



T.C.
SOCIAL SCIENCES UNIVERSITY OF ANKARA
INSTITUTE FOR AREA STUDIES

YİĞİTCAN UYKAN

UNDERLYING FACTORS OF THE ECONOMIC MIRACLE OF
JAPAN AFTER THE SECOND WORLD WAR

THE DEGREE OF MASTER OF ARTS
IN
ASIAN STUDIES

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I hereby declare that all information in this document has been obtained and presented in accordance with academic rules and ethical conduct. I also declare that, as required by these rules and conduct, I have fully cited and referenced all materials and results that are not original to this work. I declare that this thesis is written according to the writing rules of Social Sciences University of Ankara, Institute for Area Studies.

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My interest in Japan and many aspects of it, such as history, economy, and culture, have been my personal motivation for doing this specific research. Understanding the factors that contributed to the Japanese miracle has been a great opportunity for me to increase my knowledge of the subject. Therefore, I would like to express my sincere, innermost, and special thanks to my supervisor Assist. Prof. Resul Yalçın to whom I am greatly indebted for his advice, encouragement, and invaluable assistance during the preparation of this dissertation. Without his assistance and friendly attitude, this dissertation could not have been written. I would also like to thank all the academics and students of Asian studies for their friendliness and supportive assistance.

ABSTRACT

Japan has undergone four significant phases in the post-war period: reconstruction in the late 1940s of the war-induced economic downturns, stability period in the 1950s, fast growth in the 1960s and early 1970s, and ending fast growth triggered by the first oil crisis in 1973. The aim of this thesis is to determine the factors related to the evolution of Japan's economic development called as Japanese miracle after the Second World War and until the oil crisis of the 1970s. In the post-war era, following the occupation and influence of the United States along with the increased intervention of the Japanese government in the economy, enhancing its capacity to foster sustainable growth through exports and investment, Japan experienced an economic miracle and became one of the most flourishing industrial economies in the world. A series of reform policies have been set out by the U.S. occupation of Japan aimed at rebuilding and restoring the ruined nation and ultimately creating an opportunity for Japan to become an industrial superpower. These reform policies have had a significant effect on the democratization and transformation of the nation which affected the capacity of the nation to evolve. Furthermore, Japan as a 'developmental state' set out policies aiming to achieve fast growth through promoting and protecting the key industries from foreign competition under the guidance and control of the state. In order to understand the Japanese economic miracle, the key concepts of political, social, and economic shifts accompanied by the impact of the state's capacity during the 20th century will be examined. Additionally, this thesis also seeks to contextualize the mechanism of Japanese growth under the state's intervention in a country of a different culture and that has been experiencing ongoing economic growth.

Keywords: *Japanese Government, Reforms, Economic Growth, Developmental State, Policies, State Capacity.*

ÖZET

Japonya İkinci Dünya Savaşı sonrası dönemde dört önemli aşamadan geçmiştir:1940'ların sonlarında savaş kaynaklı ekonomik gerilemenin yeniden yapılanması,1950'lerde istikrar dönemi, 1960'larda ve 1970'lerin başında hızlı büyüme ve 1973'teki ilk petrol krizinin tetiklediği hızlı büyümenin sona ermesi.Bu tezin amacı, İkinci Dünya Savaşı'ndan sonra ve 1970'lerdeki petrol krizine kadar Japon mucizesi olarak adlandırılan Japonya'nın ekonomik gelişiminin evrimi ile ilgili faktörleri belirlemektir.Savaş sonrası dönemde, ABD'nin işgalini ve etkisini takiben Japon hükümetinin ihracat ve yatırım yoluyla sürdürülebilir büyümeyi teşvik etme kapasitesini artırarak, ekonomiye müdahalesinin artmasıyla birlikte, Japonya ekonomik bir mucize yaşadı ve dünyanın en gelişen endüstriyel ekonomilerinden biri oldu.ABD tarafından Japonya'nın işgali sırasında, harap olmuş ülkeyi yeniden inşa etmeyi, eski haline getirmeyi ve nihayetinde Japonya'nın endüstriyel bir süper güç haline gelmesi için bir dizi reform politikası ortaya konulmuştur.Bu reform politikalarının ülkenin gelişme kapasitesini etkileyen ülkenin demokratikleşmesi ve dönüşümü üzerinde önemli bir etkisi olmuştur.Buna ek olarak, 'Kalkınma Devleti' olarak Japonya, devletin rehberliği ve kontrolü altında ülkenin önemli endüstrilerini dış rekabetten koruyarak ve bu endüstrilerin kalkınmasını teşvik ederek hızlı büyümeyi amaçlayan politikalar ortaya koymuştur. Japon ekonomik mucizesini anlamak için, 20. yüzyıl boyunca devletin kapasitesinin etkisiyle birlikte siyasi, sosyal ve ekonomik değişimlerin temel kavramları incelenecektir.Buna ek olarak, bu tez aynı zamanda Japonya'nın ekonomik gelişimini farklı bir kültüre sahip olan ve devletin müdahalesi altında halihazırda ekonomik büyüme yaşayan bir ülkeye bağlaştırmayı amaçlamaktadır.

Anahtar Kelimeler: *Japon Hükümeti , Reformlar , Ekonomik Gelişim , Kalkınma Devleti , Devlet Kapasitesi , Politikalar*

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ABBREVIATIONS

BOJ: Bank of Japan

FILP: Fiscal Investment and Loan Program

GATT: The General Agreement on Tariffs and Trade

GHQ: General Headquarters

JDB: Japan Development Bank

JETRO: Japanese External Trade Organization

MITI: Ministry of International Trade and Industry

MOF: Ministry of Finance

OECD: Organization for Economic Co-operation and Development

OPEC: Organization of the Petroleum Exporting Countries

SCAP: Supreme Commander for the Allied Powers

WW2: World War 2

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INTRODUCTION

The miraculous success of Japan's economic recovery after World War II has been an interesting topic for many researchers and a great example to give for any countries who faced economic destruction.

After WW 2, Japan was in a difficult situation: devastated by the war economy of the military regime, lost her colonies, and the U.S occupation that controlled pretty much everything. It has been undeniably one of the worst economic conditions in which Japan has experienced. Nevertheless, in such a short period of time, Japan has managed to overcome the obstacles and rebuild her economy which ultimately led her to become the second-biggest economy in the world after the United States. The achievements of the Japanese economy are built upon peculiar mechanisms many scholars have attempted to examine and understand. The post-war growth of Japan was referred to as a miracle that stunned the world (Johnson, 1982, p. 40). This miracle has historical significance in the sense that many underdeveloped countries, particularly in the Asian region, have seen Japan as a model of success and therefore they have attempted to follow her model since Japan has been the first East Asian country to undergo such an economic growth at the level of Western nations. As a result, steps taken in Japan have prompted other countries in the region, such as China and Korea, to take similar steps.

The Japanese model relies on state-led policies in order to promote the economy which the other East Asian Economies imitated. For example, the protectionism which was already prevalent in Japan has been imitated in a different way in China because of its political structure. Therefore, this study will concentrate on Japan's state capability regarding the relation between state capability and the economy of Japan, and its effect on and the Japanese economic miracle in order to figure out whether the same steps could be applied in a country with a different culture that has been undergoing a certain degree of development.

1. Problem Statement

Japan's defeat in World War II left the nation in ruins. However, the nation managed to rebuild its economy and promote economic growth through reforms and policies implemented by the state. Thanks to the close cooperation between the state and the large businesses, the Japanese economy had surpassed prewar levels. Therefore, Japanese transformation was seen as the model to follow for many developing Asian countries since Japan has been the only country in Asia to undergo economic development on par with other Western countries.

The role of the state in a country's economic development has aroused the attention of economists and academics. The relationship between government intervention and economic growth has been widely debated for several years, but there are many disagreements among scholars about the true effects of government intervention on economic growth. While some scholars such as Robinson & Acemoglu (2005) consider state intervention as essential for economic growth, others Bailey et al. (2007) criticize it, claiming that it weakens the free competition by favoring some businesses over others.

Despite the fact that there is a considerable number of literatures on the role of the state in economic growth, there is very little in the Japanese case. This is the driving force behind this study, as I seek to determine whether there is a connection between government intervention and economic growth in Japan. Moreover, the effects of implemented policies as well as exogenous factors will be analyzed.

2. Research Questions

This thesis seeks to answer the questions listed below.

- How did Japan cope with defeat after the Second World War?
- What problems did the Japanese economy face in the postwar period?

- What does the Japanese miracle mean?
- What is the main factor of Japan's economic success?
- What can we learn from the Japanese economic growth?

3. Research Aims

- To determine the main characteristics of the policies implemented by the Japanese government through historical background,
- To provide analysis of such policies in terms of their contribution to the economic growth,
- To explain why Japan's state-led policies have been so effective,
- To find out whether the outcome of these policies can be applied to any other nation under such circumstances.

4. The Significance and Purpose of the Research

The main objective of the study is to find out the factors that the scholars have been advocating as a response to Japanese economic growth after the Second World War until the oil crises in the middle of the '70s and evaluate whether the Japanese miracle took place. The researchers argue that the government-led policies and exogenous factors require special attention to the rapid economic growth of Japan. In order to draw a conclusion on each of the variables; the study includes both a bibliographical analysis of the scientific studies and statistical analysis of the official data regarding this subject. The study has significance because it focuses on the era known as the high growth period, during which Japan experienced rapid development. Moreover, the study will concentrate on the factors that triggered such rapid growth and find out whether to contextualize the Japan's growth process in a country with a distinct culture and economy. As a result, Japan's state-led policies have significant outcomes that justify investigation and analysis since they can provide insights

based on historical findings. Centered on Japanese experience, the study both provides a comprehensive understanding of the state's role and contributes to the debate about the impact of state-led policies on economic development. The outcome of this study can be a useful guide for those interested in learning more about Japan's economic development.

5. Research Methodology

In this thesis, a mixed methodology of qualitative and quantitative analysis will be employed to understand the underlying factors of Japanese economic growth. The reason for using this method is related to the study's main focus. When studying a subject with a complex structure, qualitative analysis is used to obtain a better understanding of the underlying causes and opinions as it enables the researcher to conduct in-depth analysis of a given subject. Therefore, the document analysis technique which is a form of qualitative research will be used to obtain findings and data. According to Bowen (2009), documents provide background information and a wide range of data, making them useful for contextualizing research within the context of its topic or area. During the data collection process, secondary sources and historical data such as articles, books, and reports from scholarly journals along with government databases available on the internet will be the key sources of this study to interpret the collected information through official institutions, the Japanese government's open data as well as the articles and books that were written on this subject. These sources will contribute to providing background analysis and a review of the literature. Lastly, it will be determined whether the Japanese Miracle took place.

In order to document the information gathered in the course of this work, each scientific article and book that can be cited and covers relevant information that contributes to the explanation of various factors in this study will be listed. When evaluating information and analyzing data, a quantitative method of statistical analysis will be used to try to eliminate any bias for presenting arguments through numeric and unchanging data.

6. Research Scope

- The era between 1960 and 1980 is the focus of the study. The study, on the other hand, includes a historical background in order to provide analysis.
- The analysis is based on the policies of the Japanese government and their implementations.
- The effects of exogenous factors, human capital and business conglomerate will be evaluated.

7. The Limitations of the Study

The main limitation of the study is the data availability. For certain variables, there is a lack of data to cover the entire study period. Besides lack of quarterly data on some variables forces us to rely on annual data. Another limitation encountered when conducting this research was data inconsistency from various organizations.

8. Structure of the Thesis

The first chapter covers the objective of the study, applied methodology in the conduct of the research along with the literature review that includes previous researches and examples of the theory of state capacity as well as the role of cultural values. The second chapter covers the historical context of the Japanese miracle and demonstrates the economic situation of Japan in the postwar period. The third chapter covers the analysis of the Japanese government's macro-economic policies, particularly the Ministry of International Trade and Industry (MITI) and the Ministry of Finance (MOF) as well as stresses the role of the private sector during the post-World War II period of high economic growth in Japan. The conclusion of this thesis will be made at the end.

9. Literature Review

Japan's Model of Economic Development

The article focuses on the Japanese model of economic growth in the post-war period. The author Kimura emphasizes the factors such as macroeconomic stability, human resource development, and domestic saving rates have been the key factors for Japanese economic development claiming that these factors have enabled Japan to restart from war devastation and achieve notable economic growth in 1955-73. Additionally, he argues that industrial policy in Japan had mixed results, depending on how well it countered market failure and exploited market dynamism. He explains during the reconstruction period, Japan put a lot of emphasis on macroeconomic management due to the lack of resources, hyperinflation, and unfavorable external conditions. In order to curb up the bottlenecks, several policies have been implemented. Public organizations such as MITI aimed to boost the rapid industrialization of the nation through subsidies and special tax exemptions for private corporations and domestic saving rates contributed to the high investments and importation of foreign technology. According to him, the introduction of foreign technologies and machinery has been a crucial step in achieving international competitiveness. However, he claims that although industrial policy worked to some extent in the reconstruction period, industrial policy brought upon limiting competition between firms and providing strong leverage for bureaucrats and MITI which in return clashed with interests of private corporations in the high growth period when they were unlikely to follow the intention of the government.

In conclusion, he states that several factors that influenced Japan's growth can be applied to the developing countries today in a much better external environment, where obtaining support from the international community will be much easier.

Japanese Industrial Policy

This article examines Japan's rapid growth following the end of World War II, as a result of the industrial policy implemented. The author Nishijima regards Japanese industrial

policies as one of the most important factors for the economic growth of the nation stating that these policies have both increased the productivity and competitiveness of Japanese businesses. He also points out that Japanese industrial policy is relatively different from the rest of the world in terms of unique management style and bureaucracy since the bureaucratic system is largely independent of the political situation which enabled policy decisions to be more economic-oriented. The author argues that the Ministry of International Trade and Industry has been the most influential ministry which implemented various policies for specific Japanese companies based on the criteria of growth potential. However, the author criticizes this system for having an excessive influence on the Japanese economy through the constant intervention on the Japanese corporations which in return causing factionalism, and further adds that this system cannot work in the modern world where the market dynamics are different from back in those days. Apart from the industrial policy, the author explains that Japanese-style management such as lifetime employment, seniority-based wage, promotion, and enterprise unions have been key factors for such growth because these characteristics brought upon confidence and mutual respect between employer and employee.

In conclusion, the author thinks that some aspects of Japan's industrial policies appear to have significant consequences for developing nations.

Savaş Sonrası Japonya'da Sanayi Politikası : MITI Ne kadar Başarılıydı

The author Uzun aims to investigate the effect of postwar Japanese industrial policy, as well as MITI initiatives, on Japan's economic recovery and growth process following WWII.

She defines industrial policy as any form of government intervention in specific sectors with the goal of boosting those sectors' growth prospects and promoting overall economic development. In the case of Japan, she states that three core strategies have been used. The first of these has been targeting key industries for rapid growth. The second has been the protection of emerging and strategic industries from foreign competition by

restricting imports in the early stages, as well as subsidization of declining industries. The third step has been to promote the exports of manufactured goods, especially through government assistance such as marketing institutions and other export mechanisms.

She further divides periods into sub-periods in order to analyze the development of Japanese industrial policy in the post-war period. In the period from 1945 to the 1960s, the Japanese economy started to recover from the war destruction and the Priority production system was introduced which the government aimed to increase coal and steel production by various incentives. The Korean War also helped to the recovery of the economy. She points out that the enactment of the Anti-Monopoly Law and steps to ensure macro stability enabled the increased competitiveness and productivity of the Japanese economy. From the 1960s until 1973 she argues that Japanese industry was at the peak as the nation's GDP grew over 10% and the economic structure shifted from agriculture to industry and the industrial structure from light industries to heavy industries such as petrochemical and automobile. MITI in this period promoted several key industries through tax benefits and subsidies. She claims that most of the MITI's acts have been successful in this period. However, she also criticizes that some of the steps that the MITI took were against the Japanese Industry and competitiveness by giving an example of MITI's failed attempt to merge different Japanese automobile manufacturers or giving more subsidies and guidance to the low productivity sectors such as mining than electronics.

In conclusion, the author argues that even though the Japanese industrial policy has contributed greatly to the transformation of the nation from a technology importer to an exporter, it was the willingness of the Japanese business community and their private investments towards creating a business which was more competitive. According to her, considering MITI as a contributor toward the businesses has been in the role of creating an environment where the investments in the private companies were encouraged as well as the low corporate taxes unlike the interventionist steps.

Rapid Economic Growth in Post-War Japan

The article focuses on the postwar economic growth of Japan by analyzing the Japanese Keiretsu companies as the fundamental driving force for such growth.

The author Miyazaki states that the fierce competition among the keiretsu companies has been a driving force in the postwar economic growth of Japan because these companies aimed to maximize their profits, therefore, spending much money on plants, equipment, and r&d. He distinguishes the keiretsu companies from the pre-war zaibatsu groups in a way where they center on and how they operate. Unlike zaibatsu groups which are run by family members as a holding concentrating on the commercial sector of their businesses, keiretsu groups are centered on the heavy and chemical industries where constant innovation is required and there is no family-run holding in this group. According to him, the emergence of keiretsu groups after the dissolution of zaibatsu groups along with anti-decentralization act brought about serious competition between companies, and the nation's economy has been benefited from this competition because companies expanded their investments and fields of work in order to become a leading company.

The author claims that Japanese style indirect financing of keiretsu companies has been a leading factor for these companies to finance their investments. This indirect financing is a method that is centered on private financial institutions giving out loans backed by the Bank of Japan to keiretsu companies. The competition among the private financial institutions in loans has resulted in obtaining large sums of money with low-interest payments. However, he also argues that this method favored the large companies and placing a great gap between small and large companies.

In conclusion, the author sees the great competition between keiretsu companies favored by the government initiatives to boost productivity as the backbone of the Japanese postwar economic growth.

Factors in Japan's Economic Growth

The author Shinohara focuses on various factors that contributed to the Japanese economic miracle in this article. In order to better understand the factors in the post-war period, he divides the post-war period into three phases, 1946-1951-rehabilitation, 1951-55-consolidation, and 1955-61-high growth.

In the rehabilitation period, the author explains that Japan implemented reforms such as land and labor reforms along with production priority reforms which increased productivity. During this period, the nation also decreased military expenses since the nation was under the control of occupation forces, not allowing them to possess heavy artillery and weaponry. These military expenditures were then channeled to expanding investment thus accelerating growth. With the newly implemented reforms contributed to the growth by increasing productivity, Japan also focused on expanding its market, and thanks to the Korean War, Japan was able to accumulate enough foreign capital to finance its technological innovation.

In the consolidation and high growth period, he states that the increase in the labor force combined with the introduction of new technologies resulted in lower prices and expansion of exports. The role of government has been particularly important for key sectors by introducing policies such as tax revision, foreign exchange allocation for their investments in plant and equipment with the backing of the Japanese financial structure. The Japanese financial structure was in favor of lending loans with low interest to the big companies which he called indirect financing.

On the other hand, He argues that only big enterprises have benefited from this system which arouses dualism in the economy. He states the dual structure in the economy has been essential for the rapid growth because if a country that is late in development tends to have a dual structure at home. He explains the dual structure as having small and medium enterprises coexist with top-level modern industries. This results in a high rate of export growth and domestic growth with the benefit of low prices. However, he argues that this benefit started to fade away as the low-wage differentials were narrowed over time.

In conclusion, he emphasizes the motive factors for the rapid growth were the structural factors such as financial and dual structure which caused export growth and market expansion, and the rehabilitation factors such as decreasing military expenditures and implementing new reforms with the role of the state.

Trade, Growth, and the Balance of Payments of Post-War Japan

The article focuses on the role of foreign trade and the balance of payments in the post-war economic growth of Japan. The author Ozaki claims that since the recovery period Japanese economy has accelerated steadily in subsequent years thanks to the increase in the volume of foreign trade through nations' exports. These exports accumulated an inflow of foreign capital which in return enabled the nation to fix its balance of payments, concentrate more on innovation on its exported products as well as finance its imports contributing to nations' growth. He states that the role of trade in Japan's post-war growth acted as a cushion for internal recessions and drastic economic contractions. The post-war period of hyperinflation followed by the period of stagnation turned out to be short-lived with the outbreak of the Korean War which caused a high demand for Japanese products and led to an investment boom, facilitating the growth of the Japanese economy. He also emphasizes that the United States economic aid had a significant impact on the reconstruction of the Japanese economy since the aid became a major source of improving the balance of payments and promoting strategic industries during that time. According to him, the reason why Japan was selected for special US procurement is due to her already achieved fair development which could manufacture certain goods and its geographic proximity to Korea.

After the war, he states that the increased influx of foreign capital and decline in the prices of Japanese imports contributed to the savings of foreign exchange and balance of payments. Through accumulated foreign reserves and government policies, the nation concentrated more on technological innovation and diversification of its exported goods. However, he criticizes the increased intervention of the government on which products should be prioritized and which sectors should be benefitted claiming that while this boosted

some sectors and their volume in foreign trade such as technological products, it also discouraged some other sectors.

In conclusion, the author regards the rise in the trade as one of the most important catalysts for the Japanese steady growth, stating as the country could produce high-level products with competitive prices in order to win in international competition through a catch-up process with Western economies so did the Japanese economy keep on growing.



CHAPTER 1

1.1. Japanese Model of Postwar Economic Growth: Industrial Policy

Industrial policy can be defined as any policy implemented by the state with the aim of achieving the economic development of a nation through designing strategies and intervening in the allocation of resources across industries or sectors (Pack and Saggi, 2006). There are ongoing disputes related to the effectiveness of the industrial policy. Those who support this policy claim that industrial policy is one way to fix market failures and promote economic growth through the capacity of bureaucrats to deal with business failures and the capacity of government to distribute resources properly by serving as mediators when market forces and private sector activities are inadequate to foster development and business transformation, the government steps in (Rodrik et al., 2008). But others argue that markets can work without government intervention, arguing that coping with market failures effectively is virtually impossible by intervention as the government faces a lot of challenges in finding the best tool to meet the objectives, thereby creating the possible market disruptions as well as bureaucrats are not as successful as markets in controlling all the knowledge that is scattered. (Buigues&Sekkat, 2009).

The Japanese case demonstrates that industrial policy had a major impact on increasing productivity and thereby improving economic efficiency since market failures existed and institutional reform was needed after WWII. The aim of Japan's industrial policy was to provide direct support to industries in order to foster economic development. The focus of industrial policy was on large corporations, which were seen as crucial to the recovery of the economy after the Second World War. According to Kimura (2009), with the role of industrial policy and the support of the government in the form of industrial policy to large companies, enabling them to buy and import foreign technology which led to its industrial growth, Japan is seen as the first nation outside the western hemisphere to achieve a strong industrial development. It began with severe capital shortages, but through self-

financing and high savings rates, it was able to accumulate capital without relying on foreign direct investments as Johnson (1982, p 9.) argued in his study, "Government industrial policy has made a difference in the rate of investment in some economically strategic industries, such as the growth of the production and efficient marketing of petrochemicals or automobiles."

Schaede(2004) states that production-oriented policies built around this framework have fueled Japan's development. Either directly or indirectly, government policies supported large companies and their employees. Small companies and sectors that were not part of the development model, on the other hand, were supported by special policies or subsidies.

Tomlinson and Cowling introduced Japan's growth model which not only was key in outpacing international competitors but also seen as an alternative to Communism and Neo-liberal model based on two major elements: interventionist industrial policy and the institutional structure based on The Japanese Corporation (Cowling & Tomlinson, 2011). They argue that government policies helped large Japanese companies grow their businesses. For example, during the high-growth era, the company's commitment to optimizing growth while also prioritizing internal growth over acquisitions created several opportunities for employees to become more active and It also contributed to Japan's economic success since the corporate interests are aligned with the country's growth.

From the historical viewpoint, the Japanese economy in the following World War II can be seen as a continuation of the national attempt to catch up that started at the end of the 19th century. Gerschenkron and Hunter (1963) highlighted the underlying difference in the development mechanism of industrialized and emerging economies in their study on "backward" economies, and their ideas have since been integrated into systematic models of economic growth. Backward nations, according to Gerschenkron and Hunter, have a greater capacity for rapid growth. In other words, these nations can catch up quicker with developed nations if they are originally somewhat backward. The "backwardness" of the Japanese economy compared to the developed Western economies was the fundamental factor for

growth since Japan could benefit significantly from technologies imported from more industrialized nations. Japan, as a latecomer to modernization, was able to avoid some of the trial and error that other countries had to go through while developing industrial processes. This has shown Japan a high potential for rapid growth with the implementation of these new technologies. Besides, Japan's relative backwardness allowed her to not only take advantage of available foreign technology but also to take advantage of internal opportunities with dedication not only to the improvement of its industrial capacity by patent acquisitions, technology licensing, and replication or refinement of foreign inventions but also to research and development in the 1970s and 1980s.

On the other hand, Prescott, and Hayashi (2008) state that the key factor for the Japanese miracle was the shift in the allocation of labor and capital resources from the agricultural sector that yields comparatively low productivity and revenue to the non-agricultural sector. The Japanese government has adopted certain policies to encourage the distribution of labor force to strategic sectors by nationalizing employment agencies and by developing a framework in which the agencies promote the recruitment of graduate students that encouraged young people from rural regions in mass migration to the cities in search of work after graduation. The structural basis for the key reallocation of the postwar labor market, especially the market for new graduates through institutional changes, was laid by this cooperative government-supported job-matching scheme. In addition, they further note that the reallocation of resources to indirect finance based on bank deposits and postal savings offered the financial foundations for accelerated economic growth by promoting the accumulation of savings and the effective distribution of capital.

It is also worth noting the implementation of numerous reform policies such as the land and labor reforms or disintegration of Japan's large family-controlled banking and industrial groups during the post-War period of the US occupation were not only responsible for the rapid economic growth but also democratizing and modernizing the nation (Beckley 2018, p. 2).

1.2. Japanese Model of Postwar Economic Growth: The Theory of State Capacity and its Implications in Japan

State capacity theory is a defining feature of every political system which was founded in the 1960s and developed over time (Almond & Powell, 1966). The state capacity theory mainly stresses the state's position on how to administer its territories, collect taxes, enforce law, order and deliver services (Evans, 1995; Sobek, 2010; Skocpol, 1985). The state plays an important role in establishing basic pillars for economic growth, such as stability, legislation, and infrastructure. Even though there are many scholars who contributed to this study, there is no single definition regarding the state capacity concept. However, the literature contains various definitions, which convey a similar meaning of this theory.

Recent literature argues that state capacity is essential to economic and financial growth as well as political stability (Robinson & Acemoglu, 2005). Scholars have emphasized the state's position in establishing and sustaining a market society and how states achieve collective objectives, rather than merely functioning as bodies of individual interests (Polanyi 1944; Evans 1989). (Wilensky 2002; Pierson 1996) have pointed out that states have developed welfare regimes both to promote economic growth and to protect people from the harshest effects of capitalist transformation. Pierre & Painter (2005) have claimed that state capacity focuses on state-society ties in order to get results by mobilizing social and economic assistance and approval from society for the achievement of public objectives.

In general, even though the explanation of state capacity varies from scholar to scholar, the role of the state capacity is referred to as the state's ability to achieve development. Japan is the perfect case in terms of state capacity and the state's role in economic growth since the Japanese government played an important role in encouraging economic growth by mobilizing human resources, skillfully using fiscal policies, guarantees, and subsidies under 'administrative guidance' whereas Collantes (2008) states that a strong state with a high capacity to intervene in the economy under the administrative guidance has been a key factor in Japan's success and economic development after the Second World War

since the state influenced the distribution of investment and therefore played an important role in the development of highly technologically-intensive industries capable of competing in international markets through a strict monitoring procedure. Furthermore, Kellman and Landau (1984) add that the Japanese government's assistance to businesses has consisted of incentives for research and development, creating joint development projects between competing firms within the sector, offering technical assistance and guidance on finance, technological innovation which fostered the highly efficient domestic competition for the nations comparative advantage. Therefore Johnson (1982) regards Japan as a traditional "state-led" economy.

1.3. Japanese Model of Postwar Economic Growth: the Japanese Developmental State After the World War II

Japan has experienced a dramatic increase and decline in terms of economic growth from 1945 onwards. Postwar Japan has established a different kind of capitalism which is based on state-guided capitalism which enabled various interventions in the economy by the state via its formal institutions than the American one as Chalmers Johnson states “nurturing the economy has been a major priority of the Japanese state because any other course of action implied dependency, poverty, and the possible breakdown of the social system” (Johnson, 1981, p. 307). Therefore, bureaucrats had privileges, authority, prestige, and a range of methods to impose their will. Public-private collaboration between bureaucracy and business is also one that has been generated and perfected over time by structural adaptation and reacted flexibly to evolving conditions (Cumings,1999). The Ministry of Finance, the Bank of Japan, and the Ministry of Foreign Trade and Industry have been the highest institutions in interfering with the economy of Japan. Hall (2001, pp. 110) states that The Coordinated Market Economy led by the state has contributed to the Japanese economic miracle by emphasizing the government's position in economic and industrial policies with the goal of the state is to boost the long-term national economy which entails a well-defined industrial policy under the strong and constant state involvement in economic activities in order to increase the international competitiveness of its domestic economies and the

industrial structure's export output has been seen as a required prerequisite for the achievement of certain developmental objectives, such as rapid growth, full employment, a high and equitable distribution of income and foreign exchange surplus to fund imports.

There are many studies on the state's role in Japan's economy, as the Japanese economic growth is strongly linked to the state and its actions. Many academics have expressed their views on the Japanese state as a key to Japan's economic development. One of the first scholars to carry out a detailed study on Japan's growth model was Chalmers Johnson, who was a specialist in this area, attempting to understand the characteristics and consequences of the Japanese development model after the Second World War in his book "MITI and the Japanese Miracle: The Growth of Industrial Policy, 1925-1975".

Johnson (1982, pp. 305-319) states that Japan is taken as the model of the 'developmental state'. The term was first introduced by Johnson regarding the state of Japan. The biggest difference from Western-style structures was that the state played a major role in the production and growth process. A developmental state describes a state which impacts the course and speed of economic growth by actively interfering in the process of economic development of the nation through its strong institutional capacity instead of relying on the uncoordinated power of market forces to distribute economic capital. In addition to referring to economic and human development, the developmental state defines the vital role of the state in harnessing national wealth and steering incentives to achieve the possible fastest growth through a distinctive policy-making mechanism. The developmental state is strongly associated with the private sector but maintains adequate distance where financial interests are conflicting with national growth for the renegotiation of priorities and policies. In the economic development of the nation, as a social partner of the private sector, the state has been a key body, and businesses react to the incentives and disincentives that the state offers. Bureaucrats working for the government are seen as vital to development because they have been responsible for designing and executing growth policies by taking initiatives. In other words, the developmental state's political structure divides reigning and ruling politicians govern and bureaucrats rule. Identifying and selecting industries to be funded, determining the best ways to feed these industries, and supervising them to ensure their effectiveness are

all essential responsibilities of this bureaucracy (Johnson 1982 p. 316). The pilot agency in the case of Japan, the Ministry of International Trade and Industry (MITI) is responsible for steering the direction of growth itself, implementing and developing a variety of policy resources to ensure that indigenous businesses are simultaneously fostered and handled in the broader national interest. Therefore, Johnson suggests that for more than 50 years, by practicing the 'administrative guidance' approach, the Japanese state has not only assumed responsibility for the safety and welfare of its citizens but also made economic growth her first priorities, and the important institutions such as MITI were the key factors of such growth as these institutions regulated the foreign investment transactions as well as the export and import of raw materials in order to achieve industrial policy objectives. In this approach, there is no need to give direct directives to the business community, the state operates as a 'regulatory' tool to compensate for the detrimental consequences of competition. Government signals for quick access to government subsidies, tax cuts, and approval of their foreign technology import proposals and the development of cooperative ventures are typically preferred to be followed. The Ministry of International Trade and Industry (MITI) has been authorized by the Japan Development Bank to receive investment loans, to distribute foreign currency for industrial purposes, to seek imports of new technologies and equipment, to provide tax incentives, and to regulate industry competition. MITI, which also functions as a think tank in a special role to enhance decision-making, was able to leverage its power of domestic savings to offer low-cost financing to specific industries (Evans 1989). The guidance has also been recognized as an effective soft instrument adopted by the state that has led to the phenomenal growth of the Japanese economy. He also assumes that almost all countries in East Asia represent unique types of state guidance that were first seen as successful in Japan.

Linda Weiss (2003) describes the developmental state as a political structure that promotes a common project of economic transformation, where elite consensus over key national priorities occurs, and where economic bureaucracies are given ample scope to take measures and function effectively. State capacity, or the ability to develop and execute growth strategies, is the secret to a successful developmental state. In order for a state to

accomplish such a result, it both needs a strong bureaucracy, and an effective partnership with the domestic business sector, which would ultimately be the focus of any fruitful growth initiatives. In order to characterize the optimal relationship between the developmental state and the business community, the term 'embedded autonomy' has been coined by Peter Evans (1995). According to Evans, embedded autonomy means that the state needs to be embedded into society and have social links that connect the state to society and provide institutionalized mechanisms for the consistent negotiation and renegotiation of fundamental priorities and policies for the effective participation of the state in industrial transformation. The Japanese Developmental State had almost the kind of embedded autonomy defined by Evans. Key bureaucratic agencies had both personnel and policy instruments to direct the development path, a task facilitated by the close relations of the bureaucracy with Japanese businesses thanks to the interactions between the state and big businesses in Japan which enabled precisely the kind of engagement, supervision, and input that Evans considered necessary for successful growth, but also when former public servants entered private sector companies after retirement, these relationships were further strengthened.

Skocpol (1979, p 101-02) indicates that in Japan, old practices initially favored the development of a powerful and well-prepared bureaucracy which is a dominant social community of bureaucrats with predictable and coherent goals that separated the administrative class from economic classes and provided a rigorous training and discipline mechanism that played a key role in the reforms of the Japanese state and economy since the action of bureaucrats is bound by the achievement of common interests rather than individual opportunities, allowing the state to function independently of such social stresses.

Investments rely on decisions taken by the state as the state provides incentives and disincentives for direct private investment; the performance of the business, in fact, strengthens the legitimacy of the state. There is a wide-ranging dialogue on 'developmentalism,' the need for industrialization, and state action to facilitate it. The parliament in Japan had significant importance in facilitating the interests and in legitimizing the bureaucracy's actions. It worked as a mediator between society and state, avoiding the neglect of relevant social problems by the bureaucracy. Johnson (1982, pp 209-210)

emphasizes that the Japanese political system's ability to legitimize the bureaucracy was a key success of the Japanese development state over authoritarian regimes that relied on high economic growth rates to acquire legitimacy because the legitimation derives from the state's accomplishments, not from the way the state came to power. Japan has been highly successful in enforcing her industrial policies by taking advantage of her effective bureaucracy and developmental institutions such as MITI. However, there are some scholars who claim otherwise or claim such a miracle did not take place and critic the developmental states.

Bailey et al. (2007) state that the causes for the "Japanese recession" are direct government interference and a unique-mercantilist industrial policy that weakens the competitive position of its internationally based companies. Whereas Otsubo(2007) states that Japan's strong state interference excessively favored main sectors and large corporations over small-scale enterprises and impeded economic growth. Charlotte (,2008) on the other critics the developmental state. She claims that the developmental state is heaven for big businesses in reality. The combination of lack of accountability, tight relations between the state, banks, political parties, and businesses, government-directed loans, high corporate debt-to-equity ratios, and national industrial policies towards the creation of internationally competitive industries could be vulnerable to moral hazards that encourage corruption and reckless business investment. Whereas (Schmiegelow M & Schmiegelow H., 1990) claim that although the Japanese government has been encouraging and has even done much to establish an atmosphere for development, its position has been overestimated. What happened to Japan's economy was not miraculous, but that Japan's economic success was largely attributed to the actions and initiatives of private individuals and businesses to respond to opportunities offered for commodities and labor in a reasonably free market. In other words, with the most impressive results, Japan has adopted Western models.

While a significant reconsider has taken place on the role of the bureaucracy and its capacity to direct continued growth in Japan (Sakaiya 1998), Japan's economic growth is linked to the existence of independence, meritocratic and strong bureaucracy, separated from

interest groups, rooted in society, and managing a wide variety of policy tools when the market is not sufficiently mature to effectively allocate capital and resources, the state has been able to resolve the weakness of the market by increasing its role in the economy and providing welfare to its citizens. Following the internationalization of the Japanese economy and the private sector's opposition to more bureaucratization of the Japanese economy, the Japanese State's developmental characteristics have turned out to be a far more regulatory state that relies more on rules and regulations than on development and outcomes. Therefore, these changes have enabled Japan to become the first capitalist nation, which has attained a high level of economic growth and rapid industrialization without sharing the cultural tradition of Western nations by relying heavily on creating capital-intensive, high technology, high value-added industries under the close guidance of the bureaucracy. The Japanese model was lauded not only for its international competitive capabilities but also for its success in sharing the benefits of rapid economic development in an equal and egalitarian manner among the participants in the system. The distributional efficiency of the system and the development of a middle-income society have been asserted, popularized, and also propagated by both the Western and Japanese scholars (i.e., Sakakibara et al.1997, Vogel, 1979) as an apparent indication of the dominance of the Japanese style of human-faced capitalism over its western counterparts.

1.4. Japanese Model of Postwar Economic Growth: The Role of Cultural Values: Confucianism Theory in Japan

Culture and its principles have given particular importance to Japanese society but the role of cultural values in economic growth has been divided among social scientists. Supporters of the cultural hypothesis such as Kahn (1979), Cheng(1980) favor the positive role of cultural values on the industrialization of Japan. The positive features of culture in economic development are outlined by Sen (1996 p:15) as follows:

"It is important to acknowledge the far-reaching instrumental functions of culture in development by helping us in our pursuit of valued objectives, but also to recognize that culture cannot be reduced to these functions. Culture also plays, for example, an intrinsic role in evaluating the process of economic development, as well as in making room for less immediate objectives such as sustaining the environment and preserving the diversity of species."

In addition, Cheng (1989) stresses that a society's economic growth must rely on the cooperation and cohesion created by ethical and moral principles that are important to the economic and social relationships underpinning personal and business relationships and exchanges. These scholars argue that Confucianism has contributed to the rapid economic growth of Japan because Japan shares Confucian ethics in seizing the virtues of austerity, hard work, submission to authority as well as the emphasis on the virtues of loyalty rather than benevolence. The positive thoughts of Confucianism vary from political meritocracy, which insists on high moral quality and elite ability to focus on social justice, family cohesion, and social harmony. These values have helped to build unity amidst government, society, businesses, and politicians in the process of identifying national priorities and how to achieve those goals. Confucian focus on schooling, industriousness, and thrift has driven the Japanese economy to spend strongly in the accumulation of human resources and significant savings when the government allows people to invest in stimulating domestic demand. The family and community engagement illustrates the collectivist nature of the Japanese economy and the deep support for the position of the state and society. Emphasis on family and group orientation has first paved the way for family-run businesses called *Zaibatsu* in the industrial era and their dissolution to group-oriented *Keiretsu* companies in the post-war period which contributed to the success of the Japanese economy to a great extent. The Japanese practice of self-sacrifice rooted in Confucianism remains the strongest Japanese philosophy even today highlighting "The quality of work reveals the human being's spiritual quality". Therefore, working is the ultimate goal of life and not merely a way to obtain money. Individuals must work hard for the greater good at the expense of their lives. Unlike individual goals and individual competition, group unity, trust, and loyalty of

individuals to the group norms based on reverence for hierarchical relationships are emphasized in Japanese businesses, hence the Japanese generally demand that all business deals take place between partners. If social virtues such as the promotion of collective values, the promotion of community effort, and the stimulation of non-individualistic behaviors were encouraged, contemporary Japanese industrial capitalism would be supported by its obligated employee-to-company relations with its subcontractors (Ozturk, 1999). According to Ito (1997), the overstress in the group orientation, however, created a homogeneous group-oriented workforce that does not encourage the ingenuity and special skills needed for scientific breakthroughs. The decisions are made collectively by groups. Any group has the means to take decisions in group's responsibility, only when the group cannot achieve a reasonably well-accepted decision by itself, can the group ask for the aid of a higher authority. This poses therefore significant problems in describing and interpreting the principle of statehood in Japan (Wolferen, 1989).

Morishima (1982) suggests that the materialistic aspect of Japanese Confucianism is quite different from that of its Chinese equivalent. He attributes the development of Japan to the Japanese version of Confucianism, which was based on intellectualism and rationalism, provided that Confucian ethics emphasize hard work, saving, respect for education, and reverence for the government as having a direct effect on Japanese economic success. "Loyalty to the state, trust in one's mates, and respect for one's elder are all characteristics of Japanese capitalism" he claims (Morishima 1982: 86). Furthermore, Yamamura argues (1997, 749) "The Japanese capitalism resembles Western capitalism only in external and superficial ways. It is grounded in the climate and spatial foundations of Japanese civilization and thus not influenced by Western individualism". In fact, one may clearly say that Japan is a convergence of East and West, a combination of harmonious tradition and modernity. Through learning Western culture, Japan's understanding of Western culture has not only allowed Japan to gain a strategic advantage in trading relations among Japan and Western nations but has also greatly improved Japan's cultural life.

On the other hand, due to a lack of explanatory capacity, the stress on the cultural perspective has been criticized and Confucianism has been viewed as a significant barrier to the modernization process by some foreign scholars. Weber (1958) and Krugman(1994) dismiss the argument that economic growth has been influenced positively by cultural influences stressing that Confucianism was an obstruction to the rise of industrial capitalism and social development. The key explanation for Weber's stance is that Confucianism, while world-confirming and Cosmo centric, fundamentally incorporate principles that prioritize social stability and the maintenance of the status quo, stresses the self-cultivation of morality rather than the development of knowledge (Cheng,1989).

Similar arguments come from Bao (1988) and Tu (1984), According to Bao, the Confucian value system had an adverse impact on modernization because the core principles of Confucianism, such as valuing justice over profit, did not encourage trade and according to Tu, Confucian respect for natural hierarchy and recognition of the importance of status in society has contributed to authoritarianism and male domination which are incompatible with modernization. Similarly, Johnson's (1982) questions regarding the importance of cultural values are largely over-generalized and he credits the economic success of Japan is due to institutional stability in the face of shifts in demand and comparative costs coordinated by MITI and a cooperative workforce; "Consensus and group solidarity have been important in Japan's economic growth. But they are less likely to derive from the basic values of the Japanese than from what Ruth Benedict once called Japan's "situational" motivations: Late development, lack of resources, the need to trade, the balance of payment constraints, and so forth. Positioning some " special capacity to cooperate " as an irreducible Japanese cultural trait leads inquiry away from the question of why Japanese cooperate when they do, and away from the probability that this cooperation can be, and on occasion has been, quite deliberately engineered by the government and others" (Johnson's, 1982, p: 8)

Confucian principles will both encourage and impede economic growth. In the case of Japan, its benefits appear to have overcome its drawbacks. Its philosophy of learning and moral values served as a trigger for the "take-off" process of modernization and economic

growth of Japan, in which the technical-skilled labor force and the comparatively harmonious labor-management relationship, as well as the egalitarian principles between various groups and the means of consensus-based decision-making encouraged by cultural factors that have contributed to a structure of bureaucratic leadership based on public-private harmony by avoiding or mitigating large-scale dropouts, helped Japan to become one of the world economic powers of the post-World War II period.



CHAPTER 2

THE HISTORICAL CONTEXT OF THE JAPANESE MIRACLE

2.1. Japan After the Second World War

Before the Second World War, unlike other Asian nations, Japan was one of the most powerful countries in the world in economic and military terms. The nation has already experienced economic growth and industrialization since the Meiji Restoration of 1868 which has contributed to the modernization and westernization of Japan through the importation of Western technologies and notions. Consequently, the nation implemented numerous policy and economic reforms. The aim of the restoration was to make Japan a great empire that can compete with other great empires in the world. As a result, Japan was able to form an empire by controlling areas such as Taiwan (1895), Manchuria (1931) Korea (1910), Indochina (1940), and other regions. By exploiting the natural resources of these regions, Japan could maintain its economic growth and empire until the Second World War.

At the end of the Second World War in 1945, Japan was one of the most affected countries and it was in a state of destruction with around three million casualties and nearly a quarter of the properties in Japan was destroyed. Japan lost her colonial territories, which had formerly supplied raw materials and had relatively limited access to the international market for the procurement of materials in particular, losses in shipping capacity have been crucial because her shipping capacity was able to sustain imports of raw materials and energy sources. The defeat of the Japanese empire would have many consequences in later years and ultimately leading the country to economic collapse. Ito (1992) states that Japan experienced the loss of 25 percent of its resources, commodities, and structures aftermath of the Second World War. (Pelegrín & Jensana, 2011: 52) state that in 1945, industrial production didn't reach 30 percent of the 1935 average and agrarian production had dropped by 60 percent. Government debt accounted for more than 200% of the countries' GNP. As the country's productive capacity in all its industries experienced a very large decrease along with the

dissolution of military forces, unemployment rose and hyperinflation erupted, generating a variety of uncertainties and disruptions. Japanese people were unable to fulfill their basic needs, leading many to starvation and despair.

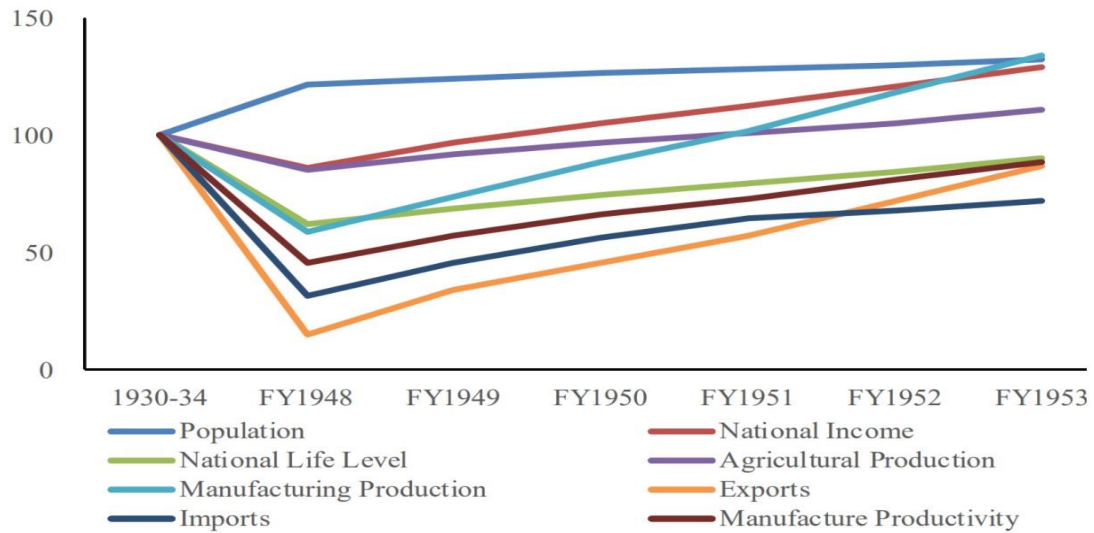
Table 2.1: The Loss of National Wealth Due to the Pacific War

(In millions of yen at end-of-war prices)

Type of Physical Asset	Before War	After War	Ratio of Destruction
Total assets	253,130	188,852	25.4%
Ships	9,125	1,796	80.3%
Industrial machinery	23,346	15,352	34.2%
Structures	90,435	68,215	24.6%
Industrial materials	32,953	25,089	23.9%
Household assets	46,427	36,869	20.6%
Communications and water supply	4,156	3,497	15.9%
Electricity and gas	14,933	13,313	10.8%
Railroad and road vehicles	15,415	13,892	9.9%

Source: Economic Stabilization Board, *A Comprehensive Report on the War Damage Caused by the Pacific War, 1949*

Figure 2.1: Postwar Economic Indicators (Unit: 1930-36= 100)



Source: Hayashi (1997)

As seen on the table and the figure above, we have encountered a devastated Japan after the war with its empire destroyed, all her economic activities and population decreased notably, the national income fell by about 15 percent and barely fulfill the basic needs of the Japanese society because of the shortages. While Japan was left with the waste and ruins of factories and facilities, Japan has managed to rebuild its economy from a new start by acquiring skills as well as knowledge from the U.S

Following the surrender of Japan on August 15, 1945, Japan lost her political independence, and The Allied powers took control of Japan in order to reconstruct its economy. However, the United States occupying forces that were called the Supreme Commander of the Allied Powers (SCAP) lead by General Douglas McArthur were the only ones who ruled Japan until

1952.(Ohno, 2006). This occupation was different from the one in Germany as there was already a Japanese government on duty and unlike Germany which was divided between allied powers, Japan was ruled only by the United States. The US authorities had practically absolute influence in Japanese economic and social policy decisions.

General McArthur has led a Japanese occupation with many objectives. These objectives were to democratize the political structure, demilitarization along with economic de-centralization which is the development of a completely capitalist model, putting an end to high inflation and the hegemony of large business companies called Zaibatsu, introducing a new agrarian reform as well as the legalization of trade unions in Japan (Takada,1999). Concerning the political reforms, the United States tried to foster democracy and hence establish Western-style institutions in order to make Japan a capitalist nation. In addition, MacArthur directed the creation of a new modern constitution, which prevented Japan from maintaining an army other than for self-defense. Under the new constitution, the emperor would have no authority in politics and the highest governing body would be the parliament of Japan which formed by the elected representatives of the Japanese people. Equal rights were granted to women and many new civil liberties such as freedom of speech were established through the constitution. Beyond all these reforms, Article 9 was designed in the new constitution to guarantee that Japan would not go to war again, and Article 9 has been written to ensure that. Article 9 provides.

"Aspiring sincerely to an international peace based on order, the Japanese people forever renounce war as a sovereign right of the nation and the threat or use of force as means of settling international disputes.

In order to accomplish the aim of the preceding paragraph, land, sea, and air forces, as well as other war potential, will never be maintained. The right of belligerency of the state will not be recognized." (Chapter II Renunciation of War, Constitution of Japan, 1946)

In addition to preventing the use of force as a way of resolving international disputes, Article 9 also aimed to prevent Japan from having an army, navy, or air force that would be

overseen by the allied forces. While this article restricted Japan from having its own military, it also allowed the country to reduce military expenditures and concentrate more on the process of re-development.

2.1.1. Breakup of Zaibatsu

When it comes to economic reforms, General McArthur aimed to put an end to the giant Japanese corporations called Zaibatsus to the further democratization of the economy and the emergence of competition.

Zaibatsus were the family-based, large financial and industrial corporations that were supported by the government through lower taxes and various financial aids. The hegemony of these corporations obstructed the creation of trade unions as well as hindered the establishment of independent companies and hampered the increase of Japan's middle class since they were more hierarchic and less democratic corporations. For the United States, Zaibatsus were regarded as the spirits of Japanese imperialism and militarism which prevented the democratization process. Hence, the Antitrust Act was passed in 1947 and the Fair-Trade Commission was created to ban all cartel activities and to compel companies with a business monopoly to decrease in size. The breakup of the zaibatsu was enforced by breaking up the holding companies, which were the center of the zaibatsu, and selling their stock to the public. Companies such as Mitsui Bussan and Mitsubishi Shoji, two traditional trading firms, were dissolved and stripped of their holdings in the stock market., the dissolution of Zaibatsus has been achieved with the aim of weakening Japan's military strength psychologically and institutionally (Minami,1986). Through the dissolution of the Zaibatsus, independent companies were formed, providing more flexibility for companies as well as allowing new companies to compete independently which led to greater economic competition.

In 1952, following the revision of the Antitrust Law concerning the abolition of monopoly restrictions, the keiretsu companies were formed. Unlike zaibatsu companies which were run by family members, the management of keiretsu companies was private

shareholders. In addition, business ties are much more competitive, more efficient, and less hierarchical, in keiretsu than those in Zaibatsu (Hadley,1970).

2.1.2. Labor Reform

The breakup of Zaibatsus and extreme working conditions in Japan with low salaries have paved the way to legalize trade unions. It was considered by the U.S that, trade unions were the key cores of a democratic nation and a capitalist system. Therefore, GHQ has announced the aim of establishing the fundamental rights of workers. By enacting the Trade Union Law in 1945 also the Labor Standards Law in 1947, provided for democratic processes in all union activities; maintained a committee on labor relations; forbid unfair job practices by employers. It also enabled workers to have the right to organize labor unions, strike and take part in collective bargaining. The improved working conditions and higher salaries obtained by the trade unions widened the domestic consumer markets and considerably affected economic growth. Through this reform, in an environment of the immense inflation and impoverishment of the entire population, as Kosai stated (1988, 498), the proportion of workers who were organized into labor unions rapidly increased in a short time from zero in 1945 to almost 60 percent in 1948-1949. Given that the world average was about 30 percent during that time, this is an exceptionally high rate(Ozaki,1966).

Table 2.2: Numbers of Trade Unions & Members, 1945-1947

	1945		1946		1947	
	August	After Sept.	First Half Y.	Second H. Y.	First H. Y.	Second H. Y.
Number of Trade Unions	0	855	9,506	4,892	6,708	5,962
Number of Union Members	0	602,706	2,816,470	864,032	1,209,392	790,655
Number of Union Members per Union	0	705	296	177	180	131

Source: The Labour Statistics & Investigation Bureau, Ministry of Labour, *Report on Labour Unions*

It can be considered that labor union reform was a success as it has caused a notable influence of collective bargaining on Japan's growth. The number of trade unions and union members experienced a dramatic increase in the postwar period. Therefore, the country

developed its productive structure by providing greater welfare for the Japanese society in the form of income. Although the Japanese economy based its economic growth on its lower salaries in order to make its products more competitive for export, thanks to the increase in productivity without compromising the competitiveness of the Japanese economy., the well-being of Japanese society has increased during that period.

2.1.3-Land Reform

The other important reform imposed by SCAP was agricultural land reform enacted in October 1946. It consisted of the Japanese government's mandatory purchase of land on lease by landlords and its resale to former tenants, rendering them owners of the land they cultivate in order to increase the productivity of the land. This reform has led to an increase in the population of land-owning farmers because in prewar Japan the land structure was defined by several feudal-state factors. Landlords who owned the land used to rent it to the farmers for benefits such as half of the crops the farmers grew. According to Kosai (1988:495,) before the land reform, 45.9 percent of Japan's farming was leased by landlords, but this figure hit around 90 percent at the beginning of 1950. Landlords were no longer regarded as being above the social status of farmers. By abolishing the class structure based on landholding, strengthening the rights of farmers, and making them more independent economically that resulted in the notable increase in agricultural productivity, agrarian reform is considered as one of the most successful agrarian land reforms ever carried out after the Second World War and it was a fundamental starting point in subsequent Japanese economic growth (Ōchi,1966).

2.1.4. Production Priority Policy (1947-48)

Based on the government-business collaboration, the Production Priority Policy is seen as a good example of an interventionist policy in the heavy and chemical industries.

The Production Priority Policy refers to economic planning of boosting the reconstruction by focusing on primary coal and steel industries which were the only available natural resources in Japan. In addition, these industries were promoted since they would lead

to rising in employment and export and thus contributing to foreign exchange reserves. The economic decline in industrial output after World War 2 was so extreme in Japan. During this period, the mining and manufacturing industries' output index was about 20-30 percent of the pre-war era as seen in Figure 2.2. In order to reduce the enormous inflation and rebuild the economy by boosting coal and steel production, the Japanese government adopted a "Priority Production Policy" in 1947 and 1948. The coal and steel industries were prioritized under this scheme since they were the scarcest resources. The Japanese government formed the Reconstruction Finance Bank in January 1947 to support this policy through funding long-term loans to private businesses and encourage them to regain the level of production of coal and steel. In addition, the government interfered directly with the sector through price restrictions combined with subsidies, and the distribution of limited imported goods. 80 percent of government investment loans were used by the two sectors, as well as price supports that accounted for 24 percent of government fiscal expenditure. As a result of the increase in the production capacity of the coal and steel industries, this priority policy helped to overcome the lack of production potential and promoted the recovery of the economy by providing a solid preparation for heavy and chemical industrialization at the next level (Nishijima,2014).

Figure 2.2: Production Indices (1934-36=100)



Source: Ministry of Finance ed., *Showa Zaiseishi :Shusen kara Kowa made*

(Financial History of Showa: From the End of World War II to the Peace), vol.19, Toyo Keizai Shinposha , 1978.

As seen on the figure above, coal production has recovered to 81.6 percent of the pre-war level, whereas the steel industry production has recovered more than 80 percent of the pre-war level (Elbaum, 2007).

Improving the supply and demand situation of raw materials through the implementation of the priority production policy has led to an increase in production and consumption and thus to the establishment of raw material industries that contribute to Japan's economic recovery.

2.1.5. Inflation and the Dodge Plan in 1949

After World War 2 ended, Japan started to experience shortages and a drastic rise in unemployment levels. Shortages were extremely high as food became ever scarce, many people were afraid of starving to death and living conditions were the lowest in 1946 and unemployment started to rise since veterans returned from war fronts and ex-colonies. In addition, retail prices were rising quite sharply, in part due to supply and demand imbalances. The excess demand has caused the emergence of large numbers of black markets. However, due to the severe shortages, prices on the black market have become extraordinarily high compared with the official prices and only in the early 1950s did the price gap vanish. (Uchino, 1978, p.26,) states that the prices of sugar and soap were more than 200 times higher than the official prices, while rice and eggs were about 150 percent higher on the black market. Japanese people were forced to sell their personal belongings in exchange for food and basic necessities in order to sustain their lives.

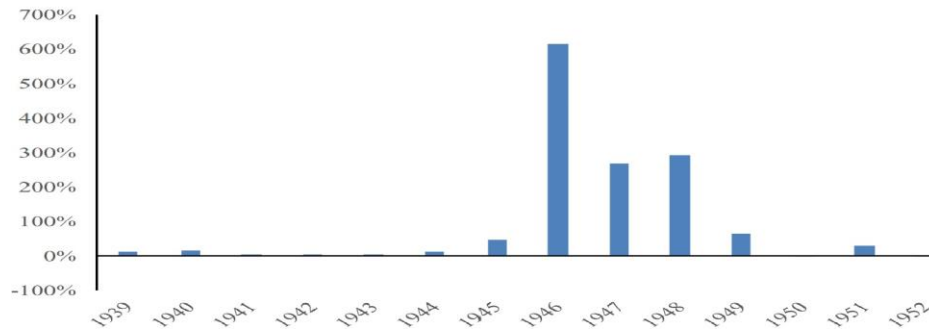
Table 2.3: Multiple Ratio of Black Market Prices to Official Prices in October 1945

Items	Ratio
White Rice	132
Bean Paste	20
Soy Sauce	45
Alcohol	44
Cotton Thread	73
Cigarette	37
Vegetable Oil	75
Radish	50
Tyre for Rear-car	8
Electric Light Bulb	17

Source: Asahi Shimbun, October 28, 1945

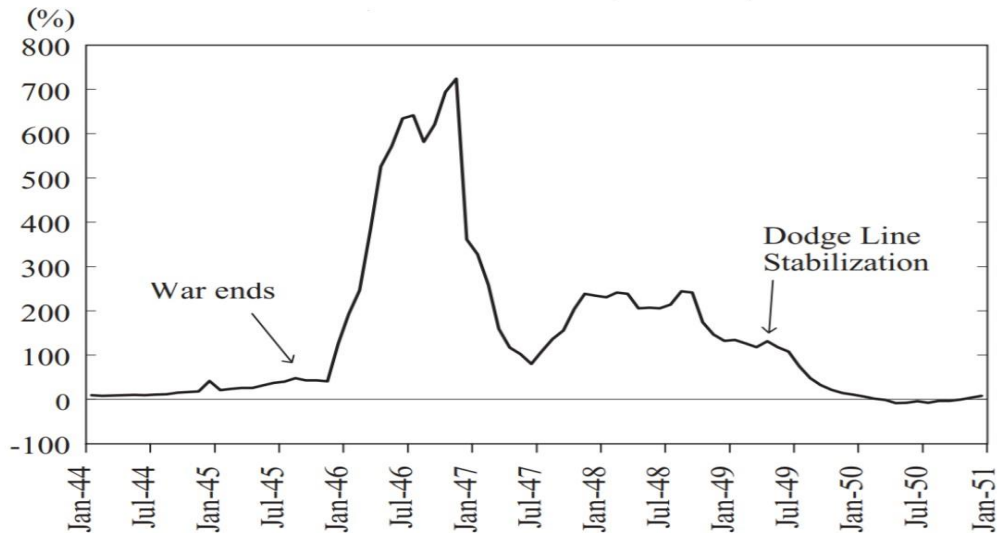
At the end of 1945, the typical black-market price of consumer goods was more than 50 times higher than the official price in average. Owing to the serious scarcity of food and basic needs after the war, black market rates have been incredibly high relative to official prices.

Figure 2.3: Postwar Inflation in Japan (Tokyo Retail Price Index)



Source: Hoshino (2003) pp.16-17

Figure 2.4: Retail Price Inflation in Tokyo
(Official prices , change over 12 months)



Source: Management and Coordination Agency, Historical Statistics of Japan, Vol. 4, 1988.

As seen in the figure and table above, the inflation problem caused by excess demand and supply shortages was evident. In order to deal with this situation, The Bank of Japan has printed money to finance subsidies while the government-enforced price controls on goods.

This excess supply of money resulted in extraordinary inflation and induced excessive demand indirectly. Controls have become inefficient due to the emergence of large numbers of black markets. The monetization of fiscal deficits produced triple-digit inflation between 1946 and 1949. This was Japan's highest inflation ever (Ohno,2006). The hyper-inflation caused by the government debt monetization has been one of the biggest problems the SCAP needed to handle.

Economic planning lasted until 1949 in order to cope with the inflation problem and to stabilize the Japanese economy. SCAP has regulated all foreign trades also limited the international trade volume. The US provided Japan with substantial quantities of humanitarian and economic assistance, apart from regulated trade, amounting to a total \$1.95 billion between 1946-50, which helped to relieve the shortages of food and consumer

goods(Ohno,2006). Nevertheless, these supports were not enough to revive the Japanese economy.

Due to the important role, he played in the western occupation zones of Germany which paved way the for German economic growth, The US government sent Joseph M. Dodge, president of the Detroit Bank to Japan along with tax expert economist Carl Shoup in 1949 to speed up Japan's economic recovery and also provide guidance on the economy of Japan. While Shoup introduced a new taxation system in the Japanese economy on the basis of direct taxation, such as income and company taxes, Dodge has adopted four specific policies known as Dodge Line aimed primarily at resolving the severe inflation problem and ensuring Japanese stabilization.

These policies were:

- 1) Cancellation of subsidies and loans granted by the Japanese government,
- 2) Creation of a Balanced Budget to reduce inflation,
- 3) Reinforcing a new taxation system, stabilizing wages, and cutting expenses.
- 4) Setting the value of the yen to 360 per 1 US dollar fixed exchange rate in order to maintain the Japanese export prices low.

The Dodge Plan started to bear fruits in a short period of time since it led to price stability by the regulation of prices and the reduction of subsidies in a highly intervened economy. The household savings rate and the investment rate have risen during this time meanwhile, the surplus budget policies have calmed both black market and free-market prices. As a result, inflation which was three digits in the years of the post-war era was steadily decreased to two percent in 1952(Hamada & Kasuya,1984). Achieving price stability under the Dodge Plan has eventually led to the abolition of price controls gradually which enabled Japanese companies to compete with foreign counterparts, increase in productivity, and enabled Japan to return to a free, deregulated economy. Exports grew dramatically during

the first half of 1949 under the fixed exchange rate and nearly doubled at the end of the year. However, the Japanese economy has experienced extreme deflation due to a lack of internal demand and the abrupt measures plunged the economic activities, making the unemployment rise which later caused a short recession in Japan.

2.1.6. The Effects of the Korean War (1950-53)

The Korean War (1950-1953) can be seen as a turning point for the Japanese economy in the post-war era since the nation shifted from economic recession to economic recovery with high speed. The war began in June 1950 with the invasion of North Korean forces backed by the Soviet Union to South Korea. As a response, the president of the U.S at that time Harry S. Truman commanded the U.S. troops led by General Douglas MacArthur to intervene in the Korean conflict to halt the expansion of communism.

When the Korean War broke out in June 1950, Japan's economic situation started to show positive changes which later saved the Japanese economy from the serious stagnation of the Dodge Plan as The Korean War boom has led to a rapid rise in demand in the economy and marked the beginning of the economic miracle. For the United States-led United Nations forces deployed on the Korean peninsula, Japan was a staging point and strategic base of support for the troops of the United States and the United Nations. Japan found itself in a strong position to attract a large amount of foreign exchange inflow as the U.S. purchased Japanese goods and services. Since the start of the war, Japan has devoted itself to meeting all the needs of the United Nations especially in terms of alimentation (which Japan at that time had a certain competitive advantage), but industrial production was fundamentally stimulated as well. In order to stop the North Korean invasion of South Korea, The United States forces used Japan as a logistics base and obtained vast quantities of military and civilian goods from Japanese firms such as ammunition, trucks, uniforms, consumer goods. From 1950 until 1951, world trade has increased by around 35% percent which favored Japan's development most. Rise in Japanese international trade accompanied by global

demand, the exports of Japan increased by almost 70 percent and Japan received a temporary dollar revenue of 60 to 70 percent of her exports from the U.S. military which led to an economic boom and putting an end to the recession (Nakamura,1995). The Japanese economy thus witnessed a series of booms following the direct impact of war procurement demand in 1951 which led to the consumption boom in 1952 and investment boom in 1953 after the Korean war is over(Hamada,1992). It was also particularly important for Japan's growth that the large inflow of foreign currency allowed Japan to finance the entry of machinery, among other things, which favored productivity increases at both agricultural and industrial levels. Many companies' balance of payments improved, funding sources became abundant and profits also rose(Kosai,1986). Whereas Tsuru assesses the effects of the Korean War as follows:

“The rush orders for large quantities of all kinds of Japanese goods by the U.S military which were called as special procurements were expanded to cover a wide field of economic activities as the Korean conflict became more intense. By the time the cease-fire agreement was signed in 1953, the special procurements amounted to a total of 970 million dollars. This category of extraordinary dollar receipts for Japan lingered on until 1955, by which time the aggregate amount was estimated to have reached 3.56 billion dollars. (Tsuru, 1993, p.60).

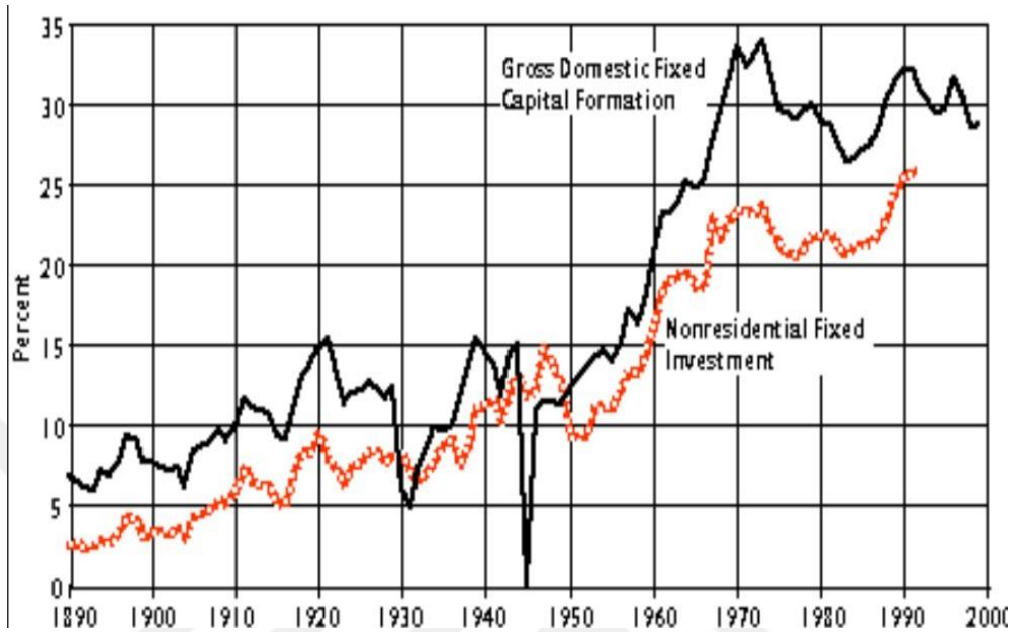
The Dodge Plan's radical stabilization policy following the Korean War procurement boom has allowed the Japanese economy to complete its rebuilding process. Maintaining price stability and abolishing price regulation and subsidies eventually allowed Japan to return to a freer economy. Other than the monetary income from the exports, US monetary aid, which was used to rebuild the country and lasted until 1951, played a crucial role in the structural change from an agrarian economy to an industrial economy of Japan during this period. This, along with economic reforms, has provided an initial boost to the Japanese economy, in which the country would undergo rapid growth for the next half a century with averaging growth of around 10 percent in the '50s and around 13 percent in the early '60s(Yoshikawa 1999). Once the complete recovery and stabilization of Japan have been clearly realized entirely after the end of the Korean War thanks to the rapid rise in production and economy as a whole, The Treaty of San Francisco was signed on September 8, 1951, but entered into

force on April 28, 1952, formally putting an end to Japan's American-led Allied occupation, thereby restoring Japan's full sovereignty(Llamas,2014).In 1952, Japan was a sovereign nation, with a high demand for Japanese products, particularly from the United States, which led to the influx of dollars that supported the Japanese structural transition from a mainly agrarian economy to the initiation of industrial growth.

2.1.7. The Economic Miracle Period

What is commonly known in the literature that the Japanese economic miracle relates to Japan's rapid post-war growth following the recovery period of 1945-1949 and the Korean War in 1950 until the 1973 oil crisis with growth rates averaging 9.3 percent between 1946 and 1973 and reaching 11 percent in the 1960s. Since the early 1950s, the heavy industrialization policy of the Japanese government has been a fundamental factor in the rapid economic growth following the resumption of the basic raw materials industries along with implementing new techniques and adoption of new technologies from abroad. Japan's Gross National Product level exceeded the prewar levels in this period. This fast growth has transformed the Japanese economy and Japanese society as well. In 1953 the income per capita had already surpassed its pre-war level because of the increases in industrial production. Japan has become the second greatest economy in terms of (GNP) surpassing West Germany by the 1970s (Ohno,2006). The considerable rise in the Japan's GNP have attracted foreign investments. As the GNP increases so does the ratio of foreign investments.

Figure 2.5: Ratio of Investment to GNP in Japan ,1890-1999



Sources: Nonresidential fixed investment: Angus Maddison, “Standardized Estimates of Fixed Capital Stock: A Six-Country Comparison “in Explaining the Economic Performance of Nations(Brookfield, Vermont: Edward Elgar Publishing Co. 1995). Gross domestic fixed capital investment: Management and Coordination Agency, Statistics Bureau, Historical Statistics of Japan on CD-ROM (Tokyo: Japan Statistical Association, 1999)

Japan also benefited from the international perspective in various respects during this period. On the one hand, the beginning of the Cold War resulted in the United States’ taking advantage of the industrial potential of Japan to improve its military position against the Soviet Union. In this way, the goal of the United States is to make Japan the industrial hub of Asia. On the other hand, the US promoted the transition of technologies to Japan, acknowledged the undervaluation of the yen, opened its market to industrial exports from Japan, and permitted a Japanese government security program of the national firms against the foreign businesses. (Collantes, 2008). The country has experienced high increases in industrial productions as the Asian nation was appealing for the low prices as a result of low wages. However, along with the increased demand for Japanese products during this time, Japan experienced a price boom especially in raw materials such as coal and steel which ultimately caused exports to decline as Japanese products became less competitive in the

market. As the high prices reduced the competitiveness drastically, the Japanese government started to take fiscal measures to deal with the lack of competitiveness and overvaluation.

Gorika which means rationalization policy has been adopted by the Japanese government in order to reach international competitiveness in various industries such as coal, steel, electrical, and petrochemical in the 1950s. This policy has favored productivity improvement by investing not only in new technologies and equipment but also in management and development reforms to “catch-up” international level as these industries especially the coal and steel industries had a problem with their outdated production equipment, which would reduce efficiency and competitiveness. Furthermore, in this era, several sectors were targeted for "set-up" (establishing new industries), including the automotive, heavy electrical equipment, and computer industries which were seen as “emerging industries” with high growth and high return prospects that required government policy coordination (Nishijima, 2014). Thanks to the Korean War, many Japanese firms have experienced a boom in US military procurement and added up gains. These revenues were the key source of financing for the implementation of new technologies and equipment.

The Japanese government introduced several measures to realize the rationalization policy. These measures were special tax provisions, accelerated depreciation of the asset, the tax exemption for imported machinery and technologies from foreign countries, and subsidies aimed at lowering inflation to zero level and promoting companies to minimize the costs. To finance these measures The Fiscal Investment and Loan Program (FILP-Zaisei Touyushi) was introduced which is the collection of funds by government financial agencies from the postal and social security savings and then investing and loaning public funds to the industrial sector in order to promote key industries such as mining, shipping, and steel. These steps showed some positive effects. However, not all industries were able to manage the *Gorika*. Steel industries performed better and increased their productivity but the coal industry struggled and leading to the disappearance because of the rapid change of the world's energy supply from coal to cheaper one, oil (Ohno,2006).

The year 1955 is considered to be the historic year in the history of the Japanese economy. It was the beginning of strong economic growth. In this year Japan experienced a growth rate of more than 10% with a surplus in the balance of payments along with price stability. The Japanese economy had grown significantly during this time and exceeded pre-war averages in both GNP and living standards (Sadahiro,1991). It took 12 years for the Japanese economy to recover its pre-war levels. During this period, Japan underwent a structural transformation in production that contributed to increases in the value of her industrial productions (Llamas,2014). Labor unions have been formed on an enterprise basis and industrial relations have strengthened. A new wage bargaining system called "Shunto" (Spring Offensives) began in 1955 which enabled labor unions and employers to negotiate the wages once a year. Under this system, wage rate increase has been calculated by looking at the increases of consumer and producer price indexes (Hamada & Kurosaka,1984). On the 23rd of December 1955, the Japanese government launched the first national economic plan called the Five-Year Plan for Economic Self-Support. This plan used to aim at achieving a self-sustained economy without U.S aid and special procurement caused by the Korean War along with improving the conditions of employees. This plan has stressed fiscal and monetary policies as the key tools of long-term economic planning, rather than direct government control. Implementing this plan has caused a high growth in the Japanese economy since the real national income growth rate rose to 13.9 percent and was well above the projected 6.5 percent of GDP growth (EPA 1972, p.106).

In 1956-57, Japan experienced another boom which is called as Jimmy Boom named after Japan's first Emperor as it was the first genuinely widespread development in the history of Japan (JILPT,2016). There was a profound transformation in the structure of the economy. The proportional share of agriculture, forestry, and fisheries decreased steadily, although manufacturing and construction grew dramatically. Both government and businesses plan very carefully and deliberately to manufacture products with high global demand and to achieve market competitiveness by effective production. During this period, by developing a consumer-oriented economy focusing on high-quality productions, Japan had gone from having little international trade, primarily with the United States, to worldwide

which surpassed the pre-war period as the increased value especially in consumer goods attracted global demand. There have also been technological developments in both the agriculture and manufacturing industries and the speed of development has been increased by international technology imports (Goto, 1991). Both the Japanese people's ability to adapt the skills and knowledge gained mostly from the U.S and Japan's technology imports combined with domestic innovation have made a major contribution to Japan's economic development, as technological developments in one industry have driven many other industries' growth leading to more diversified and sophisticated manufacturing output. Production in a variety of areas, including calculators, sewing machines, optics, shipbuilding, or cameras marked the first beginning of technological progress in Japanese manufacturing that led to increasing private investments (Takada,1999). The automotive and naval industry began to grow at the beginning of the 1960s and would become the world leader in automobile manufacturing, shipbuilding, and precision optical instruments in subsequent years. Japanese industry experienced such a high growth during this time after the Second World War, considering the productive investments made with the entry of foreign exchanges, resulting in high demand from all over the world, particularly the United States. The nation started to use its own technologies rather than importing from outside. With the inflow of foreign exchange together with having a trade surplus, Japan improved its own innovations enabling the Japanese products to compete on foreign markets even though there were still several years left for the country to be a technology exporter and not an importer(Llamas,2014).

2.1.8. The impact of Recession on the way to High Growth Era (1957-62)

In 1958, there had been a global recession known as the Eisenhower Recession in world trade which lasted around 8 months. It caused an economic downturn in post-WWII history by 10% surpassing the Great Depression (Gable,1959 pp. 557). During this period the price index of goods increased in Japan that caused the exportation to halt with the other countries, especially the U.S. The downturn in exports has led to a decrease in foreign exchange reserves. With Japan's increasing demand for imports, the balance of payments

deteriorated dramatically. The Japanese government announced another economic plan called The New Long-Range Economic Plan to boost people’s living standards and employment levels by maintaining a high rate of economic growth as well as price stability. Therefore, the Bank of Japan introduced a new restrictive monetary policy in order to lower the prices and stabilize the balance of payment. As a result, a year later in 1958, the economic growth resumed. The trade volume has surpassed the prewar levels given that Japan had a high trade volume with its former colonies and subsequently in 1960 industrial production doubled. On the other hand, in 1961, the Japanese government initiated another economic plan, The National Income Doubling Plan to attain the objective of doubling economic growth in 10 years. Consequently, The National Income Doubling Plan aimed to maximize growth by targeting growth rates for the first three years of the Plan were set at 9 percent and for the remaining seven years at 7.2 percent and under this Plan, the targeted GNP rate was to be accomplished in only three years, not the expected five years (Takeda,2014). By improving prosperity, adjusting the balance of payments, and increasing private investment, the preconditions for the remarkably high growth period of the 1960s were gradually created (Kosai, 1986).

Table 2.4: Yearly Total Value of Exports and Imports Fixed base (Unit: 1000 YEN)

Calendar year	Export	Import
1950	298, 021, 052	348, 195, 583
1951	488, 776, 775	737, 241, 298
1952	458, 243, 197	730, 351, 682
1953	458, 943, 408	867, 469, 443
1954	586, 525, 032	863, 785, 437
1955	723, 815, 976	889, 714, 970
1956	900, 229, 011	1, 162, 704, 360
1957	1, 028, 886, 636	1, 542, 090, 900
1958	1, 035, 561, 686	1, 091, 924, 896
1959	1, 244, 337, 203	1, 295, 816, 732
1960	1, 459, 633, 161	1, 616, 807, 363

Source: Ministry of Finance: Trade Statistics of Japan

https://www.customs.go.jp/toukei/suii/html/nenbet_e.htm

Japan's economic development has been driven by a rise in exports and imports. The more the nation imports the more it exports.

2.1.9. High Growth Era (1961-72)

The years from 1961 to 1972 were the years of the highest growth rate in Japan with around 12 percent in real terms which is known as the period of double-digit growth symbolized by then-Prime Minister Ikeda. On the other hand, Japan's growth rate in the 1960s was on average significantly greater than that of the large western countries. The volume of trade and industrial production was five times higher than in the pre-war period (Llamas,2014). Better distribution of resources and labor force from low productivity sectors such as agriculture or fishing to the higher productivity sectors such as manufacturing has made a significant contribution to the growth.

During the high growth period, the main factor of Japan's growth was not only the export-led growth but also the high home demand-led growth because of the development of domestic markets and the rise in wages that started to increase consumption. In 1961, the national income per capita was \$400, just twenty percent less than Italy's (Sakisaka,1963). In fact, Japan's reliance on exports and imports as a proportion of GDP was consistently smaller than that of other developing countries, which accounted for about 11% and 10% of her GDP respectively whereas European figures were around 21 and 20 percent. At the end of the 1960s, Japan's exports accounted for just 9.6 percent of GDP, compared to 19.7 percent in Canada from 1953 to 1972(Johnson, 1982). The rapid growth period was also reflected by the Japanese economy's swift structural transition. The accumulation of foreign investment in technology and heavy industries was one of the most important components of the development due to increased knowledge and management in these industries. After WW2, Japanese goods were cheap because of the low labor costs which was the main attraction, especially for the U.S. However, in the 1960s, Japan's trade liberalization process increased

the competitiveness of domestic industries and enabled manufacturers to focus their efforts on improving production through extensive technological innovation. As a result, the quality and the prices of the Japanese products improved drastically that led to the higher wages of the Japanese workers as the country underwent rapid growth. The importance of wage increases had significant effects on the Japanese economy. On the one hand, it has increased domestic consumption mainly for durable consumer goods leading to higher demand as well as boosting economic growth. On the other hand, it has contributed to price stability ensuring that no deflation or high inflation is triggered by wage increases.

As Japan grew economically, it gradually became part of the international economic system and realized the need to become a member of OECD and GATT. Japan was expected to liberalize its international trade and capital market through a liberalization agenda to achieve this. Therefore, The Liberalization of the Capital Market (FDI) started in 1967 and the industrial policy has mainly focused on the liberalization of capital and trade of productions following the lifted restrictions of many goods such as buses, trucks, and computers in this period. These liberalization incentives helped entrepreneurs and companies to be prepared and take part in international competition. Since Japan joined these international organizations, Japan was able to make good use of the membership advantages, such as convenient access to global markets, both as an export market and as a foreign investment market. The Japanese government's projections for the period 1967-71 could not expect massive Japanese growth in a period that was deemed to decline due to wage rises and to achieve maturity in its economy. Although the government planned to surpass 8% of GDP growth in those years, it surpassed an average of 12% in fact. The productivity growth witnessed by the Japanese economy has continued to increase which led to the export of Japanese goods favored by the international community (Llamas,2014).

2.1.10. The Period of Economic Slowdown and Oil Crisis (1973-82)

While Japan was able to experience growth since the 1950s, Japan's high growth era reached its peak in the early 1970s. During this period, Japan has been a giant economy with

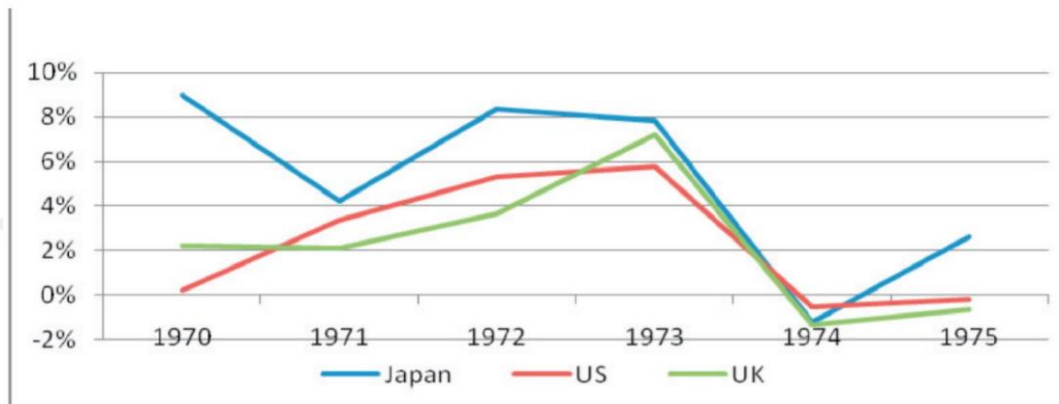
its Gross National Product was around 200 billion dollars, catching up with the European and US economies that resulted in the entrance of Japan into the mass consumption society (Sadahiro,1991). However, subsequently, Japan has faced a few challenges that have stalled economic growth both within and outside the country. The domestic challenges were the limited natural resources that affected the export of the heavy manufacturing sector, the severity of the shortage of labor due to the decreasing birth rate and the agricultural sector's shrinkage, Japan's external surplus, and the appreciation of the yen. The external challenge was the rise in oil prices almost quadrupled from \$2 to \$11 per barrel as a result of the Yom Kippur War in 1973 between Israel and Arab countries. The price of crude oil per barrel has long been low and stable after the WW2 era. However, oil-producing Arab countries have initiated an embargo on Western countries that supported Israel and have limited their oil production. In 1979-80 the price was raised again to around \$30 per barrel as a result of the Iranian Revolution and following the Iran-Iraq War.

The unexpected rise would have serious consequences not just for the Japanese economy but for the whole world because increases in oil prices are normally assumed to raise inflation and minimize economic growth. Japan, in particular, is not an oil-producing country because of the characteristics of its territories and instead relied entirely on the outside for its usage. Japan's oil dependency was around 99.7 percent while the OECD countries were around 67 percent during that time (Ohno,2006). During the past eras, this dependency was not a worry as the price of oil was cheap but when the Arab states of OPEC decided to increase the prices, Japan was completely affected. Since oil had become the main source of energy in many industries, such increases caused not only a decline in the supply of goods, especially petroleum products such as toilet paper and soap but also a sharp rise in the costs and consumer prices. Japanese firms have had to raise the prices to cover the expenses which ultimately leads to increased inflation and erosion of Japan's competitive edge contributing to the deceleration in economic growth.

Ito (1992) states that for Japan, this oil crisis led to a decrease in the growth rate to the middle of the previous stage and Japan's economy has faced inflation, unemployment,

and external deficit difficulties. In the 1970s and 80s, the annual growth rate dropped to an average of about 4 percent.

Figure 2.6: Japanese Economic Growth versus US and UK (1970-1975)



Source: http://www.esri.cao.go.jp/en/sna/data/kakuhou/files/1998/12annual_report_e.html, last use: 26.07.2012, (Johnston & Williamson 2011) <http://www.stat.go.jp/english/data/chouki/03.html>

As seen on the figure above, Japan's growth rate was higher than the Western pioneers until the oil embargo of 1974 when its growth rate recorded in negative terms for the first time during the post-war era.

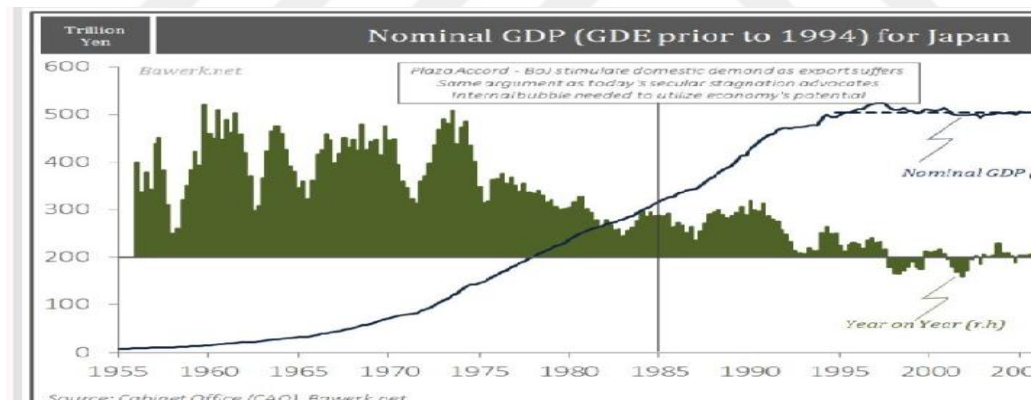
In order to cope with the inflation and recession, the Japanese government has taken interventionist steps to increase social spending and promote rationalism for energy-intensive sectors with the intention of minimizing energy import dependency by focusing more on diversification of the energy such as renewable and geothermal energy (Ohno, 2006). The Bank of Japan has increasingly tightened monetary policy to curb inflation; the Japanese government eventually shifted into knowledge-intensive industries owing to the high-power consumption of heavy industries and The private sector transformation from energy-intensive to one with energy-saving manufacturing technology has been improved and strengthened. This transition caused a sharp decline in the investment volume of heavy industries such as steel and petroleum products whereas a sharp increase in microelectronics and automation (Sun, 2006). The intervention of the government enabled the second oil shock

to have a slight impact on the economy of Japan and the boom in exports of vehicles and electronics which increased faster than imports, was the key to the recovery. The economic growth continued to increase around 6 percent annually though not at rates as high as in the postwar period.

2.2. Has the Japanese Miracle Truly Occurred?

Before analyzing the various factors that have contributed to the Japanese economic development in the twentieth century, we need to verify whether such a miracle existed or not. In order to assume that the so-called miracle occurred, we need to analyze the Gross Domestic Product increases (Figure 2.7) during this century.

Figure 2.7: Gross Domestic Product of Japan



Source: Cabinet Office (CAO), Bawerk.net,

<https://snbchf.com/2016/08/bawerk-secular-stagnation-redux/japan-gdp-1955-present-jpg>

As we can see above on the chart, there is a gradual increase over time in GDP. When we look at Figure 2.8 below that shows the growth rate of the Gross Domestic Product, we can clearly see the disproportionately rising economic growth until the end of oil embargo in 1974.

Figure 2.8: GDP Growth of Japan (Annual %) 1960-1975

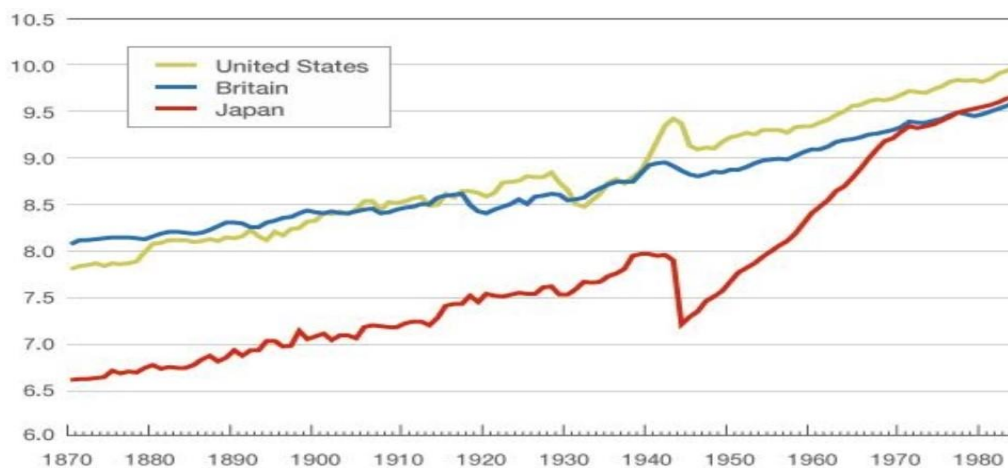


Source: Worldbank

<https://data.worldbank.org/indicator/NY.GDP.MKTP.KD.ZG?end=2019&locations=JP&start=1961&view=chart>

Another way of understanding Japan's economic miracle would be to look at the per capita gross domestic product (GDP), which is a country's economic output measure that correlates to the number of people, because the output itself tells us little about whether or not the Japanese people's quality of life has improved.

Figure 2.9: Growth in Real Per Capita GDP in Japan Britain, and the US, 1870-1980
(Natural log of per capita GDP in 1990 international Geary-Khamis dollars).



Source: The Maddison-Project

(<https://www.ggd.net/maddison/maddison-project/home.htm>, 2013 version).

By 1956, as the chart above shows, GDP per capita had surpassed the pre-war level in 1940 while the Japanese population had grown over this time, Japanese production had grown to an even greater extent. Japan started to close the gap with Western Countries at a pace far greater than its prewar progress. Besides the GDP per capita has kept on rising every year even though there had been economic crises in the 1970s which only slowed down the growth.

In order to compare the Japanese economic miracle with the top developed countries we need to look at the data provided below to compare this development (Table 2-5).

Table 2.5: Annual Comparative Rates of Gross National Product from 1950 to 1968

	1950-1960	1960-1968
Japan	9,5	10,3
United Kingdom	2,7	3,0*
United States	2,9	5,0*
West Germany	7,6	4,3*
France	4,3	5,5*

Source: Japan's Economic Policy, Allen, G(1980: 279)

The data we observe in the first column is the Gross National Product of the countries. In the second column, though, only Japan's GNP data, whereas other countries have Gross Domestic Product data. IMF describes the difference between Gross National Product and Gross Domestic Product as GNP calculates the value of goods and services produced by residents of only one country, both domestically and overseas while GDP measures the value of goods and services generated both by citizens and non-citizens within the boundaries of a country. We can thus see from the data that the two fastest-growing countries were Japan and West Germany in the 1950s. West Germany, however, would not be able to keep the growth rate as high as the United States and France, only surpassing the United Kingdom in

the 1960s. Japan, on the other hand, increased more its growth and exceeded the double digits.

We can also analyze whether there has been a change from the primary and secondary sectors to the service sector that has been called tertiary in the Japanese economy over the years. According to Allan Fisher and Colin Clark, supporters of the three-sector model, in economics, the three-sector model splits economies into three fields of activity: raw material production which is primary, manufacturing is secondary, and services is tertiary. The key emphasis of an economic activity moves from the primary, through the secondary and eventually to the tertiary market, according to the model. Therefore, underdeveloped countries are mainly focused on the primary sectors which include agriculture, forestry, etc. whereas developing countries are focused on the secondary sectors which include manufacturing, and the developed countries are mostly focused on the tertiary sector” (Fisher, 1939; Clark 1940).

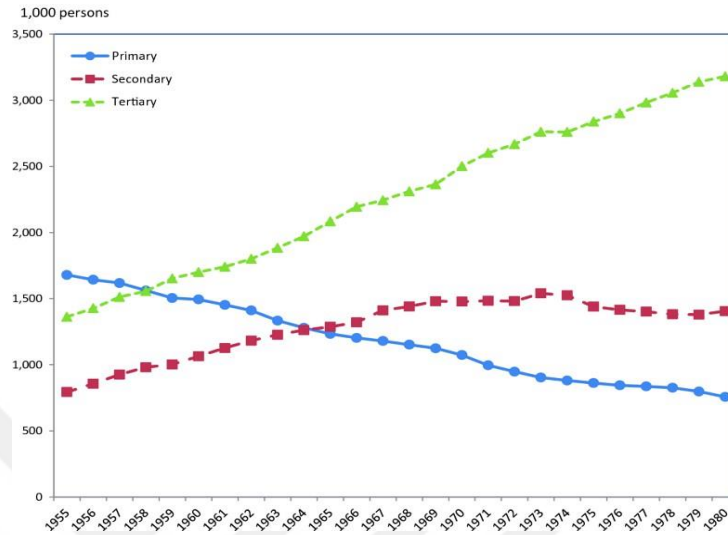
Table 2.6: Distribution of Workforce in Japan

Year	Total Employment	Primary Sector (%)	Secondary Sector (%)	Tertiary Sector (%)
1930	29.649	49,7	20,3	29,8
1950	36.025	48,5	21,8	29,6
1960	43.961	32,6	29,2	38,2
1970	52.468	19,4	33,9	46,7
1975	53.140	13,9	34,1	51,7

Source: Komiya, Okuno and Suzumura Japan’s Industrial Policy (1988:51)

Here the table illustrates that as Japan grew and started to be a more developed country, its workforce transited from the production and manufacturing sectors to the service sector.

Figure 2.10: Structural change in the Japanese economy (1955-1980)



Source: Economic and Social Research Institute, Cabinet Office, Government of Japan (2001)

Figure 2.10 and Table 2.6 above show that how the distribution of the workforce has started to be concentrated in the tertiary sector, comprising more than half of the total employment in all sectors, with considerable participation from the secondary sector as well. It is noteworthy that these structural changes through resource reallocation from lower productivity sectors to higher productivity sectors had a significant effect on productivity. In this respect, the high growth was a phase of capital reallocation from the primary sector to the secondary and tertiary sectors.

More indirectly, we can see if there has been a rise in Japan's exports and imports related to economic development as it is presumed that a country in a growth phase increases trade volume during that process.

What the (Table 2.7) shows us that the export and import figures have kept on increasing considering the fact that there had been oil crises in the 1970s. That is just another evidence that Japan has really undergone tremendous growth in years.

Table 2.7: Total Value of Exports and Imports (1950-74)

Yearly total Value of Exports and Imports –
Fixed base (Unit: 1000YEN)

Calendar year	Export	Import
1950	298,021,052	348,195,583
1951	488,776,775	737,241,298
1952	458,243,197	730,351,682
1953	458,943,408	867,469,443
1954	586,525,032	863,785,437
1955	723,815,976	889,714,970
1956	900,229,011	1,162,704,360
1957	1,028,886,636	1,542,090,900
1958	1,035,561,686	1,091,924,896
1959	1,244,337,203	1,295,816,732
1960	1,459,633,161	1,616,807,363
1961	1,524,814,578	2,091,755,631
1962	1,769,817,267	2,029,148,690
1963	1,962,761,744	2,425,081,177
1964	2,402,348,862	2,857,515,493
1965	3,042,627,204	2,940,846,741
1966	3,519,500,700	3,428,172,558
1967	3,758,966,022	4,198,711,492
1968	4,669,798,348	4,675,407,477
1969	5,756,405,162	5,408,472,791
1970	6,954,367,159	6,797,220,528
1971	8,392,768,263	6,909,956,155
1972	8,806,072,248	7,228,978,838
1973	10,031,426,859	10,404,355,041
1974	16,207,879,577	18,076,381,928

Source: Trade Statistics of Japan https://www.customs.go.jp/toukei/suii/html/nenbet_e.htm

By looking at all the charts we may indeed note that Japan, starting from a far more unfavorable situation such as war loss and scarce resources, has experienced an economic growth much higher than it was in Western countries in the same years. This growth has enabled Japan's transition to a developed country in less than three decades. Therefore, we can claim that the Japanese economic miracle has occurred following the Second World War till the late 1970s with high growth figures that not any Western countries could reach.

In chapter 4, the factors that contributed to Japan's economic miracle will be examined in depth although there is a wide literature on this subject, the most important and accepted facts will be concentrated.

CHAPTER 3

THE STATE'S ROLE, BUSINESS CONGLOMERATES AND LABOR RELATIONS

Johnson (1982, p.320) states 'Japan is a system of bureaucratic rule' by claiming it was the state bureaucracy who governed Japan. The Japanese bureaucracy is largely independent of the political situation, oriented towards using the state for economic purposes which means policy decisions are less politically influenced and more economically driven (Aberbach et al, 1990). Bureaucrats not only enact laws and legislation that govern society but exercise their influence by the judicial system to establish arrangements with the businesses they monitor, allowing official communications dependent on reciprocal confidence before taking official decisions. Bureaucrats are appointed from the highest ranks of the best law schools; appointments are taken based on national exams and are not influenced by the election results. In addition, bureaucrats usually serve in the same ministry until they retire which guarantees stability and efficiency in crucial decision-making and economic policies (Woo-Cummings, 1999). Therefore, Public-private collaboration between bureaucracy and businesses has been built and perfected over time by structural evolution. The influence of the state has been a decisive factor in the Japanese economy to promote economic activities and sustain growth, whether by regulation, taxation, or public budget execution and well after the economy regained its pre-war levels, by providing loans and subsidies via public financial institutions, the Japanese government proceeded to promote the growth of industries as well as modernize the economic structure. Therefore, this chapter includes the actions taken by the Japanese state after the Second World War that had impacts on the nation's growth.

In the pursuit of economic growth, the state-led economic policies which could integrate the public and private efforts have been significant considering that the militarization of the economic system that imperial Japan favored was not the best way to be

a great country but investment, technology, and economic growth. Throughout the post-war period, various steps have been taken to stimulate investment in the new machinery as well as in key sectors. Thanks to the state support to the private companies, Japan has managed to have a strong business force that could compete with the Western world. In this sense, the unprecedented growth of the economy has been a hybrid product of the private sector and public policies.

The acts of the Japanese state in the economy have ranged from supporting the Japanese entrepreneurs to the creation of private-sector institutions, through legislation and subsidies. There are a variety of forums and agencies that promote the sharing of views and ideas between the public and private sectors in order to strengthen cooperation. In addition to the above instruments, the Japanese government used foreign exchange regulation and tax incentives to a great degree. For example, land and labor reforms, which significantly increased the consumption base of the economy, whereas Anti-Monopoly legislation retained robust domestic competition. On the other hand, Foreign Investment Law was one of the most significant laws protecting domestic enterprises from foreign competitors. The aim of this law to prohibit the inflow of foreign capital to domestic companies. However, at the end of the 1960s, foreign capital inflows were slightly loosened, but only in the sectors in which the country was already established to have a competitive advantage over the foreign competitors.

As some of the most important economic initiatives carried out by the state can be seen above, there are many characteristics of Japan's workforce, financial system, and key organizations that played a vital role in the success of Japan. Therefore, these systems along with key organizations that have contributed to the Japanese economic growth will be reviewed.

3.1. Bank of Japan (BoJ)

Being as Japan's central bank that steers the monetary policy and ensuring financial stability by adjusting the supply of money and interest rates, the impact of the Bank of Japan during Japan's post-war growth has been prominent since it has been a public financial institution in harmony with the private sector in the pursuit of economic growth in the country. In order to increase the competitiveness of the economy abroad as well as to promote the country's exports, the Bank of Japan has played a guaranteeing role in offering financial assistance to businesses, maintained a yen lower against the dollar. It was also responsible for implementing the monetary policies we had previously seen to bring Japan out of economic recessions by reducing monetary supply and recovering Japan's low-price competitiveness.

On the other hand, it is important to keep in mind its role as the funder of the country's strategic sectors, particularly those considered to have many possibilities for rapid growth and creating a draught effect on other sectors of the economy. Namely, the Bank of Japan is a mechanism to monitor the flows of money by the government. Yonekawa(1986) states that it was the Bank of Japan that provided financial support to important sectors such as the yarn sector, endorsing its support for the growth of the textile sector through low-interest policies in order for businesses to receive loans at lower interest rates. The Bank of Japan is, therefore, a powerful public institution as it is responsible not only for advising the government on financial matters and gathering statistical, historical data but also for implementing all monetary policies with a common purpose in mind: competitiveness.

3.2. The Ministry of International Trade and Industry (MITI)

Under the influence of the United States, The Ministry of International Trade and Industry was established in 1949 by fusion of the Ministry of Commerce and Industry and the International Trade Agency with the goal of coordinating economic policies between the

public and private sectors. This integration symbolized a change from a domestically focused industrial strategy, the main purpose of which was to increase the output of basic goods, to a policy directed towards foreign markets, trade development, consolidation, and modernization of industry. The MITI Board members have been selected from among the leaders in government, industry, consumer associations, scholars, labor unions, and the press who provide MITI with good social legitimacy and consensus. MITI is possibly the most influential public institution on the Japanese economic policy in the period of the Japanese economic miracle. Many scholars, such as Johnson (1982) and Takada (1999), assume that the outstanding growth of Japan is primarily due to MITI's crucial policies.

Interacting with other ministries, such as the Ministry of Finance, MITI served as the key organization of the Japanese government, which forecasted emerging sectors, provided information that allowed businesses to adopt business dynamics, and coordinating industrial activities. The importance of MITI in Japanese growth was related to public intervention and monitoring Japan's international trade. Considering the need for cooperation between private companies and the public sector with the objective of achieving the country's economic development, MITI has adopted certain policies such as technical intelligence and financial aid to support and defend the domestic industry from foreign competition. It was also in charge of importing foreign technology which helped the Japanese companies to adopt western technology and increase the quality of their products. These policies have been used quite effectively in the procurement of imported technology and requirements for imports. The State has provided MITI with the necessary instruments to conduct these tasks which were foreign exchange reserves, credit rationing, financial incentives such as tax breaks, and subsidies. Okimoto (1989) states that the Japanese government through MITI has repeatedly engaged in the economy by setting industrial sector priorities; mobilizing financial capital to promote their development; obtaining and embedding foreign technologies in private businesses; defending infant industries; offering investment-level guidance and coordinating rationalization and anti-recession cartels. In order to receive support by MITI, three major requirements had to be met: the industry needed to achieve high productivity growth; a high demand income elasticity and would provide employment opportunities. The partnership

between MITI and private corporations was more like a collaboration than top-down administration, and administrative advice was used by MITI to steer the developmental path since MITI exchanged knowledge with companies regarding international markets and strategies for economic growth. (Johnson,1982).

García et al (2004) state that MITI has favored mainly technology-intensive industries such as computer, telecommunications, and automotive, facilitating their developments as well as supporting the activities of the various industrial business groups by short-term foreign exchange allocations, trade protection, tax advantages, or subsidies in order to increase the competitiveness of Japanese companies against the foreign companies since these were promising sectors which contribute to the full employment with high chances of rapid growth and have a positive income elasticity of demand that reduces the costs of production as the production scale increases. Furthermore, Tyson et al. (1989) add that Japanese R&D assistance is selectively focused on activity, industry, and mostly by companies. Japan's policy is motivated by the belief that the government may and should play a role in identifying and supporting high-tech winners.

MITI took several steps to improve international trade relations from the 1950s to the 1970s and with greater strength in the 1960s, as these industries developed and increased their competitiveness in foreign markets. Thus, the goal of MITI was to orient companies not only towards exports but also towards investing and acquiring foreign technology with the intention of applying it in Japan and even developing it. Importing technology was one of the core components of Japan's post-war industrial policy. Until the capital liberalization of the late 1960s and 1970s, without the authorization of MITI's, any foreign technologies could not enter the country; joint ventures could not be authorized, and patent rights had not ever been licensed without MITI's pressure on the seller to decrease the royalty or make other modifications beneficial to Japanese industry as a whole (Johnson, 1982). Furthermore, until 1971, MITI was able to keep the price of the yen artificially low compared to the dollar in order to preserve global competition due to exports becoming cheaper with low yen.

However, with the introduction of the floating exchange rate, MITI was not able to maintain this economic policy and consequently lost influence on the economic development of Japan.

One of the MITI-linked agencies responsible for handling the international trade of Japanese companies will be studied below on account of its great effect on the Japanese economy.

3.3. Japan External Trade Organization (JETRO)

Japan External Trade Organization or shortly JETRO is a government-related organization officially founded in 1958 in order to facilitate Japanese exports and mutual trade abroad. In addition to the economic difficulties in which the nation found itself, the Japanese trade was very severely affected during the US occupation as Japan remained isolated, having lost its trading places in other countries due to the breakup of Japanese business groups. Therefore Japanese business organizations agreed to establish the Japanese Foreign Trade Association in 1947, whose function is lobbying to promote free-market activity. According to (Llamas,2014) this private association was the origin of JETRO.

Although it has been a private organization, it has undergone significant changes. First, in 1951 JETRO was institutionalized, with 50 percent state control and the other 50 percent divided between the Japanese International Trade Organization and the new JETRO partner, and in 1958, it became a public institution. The main actions of JETRO are to conduct research regarding the tendencies of the international market to promote Japanese exports and participate in international fairs for both the export of Japanese goods and the import of foreign products. Its role as a consultant to Japanese and foreign companies has been significant to Japanese trade for all this especially in the post-war period when the exports of Japan has experienced a dramatic boom which caused a surge in foreign exchange facilitating Japan's import of machinery and industrialization. Therefore, this is one of the public institutions which has laid the foundations of the Japanese economic recovery in the 1950s as well as the Japanese economic miracle subsequently.

From the Meiji Restoration until the end of World War II, Japan was regarded as a country with a high concentration of business groups that had significant influence in the Japanese economy, preventing competition of small and medium firms in the market and thus criticized by the United States. In fact, one of the main objectives of the U.S. occupation after of the war was to put an end to the concentration of business groups that were blamed for supporting Japanese imperialism. Also, this characteristic of the Japanese economy strongly contrasted with the American model, where the market should be free for competition that would support the economic system efficiently and not be controlled by the actions of business groups.

Thus, given the economic growth that the nation has experienced, we should recognize this main feature of the Japanese economy as a factor to be considered through the analysis of Japan's business groups.

3.4–The Zaibatsu(財閥)

The literal translation of the term zaibatsu would be a wealthy clan which refers to large corporations developed in Japan and grew rapidly after the Meiji Restoration of 1868. Shimotani(1999) describes zaibatsu as a long-term strategic partnership between large companies and selected groups of smaller companies are formed and connected through investment and staff exchange. According to Yonekawa (1986, pp. 113-114), The creation of the Zaibatsus was due to the practice of separating business administration from their lands. Its history dates to the Japanese Feudal Era, and the Meiji Restoration as well, when the territorial leaders which called daimyo had to give all their political and military power back, as did the Shogun or military ruler, to the Emperor of Japan, who had once again consolidated that power. Therefore, in return for these political and military powers, they were given the economic strength" of a nation about to undergo changes that would take it

from a feudal country to a modern country. This economic influence was due to the fact that the Japanese government had to economically compensate the noble Japanese families that controlled the numerous territories that constituted Japan before the Meiji Restoration. These compensations were used in collaboration with the Japanese government, to concentrate financial resources, and from there to develop the country in agrarian, commercial, and industrial aspects hence the weight of the country's reconstruction fell on the former Japanese military bourgeoisie, but government support was promoting technological progress, exports and imports, even in financial or tax affairs of this class which enabled Zaibatsus to specialize in a wide variety of sectors, mostly solely by means of a monopoly secured by the government. This expertise has facilitated the substantial growth of the entire economy and, ultimately, the militarization of the economy. As a result, by the end of the First World War, the most powerful Zaibatsus had directly or indirectly controlled about 75 percent of Japan's Gross Domestic Product (Kensy, 2001). The intention of this initiative was to protect the nation against the outside world. This isolation has remained until the end of the Second World War.

The four most powerful and influential Zaibatsus so-called Big Four at the time when Japan entered World War II were: Mitsui, the first established zaibatsu in 1876 and primarily committed to commerce, banking, and energy sectors, Mitsubishi, dedicated to the shipbuilding industry, chemicals, banking, and mining.; Sumitomo, dedicated to banking, the petrochemical sector and raw materials in general; and Yasuda, specialized in finance and focused on trade. By the end of the war, their operations grew in sectors such as steel, commerce and banking.

Table 4.1 : Industrial Diversification of the Ten Major Zaibatsu in 1945, in Millions of Yen

<i>Zaibatsu</i>	Industry				<i>Zaibatsu</i> Total	<i>Zaibatsu</i> (% of economy)
	Finance	Heavy Industry	Light Industry	Other		
Mitsui	169	2,214	274	404	3,061	9.4
Mitsubishi	160	1,866	73	605	2,704	8.3
Sumitomo	65	1,469	29	102	1,667	5.2
Yasuda	209	119	117	64	510	1.6
Nissan(Aikawa)	5	1,558	103	38	1,703	5.3
Asano	0	419	89	76	594	1.8
Furukawa	4	479	3	4	490	1.5
Okura	6	218	34	56	314	1.0
Nakajima	0	188	24	0.768	213	0.6
Nomura	26	50	27	62	165	0.5
Top ten zaibatsu total	644	8,582	773	1,412	11,420	35.0
Economy total	1,215	17,513	4,600	9,108	32,437	100.0
Top ten zaibatsu (% of economy)	53	49	17	16	35	

Source: Holding Company Liquidation Committee (HCLC), Japanese zaibatsu and its dissolution, as cited in Yasuoka (1976, pp. 34-35)

As I mentioned in the historical context of the Japanese economic growth when the American occupation took place after Japan's defeat in the Second World War, American forces determined to dissolve this structure by not only dismantling the Japanese Zaibatsus especially the biggest ones into various small businesses to make them fully autonomous since it has been believed they were hindering the idealized perfect competition over monopolization of the market but also to eliminate the huge Japanese families that run them from their offices and confiscate their shares and sold them to the public. As stated by Morikawa (1992), the Zaibatsus were blamed for being the primary economic supporters of Japanese militarism and 'feudalism.' thanks to the significant gains through the exploitation of the former Asian colonies. It was therefore seen as a threat not just to Asian nations, but also to American interests in the region.

As a result, in 1947, the Antimonopoly Act was passed in order to put an end to the zaibatsus and keep them from being eventually reconstructed. From 1948 however, this act was eased for Japan's economic recovery by the US in order to stop the spread of communism as Japan was considered as a buffer state between the Communist nations and the US, The United States thus wanted a powerful Japan with a strong economy (Russel & Miyashita, 1994). As a result, The dissolution process has been halted, control of the great Japanese families was restored in 1950, and in 1952 the law of restoration of the Zaibatsus was passed, which modified certain aspects of zaibatsu and created the new businesses referred to as keiretsu. These business groups have extended to exercise their impact on the economy with the government's support as they are considered to have a positive influence on Japan's growth ever since. However, it has generated international problems because of the great export potential of these companies.

There are very subtle differences between the Zaibatsus and their transition to the Keiretsus, the concentration of businesses run by a single organism with a single common objective in both structure however the way of concentrating varies in both systems, the Zaibatsus belonged to groups of families according to Morikawa (1992), zaibatsu is characterized as a family-run business group in which a diversified business is solely owned by a single-family or an extended family, while the assets are attributed to banks and other shareholders in the Keiretsus. This means that the system is much more hierarchical in the Zaibatsus than in the Keiretsus since control is more centralized and decisions are taken in the pyramidal structure, whereas in the Keiretsus the control is de-centralized depending on each governing body of the various companies that form it. One of the characteristics of the keiretsu structure is cross share ownership, which was built on the basis that companies hold shares of one another. Additionally, since they don't have a parent or holding firm, they are not conglomerates.

Table 3.2: Corporate-specific Features; Comparison by Anglo-American & Japan

	Japan	Anglo-American
Company's goals specify	Active stakeholders (e.g. managers and employees)	Shareholders
Nature of companies	Social importance corporation	Financial importance corporation
Corporate governance institutions and mechanisms	Main banks Cross-shareholding Employees	Stock markets
Labour relations character	Harmony and balance between interests of managers, employees and shareholders	The primacy of interests shareholders over employees

Source: based on: R.Dore (2000) , J.Bossak , W.Bienkowski (2004)

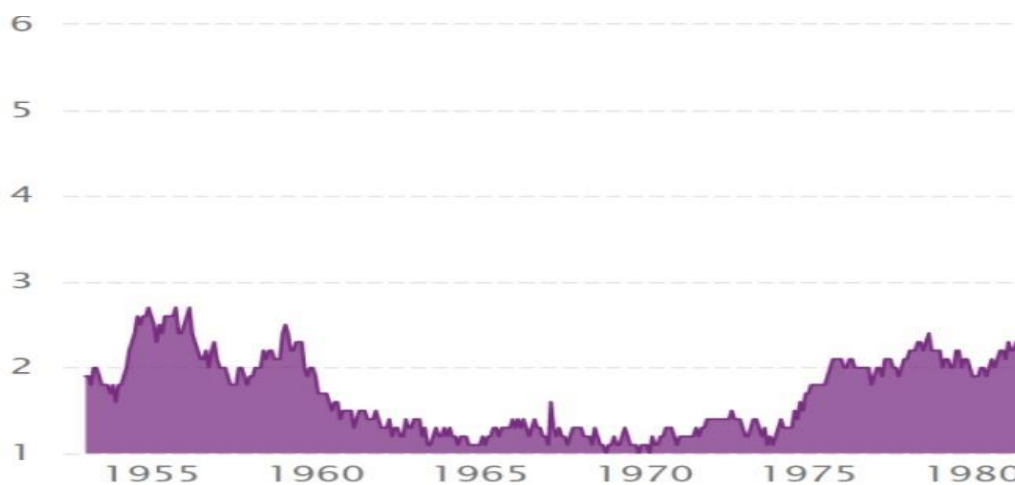
3.5-The Keiretsu (系列)

The term keiretsu can be translated as a "group" or "system" in English. Keiretsu is the Japanese business structure that was established by a coalition of firms like the holding, either from the same industry or across different industries after the Second World War. The role of keiretsu by maintaining close ties with the Japanese government had major effects in the post-war era, as the Japanese industrial sector linked to the Keiretsu had transformed the nation by raising the national standard of living from poverty to one of the highest in the world (Miyashita et al. ,1994, p.194). The keiretsu structure stresses the collaboration between associates and defends them against fusion and acquisition. Through this structure, business groups are collectively assisting and collaborate with each other, diversifying the areas of activity to minimize the risk, products, and services are sold at a more favorable price than the retail price, while the profit margin decreases as certain keiretsu enterprises compete with others also receiving public guarantees when investments are made. Such

attributes have had many impacts on the economy. Kosai (1988) notes that the quality and quantity of labor supply had a significant advantage as the workforce accounted for 65 percent of the population, increasing from 3,484,000 in 1948 to 5,326,000 in 1973. However, Allen, G(1980) states that even though there has been an increase in the workforce overall, employee percentage in small businesses has decreased which led to the gradual increase in the participation in the employment of medium and large companies.

On the one hand, labor mobility has been promoted, as keiretsu workers can work in many coalition firms, rather than being fired, they were trained and mobilized into another firm, from a depressed to a thriving industry, for example. On the other hand, businesses minimize the negative effects on the economy by their actions, such as unemployment, which was around 2,5% in 1955 and less than 2% until the late 1980s.

Figure 3.1 Japan Unemployment Rate in Percentage (1955-1980)



Source: CeicData <https://www.ceicdata.com/en/indicator/japan/unemployment-rate>

Another beneficial result for the Japanese economy resulting from the keiretsu structure can be seen in the capital investment of large companies in efforts to progress its business objectives. According to Pelegrín and Jansana's data (2011, p.56), Investment in plants and machinery has risen around 22 percent from 1951 to 1973 which can be considered as a high proportion for a war-torn country. Considering the great investment capabilities with more sums of savings thanks to the larger economies of scale than small companies as well as having a financial institution that facilitated their financial needs, it is reasonable to assume that the investment proportions of these business groups have been high.

An important feature must be considered of the Japanese business groups however, which is the low inflow of foreign capital because of the complex form of ownership of certain businesses over others. Cross shareholding and ambiguity about the distinction between what business they own have made it much harder for international companies to acquire sufficient shares of keiretsu companies with the intention of owning. This had both benefits and drawbacks. On the one hand, it is clear that by not engaging foreign investors in Japanese firms, the administration of such companies by the management of the business conglomerate has been much easier and has allowed economies of scale. As Johnson (1989) claims by supporting and protecting Keiretsus from any sort of legal or financial challenges from foreigners, each industry has enjoyed a sustainable, cooperative atmosphere. Whereas Morris and Adelman (1989) state that Japan shows how import-substitution policies and efficient national political structures combined with foreigners' restricted influence over domestic economic policy achieved domestic growth that is effectively diffused. On the other hand, however, when no more foreign investors joined the shareholding market, equity funding was more costly for businesses, but the financial factor was not a severe problem for these firms during this time since financial institutions such as banks were within their ranks.

In many respects, state influence on the Keiretsus has always been notable. For example, the State tried to guarantee investments made by the keiretsu firms through financing businesses at a very low cost and even zero, thus reducing the risk and also protecting the businesses monopolies from the outside despite the foreign pressure against

the keiretsus that were criticized for having different competition values than Westerns since exclusive trade within Keiretsu companies poses an obstacle that excludes non-affiliated businesses from entering the market and hence creating a non-competitive environment.

Russel and Miyashita (1994, p.10) state that the keiretsu is formed by the financial institutions, the trading company, and the major producers. The trading company is specialized in exporting and importing which also serves as intermediaries for foreign trade across multinational networks of subsidiaries and stations around the world. When serving as intermediaries, the trading company also has a substantial share of trade credit and short-term loans provided to small companies involved in import and export activities. Although these business groups are formed by businesses from the most diverse fields, most of them usually have several businesses that form the basis of keiretsu, which affects others' activities, but there is no control group that guides the operations of the group. Conceivably the most decisive group of all keiretsu is the bank. Most of the Keiretsus own one and banks play the financial role for activities of the business groups with other businesses as the banks typically own the shares of other keiretsu firms, so they exercise some influence over them if a company falls into trouble or badly managed. This cross-share arrangement offered ample incentives for companies to concentrate on long-term initiatives and growth goals instead of implementing short-term profit maximization policies because they were free from shareholder pressure and hinders the possibility of hostile take-overs (Comert,2005).

Keiretsu companies are made up of industrial businesses from a wide range of sectors infrastructure, communications, or automotive which supply the goods to the market and try to adapt to the evolving business model circumstances. There are two types of keiretsu: Horizontal and Vertical. A horizontal keiretsu refers to a consortium of cross-shareholding firms financed by the main bank through a variety of financial services. Usually, one of the core businesses is a trade-oriented company that not only exports its manufactured goods but also imports other products such as machinery, raw materials, and technology. There is no controlling group that directs the group's operations because of the mutual crossholding of stocks between companies preventing takeovers. Along with the financial institution, the

trading firm, and the major producers, the horizontal keiretsu is established (Russel and Miyashita,1994, p.10). Horizontal Keiretsus are known for their ability to offer long-term flexibility, risk mitigation, productivity, and collective support. These horizontal Keiretsus facets have been institutionalized primarily by indirect funding and labor relations. Mitsubishi, Sumitomo, Mitsui, Fuyo, Sanwa, and Daiichi-Kangin are the six greatest business groups forming Keiretsu that were associated with the Japanese economic growth. For example, Mitsui is still a keiretsu around Japan's first private bank Mitsui bank itself along with some of the companies that make it up are Toshiba Corporation, Mitsui Construction, and Mitsui Industries. The Mitsubishi group is made up of the Mitsubishi Bank, Mitsubishi Heavy Industries, and Mitsubishi Motors. One last keiretsu as an example to give which was significant was Sumitomo, established in 1895 on the basis of the Sumitomo Bank and companies such as Sumitomo Heavy Industries or Nippon Electric. In order to defend themselves from rivalry and build the strongest competitive situation, these businesses allied themselves with other companies who have the same trading needs and economic prosperity. The alliance then aligned itself with the banks for greater bank confidence and less risk of defaults on loans. However, keiretsu style new partnerships were not conglomerates, unlike the zaibatsu companies, since there was no single ownership, top board executives meet on a monthly basis to address the economic condition of each company.

Vertical keiretsu is a network of small or medium-sized businesses affiliated with larger companies that work together as subcontractors to improve effectiveness and minimize the costs of the products. More specifically, the vertical Keiretsus are hierarchical supply chains at multiple levels that connect the parent keiretsu at the top of the pyramid with hundreds of products or sub-component suppliers (Selig, 1997). It is composed of assembled suppliers, subcontractors that manufacture components and products, wholesalers and retailers that sell their goods for larger companies. Many of the big vertical Keiretsus have emerged in the automotive and electronic industries. Companies such as Toyota, Nissan, Sony, and Hitachi are vertical Keiretsus with various suppliers of materials, components, and electronics, manufacturers of parts, and sales companies linked closely to them through long-

term commercial partnerships. Vertical keiretsu offers effective, long-term mutual advantages to the parent organization and its vendors, including strategy and investment coordination, technology and knowledge exchange, quality monitoring and distribution, and stability over the market cycles (Saito, 1997). These companies have supported Japan in the field of exports and thus encouraged her economic growth because it concentrated primarily on exports.

3.6. Impact of the Keiretsu on the Economic Growth

There is an argument in the literature concerning the real impact of the keiretsu business groups has had on Japan's growth to become one of the world's most powerful economies. On the one hand, there are some who defend this structure as the most important factor in Japan's economic growth. Scholars such as Orduna(1986) argues that the existence of keiretsu is the main factor explaining the success of Japanese economic policy since large Japanese businesses have been able to allocate large amounts of money to investment and innovation that small and medium-sized businesses have not been able to do to that extent. The Japanese government served as a business partner for many of these companies, providing regulatory supervision, tax concessions, and cheap loans. As a result, companies concentrated on long-term investment ventures. With the success of the adaptation of innovations in production or foreign technology through fierce competition of keiretsu businesses, Japan's economic policy should be followed as an example in other countries. Moreover, Gaul and Jungblut (1981) argue that the keiretsu structure is the key factor for the Japanese economic miracle by implying there is a certain connection among businesses that influences one another. This framework both improved cooperation between groups of companies through the provision of knowledge networks and sustained financial and other assistance to affiliated companies in the event of an emergency. Therefore, the competition with the large Western businesses can be achieved by uniting Japanese businesses under one roof in order to acquire mutual knowledge and thus benefit from both sides, something uncommon in the West. On the other hand, there are others who argue that the economic

impact of these big businesses is overrated, and the Japanese miracle is due to other significant factors, such as investment. Scholars such as Allen (1980) believe that business concentration has not influenced the economy in such a large way, arguing that while there were some businesses with greater economic power, there were also many other small and medium-sized enterprises that contributed significantly to economic development. He also adds Zaibatsus and the later Keiretsus did not have complete control over the economy. These big businesses were competing with one another rather than supporting each other, creating an effective market system based on competition that helped Japanese growth. Whereas Morikawa (1992: 243-244) assumes that it would be a mistake to believe that the Japanese economy would grow only on the basis of Zaibatsu-led united companies until 1945 and after with Keiretsu businesses even if they had been promoted by the state.

As we can see there are different views on this aspect of the Japanese economy. However, it is fair to say that competition of these businesses in the market has been the fundamental factor in the development of Japan.

3.7. Labor Relations

The evolution of labor relations after the Second World War had a significant influence on the development of Japan since the labor relations of the Japanese people are different from the rest of the world which have certain connections with their culture. Lifetime employment, seniority-wage, and promotion scheme have been recognized as distinct aspects of Japanese work practices. It should be noted that these aspects of the Japanese people have been an important factor in post-war economic development, influencing all the economic activities from the productivity of businesses to the distribution of income, unemployment, etc. since Japan obtains great labor loyalty, loses fewer days to protests, can innovate more quickly, has greater quality management, and usually generates more of the right thing faster than its foreign counterparts because of these facets of Japan's corporate structure (Johnson, 1982).

The Japanese system of labor relations starts in the educational system. The Japanese system of education is intricately linked to the private sector, which means that a student can start working in a business in the case of a university student even if they have not completed their studies, effectively promoting entrance into the private sector. Academic success is essential to the sustainable development of a nation as it increases the efficiency of labor, leading to higher labor efficiency-higher wage earnings, technical and administrative capabilities, industrial productivity, and economic prosperity globally (Tai, 1989). Llamas (2014) states that to recruit hardworking employees, employers of large businesses negotiate with successful students as well as universities, creating a highly competitive job market and therefore it is really essential for the Japanese students to study in the prestigious universities through which they can acquire a job in one of the leading companies that ensure their future. This means that many employees can enter a particular company shortly after graduating from university and remain with that company until the compulsory retirement date. Even in an economic crisis, these workers remain as permanent employees of the company, and dismissing workers is not so usual. In return, employees promise an almost infinite degree of commitment to their companies and do not resign or reject any work assignment. This is called a lifetime employment system. However, this situation creates an imbalance between medium or small-scale and large businesses as those benefits large businesses by leaving the former to contract average students.

In the first chapter, we were able to see how the labor unions began to shape after World War II under the U.S. occupation as means of westernizing the Japanese economy. The unions, which arose to compensate for the high entrepreneurial power of the old Zaibatsus, actually ended up being an extension of the influence of large corporations since these businesses offered long term contracts to the employees which were perceived as a protection for the future by employees hence the unions did not serve the initial purpose intended by the Americans.

Japanese companies are well known for their achievement in fostering a "community of fate" focused on participatory management, work stability and mutual consultation

between labor and management, horizontal interaction, team benefits, and a comparatively limited difference between the highest and lowest wages (Ozturk, 1999). One of the characteristics of the Japanese recruiting system is that contracts are supposed to be indefinite-term which means employees are guaranteed to have a position in the business before retirement that is most likely to take place at the age of 60 since this helps to encourage the full performance of the worker by creating better relationships and safety and it is very difficult for employers to release or lay off workers unless the worker is involved in any sort of misconduct. Therefore, retaining work changes of employees and unemployment rates low. Employees under the life-time job scheme usually have seniority-based salaries, earned promotions, and bonus payments depending on the length of employment in the company which means after spending many years in the company, employees can not only reach a higher role and thus rewarded with higher wages and benefits based on the company's profit but also more responsibilities to stimulate the emotional link with the business whereas a new employee would not have a high salary or obligations. Since employees are unlikely to quit, this stable workforce has allowed the administration of companies to successively implement new technologies and where possible, retrain employees for multi-functional duties as long as jobs were secured (Yonekura,1993). At their current stage, rotation made workers flexible and trained them for higher roles in the same company. This investment in company-specific human resources has helped improve the productivity of employees in the long term (Ito, 1992). In return, at the cost of individualistic preliminaries, a company employee prioritizes the welfare of the company, often without expecting direct pay for any of the hours dedicated to work. The long-term dedication formed by both labor and management generates legitimacy, loyalty, and uncommon levels of confidence and trust which are characteristics of the Japanese business. The shared experience, the comparatively small financial and social gap between the top and bottom, as well as the sense of security together make a consensus and group decision-making mechanism possible in which the viewpoint of all workers is consistently pursued and compensated. Almost everyone at every level appears to have a sense of personal engagement and identity with work (Robinson, 1982). While the root of such employment activities dates to the pre-war years, it is argued

by some scholars that this system eventually became a core aspect of the Japanese employment structure only after the Second World War (Ryutaro 1990, Allen,1981).

The size of the company has been especially important in Japan. Therefore, a distinct dual employment system exists between "large" and "small -medium-sized" businesses within the manufacturing sector. While the large businesses are able to pay higher salaries to recruit better-educated employees and make investments in employees' training to handle advanced technological equipment which requires a reliable supply of employees for manufacturing activities thanks to the strong capital structure of large businesses that makes it possible to implement high-capital-intensive manufacturing practices, which, in return, make high efficiency and high-wage possible, small and medium-sized firms, on the other hand, follow labor-intensive approaches owing to their vulnerability in terms of accessibility to capital, as well as the weak capital structure. Therefore, they recruit seasonal employees with low skills, pay low salaries and give minimal benefits even in cases of long service. Such wage differentials may refer to several variables, such as age, gender, education, and training of an employee (Comert, 2005).

Since Japan comes from a machismo society, in the Japanese labor system, contracts for women were typically short-term, women used to work for a short period of time, and hence they did not earn a high salary or great responsibilities. This contributed to a significant amount of cheap and temporary labor, leaving men with the most important positions in the company. Another source of cheap labor has been the employment of retired people. Considering Japan has one of the highest life expectancies, the Japanese pension system was relatively different from other countries in which the people retired before they reached the age of 60 by 1987. In fact, Japanese firms instituted reemployment policies that provided a job to the retired workers, but a much lower wage and lower-ranking jobs were offered. These people, therefore, worked with low wages to make ends meet (Clark, 1991).

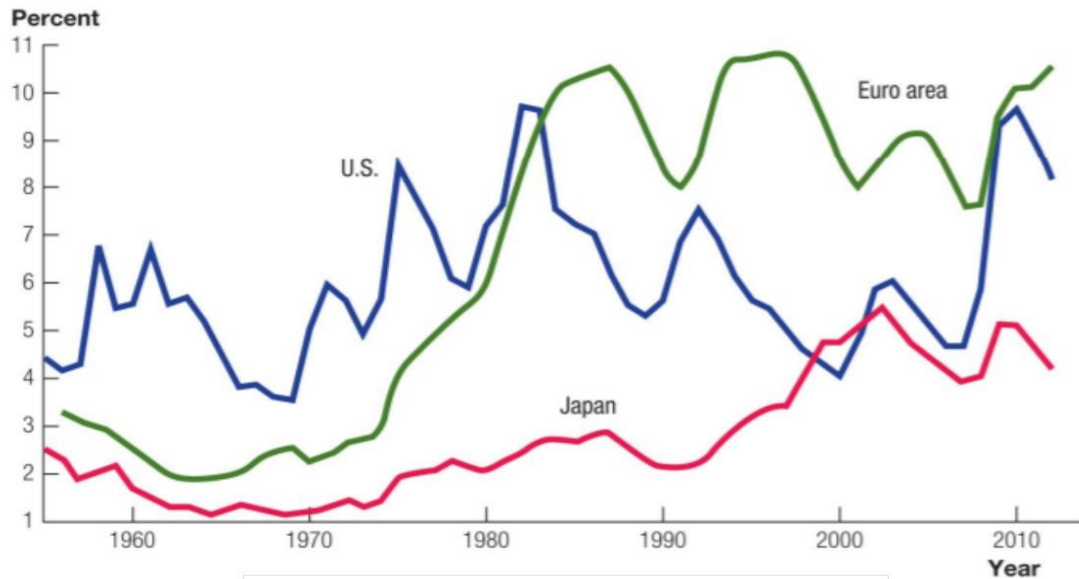
The dual structure of the Japanese economy has been reinforced by wage differentials indicated through the use of comparatively cheap labor in medium and small businesses and

excessively low-interest rates for large businesses however since large and smaller businesses are in a complementary relationship, various small-capital enterprises continue to exist.

MITI's industrial policy to modernize and develop small and medium-sized businesses has managed to compensate for these detrimental effects and expand regional economies to preserve social stability. In addition, the development of small and medium-sized businesses has led to the formation of an industrial network between large and smaller businesses, which would reduce transaction costs for the industrial sectors. Large enterprises use labor-intensive products provided by cheap labor in smaller enterprises through the subcontracting model and the establishment of similar firms under their use medium and small businesses as a buffer against market volatility which brings out the dependency of small and medium-sized businesses and these businesses enjoy being subcontractors of large businesses in order to evade administrative instability resulting from poor and obsolete production methods. This form of network is one of the reasons for the productivity and technological progress of the Japanese manufacturing industries.

When we observe the figure below, we were able to see that the unemployment rate was exceptionally low in the period of economic growth and even lower than the U.S and European countries. This aspect of the Japanese economy is attributed to the reason that businesses were doing an incredibly significant social task by keeping their employees in their employment amid the poor economic moments the business might go through. Indefinite-term contracts offered to the employees as well as the exchange of the employees among the keiretsu companies have maintained the unemployment rate low.

Figure 3.2: Unemployment in Japan, the United States, and Europe Since 1955



Source: OECD Main Economic Indicators and the European Central Bank's Statistical Data Warehouse

Japanese trade unions which represent a significant proportion of union workers are generally organized under enterprise unions rather than industry-wide unions or craft unions. An enterprise union is a corporate union that encompasses the blue-collar and white-collar workers regardless of the jobs they do and low-level managers. The enterprise unions offer solid job stability, good wages, and bonuses to regular workers, also encourage employee involvement in the company and therefore the commitment of workers to companies that contributed to the businesses' long-term investment strategies. Because of this reconciliation, labor gained a position outside of its existence as a manufacturing function as a legal member of the corporation. Centered on this accommodation, labor started to engage in production and management decision-making through different structural structures to improve productivity in return for its equal share of income. This dense network of exchanges between management and labor led to the versatile production structure in Japanese manufacturing industries (Kume,1998)

Human capital investment is another characteristic of Japanese businesses since it's believed that investment made in the employees could foster the loyalty of employees and

increase harmony within firms contributing to the company's success in the long run. Hence, there is a strong relationship between employees and the employer in which each has his own role and responsibilities within a hierarchical order. Since Japanese culture places great emphasis on family relationships and responsibilities the business is seen as a family, the existence of the business has become a major issue for employees and employers and unity inside a company has become a core concept and a corporate goal.

In conclusion, the key features of the Japanese employment system which contributed to the economic development of Japan are the indefinite contracts, the salaries according to seniority, the recognition of the business as a family.

CHAPTER 4

JAPAN'S TECHNOLOGICAL ADVANCEMENT, THE ROLE OF TRADE, THE FINANCIAL SYSTEM & BANKING SECTOR

4.1. The Root of Technological Development

Technological innovation has been one of the key factors that contributed to the evolution of the Japanese economy. From a historical point of view, the general orthodox opinion is that the Japanese have been surprisingly vigilant and successful in maintaining the transition of technology from the West to their own nation and that the "Western" technology has been efficiently absorbed which in return, Japan has demonstrated excellent success with her high-quality labor power in the implementation and commercialization of this technology which contributed to the rise in economic productivity dramatically as a result of substantial technological advancement. In fact, most of the Japanese's achievements could be attributed to their investment in the adopted technology and hard work. In this chapter, the details about the evolution of technological growth in the Japanese industry will be given.

There was a considerable gap between Japan and the West in terms of technological capability after World War II, but Japan began to replace most of its industrial capacity with the introduction of technology. According to Pyle (2006), The massive influx of technologies by foreign companies quickly filled this gap. Because after World War 2, Japan did not allow foreign investment directly, the introduction of foreign technology was accomplished by technological collaboration without takeovers, preventing the foreign influence on the Japanese industry. As the Japanese market was viewed as too limited to be worth developing, several foreign companies were able to sell their technology. The productivity of the Japanese industry has been tremendously improved by technological advances. The Japanese even sought to improve the technologies they imported, increasing the international competitiveness of Japan.

Table 4.1: Technological Imports, 1949-1975

Period	imported items	price paid (US dollars)
1949-55	1,141	69 million
1956-60	1,773	281 million
1961-65	4,494	684 million
1966-70	7,589	1.536 billion
1971-75	10,789	3.205 billion

Source: Kosai (1989 ,521)

As we have seen a significant increase in all industrial productions since the 1950s in Chapter 2 and changes in the workforce based on the structural changes in the economy in Chapter 3, Japan has transformed from a technology-importing country to become one of the technological leaders in the world thanks to a supportive state policy and the contribution of businesses to technological growth. State intervention in directing industrial policies in the economy focused on the secondary sector via its institutions has tried to achieve public goals in private companies which were increasing the value of production and specialization.

As claimed by Kosai (1988; 27-50), Japan went through three stages in the reconstruction period. The first phase covered the state's intention to recover the production of industrial materials in important sectors such as coal and steel. The second phase intended for lowering the prices of these materials to boost economic growth through exports and competition in the market since these materials were the most demanded ones in the Korean War. Japan has favored these sectors with subsidies and tax cuts in order to reach competitiveness. Ultimately, the last phase aimed at maintaining economic growth by improving the welfare of the citizens and achieving full employment.

Industries that emphasized the use of technologies and projected to expand dramatically were targeted, with labor productivity expected to rise rapidly. Japan's Development Bank issued low-cost loans. Foreign technology was able to be implemented

and products were manufactured for the markets by cooperation with different manufacturers and this cooperation not only allowed the standardization and specialization of productions but also the cost reduction and quality enhancements. Then export sales were organized to restrict unfair competition. For that, international trade tended to be favored and the promotion of heavy industry was encouraged as well. Large industrial infrastructures such as Toyota were sought to be built that favored the increase in industrial production.

During this period, the transportation industry has become one of Japan's most important economic industries. Mass production of cars, trucks, buses, trains, and among others, has supported the economic growth, boosted exports as well as offering facilities for the population to transport. Shimokawa (1994) states that it was after the Korean War when the Japanese automobile industry has become one of the most important producers thanks to the rise in foreign demand for the automotive industry and the deals between Japanese and European companies to import automotive technology. Under these conditions, Japanese car industries have formed so-called 'investment rivalry' rather than 'market competition,' which is an oligopolistic competition about investment in plant and machinery, and R&D (Research and Development) has been dominant in order to gain the 'first-mover advantage' in terms of productivity and quality (Spence, 1979).

The investments have played a crucial role in the development of Japan from a devastated and largely agricultural economy into a developed economy thanks to the nation's achievement in allocating her resources such as the foreign exchange inflows that came mainly from the Korean War to the investment of private companies in heavy and high-tech industries which favored the import of new industrial machinery and develop her own technology since the most significant determinant of long-term development, depending fundamentally on savings ratios were investments into the industries where Japan had a comparative advantage. Technological advances have made a significant contribution to economic development and encouraged businesses to find various ways to expand, and this led the Japanese economy to compete in foreign markets as technological improvements in one industry have had an impact on the growth of other industries. Japanese industries have

tried very hard to borrow the best technology available in the world and then improve upon it. (Ichimura, 1998, p. 20) For instance, the improvement of steel production has successfully enhanced the quality of the special steel used in vehicles which led the automotive sector to compete in foreign markets. According to De Long and Summers (1991, p. 446):" High investment rates in equipment can account for almost all of Japan's exceptional growth performance." In addition, investments have also contributed to education, improving the quality of education which in return provided skilled labor to large companies over time. This contribution among other factors has influenced Japanese productivity (Llamas,2014).

4.2. Savings

Japan has concentrated her resources on industries that were considered strategic such as cars and computers and the development in these industries demanded massive investment, and since Japan did not want to allow foreign investment, funding had to come from domestic savings. High national savings have become the source of business investments without resorting to foreign borrowing since the domestic saving ratios kept on increasing during the high growth period and household savings were the largest portion of domestic sources thanks to the government's low-interest income taxes policies and the semi-annual incentive scheme, urging citizens to save. If the saving ratio had not grown steadily after the Second World War, the phenomenal economic development of Japan after the war could not have been accomplished because the high level of household savings had become a significant financing tool needed to improve the nation's productive capacity for investing in plants and machinery through corporations. (Sato ,1987).

As can be seen from Table 4.2 below, during the 1950s and 1960s, the household savings rate was about 15 percent and increased to around 20 percent at the beginning of 1970 which Japan strictly abstained from the domination of foreign capital and thus depended heavily on citizens' domestic savings.

Table 4.2: The Japanese Household Saving Rates 1955-1970(Percentage)

<u>Year</u>	<u>saving rate</u>	<u>year</u>	<u>saving rate</u>
1955	13.1	1963	15.3
1956	13.7	1964	15.4
1957	11.7	1965	14.9
1958	12.0	1966	14.3
1959	13.4	1967	15.5
1960	14.7	1968	15.6
1961	15.3	1969	16.7
1962	14.8	1970	18.5

Source: The Economic Survey of Japan, 1996-97, long term statistics

There are numerous explanations to justify Japan's strong savings: a non-inflationary currency, tax breaks for saving, a pro-saving mindset, a comparatively weak social insurance system; a wage system that involves substantial lump-sum bonus payments twice a year, a pension system that dramatically decreases the wages of an employee until the age of 60, and a widespread postal saving system which is a banking mechanism based on government-run post offices where individuals can deposit and withdraw cash with guaranteed competitive interest rates at various post offices around the country as well as the high pace of income growth have been described as the most significant factors while many scholars have stated "tradition or culture" as a fundamental justification of Japan's high household saving rate, suggesting that the Japanese people's ability to work hard and save is primarily attributed to their Confucian origin, which treats vigilance and frugality as virtues (Kurosaka & Hamada, 1984, p. 118), but each factor has played a key role in achieving high savings rates in Japan.

In sum, technological advancement has been positively influenced by various factors but with the adoption and specialization of the imported products, the private and public

sectors have been able to lead the economy in order to be ahead of developed countries. The Japanese household's high saving rate has also helped to achieve a high investment rate without having to borrow money from abroad as the state has relied on household savings to provide investment funds to industries (Ito,1996).

4.3. The Role of Trade

Japan's foreign trade policy has been essential to economic growth since Japan has been widely agreed to be a highly specialized country in many industries where it gained a competitive advantage, and thus required foreign trade to procure goods where it did not gain an advantage by manufacturing them. As a nation with a certain scarcity of raw materials and limited resources, foreign trade and the specialization of imported materials have made economic growth possible. Before the Second World War, thanks to its colonies in Asia, Japan was able to exploit the raw materials needed for its industry with the dissolution of the Japanese Empire however, Japan was no longer so competitive abroad and its trade was strongly reduced. Nonetheless, thanks to the establishment of trade policy which favored trade protectionism to stimulate the economy, the pre-war trade level recovered in twelve years without the need to establish an empire, and Japan was still one of the world's most traded countries at the end of the century.

There are different opinions about the increase in Japanese trade in this period. Shimokawa states:

“Several reasons can be attributed to the success of the Japanese industry in international markets, including rises in the production scale, technical changes due to the introduction of low relative labor costs for automobiles and computers, and an increase in the technological level of the production of automotive parts.”
(Shimokawa , 1994 , pp. 8-9)

While Yamazawa(1990) claims that integration into the world economy by lifting trade borders, liberalization of the Japanese economy as well as efficient specialization is regarded as an explanatory factor for the growth of Japanese trade. On the other hand, Kosai (1988:54-55) claims that Japanese economic growth has been based on the nation's entrance to the international market. Therefore, we can clearly say that as the nation's economy gained greater competitive advantages in the manufacturing of various goods, Japan has gradually become part of international trade.

As I mentioned in the previous chapters, Japan's economic growth paradigm was centered on export-led growth which sought to boost the country's industrialization process by exporting goods for which the nation had a comparative price advantage. In this way, public funds and other forms of subsidies have been directed by the Japanese government to export industries in order to promote exports. Along with the export of products, enough foreign exchange was obtained to subsidize the entry of foreign machinery and technology to develop its own production system into large and competitive industrial sectors that were forged over time. The imports of this period were composed primarily of modern machinery and technology to establish new business activities, apart from agriculture, textiles, or steel, and increase productivity in order to increase exports further.

In Chapter 2, we have seen the rise of Japan's trade value over the entire period both in exports and imports even though there had been halts in 1957 and 1961 due to the economic challenges the nation faced. During these periods, in order to protect industries where Japan had a comparative edge on the international market such as the textile sector, the state intensively regulated foreign trade to discourage the import demand from the domestic market and to limit access to the competitive foreign goods. Nevertheless, the Japanese government not only eased the restrictions on critical energy sources, technology equipment, or raw materials but also promoted imports, providing various supports such as tax reductions. Many medium and small businesses have made significant improvements in technology and efficiency through new production techniques and investments, keeping pace

with the development of the economy of Japan as a whole. Japan, therefore, has transformed from having a trade deficit country to a trade surplus country.

Having said that, there are two essential factors that have contributed to changes in the Japanese production. First the economic support of the United States to Japan for the nation's reconstruction after the Second World War along with the special procurement by the U.S army. Second, after the War, the shape of the industries shifted. Industries such as cotton that relied entirely on raw material imports gradually decreased their shares, while the heavy and chemical industries, which relied less on imports, increased their share of production (Fujii,1962).

Although Japan secured its domestic industries, trade liberalization has served as a reliable catalyst for the private sector to increase its competitiveness and support the nation's global market exports. Seeing that we have seen how Japanese trade has grown over time, it would be helpful to take a look at the table below which goods were the most exported.

Table 4-3 Rates of Contribution to The Increase in Exports

	1953—56	1956—60
All commodities	100.0	100.0
Chemicals and heavy industrial goods	42.8	53.5
Chemicals	{ 4.5	{ 7.1
Metals	{ 9.5	{ 9.1
Metal manufactures	{ 3.0	{ 5.2
Machinery	{ 25.8	{ 32.2
Textiles	32.7	19.9
Others	24.5	26.6

Source: White Paper on Economy 1961 pp. 522-23

Before the Second World War, Japanese exports were mainly based on the textile, iron, and steel industries as well as foodstuffs which the nation had a considerable advantage. However, as the nation underwent a rapid reconstruction, Japanese exports have been linked to her productive mechanisms and her development in technology. This shows that the country has specialized in new high-investment industries, and while it has remained a technology importing country over the years, it has also been able to export new Japanese technology.

On the import side, Japan has always had to trade with the outside world in order to sustain its economy and industry due to the lack of raw materials. Ozaki (1967, p.175) notes that Japan depends 100% on the international supply of goods such as cotton, wool, and nickel. The Japanese miracle, as we have already covered in the second chapter, came to an end in the '70s, precisely because of the global oil crisis, which led to higher prices and costs. Here we can understand that Japanese dependence on the outside for the energy needs has triggered the end of tremendous economic growth.

Machinery importation also increases with the nation's economic growth, reinforcing the concept of an increasingly developed country where it is essential to obtain the latest technology in all sectors to sustain its competitiveness in international markets. Japan has thus achieved a scale like that of the major economic nations, which are both importers and exporters of machinery and technology based on a large secondary sector, so as not to lose competitiveness. By the 1970s, when Japan's rapid growth came to an end, the nation was already meeting Western economic powers with a huge trade surplus, having surpassed France, and approaching another major economic and commercial power such as Britain (Llamas,2014 pp. 77-78)

Table 4-4: Export and Import Ratios of Various Machines

(Import ratios in brackets)

	1955	1957	1959	1960
Sewing machines	98.4	82.8	72.9	60.3
Radio receivers	2.7	16.2	66.6	71.4
Bicycles	13.5	16.5	8.0	18.6
Optical instruments	57.2	44.2	52.6	65.3
Power-generating machines	8.4(22.1)	6.3(16.5)	4.6(18.4)	6.8 (9.1)
Machine tools	19.4(52.3)	4.7(44.7)	2.0(43.0)	3.6(43.6)
Metal-working machines	2.5(18.8)	3.2(16.7)	1.9(33.3)	2.8(21.1)
Ships	31.0	27.6	17.0	12.8
Railway vehicles	..	18.7	11.4	14.9
Motor cars	2.4 (3.1)	2.9 (1.6)	4.6 (1.0)	8.3 (3.5)
Total machinery*	10.0 (5.4)	11.1 (5.4)	10.0 (4.5)	8.2(3.6)

Source: Ministry of international Trade and Industry, *White Paper on Foreign Trade* pp 388-89

Before finalizing this section, we can see the complete protection of the Japanese state for its foreign trade as well as the structural transformation of the Japanese industry resulted in tremendous trade surpluses and capital accumulation. Thanks to the state's contribution to the export promotion and rise in international trade that encouraged product-specialization in Japan since the country's natural scarcity of especially raw materials required specialization in other areas to finance the imports needed for the economy aside from the effect it had on rapid growth.

4.4. The Financial System and Banking Sector

The Japanese financial system and banking sector are worth studying for the fact that they have given credit support to manufacturing industries which enabled the new investments of businesses on the imported machinery to promote the country's economic growth during the period of economic development of Japan. Many characteristics of the Japanese financial system were often distinct from those of other developed nations which

were structured to provide the required resources for high levels of investment in order to increase the competitiveness of domestic companies in the international market. According to Llamas (2014), the financial system has acted as an important support point for the economy since it was intricately connected to both the public and private sectors even though it suffered drastic changes under the U.S occupation which planned to disintegrate the banking concentration to restructure the system and set up separate commercial banks. With the aim of enhancing government economic policies, Japanese banks have strong relations with the Japanese Ministry of Finance and Bank of Japan as well as big businesses. As we have seen previously, the majority of Keiretsus was centered on a large bank that pooled the actions of the other companies and provided financial support for their operations. Therefore, their role as lender and shareholder had a direct effect on the Japanese economy to a great extent. These banks however depended highly on the Bank of Japan for liquidity which was enforcing monetary policies since most banks were private financial institutions.

The state has also engaged in financial matters by establishing the Development Bank of Japan, via which strategic industries were provided with economic support. The companies that were financially supported by the state were primarily the biggest ones that would belong to the Keiretsus. Yet again we can observe the close relationship between the state and private enterprises, especially through intermediate institutions facilitating decision making. The relationship between the Keiretsus and public institutions, which were comprised of manufacturers, banks, and exporters among several other businesses, encouraged the effective use of these supports in the industries that were more favorable to development. In this context, indirect funding and the main banking system have played an important role. The main banking system can be seen as a shareholding system in which the main bank not only provides the company with loans and other financial services but often has the company's shares and monitoring the activities of the company. In exchange, businesses use the bank for large transactions in which the bank receives commissions and profits. If the company gets into trouble, the main bank can even take over the control of the company (Hoshi,1993). Aoki (1990) suggests that this facilitates sustainable productivity and helps to lower operating risk by protecting the businesses from the rigors of the financial and

labor markets. The major explanation for corporate borrowing from the main bank in a long-term partnership is because the main bank, as a major shareholder, can maintain careful track about what's going on within the company, while largely minimizing knowledge and incentive issues. The benefit of lender supervision is essential to long-term entrepreneurial success (Frenkel, 1991).

As stated by Hoshi (1987), State financial institutions are guarantors, supporting not only targeted sectors but also banks and private banks have an influential role in shaping the state involvement in the economy.

4.5. What Should We Learn from the Japanese Miracle?

As we have discussed throughout this study, there are some important lessons to be drawn from the Japanese miracle for developing countries like Turkey to stimulate new growth. The essential lesson to be learned from the Japanese miracle is that well-designed systems and institutions play important role in promoting the efficient allocation of resources and stimulating economic growth. The Japanese experience has introduced several important national policy objectives to be followed if one wants to introduce and implement policies for successful economic growth. Therefore, the Japanese experience, regardless their cultural differences, can provide light and insights for the developing countries seeking new growth. The emphasis on the importance of the Japanese institutions, autonomous bureaucracy with its own set of economic policies and responsibility in pilot agencies, such as MITI's industrial policies, the virtuous cycle of high savings and high investment in creating and adopting new technologies, and increased labor engagement have been the key attributes of the Japanese high-growth period. Due to its accumulated wealth, highly trained employees, and a well-developed institutional framework, Japan had an immense capacity for growth.

National security under the U.S reduced the military expenses and enabled nation to focus on innovation and development policies for their industries by allocating its resources from military industry to manufacturing and service sectors. The economic situation, which was bolstered by macroeconomic stability, labor market flexibility, and strong economic

governance, all of which were aided by supportive legal and political institutions, stimulated production, high investment, and effective utilization of resources. The elimination of national security risks would no doubt assist and enable the developing countries to focus on innovation and development policies for their industries by allocating resources from the military industry to vital economic sectors as it has been the case in the Japanese experience. Perhaps in this context the developing nations need to establish strong alliances with major regional and/or international powers to provide national security till they developed sustainable economic structures and achieved industrial growth. In a context of globalization and greater economic integration in recent years, the connection between the economy and national security has become increasingly interlinked. These links represent both opportunities and potential threats for countries' national security. Recognizing this, economic security must emerge as an important strategic priority for the developing nations, with a link between economic security and broader national security. Corruption, fraud, and socio-economic inequality also represent risk vectors, which represent the means by which economic variables and events can affect critical infrastructure, industries and processes in ways that may also threaten national security.

Administrative guidance: economic and fiscal policies such as tax reductions, concessional loans and offering technical assistance to *strategic industries* provided by the Japanese government to finance major industries that have comparative advantage such as automotive, computer, and machinery to form an economy that is competitive and technologically advanced and are also export oriented. Therefore, developing nations should develop a technology and growth-oriented outlook in both public and private sectors. Important industries should be protected and supported by the governments under *industrial policy* through subsidies and tax breaks until they meet international standards in the quality of their productions and offer a competitive advantage on the market. The savings of the citizens should be encouraged by several incentives that promote *national savings* and channeling those savings into industries that have economies of scale. In addition, commitment of *export push strategy* needs to be realized for these industries to obtain influx of money for innovation and R&D purposes which leads to greater productivity.

CONCLUSION

Japan has become one of the world's most industrialized countries and the first non-western country to achieve full-scale industrialization in just a few decades since the ruins of WWII. From the early 50s through the 1970s, Japan underwent rapid development and industrialization supported by several factors such as industrial policy, institutions, and cultural values. Japan has also established impressive high-technology industries that have dedicated much of their efforts to further sustainable growth that led her to become the second-largest economy after the U.S in the late 1960s. Adapting Western practices has been seen as a prerequisite for catching up with and surpassing Western countries. In this way, the retention of traditional beliefs such as Confucianism and certain historical aspects went hand in hand with the phase of Westernization. The post-war era and the American occupation were perceived as pioneering shifts, creating completely new economic and social systems. On the other hand, the longevity of the preceding era regarding institutions, industrial policy, and bureaucrats remain intriguing. As a result, Japan could be regarded as a developmental state driven by its competent bureaucracy, which takes all necessary steps to achieve its agenda of industrialization in a largely autonomous manner.

As Japan was seen as the driver of the regional economy, the other East Asian nations have sought to imitate the transformation of Japan due to their attraction to Japanese advancement (Johnson, 1982, p. 90). Japan's developmentalism in the post-war decade and its strongly shaped characteristics by Japanese culture has proven acceptable for other Asian nations with distinct cultures from Japan and these characteristics can be perfectly modified. In fact, Japan's high growth success is not simply a post-war phenomenon because Japan was not a stereotypical underdeveloped nation and the rapid growth of Japan cannot be viewed as the advancement of a developing nation. On the opposite, before the Second World War, Japan possessed a significant industrial and military power while, in comparison to other major industrialized nations at the time, Japan showed some flashes of backwardness in terms of the capacity of technology. Therefore, Japan had maintained well-trained human

resources, economic and institutional structures from the pre-war years, enabling its economy to take advantage of the opportunities that were present to Japan after the war.

The historical evolution of Japan in the timeframe and the various influential variables on the economic growth that most scholars claimed have been studied but there is no definite consensus as to what led to such development by scholars such as Hayashi (1997), Kosai (1980), Johnson (1982) and Yoshikawa (1992). On the one hand, some scholars claim that this was partly due to the changes in the Japanese business structure, the reforms under the U.S occupation, or emphasize the importance of the Japanese institutions, autonomous bureaucracy with its own set of economic policies in pilot agencies, such as MITI's industrial policies. On the other hand, others claim that it was due to exogenous factors such as the balance of power between the United States and the Soviet Union provided an advantageous situation to Japan by Korean War Boom along with the U.S procurement program which helped the revival of Japanese economy, or they attempted to account for Japanese performance in terms of the country's cultural and religious characteristics. Japan's success in industrialization, according to this viewpoint, is due to its unique cultural and religious characteristics but it is exceedingly difficult to classify a single element as the only catalyst of high growth when all variables were interlinked. Nor does any consensus exist to determine the years when the Japanese miracle took place. Ito (1992) claims that since there is no high growth rate, the first five years aftermath of the Second World War are not part of the Japanese miracle, claiming that this growth took place with the beginning of the Korean War. However, many scholars including Ito consider the end of this growth took place in 1973 when the oil crisis began which caused a decline in the high growth rates.

As several scholars have stated, the virtuous cycle of high savings and high investment in creation, adoption of new technologies, and increased labor engagement have been the key attributes of the Japanese high-growth period. Due to its accumulated wealth, highly trained employees, and a well-developed institutional framework, Japan had an immense capacity for growth, and even though there are many factors contributing greatly

to the Japanese miracle, including the US support, zaibatsu breakup, the commitment of Japanese people and a variety of occupational reforms, such as land reform, labor reform, at the same moment it should be emphasized that the Japanese still had the potential to absorb the beneficial facets of these reforms since this potential was developed over the long history of the importation of foreign culture and technologies from both China and Western nations. However, it is the interventionist state that has played the pivotal role in the economic growth of Japan in the post-war era and Japan's leading role in East Asia through enforcing policies that comply with various goals to achieve economic success and 'catch up' with developed countries as a 'late-comer'. As outlined by Patrick and Rosovsky (1976):

" Catching up is very much a Japanese perception. It means Japan has no longer a definitive socioeconomic Western model to emulate. Catching up does not imply that Japan will henceforth become more inward-looking." (Patrick & Rosovsky, 1976, p. 162)

It's important to consider the economic situation in Japan after WWII. Due to a lack of natural resources, large population, capital shortages, and the need for trade ties, state intervention was needed for stability and high growth. While the role and instruments of the government have steadily changed in many respects, the role of the government has remained crucial. Economic growth could be facilitated by government initiatives paired with private-sector interests. In the 1950s, the government's industrial policy played a major role in changing Japan's industry from textiles to machinery. By driving Japan's economy through various channels, the government used all sorts of resources to accomplish the former motto of 'powerful economy and nation' rather than 'powerful army and nation' by following industrial policies. Unlike direct state intervention, administrative guidance, economic and fiscal policies such as tax reductions, concessional loans to strategic industries have been provided by the Japanese government to finance major industries that have comparative advantage such as automotive, computer, and machinery to form an economy that is competitive and technologically advanced. Household savings would be used to fund high-capital-accumulation activities since the consumption behavior of the Japanese differed from that of the West. Additionally, having a dual economy fulfilled two essential purposes. On

the one hand, for industrial growth, the agriculture sector offered the required labor supply, while putting little pressure on salary rates. On the other hand, the manufacturing sector benefited from a great deal of flexibility thanks to the subcontracting scheme. In addition, by stabilizing and rationalizing the key industries centered on the criterion of 'high growth capacity' even after the economy has regained its pre-war level, both the Japanese economy has dramatically recovered, and the leading role of the state in regulating the economy has strengthened. The state capability contributed to an economic force that was powerful enough to compete overseas.

Economies of scale have also helped the nation. Following World War II, large holding companies known as zaibatsu were dissolved into modern industrial business groupings known as keiretsu. The incorporation of smaller subcontractors and the organization of activities within the keiretsu groupings improved industrial productivity. Larger businesses were the most profitable, even though medium-sized and small businesses employed the majority of the country's workforce. Many industrial businesses merged to create bigger, more profitable businesses. These businesses devised growth-oriented strategies focused on gaining market share instead of making a quick profit, which led to their phenomenal success. Product diversification became an important component of many keiretsu's growth patterns, as they added plant and human resources ahead of demand.

Japan's institutional and financial framework has also been associated with high growth under the influence of Japanese cultural characteristics. Some of the unique cultural characteristics of the Japanese labor market for instance lifetime employment, company-based unionism, and incentive payment schemes were different from the Western model of the labor market. As a consequence of this scheme, relative equilibrium in the labor market has been maintained and the productivity of the labor improved since employees were perceived to be one of the owners of the business they worked for, and this workforce has been highly qualified and educated. Other unique Japanese characteristics in her industrial structure are Cross-shareholding and a division of ownership and management. Since they were resistant to shareholder pressure and hostile takeovers, these Japanese characteristics

offered enough incentives for businesses to concentrate on long-term initiatives and growth targets rather than short-term profit maximization policies. Moreover, when one company runs into trouble, other companies with cross-shareholding alliances with that company typically come to its assistance.

Industrial policies shaped by the government provided such stimuli to the private sector, such as easy access to financial services, tax cuts, and authorization of initiatives to import foreign technology or form joint ventures. These incentives and subsidies have established strong government-business cooperation in particular and provided Japanese companies the growth opportunities and to take part in international markets by competing with foreign companies. This trend resulted in high-speed economic growth by taking advantage of international trade because it has helped to enhance the nation's exports quickly enough to cover machinery and technology imports without going into debt.

Therefore, if we want to introduce policies for economic growth in countries with economic difficulties, just like Japan faced after the Second World War, we could seek answers from the Japanese experience given the difficulties of implementing them to completely different countries regardless of their cultural differences since Japanese experience has already given the requisite knowledge from which East Asian countries could benefit a great deal and how to formulate and successfully implement economic policies. East Asia has become the only region in the world to sustain substantial economic growth, and no other East Asian nation has fared better than Japan. Following Japan's success, many developing countries in East Asia sought to adopt a policy like Japan in the postwar period. In these nations like in Japan's case, the industrialization and transformation of industrial policy have been driven by the shift from low value-added to high value-added industries through high savings and investment together with the limited state interventions in resource allocation and subsidies toward strategic industries. As a result, East Asian countries' political and economic structures have tended to imitate those of Japan.

In conclusion, after conducting the study, I have concluded that Japanese state-led capitalism has done a great job of solving a variety of problems in order to achieve economic growth following WWII by enacting policies and measures which facilitated cooperation between government and industry that no other country could have implemented. It is obvious that without an efficient government, the Japanese people would not have been able to imitate and implement the skills, experience, and technology imported from the powerful Western nations to play a significant role in the achievement of the economic miracle. In addition, the global environment provided an impetus to Japan's economy that had never been seen before in any country in the world, which, when combined with endogenous factors that had been accumulating for more than three decades, managed to propel the Japanese economy to its peak in what has become known in literature as the Japanese economic miracle.

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