policy.

Then, as the production base developed, direct controls were gradually removed. by the mid-1950's, the Japanese economy had almost recovered, bringing the country out of its material shortages.

Next, *consolidation* of the economic foundation and *rationalization* of industrial productivity were promoted through every policy means available, to prepare for the opening of Japanese economy to international competition. In this period, industrial rationalization was the key word. For that, import of modern machinery and modern technology were encouraged. Expansion of export was also very important policy objective. For that purpose, lowering cost of products were regarded imperative, and enlarging production for the sake of economies of scale were pursued.

(III) Period of Qualitative Consolidation (1970–1979)

In this period, Japan devoted its main efforts to improve the structure of supply and demand. Thanks to the development of heavy and chemical industries in the 1960's, Japanese industry as a whole strengthened its competitiveness in world markets. Since 1965, for the first time in its almost 100 years after started international trade, Japan has consistently run balance of payments surpluses, and by 1975, the material standard of living of the Japanese people had caught up in some respects with that of Western industrialized nations. But, on the other hand, the heavy concentration of industries and population in Japan's Pacific belt area led to serious problems of environmental pollution. Facing these situation, we felt it is necessary to re-examine the industrial policy.

In 1971, the Industrial Structure Council compiled "vision of MITI Policies in 1970's". It proposed a shift to a *knowledge-intensive industrial structure*,

High technology assembly industry, such as in computer and numerically controlled machine tools showed increased growth. On the other hand, textile, sundries, jute and phosphorus become the declining industries. Many firms of these industries were compelled to seek new lines of business or also disappeared entirely. They were labor intensive industries. Because of appreciation of Yen and more intense competition with developing countries they could not survive as it were. Also, because of drastic hike of oil prices after oil crisis, energy intensive industries faced serious difficulties. The oil crisis in 1973 marked a turning point in the direction of energy policy. Energy conservation and development of alternative energy has been promoted.

11. We have quickly reviewed the history of industrial policy in post war period. Then what is the present industrial policy? In march 1980, the Industrial Structure Council submitted a report entitled "Vision of MITI policies in 1980" that you have now in your hand. Based on the recognition that Japan had accomplished its national goal to catch up with advanced nations in Europe and North America, this vision suggests three policy goals.

- (i) Contribution to the international community.
- (ii) Overcome the limitation of natural resources and energy.
- (iii) Co-existence of dynamism of society and improved quality and comfort of life.

As an economic power who has 10% of the world production, Japan should make due contribution to the development of the world economy. Specifically, this contribution must include (1) the maintainance of free trade system, (2) promotion of an international division of labour (3) and comprehensive economic cooperation with developing countries This is the first goal.

As for the second goal : As a nation which rely on import for 90 % of its energy and 55% of its food, Japan must lessen its dependence on foreign supply. This calls for an all-out effort on the government and industry to develop alternative energy, speed up basic reserch and development, and push forward with economic growth.

As for the third goal : Japan's drive for economic growth should be balanced against efforts to improve the quality of life.

The summary of this vision is in your hand, please read it. This is the guideline of the present industrial policy.

12. One important point that I would like to emphasize is that the present industrial policy is aiming to achieve these goals, by *developing the vitality of the private sector* which is essentially *competition oriented*, without distorting the *market mechanism*, on the premise that the domestic market will be kept *open*. By doing so, overall industrial development and adjustment can be facillitated efficiently and through such structural adjustment, trade protectionism will be prevented. This is the philosophy of present industrial policy.

Industrial development and adjustment are achieved primarily through market mechanism and by the vitality of private sector. But it is necessary to complement the function of the market by means of industrial policy. Because (1) real market is not the prefect mechanism like in the text book of economic theory. (2) And there are external economies and external diseconomies. (3) and particularly from the view point of longterm and dynamic industrial development, market cannot provide accurate information. (4) Coordination between countries of international economic relations such as trade and investment cannot be left to market forces. Therefore it must be complemented or improved by industrial policy, This is the *raison d'etre* of industrial policy. under the free-enterprise economy and free market system.

13. Lastly, we will come back to the distinction between old industrial policy and new industrial policy.

There are two clear distinction : one is in the spirit or determination and others related to the tools.

First : Japanese new industrial policy has a strong commitment or determination that "*we will not go back to the protectionism again*". As we have seen before, it is true that Japan had and effectively practiced import quota system and export promotion policy measure such as tax benefit as part of industrial policy. But it was an old story. It was conducted up until middle of 1960's. For example, steel was liberalized in 1961. color T.V.

in 1964, automobiles liberalized in 1965. That means protective industrial policy towards not only light industry but also heavy and chemical industries that were nurtured as important industries in those days, has ended around the middle of 1960's.

Tax benefit for the export promotion was abolished in 1964, and on the other hand, all efforts were made to reduce import tariff rate. Now Japan's import tariff rate is the lowest compared to U.S. and E.C. Furthermore, Japan made a firm determination not to go back to the protectionism again. Today, we can see many examples of the newly introduced protective trade measures in E.C. or even in U.S. facing the severe competition from the developing countries. Japan has no newly introduced protective trade barriers such as import restrictions.

Japan is no exception that there are many industries who faces difficulties because of severe competition with the rapidly growing industries in developing countries such as NIC's.

In order not to introduce new protective trade measures and in order to maintain the free trade system, two policies are necessary and very important.

One : expand the frontiers of their economy.

Two : phase out their declining industries.

From this point of view, there are two broad tasks confronting Japanese industrial policy. One is to facilitate the development of high technology, and other is to encourage positive adjustment in industries facing structural problems. By the development of high technology, our industrial structure can be enhanced and we can reduce the dependence on the traditional type of industries which developing countries such as Thailand are dramatically showing rapid growth. In this way we can reduce the necessity to introduce new import restriction for those products. Structural adjustment of declining industries is also aim to resist the temptation to introduce import restrictions, through reduction of excess manufacturing capacity which lose economic rationality or business tie-up for scale of economy or revitalization investment for technological development or energy conservation. In this way, we can say that new industrial policy is the policy to avoid protectionism and to promote international division of labour and to contribute to the stability and development of developing countries like Thailand.

Second difference : as for tools. Tools of Japan's new industrial policy are very *soft-handed* one, compared that of old industrial policy and other countries' industrial related policy. Tools of industrial policy have changed over the year as we have seen. New industrial policies consists of *indicative* and *indirect* policies and guidelines. In new industrial policy, the visions are considered as the base for policy measures. Tax benefit, financial

measures, budgetary measures or legislative measures are also designed to complement the market mechanism. But they serve only as a pump-priming for industrial development and adjustment. Their contributory effects are limited. For example, the budget of MITI is only 1.6% of Japanese government expenditure. Tax benefit is only 2.7% of total corporation tax revenue. Financing by Japan Development Bank to the industrial development and adjustment is only 0.5% of total money supply for industries.

So, vision is the main tool of new industrial policy. There are various kinds of vision : some cover overall industrial structure; other relate to certain segments of industrial structure or specific problems such as energy and industrial adjustment. And there are also vision called "regional visions" which deal with the development of regional economies.

Vision on the industrial structures are designed usually as follows :

- (1) (a) Analyze changes in the economic society as it relates to industry (such as trends in the needs of the people and state of technological innovation)
 - (b) and analyze the current condition of industry and the industrial structure as reflected in such changes.
 - (c) and clarify the problems involved.
- (2) On the basis of these analysis,
 - (a) clarify emerging trends from such changes in the economic society.
 - (b) and propose a desirable industrial structure to be aimed for.
- (3) Outline policy task for facilitating such an industrial structure and indicate the direction in which such policies will be implemented.

You can see these things in "Vision of MITI policies in 1980's" in your hand.

What is the vision's function ?

Just these information is well-arranged, and useful, and indicates the basic direction of medium and long-term policy. That reduces uncertainties in the market economy, so private enterprises can demonstrate their vitality more fully using these information to form their own strategy in the market. However, it *completely up to them* how they interpret those information or how they use them.

Then why can vision be effective as an tool of industrial policy?. One reason to this related to the fact that many Japanese businessmen know well how visions are formulated and the quality of them. Vision are not formulated by the government alone. They are formulated through open discussions of councils composed of representatives from various quarters, including not just industries but also financial institutions, academic circles, journalism, labour, small business, consumer and local public entities. Daily exchange of views

with corporate managers, careful analysis of industries and industrial structure, and opinion from the press, form the basis of discussion. Typical of such councils is the Industrial Structure Council.

There is a saying "Four eyes see more than two". In this sense, vision are the wisdom that more than four hundreds or four thousand eyes saw. If there is such wisdom before them, don't you think it is clever for businessmen to use that wisdom and to follow it? But as I said, it is up to them whether they use it or not. Here exists the essence of new industrial policy of Japan.



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