

Chapter 1

Introduction: Overview



1 The Mission of the Ministry of International Trade and Industry (MITI)

This book provides an in-depth examination of Japan's policy responses to the economic challenges of the 1980s and '90s. While MITI's earlier role in promoting rapid growth has been addressed in other studies, this volume, based on official records and exhaustive interviews, is the first to examine the aftermath of rapid growth and the evolution of MITI's interpretation of the economy's changing needs. Covering such topics as the oil shocks, trade conflict with the United States, and the rise and collapse of the so-called bubble economy, it presents a detailed analysis and evaluation of how these challenges were interpreted by government officials, the kinds of policies that were enacted, the extent to which policy aims were realized, and lessons for the longer term. The legal basis for MITI policies covered in this volume is found in the following sections of the 1952 Ministry of International Trade and Industry Establishment Law, Article 3 (Odaka 2013, p. 3–4):

- 1.1 Promotion and coordination of trade, and coordination of foreign exchange in commerce
- 1.2 Promotion of international trade and economic cooperation
 - 2 Advancement, improvement, coordination, and inspection of the production, distribution and consumption of mining and manufactured goods
 - 3 Administration pertaining to the rationalization and optimization of commercial enterprises
 - 4 Administration pertaining to weights and measures, and to measurement
 - 5 Operational coordination of electric, gas, and heat utilities (supply businesses)
 - 6 Securing the supply of energy: development of mineral resources, promotion of the utilization of these resources, coordination of hydraulic power generation
 - 7 Clerical oversight of mine security
 - 8 Affairs concerning industrial property rights

- 9 Promotion and guidance of small and medium enterprises
- 10 Experimental research on the science and technology of the mining industry and dissemination of its results
- 11 Elucidation and dissemination of industrial standards
- 12 Oversight of surveys, statistics, and other duties related to commercial mining and manufacturing
- 13 State-owned trade businesses
- 14 Alcohol monopoly

Although responsible for industrial policy overall, MITI did not have exclusive jurisdiction over it: coordination and cooperation with the Ministry of Foreign Affairs were required on trade-related issues, and with the Ministry of Finance on the administration of foreign exchange and the introduction of foreign capital; shipbuilding, because of its relationship to the maritime industry, fell under Ministry of Transportation jurisdiction, and boundary questions also arose with the Ministry of Posts and Telecommunications with regard to the information and communications sectors.

The need for or pertinence of policy involvement in these areas was dictated in any given era by the then-prevailing understanding of Japan's economic issues (Nakamura 1995). In hindsight, using an economics framework, it is evident that policy involvement arose in cases in which: "(1) the market was under- or undeveloped; (2) information was biased or incomplete (in other words, cases of information 'asymmetry'); (3) an economic entity's behavior raised costs for third-party economic entities (in other words, cases of 'external diseconomies'); (4) market participant behavior was excessively selfish and therefore generating confusion in the market; and, finally, (5) government actions that were deemed necessary for political reasons (such as the resolution of international trade friction) were justified in order to correct, supplement, or revise market movements that did not fully meet their desired role, for the sake of upgrading and improving economic welfare" (Odaka 2013, p. 5). Based on the above, it is now widely accepted that the aims of trade and industrial policy were to (1) encourage market development, (2) correct information asymmetries, (3) remove external diseconomies, (4) maintain market order, and also (5) to respond when necessary for political-economic reasons.

However, a policy's legitimacy was not in its own day explained with words like "information asymmetries" or "external diseconomies," but rather in terms of Japan's economic backwardness, its structural vulnerability, or its lack of international competitiveness. It is probably beyond dispute that this perspective was especially pronounced in the years from postwar recovery to high economic growth, as is made evident in the first edition of the *History of Industrial Policy*, which focuses on the period up until the 1970s. Thereafter as well, however, the Ministry of International Trade and Industry continued to interpret policy issues along the lines of the earlier era and to formulate and promote prescriptions for their resolution. Because these prescriptions were justified in terms of the challenges facing the Japanese economy at any given time, they were not driven by a consistent set of principles. Rather, characteristic of industrial policy was its flexible response to changing times and its attempts through trial and error to develop prescriptive policies to resolve problems (Hashimoto 2001).

2 The Keynotes of Industrial Policy

2.1 *The Organizational Reform of 1973*

Although MITI's approach was characterized by this flexibility, it does not necessarily follow that its policies were ad hoc responses to circumstance. Each era was characterized by major economic trends, such as declining growth rates or the severity of international economic friction, and the attendant changes in the underlying policy philosophy are clearly discernible in the industrial policies addressing these trends.

To summarize in the broadest terms:

Two successive stages are evident in the basic "philosophy" of industrial policy during the period from the 1970s until the end of the century.

Even after the controls of the postwar recovery era had been lifted, MITI continued to adhere to the 1950s model, developing corrective market policy interventions as needed to promote the modernization and rationalization of the Japanese economy. Industrial policy aimed to rationalize key industries, nurture infant industries, and make adjustments for declining industries, and so on, while trade policy was designed to facilitate the orderly expansion of exports and controls on imports suitable for economic development under foreign currency constraints.¹

These policies engendered moves by domestic business for greater independence from the government, as reflected in the Draft Law on Temporary Measures for the Promotion of Specified Industries, as well as international criticism of the close ties between government and business, encapsulated in the term "Japan Inc." It was against this backdrop that MITI undertook a broad reconsideration of its policy aims and measures and shifted its sights to the establishment of an internationally open economic system. Its means were the liberalization of trade and foreign exchange, which began in the 1960s, and the capital liberalization that followed.

The need for policy change was expressed explicitly in the call for a "shift to a knowledge-intensive industrial structure" in the *1970s Vision for Trade and Industry Policy*. This position was based on the recognition that as its heavy and chemical industrialization progressed, Japan was becoming a mature industrial society like the other advanced economies, and that it therefore needed to seek out new directions for industrial development. The limitations of the traditional policy framework were becoming evident as core industries became fully competitive internationally and as independent corporate entities no longer needed government support, meaning that policy questions needed to be addressed from a broader perspective than before.

This policy shift also reflected the need to ascertain what policy measures could be used by way of support, given that liberalization was proceeding more smoothly than expected and that the means of policy intervention were gradually being lost (the

¹Sumiya Mikio, in his general discussion of the history of industrial policy in the first era, pointed out the multifaceted character of policy development, as seen in the terms "birth and nurturing," and "terminal care" for policy corresponding to the life cycle of industries (Sumiya 1994, p. 112).

biggest among these being foreign currency allocation). In the 1970s, when Japan's status as an economic power became fully apparent, it was no longer sufficient in international eyes for Japan to prioritize its domestic interests as if it were still a "small country." Rather, Japan was called on to take responsibility for its influence on the world economy and to make changes to reflect its changing international status.

However, that same growth gave rise to domestic challenges where economic development intersected with people's lives: environmental conservation issues, overcrowding and depopulation, consumer issues, and price problems, among others. The limitations of policies directed at export expansion and at upgrading an industrial structure centered on heavy and large-scale industries became increasingly apparent, generating calls for a more "knowledge-intensive" industrial structure (greater knowledge intensity). At the same time, new and mounting problems in external affairs, including trade friction, the international balance of payments problem, and currency exchange issues, required policy responses.

It was in this context that the Ministry of International Trade and Industry launched a large-scale organizational reform, which marked the starting point of the period under examination in this volume. The basic policy governing the organizational reform—"To achieve a comprehensive internal reorganization of this Ministry by utilizing the particular strengths of the bodies charged with design, planning, and implementation and coordinating among them for a well-balanced result"—was summarized by MITI as follows:

(1) Unification of the trade policy bureaus. This meant reconfiguring the existing International Trade Bureau and Trade Promotion Bureau as the International Trade Policy Bureau and International Trade Administration Bureau.

(2) Conversion of the existing Enterprise Bureau into the newly named Industrial Policy Bureau, in order to strengthen efforts toward cross-sector (horizontal) policy principles.

(3) Establishment of the Industrial Location and Environmental Protection Bureau to engage actively in their namesake issues.

(4) Reconfiguration of sector-specific organizations (vertical divisions). For this purpose, the various industries were reassigned according to shared organizational principles into the Basic Industries Bureau, the Machinery and Information Industries Bureau, and the Consumer Goods and Services Industries Bureau.

(5) Last but not least, the establishment of the Agency of Natural Resources and Energy, charged with promoting a strong and comprehensive energy administration (Odaka 2013, p. 262).²

The trade policy bureaus (item 1) were reconfigured so that international economic policy planning would be undertaken in one, and trade policy—a unified administration of exports and imports, insurance matters, etc.—in another. The Industrial Policy Bureau (item 2) was charged with the central task of coordinating shared policy areas, while its divisions focused on specific areas: the Price Policy Division concentrated

²Original materials are found in Ministry of International Trade and Industry, *Overview of the organizational reform of the Ministry of International Trade and Industry*. June, 1973.

on price problems, the Business Behavior Division “promoted appropriate corporate action,” the Industrial Structure Division “forwarded the knowledge intensification of the industrial structure,” and the International Business Affairs Division “promoted industrial structure policies from an international perspective.” With the establishment of the Industrial Location and Environmental Protection Bureau (item 3), the departments related to industrial sites (previously in the Enterprise Bureau) and pollution protection were integrated into a single bureau. Similarly the Agency for Natural Resources and Energy, was established as an affiliated agency that combined the former Mining and Coal Bureau and Public Utilities Business Bureau. The merger was based on the reasoning that a comprehensive and powerful resource and energy administration is needed in order to advance policies in such areas as: the securing of stable supplies of resources and energy, energy efficiency, the increasingly serious pollution problem, resource conservation, and energy conservation (Fig. 1).”

2.2 *Toward a Shift in Industrial Policy*

In order to trace how policy trends changed based on the awareness described above, let us focus on the major issues as seen in the “New Policy” prepared each year by the Ministry of International Trade and Industry (Table 1). The document’s subtitle, “Industrial Policy Priorities” corresponds to the basic policy stance of the government. In the 1970s, this meant responding to the ruling Liberal Democratic Party’s reconsideration of the high-growth path and its shift to pledging to build a welfare society. The emphasis in domestic policy became the “improvement and enhancement of national welfare,” and in foreign policy, the importance of international cooperation in areas such as foreign currency problems.

Under this framework, industrial policy from the mid-1970s on was from the most basic level addressing different policy problems than before, including: (1) how to locate new industries and bring their development to fruition, and (2) how to fulfill Japan’s responsibilities in the international community. The principal areas of focus (the so-called *itchoume ichibanchi* or “priorities”), listed in the policy menus published from 1976–1979 (see prologue appendix), are shown below.

- 1976 Promotion of industrial policy to achieve Japan’s economic recovery and stable development
- 1977 Newly developing industrial policy under stable growth
- 1978 Developing pump-priming measures and new industrial policies
- 1979 Formulating the *1980s Industrial Policy Vision*

Industrial policy had reached a stage of seeking new directions and that contributing to the world economy had become a major priority, reflecting the international pledge made in 1979 by the Takeo Fukuda cabinet. This is an indication that shift in policy principles had occurred.

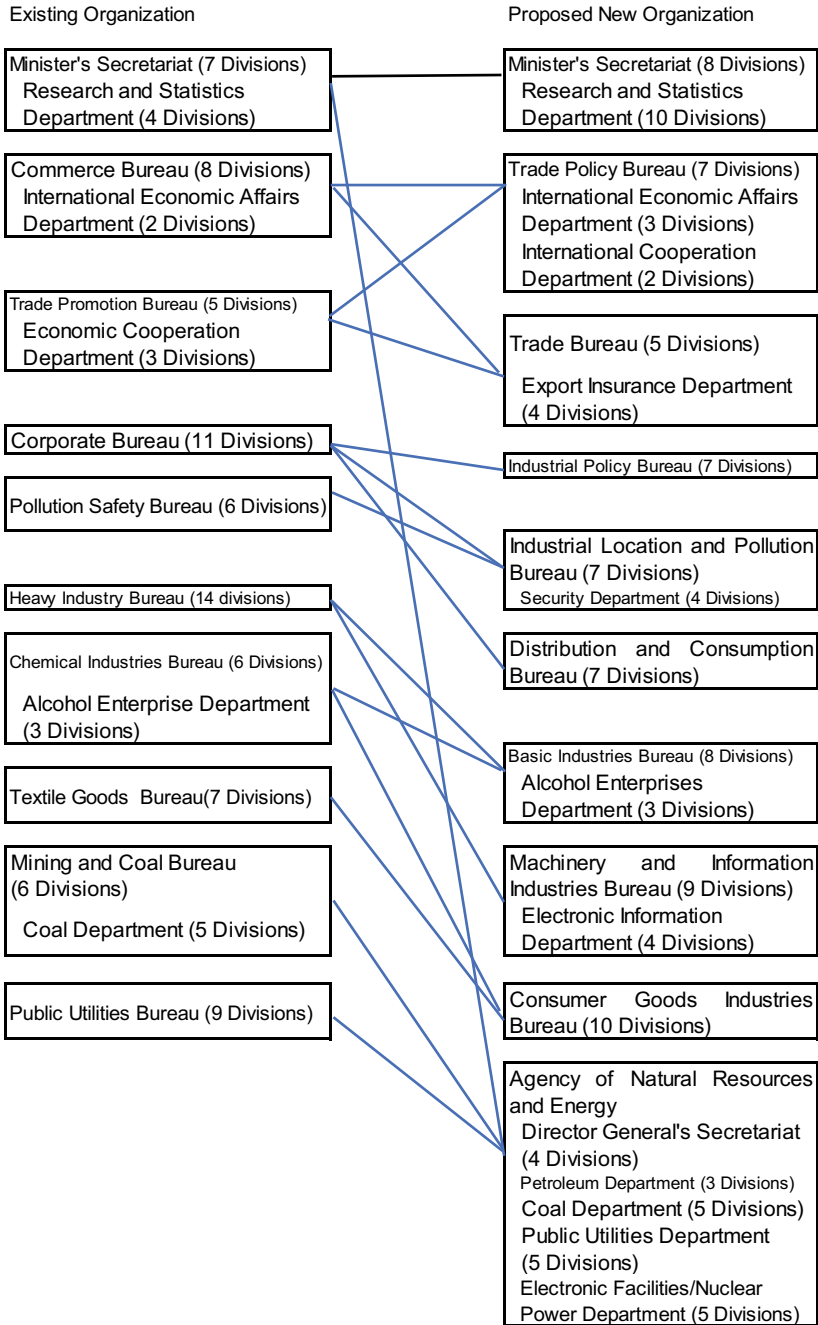


Fig. 1 Overview of the organizational reform (1973)

Table 1 Changes in the headings of the “New Policy Priorities” (FY1973–2000)

FY	“Industrial Policy Priorities” (Subheadings)	“Priorities” (Headings)
1973	The improvement of domestic welfare and promotion of international cooperation	To construct a non-polluted society
1974	The achievement of domestic welfare and promotion of international cooperation	Price stability and an enriched consumer life
1975	The further improvement of domestic welfare and cooperation with the international community	Price stability and an enriched consumer life, to establish the foundations for a comfortable life
1976	The improvement of domestic welfare; contributions to the development of the international economy and society	Promotion of industrial policy to achieve Japan’s economic recovery and stable development
1977	The further enrichment of domestic welfare and active contribution to the stable development of the world economy	Newly developing industrial policy under stable growth conditions
1978	Opening of paths to a new prosperity; and development of Japan’s economy and society	Developing pump-priming measures and new industrial policy
1979	Forming the foundation for achieving an enriched domestic life and a smooth transition to stable growth and securing the motive power for the prosperity and development of Japan’s economy and society	Formulating the <i>1980s Industrial Policy Vision</i>
1980	None	Ensuring energy security
1981	Aiming for a society with vitality and economic security	Establishing energy security and preparing for extrication from petroleum dependency
1982	Aiming to establish the foundations for long-term development of the Japanese economy	Steadily developing a comprehensive energy policy
1983	Aiming for active contribution to the world economy and the establishment of the foundations for Japan’s economic growth	Promoting industrial revitalization and technology development with a mid- and long-term perspective
1984	Contributing to the sustainable development of the world economy and establishing a creative society	Forming the foundation for creative development
1985	Establishing the foundations for long-term development and international contributions thereby	Building the foundation for technological development
1986	Achieving new dimensions of internationalization and establishing the foundations for long-term development	Aiming for new dimensions of internationalization

(continued)

Table 1 (continued)

FY	“Industrial Policy Priorities” (Subheadings)	“Priorities” (Headings)
1987	Toward constructing a new economy and industrial society aimed at creative development	Promoting policies on industrial structure based on an international perspective
1988	Aiming at international harmonization and bringing vitality to economic society	Bringing vitality to local areas
1989	Dedication to the world and new long-term development	Dedication to the international economic community
1990	Toward the realization of “Coexistence and coprosperity at a global scale” and “an economic society replete with leisure and vitality”	Correcting external imbalances and realizing internationally harmonized economic structures and industrial activities
1991	None	Realization of lifestyles of comfort and richness
1992	Seeking “links and coordination with international society” and “creating regional industrial culture”	Dedication to international society and promotion of self-reform
1993	Overcoming global issues and creating a “creative and comfortable society”	Comprehensive promotion of policies on energy and the environment
1994	Self-reform for further development and responsible responses to the international community	Structural adjustments and the maintenance of developmental foundations for creative innovation
1995	None	Promotion of reform to realize a rich economic society opened to the international community
1996	Aiming to create a new economic society	Accelerating structural economic reform
1997	Toward realization of a knowledge-creating country	Structural economic reform aimed at a knowledge-creation country—measures aimed at industrial hollowing out
1998	None	Strongly promoting structural economic reform
1999	Realization of economic regeneration through revitalization of industry	Breaking away from a sluggish macro-economy
2000	Foundations for the regeneration of 21st century economic development	Recovery to stable growth trajectory centering on private demand

Odaka (2013, pp. 30–32). Author’s reconstruction based on Odaka’s table

However, these new directions were not pursued in a clear and sustained way, because of exogenously generated “shocks.” As is well known, price and energy problems came to the fore intermittently during these years because of the transition to a floating exchange rate regime and the turbulent rise in crude oil prices. In the two years immediately after the first oil crisis, MITI found it necessary to prioritize

price stabilization and improvements to consumer life, as evident in the “priority” policies of 1974 and 1975:

1974 Price stability and an enriched consumer life

1975 Price stability and an enriched consumer life, to establish the foundations for a comfortable life.

Similarly, energy policies became the priority in 1981–1982 due to the worsening oil situation:

1981 Establishing energy security and preparing for extrication from petroleum dependency

1982 Steadily developing a comprehensive energy policy.

Among the policies on prices, MITI’s Aggregate Demand Control Policy produced results in a relatively short period, even as compared with other advanced economies.³ Energy conservation efforts began to penetrate, even as the issue rapidly lost its urgency with the stabilization of oil prices.

Moreover, the medium-range aim of decreasing Japan’s dependence on fossil fuels was aided by the mid-1980s takeoff of nuclear power generation at light-water reactors. It became the dominant view that this tailwind would help enable Japan to achieve both economic growth and a stable energy supply.

In this way, the Basic Direction of Trade and Industrial Policies as defined in the early 1970s emerged once again as a top priority concern. Construction of a “long-term development base” frequently appears in the New Policy subtitles, as illustrated in the priority policies of 1983–1985:

1983 Promoting industrial revitalization and technology development with a mid- and long-term perspective

1984 Forming the foundations for creative development

1985 Building the foundations for technological development.

MITI’s emphasis on technological development points to an expectation that the new technologies and systems would become the foundations for future industrial development. This was the case in new energy, developed against the backdrop of urgency in energy issues, in information processing and semiconductor technology, in factory automation (FA), the utilization of microelectronics technology (ME), and, related to these, the area of space development.

Fields such as these require large-scale investment in research and development, making it difficult to rely on voluntary action by private enterprises to assure sufficient investment. In other words, MITI sought policy involvement in areas that could not

³In general, due to small budgets (excluding bank loans based on the Fiscal Investment and Loan Program (FILP)), industrial policy was rarely affected by cyclical fluctuations such as economic stimulus measures. One feature of industrial policy, therefore, was that it was able to maintain its basic stance regardless of fluctuations in the economy. It is therefore not clear how much MITI contributed to the calming of prices under the policies of restraints on aggregate demand. Further investigation is needed on the contribution of MITI to cyclical conditions of this kind.

be left entirely to market forces, and began especially to take note of these as priority issues.⁴

Looking in aggregate at the measures aimed at new industrial development, however, it is clear that they could not be detached from policy authority over the information and communications industries that were at the core of that development.

Although communication means and information acquisition were expanded and diversified far beyond expectation in the data communications field (areas such as VAN, or value-added networks), MITI's involvement in the field, beginning with the liberalization of the principal communication networks, was restricted by its need to share that role with other agencies granted jurisdiction by the government.⁵ This continued to act as a constraint on the effort to develop an integrated industrial policy.

2.3 Emphasis on Free Trade and Deregulation

The development of industrial technology was prioritized over international contributions in the early 1980s because Japan's trade surplus contracted temporarily with soaring resource prices, especially that of crude oil. When crude oil prices then fell, Japan's trade surplus recovered, arousing criticism from the United States and Europe and resulting in serious trade friction. For this reason, MITI's emphasis also shifted to trade policy in the latter 1980s. This is evident in the growing importance

⁴Nevertheless, with regard to pollution and environmental measures, which became policy priorities in this period, strict corporate emissions regulations were maintained based on environmental regulations. It is important to note that the stance of entrusting this to the voluntary action of businesses and expecting that markets would adjust accordingly was not equivalent to the pursuit of a hands-off policy. Of course, MITI's position on this matter served as a counterweight to the strong regulatory bent of the Environment Agency, aimed at preventing excessive burdens being placed on industrial enterprises. In the division of labor among ministries and agencies, MITI's position was in general to restrain interventions in the market. On the other hand, when it came to policy on industrial location, it could use financial and tax incentives to help ease the overconcentration of industrial sites in the Pacific belt. MITI pursued efforts to disperse industrial sites and achieved some results (although no greater a range of diffusion than was originally sought), and MITI therefore did not hesitate to adopt policy measures to correct external diseconomies. In policy on small and medium-sized enterprises as well, traditional interventionist policy measures were maintained in much their original form.

⁵It would not be correct, however, to see MITI's inability to fulfill its own claims as the result only of disputes over authority. Information and communications technology made more progress in development of software than in that of hardware (such as large-scale computers) that MITI had emphasized up to that point. As these became integrated in overall communications at production sites, greater significance was attached to a highly dispersed, guerilla-style development, accumulation, and transmission. This action resulted because MITI was not necessarily able to find policy issues and take appropriate measures to respond flexibly to change, because it had little experience with policy intervention regarding consumer goods. In that respect, the postal administration cannot be said to have been effective either. Regardless, given the continuing restrictions on MITI's involvement in the information and telecommunications field, it was difficult to develop ideas about Japan's future industrial structure and to establish adjustment policies to address them. It should be noted that those restrictions were not removed even in the organizational reform of 2000.

given to international harmonization, and illustrates the fact that in the later half of the decade, a greater priority was placed on international contributions.

- 1986 Aiming for new dimensions of internationalization
- 1987 Promoting policies on industrial structure based on an international perspective
- 1988 Bringing vitality to local areas
- 1989 Dedication to the international economic community
- 1990 Correcting external imbalances and realizing an internationally harmonized economic structure and industrial activities.

Where these policies concerned international relations, the following points are notable:

First, the demand that they be considered for diplomatic reasons—namely, Japan–US relations—placed strong constraints on the policy options; second, they bear the strong influence of the earlier temporary export restraints that had been promoted for the sake of “orderly exports.” As a result, bilateral and bi-regional negotiations under these conditions were repeated endlessly, with only the item in question changing, and Japan was forced to make unilateral concessions.

Nevertheless, MITI continued to promote the development of the Japanese economy while at the same time reaching a clear understanding of the new direction Japan would have to pursue in order to fulfill its international responsibilities. That is, rather than promoting measures that limited free trade, such as voluntary export restraints based on bilateral agreements, Japan would adopt policy solutions based on international rules agreed upon multilaterally. This was the shift in principle that MITI had been seeking since the 1970s. In the negotiations that led to the World Trade Organization (WTO) agreement, Japan’s response to international trade friction was to advocate “maintaining the free trade regime” and to limit the scope of issues handled either by single governments or by bilateral agreements between governments. In other words, it achieved better results in its negotiations with the outside world when it sought to avoid quantitative targets in trade and demands for preferential treatment for certain trading partners. This approach in turn exposed the need to overhaul the myriad regulations that shaped industry and the relationships among industries domestically.

Deregulation arose as a result not of foreign pressure but of internal pressures. To avoid raising corporate taxes, while at the same time overcoming the burden of government debt due to Japan’s post-oil-crisis macroeconomic recovery measures, the Second Extraordinary Administrative Investigative Committee called for “small government,” or administrative reform, in the early 1980s.

MITI, ahead of other ministries and agencies, aggressively promoted deregulation as a measure for easing trade friction. It is not clear that this approach contributed to an actual expansion of imports⁶; its significance was often only symbolic, but

⁶While it is true that Japan’s import structure changed greatly by 1990 with an increase in imports of manufactured goods, the main reason for the change was the overseas relocation of enterprises due to the yen’s appreciation and Asian industrialization; it was not that trade relations expanded with industrialized countries more analogous to Japan.

deregulation conveyed a clear message to the outside world that the government was doing its best within the limits of its jurisdiction. At the same time, given the marked confrontation that had always characterized the relationship between industrial policy and the Antimonopoly Law, this new emphasis on deregulation raised the question of how government could engage in a competitive order shaped by the Antimonopoly Law.

As I argue in detail in the main body of this work, it is apparent from the key industrial policy measures of this era that a major shift took place. The 1978 Law on Temporary Measures for Stabilization of Specified Depressed Industries and the Industry Stabilization Law, the 1983 Temporary Measures Law for the Structural Adjustment of Specific Industries and the Structural Improvement Law, the 1987 Law on Temporary Measures to Facilitate Industrial Structural Adjustment, the 1995 Law on Temporary Measures to Facilitate New Businesses, and the 1999 Law on Special Measures for Industrial Revitalization and the Industrial Revitalization Law all suggest that the thrust of industrial policy was no longer one of seeking exemptions from the Antimonopoly Law.

This approach did not change significantly even after the collapse of the bubble in the early 1990s. The subtitles of the Priority Measures were frequently omitted or the wording changed due to policy fluctuations in the short-lived government administrations of the first half of the 1990s, but as discussed below, there was no perceived need for a major change in the framework of priorities established in the 1980s: (1) to achieve balanced trade through multilateral coordination, (2) to promote regulatory reforms limiting government involvement, and (3) to achieve both a stable supply of energy and economic growth.

- 1991 Realizing a comfortable and affluent lifestyle
- 1992 Dedication to the international community and promotion of domestic reform
- 1993 Comprehensive promotion of policies on energy and the environment
- 1994 Structural adjustment and improvement of developmental foundations aimed at creative innovation.

2.4 Seeking Another Conceptual Shift at the End of the Century

As the recession dragged on, however, regulatory reform began to be deployed as part of the efforts to reform Japan's economic structure. It was also looked to for a comprehensive resolution to multiple policy issues, including the handling of non-performing loans, fiscal reconstruction, and economic recovery.

These efforts indicate that new principles were once again being sought for industrial policy. Because this process is still ongoing, caution is needed in making any definite assessments, but I will make a preliminary attempt to examine the prospects for a shift and the direction it might take.

The principle measures of the latter half of the 1990s are shown below. One of their key terms was the above-mentioned “economic structural reform,” but in this case the explicit macroeconomic goal was economic recovery and a return to economic growth (see 1999 and 2000, below).

- 1995 Promoting reform for a rich economic society open to the international community
- 1996 Accelerating structural economic reform
- 1997 Structural economic reform aimed at knowledge creation, measures for addressing the hollowing out of industry
- 1998 Strongly promoting structural economic reform
- 1999 Pulling out of sluggish macro economy
- 2000 Recovering a stable growth trajectory centered on private demand.

To promote structural reform of the economy, MITI has shifted to a principle of promoting competition and undertaking comprehensive regulatory reform, for example attempting bold changes in its policies on small and medium-sized enterprises to make firms take on more responsibility. Trade policy has also changed somewhat due to Japan’s long-term recession and to the advancing industrialization of South Korea, China, and others, but overall, MITI has adhered to its emphasis on multilateral coordination.

However, faced with the need to focus on macro growth, MITI’s stance on policy has taken on a new dimension. Although industrial policy prior to the early 1990s indeed led ultimately to economic growth, that does not mean that the aim of the policies was economic growth itself. Rather, they were concerned with issues such as distribution and with the distortions to the economic structure that were caused by the market economy. For example, the reason MITI sought the modernization and rationalization of the tiny, small, and medium-sized enterprises that were hindering economic development in the first half of the high-growth period was that it concluded that policy intervention was the only way to resolve the problems posed by the dual economy. Its decision to address such issues as nurturing new industries or the tensions arising with declining industries was also due to its judgment that active intervention was needed for economic development to be realized in the medium term. In the latter half of the 1990s, however, when the long recession came to be viewed as a consequence of structural problems in the Japanese economy, MITI began to see not only structural reform but also economic growth itself as a policy concern.

Because macroeconomic policy was key to the market intervention regulations designed to address the vicious downward cumulative cycle inevitable in market economies, the logic that industrial policy could enable economic recovery simply by ensuring the broadest possible freedom for corporate behavior was insufficient as a foundation for policy thinking. Thus, while the macroeconomic perspective on business cycles remained a priority along with policies promoting the competitive order, it was also evident that companies were players in the market and therefore that their own reform and the reform of Japan’s corporate and employment systems would also be necessary for achieving economic growth.

At the same time, it was becoming increasingly difficult to reach agreement with other countries on multilateral policies for resolving conflict, because of new moves to form regional and bilateral agreements. This in turn made it hard to pursue economic growth solely on the principle of “protecting the free-trade system.”

These were the various elements leading to a second phase in the change in the underlying principles of industrial policy. The ultimate trajectory of these new moves is not yet clear, but the conclusion reached in the course of this study—that this represents a “transitional period”—is probably not far off the mark.

This volume proceeds as follows. This chapter explores the shift in industrial structure premised on the *Vision for the 1970s*, and it presents the prototypical policies formulated to respond to the crisis posed by the yen’s appreciation and constraints on resources. It also discusses the policy-formation process. Chapter 2 traces the progress of the shift to a policy system based on rules and on a prioritization of external policies. Chapter 3 lays out the path by which “economic structural reform” became the clear focus in the course of Japan’s long-term recession.

Appendix to the Introduction

The “New Policy” Formulation Process

Every year, MITI produced an explanatory document or “Approval Request Form” to accompany its new budget request for the next fiscal year (Odaka 2013, p. 88). This was included in the government budget plan after examination by the Ministry of Finance and the year-end Cabinet Decision, and its content was determined through debate in the Diet after the new year. To formulate its budget request, MITI thought through a variety of policy plans, or “New Policies,” to serve as its constituent elements, and carried out broad-based preliminary discussions internally.

The New Policy was formulated as follows. From March to April each year, the Assistants to the General Affairs Division of each department gathered at the Minister’s Secretariat General Coordination Division and created a draft. This draft became the springboard for discussion of the thinking that should underlie the New Policy and was forwarded to all the departments in the Ministry. These departments created “Materials for the New Policy” related to their own areas. At the same time, the General Coordination, Budget and Accounts, and Personnel Divisions examined the underlying laws pertaining to their particular areas, budgets, personnel, and so on. In April, two meetings (in-house hearings) to review the New Policy were conducted within each bureau. Based on the attendant reference materials, the Ministry conducted full-scale hearings focused on the bureau findings, with the aim of developing the pillars of the New Policy. In many cases, they met twice. At the first hearing, the Director of the Budget and Accounts Division carried out the examination of those proposals that had survived the process thus far (so-called *tama*). The proposals for

the Fiscal Investment and Loan Program were decided on relatively early for accounting reasons. The last proposals to be deliberated were those whose funds would come from the General Accounting budget. The second hearing involved the entire Ministry, which carried on the discussions of the *tama*. The centerpiece or key points of the New Policy in the budget request for the following year were decided in mid-July. Then, from late July until early August, the “Industrial Policy Priorities for the Next Fiscal Year” were presented for deliberation by the governing party’s Commerce and Industry Committee and the Industrial Structure Council. Once approved, an “estimated request (draft)” was created. This was submitted by the end of August to the Ministry of Finance Budget Bureau Budget Examiner in charge of trade and foreign affairs. Budget negotiations with the Ministry of Finance then began in advance of the Diet deliberations that started in November and the year-end Cabinet decision on the upcoming budget. That said, changes were rarely made to the content of the budget proposal and policy objectives.

This process changed in response to the needs of the times. In the early 1980s, the margin for political negotiation narrowed. In the early 1990s, the Prime Minister’s Official Residence (*Kantei*) took center stage in the policy-formation process. Until the 1980s, Japanese administrative agencies had sufficient investigative and administrative capacity for policy planning, which enabled parliamentarians to redirect much of their time and energy to other tasks. Japanese politicians therefore did not necessarily have occasion to acquire policy-planning skills. Such skills could not be immediately upgraded, which led to a loss of credibility for the executive branch. It is fair to say that policy planning’s becoming more politicized was not necessarily the best outcome for the national welfare.

MITI’s internal policy-making process also changed. The Ministry continued to put younger bureaucrats to work seeking out new ideas but also reformed its approach in order to devise policies that would both align with and exert influence over the policy directions of the Advisory Council and the Cabinet. New Policy items accordingly became more extensive and exhaustive. Lastly, the turn of this century also saw changes in response to growing doubts within the Ministry about the New Policy planning process, which had become increasingly self-interested. Tentative plans (*tatakidai*) were proposed, serving as springboards for discussion; they were created and disseminated based on the assessments of current conditions heard by the Minister’s Secretariat, and each bureau and division then revised and submitted their New Policy proposals accordingly.

Under what is known as the “1955 regime,” preparation of the policy drafts—New Policy formation and the formulation of its associated budgets—was often delegated to central government offices by the ruling LDP. As politically neutral and competent actors, the government bureaucrats devised policy proposals based on Cabinet policies and also on what they themselves judged to be national needs; and while taking into account the views of private-sector members of the Industrial Structure Council and consulting with the relevant members of parliament, they submitted the approved draft (or revised draft) to discussion and negotiation within the Ministry. When it had been approved in these discussions, the responsible minister presented it to the Cabinet, along with the budget proposal and bills already assessed

by the Finance Ministry. Once approved by the Cabinet, it was passed on for Diet deliberations.

The formation of the policy plan was thus based on mutual trust between the political and the bureaucratic parts of the government. Preparing an excellent policy plan required familiarity with the actual conditions and needs of the target of the policy. It is a task that requires significant time and effort on the part of those with specific expertise and skills, and it was therefore natural, even inevitable, that the process would be left in the hands of bureaucrats specializing in these areas.

This system began to change, however, with the end of the so-called 1955 regime. One of the factors spurring this change was the accumulation of budget deficits, which weakened the bonds that had enabled team play between the government and the bureaucracy. In addition, the eruption of scandals (such as the Recruit Incident) implicating politicians and bureaucrats triggered political reform and the introduction of a single-member electoral district system and so on. As the exploration of new political systems proceeded, greater emphasis was placed on political leadership in the policy-making process. This reform manifested itself in the instances of the top-down policy making mentioned above. The large-scale organizational reform of central government agencies at the turn of the century reflected the centralizing trend in policy making through demands for administrative reform.

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