

The Industrialization and Global Integration of Meiji Japan*

Prologue

For the past several years, I have taught the economic history of Japan, in English, to foreign students comprising mostly of junior civil servants from developing and transition countries in a newly-established graduate school in Japan. The students' greatest interest naturally lies in understanding how Japan was able to catch up to the West from so early on, and what the policy and systemic sources for this feat were. Strictly speaking, this topic is outside my specialty. However, as I wanted to re-examine Japan's modernization process from the perspective of economic development and systemic transition, I happily took on the lectures. Owing to this, I had to dedicate rather a long time to preparing my notes and handouts for the course in the first year¹. The experience, however, proved to be intellectually challenging and perhaps I learned more than my students. What for Japanese are merely historical facts seem fresh and surprising to students from transition economies like China, Mongolia, or those in Central Asia. Comparison of Japan's modernization process with that of other countries over space and time, contrasts common aspects with those that are peculiar to Japan.

In the very first lecture of every year, I say the following to my students:

“All of you have come here to learn lessons from Japan's experience that you can apply once you return to your countries. This can be achieved on several different levels. First of all, you can learn facts about what Japan did in the past. Whether this be its support of industry or the financial policies it implemented, absorbing these facts is easy. And no doubt, my lectures will provide numerous examples of this kind. Second, in carefully comparing conditions in Japan at the time of its modernization to those that your countries now experience, you should be able to judge what lessons are transferable to your home-country setting. This exercise is an important one, but not sufficient. Lastly, from studying the development experiences of a broad selection of countries, including Japan, you will acquire the general skill of knowing what kind of questions to ask in response to the problems your countries are grappling with, and how best to answer them. This is the most difficult yet most essential ability for you to

*This is a full translation of Chapter Three of the book, *Tojokoku no Globalization: Jiritsuteki Hatten wa Kanoka* (Globalization of Developing Countries: Is Autonomous Development Possible?), Toyo Keizai Shimposha, 2000. Explanations have been occasionally added for the benefit of non-Japanese readers. The book won the Suntory Prize for Social Sciences and Humanities and the Osaragi Jiro Award for Critical Works in 2001.

¹ In preparing my lectures, *Nihon Keizaishi* (The Economic History of Japan, 8 volumes, Iwanami Shoten, 1988-89), a collection of academic papers that cover events from the Edo Period to the recent past, was particularly helpful. Also, Tetsuji Okazaki's *Kogyoka no Kiseki* (The Path of Industrialization, Yomiuri Shimbunsha, 1997) which argues from the perspective of comparative institutional analysis is very interesting. I believe that if more of this type of literature were translated into other languages, it would contribute greatly to a better academic understanding of Japan.

develop here. Merely implementing the policies formerly adopted by Japan in your homelands will not achieve much.”

Once I was lecturing about the absorption of industrial technology by Japan during the Meiji Period (1868-1912) when a student asked me, “From which countries did Japan receive foreign direct investment and how much did it receive?” This is a natural question to ask in today’s world where industrialization and attracting direct investment mean much the same thing to latecomer countries and each country vies aggressively to lure foreign companies. I paused for a little while and replied:

“Japan at the time did not receive any direct investment in the sense that you all are familiar with. Factory construction in the early Meiji Period was mainly achieved through public works or financed from domestic savings, private capital or joint stock companies. Japan adopted technology from abroad enthusiastically, but funding for the most part was self-generated. The absence of direct investment from abroad is not only characteristic of this period; it is in fact a salient feature of Japan’s whole industrialization process – with the exception of certain sectors such as the auto or electrical machinery industries during specific periods.”

My students, although looking somewhat puzzled, seemed to accept my explanation.

Most of these students, having completed their Masters, will return to posts in their respective governments. Depending on the country, they will either return to the same junior positions as before, leaving them unable to make use of their training abroad, or conversely, they will immediately be singled out to work in positions of responsibility. In the latter case, I sometimes wonder if it is indeed appropriate to entrust such important policy making to some of the graduates who did not show much distinction in my classes. Whichever the case may be, I strongly believe that the serious time I spent with these young men and women in the classroom will have some positive effect on the development of their societies, however indirectly or even with much delay.

1. The Salient Features of Japan as a Developing Economy

Lessons from the Meiji Period

For a long time after the Edo government opened its ports (1854), Japan remained a developing country. This fact is deeply imprinted in the consciousness of our close forebears who lived during the Meiji (1868-1912), Taisho (1912-26) and Showa (1926-89) Periods. At the beginning, Japan’s productivity, technology and industrial infrastructure were clearly inferior to that of the West. However, while receiving strong impetus and pressure from abroad, Japan made earnest efforts to mobilize its civil service and people to catch up. This process not only raised income, but also proved to be a dynamic force of change that produced countrywide and continuous social transformation. Japan became the first non-Western country to succeed at industrializing and was the first to rank equal with Western Powers. Historically, this kind of catch-up effort is not guaranteed to bear fruit; more countries have failed at economic development than succeeded. Even today, few non-Western countries can compete with Europe and North America equally in the global market. In this sense, Japan’s great achievement over the past century and a half is worth wondering at afresh.

When policy makers from developing and transition economies refer to learning from Japan’s experience, topics like the priority production system, industrial policy, small and medium enterprise (SME) development, policy loans and the public-private partnership of the postwar and high-growth

periods are popular subjects for study. Indeed, these are important policy issues and this was an important time. However, to understand the circumstances in which latecomer countries are currently placed, the political and economic history upstream of the postwar period, especially that of the Edo (1603-1868) and the Meiji Periods, furnishes more useful information. This is not because Japan then and latecomer economies now bear some resemblance. On the contrary, the Japan that experienced the tremendous external shock of opening up was very different from the latecomer economies of today. The domestic and external conditions of Meiji Japan, when viewed from today's standards, are distinctive in the extreme. Appreciating this fact helps to explain Japan's precocious catch up — a full century earlier than other countries — and at the same time provides a key to understanding why many countries, despite financial and technical assistance, still cannot free themselves from the poverty trap.

Strong Institutional Capacity from Early On

In comparing Meiji Japan to latecomer economies of today, two major differences are discernible. One of these relates to Japan itself, while the other is concerned with the country's external relations. Both of these differences are substantial and form the basic reason why latecomer economies of today cannot pursue the same path to development as Japan did in the past.

Let us first turn to the country itself. In comparing Meiji Japan to modern latecomer countries, we find that its domestic institutional capacity to respond to external shock was clearly superior. On reading the history of the period, what immediately strikes everyone is that not only the urban elite, but the whole of Japan — including the rural population — was ready to respond strongly to stimuli from the West². Japan at the time was a seed waiting for beneficial rains, or a solution waiting only for a catalyst to propel the chemical reaction. In the social confusion that followed the opening of the ports in the late Edo Period and that continued into the early Meiji Period, individuals with ability — irrespective of their former position in the feudal society — introduced new institutions or technology from abroad or adapted these imports to suit the needs and conditions of Japan. This was true of government officials, intellectuals, businessmen, engineers, rural landlords and civil rights activists. Especially important to note is that private entrepreneurs continued to emerge and start new businesses. Entrepreneurship was not limited to wealthy merchants or samurai families, but rather included many newcomers who did not readily fit into the social hierarchy that had existed until then. Moreover, shifts and reversals in fortune among them were fierce³.

Shokusan Kougyou (industrial promotion) in Meiji Japan did not stop simply at being a government slogan; it was the national goal of both the people and those in civil service. This led to interaction between the dynamic private sector and the public support of industry⁴. Again, this situation is

² This compliment on systemic capability does not extend to the policy of the Bakufu (Edo government) on its collision with foreign diplomacy. In this instance the Bakufu forced open the country without sufficient domestic debate or obtaining Imperial sanction, while suppressing any opposition against it. Even if Japan clearly had no other option than to open up to the outside world given its military inferiority, the clumsy way in which the Bakufu acted stirred up distrust and criticism. Moreover, the unequal treaties that it concluded further undermined its authority. This foreign policy error and the inflation that accompanied Japan's opening up formed the major trigger for the movement to overthrow the Bakufu.

³ Matao Miyamoto, *Nihon no Kindai 11: Kigyokatachi no Chosen* (A History of Modern Japan, Vol.11: Challenges of Entrepreneurs), Chuo Koron Shinsha, 1999.

⁴ While there is no doubt that government policy in general did promote industrialization, some initiatives were harmful to private sector development. During Meiji, being on friendly terms with high-ranking officials was indispensable for wealthy businessmen. In addition to drawing out assistance, it enabled them to obtain prior knowledge of capricious and unreasonable policies and to seek measures against them. For example, in 1874, the government suddenly notified merchants entrusted with official deposits that the collateral required had increased from one-third of the deposit to the total amount, and, demanded that the difference be paid in less than two months (keepers of official deposits made huge profits because they did not have to pay interest on these deposits). Mitsui, which was able to obtain this information in advance,

not unique to the Meiji Period but is a major characteristic throughout Japan's modern history, including the wartime, postwar and high economic growth periods. Clearly, much capability is required of both the public and private sectors. But if we were to ask which sector contributed more to the country's economic development, the answer must be the dynamism of the private sector. Schumpeter-type entrepreneurs, who continually carry out innovation as the Japanese ones did, are not to be found everywhere. There are few developing countries today that possess a vibrant private sector, even with the assistance of the government or international organizations in setting the playing field⁵. If Japanese-style industrial policies were implemented in an environment where the market economy is underdeveloped, all that would be visible is scrambling for official protection rather than a dynamic entrepreneurial response.

Another prominent feature of Japan is that as well as having commerce and service industries that aim at short-term profits, it is successful at launching manufacturing enterprises that call for the cumulative learning of technology and substantial initial investment. This feature, which can consistently be observed from the Meiji Period to the present, is attributed to Japan's fascination with *monotsukuri* (making things). Although overseas Chinese are active in Asia's economic scene today in the fields of commerce, finance, property development and low-skill assembly, they do not possess significant strength to be leaders in high-level manufacturing. Other than Japan, the only non-Western countries that have managed to develop domestic manufacturing capability of international standing are Taiwan and Korea. The industrial development of ASEAN member countries is remarkable too, but their production is highly dependent on foreign investors rather than domestic technology, human resources and production linkages. Where does Japan's dynamism supported by a *monotsukuri* culture not evident in today's latecomer economies come from? To find out we must study the period that preceded industrialization, that is, the Edo Period (Section 2).

A World that Discriminates Against Latecomer Societies

Secondly, with reference to the external circumstances, the global environment surrounding latecomer countries during the latter half of the nineteenth century was completely different from that of today. Under the imperialism of the nineteenth and the first half of the twentieth century, the relationship between Western and non-Western countries was that of the "ruler" and the "ruled," and the major powers did not expect nor desire that latecomer countries adopt the same standards as the West. A blatant discrimination existed between developed and latecomer countries. The absence of international organizations and development assistance at the time meant that the importing of technology and funding of investments all had to be conducted by the latecomer countries themselves. Added to this, it was a harsh period where countries that were not vigilant were in danger of ending up as colonies.

In 1881 the Meiji government declared that a constitutional government would be established within ten years. In the following year, Hirobumi Ito, a leading statesman, traveled to Europe to study the contents of the proposed constitution. He was surprised to hear Wilhelm I, the German emperor, and Rudolf von Gneist, a professor of law at Berlin University, declare that a constitution and a parliament

was able to prepare the funds and survived, but the Ono Group and the Shimada Group, which could not procure the capital required, went bankrupt.

⁵ Bazaars traders, stall-owners, or black marketeers often observed in developing and transition countries do not indicate the existence of a modern, sound market economy; rather they are evidence of its underdevelopment and imperfect functioning (recollect the post-World War II black market in Japan). That high-level officials from international organizations take the existence of the informal sector in developing countries as proof of the universality of the market mechanism is a point that I am totally unable to comprehend.

would be of no use to Japan and that a dictatorship would suit it better. Ito later indignantly wrote that their advice, which was totally unexpected, was too soft on despotism⁶.

Reacting strongly against this type of contempt thrown at Asia from the West, Japan used its sense of inferiority as a springboard to aim for national unity and become a first-class power. Japan accomplished this in half a century if we, for the moment, assume Japan's opening (1854) and the Russo-Japan War (1904-05) as the starting and ending points. In the period between the two World Wars that followed, Japan was accepted as a member of the 'Big Five' (together with USA, Great Britain, France and Italy) at international conferences and grew to be a power to be reckoned with, even in economic and military terms.

In contrast, latecomer countries of the present day are required to quickly adopt institutions that are the same as or similar to those in the developed countries. Regardless of their stage of development or social structure, international organizations urge all countries to liberalize and open up their economies in order to converge into a single economic system. This seems to have become prerequisite for being accepted as a member of the international community. Furthermore, the number of areas that ought to be integrated internationally is considerable, while the period allowed for this process is extremely short. To overcome this difficulty, latecomer countries actively attract foreign direct investment, while making use of technical and financial assistance from the donor community. Multilateral organizations such as the United Nations, the International Monetary Fund, the World Bank, the World Trade Organization and the Asian Development Bank offer the carrot (aid) and the stick (conditionality) to draw lagging countries into the existing international framework. Because democracy and the market mechanism are now regarded as universal values, the excuse that a country is poor or has a unique social structure is no longer acceptable for avoiding this integration. However underdeveloped a country is, the argument goes that it must be receptive to democracy and the market economy. This is how much the situation has changed in just over a century.

The world that attempted to fix latecomer countries in a subordinate position to exploit them has changed to a world that forces the system of developed countries onto latecomer ones. It is hard to tell which situation is more arduous for a latecomer country. However, the difference between Meiji Japan, which was able to successfully complete an industrial revolution despite the conditions of the former age, and latecomer countries today, which are unable to make a start at economic development despite the modern day world, must be sought mainly in the extent to which a country is endowed with a domestic capability to respond to external pressures. Japan's success in the latter half of the nineteenth century and the failure of most latecomer countries today naturally reflect their different abilities. If this is the case, we need to elucidate what forms the essence of this capability. Clearly, this cannot be achieved by merely listing the concrete policy measures Japan implemented at each point. Such a superficial imitation of Japanese policies would not be productive.

2 The Edo Period: A History of Pre-Industrial Japan

The Endogenous Growth of Commerce

Without doubt the technology and machinery of Edo, the period that preceded Meiji, was antiquated. However, in terms of economic systems, conditions were ripe for the active import of the

⁶ Letter from Hirobumi Ito to Masayoshi Matsukata (September 6, 1882), as quoted in Yasushi Toriumi, *Nihon no Kindai* (Modern Japan), University of the Air Press, 1996.

industrial revolution. In recent historical research, the largely negative view of Edo Japan as a stagnant feudal society isolated from the rest of the world no longer holds sway. Heita Kawakatsu has developed a unique theory that proposes that the islands of Britain and Japan, located on either side of the Eurasian continent, each carried out their domestic development independently until the nineteenth century, and claims that the industrial successes of both were autonomous and not due to external stimulus⁷. Placing Japan and Britain of the nineteenth century on the same level, at least in terms of technology and economic power, may be going a little too far. We cannot ignore what was blatantly clear in international relations at the time; that Britain was the world's leading industrial economy and Japan was no more than a backward agrarian society of the Far East. Nor can we put aside the shared perceptions of the Japanese people at that time (see Soseki Natsume's lament at the end of this chapter). However, if we focus exclusively on the systemic potential of the Edo economy, then even Kawakatsu's bold theory which sets Japan and Britain on equal pegging is not totally off the mark.

Below is a list of characteristics that enabled Edo Japan to catch up rapidly with the West in the periods that followed. It is given to my students as a near-consensus view among Japanese economists.

1. Political stability and unity under the Tokugawa administration
2. Agricultural growth (expansion of farmable land in the pre-Edo and early Edo period and rising productivity in the late Edo Period)
3. Establishment of a communications and transportation network and the integration of the national economy
4. Increased commodity production, including a large number of local specialties
5. Development of commerce and finance and the emergence of an affluent merchant class
6. Official promotion of industries, especially at the level of han (local) governments
7. The spread of education through Bakufu and han schools, private academies and *terakoya* (private schools for children)

These items may strike Japanese as nothing out of the ordinary. However, we must realize that these conditions are still rare in latecomer countries of today. A few exceptional countries like Taiwan, Korea and Singapore have achieved a high level of industrialization and now fulfill the above seven points. On the other hand, as for transition economies and the poorest countries of today, none of them boast *all* the conditions that Japan of the late Edo Period enjoyed, and only a few of them can provide even some of them.

Of the seven points listed above, 3, 4 and 5 are closely connected and can be summarized into a single phrase: the endogenous growth of commerce. From my experience in working with developing and transition countries over the past several years, I have come to consider this as the key factor desperately lacking in countries that do not grow despite economic liberalization. In societies where private-sector business activity is lethargic and a nationally integrated market does not exist, bold liberalization measures, the privatization of state-owned enterprises, the support of small and medium enterprises, free trade and the establishment of a legal system are unlikely to ignite private sector dynamism. The optimistic view that the removal of bad policies and the leveling of the playing field for private as well as state-owned enterprises will automatically release hitherto suppressed economic dynamism does not hold for the latest comers that are attempting to jump-start production in the twenty-first century. The sound growth of a market economy requires several conditions to be fulfilled. Naturally, not every country is equipped with all of them. This is

⁷ Heita Kawakatsu, *Nihon Bunmei to Kindai Seiyō: Sakoku Saiko* (Japanese Civilization and the Modern West: Rethinking the Closed Door Policy), NHK Books, 1991.

the point that Japanese development economists repeatedly emphasized to international development organizations throughout the 1990s.

Two Distortions that Stunt the Development of a Market Economy

What are the prerequisite conditions for creating a market economy? Shigeru Ishikawa, an authority on Japanese development economics, offers the following three: (1) a division of labor in production associated with an increase in productivity, (2) the development of a merchandise distribution system, and (3) the adherence to the rules of market transaction, including the strict observance of business contracts⁸. Taking the example of China in the 1980s, he indicates several incidents where economic liberalization did not bear the intended results, and argues that this occurred in large part because of the enormous gap between the level of systemic maturity required for such policies to be effective and the underdeveloped systems that China actually possessed. Ishikawa stresses that the mission of development economics, as a policy-oriented science, is to correctly identify the gap between policy and reality, and to work out the appropriate next step for a given stage of development in the context of a particular country. That is to say, it must formulate a delicate policy mix that promotes the development of a market economy without perpetuating the present situation or throwing the society into crisis.

What is vital here is the ability to discriminate between the *innate* and *artificial* distortions that disrupt the formation of a market economy⁹. On the one hand, every society is stamped with unique features that are historically formed and are not easy to erase. These include the existence and nature of certain characteristics such as social unity, mutual trust, morality, long-term vision, entrepreneurial spirit, the observance of law and attitudes towards outsiders. Some of these innate features are barriers that must be overcome in order to form a market economy. Imagine, for example, a society that does not trust newcomers because of a history of continual warfare, or a society where food is so plentiful that there is no thought to invest for the morrow, or even a society where all wealth is equally redistributed among villagers and thus the desire to work and save is absent. These features arise from the unique ecological background of a particular society and originate well before colonialism, and thus cannot be attributed to the past few centuries of foreign rule.

On the other hand, the suppression of private sector activity through artificial constraints imposed by the government is certainly possible. These include various types of control, monopolies, exclusive cartels, excessive and unpredictable taxation, and misappropriation of the nation's wealth by those in power. An extreme example of such economic suppression was the adoption of a command economy by socialist states. If economic stagnation is caused by this kind of policy distortion, but the fundamental structure of society itself is compatible with a market economic system, then removing bad government or bad policies alone will suffice as a development strategy. After a bold liberalization drive, economic activity can be left to the private sector, and the government and international organizations would not have to worry about institution building or fostering production. However, if the cause of a lackluster economy derives from innate distortions, which reflect the social structure at a deeper level, then it is clear that *laissez-faire* policy will not succeed. We cannot decide *a priori* which cause is holding back a given country. But if the private sector does not respond to bold and repeated liberalization initiatives, we can suspect that it is due to innate distortions.

⁸ Shigeru Ishikawa, "Underdevelopment of the Market Economy and the Limits of Economic Liberalization," Chapter 7, *Kaihatsu Keizaigaku no Kihon Mondai* (Basic Issues in Development Economics), Iwanami Shoten, 1990. Translated in K. Ohno and I. Ohno, eds., *Japanese Views on Economic Development*, Routledge, 1998.

⁹ Shigeru Ishikawa, "*Shijokeizai Hattensokushinteki Approach: Rironteki Ichizuke to Oyou*" (Approach to Promote the Development of a Market Economy: Theoretical Underpinnings and Applications), *Kaihatsu Enjo Kenkyu*, Vol.4, No.1, Overseas Economic Cooperation Fund, 1997.

The Edo Period: A Mercantile Perspective

John Hicks developed an economic growth theory based on the strength and scope of mercantile activity, and Yonosuke Hara further expanded the thesis to the Asian context¹⁰. What they propose is an extremely interesting and useful idea for our purpose. Their argument can be summarized as follows: A market economy is not a system that can be created through socio-economic engineering and quick policy switches. Rather, it is a product of a long historical evolution, which is realized only in societies that satisfy specific conditions. If we look back at the history of civilization, we see that market economies first emerged from the groups of free-trading city ports that surrounded the richly islanded seas of the Mediterranean and Southeast Asia, where the activity of itinerant traders formed ties among them (it is worth noting that market economies were not born of continental empires with relatively closed economic activity). The traders gradually extended their trading network based on mutual trust, just as a plant slowly spreads its roots, to overcome the uncertainties of long-distance transportation and renegeing on contracts. Essential for the growth of this network was the development of financial services that offered account settlement, foreign exchange, and insurance, as well as a government that took on the role of protecting traders from physical harm or fraud. However, while such financial services tend to emerge spontaneously from a market economic system, there is no guarantee that government protection will. If a government takes predatory action on international traders, economic activity is likely to wither.

The rise and fall of this type of long-distance trade has been observed throughout history, depending on the ecological and geographical conditions of the region and the kind of government that existed. The Industrial Revolution of the latter half of the nineteenth century associated with technological innovation was an event that grew out of the successful development of a mercantile economy. However, a new problem arose with the advent of the Industrial Revolution: commerce and finance are activities that are naturally arising within the market mechanism, but labor, on which the success of industrialization critically depends, is not dealt with well by the market. To handle it better, institutional innovations such as the firm in the private sector and industrial policies by the government were required.

This mercantile theory highlights the following three points: (1) the market economy exhibits a natural tendency to evolve from commerce to manufacturing, however, (2) the success of this evolution is not guaranteed, and (3) traders and merchants are the key players in this evolution while the government must also play an important supplementary role. But if the government fails to fulfill this responsibility or even engages in harmful activity, it will hinder the expansion of the market economy. To consider the economic development from Edo to Meiji in light of this theory is extremely interesting. In Edo Japan, the use of sea routes allowed nationally integrated markets to be established and thanks to vibrant commercial activity a class of wealthy merchants with considerable capital came into existence. Furthermore, a distribution system for goods along with a financial system developed with Osaka at its center. These systemic developments were geographically limited to within Japan, but they constituted the very ingredients needed to fire an industrial revolution.

Meanwhile, despite many mistakes made along the way, central and local governments in the Edo Period continued their support of trade and industry. For a revenue source, the governments at both levels relied heavily on a tax-in-kind levied on rice, which was collected and then redirected for sale to consuming regions. When the Tokugawa administration was established in the early 17th century, in addition to Osaka and Kyoto, which were already major cities with significant production capacity, a large

¹⁰ J. R. Hicks, *A Theory of Economic History*, Oxford University Press, 1969; Yonosuke Hara, *Asia Dynamism* (Asian Dynamism), NTT Press, 1996; and Yonosuke Hara, *Area Economics: Asia Keizai no Topology* (Area Economics: Topology of Asian Economies), NTT Press, 1999.

urban area for consumption was created artificially in Edo by resettling samurai who by nature were not engaged in production. This means that the functioning of the Edo economy presupposed the existence of a nationally integrated distribution network. To support this system, the Edo government introduced policies for sea routes, the provision of highways, the alternate attendance system (requiring all daimyo to reside in Edo every other year) and the courier system.

However, with regard to the promotion of private commercial activity, the policies of the central government remained highly inconsistent throughout the Edo Period. Just as soon as it had officially recognized and even enforced *kabunakama* (trade cartels) to tighten its control, it would ban them and return to an economy with free entry and competition. As for the taxation of commerce, it was extremely arbitrary and unpredictable. As the production base steadily shifted from rice production to commercial crops and handicrafts industries, and then onto commerce based on them, the inability of the government to create a stable tax base from these new sources became the basic cause of fiscal difficulty. Furthermore, the debasement of gold and silver coins to finance the fiscal deficit gave rise to inflation. However, even with the government firing out policies that were of no help to the private sector, it was not inept or destructive enough to quash commercial activity entirely. In other words, the vitality of the private sector was strong enough to survive this level of inexpedient policy. Turning our attention to the local governments, due to the fiscal crisis they too were pressed by the need to enlarge their annual revenue. Thus, efforts to encourage industry by the various han administrations at the regional level intensified, and some even succeeded brilliantly and cleared the deficits.

However, if we visit the transition countries of Indochina or Central Asia today, there are few signs of a nationally integrated economy, the growth of private commercial capital, or the autonomous development of a financial system. Nor do these countries have a civil service or governing structure that is able to effectively design and implement policies for industrial promotion. In Vietnam, for example, family-run subsistence agriculture is dominant and a large part of rice production is for domestic consumption only. Any surplus rice from the Mekong Delta region in the South of the country is transferred to the North by state-owned enterprises, not private ones. Through trade and investment, the large urban centers of Hanoi and Ho Chi Minh City continue to integrate into the world economy, but the economic links between the cities of Vietnam and the countryside where 80% of the population lives are still weak. In Central Asia, the bazaars are crammed full with Chinese goods brought over by peddlers, yet a formal distribution system is not yet in place. Because enterprises are unable to borrow working capital, let alone investment capital, from banks, they are forced to resort to barter or accumulate arrears to one another. In the great plains of Central Asia, transportation costs have rocketed because of the large number of illegal police checkpoints demanding bribes from passing long-distance truck drivers.

The Edo Period is often viewed in a negative light. Compared with earlier periods, Japan's closed door policy (1639-1854) during the Edo Period significantly reduced stimulus from abroad. It cannot be denied that its feudal hierarchy also contributed to the rigid social structure. However, with regard to the economic system, considerable achievements were made: thanks to peace and stability, the agricultural sector generated a surplus, commercial and handicraft businesses developed, trade among adjacent regions was activated, and the sea routes connecting these regions created a nationally integrated market. In other words, the *national economy* steadily grew, tracing the natural order outlined by Hisao Otsuka¹¹. This remarkable economic development spanned more than two centuries, but by the end of the Edo Period, a systemic gap had emerged between the rigid form of the Tokugawa system with a revenue base totally dependent on rice farming and the dynamic reality of commodity production backed by a nationwide

¹¹ Hisao Otsuka, *Kokumin Keizai: Sono Rekishiteki Kosatsu* (The National Economy: A Historical Study), Kodansha Gakujutsu Bunko, 1994. Otsuka's idea is discussed in Chapter 1 of the original book.

distribution system. To overcome this contradiction and propel the Japanese economy to the next stage of development, Japan needed more liberal, open and industry-friendly policy. In this sense, the great shock of opening the country up was fortuitously timed. If Commodore Perry's black ships had visited Japan much earlier in the first half of Edo period, Japan's economy would probably have been unprepared to respond successfully. On the other hand, if Japan had not been forced open in the middle of the nineteenth century, the country would have had to invent new systems to resolve the inconsistencies by itself.

3 Catching Up as a National Goal: The Joint Efforts of Government and Business

The Policy Goals of the Meiji Government

It may be difficult to imagine from the ineptitude of the Japanese government today, but the policy goals of the Meiji Japan that sprang into the international community were remarkably clear and deadly earnest. Furthermore, the goals were not only proposed by the government but shared by the whole nation, including the political opposition. Immediately after the opening of Japan to the rest of the world, the national priority was security-oriented and defensive, namely, to avoid colonization and to protect sovereignty. However, with time and as the threat of being subjugated by the Great Powers diminished, the national goals took on the more positive aim of making Japan a "first-class" power to rank equal with the West. These goals were summarized in the famous phrase, *fukoku kyohei* or enriching the country, strengthening the military. It is important to understand the acute inferiority Japan must have felt as it encountered countries clearly more powerful than itself as well as grasp the simultaneous surge of pride that urged it on to overcome its backwardness. Nationalism grew as a result of Japan's contact with the outside world following its long seclusion and at the shock of discovering that it was merely a backward country in the world system. This desire to catch up backed by a fierce national pride was to strongly color the history of Japan for the following half a century or more, ending with the Pacific War.

However, let us now return to the early part of the story. In the early years of Meiji, conflicting policy lines on how to become a first-class power were already apparent within the government. There were three major issues which concerned the high officials of the Meiji Government¹²:

1. Industrialization on the economic front (*shokusan kougyou*, or industrial promotion)
2. Expansionist policy on the international front (for example, *seikanron* or the argument for the "Korean Expedition")
3. The establishment of a constitutional government on the political front (which called for a constitution and a parliament)

However, for a Meiji government that had just come into being and whose power and financial basis were fragile, pursuing all of these goals at once was impossible, and the question of sequencing set off fierce confrontation within the leadership. The complicated political development of the early Meiji Period can be understood fairly well if we keep the debate over these policy priorities in mind¹³.

¹² Apart from these three issues, the revision of the unequal treaties with the West was an important diplomatic goal remaining from the Edo Period.

¹³ Takuji Shibahara, *Sekaiishi no Naka no Meiji Ishin* (The Meiji Restoration in World History), Iwanami Shinsho, 1977; and Junji Banno, *Nihon Seijishi: Meiji, Taisho, Senzen Showa* (The Political History of Japan: Meiji, Taisho, and Prewar Showa), University of the Air Press, 1993.

The first policy (industrialization) was advocated and implemented by Toshimichi Okubo, who was successively in office as minister of finance and then as home secretary. After his assassination in 1878, Shigenobu Okuma and Kiyotaka Kuroda inherited this policy line.

The second policy was proposed by Takamori Saigo and Taisuke Itagaki, and behind it lay the strong sense of danger that if the dissatisfaction of disaffected samurai was not deflected externally, the new government would not last long. However, because of stern opposition from Okubo and Takayoshi Kido to the military expedition, the councilors who made up the Korea Expedition Faction were forced to leave the government in 1876. After this event, Saigo was exalted as the leader of the disaffected samurai groups and led an uprising against the government (Satsuma Rebellion). Meanwhile Itagaki and his followers started an anti-government offensive as the self-proclaimed leaders of the civil rights movement.

The third policy (political reform) was prepared by Kaoru Inoue and Hirobumi Ito from within the government. Their plan stressed gradualism and aimed at the Prussian model of a constitutional monarchy, as opposed to the more advanced British-type of democracy with a party government. Shigenobu Okuma, who proposed the latter model, was forced from power during the Crisis of 1881. From outside the government, Itagaki, who had left public office, and other civil rights campaigners like Kenkichi Kataoka and Emori Ueki called for radicalism. The popular movement which called for the immediate introduction of a parliament and prepared private drafts of a constitution spread like wildfire through the country, politicizing wealthy farmers and poor peasants alike, and at times turned quite violent.

This type of political wrangling among the political elites was not confrontation over fundamentally incompatible goals. It was persistent argument over how to set priorities and the sequence in which the country should realize what were mutually agreed upon as common goals. Therefore, a confusing process came into being where the same person drove forward opposing policies in quick succession, and political alliance would form and dissolve depending on the issue at hand. For example, Okubo, who opposed Saigo's expansionism and ousted the Korea Expedition Faction in 1876, dispatched troops to Taiwan in the following year, and in the year after that, sent a battle ship to Korea in provocation. Itagaki, who had resigned from public office and was supposed to be on the side of criticizing the Meiji government, later returned to the government only to leave it again before long. However, ferocious conflict among politicians over how to realize commonly held goals is not unique to the Meiji Period, it is a universal phenomenon throughout world history.

Constitutional Government and Nationalism

Do the latecomer countries of today embrace policy goals similar to those of Meiji Japan? In our age, the option of invading other countries no longer exists¹⁴. However, as for the other two goals, the question of how economic and political development should be sequenced remains unanswered even today. The ongoing debate over whether economic development should precede democracy, whether these two goals are compatible, or how the authoritarian developmentalism of East Asia should be evaluated are all variations of the same question. However, unlike the passive adoption or rejection of a single Western model recommended (or enforced) by the IMF and America, which many developing countries are driven to today, Japan's policies were the product of a pro-active attitude that selected the appropriate model in

¹⁴ The colonization of other countries through overt military action has definitely become a feature of the past. However, the use of hard-line foreign policy as a centripetal force to unite the government and mobilize national sentiment is still alive. Consider the launching of missiles by North Korea, the competition over nuclear capability between India and Pakistan, the anti-U.S. policy of Iraq and Iran, the tension between Mainland China and Taiwan, as well as the criticism of foreign private investors in Malaysia.

light of the historical circumstances in which the country was placed. Moreover, Japan was not only able but permitted by the international turn of events, to take this course.

From 1871, a high-level mission headed by Tomomi Iwakura and including about half the government ministers was sent to America and Europe for nearly two years. Its purpose was to (1) conduct preliminary negotiations for the revision of the unequal treaties, and (2) study Western technology and systems. The mission failed in its first objective because the West would not treat Japan equally as long as its institutions were considered backward. However, it did succeed in gaining insights with regard to its second objective. The mission was warmly welcomed wherever it went.

Upon the return of the Iwakura Mission, Toshimichi Okubo, one of the principal mission members, wrote "Proposal for a Constitutional Government." His views can be summarized as follows¹⁵: Democratic government and monarchy both have their advantages and disadvantages. Obviously, democracy in its ideal form is superior to monarchy. But in reality it often disintegrates into factionalism and in the worst case may descend into a tyranny of numbers which brutally suppresses political opponents (Okubo had in mind the reign of terror after the French Revolution). On the other hand, a monarchy functions well where the ruler is wise and the people are unenlightened. But if the ruler is tyrannical and the officials corrupt, the misery and the resentment of the ordinary people will be limitless. Compared to England, Japan is only semi-civilized and cannot rid itself of the customs of feudalism. For us, monarchy is already a thing of the past, but preparations to install a democratic system immediately are incomplete. Thus, to carry the various reforms through with resolve, the central government should maintain a strong position as the mainstay of a policy-making. The realistic path for Japan is to introduce a constitutional monarchy based on the principle of the gradual installment of a constitutional government adjusted to the speed of social change. This, for the moment, means joint governing by the Emperor and the people under a constitution.

Let us contrast Okubo's argument with that of Yukichi Fukuzawa, another intellectual leader of the Meiji Period. In his main work, *An Outline of the Theory of Civilization* (1875), Fukuzawa categorizes each country as civilized, partially civilized or uncivilized, and ranks Japan as semi-civilized. He also states that the relative merits and demerits of democracy as opposed to monarchy cannot be generally ascertained. Up to this point, his argument is in line with Okubo's. Moreover, his emphasis on Japan's need to avoid the threat of Western imperialism and preserve political independence is not especially original. He advocates that Japan should cast away its traditions and customs and adopt Western civilization to its advantage. Fukuzawa notes that civilization has a spiritual and material aspect. Imitating the material is easy, but imitating the spiritual is hard. To those who desire civilization, he advises that they "tackle the difficult first and then the easy: first change the hearts and minds of the people who will have an affect on the laws made by the government, then finally move onto the material issues." This advice vividly contrasts with that of Okubo. Fukuzawa, the enlightened thinker, gives precedence to the disposition of free and broad-minded people in the private sector, while Okubo, the high official with a grand vision, endeavors to accelerate the pace of "material" civilization by applying the strong hand of the central government.

How did history actually progress along the three policy lines? From the earliest years of Meiji, economic development was actively pursued through the policies of the Ministry of Industry, the Ministry of Finance and the Home Ministry, and we can say that their efforts met with a great deal of success. As for the expansionist campaign, it was at first set back because of the expulsion of the Korea Expedition

¹⁵ Yasushi Toriumi, *Nihon no Kindai: Kokumin Kokka no Keisai, Hatten to Zassetsu* (Modern Japan: The Formation, Development and Collapse of the Nation State), University of the Air Press, 1996.

Faction in 1876. But militarism subsequently gained in force gradually right up to the middle of the twentieth century as Japan repeatedly waged war to secure its interests abroad and add to its colonies. As for the establishment of a constitution, this proceeded in line with the gradualist approach of the government. In response to the growing civil rights movement, in 1881, the Meiji government announced, in the form of an Imperial Order, that a parliament would be inaugurated within ten years. Thereafter, Hirobumi Ito and Kaoru Inoue conducted research on constitutional systems and prepared a draft constitution, which was deliberated by the Privy Council. In 1889 the leadership enacted a constitution as promised, and in the following year the first Imperial Parliament opened. This happened twenty-two years after the Meiji Restoration.

An interesting point here is that not only the public at large, but even the political opposition (known as the *jiyu minken ha*), which severely criticized the government previously and was in turn suppressed by it, warmly welcomed the promulgation of the Meiji Constitution. For example, Yukio Ozaki, who was ordered to leave Tokyo under the Preservation of the Peace Acts, praised the Constitution as “wonderfully made,” and Sanae Takada, the education specialist, added strong support with “I think that the Constitution of the Empire of Japan is a good constitution, it exceeds our expectations.” To our modern day sensibilities, the fact that opposition leaders applauded the establishment of the Meiji Constitution that featured a strong emperor and led the country down the path to militarism is very strange. However, we should remember that at the time Japan was the only country outside the West to have a constitution. Even if opponents were somewhat dissatisfied with the content or wording, it is still easy to imagine that the constitution was a source of enormous national pride for them. Furthermore, the Meiji Constitution was fairly ambiguous in its prescription for the form of government, and depending on its interpretation and application, it could even accord with a party cabinet system. At least on the political front, with a constitution Japan had furnished itself with the condition it needed to be accepted among the Western powers. Nationalism, it seems, was stronger than the enmity between political opponents.

Eiichi Shibusawa: Builder of the Market Economy

I always introduce Eiichi Shibusawa as a “super businessman” in my lectures. Unlike Okubo, Shibusawa did not like being a bureaucrat very much. Invited to the Ministry of Finance shortly after its inception, his task was to lay the foundations for a market economy through the introduction of a joint-stock company system, a monetary system, new weights and measures, a railway line, nationally chartered banks, the Tomioka Textile Factory and so on, all of which he achieved with tremendous results. Furthermore, he managed this in the four years between 1869 and 1873, while he was between the ages of 29 and 33. On leaving the Ministry, he became the head of the First National Bank, which he had established, and reigned supreme in the business world until his death at the age of 91. He spent all his efforts creating a myriad of enterprises, economic organizations and social bodies.

Shibusawa was cast in a completely different mold from another great business leader of Meiji: Yataro Iwasaki. Iwasaki, who founded the Mitsubishi *zaibatsu* (business group) from scratch, was a capitalist through and through. He relentlessly pursued his own interests using his enterprising spirit and government connections to the maximum while engaging rival businesses in repeated and fierce battles. Shibusawa, on the other hand, did not form his own *zaibatsu* and had no interest in expanding his business empire. He was not so much a player on the market, but one step removed from it, he acted as a business promoter and dedicated his whole life to forming Japan into a modern economy. When he called for the establishment of a new organization, his motive was not profit or market share, but the fact that Japan needed such an activity. Shibusawa’s business philosophy was neither that of the self-seeking individual nor the utilitarian, but one that unites economics and ethics, the latter of which was based firmly on the Analects of Confucianism.

Shibusawa was quick to perceive the needs of the Japanese economy, and was the type to instantly act to fulfill them. In setting up a business, his usual practice was to proclaim himself as an investor in a newly established joint-stock company and urge other men of substance to invest with him until a sufficient funds were collected. In this manner, Shibusawa was involved in the establishment of more than 500 companies¹⁶. He was also largely involved in the establishment of other economic organizations, universities, and welfare institutions¹⁷. Furthermore, as a private emissary, he made strenuous efforts to improve Japan-US relations as dark clouds began to gather. Of course, for a single man to be involved personally in so many activities is physically impossible, and in fact in many cases it was just his name that was lent to the project. He did not intervene deeply in day-to-day management. Only when a problem arose did he offer necessary support and dispatch advice.

Well before he became a super businessman, Shibusawa's youth was already unique. Those who have read his autobiography¹⁸ cannot help but be overwhelmed by his energy and the speed at which he adapted to change. He was born in 1840 in what is now Fukaya City in Saitama Prefecture. He was the oldest son of a wealthy farmer who traded indigo. From his youth, he was a shrewd businessman and also stood up to local officials that tried to collect funds "for official purposes." Before long, the young Shibusawa became resentful of the absurdity of the feudal system and burned with the desire to overthrow the Tokugawa administration and to expel foreigners. He planned to attack Takasaki Castle and from there storm the foreign settlement in Yokohama to set alight the mansions of the foreign residents. However, this ridiculous plan fell through and the twenty-three-year old Shibusawa fled with his companions to Kyoto. In Kyoto he made the acquaintance of and then served Yoshinobu Hitotsubashi, one of the most illustrious relatives of the ruling Tokugawa family. Even here Shibusawa was quick to reform the military system for the Hitotsubashi family, encourage industry in the territory, and issue local money that circulated with much confidence. Shortly afterwards, in a strange turn of events, Yoshinobu was promoted to Shogun and before Shibusawa knew it he had been transformed from an anti-Tokugawa campaigner into a retainer of the Tokugawa family. But Shibusawa knew that the Tokugawa administration was doomed to collapse before long. This being the case, not only was he a traitor, but it was certain that he would end up on the losing side. Despondent with his lot in life, for a while, Shibusawa spent his days "dissatisfied and enjoying nothing."

Soon however, the prospect of going to France arose. It was as an attendant for the official delegation to the Paris International Exposition and to serve the fourteen-year-old Akitake Tokugawa who was to study abroad. Shibusawa departed for Europe with joy, and while working as treasurer, he was entrusted with solving a number of problems that arose. Finally, however, the Tokugawa government did collapse. Rushing back home, Shibusawa decided to live a quiet life in Shizuoka near the unfortunate Yoshinobu who had been forced to retreat there. However, he was not the type to sit still for long. He proposed that the local government of Shizuoka use funds provided by the new government to develop the regional economy by establishing joint stock companies, and the proposal was instantly adopted. However, just as his new project was taking off, an order to come to Tokyo was sent down from the new government: Shibusawa was to join the Ministry of Finance and participate in the construction of a new economic

¹⁶ The following companies were among those established with Shibusawa's assistance: First National Bank, Oji Paper, Japan Railway, Kyodo Transportation, Osaka Spinning Mill, Tokyo Gas, Japan Mail Shipping, Imperial Hotel, Sapporo Beer, Japan Sugar Refining, Oriental Shipping, Keihan Electric Railway, Tokyo Electric Power, and NKK.

¹⁷ Shibusawa helped to create the following institutions: Tokyo Commercial School (later to become Hitotsubashi University), Tokyo Bankers' Association, Tokyo Chamber of Commerce, Tokyo Stock Exchange, Japan Women's College, Tokyo Clearing House, Tokyo Municipal Orphanage, Imperial Theater, Japan Anti-Tuberculosis Association, and Tokyo Women's University.

¹⁸ *The Autobiography of Shibusawa Eiichi: from Peasant to Entrepreneur*, translated by Teruko Craig, University of Tokyo Press, 1994. The book combines a complete translation of *Amayo-gatari* and excerpts from *Kosei Nikki*.

system. Shibusawa stiffly declined the offer at first, however, the earnest entreaties of Shigenobu Okuma (a leading statesman of the Meiji Period who later served as a prime minister) moved him, and he finally accepted. His activities from this point are as I described earlier.

Shibusawa cannot be classified as a farmer, merchant or samurai. He was the unique product of a tumultuous period in Japan's history. He was a keen observer and was highly sensitive to irrationalities and inefficiencies. If he noticed any such problems, he would immediately suggest a solution, and would take the lead in transforming it into action. Where obstacles existed, he did not relent until he overcame them. He was able to respond to any change in circumstances. He could not bear emotional attachment to the past, undue formalism, or red-tape bureaucracy. Besides that, Shibusawa was a womanizer. With a man packed solid with such energy reigning in the business world, the Japanese economy had no choice but to develop!

Is there an Eiichi Shibusawa in any of the latecomer countries of today? How about other types of business leaders such as Yataro Iwasaki (the founder of the Mitsubishi *zaibatsu*), Tomoatsu Godai (a business promoter in Western Japan), Rizaemon Minomura (the reformer of the Mitsui *zabatsu*), Soichiro Asano (the founder of Asano Cement Company and the Asano *zaibatsu*), and Ichibei Furukawa (the founder of Furukawa *zaibatsu*)? A market economy does not arise out of laws and policies only. Nor can everything be decided simply by supply and demand. The true heroes in a market economy are entrepreneurs of strong character, like Shibusawa and the others. To produce such heroes continuously, a society must be equipped with mechanisms to encourage and support them.

4 The Establishment of New Industries

Silk, Cotton and Machines

In its early years Meiji Japan was an agrarian society in which farming, forestry and fishing employed more than seventy percent of the working population and supplied over sixty percent of national output. This situation was also reflected in the trade structure. Throughout Meiji (1868-1912), Taisho (1912-26) and pre-war Showa (1926-36), Japan's top exports were raw silk yarn, tea, and marine products. The main market for these commodities was America. Along with the opening up of Japanese ports, demand for these primary commodities suddenly ballooned and domestic producers greatly profited from it. Virtually unseen in Japan nowadays, during Meiji all villages that could cultivate mulberries to rear silkworms, and many earned a good income from this activity. In this sense, silk was not only a traditional product that brought wealth to rural areas, but it also made an important contribution to Japan's industrialization by earning much coveted foreign exchange. Moreover, mining, which had continued from the Edo Period, was largely requisitioned by the new government and later sold off to the private sector to become one of Japan's principal industries.

However, from another perspective, trade structure in Meiji accomplished a dramatic change. The greatest transformation came from the success of import substitution in the cotton industry and the shift to export-oriented production. In the early part of Meiji, nearly half of all imports came from Great Britain in the form of cotton and woolen goods and cotton yarn. Japan exported primary commodities and imported manufactured goods — the typical vertical trade pattern of latecomer countries. However, as Japan's cotton industry grew, the import of textile products fell steadily and around the 1900's it was close to nothing. Furthermore, from the latter part of the 1890s, Japan began to export cotton yarn and clothes to neighboring Asian countries, and at the same time it started to import raw cotton in large quantities mainly from India. In other words, the industrialization of the Meiji Period was a *light* industrial revolution, which

made its way from importing to domestic production and then onto exporting. Within this transition, cotton production played a central role.

What about Japan's heavy industry? The iron and steel, shipbuilding and chemical industries, as well as the manufacture of electrical machinery and appliances were in their infancy and the country was still in the process of learning by imitating the West. These industries were not yet in any condition to be called the main forces of production; they were not internationally competitive and importing the necessary machinery from the West was the norm. Moreover, the scant production of machinery and tools that did exist was mainly in the hands of state-owned enterprises, especially munitions plants like the Tokyo Artillery Factory, the Yokosuka Naval Arsenal, the Osaka Artillery Factory and the Kure Naval Arsenal, all of which used technology and machinery solely from the West. However, by late Meiji, private-sector production in the areas of shipbuilding, railway carriages and machine instruments had slowly emerged. Meanwhile, engineers and workers who had handled new technology in the state-owned munitions plants began to transfer to private-sector businesses or set up their own. In this manner, the production technology of the West propagated widely and small businesses and subcontractors began to form in Tokyo and Osaka. Thus, while heavy industry was in its infancy during the Meiji period, it was preparing itself for a rapid leap in the period after the First World War.

Because of the unequal treaties that had been signed by the previous government, Meiji Japan did not have autonomy over its tariff regime and import duties on all goods were set at the low rate of around five percent (according to the World Bank today, low and universally applied tariff rates are ideal). Surely, this constraint must have had an enormous effect on Japan's industrialization? In my opinion, it did not. Japan at the time did not have industries that needed to be cocooned with protective tariffs. Setting aside the diplomatic issue of the loss of autonomy and the financial issue of insufficient tariff revenue, the fact that Japan could import manufactured goods and machinery from the West at low tariffs under these circumstances worked in favor of its industrialization. At this stage, where the light industrial revolution was in progress, free trade worked well for Japan¹⁹. However, before long industrialization was to progress a stage further to foster heavy industry. Here, technology accumulation and large investment in capital equipment were of great importance, and new industries would not have been able to gain a foothold without government support or protection from imports. Around the same time that Japan reached this stage (end of Meiji), tariff autonomy had been restored — first partially in 1899 and then completely in 1911 — and the government happily began to raise tariffs on industrial products. The timing was more than fortuitous. After this point, Japan was able to achieve industrialization based on heavy, chemical and manufacturing industries, which were protected by the interruption of trade during the First World War and high tariffs during the period between the two world wars. However, it is questionable if latecomer countries of today would be permitted to use this strategy of increasing tariffs which were previously low, as industrial development progresses.

The Role of Engineers

For the past several years, the development strategy of the international organizations, including the World Bank, has strongly emphasized the early establishment of Western values such as rule of law,

¹⁹ In his article, "Hogozei o Hi to Suru Setsu" (Why Protective Tariffs Are Undesirable) in *Meirokei Zasshi* (Journal of the Sixth Year of Meiji), Volume 5, 1874), Mamichi Tsuda put forward the following reasons against protectionist tariffs aimed at relieving the trade deficit: (1) they are impossible within trade agreements, (2) foreign goods such as iron and steel are much cheaper than domestic production and the latter cannot be protected by tariffs alone, (3) no factories that can produce Western-style manufactured goods exist in Japan as yet, (4) it is inconsistent to cut off imports when the nation's desire for imported goods is strong, and (5) the fact that Japan is backward and needs a large volume of Western products cannot be helped. Incidentally, in 1878 tariff revenues amounted to 9 percent of the total fiscal revenue. This ratio is fairly small when considered from the perspective of Japan's development stage at the time.

transparency, partnership, good governance, accountability, and civil society. International organizations assert these values as if they form the core of all development issues, and assume that just with their provision, the economy and society of a latecomer country should be able climb onto a steady track to development. However, does this intoning of fine but abstract phrases while ignoring the individual character and history of a country really amount to a development strategy?

What supported the startling industrialization of Meiji Japan was not the direct import of vain invocations from the West. It was individual businessmen of strong character who burned with zeal and the proud engineers who absorbed new learning like a sponge absorbs water and raced around the machines that equipped the factory floors. Japan during the period of its industrial revolution was very much like a living museum packed with energetic industrialists.

Twenty-six-year-old Takeo Yamanobe was a foreign student in England who studied Economics and Insurance at London University. In 1877, he unexpectedly received a letter from Eiichi Shibusawa. The letter read something like this: "I heard about you from a friend. In Japan, state-owned spinning mills are in a poor state and the import of cotton yarn is huge. For the good of our country, it is imperative that we establish high-performing spinning mills under Japanese control. For this to be possible, people familiar with technology and operations are indispensable. I plan to set up a spinning mill and I ask you to forget economics and start studying the technology of Britain's cotton industry." Enclosed with this letter were entreaties from his father and friends. How bewildered Yamanobe must have been at such an audacious proposition! Nevertheless, after some consideration Yamanobe decided to accept Shibusawa's request.

Yamanobe transferred to Kings College and began to study Mechanical Engineering. However, he noticed that his course focused on theory and was not linked to practice. He moved to Manchester, which was the center of the world's cotton production at the time, and there he visited factories and advertised in the newspapers requesting "employment as a trainee who was willing to pay tuition." He suffered countless rejections. At long last he met Mr. Braggs, the owner of a cotton textile factory, and for the next eight months he learned the ins and outs of cotton spinning — from ginning, spinning, and finishing to the purchase of raw cotton, the sales and marketing of finished goods, packaging and shipping. The cost of the traineeship was covered by research funds of 1,500 yen that Shibusawa sent to him. Regarding this large sum, Shibusawa remarked: "It was a leap of faith, like jumping down from the stage at Kiyomizu temple and hoping to land well!" Yamanobe was the first Japanese to learn the latest theory and practice of cotton production, and before he set off for home he purchased spinning machines and steam engines from Pratt & Co. and Hargreaves & Co..

On his return, Yamanobe, together with Shibusawa, set about locating a site for the mill. Moreover, Shibusawa had raised 250,000 yen in capital from businessmen and nobility, and had arranged for the operating costs to be financed by the First National Bank, of which he was president. In this manner, the Osaka Spinning Company was born in 1882. From the very beginning, the performance of the company was startling. Both on the technology and management fronts, ideas of the past had been thrown out completely. Innovations featured a five-fold increase in output capacity, the use of steam power, locating the mill in a large urban area and not in the backwoods, round the clock production, the selection of goods that would not compete with Britain, and a shift to using cotton from China as opposed to the domestically-grown cotton as the raw material. Stimulated by the rapid success of Osaka Spinning, Mie Spinning, Kanegafuchi Spinning, Settsu Spinning, Amagasaki Spinning and a host of other mills modeled on it sprang up all over Japan. Thus, cotton spinning grew into the key industry of the Meiji Period.

However, in the stock companies of Meiji Japan, including the cotton industry, the voice of shareholders who had little knowledge of industry was powerful, and they severely criticized the management if investment returns fell short. In contrast to this, technical experts like Yamanobe, who had a deep understanding of industry, bore the long-term development of the business in mind rather than focusing solely on short-term profit when working out production and investment plans. This was the archetypal clash between the owners and management. Particularly during the recession around the 1900s, this confrontation between the owners and management heated up at Osaka Spinning, and the president and shareholders alike criticized Yamanobe, its chief engineer. Discouraged, Yamanobe went to Shibusawa to tender his resignation. Instead, Shibusawa firmly supported him and advised him to remain in his post. Finally, as the economy recovered, Yamanobe was appointed president of Osaka Spinning as a specialist who combined technical knowledge and management experience²⁰.

What if Shibusawa had not sent that first letter, or what if Yamanobe had persisted with his study of economics? Or, what if Shibusawa had not supported Yamanobe in his time of difficulties? It is possible that the cotton industry of Meiji Japan would not have emerged. The source of the vitality of the Meiji economy was the social environment which produced men of caliber such as Shibusawa and Yamanobe one after another, and that is the secret of the country's phenomenal catch up.

Policy Assistance and Macroeconomic Management

What about the contribution of the government? Meiji Japan adopted the following policies with the aim of adopting technology. As mentioned before, this list does not include attracting foreign direct investment, which is the most popular method today.

1. Hiring of foreign specialists
2. Nurture of Japanese specialists through study and training abroad, at engineering schools and universities, and on-site at state-owned factories
3. Investment in munitions plants, railways, mining, shipbuilding, and agriculture
4. Transfer of state-owned enterprises in the areas listed above to the private sector
5. Establishment of indigenous Japanese *zaibatsu* by assisting *seisho* (influential businessmen) and the easing out of foreign interests
6. Encouraging invention and domestic production through industrial expositions

Some comments and notes on the above list are in order. First, state-owned enterprises had experienced little commercial success, as Shibusawa had mentioned in his letter. Moreover, the general consensus is that they contributed little towards the "suppression of imports," which is what the government had hoped for. However, even with this record, the state-owned enterprises of Meiji cannot be wholly dismissed as only a drain on the national budget. These enterprises, through the strong demonstration effect of modernization, the employment of foreign specialists and the latest machinery, and by using the latter to train Japanese technical specialists established the groundwork for the rapid growth of private-sector industry.

Furthermore, because all public works, with the exception of munitions plants, were eventually sold off to the private sector, they in fact became part of its capital stock. The process of privatization was not transparent and criticized as only benefiting *seisho*, who paid almost nothing for the factories in comparison with the capital that had been invested in them (a similar criticism arose in the privatization processes of the countries in the former Soviet Union in the 1990s). However, as mentioned before, a large

²⁰ Matao Miyamoto, *Nihon no Kindai 11: Kigyokatachi no Chosen* (A History of Modern Japan Vol.11: Challenges of Entrepreneurs), Chuo Koron Shinsha, 1999.

number of these businesses were in the red and many of them needed large amounts of fresh investment to survive. We have to give just credit to the businessmen who willingly took on these loss-making businesses and successfully turned them around. Also, the role of the government, which took on the risk of modernization and bore its initial costs through establishing state-owned enterprises, should be duly acknowledged. All in all, we can call the state-owned enterprise strategy of the Meiji government a success. This is a considerably different opinion to that prevalent today in the development community, which flatly denies any role to state-owned production.

Turning our attention to technology transfer, this was achieved through three channels²¹. First, the employment of foreign specialists: Here, the cost of employing these professionals was so high that it became a major pressure on the national budget. To ease this, the government attempted to replace foreign specialists with Japanese, and this effort bore fruit around the 1900s when the number of foreign nationals employed dropped dramatically.

Second, the training of Japanese specialists: This was achieved through study and training abroad, the founding of *Kobu Daigakko* (an engineering university that later became the Faculty of Engineering of Tokyo University), and the creation of a multitude of technical vocational schools. The Japanese who studied abroad at the time attended the best universities in America and Europe to learn about the latest technologies, and it was not unusual when they replaced the foreign specialists on their return to Japan. At *Kobu Daigakko*, located in what is now Kasumigaseki in Tokyo, the teaching materials were all foreign texts and many of the lectures were conducted in either German or English.

Third, the importing and imitation of machinery: Here, Japanese engineers demonstrated an amazing capacity for selecting technology appropriate for the country and then absorbing and adjusting it. For example, when it was time to introduce a telephone service, Saitaro Oi of the Ministry of Communication and his fellow graduates from *Kobu Daigakko* collected publicly available information, conducted research in the West, and after negotiations with telephone makers there, decided on a system to adopt.

From around the 1900s, in an attempt to start up its own machinery production, Japan initiated a new method for adopting technology through collaboration between domestic and foreign businesses. Some examples of this cooperation included Japan Steel Manufacturing (a warship outfitter), a joint venture of the Mitsui Group and the British firms of Armstrong & Co. and Vicars & Co.; Nippon Electric Company (telephones) established with technical assistance from America's Western Electric; Tokyo Electric Company (light bulbs), which had a similar relationship with the US firm General Electric; and Shibaura Manufacturers (heavy electrical machinery, later to become Toshiba), which also received technical assistance from General Electric. Even in these cases, Japan quickly digested the new technology and was also able to adjust it for its needs. Behind all of this activity was a large number of Japan's elite who avidly studied engineering (not finance, law or management!). They advanced into every branch of industry and formed a rich pool of human resources for Japan's industrialization process. (A more recent example of this phenomenon was visible in the construction of the Pohang Steel & Iron Co. (POSCO) in Korea where Korean engineers, having received wide-ranging technical assistance from Japan, were quickly able to make the technology they worked with their own).

A point that we should not forget is that native craftsmen and artisans from the Edo Period did not just molder away upon the introduction of Western technology. Certainly, new industries such as the

²¹ Hoshimi Uchida, "Gijutsu Iten" (Technology Transfer) in S. Nishikawa and T. Abe, eds., *Sangyoka no Jidai 1: Nihon Keizaishi 4* (The Age of Industrialization 1: Japanese Economic History) Vol.4, Iwanami Shoten, 1990.

railways and telegraph and wire communications had to be adopted as completely novel forms. However, as regards construction, sake-making and brewing, printing and the making of hand tools and instruments, traditional production technologies managed to survive for a long time. They went through an evolution, sometimes merging with Western technology, sometimes existing alongside modern equipment that had been introduced on a small scale, or by finding a niche market. Takafusa Nakamura calls this coexistence of traditional and modern technologies “new indigenous industries,” while Konosuke Odaka describes it as “the parallel development of the indigenous and the modern.”

This tendency is most vividly depicted by the development of the cotton industry. As mentioned before, this was the star industry of Meiji Japan. However, along with the modern spinning mills with hundreds of young female workers standing in rows operating cutting-edge machinery, a completely different traditional workplace for cotton goods production —through the *putting out system* or the small-scale household production coordinated by a broker — existed for a long time in parallel. In the beginning, modern mills were devoted entirely to spinning and traditional production for the most part took on the task of weaving. Modern factories first wove cloth from domestically produced yarn as Japan entered the twentieth century. Also around that time, powered looms were adopted into traditional production and the mechanization of the textile industry advanced. Thus, Japan’s light industrial revolution was a process where traditional and new technologies worked together and complemented each other.

In addition to the policy of technology absorption, macroeconomic management also strongly affected the ups and downs of the private sector. The monetary and financial systems of early Meiji were in turmoil. Moreover, the reckless printing of unconvertible paper money to cover the cost of quelling the Satsuma Rebellion in 1877 caused inflation. This inflation enriched farmers but impoverished the samurai class whose rice salaries had been changed into the one-time receipt of government bonds (whose value was nominally fixed). This situation of monetary confusion was terminated by the deflation policy adopted by finance minister Masayoshi Matsukata in the early 1880s. During the Crisis of 1881, as noted earlier, Shigenobu Okuma and his faction which advocated political radicalism were ousted from the government. Okuma was also a fiscal activist and once he was gone, Matsukata assumed the councillorship for finance and the government was ready to pursue a policy of tight money and fiscal austerity. The price deflation that followed plunged Japan into recession. The price of rice fell especially hard.

When viewed from the perspective of long-term industrial development, the Matsukata deflation was significant in two ways. First, it caused the farmer class, which had grown rich until now, to fracture and accelerated the differentiation of the class into landless farmers and absentee landlords. It also brought the civil rights movement that had been financially supported by wealthy farmers to a standstill. Secondly, Matsukata built the financial foundation for industrial growth by establishing the Bank of Japan as the sole authority to issue money, thus ending the state of monetary confusion. Using slightly outdated terminology, we can say that the Matsukata deflation, by creating a proletariat class and providing financial capital, built the basis for capitalism in Japan.

Once the Matsukata deflation was over, the Japanese economy entered the so-called *kigyo bokko* (company boom) period. This period, beginning in 1886, released the energy of the young private sector and the country rushed into an unprecedented boom of setting up joint stock companies. Railway construction and textile production occupied the core of this activity. Moreover, the government underpinned the boom by providing easy money and permitting the yen to depreciate in foreign exchange. A succession of waves to establish stock companies again surged in the late 1890s, at the end of the 1900s, and during the First World War. Besides this, after both the Sino-Japan War (1894-95) and Russo-Japan War (1904-05), the central and local governments adopted the policy of “post-war management,” namely, active fiscal spending for military buildup, railways, telecoms, steel production, waterworks, road-building,

education, and the administration of Taiwan (Japan's newly acquired colony). The small government by degrees transformed into a big government and brought about a widening of the balance-of-payments deficit, a reduction in gold reserves, an increase in the outstanding balance of government bonds, and the external borrowing of local governments. The policy disputes between fiscal activists and the *minryoku kyuyo* (easing the popular burden) faction, which advocated tax and spending cuts and a free economy, persisted from the first Imperial Parliament in 1890 to the eve of the Pacific War and formed the biggest economic issue for the-whole of pre-war Japan.

Akira Hara, an economic historian, summarizes the industrialization of the Meiji Period as follows:

“The industrial revolution that started with the *kigyo bokko* period progressed rapidly during the Sino- and Russo-Japan Wars, and was almost over by the end of the Russian conflict [1904-05]. Cotton spinning, the silk industry and textile production alike developed rapidly, while shipbuilding and machinery production, and the steel industry on which they were based, also formed a foundation for future progress. The coal-mining industry secured a source of energy, while the silk industry earned the foreign exchange that supported the frail machinery industry. Munitions plants also became autonomous by relying less on imports”²².

There is a great deal more that can be said about Meiji industrialization. But even with the limited description in this chapter, I hope the reader is able to sense the atmosphere that abounded in the extraordinary period known as Meiji. It possessed a strangely fluid and dynamic society which nurtured groups of people with outstanding ability while allowing an inventive private sector and government support for industry to mesh. The agents of change during Meiji lamented the country's hopeless backwardness. However, knowing what we do of latecomer countries today, we can say in hindsight that Japan of that time fared pretty well. I wonder if there is a way to transmit the atmosphere of Meiji society and its dynamism to latecomer countries of today.

5 Japan, the First-Class Power

The Words of Soseki Natsume

With Japan's military, economic and political catch up to the West for the most part complete, when was it that Japan became aware of itself as a first-class power? Even if the exact point cannot be clearly identified, the Russo-Japan War (1904-05) was without doubt an important milestone for the country. The nation, drunk on its victory against white Imperialist Russia, criticized a government unable to win indemnity payments as part of the Portsmouth Treaty. The mass media in unison raised the slogan of “Down with the shameful peace, on with the war!” The National Anti-Peace Conference, a rally against the signing of the treaty held in Tokyo, broke down into a mob that burned and looted (Hibiya Riots).

The life of Soseki Natsume (1867-1916), perhaps the most popular novelist in Japan then and now, largely coincided with the Meiji Period. He was well acquainted with both English and ancient Chinese literature. His early novels were sometimes comical (*I am a Cat* and *Bocchan*), sometimes romantic (*Sanshiro*) and even aesthetic (*Kusamakura*). But his later novels exposed the dark side of modern Japan, featuring individuals who struggled within human limitations and feudal constraints in modernized life without success (*Sorekara* and *Mon*). In his lecture, “The Development of Modern Japan,” delivered in

²² Akira Hara, *Nihon Keizaishi* (The Economic History of Japan), University of the Air Press, 1994.

Wakayama in 1911, Soseki cast the following words at his compatriots around the time they had begun to swell up with self-confidence and conceit at Japan becoming a civilized nation that ranked equal with the West (this was the year in which Japan's autonomy over its tariff system was fully restored).

The development of the West was an endogenous process, while that of Japan today is exogenous. Here, "endogenous" means to come naturally from within, just like a flower opens from a bud in an outward motion of its own accord, while by "exogenous" I mean being forced to take a certain form under an external influence... Japan's development since that time [the opening of the country in the late Edo Period] started to take a completely new course, due to the enormous shock we sustained that made change unavoidable. To use the term I introduced earlier, our nation, which until now had evolved endogenously, suddenly lost control and found itself coerced to take whatever action that was forced upon it, whether willing or not.

I sense that this is a problem shared widely by the latecomer countries of today. If I were to call Meiji Japan a transition economy and liken its opening to the West to the collapse of the Soviet Union, then would it be too bold an analogy to liken the WTO and IMF to Commodore Perry's black ships? A nation having global integration forced on it is unsettled because the change is not of its own making.

The waves that direct Japan's development come from the West. Because, we Japanese who ride these waves are not Westerners, as each new wave approaches we feel uneasy, like a person living in someone else's house... Instead of being able to enjoy the many delicacies offered to our heart's content, it is as if they are cleared away and the table is set again with new dishes before we have a chance to clearly see what was on offer. A nation that experiences this kind of development process must be left with a feeling of emptiness and insecurity. We should not pretend that this type of development is somehow endogenous. Such an attitude is make-believe. It is insincere, shallow, and not acceptable.

So, what should we do? Soseki has no good answer.

However much we flatter ourselves, one part or even a large part, of our development process can only be evaluated as superficial. That does not mean we should put a stop to it because it is no good. We must accept reality. After swallowing our tears, we have to continue sliding along on our superficial course... I have no brilliant solution to offer. All I can say, just for the record and without much substance, is that we should try to evolve as endogenously as possible while avoiding a nervous breakdown.

The discomfort of the Japanese that Soseki witnessed stemmed from the feeling of loss of autonomy and self-esteem. This is an experience common to all latecomer countries that have to integrate into the periphery of an existing world system. Not only Japan, but all societies placed in this position must endure it. Despite Soseki's lamentations, Japan thereafter accomplished a spectacular catch up to the West on the material as well as institutional front (even with the enormous tragedy of the war that intervened). However, who have we ourselves become, the "we" who are so successful at imitating others? After all these years, we have neither resolved nor eliminated the issues Soseki raised. We have swept them under the rug but they still remain in the depth of our consciousness. Whenever we are ready to face them, these problems will immediately surface and challenge us. Since the end of Meiji, this important question concerning the Japanese identity has been neither deepened nor dealt with squarely. Even in today's latecomer countries, the impact of global integration on their societies and spiritual life has escaped proper attention and analysis, leading only to a repulsion of and dissatisfaction with external pressure at the emotional level. The investigation of this issue as a legitimate branch of social science is an important task

in economic development — a task becoming of a Japan that succeeded in catching up with the West while maintaining its non-Western traditions.