Economic Strength as a National Security Issue

Japanese Hypercorporatism. One crucial difference between the United States and Japan is that Japan is a country that holds government in high esteem, whereas the American public has a fundamental distrust of government. This difference is significant because, as many have pointed out, postwar Japan has become an economic superpower under the "administrative guidance" of the Ministry of International Trade and Industry (MITI), the government department whose function is to formulate and implement Japanese commercial and industrial policies. In order to rebuild a country that had been reduced to rubble during World War II, the Japanese government adopted policies that favored production and provided indirect
support to help producers maximize their market share. In contrast, a mature capitalist society like the United States tends to regard government intervention in the activities of producers as undesirable and favors policies that improve the well-being of the consumer. In an article in the Nihon Keizai Shimbun of September 17, 1990, I called this sort of Japanese capitalism "hypercorporatism" and the mature capitalism of North America and Europe "hyperconsumerism." To adopt the terminology of Alfred Chandler in Scale and Scope: The Dynamics of Industrial Capitalism, if the United States is a system of competitive managerial capitalism and Germany is a system of corporate managerial capitalism, then perhaps we might call Japan a state managerial capitalist system.

Spurred by the astonishing prosperity Japan has achieved, some American and European policymakers have begun to advocate a form of government-led capitalism that would provide support to corporations. The reaction in America to industrial policy, however, has been consistently negative. Although Washington has, in fact, stepped in to protect producers on numerous occasions, the American people have a deep-seated, almost physical, aversion to providing systematic protection for particular companies.

In Japan, however, although some of the glitter is gradually wearing off the hypercorporatist system, the Japanese people still have absolute trust in those in positions of authority. The reason everything in Japanese life converges on Tokyo is that that is where the okami—the higher powers—congregate and govern their subjects from a position that is above the law. Tokyo's ability to attract those who have an exclusive
hold on power and information is prodigious. The city is Washington and New York combined.

In America there is a clear distinction between the functions of those two cities: power is in the hands of the government in Washington; the private sector, based to a large extent but not exclusively in New York, controls information. Power itself is regarded as something that is entrusted by the people to political leaders and can be taken away from them at the first sign of any slip. Deep down Americans have little confidence in government. Mistrust of Washington is particularly deep-rooted among state governments.

This hostility to government is ingrained in the American people. Government service has little appeal for young people. Many of the most gifted undergraduates at American universities go on to pursue advanced degrees in graduate or professional schools; the second-best go to work for major corporations; few of the elite seem interested in a career in government. In contrast, the top graduates of Japan’s top university, the University of Tokyo, set their sights on passing the civil service examination and enter the government in droves. The American image of government is one of agencies squabbling with each other over money (a bigger share of the budget), and for that reason the government commands little respect. Recently, I must admit, similar feelings have been gaining ground among the Japanese as well.

In 1989 I had a conversation with a former vice-minister of MITI who asked me an extremely interesting question: “With all this talk about the American economy being on the decline and the United States falling behind in technology, why does the American
government stand idly by? Why doesn’t it do something? In Japan MITI would have taken action long ago.” Although one can understand the vice-minister’s perplexity, the United States makes a sharp distinction between the sphere of government and that of the private sector. No matter how frustrated the American government may feel, no matter how much authority it may have, the American people would not tolerate its interfering in private enterprise.

The only areas in which Washington can openly intervene and make policy decisions are those related to military matters and national security. Conversely speaking, if these areas can be used as justification, the government can get involved in anything it wishes. All it has to say is that national security is at stake and those who ordinarily would object will remain silent. National security is the “open sesame” that unlocks all doors. Setting aside what might be done behind the scenes, any top U.S. government official who openly attempts to give public support to a private company will immediately lose his job. What makes James Fallows’s proposal for containing Japan so difficult to adopt as a policy measure is that the U.S. government would have to support one corporation or industry over another in order to win the trade war with Japan. Washington, however, cannot openly propose special rules for private corporations.

What then is it to do? When the government chooses to give support to the private sector, it dreams up an excuse for doing so, namely, that such action is necessary for military reasons or in the interest of national security. Once an action can be justified on these grounds, anything is possible. Thus we have seen Fuji-
tsu prevented from buying Fairchild Camera and Instrument Corporation, the smashing of a Toshiba radio cassette player on the steps of the Capitol, and Washington’s blithe reversal of its own decisions about the FSX fighter support plane.

Exeuses for Japan-Bashing. Each of these incidents was justified on grounds that came close to pure fabrication. The reason given by the Commerce Department, the Defense Department, and the Congress for stopping Fujitsu from buying an 80-percent share of Fairchild in 1987 was that semiconductors are a strategic, high-tech product and that the takeover of a leading American semiconductor company by a foreign firm would pose a serious national security problem. Fairchild was a subsidiary of a French firm, however, and not an American company at all, to say nothing of the fact that Schlumberger, its French parent company, wanted to sell it because of management difficulties. Yet as soon as national security was invoked, the American government felt it could step in and call the deal off.

The Toshiba affair was also highly suspect. In 1985 the United States informed the Japanese government that Toshiba Machine Company, a subsidiary of Toshiba Corporation, had sold precision milling equipment to the Soviet Union in violation of COCOM, the coordinating committee for controlling East-West trade. This equipment, it was claimed, had made it possible for the USSR to reduce the noise of its submarines, thereby making them harder to detect. As a result, the United States had been forced to assume an additional defense burden of $30 billion. No cause-and-
effect relationship between Toshiba's milling equipment and the noise reduction was ever established, nor was any reliable source ever given for the $30-billion figure. Nevertheless, when the incident was made public in 1987, hawks in the Congress, under the banner of "national security," smashed a Toshiba radio cassette player with sledgehammers on the steps of the Capitol. A Norwegian company, Kongsberg Vaapenfabrikk, had also sold this kind of equipment to the Soviet Union, however, and Russian submarines had become quieter well before the sales by Toshiba Machine began. To put it bluntly, Japan was "had" by then Secretary of Defense Caspar Weinberger.

As for the FSX, Japan was forced to make humiliating concessions in its plans to develop the next generation of support fighters for the Japanese Air Self-Defense Force. By making the FSX into a political issue, America was able to indulge in as much Japan-bashing as it pleased.

Under pressure from Weinberger, in January 1988 Japan abandoned plans to develop its own fighter support plane and agreed to a joint U.S.–Japan development project. That November the two countries exchanged a memorandum of understanding to the effect that Japan would assume the entire cost of the project in exchange for American aviation technology. On January 29, 1989, however, the Washington Post carried an article by Clyde Prestowitz entitled "Giving Japan a Handout," which charged that America was giving away its airplane technology to Japan. Although an agreement had been reached the previous year with the Reagan administration and a memo of understanding had already been exchanged, the United States un-
reasonably demanded that the issue be reopened. The upshot was that America withdrew its promise to furnish "critical" jet engine technology, and the baffling decision was made that Japan was to unconditionally turn over to the United States the technology it had independently developed. At the heart of the issue was America's fear that if it provided Japan with technology, Japan would "beat the United States at its own game" and overtake America in aerospace and defense-related industries as it had in other areas. In the words of Newsweek (August 7, 1989), "For the first time, policymakers treated America's economic strength as a national-security issue."

Public hearings on the FSX project were held during the spring of 1989. American congressmen know nothing about Article 9 of the Japanese constitution that forever renounces "war as a sovereign right of the nation and the threat or use of force as a means of settling international disputes." They are equally ignorant of Japan's three principles on weapon exports, first promulgated by Prime Minister Eisaku Sato in 1967, that forbid the export of weapons to communist countries, to countries to which the United Nations prohibits the export of weapons, or to countries that currently are, or might become, involved in international conflict. The purpose of the hearings was to provide an opportunity for U.S. government officials to explain these and other issues and answer any questions.

As I watched the coverage of the hearings on C-SPAN, it was abundantly clear that trade matters and national security issues had become closely linked. The members of Congress bombarded the witnesses with questions. Secretary of Defense Richard Cheney was
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asked what would happen if Japan diverted the FSX technology the United States was to supply and sold it to the Soviet Union. Cheney replied that there was no cause for concern on that subject because of Japan’s peace constitution and its three principles on the export of weapons.

Almost before Cheney had finished answering, another congressman jumped in with the next question. Wasn’t it clear that Japan would steal our technology? Didn’t the Japanese pose a threat to the supremacy of the American aeronautics industry? Secretary of Commerce Robert Mosbacher answered that he too had been most concerned about that point so he had gone over everything more than once including the black boxing of the essential software. He assured his interlocutor that there was no need to worry. Other questions followed: 60 percent of the procurements were to be awarded to Japanese contractors and only 40 percent to Americans. If America supplied the technology, shouldn’t its share be 60 percent? The government’s reply was that the Japanese government was putting up all the money for the FSX. Under those circumstances, a 40-percent share for the United States was a “good deal.”

Two things became clear from the hearings. First, Cheney and Mosbacher pleaded Japan’s case with as much fervor as officials from Japan’s Ministry of International Trade and Industry might have done. The American departments of Defense and Commerce were clearly not at variance with MITI and the Japanese Self-Defense Agency on this matter; the problem lay with the U.S. Congress. Moreover, as is the case with politicians in other countries, these congressmen were poorly in-
formed. The fact that votes are more important than issues clearly holds true of legislators on both sides of the Pacific. Secondly, a clear link was forged between trade and national defense. This, of course, is a dangerous precedent because once economics and national defense are linked, Congress may be encouraged to indulge in Japan-bashing in other areas.

There was one amusing incident during these hearings. At one point the representative from Samoa raised his hand and said that he was very upset by the Japan-bashing he had been witnessing. Samoa, he said, had good relations with Japan, which was a valued friend. Some had said that Japan was unfair to foreigners, but one of his relatives, Mr. Konishiki, had just become the sumo champion. The hall erupted with laughter. A black Congressman immediately retorted that Mr. Konishiki might be well treated, but the Japanese were prejudiced against blacks. He was strongly opposed to the FSX deal for Japan because Japanese companies refuse to employ black workers.

As this exchange indicates, the FSX hearings were not limited to a discussion of the FSX. They provided a forum for statements for and against Japan, its fairness or unfairness, that extended ultimately even to matters of race. Although special broadcasts of the public hearings were carried live on cable television, the newspapers and the regular television news programs were highly selective in their coverage and constantly distorted the truth. Even the *New York Times* in an editorial on May 2, 1989, asked why Japan, with its enormous trade surplus, was insisting on developing its own plane rather than buying the F-16 from the United States. Needless to say, no one bothered to report
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Cheney's statement that the United States would receive approximately the same benefits from the FSX joint project as it would from selling the F-16, or that the F-16 is not necessarily suited to Japan given the country's limited land space and the vast extent of the territory it must defend. It is easy to understand why the American public, who knew none of the details of the FSX deal and read only patchy accounts of the proceedings, might be led to believe that Japan's development of the FSX posed some sort of a threat to the United States.

Without knowledge of this background, it would be impossible to understand why the appearance of a pirated translation of The Japan That Can Say "No" in the late summer and early fall of 1989 created such a furor in the United States.* For America the most important issue of all is national security. The Japan That Can Say "No" presented the perfect opportunity to play up that issue. American trade hawks took full advantage of Shintaro Ishihara's boasts about Japan's technological superiority and created a huge sensation. Having won the FSX battle, they now turned their attention to high-definition television technology, which Japan had the lead in developing, and attempted to link it too to national security. Thus, The Japan That Can

*The Japan That Can Say "No" was published in Japan in January 1989. Based on transcripts of talks given by Akio Morita, chairman of Sony Corporation, and Shintaro Ishihara, a member of the Diet for the supporters of the Liberal Democratic party (LDP), the book consists of five chapters by Morita and five by Ishihara. The authorized English translation, which was published in 1992, contains only the sections by Ishihara, because Morita withheld his consent to the project.
Say "No" provided America with a number of excuses for Japan-bashing. The book was a classic example of how Japan’s nationalistic rhetoric can play into the hands of its opponents on this side of the Pacific. It was a tragedy—a minus-sum game—a bad situation for both sides. By no means could it be characterized as zero-sum. Japan lost and so did the United States. When Akio Morita and Shintaro Ishihara, the book’s authors, first published the book, neither of them intended, or even suspected, that their book would cause such a stir. The situation was truly absurd.

The Japan That Can Say “No”

Rational and Irrational Policies. Economic policies have their rational and irrational sides. Some are based on reason; others are quite illogical. A glance at post-war America and Japan reveals that logical policies have coexisted with illogical ones in both countries. As far as trade is concerned, Japan’s economic policy is extremely rational. In order to expand exports, Japan has boosted competitiveness and offered large quantities of good products at low prices to the rest of the world while making every effort to economize at home and earn foreign currency. This eminently logical policy is Japan’s rational approach to foreign trade.

Japan’s domestic policies, on the other hand, have been extremely illogical. Good examples are the food control system and the distribution system, both of which reflect a built-in favoritism toward certain interest groups. Even without America making an issue of these policies, it is readily apparent that there is some-
thing strange about them. In these areas custom wins out over efficiency, and business is conducted in an opaque and ambiguous manner that international society finds incomprehensible. The rules of competition and all the other principles of modern economic theory simply do not apply.

Under the Staple Food Control Act, for instance, rice cannot be imported into Japan. This law serves both to protect Japanese farmers and to allow Japan to remain self-sufficient in its staple food (see chapter 4), but it also means that the Japanese consumer has to pay several times the world price for rice. A similar situation holds true with regard to the distribution network. Although European goods, for example, are sold at reasonable prices in the American marketplace, as soon as they enter Japan’s domestic market, they wind their way through mysterious channels and emerge bearing higher price tags than can be found anywhere else in the world. This is true of Burberry, Gucci, Louis Vuitton, and all the rest. Someone somewhere seems to be making an exorbitant profit, but who?

A country’s logical and illogical policies are what I like to think of as its “front door” versus its “back door.” If Japan’s logical trade policies are viewed as a front door, then its illogical domestic policies are its back door. Japan has kept its main entrance neat and clean for all to see, but its back door is a mess. When the United States finally became aware of this, it began complaining that Japan’s dirty domestic policies block America’s access to Japanese markets. Its demands for a back door that would give America easier access was what the 1989–90 U.S.–Japan Structural Impediments Initiative talks were all about.
The Japanese themselves, however, do not think their back door is messy or illogical at all. When America points out problem areas in Japan’s domestic policy, the Japanese response is “mind your own business.” The reason for these policies is the relative homogeneity of Japanese society. In a gemeinschaft society like Japan, where everyone has the same features and the same color skin and where lifestyles and patterns of behavior are similar, the most important policy is to prevent too great a gap from developing between rich and poor and to satisfy as many people as possible by creating a large middle class. To do so, Japan liberally protects farmers, maintaining price supports for rice and paying out subsidies to reduce the acreage under cultivation no matter how illogical these measures may be. It also protects mom-and-pop stores by limiting the size and number of new stores under the Large-Scale Store Law (see chapter 4) no matter how much this may violate the workings of market mechanisms. As a result, Japan has succeeded in creating a country with a population of more than 120 million people, all of whom belong to the middle class. What is wrong with that? Japan asks.

This type of reasoning is incomprehensible in the United States, however, which has a healthy consumers’ movement and an efficient market system based on the principle of offering quality products at reasonable prices. To return to our earlier metaphor, this is America’s front entrance, which it keeps neat and well swept. But America, too, has a back door, its foreign policy, the irrationality of which is particularly noticeable in the areas of diplomacy, national defense, and trade. For example, the United States regards the coun-
tries of Central America as its backyard. It sends its troops there whenever it pleases and has even arrested the leader of one country and forcibly carried him off to America to stand trial without thinking twice about it. It provides arms and money and abets antigovernment guerrillas in countries that are unfriendly to the United States and has no scruples about doing other things that most Japanese find equally shocking. No matter how illogical these acts seem to Japan, many Americans regard them as right and just and a reflection of American prestige. A foreign policy success in America has traditionally translated into a sudden rise in a president’s popularity ratings. According to a January 1990 Gallup poll, after General Manuel Noriega had been taken prisoner in Panama, President Bush’s approval rating soared to 80 percent. In March 1991, after the successful conclusion of the Gulf War, it reached an unprecedented 89 percent.

Thus both Japan and the United States have their logical and illogical sides. In Japan the logical side is the face it shows to the rest of the world; the illogical side is its domestic policies. In America the situation is just the opposite. Until recently this has worked very much to Japan’s advantage. Japan’s front door—exporting—has matched perfectly with America’s front door—domestic consumption. As a result, Japanese exports have expanded enormously, and U.S. consumers have been able to enjoy large quantities of high-quality, low-priced goods. Up till now Japan has also been lucky because America’s illogical side has not had much effect on Japan since it has been directed toward countries, the Soviet Union in particular, that have been ideological opponents of the American system.
The American attitude toward communism has long seemed quite irrational to outside observers. In the past, whenever news unfavorable to the Soviet Union was reported, the reaction was “See? Russia really is evil. We must fight communism.” This only caused anticommunist sentiment to escalate even further. Whenever I encountered instances of this irrational antipathy, I would think to myself, “The Soviet Union isn’t really as bad as all that. How frightening it would be if Japan were regarded in this way.” In 1989 these fears seemed about to materialize. Although Japan had managed to avoid provoking American wrath in areas involving U.S. national security or military affairs, during the mid to late 1980s the situation began to take an ominous turn. As the Soviet Union became less of a threat, America began to link economics with national security. Just as the USSR had been branded the “evil empire,” Japan was being branded as “unfair.” Whenever reports were published about bid rigging for construction projects or computer companies that submitted winning bids of one yen for long-term municipal contracts, a chorus of voices greeted the news with “See? Japan is unfair.” The result of tossing a book as inflammatory as *The Japan That Can Say “No”* into this potentially explosive atmosphere was all too clear.

Why The Japan That Can Say “No” *Provoked American Wrath*. When *The Japan That Can Say “No”* came out in Japan in January 1989, neither of its authors foresaw the controversy their comments would cause. After all, in the past, many critics had made statements similar to theirs with impunity. But in the early fall of 1989 problematic passages from the book were translated
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and distributed throughout the U.S. Congress. A pirated translation was subsequently circulated around the country via fax machines and electronic mail networks. Contributing to the book's notoriety was the fact that one of the authors, Akio Morita, chairman of Sony Corporation, is synonymous with "Japan Inc." and the other, Shintaro Ishihara, a member of the Diet for the Liberal Democratic party (LDP), was described as a prominent politician. It is not strange that congressmen as well as ordinary Americans, who know little about Japanese politics, might mistakenly believe that Ishihara was a politician of considerable stature in Japan. In fact, Ishihara was later compared to Richard Gephardt and Morita to Lee Iacocca. Since these two important people had made these statements against America, it was perhaps only natural for Americans to assume that all Japanese must think the same thing.

Some of the blame for the controversy lies with the Japanese publishing world, which has a predilection for cheap, sensationalist titles that, like tabloid headlines, seem to hint at some big scoop. The Japan That Can Say "No" is a clever title from a marketing point of view, but considering the harm it did to U.S.-Japanese relations, it was a little like killing the goose that laid the golden eggs. As in the case of James Fallows and "Containing Japan," for Morita and Ishihara too, the title of their book took on a significance of its own, quite independent of its contents, and caused all sorts of problems. To be sure, the book contained disquieting statements, but if it had been published under a different title, Proposals for U.S.-Japan Relations, for example, it would most likely not have provoked much of a reaction.

When the Morita-Ishihara book first created a stir in
When the Morita-Ishihara book first created a stir in the United States, Japanese misunderstood what the fuss was about and jumped to the conclusion that Americans were reacting to the book’s title. This provoked a backlash in the opposite direction. What was so wrong, Japanese asked, about Japan saying “no”? Does America have the right to expect Japan to do everything its way? What had upset America, however, was not the possibility that Japan might say “no.” In fact, the United States would greatly welcome a clear “yes” or “no” from Japan, instead of the vague, non-committal responses that Japanese officials are all too prone to make. A good case in point was the U.S.–Japan agreement in August 1991 to increase the foreign share of the Japanese semiconductor market to 20 percent by the end of 1992. When the goal was not reached by that date (it was, in fact, achieved in March 1993), the Japanese side responded that the 20-percent figure had been a target at which to aim, not a goal that they were committed to fulfill. This inability or unwillingness to give a definite answer has created a climate in which misunderstanding thrives and has driven America to complain that negotiating with Japan is somewhat akin to peeling an onion—responses are always piecemeal and one obstacle follows another ad infinitum. When Japan means “no” it should say “no,” and when it means “yes” it should say “yes.” America would have no serious objections to that.

The problem lies in what Japan might say “no” to. On issues related to America’s national defense and security, Japanese should be very cautious about even hinting, as Shintaro Ishihara did, that Japan might bypass the United States and enter into friendly relations
with the Soviet Union or that it might use its superior technology as a trump card in negotiating a trade deal. Statements in *The Japan That Can Say “No”*—such as “Japan’s technology has advanced so much, that Americans get hysterical”; or “If . . . Japan sold [computer] chips to the Soviet Union and stopped selling them to the United States, this would upset the entire military balance”—had the effect of salt rubbed into a wound with a scrubbing brush, and they inevitably provoked American rage.

Some may ask why it is wrong to tell America the truth. I would answer that it is not the whole truth. Although the technological strengths of the two countries are converging, comparisons of which country is ahead and which lags behind can be made only in certain areas. Japan may have outstripped the United States in these areas, but if it fails to grasp the full picture of America’s national strength, it is not seeing the forest for the trees. To say Japan should not be intimidated by the United States is all well and good, but no advantage whatsoever can be gained by worsening U.S.–Japan relations nor is there any need to annoy America simply for annoyance’s sake.

A striking example of the reaction the book provoked was the op-ed article that economist Lawrence Summers, a middle-of-the-roader who personifies American good sense, wrote for the *New York Times* (December 3, 1989) which began “Dear Mr. Morita and Mr. Ishihara”:

Most American economists, myself included, reflexively oppose any sort of policy proposal that interferes with free domestic and international markets. Your new book, “The Japan That Can Say ‘No,’” shakes my faith.... You both
make it clear that Japan’s strategy has not been one of maximizing the consumer’s gains from trade. . . . Instead, economically, financially and technologically, Japan has tried—and succeeded in—converting the Japanese-American relationship from one of Japanese dependence to one of mutual dependence. You make it all too clear that the risk, from an American viewpoint, is that before too long, the United States will depend heavily on Japan, but it will not be mutual.

Summers then went on to outline the steps he felt were needed to counter this perceived threat: saving more and investing more in America’s physical and human capital; supporting efforts to maintain a viable semiconductor industry to obviate “the risk posed by America’s dependence on a supplier of vital military parts whose leaders openly threaten a cutoff”; cultivating the newly industrialized economies of Asia; and aggressively confronting Japanese mercantilism.

Summers’s letter concluded:

I do not know what motivated you to write “The Japan That Can Say ‘No,’” but I am glad you did. You have helped remind an excessively complacent economics profession that some things like national security are more important than good jobs at good wages. And I suspect your America bashing may have made a stronger case for a new American policy toward Japan than any American ever could.

How should we interpret this profoundly ironic letter that reveals such a deep distrust of Japan? Lawrence Summers is one of the rising stars of American economics. He is also a well-respected figure in political circles, who served as economic adviser to Michael Dukakis during the 1988 presidential campaign and is currently undersecretary of the treasury for international affairs in the Clinton administration.
Summers has always avoided sensationalism and is noted for his sensible statements and calm, dispassionate manner. But the tone of his letter was that of a man seething with rage. As an acquaintance of his, I was profoundly shocked when I read what he had written. When it comes to matters of national security even sensible scholars like Summers share the national belief that money making should take a back seat to national security and that military matters must take precedence over economic concerns. Despite the strong temptation to sell Coca-Cola and Pepsi Cola to the Soviet Union, for years America denied economic logic on the grounds that such sales would boost the Soviet economy and affect U.S. national security. Now that Russia has relinquished its role as The Enemy, hamburger shops have opened in Moscow.

What would happen if Japan were to move into the position that Russia has vacated? No matter how inexpensive or well-made Japanese products might be, Americans, if they thought that enriching Japan would threaten their national security, would flatly repudiate economic principles. Such a backlash might well develop into a boycott against all Japanese products, not just those made by Sony and Toshiba. This sort of response is not confined to the United States alone, however. During World War II, Japan lived in an irrational world of its own, vilifying British and American “devils” and vowing to suppress all personal desires until after Japan had won the war.
The Secret of “Made in Japan”

National Security as “Public Good.” It is difficult to reach a political consensus in America, unless, as I have already noted, an action is justified on the grounds of national security. A closer examination of this proposition inevitably leads to the question “what is the role of government?” Since the days of Adam Smith and David Ricardo this question has been a subject of debate among economists. One of the answers that the various schools of thought on this issue have come up with is this: The role of government is service to the people.

Taxes are a means to this end, not an end in themselves. In Japan, nozei, the word that means paying taxes, still conjures up the image of taxes as something paid as tribute to a feudal overlord, but in America, where democracy has flourished since the country’s founding, the word taxpayer implies that taxes are paid by each individual citizen in return for services rendered by the state. In other words, the citizen who pays taxes is a customer to whom the government provides special services that cannot be provided by private enterprise. Because government services are meant for all the people, they cannot be the personal property of a particular individual. The government provides “public” goods and services.

One of the first people to popularize the expression “public goods” or “social goods” was Harvard professor emeritus Richard Musgrave in his book The Theory of Public Finance: A Study in Public Economics. Musgrave’s theory is based on the idea that there are “pub-
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lic wants” and “public goods” and that the government’s role is to fill public wants with goods and services. This theory is part of the mainstream of American thought on such matters and has provided an extremely important starting point for thinking about the activities of government. If it is not the role of government to provide private goods, then it logically follows that government should not support, or intervene in, private enterprise. When the U.S. government considers giving its support to something, the inevitable starting point for any discussion is whether a public good or a private good is involved. Thus America, unlike Japan, finds it difficult to adopt an industrial policy and, if forced to do so, must make some arbitrary connection with a public good such as national security. The Japanese government is not concerned about whether something is a public or a private good. Government agencies band together to protect the weak, rushing to the rescue of rice producers, coal mining, or the aluminum industry. This is a major difference between U.S. and Japanese concepts of government and government policy.

What precisely is the difference between a public good and a private good? A private good is one that a particular person pays for with the intention of making it personal property and thereby causing it to come under his or her private ownership. The very fact of ownership means that it cannot belong to anyone else. This is what is known as “the exclusion principle.” The goods to which this principle applies are private goods.

Conversely, public goods are those to which the exclusion principle does not apply, those which belong to all the people or which no amount of money can trans-
form into personal property. Thus, when the American government tries to adopt a policy, the exclusion principle has the potential to raise problems. A policy to which the exclusion principle does not apply is easy for Washington to justify as a public good, but it would have a hard time defending a policy to which this principle does apply, one that provides benefits only for the people who pay for it. The existence of the exclusion principle is a serious problem, the dimensions of which are hard for Japanese to conceive.

For these reasons, it is understandable that in the United States the most readily identifiable public good is national defense. Because defending the security of America is the single most important service the government provides, no American citizen can say "no" to it. This is the reason national security policies are enacted fairly easily. Industrial policies, however, encounter serious obstacles because industrial policy is an area where the exclusion principle is apt to operate.

The distinction between public and private goods also helps to account for the American reaction to *The Japan That Can Say "No."* If that book had limited itself to a discussion of industry and had not mentioned American defense, it probably would not have provoked much of a backlash in the United States, despite the caustic nature of its criticisms. By referring to a public good like defense, however, it made Americans' blood boil.

The negative reaction to the statements made by Shintaro Ishihara was clearly stronger than the response to what Akio Morita of Sony had to say. This was due to the fact that Morita's criticisms were about private goods whereas Ishihara's were about public
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goods. Morita made some scathing comments—Japanese companies look ten years ahead, U.S. companies ten minutes ahead; America claims to be a country that protects human rights but it lays off workers as soon as business is bad, and so forth. Since these barbs were directed at industry, however, Americans were willing to listen. Even if the comments rubbed them the wrong way, Americans could react rationally and say “well said” without any of Lawrence Summers’s irony. When it comes to such matters, the American sense of fair play clearly comes to the fore. But Ishihara’s criticisms touched on national security, and that’s a different ball game.

The Perception Gap over Defense. The concept of public goods can be used to shed some light on the true nature of the clash between the United States and Japan over defense. Back in 1981, then Prime Minister Zenko Suzuki announced that Japan would protect the commercial sea lanes up to a thousand nautical miles from Japan. This decision was made to ensure the free movement of vital imports, especially oil from the Persian Gulf. At the time, however, the United States was particularly concerned with the movement of Soviet submarines through the Sea of Japan on their way to the Pacific Ocean from their base at Vladivostok. As part of its military strategy vis-à-vis the Soviet Union, it wanted the Japanese to assume responsibility for their maritime self-defense. When relations between America and Japan began to deteriorate and disputes flared up in a wide variety of issues, the flames quickly spread to the area of defense. The United States claimed that Japan was enjoying a free ride under the
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U.S.–Japan security treaty. It was not paying its fair share but was pouring its energies instead into trade and money making.

Japan interpreted this criticism as merely an extension of the commercial frictions existing between the two countries—America, frustrated in the areas of investment and trade, was now finding fault with Japan in the area of defense. But this view is fundamentally mistaken. Keeping the sea lanes open is clearly an international public good and because the United States and Japan both share in the benefits, they should both contribute their share of the cost of protecting them. Similarly, the service provided under the U.S.–Japan security treaty is an international public good, and that fact naturally puts it in a different sphere than beef, oranges, automobiles, or VCRs. Although countries may bargain about public goods, such bargaining ought not to be construed as friction of the sort that arises in trade disputes over private goods.

Imagine a park, for example. This park is clearly a public good for the particular area in which it is located. No individual can make it his or her personal property, yet he or she and everyone else can use it freely without paying money. The park is, therefore, a public good to which the exclusion principle does not apply. When a park is being created at neighborhood expense, however, troubles may arise over how to allocate shares of the cost. If everyone were perfectly honest, there would be no difficulty, but human beings are fallible. Some will claim they are too poor to contribute; others that they have no children and thus won’t use the park. That is where bargaining comes in.

There are two ways to determine who pays what in
such a situation. The first is based on the ability to pay; the second is the benefit approach. Using the first approach, a wealthy person would be asked to pay one thousand dollars; a poor person would be asked for one hundred dollars. In the second scenario, a household with five children would pay five hundred dollars; a household with one child would pay one hundred dollars. Broadly speaking, these are the two methods for determining each person's share. But because there will always be holdouts or those who try to pass the responsibility on to others, some sort of bargaining is inevitable. Thus, there is an inherent weakness associated with the problem of determining who should provide public goods.

By contrast, when private goods are bought and become someone's property, the only potential problem is the ability to pay. There is no bargaining game as in the case of public goods, only endless friction over whether to buy or not buy, sell or not sell, and over who owes what to whom. Insofar as the U.S.-Japan security treaty is an international public good, bargaining about each side's share of the defense costs is only natural. When America says, "Japan is getting a free ride," Japan responds, "That's not true. Our peace constitution and three principles against exporting weapons bind us hand and foot so that we cannot move an inch. Instead, we will pay our share of the expenses for American troops in Japan and buy fighter planes." This is bargaining. It is intrinsic to any public good and must never be confused with trade disputes over exports. It is, therefore, a mistake to confuse public goods with private goods and interpret defense as just another area of friction between the United States and
Japan. Bargaining over defense issues will always exist regardless of whether or not there are trade disputes.

Looked at in this light, Japan’s $13-billion contribution to the Gulf War effort might be called its share in the costs of an international public good. The reason Americans were so annoyed by Japan’s dilatory response to the contribution question was their belief that, given Japan’s ability to pay and its role as a beneficiary of oil from the Persian Gulf, it should have been only natural for Japan to make an immediate decision to assume a large share of the costs.

During the Gulf War, even some Japanese began to have second thoughts about Japan’s parochial attitude toward foreign policy. If, as we saw in chapter 1, in a world of growing economic interdependence, it is impossible for one country to grow rich while others fail to prosper, it is becoming equally impossible to remain on the sidelines in international disputes. If the idea that there can be prosperity in one country without prosperity everywhere else reflects Japan’s egocentric attitudes toward economics and technology, then the belief that many Japanese seemed to have during the Gulf War that there could be peace in one country regardless of what was happening in the rest of the world reflects a similar egocentrism in foreign affairs. The Japanese government’s decision in the summer of 1992 to send members of the Self-Defense Force to Cambodia as part of a UN peace-keeping mission, the first Japanese troops to be sent abroad since World War II, seems to signal a greater willingness on the part of Japan to shoulder more of the military as well as the monetary burdens of the international public good.
Why Can't the United States Adopt an Industrial Policy?

Although, as we have seen, it is difficult for the American government to adopt policies that do not involve public goods, one should not conclude that Washington gives absolutely no support to private goods. Support to private companies would, of course, provoke a huge backlash from the American people, but the government spends vast sums of money on welfare and other areas that are not public goods per se, including Social Security, aid to individuals such as the elderly and the disabled, and aid for disadvantaged or minority groups. The failure of the Democratic party to win a presidential election during the 1980s is generally attributed to popular discontent over all the money spent on these causes during earlier Democratic administrations.

Why are the American people so generous? The answer can be traced back to the humanistic tradition of Western thought. America moves back and forth between the theory of public goods, on the one hand, and the ideals of humanism, on the other, sometimes mixing the two, sometimes keeping them completely separate. This is impossible for Japanese to understand. They find it strange that, despite all the complaints about the erosion of the American economy, the United States has made no effort to adopt a national industrial policy. They find it equally strange that when the Soviet Union refused to let Jews emigrate or the Chinese suppressed protests in Tiananmen Square, Americans were quick to complain about the infringement of human rights and the lack of regard for the individual in these countries, while doing nothing for
the homeless in their own land. Or at least that is how it looks to the Japanese.

In grossly oversimplified terms, the people who typify American humanism are the progressives, primarily Democrats, who advocate aiding the disadvantaged. Perhaps not surprisingly, one of the first projects Bill Clinton set in motion upon becoming president was an overhaul of the health care system. The conservatives, mainly Republicans, are supporters of the theory of public goods: They believe that while aid is a good thing, too much of it may deprive people of the will to work. These two concepts, or a combination thereof, take turns guiding American public policy. Corporate activities have no place in this scheme of things because they fall somewhere between the two. The Republican party is generally viewed as speaking for industry. For many Americans, however, industry has a bad image. It is seen as the source of pollution and as being interested only in making money. As a result, many people feel that its activities should be closely scrutinized. This is another reason America cannot adopt a strong industrial policy.

In Japan if something will help the country’s exports—be it a public good or a private good, defense related or consumer oriented—government, industry, and academia band together to develop the product and ship it out to markets around the world once it has been perfected. These groups cooperate because it is in the national interest of Japan to do so. From America’s perspective this Japanese brand of capitalism is quite “different.” Although both America and Japan are capitalist countries, the principles they are based upon are
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in fact very different: Water and oil are both liquids, but they are very different substances.

The classic example of Japanese industrial policy is the development of color television, which is often cited in courses at American business schools. As Christopher Freeman notes in his book *The Economics of Industrial Innovation*: “Japanese manufacturers were the first to introduce integrated circuit technology into the colour television industry (with the important economies in assembly labour that it involved). The success of this innovation was based on a joint research effort starting in 1966 and involving five television manufacturers, seven semiconductor manufacturers, four universities and two research institutes and the overall backing of MITI.” That is how things are “made in Japan.”

In America this sort of collaboration is inconceivable. Any such project would face two huge obstacles. Suppose, for example, that the American government decided to develop a new computer and called upon five large corporations to work on the project. Because the corporations would develop the computer with taxpayers’ money and would also receive other forms of financial assistance, they would probably be quite willing to participate. So far so good. But what would happen when they succeeded in developing the computer and reached the stage of unveiling the new product? Small and medium-sized companies, not to mention the other large companies that had not been asked to join the development group, would not stand idly by. Incensed that preferential treatment had been given to other companies, they would sue the government. After an enormous expenditure of time and money, the court
would render its verdict; high-ranking government officials would be fired; and the affair would become a huge scandal.

Even if this first obstacle could be overcome, the quality of the engineers who would be assembled for the project would pose a second stumbling block. In Japan the participating companies would commit their best engineers to such a project. In America the opposite would more than likely happen. The American companies would send only their second- or third-rate engineers because the ones to reap the benefit of the new technology would not be the companies but the individual engineers who participated in developing it. The engineers whose research and development efforts were successful would be free to quit their original employers and take the new technology with them, either to join a rival firm or to set up companies of their own. Because American companies cannot afford to let this happen, they would send their second- or third-rate engineers, and the chances of success would be pretty slim. Since any American joint development project can expect to encounter these two obstacles, the United States will never be able to adopt the kind of industrial policy that exists in Japan.

As long as the United States adheres to the two major principles of humanism and public goods, it cannot openly adopt an industrial policy. For America to set up an equivalent of MITI that would support private goods and favor producers over consumers would be even more out of the question. If Japan believes that the producer comes first, in America it is the consumer who comes first.

For these reasons, any industrial policy that the
United States adopts must somehow be involved with national defense or areas such as space, rockets, and aeronautic technology that are reflections of national prestige. The fact that industrial policy in America is limited to the sphere of public goods whereas industrial policy in Japan is free to cover private goods has unquestionably benefited Japan in the free-trade system and helped bring about America's decline. America's response has been twofold: first, the Structural Impediments Initiative, a list of over two hundred items that America presented to Japan with the demand that Japan play by the same rules; and, second, the threat to abolish the free-trade system and adopt a policy of managed trade. When all is said and done, however, the economic frictions between the United States and Japan are merely the discordant notes produced by a clash between two societies—one that bands together to give priority to the pursuit of money, the other that achieves unity through the pursuit of its own highest priority, power.

Why Japan's Industrial Policy Has Succeeded. In thinking about why Japan's industrial policy has been so successful, there is one other point to consider—the practice of targeting. A major factor contributing to success in any area, not just industrial policy, is having goals. Japan's industrial policy has succeeded because it has had clear goals and because Japanese industry, government, and academia have joined forces in an effort to achieve them. What has motivated the nation is that Japan is number two as a global economic power and has always been tempted by the possibility of becoming number one.
Japan has been given a goal for which it is innately suited—that of providing better goods more cheaply to the rest of the world. It has used the practice of targeting to its advantage in manufacturing color television sets, automobiles, VCRs, and a range of other products. To use the analogy of Richard Zeckhauser, my colleague at Harvard, the situation could be compared to a bicycle race. In a bicycle race it is extremely difficult for the lead rider to hang on to the number one spot. He can’t see the riders in back of him, and he receives the full brunt of the wind. The number two rider, following right behind, has it much easier. The most skillful riders, therefore, stick closely behind the lead rider and make a sprint to the finish.

In formulating a successful industrial policy, whether you are in the number one or number two spot makes an enormous difference. The conditions under which an industrial policy can operate effectively favor the country in the number two position and make it difficult for the leading country to even launch such a policy. If in the future Japan should ever actually become the world’s premier economic power, the industrial policy that it has been following would no longer work so well for one obvious reason: Japan will no longer be able to practice targeting.

For some time now Japanese companies have been targeting existing American products and manufacturing higher-quality versions. Japan has been particularly efficient about observing America’s failures so as to avoid making the same mistakes. If Japan were at the top, however, this strategy would no longer work. Targeting is much talked about these days. But even if America were to adopt an industrial policy like Japan’s
that involved private goods, since the United States is already number one, it would be hard pressed to know what to develop or how to develop it. Given such uncertain prospects, the government would have trouble justifying the use of taxpayers' money and thus would find it better to leave the whole thing to private enterprise. This sort of thinking makes adopting an industrial policy in the United States even more difficult. Perhaps that is the fate of being number one.

In Japan the situation is just the opposite. The risks are too great to entrust the matter to the private sector. The government must lend a helping hand. Moreover, the Japanese people are by no means opposed to big business. The technology that is developed with the government's help is made available to all companies. The objective is "Japan Inc." and exports. That is the advantage of being number two. As far as industrial policy is concerned, being number one is a tremendous handicap, and that is why America cannot make a bold initiative.