



A History of Japan's
Government-Business
Relationship

THE PASSENGER CAR INDUSTRY

Phyllis A. Genther

UNIVERSITY OF MICHIGAN
CENTER FOR JAPANESE STUDIES

A HISTORY OF JAPAN'S
GOVERNMENT-BUSINESS RELATIONSHIP

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The Passenger Car Industry

by

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Center for Japanese Studies
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PREFACE

Interdependence between the United States and Japan increases daily and with it concern over the relative economic role of each country during the 1990s. As a result, the two countries will remain high on each other's corporate and public policy agendas for the foreseeable future.

Concern increasingly is being expressed differently than in the past as the United States and Japan reach a new stage in their trade relationship. American domination of the relationship has ended, and overt Japanese tariff and nontariff barriers have been largely eliminated. The outstanding issues now revolve around deeper structural and cultural issues, including how industrial policies and government-business relationships affect global competitiveness and flexibility. At the beginning of the 1980s, it was the U.S.-Japan automobile crisis that presaged the new stage of bilateral trade relations by bringing the issue of industrial policy, and with it that of government-business relationships, to the forefront of the trade debate.

Despite the economic and political importance of the U.S.-Japan relationship and the extensive attention paid to automotive trade, few American scholars or policy makers are familiar with the history of Japanese government-business relations, either generally or for specific industries such as passenger cars. This book hopefully helps in a small way to fill that gap in our knowledge and, thus, to help strengthen the foundation from which we make public policy decisions about bilateral trade.

The few existing English-language books about the Japanese automobile industry contain little discussion of government-business relations. Japanese-language books contain even less. Michael Cusumano's book, *The Japanese Automobile Industry*, focuses primarily on the development of corporate strategies and technology. It is valuable in helping us understand how business positioned itself but tells us little about the formation of public policy. While C.S. Chang's study, *The Japanese Auto Industry and the U.S. Market*, briefly discusses certain policy actions, it contains no framework of how Japan arrived at decisions. In addition, it does not cover the important events of the American Occupation. Other

books such as William Duncan's *U.S.-Japan Automobile Diplomacy* and David Halberstam's *The Reckoning* provide useful information on particular aspects of the industry's history.

This book represents with some minor modifications my doctoral dissertation. I particularly acknowledge the support and guidance of Eleanor M. Hadley, to whom I owe the great majority of my knowledge about the Japanese economy. I am indebted to my other professors at George Washington University, especially Gaston Sigur and Benjamin Nimer, who helped oversee my dissertation. I also thank Takafusa Nakamura for sponsoring my study at the University of Tokyo and for allowing me to be part of his graduate seminar.

In addition, I am grateful for the support received from my friends and former colleagues at the Japan Economic Institute who generously allowed me the time necessary to pursue my doctorate and later provided needed workspace to write the original dissertation after I returned from Japan.

I also appreciate the generosity of many people in Japan who made my research possible: the Matsumoto and Takasaki families who allowed me to share their homes, Yoshio Nakamura and others at Keidanren, Kazuko Maekawa, Kyoko Nakamura, and Hiroshi Ando. Many individuals in the Japanese government, automobile industry, and academia willingly shared their time and knowledge with me.

My dissertation also could not have been completed without the support provided by a Fulbright Fellowship that funded my research in Japan. I am especially proud to have received one of the first two grants funded by the GARIOA/Fulbright Alumni Association of Japan. The Association for Asian Studies aided by providing a travel grant for research in Michigan.

CHAPTER 1

GOVERNMENT-BUSINESS RELATIONSHIPS IN GLOBAL COMPETITION

During the 1980s, American policy makers repeatedly raised the issue of the Japanese government-business relationship as part of the industrial policy debate. Some portrayed the relationship as more effective than that of the United States and stressed the Japanese government's ability to intervene in, and restructure, the economy. At the same time, other policy makers continued staunchly to defend the separation of government and business as the essential ingredient of a strong market economy. They claimed that Japanese industrial policies with their special government-business relationship have been ineffective at best and counterproductive at worst. These opposing perceptions were used to help to justify both interventionist and free trade policies in the United States. By doing so, a debate arose over whether or not certain government-business relationships can provide advantages in global competition by making public policies more effective and business more competitive.

This book examines the debate by investigating interactions between the Japanese government and the Japanese automobile industry from the industry's origins to the implementation of voluntary restraints on automobile exports to the United States in 1981. It starts with the premise that government-business relationships exist and are far more complex than usually depicted by those who attempt to use them either to justify or to counter government intervention. It defines the relationships as institutional structures within which states and private companies interact and work together, or fail to work together, to formulate and implement commercial policy. It finds that, while relationships differ across nations and across industries within nations, the need to define competition globally necessitates understanding how and why specific interactions occur.

The Japanese automobile industry's experience adds to our understanding of the role and competitive implications of

government-business relationships. This book sheds light on the effects of Japanese government and automobile industry interactions over time on Japanese economic development and thence on global competition.

The Automobile Industry

Although there are inherent limitations in using a single industry to understand Japanese government-business relations overall, it is only possible to understand these complex interactions when individual industries are studied in enough detail to create a broad base of knowledge. And, it is the discovery of interactive patterns in individual industries through which the nature of government-business relationships are revealed.

The Japanese automobile industry is important to investigate because it is central to American and Japanese manufacturing economies. As such, it exerts tremendous influence on both nations' economic health. In addition, automobiles and automotive parts have grown increasingly important in U.S.-Japan trade since the early 1960s and are currently the most important items, in monetary terms, in bilateral trade. The United States imported approximately \$33.7 billion of these products in 1989, which accounted for 68.7 percent of the \$49 billion U.S. trade deficit with Japan.¹ Thus, the automotive industry also exerts a tremendous influence on the health of the U.S.-Japan bilateral trade relationship.

Another reason to investigate government-business relations in the Japanese automobile industry is this issue's close ties to the U.S. debate over industrial policy. Although *The Economist* broached the industrial policy issue as early as 1962 in a series of articles and some Japan specialists studied it, the issue did not become popular in the United States until the time of the automobile crisis in 1979.²

Industrial policy became a trade issue at the time of the automobile crisis in large part because of the existing hostile relationship between the U.S. automobile industry and the press—and thus consumers—that grew out of earlier conflicts over safety and emissions standards.³ Automobiles are also visible consumer products that create feelings of economic vulnerability that earlier conflicts over textiles and steel had not. The importance of the automobile industry to the economy and the mystique that makes

the industry the ultimate symbol of American capitalism added to the depth of the shock. It was reasoned that, if the automobile industry was in trouble, perhaps something more was wrong than simply the unfair trade practices of other nations; maybe the American system needed to be revamped.

The concept of industrial policy that initially emerged out of the automobile crisis focused on what was seen as one of the elements of Japan's success—the existence of a close, cooperative government-business relationship that led to increased competitiveness through judicious use of public policies. An immediate result of the new perception was the Carter Administration's attempt to set up a tripartite committee between government, business, and labor in 1980 to address the U.S.-Japan automobile trade issue. Exemplifying an introspective use of the concept, attempts such as this sought the basis for the U.S. automobile industry's lack of competitiveness within the U.S. economy, and a number of articles, books, and conferences on learning from Japan were published. While this perception of Japanese industrial policy has not disappeared, it has been supplemented by the negative connotations applied to industrial targeting.⁴

The targeting argument was a new basis for blaming trade problems on factors outside the United States and for protecting its market. In the industrial policy context, it rejected introspection and returned to the more conventional view that the major source of U.S. trade problems was external. Despite this fundamental difference, the targeting argument also assumed that cooperative and state-directed government-business relationships in Japan affected international competitiveness. For example, the "successful targeting" of the Japanese automobile industry was seen as reason enough to impose import restrictions on U.S.-Japan automotive trade. At a hearing before the House Subcommittee on Trade in March 1980, Chairman Charles Vanik stated:

Japan has a great auto industry and it grew to strength and prosperity behind some of the most protectionist walls in modern industrial history.

Now, the industry has been unleashed; it is surging all over the world, wrecking havoc on our industry which for fifty years has been totally supportive of world trade.⁵

At the same hearing, Douglas A. Fraser, president of the United Auto Workers union at the time, after quoting George Ball that Japanese trade responds to government decisions and not simply to

the decisions of industry, stated, "Unfortunately, our auto industry must also be included in the list of industries 'incisively targeted' by Japan."⁶ Although first gaining prominence in U.S. trade policy during the debate on U.S.-Japan automobile trade, the targeting concept was refined and used again quite effectively in later debates over machine tool, semiconductor, computer, and other sectoral issues.

A third reason the Japanese automobile industry's case is particularly provocative and instructive from a policy perspective is that it has become an example of an industry that reveals the effectiveness as well as the ineffectiveness of Japanese industrial policy.

One side argues that government-business interactions in the Japanese automobile industry are characterized by an adversarial relationship and the triumph of the private market.⁷ The automobile industry in Japan did receive much less government attention, especially financial, than other industries such as steel. Automobiles are the consummate consumer good in a society that values saving more than spending, and the industry does have many exemplary entrepreneurs such as Shoichiro Honda. In addition, the industry's experience in the 1960s has been used as the prime example of the triumph of the private market over the attempts by the Japanese Ministry of International Trade and Industry (MITI) to change Japan's industrial structure.

The other side cites the Japanese government's successful targeting and protection of the automobile industry as the prime reason for the industry's postwar success. The government had forced the American automobile companies out of the market in the 1930s through extensive restrictions. After World War II the automobile industry was identified as a key industry by the Japanese government. In the 1950s and 1960s the Japanese government carefully controlled technology inflow and foreign direct investment to try to influence the character of the industry. These factors support the primacy of the government, not of the market, in economic development.

It has been possible to use this government-business relationship to support opposing positions in the trade debate and in analyses of the role of industrial policy in Japanese economic development precisely because interactions in the Japanese automobile industry reflect so many different patterns. Thus, it is possible to understand government-business relations only as complex interactions between government and business and not primarily as the ability of government to influence business or the ability of business to resist government intervention.

For these three reasons, the automobile industry is a prime example of how the issue of government-business relations is used in the U.S.-Japan trade debates and, further, how industrial policy and government-business relations became one and the same issue in the minds of many policy makers.

Perspectives on Government-Business Relationships

The differing perceptions about industrial policy and the role of government-business interactions are rooted in the way we analyze the nature and role of the international, American, and Japanese economies. These analyses provide a foundation from which to explore the complex interactions between the Japanese government and the Japanese automobile industry. They approach the issue from several different perspectives, each of which contributes to our understanding.

Since the late 1960s, awareness of international economic issues has increased substantially among American scholars and policy makers. Attention focused first on how the activities of global actors, such as multinational corporations and regional economic associations, affected the power of nations. For example, writers argued over whether there was a newly emerging phenomena of economic interdependence that might partially supplant the nation-state.⁸ A few writers pointed out that the economic issues always existed; awareness had simply increased. Yet, there was an implicit assumption by most policy makers that economic issues were important because they affected political relationships. In the study of international relations, economic issues were not assigned the same importance in and of themselves as were political and defense issues. This assumption has been accepted by many scholars and policy makers and has reemerged in discussions over appropriate trade policies and the weight that should be given to economic versus political considerations in relationships between nations.

As a result, policy makers paid little attention to how interactions between government and business within nations affected global trade competition or to how the international economy in turn affected such interactions. There was little recognition that such interactions changed over time or of the factors that led to change.

When attention did turn to these interactions during the industrial policy debate, another conceptual problem arose. Many

scholars were unable to separate their study of government-business relationships in global competition from their preferences concerning the role of the government in the American economy. Many studies sought proof of existing preferences rather than looking at how and why interactions occurred in Japan at different times. Again, these studies dealt primarily with the ability of government to influence business or the ability of business to resist government intervention.

The Domestic Perspective

Scholars who study American government-business relations often refer to the relationship as a static condition facilitating or hindering economic development by positing a fundamentally adversarial relationship in the United States versus a cooperative relationship in Japan.⁹ These scholars tend to transfer the way the relationship is dealt with as a domestic issue—primarily as the effect of regulatory policies on the economy—to the international arena. Since regulatory relationships involve the imposition of costs to achieve social goals or to control undesirable behavior, the studies do not have the tools to analyze instances of mutual cooperation. They are helpful in looking at interactions that occur when legislated regulatory solutions to social problems exist by pointing out that such interactions tend to be adversarial.

In depicting U.S. government-business relations as adversarial, scholars almost exclusively discuss interactions as effects of the domestic environment—legislation, culture, and historical experience. This perception leads them to trade policy options that stress that if weaknesses resulting from domestic, social, and technological changes are resolved, American businesses would be competitive and as such would resolve any international trade problems.

Because of the emphasis on the domestic environment, some of these scholars discount the relevance of comparative studies of government-business relations in foreign countries altogether. Michael Blumenthal stated:

A comparative study of business-government relationships in other countries is a fascinating field of study, but I doubt that many insights useful in the United States could be derived from it. Whether one considers Japan, or France, or another nation, the business-government

relationships are part of the total fabric of their societies. They reflect their own histories, philosophies, and social structures, and would not be a guide to action in the United States.¹⁰

This perception reflects a weakness in using concepts developed in studies of American government-business relations to study the effect of such relationships in trade because they ignore the impact of the international environment and disregard relevant experiences in foreign countries.

Thus, while the traditional approach to studies of American government-business relations does shed light on regulatory interactions, it is not suitable by itself to a study of the role of government-business relations in international trade. It is limited in its ability to incorporate variables external to the domestic environment and to deal with other than regulatory policies. It shows that interactions can be adversarial but fails to discuss instances of cooperation or the existence of mutual goals. It also assumes an idealized *laissez-faire* environment with static relationships that do not change over time.

The Japan Perspective

Scholars have discussed government-business relations in the context of U.S.-Japan relations. For the purpose of examining and simplifying concepts that help to understand government-business interactions, these studies fall into three basic groups. The first group views the relationship as a reflection of cultural and historical factors. The second group concentrates on the concept of industrial policy and the role government plays in economic growth. The third group looks at Japanese government-business relations as an interactive partnership.

Historical and cultural determinants. Studies in the first group describe the relationship as the “missing element” that explains Japan’s postwar economic performance.¹¹ They stress the “special and unique way in which the Japanese government has guided the economy’s development,” a way influenced by Japan’s history and culture.¹²

Historically, it is the close communication between the government and the business community that these writers believe has existed since the Meiji era (1868–1912). Because Japan was forced to open its market, it had to design policies to achieve the rapid and

forced growth of industry to avoid being partitioned like China. Thus, the unique relationship between government and business—a special coalition between the bureaucracy and the private sector—grew out of the Meiji government's attempts to foster modern industry through various subsidies such as the sell-off of government factories.

The cultural elements stem from Confucianism and native traditions. They often are behind references to “consensual decision making,” the “group spirit,” or “the vertical society.”¹³ In the context of government-business relations, this view implies that Japanese leaders are conditioned by their culture to preserve harmony in their relations, as for example in the postwar practice of consensual decision making, *ringi sei*. It also implies that horizontal mergers are difficult to achieve because they go against cultural predispositions toward vertical relationships and group cohesiveness.

This group of studies, like the studies of American government-business relations, provides only a partial insight into government-business interactions as a trade issue, but policy makers are guided to some extent by cultural norms and historical experiences. These factors offer insights into such practices as the formation of coalitions, provide policy makers with historical lessons, and remind us that culture can affect how events and concepts are perceived. But, if cultural and historical contexts are the primary shapers of the government-business relationship, we would expect the relationship to change quite slowly and we would be able to explain all current behavior as extensions of some previous patterns. These patterns, however, are often overridden by other considerations.

Industrial policy perspective. This category of study examines the Japanese government-business relationship within the context of industrial policy and the role of government policy in economic development. It asks whether government or business is primarily responsible for Japan's rapid economic development. This category includes two perspectives; one supports the supremacy of the state, the other the importance of the market.

The statist perspective often presents political institutions, such as MITI, as the primary determinants of the government-business relationship.¹⁴ Proponents of this point of view attribute a large role to the state in economic development and see a world “in which bureaucrats wield exceptional power and influence.”¹⁵ Some want the United States to learn from the Japanese government's perceived success in facilitating development; others use the concept

as justification for an activist U.S. trade policy to offset the effects on world trade caused by the intervention of the Japanese state.¹⁶

Political institutions can help predispose a relationship to be cooperative or adversarial and can place constraints on business actions. As such, they offer insights into how the government perceives and attempts to carry out its role in economic development. However, these studies often fail to pay sufficient attention to the actions and initiatives of the private sector and so fail to fully account for variations in government-business relationships across industrial sectors and for instances in which public policies fail to achieve their stated purposes.

Advocates of the market perspective depict political institutions as playing only a small role in promoting economic development.¹⁷ Their studies correctly point out the existence of a strong private sector in Japan and the developmental effects of competition. They stress that Japan's economic development resulted from a free market typified by intense competition and successful entrepreneurs and cite instances where the Japanese government failed to impose its ideas on business. In this context, the only legitimate government roles are the creation of a macroeconomic environment conducive to business and the imposition of regulations to achieve social goals. However, in their attempt to demonstrate the supremacy of the private sector, they discount the role of states, and thus the importance of government-business interactions in shaping economic development.

The separation of politics and economics reflects an academic tradition dating to eighteenth-century classical economic theories and to late nineteenth-century neoclassical economists such as Alfred Marshall.¹⁸ Theorists separated the two disciplines by arguing that while economics is a system based on production, distribution, and consumption that operates under natural laws, politics is a system of power, influence, and public decision making that disrupts natural laws but is necessary to provide essential services such as defense. Therefore, the disruptive influence of government should be excluded from the harmonious economy. This underlying assumption obviously hinders the study of government-business interactions by imposing an ideal in which there is as little interaction as possible.

Interaction perspective. This group looks at interactions between government and business over a period of time. Richard Samuels terms this interaction "the politics of reciprocal consent," in which a partnership exists in a constant state of negotiation and renegotiation.¹⁹ Yasusuke Murakami's theory of compartmentalized

competition recognizes interactions between “the economy, the polity and the culture” in creating economic development during Japan’s high growth period.²⁰

Two other studies employ an interactionist perspective. David Friedman’s case study of the Japanese machine tool industry, while centering on flexible manufacturing and the role of small-scale firms in Japan, defines political economy broadly. He states that “politics is much more than just the actions of the state” and records instances of political conflict and compromise among government, business, and other affected actors.²¹ Frank Upham discusses attributes conducive to cooperative Japanese government-business relations that include a consultative policy-making process.²²

These studies record instances of government and private initiatives that result in market transformations but try not to presuppose the supremacy of the state or the market. They rely heavily on a detailed knowledge of interest group interactions within specific industries. They propose that no monolithic government or business exists; rather there are many players and levels of interaction. Because a detailed knowledge of each industry is necessary, these studies sometimes are dismissed as presenting concepts that are unique to a specific industry and not transferable to others or to economic development in general.

By looking at specific case studies, however, they do delineate factors that place constraints on, or encourage, interaction. They recognize that no single factor, such as culture or the market, can explain fully either the interactions themselves or economic development. They also indirectly imply that changing circumstances can alter both the interactions themselves and the role of individual factors in determining outcomes. Thus, the case studies taken together provide a framework within which to analyze interactions.

This book complements the third group of studies by adding a case study of government-business relations in the Japanese auto industry to previous work on other Japanese industries, including energy, machine tools, and textiles.²³ It attempts to systematically present the circumstances in the automobile industry that surrounded public policy actions. By doing so, it finds that Japanese government-business relations in the case of the automobile industry were interactive, that government and private initiatives existed, and that relations changed with variations in needs and the external environment.

The changes in and the types of interactions depended on several major factors, which will be discussed further in the conclusion and which are revealed in the history of the relationship from

its origins to the 1980s. These factors are (1) cultural and historical lessons that influenced the behavior and decisions of policy makers; (2) administrative rules, the perimeters agreed to by consensus or imposed by force within which the government made and carried out policy; (3) the competitiveness of an industry; and (4) the importance, real or perceived, of an industry to economic development.

Conclusion

As international economic policy is accorded a significance equal to political and security policies, policy makers must step back and come to terms with how interactions between government and business affect the strength and competitiveness of nations.

This book seeks insights into government-business relations as interactions, and thence as possible factors in economic development. As new nations emerge and challenge the supremacy of older industrialized countries in technology-intensive products, perceived differences in government-business relationships and their roles in economic development have become an important aspect of the trade debate that rarely has been examined. Because policy makers frequently use these perceived differences to support domestic industrial policies and to justify protectionist or free trade actions, it is essential to examine and to understand the realities involved. The realities in turn help determine how and if the Japanese government-business relationship is relevant for other nations' economic development policies and what role, if any, it should play in trade policy.

NOTES

¹U.S. Department of Commerce.

²"How Japan Does It," *The Economist*, 24 March 1962, pp. 1,140-41 and 31 March 1962, pp. 1,261-62.

³An unpublished review by this author of auto-related articles from approximately twenty-five U.S. newspapers for the first six months of 1980 revealed that the American press, particularly editorial writers, took an antagonistic position toward the U.S. auto industry. These articles frequently cited safety problems with the

Ford Pinto and GM Corvair, the Chrysler bailout, and the industry's lack of response to pollution and fuel efficiency problems as evidence that problems in the U.S. industry were internally generated.

⁴The industrial targeting debate can be symbolically traced to the December 1981 publication of "Japan's Ominous Chip Victory," in *Fortune*. One of the industry's most polished espousals of the targeting argument is the Semiconductor Industry Association's publication, *The Effects of Japanese Government Targeting on World Semiconductor Competition*, released in February 1983.

⁵U.S. Congress, House Subcommittee on Trade, *Hearings, World Auto Trade: Current Trends and Structural Problems*, 96th Cong., 2nd sess., March 1980, (Serial 96-78), p. 2.

⁶*Ibid.*

⁷For example, see Philip Tresize, "Politics, Government and Economic Growth in Japan," in *Asia's New Giant*, ed. Hugh Patrick and Henry Rosovsky (Washington: The Brookings Institution, 1976), pp. 753-811.

⁸For example, see George Modelski, *Principles of World Politics* (New York: The Free Press, 1972).

⁹For example, see Alfred A. Marcus, *The Adversary Economy* (Westport, CT: Quorum Books, 1982); Damodar Gujarati, *Government and Business* (New York: McGraw-Hill, 1984); and Neil H. Jacoby, ed., *The Business-Government Relationship* (Pacific Palisades, CA: Goodyear Publishing Company, 1975).

¹⁰Jacoby, ed., *The Business-Government Relationship*, p. 162.

¹¹U.S. Department of Commerce, *Japan, The Government-Business Relationship*, ed. Eugene J. Kaplan (Washington: Government Printing Office, February 1972) and case studies prepared by the Boston Consulting Group.

¹²*Ibid.*

¹³For example, see Chie Nakane, *Japanese Society* (Berkeley: University of California Press, 1970); Ronald Dore, *British Factory-Japanese Factory* (Berkeley: University of California Press, 1973); and Robert Bellah, *Tokugawa Religion* (Glencoe, IL: Free Press, 1957).

¹⁴For example, see Chalmers Johnson, *MITI and the Japanese Miracle* (Stanford: Stanford University Press, 1982).

¹⁵David Halberstam, *The Reckoning* (New York: William Morrow and Company, 1986), p. 27.

¹⁶For example, see Ezra F. Vogel, *Japan as Number One* (Cambridge: Harvard University Press, 1979) and Ira C. Magaziner

and Robert B. Reich, *Minding America's Business* (New York: Harcourt Brace Jovanovich: *Law and Business*, 1982).

¹⁷Toshimasa Tsuruta, *Sengo Nihon no sangyo seisaku* [Japan's postwar industrial policy] (Tokyo: Nihon Keizai Shimbun Sha, 1982), pp. 1-287.

¹⁸Many liberal economists, who espoused the preeminence of the market mechanism and price competition, trace their ideas to the work of the British philosopher, John Stuart Mill. Mill emphasized the primary value of liberty [individualized choice]. Therefore, he preached that the power of government in any form should be minimized, stating that "laissez-faire should be the general practice; every departure from it, unless required by some greater good, is a certain evil" (idem, *Principles of Political Economy* [London, 1864], p. 569).

¹⁹Richard J. Samuels, *The Business of the Japanese State* (Ithaca: Cornell University Press, 1987), pp. 1-290.

²⁰Yasusuke Murakami, "Sengo Nihon no keizai shishutemu" [Japan's postwar economic system], *Economisuto*, 14 June 1982, pp. 38-54 and Yasusuke Murakami, "Toward a Socioinstitutional Explanation of Japan's Economic Performance" in *Policy and Trade Issues of the Japanese Economy*, ed. Kozo Yamamura (Seattle: University of Washington Press, 1982), pp. 3-46.

²¹David Friedman, *The Misunderstood Miracle* (Ithaca: Cornell University Press, 1988), pp. 201-27.

²²Frank K. Upham, *Law and Social Change in Postwar Japan* (Cambridge: Harvard University Press, 1987), pp. 164-204.

²³For examples of case studies see Samuels, *The Business of the Japanese State*; U.S. Department of Commerce, *Japan, The Government-Business Relationship*; and Daniel I. Okimoto, Takuo Sugano, and Franklin B. Weinstein, eds., *Competitive Edge* (Stanford: Stanford University Press, 1984).

CHAPTER 2

THE INDUSTRY'S EARLY YEARS

Origins

The Meiji Era

After the Meiji Restoration in 1868, Japan underwent a profound transition caused by industrialization and internationalization, trends that stemmed from changes within Japan and from fear of Western domination. The changes affected all aspects of Japanese society, including government-business relations.¹

The Meiji government felt compelled to design and implement policies to achieve the rapid and forced growth of industry in order to avoid domination by Western powers. Beginning in the 1870s, it implemented the *shokusan kogyo* (develop industry and promote enterprise) policies that centered on development of a national banking system; infrastructure investment in railroad, postal, and telegraph networks; the sale of publicly built factories; and the lending and sale of equipment to the private sector.² These policies resulted in a short period of direct government ownership and control of business and, after the early 1880s, in a special partnership between the bureaucracy and the developing *zaibatsu*. Many reasons have been posited for the development of the partnership.

William Lockwood states that as the influence of the *zaibatsu* rose, they became makers of national policy along with the military, bureaucrats, and politicians.³ By the 1930s, the government and the *zaibatsu* were so closely affiliated that it was difficult to tell where one left off and the other began.

While the *zaibatsu* gained increasing power, they never attained a decisive position in prewar Japanese politics because they disagreed among themselves. Until the imposition of military controls in the 1930s, the government also did not hold a decisive position and was dependent upon its relationship with business. Lockwood writes: "When the national government stepped in

with its financial resources or its coercive powers it was more as a protector or partner of large-scale business than as a policeman or competitor."⁴

G.C. Allen also depicts the relationship as growing out of security needs. While Allen presents a stronger role for government than does Lockwood, both stress the development of a government-business partnership.

Moreover, she (Japan) feared for her security, and her leaders could not neglect the strategic aspect of economic development. Hence the active part played by the State in the early and middle years of Meiji in the founding of new industries; hence the continued concern of the Government and of the business families through which it worked with enterprises that touched on national power.⁵

Johannes Hirschmeier presents another theory as to why a government-business partnership developed.⁶ He stresses that relationships in Japan are culturally determined. He believes there is a lack of individualism in Japanese business that arose from traditional cultural values. He states that a vertical value order (individual-family-emperor) combined with groupism (individual-firm-nation) to make economic leaders and commercial activities susceptible to government leadership.

In yet another view, Keiichiro Nakagawa believes that the partnership developed primarily because of a "peculiar foreign trade situation," the inability to charge import duties higher than 5 percent because of unequal treaties imposed by Western powers.⁷ He states that "in Japan, the government had no authority to intervene in foreign trade, and thus freely engaged in [domestic] activities promoting and regulating private industrial enterprises."

None of these explanations can fully explain the partnership. The government-business relationship in the Meiji period evolved because of both culture and the existing environment. Existing cultural values gave strength to a partnership that evolved in reaction to a strong international threat and the need for industrialization. The domestic environment continued to create pressures on the relationship as it evolved and changed.

The central partnership and the experiences it grew out of had little direct effect on most companies. The government-business partnership was most active in heavy industries such as steel and shipbuilding. Light industries and new sectors, such as the automobile industry, were developed by private entrepreneurs

without much government involvement because they had no direct relationship to national security.⁸

Until the 1930s, relations between the automobile industry and the government fell into this category. As a result, the government paid no attention to the fledgling automobile industry as part of its industrial promotion efforts. The industry's production was so small that no potential contribution to the industrial base was apparent. Cars seemed to be only toys for the rich. Yet, indirectly, the growing industrial base did provide a foundation of entrepreneurial and technological skills for early efforts to create a motor vehicle industry, as did increasing political stability. The lack of a market for domestically produced vehicles, however, heavily outweighed these benefits.

The Early Entrepreneurs

Motor vehicle use in Japan began in 1899 when an American living in Yokohama imported a three-wheeled electric vehicle called the Progress.⁹ Over the next few years, the number of registered vehicles grew slowly as Japan imported cars from Europe and America. Imports rose from 16 in 1907 to around 500 in 1912. These imports were primarily steam- and electric-powered passenger cars.¹⁰

The Japanese quickly established domestic production and assembly operations, but these efforts were mainly attempts at trial production in small family shops. Many of these shops, as in the United States, originally produced and repaired bicycles. The earliest known domestically assembled vehicle was a twelve horse-power, two-cylinder steam-powered car made by the Automobile Trading Company in 1902 from imported parts.¹¹ In 1904 Torao Yamada built the first vehicle, a bus, that was built entirely of domestic parts, many of which he made himself.¹² The first gasoline-powered car was built in 1907.

The best known early producer was Masujiro Hashimoto, the founder of Kaishinsha.¹³ He was a graduate of Tokyo Technical High School and worked as an engineer in mines and ironworks. In 1902, the Ministry of Agriculture and Commerce sent him to a steam engine plant in the United States to work as a trainee. After returning, he established Kaishinsha in April 1911. He first repaired and imported cars from the Swift Company in England and later went on to produce the DAT (Datsun) car line, making seven DAT cars between 1914 and 1917. Kaishinsha merged in 1926

with another early company, Jitsuyo Motors, to form DAT Motors. In the 1930s, Tobata Casting Company, the parent company of Nissan Motor Corporation, acquired the production rights to the DAT car line. The DAT car line ultimately became the foundation of Nissan's passenger car production in the 1950s along with a knock-down version of the British Austin.

The early producers possessed a strong entrepreneurial spirit but had little effect on later developments in the industry. Without government support, they had a difficult time surviving and were unable to establish a domestic automobile industry. The low overall technological level of the machinery industry and other support industries inhibited mass production. Mass production also was limited by the small market for domestic vehicles. Consumers still preferred the status afforded by a more advanced imported automobile.

The Military Subsidy Program

The government did show some interest in the automobile industry in the early 1900s, not for its economic development potential but for its military applications. A relationship began as the military and industry cooperated to produce trucks. This relationship remained outside the close partnership that existed between the government and the *zaibatsu* because the companies involved were small and their interaction with the government was limited to the military subsidy program.

After the Russo-Japanese War (1904-1905), the Japanese army began to investigate possible military applications of motor vehicles.¹⁴ In 1906 and 1907 the army imported one truck each year from France to study. In the next few years, it imported additional vehicles from France, England, and Germany. By 1910 the army had made two experimental trucks and concluded that trucks could be produced domestically.

In 1912 the army established the Military Motor Vehicle Evaluation Committee, which was set up to create a policy to support truck development. This committee determined that it was too difficult for the army to produce and maintain a large number of trucks. Instead, it suggested following the European model where subsidies were given to private producers with the stipulation that subsidized vehicles could be requisitioned by the army in times of war.

There was a major difference in orientation between the early independent producers and the army. The producers were interested in building passenger cars and the army, in trucks only. Until the end of World War II, the army's interest in truck production helped to stifle the research and production of passenger cars, beginning with the passage of the Military Vehicle Subsidy Law (Gunyo Jidosha Hogoho) in 1918.

This law enacted the recommendations of the Military Motor Vehicles Evaluation Committee and provided manufacturing, maintenance, and purchasing subsidies to producers and buyers of qualified vehicles.¹⁵ (See table 1.) In order to qualify, the vehicle had to be made by a government authorized manufacturer. In order to be authorized, over 50 percent of the capital and voting rights of a company had to be held by Japanese nationals and most motor vehicle parts had to be supplied from within Japan. Any use of foreign-made parts required special authorization. Initially, the production of four-wheeled trucks was subsidized. Six-wheeled trucks were added in March 1930 for use in Manchuria. After the Manchurian Incident on September 18, 1931, only six-wheeled trucks were eligible for the subsidy.

Seven companies were authorized under this law.¹⁶ These companies were mainly divisions of shipbuilders and weapons makers and reflected the entry of larger firms into the market. From these firms, three emerged as the prime domestic producers of motor vehicles into the 1930s. The others, including Mitsubishi Shipbuilding, Kawasaki Shipbuilding, Okumura Denshi Shokai, and Ikegu Iron Works, dropped out after producing only a few vehicles.¹⁷ The remaining three companies and their dates of authorization were Tokyo Gas and Electric (1919), Ishikawajima Shipbuilding (1924), and Kaishinsha (1924).

Tokyo Gas and Electric Co., Ltd. (Tokyo Gasu Denki Kogyo Kaisha or TGE) was founded in 1910. In 1917 it created an automobile division in order to produce five four-ton trucks for the Osaka Arsenal, becoming the first subsidized manufacturer. Ishikawajima Shipbuilding bought a license to produce the British Wolseley CP-model truck and set up an automobile division in 1920. In 1929, Ishikawajima Shipbuilding sold its automobile division to a private owner and the name changed to Ishikawajima Motor Works, Ltd. (Kabushiki Kaisha Ishikawajima Seisakujo). Kaishinsha merged with Jitsuyo Motors to become DAT Motors two years after receiving its authorization.

These companies became dependent upon the military subsidies to make a profit in their vehicle production and never

Table 1
Subsidies Under The Military Subsidy Program
(in yen)

	Manufacturing Subsidy		Additional Subsidy	Purchasing Subsidy	Maintenance Subsidy
	Four-Wheeled	Six-Wheeled			
Trucks					
.25-1 ton	400	1,400	500	1,000	400
1-1.5 tons	750	1,750	500	1,000	500
Over 1.5 tons	1,250	2,200	500	1,000	600
Applied Motor Vehicles					
.75-1 ton	250	1,250	375	750	300
1-1.5 tons	500	1,500	375	750	300
Over 1.5 tons	800	1,800	375	750	500

Note: Manufacturing subsidy and additional subsidy were for producers. Additional subsidy was paid when producers used vehicles. Purchasing subsidy and maintenance subsidy were for purchasers and users.

Source: Fumihiko Adachi, Keinosuke Ono, and Konosuke Odaka, *Ancillary Firm Development in the Japanese Automobile Industry—Selected Case Studies* (Tokyo: Hitotsubashi University, 1981), p. 45.

developed mass production techniques. Between 1918 and 1924, 160 vehicles were produced under the Military Vehicles Subsidy Law, compared with total domestic production of 884 vehicles between 1914 and 1926. Imports during the same period totaled 15,771.

Taizo Yakushiji attributes great importance to the military subsidy program. He discusses how "the early recognition of the potential use of trucks for military purposes by military engineers . . . later led to the birth of Japan's automobile industry."¹⁸ He believes that the strongest effect of the law was not "in the increase of production, but in the reduction and absorption of the weak enterprises. This first experience seems to create the industry's immunity to government interventions which was to last for the next 60 or so years."¹⁹

While he is correct that the strongest effect of the law was not in the production numbers but in the formation of the three major companies, he overstates the law's impact. There was a difference between other early producers and these three major companies. The early producers, and Kaishinsha initially, were more interested in building passenger cars than trucks. They failed not just because they did not switch to trucks and so would receive subsidies, but because they could not compete with European imports. The three companies that did survive were barely helped by the subsidies. They failed when the post-World War I economic boom ended and stronger producers entered the market. Military support did not create a strong industry; it only created a dependent industry with inherent obligations, obligations that the three companies could not meet in the 1930s. Thus, the foundation of the automobile industry cannot be attributed to this law.

The Military Vehicle Subsidy Law also was not a precursor of adversarial interactions between government and business. The companies continued to work with the military in a dependent relationship throughout their various reincarnations. The two successful domestic automobile companies that developed in the 1930s, Toyota and Nissan, were not initially antagonistic toward the government. They reaped great benefits from the government authorization program in the 1930s and the expulsion of foreign companies from the Japanese market. The pattern of cooperation between the industry's major producers and the government continued into the 1950s.

The Arrival of Ford and General Motors

The tremendous weakness of the early Japanese motor vehicle producers and the strength of foreign producers, especially Ford and General Motors, became readily apparent during reconstruction after the Great Kanto Earthquake in 1923. The earthquake brought to the forefront economic problems that had been building since World War I. Japan's exports had grown rapidly during the war as they replaced many European exports to Asian markets. This development led to increases in income and inflation, which contributed to the country's financial instability.

The earthquake also was responsible for Ford's and General Motors's decision to build onshore assembly plants in Japan. Because the earthquake had disrupted trolley transportation in Tokyo, the city government decided to buy buses.²⁰ But, they could not obtain the required buses in Japan because the three main producers had all been heavily damaged by the earthquake. The domestic producers, in any case, would not have been able to produce enough vehicles to fill the demand. Therefore, the city of Tokyo ordered 2,000 Model T truck chassis to be refit as buses from Ford Motor Company. They bought American vehicles rather than European vehicles because they were cheaper and shipping time was three months quicker.

Prior to Tokyo's bus order, Ford and General Motors thought China had the greatest market potential in East Asia. Until 1923 imports of Ford and General Motors cars had been handled by their agents, Sale and Frazer Company and Yanase Shokai, respectively.²¹ But, in 1924 and 1925 after the Great Kanto Earthquake, Ford and General Motors rushed to establish their own offices. Japan Ford initially was capitalized at 4 million yen (\$952,381), which was raised in 1929 to 8 million yen (\$1,739,130) in order to match Japan General Motors's capitalization level.²²

The vehicles assembled by the American automobile companies in onshore assembly plants began to dominate the market. The American vehicles replaced European imports in the Japanese market and soon overwhelmed the existing domestic producers. Initially, the American companies were welcomed because they brought cheap products and advanced technology into Japan. Many Japanese important in the postwar automobile industry, such as Shotaro Kamiya, originally worked for Ford and General Motors.²³

By 1934 American vehicles held an almost 90 percent market share. By the time Ford and General Motors were forced out of the Japanese market, they had assembled approximately 250,000

cars. The assembly operations had strong repercussions on the trade balance because of the large number of imported parts required for the plants. The effect on the trade balance, when combined with the fact that General Motors and Ford retained 100 percent ownership of their Japanese subsidiaries, became an issue in the growing nationalist movement.

Tokyo's purchase of Ford chassis signified that vehicles for civilian use were no longer viewed as just luxury toys but also as practical answers to mass transit. In September 1929, the Ministry of Railways (MOR) set up the Committee to Survey the Motor Transportation Network to explore potential uses for buses.²⁴ This investigation led to the development of trial models and the opening of a bus line in 1930 by MOR. The Law Regarding Motor Vehicle Transportation Enterprise, passed in 1932 to regulate buses, included provisions that prohibited high-floor, American-style buses from operating on MOR bus routes. This decision, along with the growth of the taxi industry, helped ensure the use of domestic motor vehicles in mass transit.

General Motors's and Ford's assembly operations represented the first major foreign threat to the development of the Japanese automobile industry. The imports from Europe had inhibited the development of the early producers but less so than Japan's lack of technology and its small market. The large scale onshore production by the American producers was a more visible threat. As a result, the government began to take much more interest in the industry.

Impact of the Early Era

The experience of the Japanese automobile industry prior to the early 1930s was important to later developments. It revealed the existence of an extremely weak domestic motor vehicle industry. Ford and General Motors quickly overran the three major producers—Tokyo Gas and Electric (TGE), Ishikawajima, and DAT Motors—at the time of the Great Kanto Earthquake. It demonstrated that in the presence of a technologically backward domestic industry, imports and onshore foreign capital would dominate the market. Such domination in turn could result in a chronic trade account deficit and shortage of foreign exchange. This period also showed a government that was interested in the motor vehicle industry only in terms of buses and trucks; private sector interest in passenger cars was not encouraged.

Interactions between the government and the automobile industry during this early period were limited because there was no mutual interest in developing the industry and no strong foreign threat until Ford and General Motors began production. (Chrysler also began limited production in Japan as Kyoritsu Motors.) The only exception was the army's continuing interest in developing trucks through its subsidy program. While very few vehicles were produced under the subsidy program, the authorized manufacturers did have a small guaranteed market. Several other small companies attempted to begin operations, but they invariably failed or were absorbed into other firms. But, when Ford and General Motors entered the market, it soon became evident that authorization and military purchases by themselves were not enough to ensure success.

Government Intervention

Economic and Political Context

By the late 1920s Japan's economic and political situation had greatly changed; nationalism was on the rise, and the economy was in trouble. Japan entered a period during which the government actively tried to influence the economy and, at the same time, became less tolerant of foreign presence through imports and investments in its economy. These circumstances created the economic and political context for the next stage of development in the automobile industry.

Two changes in the economy affected relations between the government and the automobile industry. First, the balance of payments became a significant issue by 1926 as Japan's financial crisis deepened. In June 1926 the Committee for the Promotion of Domestic Products (Kosan Shinko Iinkai) was organized within the Ministry of Commerce and Industry (MCI) to reduce the trade deficit by promoting import substitution. Second, the world depression spread to Japan and created an economic slump from 1929 to 1931. The government responded with a series of relief measures, which included the formation of the Bureau of Industrial Rationalization in 1930 to help stricken industries improve their efficiency and lower costs and the passage of the Major Industries Control Law of 1931 that allowed MCI to allocate domestic market quotas and control prices and production with the agreement of at

least two-thirds of the firms in an industry. While the effectiveness of these actions can be questioned, they did increase the government's role in the economy.

Changes in the political arena also affected the automobile industry. Nationalist-militarist thinking spread, a trend not unique to Japan. By the late 1920s, the military increasingly became disillusioned with parliamentary democracy. With the outbreak of the Manchurian Incident on September 18, 1931, it became clear that the civilian leaders could not control the military. The assassination of Premier Tsuyoshi Inukai on May 15, 1932 and the subsequent light sentences given to his assassins proved the power of the military. The major effect of these events on industrial development was that economic relief measures increasingly became vehicles of control and were used to create a wartime economy.

The "Isuzu" Standardized Car

The relationship between Japan's motor vehicle industry and the government changed radically as the health of the industry became important to the military offensive in Manchuria and China, as well as to the solution of the balance of payments problem. As the 1930s progressed, MCI and the army became involved in the automobile industry, with the army gaining greater control than MCI. Efforts by MCI and the army to obtain the voluntary cooperation of existing producers and to entice new producers into the sector failed and were replaced by more coercive measures in the mid-1930s.

On September 25, 1929, the MCI Minister asked the Committee for the Promotion of Domestic Products for recommendations on the best method to establish a domestic motor vehicle industry in order to offset the national security and foreign trade implications of the rapid increase in automobile imports.²⁵ This committee found that, while demand for motor vehicles was rising rapidly, local production of vehicles was only about 500 per year. Demand was being filled through imports that totaled over 40 million yen (\$8,695,652) per year. It also determined that the establishment of a local automobile industry was necessary for balance of payments advantages, linkages to other industries, and the strengthening of national defense. The committee also found that, while the domestic industry was stagnant and uncompetitive because of high costs resulting from low production volumes, adequate promotion policies could encourage its development.

In May 1930 the committee made its recommendations.²⁶ Priority should be given to the production of trucks and buses because the model changes required in the passenger car industry were too expensive. Subcontracting practices should be encouraged to utilize the excess capacity in existing automobile producers as well as in shipbuilding, forging, and other related industries. Eventual domestic production of parts would be necessary, but foreign designs and production methods should be studied first. The government should adopt protective measures, such as subsidies and high import tariffs, and encourage the use of domestic vehicles by government officials. This group also suggested that a research committee be formed to complete a detailed study of the industry and that a test model be made to confirm the efficiency of domestically produced vehicles. In response, the Survey Committee for the Establishment of the Automobile Industry (Jidosha Kogyo Kakuritsu Iinkai) was formed in May 1931.²⁷

The survey committee included the business, government, and academic communities and consisted of eighteen regular members, one temporary member, and eight staff members.²⁸ The eighteen regular members included two professors from Tokyo University; the presidents of Ishikawajima, TGE, and DAT Motors; and thirteen government officials—Home Affairs (2), Finance (2), Army (3), Commerce and Industry (1), Railways (4), and other (1). The committee formalized interaction between government and business in the automobile industry to create policy.

The committee announced specifications for five standardized models in September 1931 and then ordered TGE, Ishikawajima, and DAT Motors to make nine vehicles of two truck and three bus types. These companies had little choice but to comply because they were in financial difficulty and dependent on the military vehicle subsidy. These test vehicles were then studied to obtain a single standardized model, and the prototype was completed in March 1932.

The standardized car eventually became known as the "Isuzu," and 3,000 were to be produced every year.²⁹ The Isuzu was to be a truck, weighing between 1.5 and 2 tons, and therefore not directly in competition with smaller vehicles produced by Ford and General Motors in Japan. In addition, the tariff on engines was raised from 28.1 percent to 35 percent *ad valorem* and on parts from 30 percent to 40 percent in 1932.

At the same time that MCI became involved in the motor vehicle industry because of the balance of payments deficit, the army's interest increased. The army needed a large number of

trucks for its land operations in China after the Manchurian Incident in 1931. The army had continued to subsidize vehicles through the 1920s under the Military Vehicle Subsidy Act, but was dissatisfied with the small number of vehicles produced.

The joint interest of the Ministry of Commerce and Industry and the army resulted in a search for a domestic company that could build the Isuzu. MCI approached three *zaibatsu* (Mitsui, Sumitomo, and Mitsubishi), and each turned down the proposal as too risky.³⁰ Mitsubishi Shipbuilding had built a bus in 1932 and continued to build a few vehicles on its own but did not want to participate in the government project.

MCI and the army encouraged the formation of the National Automobile Union (Kyodo Kokusan Jidosha K.K.) in June 1932.³¹ Consisting of representatives from Tokyo Gas and Electric Company, DAT Motor, and Ishikawajima Motor, the Union was essentially an administrative organ in charge of supervising the sales and subsidies related to the Isuzu project. Because the companies were in small size, uncompetitive, and suffered internal conflicts, it soon became apparent that this organization could not produce the required number of vehicles.

The government next tried to merge these three companies. Yoshisuke Aikawa of Nissan became involved because his company, Tobata Casting Company, bought DAT Motors in 1931. He was instrumental in merging DAT Motors and Ishikawajima in 1932 but became dissatisfied with this arrangement because he wanted the new company to produce more than just the buses and trucks needed by the army. He pulled Tobata out and in 1933 formed a separate automobile company, Nissan Jidosha K.K., retaining the manufacturing rights to the original DAT line of passenger cars.

Eventually, Tokyo Gas and Electric Company joined the remaining portion of the DAT Motors/Ishikawajima merger in 1934 to form Jidosha Kogyo, initially capitalized at 3.2 million yen (\$1,084,746). During the next few years, Jidosha Kogyo underwent more transformations and name changes, eventually becoming Diesel Jidosha Kogyo in April 1941. This company later separated to form the postwar companies of Isuzu Jidosha and Hino Jidosha Kogyo.

By late 1934, it was obvious that the attempt to manufacture the standardized vehicle through either a merger scheme or voluntary cooperation would not work—only 450 vehicles had been produced.³² Taizo Yakushiji attributes the failure of the standardized car to the fact that its technical specifications neglected changes in market demand. A more important reason was that

Jidosha Kogyo was too weak and the new, stronger companies were not interested. The Japanese government was not able to force the stronger companies to comply with its plan in the early 1930s. Most importantly, General Motors and Ford still dominated the market.

The government's attempts to foster a domestic industry did not end with the failure of Jidosha Kogyo to produce the standardized vehicle. Rather, they were redirected as the need for trucks in the military mobilization effort increased.

The Emergence of Toyota and Nissan

During the reorganization of the existing car companies, in the 1930s, two major new entrants appeared in the motor vehicle market: Nissan and Toyota. The emergence of these two companies was important because they initially entered the market with the idea of building passenger cars, not just trucks and buses, and each became a major postwar producer. They were established by exceptionally talented entrepreneurs who believed that they could carry on with the private production of passenger cars while catering to the military. The two companies realized that they would need some government subsidies and protection to survive competition with the American companies, but each tried to maintain some independence. Yoshisuke Aikawa stated that:

Automobiles must be produced at the level of 10,000 to 15,000 units a year in order to constitute a viable business. Under existing circumstances, however, the industry needs a rather generous government subsidy and protection in order to grow.³³

Thus, Nissan and Toyota were able to enter the market at this time because of the steadily growing demand from the army (Toyota purposely began to produce a truck along with its passenger car for this reason) and the rising tide of protectionist sentiment.

Aikawa established a motor vehicle department as part of Tobata Casting Company that initially made passenger cars using DAT's manufacturing rights and that produced automotive parts for Ford and General Motors in a plant in Osaka.³⁴ After Aikawa decided to pull out of the government-sponsored merger in 1933, he set up Motor Industries with a joint investment of 6 million yen (\$2,380,952) from Nihon Sanyo K.K. and 4 million yen (\$1,587,302) from Tobata Casting. In 1934, he changed the name

of the venture to Nissan Motor and decided to build an additional plant in Yokohama by importing a disassembled plant from the Graham-Paige Company and obtaining technical guidance from several American engineers. By 1937, two years after the first Datsun rolled off the Yokohama assembly line, total production from the two plants reached 10,000. Plans were made to create an additional line of passenger cars using imported technology.

Toyota Motor Company was established on August 27, 1937 as a separate entity from its parent, Toyoda Automatic Loom Works, Ltd. The name of the company was officially changed from Toyoda to Toyota.³⁵ The founder of Toyoda Automatic Loom, Sakichi Toyoda, had been interested in motor vehicles since he visited the United States in 1910 and witnessed the early impact of the Ford Model T. In 1930 he sold a textile machinery patent for 1 million yen (\$202,593) to Platt Brothers Inc. and gave the money to his son, Kiichiro Toyoda. Kiichiro Toyoda used the money to begin research on passenger cars, which took place in secret from 1930 to 1933. A formal automobile division was established in late 1933, after overcoming considerable objection from within the company about the wisdom of producing automobiles when the large *zaibatsu* found it too risky. While Toyota developed its own designs, it did extensive studies of foreign vehicles, parts, and manufacturing techniques. Initially capitalized at 3 million yen (\$1,190,476), self-capitalization was expanded to 6 million yen (\$2,097,902) in August 1935 and to 9 million yen (\$3,146,853) in late 1936. Later, in 1937, Toyota received a loan from the Mitsui Bank for 20 million yen (\$7,722,008) and in 1939 was able to increase its capitalization to 30 million yen (\$11,583,011). The first prototype passenger car "A1" model was completed in May 1935 and the first prototype truck "G1" in August. A new assembly plant, completed in 1936 in Koromo (Toyota City), was expanded to produce 10,000 units.

Masaru Udagawa and Seishi Nakamura cite the emergence of Toyota and Nissan as typical of the appearance of "outsider" firms in emerging industries during the 1930s. They state that "these entrepreneurs were independent and innovative in their behavior, and their enterprising spirit was clearly indistinguishable from the 'Japan Incorporated' mentality of collective interdependence."³⁶ They point out that the automobile industry had a different relationship with the government than industries, such as steel, that were part of the "collective interdependence" and had more interactions. Udagawa and Nakamura are correct in that the strong, private initiative of Nissan and Toyota helped them to be successful while the dependency of Jidosha Kogyo on the government

prevented it from becoming the center of the industry. But, because they set out to prove that the independent companies rather than government-sponsored rationalization and merger programs caused industrial growth in the 1930s, they depict the interests of government and the outsider firms as "diametrically opposed." Rather, the actions of Toyota and Nissan show that they saw advantages in working with the government. Udagawa and Nakamura also attribute the failure of Jidosha Kogyo to the failure of the government-sponsored rationalization policy, but in truth it failed primarily because of the inherent uncompetitiveness of the company.

The emergence of Toyota and Nissan, along with their adoption of mass production, signified the first solid step toward building a domestic automobile industry. The industry's beginning was based on private initiative and government interest. The major domestic motor vehicle manufacturers that emerged during the 1930s were Toyota, Nissan, and Jidosha Kogyo. In addition, Mitsubishi continued to produce a few heavy trucks, and three-wheeled vehicle manufacturers, such as Toyo Kogyo (Mazda) and Daihatsu, were able to enter the market because of growing demand and the 1931 yen devaluation that raised the price of imports.

The Automobile Manufacturing Law

The government attempted to intervene in the industry again with the August 9, 1935 Cabinet announcement of the Outline of the Automobile Manufacturing Law (Jidosha Kogyo Ho Yoko). This announcement in part stated:

At the same time as the automobile industry occupies an important position in industry it also has an important significance for national defense. Entrusting such an important industry pure and simply to the complete control of foreigners is an extremely unsatisfactory situation. Regardless of previous limitations, we think that it should be placed in the hands of Japanese both in name and reality, now and in the future.³⁷

The statement revealed the government's twofold objective: the completion of the national defense and the development of industry.³⁸ The national political situation was becoming increasingly tense because of the growing military needs in Manchuria and

the continued strength of General Motors and Ford in the Japanese market.

The government felt pressure to act quickly because Toyota and Nissan were negotiating with General Motors to enter into joint ventures to obtain needed capital and technology.³⁹ Aikawa, foreseeing the eventual elimination of Ford and General Motors from the Japanese market, regarded the joint ventures as an opportunity to gain control over their assets in Japan. The Nissan-General Motors negotiations in particular progressed quickly; General Motors was extremely willing to enter into some type of arrangement as the political situation worsened. The negotiations, which lasted over four years, never succeeded because of the uncertainties raised by the changing political environment and the army's opposition to the joint venture.

Nissan courted Ford, but Ford wanted to continue on its own. Seeking to meet the increasing nationalist pressures, Ford drew increased capital for a new manufacturing plant from Japanese Ford dealers and stipulated that the plant would use only domestic parts within a few years. In April 1934, Ford attempted to buy new land for the plant from the city of Yokohama but was prevented by the army, which argued that to sell the land would sabotage domestic manufacturing.⁴⁰ Ford was able to buy land in July 1935 in Yokohama from a subsidiary of the Asano *zaibatsu*, but its application for a building permit was rejected under pressure from the army.

After the Cabinet announcement on August 9, the army again approached the major companies with a plan to produce the standardized car on a scale of at least 3,000 units per year.⁴¹ They were rejected in turn by Jidosha Kogyo, TGE, Nissan, Mitsui, and Mitsubishi. At this point, the army began to consider setting up its own national car company while MCI, as well as the Foreign Ministry, preferred to support the Isuzu project and to encourage Nissan's joint venture efforts as a method to hasten the development of the domestic industry and to prevent damaging trade relations with the United States.⁴² The dispute between those advocating the two different approaches was resolved with a decision to approach Toyota—the new company not under earlier consideration. Toyota saw an opportunity and presented an alternative plan based on a smaller production amount.⁴³ Toyota's interest, along with the army's growing political power, put the army in a position to make policy decisions that MCI opposed.

The final result of the Cabinet decision was the Diet's passage of the Automobile Manufacturing Law (*Jidosha Seizo Jigyo Ho*) on

May 29, 1936.⁴⁴ This law sought to exclude foreign capital, shut down the foreign onshore assembly plants, and prevent Japanese firms from entering into joint ventures with foreign firms. These goals were accomplished by prohibiting Ford and General Motors from increasing their production above current levels (12,360 for Ford and 9,470 for General Motors), by exacting a 50 percent tariff on imports of engines and parts, and by banning joint ventures under the Exchange Control Law. Finally, government authorization was required for automotive parts companies producing parts for more than 3,000 vehicles annually, a move to keep General Motors and Ford from entering this segment of the motor vehicle industry. These actions, combined with another yen devaluation caused by the Sino-Japanese War, forced the American manufacturers out of the market by 1940.

The law gave the Ministry of Commerce and Industry the power to reorganize producers into a coordinated national group to manufacture standardized parts and vehicles for the war effort in Manchuria. The industry was controlled through a licensing system that was mandatory for production over a certain level. This system required majority ownership and control by Japanese nationals, and obedience to the government's operational orders. Economic incentives included five-year income and corporate profit tax holidays, tariff exemptions for machinery and material imports for five years, and relaxed recapitalization requirements.

Nissan and the automobile division of Toyoda Automatic Loom submitted proposed production plans to MCI in July 1936.⁴⁵ These companies became the first authorized manufacturers under the new law on September 19, 1936. In order to achieve this status, the two companies had to greatly curtail their private activities in the area of passenger cars in favor of making trucks. Without authorization from the army, however, it is doubtful that they could have survived for long as motor vehicle manufacturers given the political environment.

The Automobile Manufacturing Law, combined with the establishment of Toyota and Nissan, created a viable domestic motor vehicle industry based on the manufacture of trucks. It also symbolized a period of government-business relations based on government control rather than joint interests pursued through a working partnership.

Summary

The period of government intervention began with efforts by both MCI and the army to encourage production of a standardized vehicle that could displace the automobiles being assembled by Ford and General Motors. These efforts were intertwined but not parallel in either motive or implementation. With the passage of the Automobile Manufacturing Law in 1936, the army gained control over policy decisions related to the automobile industry. The law also signified the virtual end of the coexistence of private efforts to make passenger cars and the need for cargo vehicles for national security purposes.

Toyota and Nissan quickly surpassed the existing domestic makers during this period by introducing foreign technology and mass production techniques. They were able to do this because support from major existing companies covered their initial costs and because of their strong entrepreneurs and an increasingly protected environment. Domestic production of four-wheeled motor vehicles soared, rising from 458 in 1930 to a peak of 42,813 in 1941. Production fell after 1941 as a result of materials shortages and did not surpass this peak again until 1952. Toyota's production rose from 20 in 1935 to a high of 16,302 in 1942 while Nissan's went from 940 in 1934 to its peak of 19,688 in 1941. Their combined share of total production averaged 75.5 percent between 1935 and 1940, and 84.1 percent between 1940 and 1945.

Wartime Controls

In July 1937, Japan entered the second Sino-Japanese War (1937-1945). Military spending, which had accounted for 16.2 percent of government budget expenditures in 1930, now rose to 53.5 percent.⁴⁶ The wartime economy necessitated the centralization of control over political parties and private business interests, a process that accelerated in late 1937 and was complete by 1940.

From the latter half of the 1930s until 1945, the Japanese motor vehicle industry was under government control. The initial, though admittedly slow, progress the automobile makers had made toward the development of a passenger car industry stalled as the companies were forced to concentrate their efforts on truck production. Entrepreneurs like Yoshisuke Aikawa and Kiichiro Toyoda did

remain interested in passenger cars and continued some limited research but were unable to continue production.

The first step toward the implementation of controls after the Automobile Manufacturing Law occurred with the passage of the Temporary Measures Law Relating to Exports, Imports and Other Matters on September 9, 1937. This law controlled the "import and export of specific goods and controlled consumption, manufacturing, and processing of trade-related goods," thereby controlling who could import and what could be imported.⁴⁷ As a result, General Motors's and Ford's Japan operations received a final death blow since they could not import the parts needed for production.

The passage of the National General Mobilization Law (Kokka Sodoin Ho) in March 1938 allowed the government to bypass the Diet and enact strong measures controlling the economy. With this in hand, MCI took the next major step directly affecting the motor vehicle industry and announced production guidelines on August 14, 1938 as part of the Materials Mobilization Plan (Busshi Doin Keikaku).⁴⁸ This plan controlled the use of materials that had no direct relationship with production for military demand, effectively prohibiting the production of passenger cars. In short, the guidelines provided for the exclusive production of cargo vehicles or weaponry (tanks) except when it was necessary to use up materials on hand suitable only for passenger car production. Any passenger cars produced were to be distributed according to orders received from the military and were not sold to ordinary people. Also, production of minicars as well as three- and two-wheeled vehicles was prohibited.

Another area of government intervention that affected the motor vehicle industry was the search for alternative fuels as gasoline consumption became a major concern in the 1930s. The government decided to encourage the production of a diesel vehicle.⁴⁹ At that time, several smaller companies were experimenting with diesel engines: Tokyo Jidosha Kogyo (the latest name for Jidosha Kogyo), Ikegai Tecko, Mitsubishi Shipbuilding, Hitachi Keikaku, and Nihon Diesel Kogyo. MCI decided that it was prudent to concentrate the research efforts in one company, Tokyo Jidosha Kogyo, with the other companies participating by supplying capital and technology. Thus, Tokyo Jidosha Kogyo on April 9, 1941 became the third company authorized under the Automobile Manufacturing Law. Its name was changed first to Jidosha Seizo before becoming Diesel Jidosha Kogyo on April 30. In May 1942, the weaponry department was detached to form Hino Heavy Industries.

The other major attempt to encourage the use of alternative-fuel vehicles revolved around charcoal-burning engines.⁵⁰ The army had imported a charcoal-burning engine from the Parker Company in 1916 and then developed its own version in 1926. These efforts had little effect as there were only eighteen charcoal-burning vehicles in use in 1934. In that year, MCI together with the Ministry for Forestry and Agriculture decided to provide a subsidy for these cars, and their number increased to 3,000 by 1938. MCI established a fuel department in 1938 that further promoted the production and use of charcoal-burning cars so that their number rose to 10,000 in 1939. After that, attention switched to the promotion of gasohol.

Concern about the general technological level of Japanese vehicles, which were notorious for their propensity to fall apart on rough Chinese roads (partially due to steel quality), led to another sequence of government-business interactions during the war. When the Automobile Manufacturing Law was passed in 1936, MCI wanted to establish a national experimental center to improve the level of automobile technology, but could not because of financial constraints.⁵¹ Later, when the army demanded that motor vehicle makers improve the efficiency of their vehicles, MCI established a Committee on Automobile Technology in August 1939. Because of a division within the MCI Machinery Experimental Bureau in 1940, this committee was transferred in December 1942 along with the Bureau to the Ministry for Military Procurement.

Although the committee consisted of sixteen experts, they did not have their own research facilities or extensive funding.⁵² They, therefore, relied heavily on cooperation with the private companies. The private companies had to cooperate given the political circumstances, but they also believed it would help prevent them from falling too far behind General Motors and Ford. Initially, Nissan and Toyota each contributed one million yen (\$427,350) to pay for land, buildings, and a test course. Diesel Jidosha Kogyo contributed 750,000 yen (\$320,513) in 1941. The government provided the operating expenses and chose a site for the facility in Higashimurayama. The main buildings and test course were not completed until 1943 and then were smaller than planned. In addition, cement could not be found to pave the test course. Major results obtained by this group during the war consisted of ten driving tests of vehicles between July 1941 and August 1944, and examination of the quality of automotive parts after 1943. This group continued in existence (it was moved back to MCI in 1946) until 1953.

The main instruments of control during the war were control associations (Tosei Kai), established under the Major Industries Control Ordinance (Juyu Sangyo Dantai Rei) of August 29, 1941.⁵³ The automobile industry was designated in the first Ministerial Ordinance issued in October 1941 as an industry in which control associations were to be founded. The purpose of a control association was to allow

the government [to implement] the national program for production and distribution in the industry concerned; the means of supplying the labor, raw materials, capital, and other demands of the industry concerned . . . control and guide production and distribution in the industry . . . provide for the complete equipping of the industry . . . develop techniques, increase efficiency, unify the regulations, and reform the management of the industry.⁵⁴

Within the automotive industry, the government established seven control associations, three of which were major.⁵⁵ The three major associations were the Automobile Manufacturing Industrial Association, which had 4 members (Toyota, Nissan, Isuzu, and Hino) with 14 plants and was responsible for standard-sized automobiles and their parts; the Japan Special Automobile Industrial Association, which had 30 members with 38 factories and was responsible for tractors, trailers, trailer trucks, dump trucks, fire trucks, fuel trucks, plows, and harrows; and the Japan Small-Sized Automobile Association, which was responsible for small-sized three- and four-wheeled vehicles, motorcycles, motor scooters, and their parts. The other four associations were the Japan Automobile Body Industrial Association, which had 140 members with 144 factories and was responsible for truck, bus, and other types of vehicle bodies; the Electric Automobile Industrial Association, which had 6 members with 6 factories and was responsible for all electric-battery operated vehicles; the Automobile Manufacturers Materials Committee, which had 630 members with 707 factories and was responsible for automotive-related materials; and the All Japan Automobile Parts Industrial Association, which had 357 members with 411 factories and was responsible for all automotive parts.⁵⁶

The most important association was the Automobile Manufacturing Industrial Association, whose members formed the core of postwar truck and passenger car production. This association left control of actual production with the private companies. The association's job was essentially to procure raw materials, a task

that became more difficult as the war progressed. In particular, it had problems obtaining nickel and asbestos for brakes, and carbon black for tires. Control of raw materials for the automobile industry began in 1938 with the enactment of the Iron and Steel Distribution Control Regulations. The Iron and Steel Control Council established an automobile department to regulate shipments of steel, the major scarce raw material. After 1941, the Association's primary task was not simply to control the distribution of raw materials but to obtain them. The motor vehicle industry throughout the war was never able to reach planned levels of production, and the drop in vehicle production paralleled the decrease in steel allocation.

The major reason that materials were difficult to locate for the motor vehicle industry after 1941 was that the military front had shifted from China to the Pacific with the beginning of the war with the United States. The need for land vehicles decreased as the need for ships and aircraft increased, and then increased again as a possible invasion of the home islands drew near. This change is reflected in the army's priority rating for the use of raw materials in the industry.⁵⁷ Industries that had highest priority were rated A1, those with less, A2 and so on. The rating for the motor vehicle industry changed as follows:

1941	1942	1943	1944	1945
B1	B2	C	C	B5

The switch to a Pacific front also created another task for the automobile control associations. The automotive makers, both major assemblers and major parts firms, were ordered to begin the production of other products, especially aircraft.⁵⁸ Toyota started an aircraft department as early as November 1938, which became a separate company in June 1942 upon the recommendation of the Military Air Force Center (the army's air force). Other sections of Toyota produced aircraft parts either within Toyota or in cooperation with other firms. The army air command told Nissan to produce aircraft engines and parts as of December 29, 1942. The industry produced less and less of all types of products as the war drew to a close, and raw materials became difficult to obtain. By 1945, auto executives such as Kiichiro Toyoda were already thinking ahead about how to survive after the war ended.

The major characteristic of the wartime period was the subordination of the automobile industry to military demand. One government priority of the interventionist period—the development of industry—disappeared, leaving only interest in building a strong

national defense, and leading to a halt in passenger car production and in technology imports.

This period saw Nissan's and Toyota's rise to dominance. Many small makers were pushed out of the market because they could not meet authorization requirements and so could not obtain raw materials. Some attempted to reenter the market after the war but few were successful. Government-business interactions geared to protecting the industry increasingly meant protecting the large companies, not all the producers in the industry. Nissan and Toyota have remained dominant producers to the present day.

Government-business relations at this time were weighted in favor of control rather than a partnership based on joint cooperation. It would be wrong, however, to describe the relationship as adversarial because many automobile industry executives, such as Yoshisuke Aikawa and Risaburo Toyoda, were strongly nationalistic and supportive of the war effort. The government and industry also cooperated to develop technology.

Conclusion

Prewar and wartime developments had significant effects on the postwar government-business relationship in the Japanese automobile industry. Many of the decision makers responsible for policy in the earlier period were key figures after the war. More importantly, the emergence of Toyota and Nissan combined with the removal of foreign competition by the Automobile Manufacturing Law formed the foundation of a viable domestic truck industry. The removal of foreign competition also helped indirectly by encouraging General Motors and Ford dealers in Japan to switch to the domestic manufacturers.⁵⁹

Japan's government and industry decision makers learned four economic lessons that affected their actions in the postwar era. These lessons were applied to the economy in general and to the automobile industry specifically. First, in the presence of a technologically backward and weak domestic industry, imports and onshore foreign capital would dominate the market to such a degree that potential domestic producers would be crowded out, or severely hindered in their development. Second, Japan's continued high dependence on imported manufactured goods would result in a chronic trade deficit and foreign exchange shortage. Third, the success experienced in increasing production with government

support during the 1930s demonstrated that government promotion of industry in conjunction with private sector involvement in developing policies could potentially have positive effects on industrial development. And fourth, government control was not an effective substitute for private sector decisions.

These periods also saw the tentative beginnings of a passenger car industry, but it was by no means clear that the visions developed in the minds of the entrepreneurs could be carried to fruition in the postwar period. Immense foreign superiority of technology and production in almost all areas would have to be overcome. There was still not a large market for passenger cars in Japan, and the road network was extremely poor. There was not a tradition of governmental interest in passenger cars: the interest that had existed was only in the area of trucks and buses. On the positive side, two relatively strong companies had emerged out of the multitude of small and extremely weak domestic producers. The industry had gained considerable experience in truck production that, while not directly transferable to passenger cars, provided a foundation for the growth of the companies. Most importantly, a postwar industry now existed that was capable of lobbying in support of its own interests.

NOTES

¹A major point of contention among scholars is whether the Meiji Restoration was a reaction to internal discontent or to the external threat typified by the arrival of Commodore Matthew C. Perry in 1853. This controversy reflects the academic tendency to separate international and domestic environments. Interestingly, studies of the Japanese government-business relationship do accord significance to the external environment during the Meiji period but stress cultural and domestic variables during the postwar period as well. In reality, both domestic and international measures had and continue to have an effect.

²Takafusa Nakamura, *Economic Growth in Prewar Japan* (New Haven: Yale University Press, 1983), pp. 59-60.

³William W. Lockwood, *The Economic Development of Japan* (Princeton: Princeton University Press, 1954), p. 563.

⁴*Ibid.*, p. 564.

⁵G.C. Allen, *A Short Economic History of Modern Japan 1867-1937* (New York: Praeger Publishers, 1963), p. 165.

⁶Johannes Hirschmeier and Tsunehiko Yui, *The Development of Japanese Business, 1600-1973* (London: George Allen & Unwin, 1981), pp. 125-32.

⁷Keiichiro Nakagawa, "Government and Business in Japan: A Comparative Approach," in *Government and Business: Proceedings of the Fifth Fuji Conference*, ed. Keiichiro Nakagawa (Tokyo: University of Tokyo Press, 1980), p. 221.

⁸Comments by Kenichiro Shoda on Sakae Tsunoyama, "Government and Business: An Introductory Essay," in *Government and Business: Proceedings of the Fifth Fuji Conference*, ed. Keiichiro Nakagawa. (Tokyo: University of Tokyo Press, 1980), p. 20.

⁹Miyake Sadao, "The Japanese Motor Industry," *Japan Quarterly* 15.1 (January-March 1968): 99.

¹⁰*Ibid.*

¹¹*Ibid.*, p. 100.

¹²C.S. Chang, *The Japanese Auto Industry and the U.S. Market* (New York: Praeger Publishers, 1981), p. 10.

¹³Takayoshi Miyada, "Shokosho shoki no jidosha gyosei" [Administration of automobiles in the early period of MCI], in *Nihon jidosha kogyoshi gyosei kiroku shu* [Collection of articles on the administrative history of the Japanese automobile industry], Nihon Jidosha Shinko Kai (Tokyo: Nihon Jidosha Shinko Kai, 1979), pp. 1-12.

¹⁴Portions of this law are cited in Chang, *The Japanese Auto Industry*, pp. 196-97 and Taizo Yakushiji, "Dynamics of Policy Interventions: The Case of the Government and the Automobile Industry in Japan" (Ph.D. diss., Massachusetts Institute of Technology, May 1977), pp. 78-80.

¹⁵*Ibid.*

¹⁶Chang, *The Japanese Auto Industry*, p. 13.

¹⁷Miyada, "Shokosho shoki no jidosha gyosei," p. 3.

¹⁸Yakushiji, "Dynamics of Policy Interventions," p. 70.

¹⁹*Ibid.*, p. 86.

²⁰Chang, *The Japanese Auto Industry*, pp. 14-15.

²¹Masami Tamaoki, "The Protective System of Domestic Car Production in the War Time," *Keizaigaku-Kiyo*, no. 9 (1974): 19-39.

²²Chang, *The Japanese Auto Industry*, p. 15.

²³Seisi Kato, *My Years With Toyota* (Tokyo: Toyota Motor Sales Co., Ltd., 1981). This autobiography contains a discussion of how Shotaro Kamiya, known as the King of Sales, decided for both nationalist and self-advancement reasons to move from General

Motors to Toyota in 1928. When recruiting Mr. Kato, also at General Motors, Kamiya said, "As long as you stay here, working for GM, your skills will be exploited. If you come with me to Toyota, there's bound to be a chance for a senior post."

²⁴Yakushiji, "Dynamics of Policy Interventions," pp. 108-10.

²⁵Tamaoki, "The Protective System," pp. 19-39.

²⁶Miyada, "Shokosho shoki no jidosha gyosei," pp. 4-6 and Yakushiji, "Dynamics of Policy Interventions," p. 105.

²⁷Miyada, "Shokosho shoki no jidosha gyosei," pp. 4-6.

²⁸Chang, *The Japanese Auto Industry*, p. 21.

²⁹Miyada, "Shokosho Shoki no jidosha gyosei," pp. 4-6.

³⁰*Waga kuni jidosha sangyo no tenbo* [Perspectives on Japan's automobile industry] (Tokyo: Hosei University, 1982), p. 36.

³¹Chang, *The Japanese Auto Industry*, p. 18.

³²William C. Duncan, *U.S.-Japan Automobile Diplomacy* (Cambridge, MA: Ballinger Publishing Company, 1973), p. 66.

³³Fumihiko Adachi, Keinosuke Ono, and Konosuke Odaka, *Ancillary Firm Development in the Japanese Automobile Industry—Selected Case Studies*, vol. 2 (Tokyo: Hitotsubashi University, 1981), p. 38.

³⁴Michael A. Cusamano, *The Japanese Automobile Industry* (Cambridge: Harvard University Press, 1985), pp. 27-53.

³⁵Toyota's history is found in Toyota Jidosha Kogyo K.K., *Toyota jidosha nijunenshi* [Twenty-year history of Toyota Motor Company] (Toyota City: Toyota Motor Company, 1958) and Toyota Jidosha Kogyo K.K., *Toyota jidosha sanjunenshi* [Thirty-year history of Toyota Motor Company] (Toyota City: Toyota Motor Company, 1968).

³⁶Masaru Udagawa and Seichi Nakamura, "Japanese Business and Government in the Inter-War Period: Heavy Industrialization and the Industrial Rationalization Movement," in *Government and Business: Proceedings of the Fifth Fuji Conference*, ed. Keiichiro Nakagawa (Tokyo: University of Tokyo Press, 1980), p. 84.

³⁷Duncan, *U.S.-Japan Automobile Diplomacy*, pp. 66-67.

³⁸Tamaoki in "The Protective System" presents these two objectives, stating that as the Sino-Japanese War progressed it became clear that the real aim of government was solely the "completion of national defense." However, at least in the case of MCI, there was an apparent awareness of the impact of the development of the automobile industry on surrounding industries. MCI's aim fell by the wayside as the army gained control of the government.

³⁹Udagawa and Nakamura, "Japanese Business and Government," p. 95.

⁴⁰Masaru Udagawa, "The Prewar Japanese Automobile Industry and American Manufacturers," in *Japanese Yearbook on Business History: 1985*, ed. Keiichiro Nakagawa and Hidemasa Morikawa (Tokyo: Japanese Business History Institute, 1985), pp. 91-93.

⁴¹Chang, *The Japanese Auto Industry*, pp. 29-30 and Yakushiji, "Dynamics of Policy Interventions," pp. 150-53.

⁴²Cusumano, *The Japanese Automobile Industry*, p. 17.

⁴³Tamaoki, "The Protective System," pp. 16-19.

⁴⁴Duncan, *U.S.-Japan Automobile Diplomacy*, p. 67.

⁴⁵Adachi, Ono, and Odaka, *Ancillary Firm Development*, pp. 22, 49.

⁴⁶Nakamura, *Economic Growth in Prewar Japan*, p. 237.

⁴⁷*Ibid.*, p. 288.

⁴⁸Tamaoki, "The Protective System," pp. 27-28.

⁴⁹*Ibid.*, p. 29.

⁵⁰Kuman Uchiyama, "Jidosha gyosei ichigenka koso no tenmatsu" [Aftermath of one-dimensional automobile administration], in *Nihon jidosha kogyoshi gyosei kiroku shu* [Collection of articles on the administrative history of the Japanese automobile industry], Nihon Jidosha Shinko Kai (Tokyo: Nihon Jidosha Shinko Kai, 1979), pp. 127-29.

⁵¹Naomitsu Shirai, "Jidosha bu no ayumi [Steps of the automobile section]," in *Nihon jidosha kogyoshi gyosei kiroku shu*, Nihon Jidosha Shinko Kai (Tokyo: Nihon Jidosha Shinko Kai, 1979), pp. 115-24.

⁵²*Ibid.*

⁵³Uchiyama, "Jidosha gyosei ichigenka koso no tenmatsu," pp. 129-30.

⁵⁴Jerome B. Cohen, *Japan's Economy in War and Reconstruction* (Minneapolis: University of Minnesota Press, 1949), pp. 31-32.

⁵⁵Supreme Commander for Allied Powers, Economic and Science Section, Industry Division, "Automotive Industry," (Typed Monograph, Tokyo, n.d.), pp. 33-35.

⁵⁶*Ibid.* The figures stated for the number of these associations seem too high, although these figures are cited in the original source material.

⁵⁷Cohen, *Japan's Economy in War*, p. 246.

⁵⁸Tamaoki, "The Protective System," pp. 29-30.

⁵⁹Cusumano, *The Japanese Automobile Industry*, p. 123.

CHAPTER 3

TURMOIL AND RECONSTRUCTION

Postwar Situation

With the public announcement of Japan's surrender by the emperor on August 15, 1945, and the signing of the Instrument of Surrender on September 2, Japan entered into a period of turmoil and reconstruction that lasted into the early 1950s.

At the end of the war, the Japanese economy was in shambles. The bombings had destroyed a large portion of Japan's residential housing as well as its factories. Industrial production had fallen drastically. Little foreign exchange was available to buy basic necessities or the raw materials needed to rebuild the country. Japan's major prewar export markets and sources of raw materials, China and Manchuria, were cut off. Japan's future was in limbo as she waited to see what the Occupation would bring.

What the Occupation did bring was a major shift in orientation, which grew out of American demilitarization and democratization programs and Japan's internal reaction to the defeat. Occupation authorities carried out major reforms in the areas of labor, land, education, and industrial organization; many top business and government leaders were purged. Moreover, they revised the Constitution, the most famous modification being Article 9, which banned military and naval forces, except for a limited self-defense force. Lastly, after the start of the Cold War, the rehabilitation of Japan's economy became a major Occupation objective.

Continuity with the past was not lost entirely. Although much of the physical structure of the country was destroyed, managerial skills, educational levels, and the bureaucracy remained. The Occupation authorities were directed to work through the existing Japanese government, further increasing continuity. Finally, many Japanese companies managed to survive and restart after the war.

The Automobile Industry's Status

Early Reorganization

In 1945 the automobile industry found itself in the same dire circumstances as the rest of the economy. It was more fortunate than other industries because it had suffered less in the bombings. It was never a primary bombing target except once when Toyota's main factory was bombed on August 14, 1945 and was 50 percent destroyed. But even this action was not as much an attempt to destroy automobile production as Toyota's aircraft parts manufacturing.¹

Much more damage was done by the attempted dismantling and dispersal of plants ordered by the army to avoid possible bomb damage after March 1945.² For example, production stopped at Nissan in May 1945 when its machine tools were shipped to a town 180 miles north of Tokyo. No buildings were constructed at the new site, so many of the machine tools were destroyed by weather. Toyota moved 50 percent of its machine shops but never started production at the new location. Diesel Motors (renamed Isuzu Jidosha in 1949) built an underground plant in Nagano, to which it moved its machine tools, but it was unable to begin production because there was no electric power connection. Many auto parts companies had similar experiences.

Other problems plagued the industry. The equipment that was available at the end of the war was outdated and worn. There was a scarcity of parts and raw materials, especially of steel and rubber. Many trained engineers also had been moved out of the automobile industry to aircraft factories.

Besides the physical damage, Japanese automobile executives had other reasons to fear that the future of the industry was in jeopardy.³ The army had designated and used motor vehicles as a military commodity. Executives wondered whether the Occupation authorities would treat the automobile industry as a military or a civilian industry. This fear gained credibility when, initially, some motor vehicle plants were designated for possible reparations and only limited production of trucks was permitted. Second, General Motors and Ford had dominated the Japanese automobile market before the war. If the American companies were permitted to reenter Japan with their markedly cheaper and better quality cars, Japanese firms could not compete.

In the final analysis, these two problems never materialized. The Supreme Commander for the Allied Powers (SCAP)

determined that the automotive industry was not a good candidate for reparations.⁴ In a letter dated December 26, 1945 to Ambassador Edwin Pauley, head of the U.S. Reparations Mission to Japan, H.D. Maxwell, Chief of Staff for SCAP, recommended:

The automotive industry as such should not be considered available for reparations. The Japanese should be allowed to decide what they want to allot to their automotive industry in the way of steel and machine tools out of what is left to them after reparations. Under these conditions, their automotive industry would be on a smaller scale.⁵

This recommendation was accepted by Ambassador Pauley. Toyota, Nissan, and Kawasaki Engineering (originally part of Mitsubishi Heavy Industries) were removed from the reparations list—Toyota in July 1946, the others in May 1948—and the production of civilian vehicles was gradually allowed to begin.⁶ Diesel Motors and Kohsoku Engineering (Ota Jidosha) were never designated for reparations.

The American companies did not rush into the market because of import controls and, more importantly, because they could not fill the burgeoning domestic demand in the United States.

In the initial months after the end of the war, only Toyota was able to continue production of vehicles. On August 18, Kiichiro Toyoda met with Ichibei Terasawa, who headed the automobile section of the Machinery Bureau of the Ministry for Military Procurement.⁷ Kiichiro Toyoda said, "The Toyota factory will continue production" and informed Terasawa of the amount of raw materials on hand. Toyota managed to produce 602 vehicles of various types between August and November. Nissan and Diesel Motors, however, were not able to restart production until November. In addition, Toyota and the other companies directed their employees to produce other items such as metal cookware and furniture in order to survive. All three major companies were ordered to help repair and refurbish vehicles for the Occupation authorities, which also helped them to survive.

On August 21, the Tuesday after the armistice, Kiichiro Toyoda chaired a meeting between Japanese government representatives from the Ministry of Commerce and Industry and the Ministry of Transportation, including Mr. Terasawa, and the top executives of Toyota, Nissan, and Diesel Motors to discuss the overall situation and decide how to deal with the coming occupation.⁸ Similar meetings were held twice a week in the next few

months. A formalized arrangement began with the establishment of the Automobile Conference (Jidosha Kyogikai) on November 25 for the purpose of rebuilding the automobile industry.⁹ The Japan Automobile Manufacturers Association (JAMA), the industry's current trade association, had its roots in these organizations that were formed to lobby General Headquarters (GHQ) and then later the Japanese government, for import protection and low cost loans.¹⁰ This organization partially took over the role of the Automobile Manufacturing Industrial Association, the wartime control association for the automobile industry, which was disbanded on November 14. While the Conference did not have direct control of the Automobile Manufacturing Industrial Association, it did have some authority for distribution and allotment because of the scarcity of raw materials.

When SCAP decided that "the Tosei Kai [control associations] performed so many undesirable functions that mere refurbishment to perform allocation functions would only be more difficult than the creation of a new allotment system," the industry was again reorganized.¹¹ In August 1946, SCAP directed the Japanese government to dissolve the existing control associations. The Economic Stabilization Board (Keizai Antei Honbu) then designated newly created public associations as auxiliary allocation organizations. There were seven such associations designated for the automobile industry, the most important being the Automobile Manufacturers Association (Jidosha Seizo Kogyo Kumiai), which had been established on December 17, 1945 by Toyota, Nissan, Diesel Motors, and Mitsubishi Heavy Industries (also the core membership of the Automobile Conference).¹² This association was the first postwar automotive trade association.

Other prewar motor vehicle manufacturers could not enter the market as quickly as Toyota, Nissan, and Diesel Motors because the Automobile Manufacturing Law was not rescinded until January 16, 1946. Until it was rescinded, only the previously authorized companies could legally produce vehicles. More importantly, the other companies did not have the resources these three companies possessed because they had been forced to curtail their production of vehicles during the war.

The next entrants into the market were Mitsubishi Heavy Industries and Hino Jidosha Kogyo, both of whom produced weaponry and tanks during the war. These companies were followed by other manufacturers, mostly from the aircraft industry, who could no longer legally produce their traditional products and wanted to move into the motor vehicle sector. This movement was

more pronounced once it became clear that the motor vehicle industry would not be considered a military industry and would be removed from the reparations list. Estimates indicate thirty-two companies moved to the motor vehicle sector, most into auto parts manufacturing.¹³

The companies that eventually began production of four-wheeled vehicles included Tachikawa Aircraft, which became Prince Jidosha in November 1946 (later merging with Nissan in 1966), and Nakajima Aircraft, which became Fuji Heavy Industries (producing Subaru passenger cars). In addition, the major prewar three-wheeled vehicle producers, Mazda Motor Corporation (formerly Toyo Kogyo) and Daihatsu Kogyo, restarted production on December 1, 1945 and April 1, 1946, respectively. Both of these companies began production of four-wheeled vehicles in 1958.

At the same time, the Japanese bureaucracy in charge of motor vehicle production was reorganized. A controversy arose over whether the Ministry of Transportation (MOT) or the Ministry of Commerce and Industry (MCI) would have jurisdiction over motor vehicle production.¹⁴ During the war the Ministry of Military Procurement had jurisdiction, but before the war MOT and MCI had automobile-related programs. Around August 20, all the staff of the automobile section of the Machinery Bureau, except for Ichibei Terasawa and one assistant, were recalled to MOT. When the Ministry of Military Procurement was disbanded by imperial ordinance on August 26, the machinery bureau was transferred to the reestablished MCI.

MOT gained administrative authority over the distribution of automobiles and also wanted to control their production. It justified its position by the fact that it controlled the distribution and production of other types of transportation equipment including railroad carriages, ships, and airplanes. MOT formally petitioned MCI for production control in November, although there were earlier informal attempts to woo Mr. Terasawa. MOT officials had told him, "You can't accomplish anything working by yourself at MCI . . . Why don't you come to MOT if you want to work with motor vehicles?"¹⁵ MOT also attempted to pressure MCI through Diet hearings held by Ichizo Goto, the son of Shimpei Goto, a major prewar political leader. MCI supported its position, by emphasizing that the motor vehicle industry was integrally connected with the parts and machinery industries, which were part of MCI. The controversy ended when MCI formally established an automobile section on January 10, 1946.

SCAP Automobile Policy

Although automobile production after the war began through private initiative, it was subject to limitations imposed by SCAP. SCAP set initial policy on automobile production during the first month of the Occupation. Ichibei Terasawa lobbied SCAP on behalf of the automobile industry, stressing the need for trucks to transport food and other basic goods.¹⁶ On September 25, 1945, SCAP in GHQ Memorandum No. 58 gave Japan permission to produce 1,500 trucks a month, which was believed to be the minimum number required to fill the economy's transportation needs. On September 28, SCAP approved rubber imports in the amount needed to produce 1,500 trucks.¹⁷ The production of passenger cars was forbidden because the scarcity of raw materials necessitated that all resources go into truck production. Actual production did not reach the approved level until 1948 because of raw material and capital scarcity. Production finally increased as supplies of coal and steel became more available and Occupation policy was clarified. The latter point was especially important for Nissan since its holding company had been designated for dissolution on December 7, 1946 and Yoshisuke Aikawa, the founder of Nissan, had been purged.¹⁸

Another early result of Occupation policy was the establishment of labor unions as part of the democratization program. After the passage of the Labor Union Law on December 22, 1945, unions were formed in each of the automobile companies starting with Toyota on January 19, 1946 and Nissan on February 19, 1946.¹⁹ A national union, the Japan Automobile Workers Union (Zen-Nihon Jidosha Sangyo Rodo Kumiai), was formed in March 1948. Like many other unions at that time, its leadership was strongly leftist.

The unions did not strongly influence developments in the automobile industry during the Occupation except for the strikes during the recession of 1949. The major impact of the unions occurred during the Nissan strike of 1953.²⁰ As a result, the Japan Automobile Workers Union was disbanded in the fall of 1954. Another national union, the Federation of Automobile Workers Unions, was not formed until August 1962.

The automobile companies were anxious to restart vehicle production after the war. The importance of production was emphasized by the presence of the highly mobilized Occupation forces, with their extensive use of noncombat vehicles such as two-and-a-half ton trucks, jeeps, and trailers. The sight of these vehicles

inspired the Japanese to say that the *yamatosamashii* (Japanese fighting spirit) had been beaten by American *butsuryo* (massive materials and equipment).

The industry's executives were especially anxious to begin passenger car production because they saw this area, particularly the production of small-sized cars (1,000–1,500 cc), as the most promising for the future. In October 1945, Kiichiro Toyoda requested that his engineers develop a new passenger car.²¹ This car eventually became the first Toyopet.

The Automobile Conference submitted a petition on March 9, 1946, to the Japanese government requesting permission to restart passenger car production.²² This request was conveyed in April 1946 by the Japanese government to SCAP in a special request to permit the production of 200 passenger cars. SCAP rejected the request on April 12 in GHQ Memorandum No. 977-A. SCAP's internal memorandum for the record states the reason for the denial:

This decision was based on the fact that the available steel could be used to better advantage in the manufacture of motor trucks than in passenger car construction. The automobile industry was allocated steel for October, November and December 1945 but due to low steel production, no steel was actually received. During the last quarter of 1945 fiscal year or January, February and March 1946, of approximately 8,000 tons allocated, none was received. For the first quarter of 1946 (April, May, June), the automobile industry was allocated 3,500 tons of steel, or approximately enough for one month's production at the reduced schedules. In general, the automobile companies had been operating to date utilizing truck chassis, spare parts and assemblies held in stock. Such stock parts (truck) had now been practically depleted. Due to the insignificant steel allocation to the automotive industry and no apparent relief in the near future, it was considered more appropriate to utilize the proposed metal allocations in continuing the manufacture of truck chassis and for spare parts in order to place in operating condition thousands of deadline vehicles. Therefore on the basis of the overall critical steel production and the minute allocation of steel to the automobile industry, the authority to manufacture passenger cars at that time was not recommended.²³

In addition, the request was denied because Nissan and Toyota used identical engines in trucks and passenger cars, so that production of passenger cars would automatically reduce the number of trucks manufactured. SCAP also was concerned that passenger car production would use spare parts needed to repair out-of-service trucks.

The Japanese government submitted a second petition on January 23, 1947 entitled "Application for Permission to Manufacture Small-Sized Passenger-Cars." This petition was accepted and SCAP, in GHQ Memorandum No. 1715, agreed to permit passenger car production in June 1947.²⁴ Japan was permitted to produce 50 large-sized cars (greater than 1,500 cc) and 300 small-sized cars (less than 1,500 cc). Private use of passenger cars was still prohibited, with sales permitted only to hospitals, doctors, police, government agencies, public organizations, business firms, and taxi companies. In addition, the 1,500 production limitation on trucks was eliminated. The petition was accepted, and the production limitation on trucks was lifted because the supply of trucks had increased substantially in late 1946 when the U.S. Army released 17,000 surplus trucks and trailers to the Japanese government. Many of the surplus trucks were used to transport food and other basic necessities and others were converted into buses to transport workers. The supply of materials had also increased.

The fifty large-sized cars were to be produced from prewar stocks of parts and no totally new large-sized cars were permitted because they used the same engines and parts as trucks. The large-sized cars could only be sold "for use as taxicabs for the transportation of accredited commercial representatives of foreign governments and foreign business firms." These cars were built by Toyota, which made fifty-three such cars from stockpiled parts.²⁵ Small-sized cars, however, would not use the same parts or production facilities as standard-sized trucks so a higher production level was authorized although such production was not given any priority in the allocation of raw materials.

In November 1948, MCI requested permission from SCAP to relax the 300-per-year restriction on small-sized cars to permit the manufacture of 4,800 vehicles.²⁶ No response was received, and the Ministry of International Trade and Commerce (MCI became MITI in May 1949) again submitted requests in March and June 1949 for the manufacture of 3,000 vehicles, out of which 600 would be exported. Again, no responses were received. A formal petition was filed on July 14, 1949, followed by a final request in a letter on August 16, 1949.²⁷

The Motor Trade Industry Association, an export promotion association established in March 1949 and headed by Kiichiro Toyoda, submitted a report to SCAP in August 1949 entitled "The Problem of Small-Sized Passenger-Cars."²⁸ This report sought the elimination of restrictions so that production could be increased, thus lowering prices and expanding exports (Japan had exported two passenger cars in early 1949 to Southeast Asia). The three producers of small-sized passenger cars—Toyota, Nissan, and Kohsoku Engineering (Ota)—had by May 1949 already produced 983 cars since the relaxation of restrictions in 1947, thus exceeding a three-year quota in only two. SCAP issued an oral directive conveyed by Mr. Wesley Melyan of the Industry Division to MITI on June 17 suspending production. The makers responded they had overproduced because they expected a favorable reply to MITI's requests since the Economic Stabilization Board had approved a five-year plan in August 1948 to increase the production limit on small four-wheeled vehicles. Their report asked GHQ to make a decision on passenger car production quickly before the companies were even further hurt by the suspension.

Production limitations on passenger cars were completely lifted on October 25, 1949 in GHQ Memorandum No. 2053 as raw materials and fuel became available. GHQ, however, informally told MITI that it expected only 5,000 small passenger cars to be built in 1950; the number controlled by the allocation of petroleum products.²⁹ The decision to lift limitations was spurred both by the requests from MITI and the Motor Trade Industry Association as well as by the number of applications received from foreign investors to import American-made automobiles to use as taxis. By 1949, the majority of prewar passenger cars still used as taxis were on the verge of complete breakdown. Because of foreign exchange constraints, SCAP and the Japanese government felt that it would be better to fill the demand for new vehicles through domestic production rather than imports.

The final decision to permit unlimited production of passenger cars was also based on the hope that the automotive industry could develop as an exporter and so lessen Japan's dependence on U.S. funds to pay for imports. A 1950 SCAP monograph stated:

As for Japan's foreign markets for automobiles, it can be said that any country in the world that has an automotive transportation system and has no automotive industry of its own is a potential market for Japanese automotive equipment. It is estimated that in the Asiatic areas

remaining open to Japanese automotive equipment, there are more than 200,000 trucks in use. This is a potential and immediate market for 33,000 replacement vehicles based on a 6 year life for the vehicles. If Japanese manufacturers secure only one-third of this potential business, there is a possible export of 11,000 trucks annually to Asia alone. However, to capture this and other markets, it is recognized that it will be necessary for the automotive vehicle producers in Japan to lower the selling prices to within a competitive range of automotive producers in other parts of the world, and at the same time improve and modernize these same vehicles.³⁰

Studies of the Japanese automobile industry pay scant attention to the early Occupation although they do attribute the delay in the start of a passenger car industry to SCAP policy in this period.³¹ However, even if passenger car production had not been prohibited prior to 1949, the companies were not in a position to immediately restart production because of the wartime controls restricting passenger car production and research. Therefore, it is difficult to attribute the delay in passenger car development primarily to Occupation controls on production. Certainly, the controls imposed on truck production had much less impact than the scarcity of raw materials.

Early Government Support

MCI's Five-Year Plan

The automobile industry began to recover slowly but it soon became apparent that it would be difficult to obtain adequate financing and raw materials without the strong support of the government. MCI had been sympathetic to the needs of the industry and had fought to maintain jurisdiction over automobile production, but had been too preoccupied with the restart of basic industries like steel and coal to do anything more. The automobile industry felt that it had not received adequate assistance or been allocated adequate supplies under the Temporary Law Regarding Material Demand and Supply Adjustment. The private sector decided to take the initiative in seeking government support under the priority production system.

The industry's leaders met in Tokyo at the Automobile Industry Crisis-Relief Convention (Jidosha Sangyo Kikitoppa Taikai) in January 1947 to decide the best way to garner concrete government support.³² Representatives from management, labor unions, and automobile-related industry associations attended this meeting, which resulted in the establishment of a standing committee, the National Automobile Industry Revival Conference (Zenkoku Jidosha Sangyo Fukko Kaigi), in April 1947.

This Conference declared that the only way to restore the motor vehicle industry was through the positive cooperation of management and labor. A proposal submitted to the Economic Stabilization Board and MCI stated that first a policy plan should be developed for the motor vehicle industry based on the opinions of the Revival Conference.³³ Second, the motor vehicle industry should be designated as an extra important industry like the steel and fertilizer industries. And third, adequate capital and raw materials should be assured. Six automobile-related trade associations submitted supporting petitions.

The Economic Stabilization Board responded with two recommendations.³⁴ First, the automobile industry should develop through imported technology. And second, the government should provide assistance through the Reconstruction Finance Bank (Fukko Kinyu Ginko). These recommendations were then given to MCI, which responded with the Five Year Plan for the Automobile Industry (Jidosha Sangyo Go Ka Nen Keikaku) in mid-August 1948, a part of the national five-year economic plan known as the Economic Rehabilitation Plan.³⁵ The details of this plan were further clarified with the release on October 28 of the Basic Policy for the Automobile Industry (Jidosha Kogyo Kihon Taisaku).³⁶

The premise of this policy was that Japan's transportation needs could not be filled by imports; therefore, the domestic industry should be supported. For such a policy to succeed, the industry would have to be able to obtain capital, raw materials, electricity, and labor. In addition, technology would have to be brought in from overseas and a council established to manage the plan. Private companies such as Toyota, Nissan, and Diesel Motors developed their own five-year plans to complement the MCI policy.³⁷ The Basic Policy itself included the following general points³⁸:

1. In order to fulfill Japan's transportation needs, the production of domestic vehicles will be increased because the need cannot be fulfilled by imports. The planned increase in transportation capacity (the

amount of freight transported by truck) is from 260 million tons in 1949 to 384 million tons in 1953.

2. Used cars from Occupation personnel could not be relied upon because their fuel consumption was inefficient and replacement parts were difficult to find.
3. The main target of future exports should be the Asian market.
4. When appropriate, officially decided automobile prices will be abolished.
5. Controls will be gradually relaxed on the distribution of automobiles.

In addition, there were specific plans made for each type of car³⁹:

1. Truck and Bus Chassis – Since Japan is capable of producing chassis comparable to foreign products, there is no need to change the way they are produced. Small modifications will be made to increase efficiency, raise quality, and lower prices. Mergers among producers such as Nissan, Toyota, and Diesel are not suitable to achieve the five-year plan; management should be rationalized and mass production established step by step.
2. Small-Sized Four-Wheeled Vehicles – Both trucks and passenger cars can fulfill the requirements of the market. Japan needs to establish new plants and equipment, while striving to ease the production limitation on passenger cars, presently at 300 a year.
3. Large-sized Automobiles – Japan should attempt to change large cars to diesels and develop diesel technology.

Finally, the policy outlined the targeted production levels, which were based on the expected level of rubber imports.⁴⁰ The production level for normal-sized trucks and buses was to increase from 19,500 in 1949 to 25,500 in 1953. Similarly, the production level for small-sized four-wheeled vehicles was to increase from 8,070 in 1949 to 21,700 in 1953 (see table 2).

Table 2
Ministry of Commerce and Industry's
Five-Year Production Plan
(in number of units)

Year	Ordinary-Sized Vehicles (Truck and Bus)	Small-Sized Four-Wheeled Vehicles (Truck and Car)
1949	19,500	8,070
1950	23,000	14,800
1951	25,500	18,800
1952	25,500	21,510
1953	25,500	21,700

Source: Nihon Keizai Shimbun

The Reconstruction Finance Bank

The Reconstruction Finance Bank (RFB) was established on January 24, 1947 to help restore Japan's production levels. The automobile industry's appeal for funding was based on the following points⁴¹: The automobile industry is indispensable in the war recovery effort; Japan cannot depend on imports when the United States cannot meet its own demand; the Japanese shipping industry received heavy damage during the war and so is unable to transport automobiles, while American shipping is filled to capacity carrying materials needed for the Occupation; and, Japan is short of foreign currency, which must be used first to fulfill basic needs, not to import automobiles.

The major companies in the automobile industry obtained loans from the RFB. They were supported in this effort by their labor unions, which included many returning war veterans who would have lost their jobs if the funding had not been forthcoming.⁴² MCI supported the loans, but the companies' success was due primarily to their own lobbying. Part of the debt of Toyota, Nissan, and Diesel Motors to the city banks was changed to guaranteed RFB loans. In fact, the very first loan given by the RFB went to Toyota. Out of Toyota's total debt of \$1,750,000 at the end of 1948, just over \$1,000,000 was owed to the bank.⁴³ Diesel Motors received a loan of \$1,950,000. At the beginning of 1950, the automobile companies

were still indebted to the bank for a total of \$3,683,333: Nissan for \$1,388,889, Toyota for \$1,344,444, Isuzu for \$658,333, Hino for \$163,889, and Mitsubishi for \$100,000.⁴⁴

The Basic Policy had to be abandoned because of the recession that began to develop in late 1948 and worsened with the institution of the Dodge Line in April 1949. Therefore, the loans from the RFB were not able to put the industry on a firm foundation.

Although the initial government effort to aid the automobile industry was interrupted, it was significant for the government-business relationship. The effort to obtain government support forced the private sector to voluntarily organize into trade associations. The two most important were the Automobile Manufacturers Association, which became the Automobile Industry Association (*Jidosha Kogyo Kai*) on April 1, 1948, and the Japan Small Car Manufacturers Association (*Nihon Kogata Jidosha Kogyo Kai*), established on March 29, 1946. The automobile industry had no previous experience in setting up this type of voluntary association. The only industry associations before and during World War II were in reality control associations. The new trade associations had to learn to consolidate their members' views if they were to win government support in an era of scarcity.

The joint effort by government and business to develop a five-year plan and to rescind the limitations imposed by the Occupation represented the start of a cooperative effort in economic development. It also represented the beginning of a real commitment by MCI and its descendant, MITI, to support a domestic automobile industry. This support was still primarily for the production of trucks, but the inclusion of passenger cars was now given serious consideration. In addition to pressure from manufacturers in favor of making passenger cars, MCI took into account the interests of consumers who wanted their own cars.⁴⁵

Hard Times

The Dodge Line

The initial government program to aid the automobile industry was interrupted by nationwide economic problems. The Japanese economy had suffered from chronic inflation since the end of the war, and, as production recovered, steps were taken to bring it under control.

On December 18, 1948, the Nine Point Stabilization Program was published jointly by the U.S. Department of State and the U.S. Department of the Army. This program was precipitated by the failure of the Japanese government to control inflation and the downfall of the Ashida cabinet in October 1948. In February 1949, Joseph Dodge, a Detroit banker, was sent to Japan to draft and implement a drastic deflationary program, the Dodge Line, that had five objectives. These were a balanced budget (actually a surplus budget), the reduction and elimination of government subsidies, the suspension of new loans from the RFB, a fixed foreign exchange rate of 360 yen to the dollar, and the creation of the Counterpart Fund Special Account.⁴⁶

The Dodge Line was successful in reducing inflation, but it also threw the nation into an economic crisis. The immediate effect was to undermine the system of priority production and the Economic Rehabilitation Plan. Japan suffered from massive unemployment, widespread bankruptcies, and a stagnant economy.

The effect on the automobile industry was enormous since it was a consumer goods industry and had relied heavily on RFB financing. Like other industries, it experienced slack sales and large accumulations in inventory. The companies had large, uncontrolled debts, and the banks were refusing to honor installment sales vouchers. In addition, sales controls on automobiles were abolished in April, throwing the automobile companies into an intensely competitive free market.⁴⁷ Even the strongest three companies, Toyota, Nissan, and Diesel Motors, were soon in dire straits.

Nissan was forced to lay off 1,811 employees in October 1949 and cut wages by 10 percent.⁴⁸ Diesel Motors abolished its labor union agreement, laid off 1,271 out of 5,474 employees, and shut down factories in Aomori, Nagano, and Sugi.⁴⁹ As a result, the company suffered the greatest setbacks because it was overstaffed with more than 8,000 workers as of April 1950 and had management problems.⁵⁰

The Toyota Reorganization

By the end of 1949, Toyota was on the verge of collapse. It was forced to scale back production plans for 1950 from 15,840 to 3,000 vehicles and shut down two factories, Shibaura and Ikamata, in the Tokyo area.⁵¹ Kiichiro Toyoda promised that he would not lay off workers, but employment in subsidiaries fell by 23 percent. Toyota itself accepted the voluntary retirement of 1,600

workers at its main office. Wages were cut by 10 percent for everyone.

Toyota could not raise the approximately \$560,000 it needed to stave off bankruptcy so it took an unprecedented step: it asked the Bank of Japan (BOJ), the central bank, for a loan. Mr. Shotaro Kamiya submitted Toyota's request for \$560,000 in late 1949 to Mr. Takeo Takanashi, the Nagoya district office director of BOJ.⁵² This request was an unprecedented move for two reasons. First, BOJ was not in the business of giving loans to private companies, only to other banks or government agencies. Second, the governor of the Bank of Japan, Naoto Ichimada, was a well-known opponent of industrial development based on heavy industry and of the automobile industry in particular.

Luckily for Toyota, Mr. Takanashi decided to support them.⁵³ He conducted detailed research on Toyota's financial background and was able to overcome tough opposition to the loan from the main office of the Bank of Japan by stressing that the economy of the Nagoya region would collapse if Toyota went bankrupt. BOJ finally arranged a loan for Toyota by forming and leading a syndicate of twenty-four banks including the Mitsui and Tokai Banks.

The loan was granted only after the company met four major conditions.⁵⁴ First, Toyota's sales and manufacturing divisions were to be split into separate companies. Second, the manufacturing division was to produce only the number of cars that the sales division could sell. Third, personnel were to be rationalized (fired). And fourth, outside personnel were to take over the company's management.

The first two conditions were easily accepted. Shotaro Kamiya was already in favor of separating the two divisions. The company history of Toyota Motors Sales Co., Ltd. states: "In truth, this separation was Kamiya's dream for a long time; in other words, this plan and Toyota's previous plan matched."⁵⁵ On April 3, 1950, Toyota Motor Sales Co., Ltd. was established with Shotaro Kamiya as its first director. It began operations on July 1 with initial capitalization at \$222,222. The second condition was imposed because of Toyota's huge inventory, which resulted in its assets being tied up as inventory. A plan was developed whereby production plans would be made only after an order was received from the sales company.

The second two conditions were much harder for Toyota to accept. Kiichiro Toyoda initially said: "I can accept the separation plan if I can avoid firing people and avoid bankruptcy."⁵⁶ Ultimately, Kiichiro Toyoda had no choice but to give in to the bank

and cut personnel. Employment dropped from 8,112 to 5,994, which precipitated a major strike at Toyota that lasted from April 7 until June 14, 1950 and brought the company to the verge of collapse for a second time in one year.

The last condition was the most difficult to accept. Toyota was a family-run company, but the banks and the labor union demanded a complete change of management. A compromise resulted in the resignation of Kiichiro Toyoda and the selection of Taizo Ishida, a cousin of the Toyoda family and the president of Toyoda Automatic Loom, as his successor. Bank representatives assumed management positions in Toyota Motor Sales (Takeshi Nagai from Tokai Bank) and Toyota Motor Corporation (Fukio Nakagawa of the BOJ). Taizo Ishida stated that he was called to a meeting in late May with Risaburo, Kiichiro, and Eiji Toyoda. Kiichiro Toyoda told him, "The bank suggested using outside personnel but this is the only condition we cannot accept."⁵⁷ The banks were willing to accept Taizo Ishida because he had established a good reputation as a manager at Toyoda Automatic Loom and was currently helping with the strike at Toyota Motor Company. Ishida took over the company formally in July but was effectively in charge by mid-June. In his resignation, Kiichiro Toyoda stated:

I think that I'll quit Toyota Motor. It is my beloved child. This child is grown up enough to no longer need parents; me. And now, he behaves in his own way. . . . I hope that Toyota Motor will disappear from my mind.⁵⁸

Toyota and the other automobile companies were still in trouble in June 1950 but had already begun to restructure after surviving the initial impact of the Dodge Line. Toyota Motor Sales' monthly installment sales plan was an example of the restructuring process that went beyond basic cuts in production and personnel. This process was greatly expedited by the outbreak of the Korean War on June 25.

The Korean War Boom

The special procurement of Japanese goods by the United Nations forces during the Korean War brought about an economic boom not just for the automobile industry but for the economy as a whole. Japan was the best source of emergency supplies due to its

location and its existing industrial base. The special procurements wiped out surplus inventories, raised production, and brought in needed foreign exchange. Industrial production by the end of 1951 surpassed its prewar peak, and the Special Foreign Exchange Account, which had stood at \$200 million at the end of 1949, had grown to \$940 million by the end of 1951.⁵⁹ Income from procurement in the broad sense of goods and services for the war and the reconstruction of the South Korean economy amounted to between \$2.4 and \$3.6 billion dollars between 1950 and 1955.⁶⁰ Most importantly, the boom occurred when Japan's economy, still suffering from the deflationary policies of the Dodge Line, was at a very crucial point in deciding the direction and success of postwar economic development.

The automobile industry benefited greatly from the economic boom. The U.N. forces ordered trucks and related parts and equipment from the Japanese automobile and parts manufacturers. Taizo Ishida said, "This is a good chance that comes only once in 1,000 years. Don't argue sales or manufacturing. I want to get [an order for] one more truck or jeep than Nissan or Isuzu."⁶¹ He succeeded in this endeavor. By the end of the war, Toyota had received orders for 5,629 vehicles while Nissan and Isuzu had sold only 5,035 and 1,256, respectively.⁶²

The Military Supply Agency (MSA) ordered 10,321 trucks from Japanese companies between 1950 and 1953, as well as related equipment such as buses, engines, dump trucks, and weapon carriers (see table 3). The majority of the orders came in the second half of 1950 with a few later as needed for reconstruction work. Toyota and Nissan received the majority of the orders, with Isuzu and the smaller firms also receiving a share. For example, Toyota supplied 2,750 gasoline-powered cargo trucks, 500 dump trucks, 54 tank trucks, and 150 weapon carriers in the first and second procurement orders.⁶³

The procurement orders aided the Japanese automobile industry by eliminating inventories, increasing production, and raising profit levels. These orders also provided the funds for the rationalization and modernization measures needed to provide the industry with a stable base for future growth. Nissan upgraded its plant by using \$56,000 from the Counterpart Aid Fund of the United States to import manufacturing equipment to make trucks for use in the Korean War.⁶⁴ Demand enabled the automobile companies to charge the United Nations' forces high prices for their products. The price for trucks rose from \$1,475 in July to \$2,788 in

December 1950—an increase of 89 percent.⁶⁵ Before procurement began, the same trucks were selling on average for \$1,250.⁶⁶

Table 3
Procured Military Vehicles
During the Korean War, 1950-1953
(in number of units)

Year	Cars	Trucks	Buses	Total
1950	--	4,365	--	4,365
1951	--	5,945	50	5,995
1952	--	10	--	10
1953	--	1	--	1

Note: Available statistics vary. The actual number of procured vehicles is probably somewhat higher than the official listings.

Source: Japan Automobile Manufacturers Association.

This rapid price increase meant that large amounts of capital became available to the companies. It is no surprise that major investments in plant and equipment began in 1951. From 1951 to 1956, investments in plant and equipment for seventeen companies that produced completed cars and chassis (ordinary, small, and three-wheeled) reached nearly \$82 million (29.5 billion yen). The price increase also engendered complaints about price gouging by the United States soon after Japan's independence in 1952. Hearings were held in Japan's National Diet that year, but the issue was resolved in favor of the Japanese automobile companies. Taizo Ishida testified:

In what kind of world does such a ridiculous story exist that merchandise after it is bought is said to be too expensive and the price is asked to be lowered. Should I ask for a discount on the machinery we have already bought from the United States? . . . Only once or so a poor Japan profited from the rich. We should not get agitated about this.⁶⁷

On July 8, 1950, the Japanese Self-Defense Force (SDF) was founded with 83,000 members and quickly became another important customer for the automobile industry. In the twelve-month

period from July 1950 to July 1951, the SDF bought 2,259 trucks from Japanese automobile makers.⁶⁸ While not as large as the special procurement purchases, these purchases were important to the revitalization of the industry. As the Korean War came to an end, the automobile companies hoped to sell as much as 20 percent of their production to the SDF and were optimistic about the future once the era of large special procurements of motor vehicles came to an end.⁶⁹

Several scholars, including Chalmers Johnson, feel that the Korean War special procurement was "the key to the revival of the Japanese automobile industry."⁷⁰ Unquestionably, the special procurements were an enormous help because they forced companies to restructure: a process that they were able to carry more quickly to fruition because of purchases by the SDF and by U.N. forces in Korea. It is important to note, however, that the restructuring process, as evidenced by the changes at Toyota, was already beginning before the Korean War. The war hastened the process, but given the prior support for the industry by MCI, it is likely that the automobile industry would have developed even without the benefit of the special procurement, although not as quickly. Michael Cusumano adds that the procurements were useful experiences for the companies in learning techniques of technology transfer and mass production.⁷¹

In addition, special procurement was only for trucks and truck-related equipment, not passenger cars. The truck industry by 1950 was already firmly established in Japan. The procurement of trucks did indirectly affect the development of passenger cars by providing the companies with the funds necessary to carry out research and development. Additional funds by themselves, however, did not ensure the growth of a passenger car industry.

The period of hard times that ended with the Korean War had a substantial impact on the later growth of the automobile industry. The special procurements were instrumental in reviving the industry. Also, by the end of this period, the government's ability to directly control the automobile industry was weakened as raw materials became more readily available and resource allocation controls were lifted. And, finally, it is important to note that while the Bank of Japan opposed the idea of a passenger car industry, it was unable to prevent its regional office from supporting Toyota.

Conclusion

The Occupation years form a critical period in the postwar expansion of Japan's automobile industry. Certain private and public policy decisions were made at this time that shaped the foundation of the industry. The events of the Occupation period and the period immediately after independence constitute the most dynamic era of developments in the relationship between the Japanese government and the automobile industry.

There are four specific developments that underscore this period's significance. Decisions that changed the direction of the economy as a whole also were reflected in specific developments in the automobile industry.

Strong voluntary trade associations were established in response to powerful external pressures imposed by the end of the war and the demilitarization and democratization policies of SCAP. Although these associations went through various organizational changes in the ensuing years, their existence, combined with strong leadership provided by individual executives and the reshaping of the Japanese economy through Occupation policies, contributed to the development of the postwar government-business relationship. The partnership between government and business that had characterized the relationship prior to the war returned. Relations were different, however, because the private sector now took a much more active role in helping decide policy directions.

The relationship between government and business was also affected by the joint effort to plan the long-term development of the automobile industry. While this plan had many opponents and was terminated because of the deflationary impact of the Dodge Line, it represented the beginning of a new way of interacting. The strength of this new relationship was demonstrated when it survived the termination of various control measures over raw materials and distribution. Initially, the partnership survived because industry and government had to work together to overcome their perceived vulnerability to powerful foreign automobile companies who were capable of dominating the Japanese market and lobbying SCAP.

MCI's decision to regard the automobile industry as fundamental to the reconstruction of the economy meant it would receive special incentives and protection. Thereafter, MCI continued to strongly support the automobile industry in policy debates within the bureaucracy. Even though the makeup of the industry was as

yet undecided and basic industries still received much more support, MCI did not alter its essentially favorable position. This support became much more important in the first half of the 1950s after Japan regained total control over its economic and foreign policies.

The foundation for a stronger, restructured automobile industry began during the Occupation. The Dodge Line fostered the recognition of the need to restructure and provided the impetus behind many private sector entrepreneurs' decisions on the future direction of their companies. Certainly the automobile executives were well aware of their weakness in comparison to the American automobile industry, but they were forced to restructure to avoid bankruptcy. The special procurements from the United Nations and the SDF during the Korean War helped to ensure that this restructuring process had a good chance to succeed. The major issues remaining for the government and business to address in the 1950s were the threat of imports and foreign capital, and whether a viable passenger car industry, in addition to a truck industry, could be developed.

NOTES

¹Seisi Kato, *My Years with Toyota* (Tokyo: Toyota Motor Sales Co., Ltd., 1981), p. 43.

²C.S. Chang, *The Japanese Auto Industry and the U.S. Market* (New York: Praeger Publishers, 1981), p. 34 and Supreme Commander for the Allied Powers, Economic and Science Section, Industry Division, "Automobile Industry" (Typed Monograph, Tokyo, n.d.), pp. 19-20.

³A particularly succinct statement of these fears is found in "Ogata jidosha kogyo: saiken sangyo o genchi ni miru [The case of a revived industry: large-size automobiles]," *Jiji Shimbun*, 19 August 1948.

⁴H.D. Maxwell, Letter to Ambassador Edwin W. Pauley of U.S. Reparations Mission to Japan, 26 December 1945, p. 10.

⁵*Ibid.*

⁶Naokazu Yamamoto, *Nihon no jidosha: Toyopeto seichosi* [Japanese automobiles: history of the growth of the Toyopet] (Tokyo: Tokyo Sogensha, 1959), p. 210.

⁷*Ibid.*, p. 203.

⁸*Ibid.*

⁹Takashi Kawazoe, ed., *Nihon jidosha sogo nenpyo* [Comprehensive chronology of Japanese automobiles] (Tokyo: Nihon Jidosha Kaigisho, 1967), p. 2.

¹⁰Michael A. Cusumano, *The Japanese Automobile Industry* (Cambridge: Harvard University Press, 1985), p. 18.

¹¹SCAP, Economic and Science Section, Industry Division, "Automobile Industry," p. 35.

¹²Kawazoe, ed., *Nihon jidosha sogo nenpyo*, p. 2.

¹³Tadahiro Iwakoshi, *Jidosha kogyoron* [The automobile industry] (Tokyo: University of Tokyo Press, 1968), p. 261.

¹⁴The sequence of events surrounding this controversy is taken from an interview with Mr. Terasawa and Mr. Uchiyama published in Kuman Uchiyama, "Jidosha gyosei ichigenka koso no tenmatsu" [Aftermath of one-dimensional automobile administration] in *Nihon jidosha kogyoshi gyosei kiroku shu* [Collection of articles on the administrative history of the Japanese automobile industry], Nihon Jidosha Shinko Kai (Tokyo: Nihon Jidosha Shinko Kai, 1979), pp. 134-37.

¹⁵*Ibid.*, p. 135.

¹⁶Yamamoto, *Nihon no jidosha: Toyopeto seichosi*, p. 206.

¹⁷*Ibid.*

¹⁸The purge did not keep Aikawa from participating in the early trade association meetings on the future of the automobile industry in Japan. It was, however, one reason that Kiichiro Toyoda was installed as president of the Automobile Manufacturers Association. For more details on what happened to Aikawa during the Occupation see David Halberstam, *The Reckoning* (New York: William Morrow and Company, 1986), pp. 134-36.

¹⁹Yamamoto, *Nihon no jidosha: Toyopeto seichosi*, p. 209 and Ichiro Saga and Tokuichi Kumagai, *Nissan sogi 1953—tenkanki no shogen* [The 1953 Nissan conflict—turning point testimony] (Tokyo: Gogatsu Sha, 1983), p. 20.

²⁰Yamamoto, *Nihon no jidosha: Toyopeto seichosi*, p. 124 and Halberstam, *The Reckoning*, pp. 166-72.

²¹Taizo Yakushiji, "Dynamics of Policy Interventions: The Case of the Government and the Automobile Industry in Japan" (Ph.D. diss., Massachusetts Institute of Technology, May 1977), p. 180.

²²Ministry of International Trade and Industry, Machinery Bureau, "Kokusan joyo jidosha no rikai no tame ni" [In order to understand domestic passenger cars] (Handwritten, Tokyo, April 1952), p. 6.

²³SCAP, Economic and Science Section, Industry Division, "Automobile Industry," pp. 24-25.

²⁴Ibid.

²⁵MITI, Machinery Bureau, "Kokusan joyo jidosha," p. 6.

²⁶Motor Trade Industry Association, "The Problem of Small-Sized Passenger-Cars," (Typewritten Report, Tokyo, 23 August 1949), p. 5.

²⁷K. Tamaki, Director, International Trade and Machinery Bureau, MITI, "Production Schedule of Motor Vehicles," letter to Mr. Wesley Melyan, Machinery and Equipment Unit, Commodities Production Branch, Industry Division, ESS, GHQ, SCAP, 14 July 1949 and C. Mori, Chief, Vehicle Division, International Trade and Machinery Bureau, MITI, "Passenger-Car Production Program," typewritten petition to Mr. Wesley Melyan, Machinery and Equipment Unit, Commodities Production Branch, Industry Division, ESS, GHQ, SCAP, 16 August 1949.

²⁸Motor Trade Industry Association, "The Problem of Small-Sized Passenger-Cars," pp. 1-8.

²⁹SCAP, Economic and Science Section, Industry Division, "Automotive Industry," p. 29.

³⁰Ibid., pp. 41-42.

³¹For example, see Yakushiji, "Dynamics of Policy Interventions" and Tadahiro Iwakoshi, *Jidosha kogyoron* [The automobile industry] (Tokyo: University of Tokyo Press, 1968).

³²Yamamoto, *Nihon no jidosha: Toyopeto seichosi*, p. 209.

³³Ibid.

³⁴Hideko Magara, "Changing Relationship between the State and Business Associations: Is the Japanese Automobile Industry Corporatist?" (Master's thesis, University of Chicago, 1984), p. 21.

³⁵"Ogata jidosha kogyo: saiken sangyo o genchi ni miru," *Jiji Shimbun*, 19 August 1948.

³⁶Kawazoe, ed., *Nihon jidosha sogo nenpyo*, p. 19.

³⁷Hiroshi Arisawa, ed., *Nihon sangyo hyakku nenshi* [History of 100 years of Japanese industry] (Tokyo: Nihon Keizai Shimbun Sha, 1981), p. 62.

³⁸"Jidosha: yunyu mikomi nasi—kihonteki shinko taisaku kettei suru" [Automobiles: no prospect for imports—decision on basic promotion plan], *Nihon Keizai Shimbun*, 28 October 1948.

³⁹Ibid.

⁴⁰Ibid.

⁴¹Fubito Heiya, "Busshi chousei kan no toyo to fukkin kinyu" in *Nihon jidosha kogyo gyosei kiroku shu* [Collection of articles on the administrative history of the Japanese automobile industry], Nihon

Jidosha Shinko Kai (Tokyo: Nihon Jidosha Shinko Kai, 1979), pp. 171-73.

⁴²Halberstam, *The Reckoning*, p. 134.

⁴³Chang, *The Japanese Auto Industry*, p. 47.

⁴⁴Heiya, "Busshi chosei kan no toyo to kukkin kinyu," p. 171.

⁴⁵Akira Kawahara, interview held at Toyota Vista in Tokyo, September 1984.

⁴⁶Tatsuro Uchino, *Japan's Postwar Economy: An Insider's View of Its History and Its Future*, trans. Mark A. Harbison (Tokyo and New York: Kodansha International, 1983), pp. 49-50.

⁴⁷Kawazoe, ed., *Nihon jidosha sogo nenpyo*, p. 25.

⁴⁸Nissan Motor Corporation, *Nissan jidosha sanjunenshi* [Thirty-year history of Nissan Motor Corporation] (Tokyo: Nissan Motor Corporation, 1965), p. 215 and Cusumano, *The Japanese Automobile Industry*, pp. 147, 181-82.

⁴⁹Chang, *The Japanese Auto Industry*, p. 40.

⁵⁰Yamamoto, *Nihon no jidosha: Toyopeta seichosi*, pp. 217-18.

⁵¹*Ibid.*, p. 29.

⁵²Akira Hirotani, *Toyota no shinjitsu* [The truth about Toyota] (Tokyo: Diamond Sha, 1983), pp. 83-84.

⁵³*Ibid.*

⁵⁴*Ibid.*

⁵⁵*Ibid.*, p. 85.

⁵⁶*Ibid.*

⁵⁷Masajiro Ikeda, *Ishida Taizo keiei roku: Toyota shokon no genten* [The management of Taizo Ishida: The origin of Toyota's commercial spirit] (Tokyo: PHP Kenkyujo, 1984), pp. 142-43.

⁵⁸*Ibid.*, p. 145.

⁵⁹Uchino, *Japan's Postwar Economy*, p. 58.

⁶⁰*Ibid.*

⁶¹Ikeda, *Ishida Taizo keiei roku*, p. 152.

⁶²Arisawa, ed., *Nihon sangyo hyakku nenshi*, p. 63. These figures include trucks and other types of vehicles.

⁶³Yamamoto, *Nihon no jidosha: Toyopeto seichosi*, p. 225.

⁶⁴Cusumano, *The Japanese Automobile Industry*, p. 222.

⁶⁵"Fukkoki no jidosha gyosei" [Automobile policy during the reconstruction], *Nihon Keizai Shimbun*, 19 January 1951, p. 1.

⁶⁶"Tokuju appaku yoyaku jakuka" [Special demand pressure finally weakening], *Nihon Keizai Shimbun*, 19 January 1951, p. 1.

⁶⁷Ikeda, *Ishida Taizo keiei roku*, p. 156.

⁶⁸"Tokuju-yushutsu nosomi usu," *Nihon Keizai Shimbun*, 16 October 1951.

⁶⁹*Ibid.*

⁷⁰Chalmers Johnson, *MITI and the Japanese Miracle* (Stanford: Stanford University Press, 1982), p. 200.

⁷¹Cusumano, *The Japanese Automobile Industry*, p. 8.

CHAPTER 4

A CONSENSUS FORMED

Introduction

The enormous international success of the Japanese automobile industry is based on a competitive passenger car industry. Before 1950 the production of trucks and buses was the primary concern, but as the Occupation ended, the focus of the government and the private sector turned to passenger cars.

By the time of the Korean War, it was clear that a Japanese motor vehicle industry based on truck and bus production could survive, but the development of a passenger car industry was still viewed by many as a ludicrous idea. Koichi Shimokawa stated that there were two options in the early 1950s: to concentrate on truck production or to promote a strategic industry by the mass production of the passenger car.¹ As the early 1950s progressed, it was clear that the decision was in favor of passenger cars.

The first Japanese passenger cars built after GHQ lifted production restrictions in 1949 were little more than small trucks. Between 1949 and 1951 Toyota sold for use as taxis about 700 SD style passenger cars that consisted of small truck chassis with attached passenger car bodies.² In addition, these cars only had twenty-seven horsepower engines and, because of the truck chassis, very high floorboards. Needless to say, their quality, durability, and styling left much to be desired.

There were only two other companies making four-wheeled gasoline-powered passenger cars, Nissan and Kosoku Kikan Kogyo K.K. (renamed Ota Jidosha Kogyo K.K. in 1952).³ Together they produced 381, 1,070, 1,594, and 3,611 passenger cars in 1948, 1949, 1950, and 1951, respectively.

Three Challenges

Before a passenger car industry could be firmly established, certain challenges had to be faced and overcome. Weaknesses in the areas of technology, production, and capital were the foremost obstacles. But, before these weaknesses could be addressed, the industry had to tackle constraints imposed from outside. Government-business interactions took on their greatest significance in facing three challenges: domestic opposition, imports, and foreign capital.

Domestic Opposition

In spite of the industry's uncompetitiveness, the movement to establish a domestic passenger car industry had strong supporters. The strongest of these supporters were the three domestic producers (Toyota, Nissan, and Ota Jidosha) and MITI's Machinery Bureau. The manufacturers had been interested in passenger cars since prewar days and felt that it was nonsense to have a motor vehicle industry that only produced trucks. After all, the strength of the major world producers was based on passenger cars. They were aware, however, that their strength in those trucks that were not in direct competition with the products of foreign producers would help them to eventually compete with the world's established passenger car makers.

The Machinery Bureau supported passenger car development primarily because it was "the pinnacle of the modern machinery industry in our country [Japan] where there is no aircraft industry" and could promote the overall development of the rest of the machinery and the steel industry by providing a market, raising technology levels, and forcing increases in quality.⁴ The Bureau felt that since machinery held a great deal of promise as a future export, "it went without saying that Japan would have to promote manufactured exports."⁵ Reliance on imported passenger cars would entail "such a gigantic amount of foreign currency consumption" that the Bureau wondered "how could the Japanese economy which is trying to become independent [economically] spend so much."⁶ It was evident that Japan would have to have passenger cars from some source, initially for the taxi industry and eventually for personal use.

The manufacturers and MITI believed that passenger cars would add to Japan's international prestige. This belief is reflected in an April 1952 MITI report on the prospects for passenger cars:

Our country is one of twelve countries that produce passenger cars. These countries, except one or two, all are strong industrial countries. It is clear that in order to produce passenger cars a country's technical and industrial standards must be at a high level. Therefore, they are envied by those [countries] that cannot produce [passenger cars]. However, our country, which is producing passenger cars, how could we renounce their production (whatever the reason) and how could we set ourselves up as a second-rate technological country . . . The lowering of technical standards is unbearable for Japanese who have the self-pride to return to international society as a nation of culture.⁷

The supporters of the passenger car were influenced by concurrent developments taking place in Europe. The 1952 MITI report and the trade magazines of that period detailed the development of small passenger cars in Europe, especially the Volkswagen. Japan's advantage was that it could watch and follow car production trends in other countries, noting that Europe was starting to build small mass-use passenger cars rather than large luxurious models. But, before these groups could begin to establish a passenger car industry, they were forced to overcome opposition from within Japan.

The Bank of Japan was the major opponent of passenger car development. The Ministry of Transportation and the taxi industry, while not opposed to passenger car development, believed that imports were needed to fill demand. A discussion developed between opponents and supporters that lasted approximately from the authorization of passenger car production in 1949 until late 1951. Another round of discussions took place in mid-1952 as part of a broader debate on imports. Because it remained a policy disagreement and "never reached a confrontation or crisis stage," the debate had no clear beginning and end.⁸

While the opponents of the passenger car never had the power to prevent its development, the discussions revealed a lack of consensus on the future of the Japanese automobile industry, and on the much broader debate over the future structure of the Japanese economy. The disagreement indicated that passenger cars

still were seen by many Japanese as a nonessential luxury item that should not be produced in a period of scarcity.

The opponents were led by President Naoto Ichimada of the Bank of Japan, who was a proponent of industrial development based on light industry. He believed that Japan's comparative advantage in international trade was in this area, and passenger cars definitely did not meet this criteria. It is important that opposition to passenger cars remained part of the broader economic debate on Japan's future industrial structure and that passenger cars were not singled out more than other areas of development.

The opponents' position is capsulized in a famous statement Mr. Ichimada made to a reporter from *Nihon Keizai Shimbun* on April 12, 1950.

In discussing increasing exports, we have to follow the principle of the international division of industry. For instance, developing an automobile industry in Japan does not make much sense.⁹

Passenger cars were opposed for another reason. Most cars in Japan were large fuel-hungry American cars that were not really suited to Japan's narrow, poorly constructed roads and to its dependence on imported oil. A misperception existed among many Japanese that these cars were typical of those used by the rest of the world, which contributed to the feeling that passenger cars were not needed in Japan.¹⁰

Ultimately, the passenger car industry won support. C.S. Chang states that "the policy conflict was finally settled in favor of the motor vehicle industry by the outbreak of the Korean Conflict."¹¹ The growing demand for motor vehicles generated by the Korean War helped demonstrate that a motor vehicle—not necessarily a passenger car—industry could survive in Japan. MITI also argued that if 7,000 imported passenger cars each at a price of \$2,200 were required annually, the cost in foreign exchange would exceed \$15.4 million.¹²

MITI used the outcome of a driving test it held for passenger cars in November 1951 to persuade those unenthused about the development of the industry.¹³ The driving test took place over a 3,000 kilometer course and was supervised by university professors. Toyota, Nissan, and Ota each provided three passenger cars to be tested. On the first day, the cars drove 600 kilometers nonstop from Tokyo to Osaka in about fifteen hours. On the fifth day of the test, British cars were pitted against the Japanese

cars. MITI and the manufacturers proudly pointed out that all the Japanese cars completed the course, while only two years before in 1949 many cars failed to complete a less strenuous test.

Although agreement was reached to support the passenger car industry, the level of support was not as great as for basic industries such as steel and shipbuilding, especially in the area of financing. The level of support that developed, however, was sufficient to ensure the growth of a passenger car industry.

Two other obstacles remained. These obstacles were imposed from outside Japan in the form of imports of used and new cars, and in the possibility of foreign capital investments.

The Import Problem

Imported cars, which were lower in price and higher in quality, were the second threat to the establishment of a domestic passenger car industry. There was considerable domestic support for imports. But, a large number of imports could potentially impede or prohibit the development of domestic models. Imports came into Japan through two channels: new car imports and the transfer of used cars. The used cars were primarily American-made models, while the new cars increasingly came from Europe.

GHQ first permitted new-car imports in December 1948. In February 1949, an official organization, the Overseas Automobile Service (OAS), was established to supervise the import dealers. Many of these dealers had been importers in the 1930s and had organized the Federation of Foreign Car Dealers in October 1946 to lobby GHQ to lift import restrictions.

The OAS was set up by the 1949 U.S.-Japan Administrative Agreement (Nichibei Gyosei Kyotei), which established licensing procedures for all automobile imports. The new-car imports initially were subject to the provisions of the Foreign Exchange and Foreign Trade Control Act of 1949. Import authority subsequently was transferred to the Japanese government in March 1950. The number of new-car imports increased slowly during the Occupation, rising from 126 in 1948 to 4,719 in 1951. In 1948 all the imports were from the United States, but by 1951 just over one-third were from Europe. New-car imports were not seen as a major threat while they were subject to controls.

This perception changed in March 1952 when, with the expiration of the Temporary Materials Supply and Demand Control Law (Ringi Busshitsu Jukyū Chōsei Hō), the government removed most

controls over the import and sale of new cars. Some foreign exchange allocation controls did remain in place. Imported new cars peaked in 1953 at 5,170 as part of an economy-wide expansion in imports that year. This level was reached despite a 40 percent tariff on automobiles. The general import expansion was primarily due to the increase in industrial activity and employment from the Korean War. Higher incomes and purchasing power resulted in a domestic consumption boom that extended to imported automobiles that by then came primarily from Europe.

The 1953 increase in new-car imports created a minor controversy because it coincided with the general increase in imports and with a different and potentially more serious import threat—the Occupation's used-car problem. These two threats combined to create a sense of peril among the domestic manufacturers.¹⁴

The gravest and immediate threat to the Japanese passenger car industry was the sale of cars brought to Japan for use by the Occupation forces (see table 4). This threat was all the more ominous because of the large number of automobiles involved and the great difficulty in regulating their sale.

By 1950, many members of the Occupation were returning home and anxious to dispose of their cars, as was GHQ itself. Domestic producers, who were just beginning to manufacture passenger cars, were afraid that no one would buy their cars if the better quality and cheaper American cars were available. Consumer demand for the used cars was indeed extremely high.

The used-car problem developed because of five exceptions to the licensing provisions written into the 1949 U.S.-Japan Administrative Agreement. Passenger cars for the U.S. Army, passenger cars for civilians connected with the U.S. Army, moving vans, automobiles given as presents to either foreigners or Japanese, and vehicles for diplomatic use were exempted from tariffs and the commodity tax.¹⁵ The consequence of these exceptions—made to facilitate the import of cars for use by foreigners—was not foreseen in 1949.

The controversy began in March 1950 when GHQ's Economic and Science Section requested permission to sell 150 used Ford passenger cars to taxi companies in Yokosuka, Japan.¹⁶ The request was approved and foreign currency granted to complete the transaction in April. Later in April, GHQ informally asked MITI, through the Foreign Ministry, if \$500,000 could be allotted each quarter so that it could sell off 2,000 cars a year. The Automobile Manufacturers Association expressed its strong opposition to this

Table 4
Imports of Foreign Used Passenger Cars
During the Occupation, 1945-1952
(value in dollars)

Country/Model	Number of Vehicles	Value of Vehicles
United States		
Buick	276	588,004
Cadillac	22	67,205
Chevrolet	465	692,336
Chrysler	70	153,986
Dodge	166	304,835
DeSoto	59	116,440
Ford	275	416,879
Frazer	12	13,780
Kaiser	8	10,930
Hudson	37	59,894
Lincoln	22	46,700
Mercury	98	180,533
Nash	52	84,040
Oldsmobile	95	206,841
Packard	77	157,821
Plymouth	144	190,069
Pontiac	148	308,287
Studebaker	44	70,840
Willys-Overland	10	11,945
Jeep	2	800
Henry J.	2	2,500
Great Britain		
Austin	15	19,070
Hillman-Minx	10	13,220
Jaguar	1	3,180
Morris-Minor	2	2,250
Morris Oxford	1	1,450
Humber	1	1,780
Rover	1	1,730
Standard	11	17,090
Triumph-Mayflower	2	2,580
Vauxhall	9	12,248
Prefect-Consul	1	1,480
France		
Citroen	3	3,250
Renault	1	1,050
Total	2,142	3,765,043

Source: Unpublished Ministry of International Trade and Industry survey of imports of used foreign passenger cars made on April 15, 1952.

request to both MITI and GHQ. MITI denied the request because "the production of Japanese passenger cars has only started very recently and is not on schedule. If we allow foreign cars to be sold, the Japanese automobile manufacturing industry will be pinched off in the bud."¹⁷ MITI formally gave four reasons for its decision¹⁸:

1. Domestic production of small passenger cars had not yet begun full operation.
2. At least three years were needed to put production on a normal schedule.
3. The used cars to be disposed of by American military personnel should be handled by OAS dealers through normal import procedures, or they should be exported to a third country.
4. Japan's limited foreign currency reserves must be used to import essential basic materials.

The Machinery Bureau of MITI at this time called in the three domestic producers of passenger cars and explained the GHQ request to them.¹⁹ MITI urged the companies to hasten the establishment of a domestic production system and to work to improve quality.

For a few months, it appeared that MITI's policy would not be seriously challenged. Several requests were made to buy American cars but none were granted. Finally in the fall of 1950, a request was received from the police that MITI could not turn down. The police complained that, because of the backwardness of their Japanese cars, they could not catch escaping criminals who were using American cars bought on the black market.²⁰ As a result, MITI pressed the manufacturers to produce passenger car models that would have more appeal to the police. Toyota responded by putting a more powerful engine in one of its cars. The new Japanese cars, really only test models with hand-tooled bodies, did not resolve the problem because they were still very expensive and of very low quality.

MITI agreed to make an exception for the police after they promised to support the domestic industry in the future. As a consequence, pressure increased from both GHQ and domestic groups, such as the taxi association and the newspapers, to permit more sales of Occupation used cars. The taxi industry was supported by the Ministry of Transportation (MOT) under whose jurisdiction it fell.

MITI entered into negotiations with GHQ and other government ministries in 1951 to decide the amount of foreign exchange that would be allocated to buy the used cars during Japan Fiscal Year 1951. MITI's policy was overruled by the other ministries led by MOT, and the amount decided upon was \$3.9 million, which was to pay for the transfer of 2,600 cars at \$1,500 each.²¹

Next, representatives of MITI's International Trade Bureau, Machinery Bureau, and Trade Promotion Bureau met with members of the Ministry of Transportation to set up licensing procedures for the sales.²² The result was an interministerial ordinance, the Regulation Regarding the Conveyance of Foreign Vehicles (Gaikoku Jidosha Uzuri Uke Kizoku) passed on June 9, 1951, formally delivered to GHQ on June 26, and effective until July 1, 1952. This ordinance included three points²³:

1. The license application must be submitted to MITI's Machinery Bureau; later a license would be granted jointly by MITI and MOT.
2. The transaction must be completed by using the foreign currency allocated for this purpose by the government.
3. Eligible purchasers included the news media, the police, hospitals, the Diet and the courts, taxi companies exclusively catering to foreigners, and others specially designated by MITI and MOT as contributing to economic and cultural promotion.

Three-eighths of the cars were to go to government and public officials, and five-eighths were to go to the private sector. From the amount allocated to the private sector, nine-tenths were assigned to businesses and one-tenth to private individuals.²⁴ On June 30, thirty companies were authorized as dealers; later on, three additional companies were added.

As the program commenced, MITI asked the three domestic manufacturers in September 1951 to comment on the effect the transfer was having on the domestic industry. The companies responded with a joint report on October 8, 1951.²⁵ They requested that the foreign exchange allocation for the transfer of used cars be minimized, if possible banned, and that an import tax be levied. This report also covered additional issues relating to the promotion of domestic passenger cars.

By the summer of 1952, the controversy over the future of imports again heated up. Discussions were held in the Cabinet and

in the Diet about the necessity for domestically produced cars. During the summer, the National Passenger Car Association, connected with the Automobile Manufacturing Association, submitted several petitions to the Diet, MITI, and MOT concerning imports and related questions, such as the creation of one administrative authority for automobiles.²⁶ At the hearing, "Discussion on the Need for a Domestic Passenger Car Industry" (Kokusan Joyosha no Hitsuyosei nisuite no Giron), held in the Transportation Committee of the House of Councillors on July 26, 1952, Mr. Chotaro Yanase of the Overseas Automotive Service presented statements in support of imports:

The lifetime of Japanese cars is short, most last only one or two years. There are 60,000 cars in Japan and the number is increasing by about 10 percent (6,000 cars) a month. Out of the 60,000 cars, 30,000 are old and will have to be replaced by new cars soon. But only 6,000 cars are expected to be produced in Japan. This proves imported cars are necessary.²⁷

Ultimately, the Japanese government allowed the guidelines on the import of Occupation used cars to lapse and permitted yen-denominated sales. Initially, the purchasers were still required to obtain permission from MITI, but this restriction was soon lifted. Subsequently, the number of used cars entering the Japanese market increased dramatically. Officially transferred cars are listed at 1,650 in 1951, 5,476 in 1952, and 13,467 in 1953. After 1953, the number decreased gradually. These statistics are not complete as the government was unable to track all the purchases, but the trend is accurate since the supply of these vehicles increased and then decreased.

MITI and the domestic industry tried but did not have sufficient leverage to prevail completely over GHQ and the domestic consumer interests. But, the consequences of the transfer of used cars and the smaller number of new-car imports was not as serious as they had anticipated. The foreign cars were absorbed primarily by taxi companies, satisfying consumer needs that the domestic industry was not yet capable of fulfilling. In this sense Mr. Yanase was correct. It was not until the introduction of the Toyota Crown and the Prince Skyline in 1955 that Japan had domestic passenger cars that could realistically compete for the taxi market.

One passenger car company, Ota Jidosha, was not able to overcome the pressure created by the imports and the release of the

used cars. Ota did not have the financial affiliations, technological capability, and other resources of a Nissan or Toyota to help it survive as a passenger car producer. It nearly went bankrupt in 1954 but obtained government loans through the Corporate Reorganization Law of 1952. It merged with Nihon Jidosha in April 1957 and, after several more name changes and reorganizations, was absorbed by Nissan in 1971 as Nissan Koki.

The importance of the increase in new- and used-car imports through 1953 was that it reinforced the perception that unchecked imports were a serious threat to the establishment of a Japanese passenger car industry. The Diet held more hearings in the summer of 1953 on the import problem. These hearings, which stressed the weakness of the domestic industry and called for infant industry protection, resulted in a reimposition of controls on passenger car imports on February 1, 1954.²⁸ The new controls stated that a foreigner or a Japanese could import only one car every two years on a non-foreign exchange basis and that these cars could not be resold for at least two years. These controls included cars imported for personal use or as gifts.

The hearings prompted Prime Minister Yoshida to issue guidelines in 1953 stating that central government agencies must buy domestic passenger cars.²⁹ Because government officials persisted in buying foreign cars, Prime Minister Hatoyama announced in January 1955 a Cabinet agreement on strengthening the guidelines. From April to December 1955, government officials bought 151 new passenger cars, of which 62 were domestic models. In the JFY 1956 budget, 63 million yen (\$173,000) was allocated to subsidize the purchase of 126 domestic cars by the various ministries. The average price of a domestic car was 850,000 yen (\$2,361) of which the subsidy would pay 500,000 yen (\$1,389), and the difference would come from each ministry's general budget. The government also moved to help eliminate the import threat by changing the tariff and commodity tax rates.

Foreign Capital

The most severe threat did not come from imports or domestic opposition but from foreign manufacturers who wanted to establish production facilities in Japan or buy existing Japanese companies. If foreign cars entered Japan through sales of completed cars, they could be controlled through foreign exchange quotas. But, if foreign cars were produced in Japan, many felt that all domestically owned

motor vehicle manufacturing would be destroyed. The memory of the strength of onshore manufacturing by General Motors and Ford in the 1930s helped to foster this perception.

The threat posed by foreign capital was very real in 1952. With the coming of independence on April 28, 1952, several foreign automobile companies planned to build knock-down (KD) assembly plants in Japan.³⁰ With the exception of Chrysler, the major firms exploring the Japanese market were all European. The American firms were not very interested in Japan because they had little excess capacity due to military demand, and they saw more potential in the European market.

Several small Japanese firms, who were interested in entering the automobile market, thought that they could accelerate their development by entering into agreements with foreign producers. MITI viewed this development as unhealthy both from the standpoint of excessive competition and because of the potential for takeovers by strong foreign firms.

By April, six companies had conducted market research studies of the Japanese market: Rootes, Renault, Standard, Opel, Fiat, and Chrysler.³¹ The Rootes Group led the movement and had already applied to the Foreign Capital Council for approval to set up a knock-down factory and had established a subsidiary in Japan, the Rootes Company.³² Standard, Fiat, and Renault also expressed interest not only in expanding their sales network in Japan, but in taking over existing companies through capital acquisition and in establishing knock-down production.

In May, the Foreign Capital Council asked MITI to comment on the Rootes application because government authorization was required under the 1951 Foreign Investment Law for all foreign capital investment.³³ Before MITI could respond, Fuji Jidosha and Chrysler submitted the first application for a technical tieup around June 1.³⁴ Fuji Jidosha had approached Chrysler about establishing a knock-down plant in Japan at a production level of 1,000 cars a year. Chrysler, interested in Fuji Jidosha's diesel technology, agreed to the arrangement. This application, along with the one from Rootes, forced MITI to come up with a concrete policy.

MITI countered in June 1952 with the "Basic Policy for the Introduction of Foreign Investment into Japan's Passenger Car Industry," which supplemented the automotive provisions of the Foreign Investment Law. It stated that the repatriation of earnings from foreign investment in marketing facilities was not guaranteed, and in production facilities only if it "contributed significantly to the development of domestic industry."³⁵

MITI stated in June that it would allow foreign firms to enter the market only through technical tieups with existing chassis makers. By limiting the tieups to chassis makers, MITI tried to ensure that only the stronger companies, who could better resist foreign takeover and better use the imported technology, would enter into agreements with foreign producers. Technical tieups were acknowledged as necessary to raise the level of Japanese passenger car technology to international levels.

MITI announced four additional provisions that it wished to see included in the technology contracts.³⁶ First, small European cars were more suitable than large American cars. Second, MITI supported the use of foreign currency allocated for the import of cars for the import of parts instead. It could, however, allocate only enough currency to build 1,200 cars per company. Third, the Japanese company should try to obtain the right to sell the knock-down cars in Southeast Asia. And fourth, if parts were initially imported, they should eventually be made completely in Japan.³⁷ These provisions had a direct impact on the way MITI responded to the applications from Rootes and Chrysler.

The Rootes application was rejected because the company wanted to set up its own knock-down plant and sales network. They next tried to develop an agreement with Ikegai Motors by which Rootes would set up a subsidiary, Rootes Motors Japan, to import parts for 1,500 cars a year.³⁸ Ikegai would then produce the knock-down cars that Rootes would sell. All investments would be made by Rootes, and all profits would be returned to England. MITI also rejected this plan. Ultimately, Rootes entered into an agreement with a major producer, Isuzu, to make its Hillman car in Japan under the terms set by MITI.

MITI also was not sympathetic to the Chrysler application because they felt that Chrysler's large cars were not suited for Japan. In July 1952, MITI suggested to Fuji Jidosha that it might allow the tieup at a production level of 500 a year.³⁹ Fuji Jidosha was forced to renegotiate with Chrysler until an agreement was approved in the fall that permitted Fuji Jidosha to import knock-down parts through Metropolitan (Chrysler's sales agency in Japan) using currency Metropolitan had been allocated for completed car imports. The agreement called for production of only fifty vehicles a month and the import of \$20,000 worth of welding and painting equipment from Chrysler. MITI felt that this production level would not have any adverse effects on domestic production. This agreement was not carried out because Chrysler decided against proceeding.

The technology tieup movement gained a great deal of momentum when Nissan began to negotiate possible knock-down production with Austin. In July 1952, the Austin representative for the Far East, Mr. J.V. Gray, arrived in Japan for discussions with Nissan. Nissan and Toyota (after the breakdown in Toyota's negotiations with Ford in 1950) had supported the domestic development of passenger cars.⁴⁰ The decision by Nissan, then the strongest Japanese producer, to enter into a technical tieup forced the government to make a final decision concerning these agreements.

The final decision, "The Policy Relating to the Treatment of Technical Tieups and Assembly Contracts in the Passenger Car Industry," was announced on October 3, 1952. The first contract to fulfill all of MITI's requirements was negotiated between Hino and Renault. At the time of its announcement, the president of Hino stated:

I believe that the only way to promote the Japanese passenger car industry is to tieup with Renault, do KD production and then domesticate [the car]. People say that a domestic car is more expensive than imports but I believe that this will upgrade production facilities and that domestication will make costs cheaper.⁴¹

The companies themselves were responsible for finding foreign partners and negotiating the contracts within the policy constraints imposed by MITI. This did not mean that all negotiated contracts were approved. Rootes had to rework its approach several times before it arrived at an acceptable agreement with an acceptable partner. Out of eleven tentative tieups, only four ultimately were accomplished. The seven abandoned contracts were Fuji Jidosha Kogyo/Chrysler, Prince Jidosha Kogyo/Morris Motors, Kyosan Seisakusho/Simca, Tokyo Jidosha/Standard-Triumph, Daihatsu Kogyo/Studebaker, Komatsu Seisakusho/Volkswagen-Benz, and Mitsubishi Nihon Jukogyo/Kaiser.⁴² The four contracts that received approval were Nissan Jidosha/Austin, Isuzu Jidosha/Rootes, Hino Diesel Kogyo/Renault, and Shin-Mitsubishi Jukogyo/Willys Overland.

The four companies that received approval were already among the major companies producing four-wheeled vehicles during the prewar and wartime eras. Mitsubishi Heavy Industries had been disbanded during the Occupation, resulting in the formation of three companies in January 1950 who all wanted to produce

automobiles: West Japan Heavy Industries (Mitsubishi Zosen), Central Japan Heavy Industries (Shin-Mitsubishi Jukogyo), and Eastern Japan Heavy Industries (Mitsubishi Nihon Jukogyo).⁴³ In June 1964 these companies remerged. Thus, while the government supported the development and protection of the passenger car industry, it did not protect all producers or would-be producers.

Policy Actions To Support Passenger Car Development

The strategy devised to encourage the development of the passenger car industry was a result of informal discussions between government and business, discussions that became especially important in late 1951 and early 1952 as independence approached. The policy statement released by the three passenger car makers in October 1951 in response to MITI's request for their views on the transfer of used cars also influenced the strategy used to develop the passenger car industry.

The makers stated that they had determined small-sized passenger cars were the most suitable for the Japanese people.⁴⁴ In order to compete with the foreign makers, mass production methods needed to be introduced, which would entail investments of \$830,000 over the next year. Appropriate government policies perceived as necessary by the makers were also outlined in the policy statement. These views were taken into consideration by the government as it drew up specific policies for automobiles during 1952. These were:

1. equipment investment loans from the Japan Development Bank;
2. the promotion of equipment imports;
3. the promotion of automotive parts imports;
4. a tax differential between large and small cars, in favor of small cars; and
5. a higher commodity tax on foreign cars.

In addition to responding to requests from the government, the manufacturers initiated discussions with government agencies.⁴⁵ For example, in 1950, the Automobile Manufacturers Association invited three MITI representatives from auto-related sections to their annual meeting on May 19 to discuss automobile issues. On

July 7, 1950, they similarly invited representatives from the Ministry of Transportation.

The foreign threats caused the companies to turn to the government for protection. MITI became convinced that a viable passenger car industry was possible, which might in turn raise the technological level of the machinery and steel industries and save foreign exchange. A report released in April 1952 detailed MITI's position. This report called for⁴⁶:

1. Aid in renewing plant and equipment, of which almost 50 percent required replacement or repair through the Enterprise Rationalization Law and loans from the Japan Development Bank.
2. Secure access to materials, parts, and electricity, including importation of special parts if necessary. Also, efforts to decrease the price and raise the quality of domestic materials such as steel and tires.
3. Introduction of technology from advanced countries. Foreign capital would be welcomed if it promoted exports and decreased imports by utilizing Japan's industrial potential.
4. Stabilization of demand by limiting imports of completed cars for use by foreigners, for technical research or other special needs. Also, efforts to promote the use of small cars by decreasing the commodity tax.

The views of MITI and the industry came together since both sides concluded that the infant automobile industry had enough potential to deserve protection. One Japanese scholar stated that they were chasing rainbows but it seemed at least worth trying.⁴⁷ By the time of independence, a policy that would give "minimum survival security" to the passenger car industry had been designed. The policy contained both protective and developmental measures. Details were changed or added in reaction to special interests, but the major tenets remained the same.

Protective Measures

There is little disagreement among scholars, even those who believe the private sector was primarily responsible for the development of the Japanese automobile industry, that protective measures

in the 1950s helped the industry. Michael Cusumano states that “a single policy—protection against imports—turned companies that would surely have been business failures into highly profitable operations.”⁴⁸

Four major types of protective measures were instituted: tariffs, a commodity tax, restrictions on imports, and restrictions on foreign capital. The measures were justified as necessary to protect the infant industry.⁴⁹

Japan’s tariff rate on passenger car imports in April 1951 stood at 40 percent, a rate that remained until 1955 when a differential was created for large and small cars.⁵⁰ The rate for small cars (less than 270 mm wheelbase) remained at 40 percent, while the rate for large cars (more than 270 mm wheelbase) was lowered to 35 percent. The tariff on trucks and automobile parts remained at 30 percent, the level set in 1951. The tariffs were progressively lowered for trucks in 1962 and for passenger cars in 1968 as the industry became competitive. Tariffs were lifted entirely in 1978 for passenger cars and trucks.

The commodity tax is a consumption or luxury tax paid by consumers upon the purchase of new trucks or passenger cars. In 1950, the commodity taxes on four-wheeled and three-wheeled cars were set at 30 and 25 percent, respectively. MITI suggested creating a differential for large and medium-sized cars in 1952, but this suggestion was not immediately carried out.⁵¹ In April 1954, after a lobbying effort by taxi drivers attempting to reduce the price of their small cars, the commodity tax was revised to 50 percent on large cars (304.8 mm wheelbase and greater than 3,000 cc engine), 30 percent on ordinary-sized cars (270–304.8 mm wheelbase and 2,000–3,000 cc engine), and 20 percent on small-sized cars (less than 270 mm wheelbase and less than 2,000 cc engine). This differential served to discourage imports since most imports were large cars falling under the highest tax rate. This tax was gradually reduced from 1962 and eliminated on April 1, 1989. It was replaced by a consumption tax of 3 percent on passenger cars with an engine size of 550 cc and under. A 6 percent tax will be levied on cars with larger engines until March 1992 when this rate will be dropped to 3 percent.

The major method of restricting imports was through foreign exchange allocation as well as transfer rules for used cars. The government used powers granted it under the Foreign Exchange and Foreign Trade Control Act of 1949 to determine through the use of quotas the purposes and purchases for which foreign exchange could be used. The controls were lifted for trucks and

buses in 1961. The controls on passenger cars were changed to volume allocations in 1964 and eliminated for completed car imports in 1965. The last remaining controls, on engine imports, were lifted in 1971. Foreign exchange allocation for automobile parts was not restricted until 1958 in order to avoid interfering with the technology tieups. Takafusa Nakamura observed that the foreign exchange allocation system (see table 5) for restricting the total value of imports turned out to offer at the same time a splendid means of protecting the industry. He states:

It had been government policy to foster the automobile industry since before the war, but by means of the foreign exchange allocation system, the government took steps to impose extreme restrictions on automobile imports over the next ten years or more [after 1949], steps that were the virtual equivalent of an import ban. Thus were created the conditions under which the automobile industry was assured of a secure domestic market for its development.⁵²

Table 5
Foreign Exchange Allocation for
New Passenger Car Imports, JFY 1954-1970
(in ten thousand dollars/number of cars)

Year	Amount	Number of Cars
1954	613	370
1955	920	545
1956	1,508	727
1957	1,836	904
1958	1,553	693
1959	2,226	942
1960	5,125	2,374
1961	8,224	3,749
1962	12,616	6,279
1963	23,069	11,704
1964	28,182	13,577
1965	28,100	13,492
1966	32,870	15,574
1967	34,083	15,108
1968	33,802	14,608
1969	45,774	17,527
1970	50,196	18,755

Note: After 1962, foreign exchange allocations did not specify end-use.

Source: Nissan Motor Corporation

The government was able to control foreign capital imports under the Foreign Investment Law of 1951 and the Basic Policy for the Introduction for Foreign Investment into Japan's Passenger Car Industry. Under the Foreign Investment Law, the government had to authorize all investment by foreign capital, thus keeping foreign investment out of areas where it could slow the development of important domestic producers. Foreign capital was permitted to enter only when it contributed significantly to the development of domestic industry. In the case of the automobile industry, foreign capital was not completely liberalized until April 1973.

The protection of the automobile industry should not be viewed as an isolated or exceptional case. In this period, Japanese policy makers were worried about many Japanese industries that they thought might be overwhelmed by foreign competition. Therefore, the Japanese government permitted virtually no imports of manufactured consumer goods. Foreign capital also was generally shut out. The widespread availability of protective measures, however, does not negate their impact on the automobile industry's development.

Developmental Measures

Developmental measures helped the industry overcome general structural problems. These measures included: loans from government institutions, special depreciation allowances, exemption from import duties on certain machinery and equipment, authorization of essential technology imports, and subsidies.

Loans from government institutions were almost entirely from the Japan Development Bank (JDB), which was founded in April 1951. Funding given to the automobile industry in the first half of the 1950s was marked for facility investment and went to the four major companies—Toyota, Nissan, Isuzu, and Hino—and later to the automobile parts industry. The JDB's twenty-five year history states:

From 1951 to 1952, 35 million yen [\$97,222] was given to finance equipment expansion and modernization for trucks and buses to fully prepare this area for production. The truck financing corresponded with the Korean War special demand and the development of electric power facilities. Bus financing was related to transportation difficulties. From 1953 to 1955, the entry of foreign

cars was prevented by promoting the function of domestic passenger cars. This was to try to save foreign exchange reserves. For this, 49 million yen [\$136,000] was provided in financing for foreign car domestication, the strengthening of passenger car production facilities, and rationalization. Further, in February 1956, JDB borrowed \$234,007,000 from the World Bank to lend to Toyota. Via this tied loan, the bank cooperated in Toyota's facility renewal through machinery importation.⁵³

Government-related loans in this period accounted for approximately 19.3 percent of capital, which included loans from JDB, the Long-Term Development Bank, and the Industrial Bank of Japan. JDB loans in later periods were directed toward weak production areas: automotive parts, industry rationalization, technology development, and pollution control.

The automobile industry's development was supported by access to special depreciation and related benefits under the 1951 Special Taxation Measures Law and the 1952 Enterprises Rationalization Promotion Law. These laws tried to encourage plant and equipment investment in key industries by providing a reduced tax burden via special depreciation on specified machinery. The automobile industry was designated a key industry in 1952. There was a special depreciation rate of 50 percent in the first year. In 1961 this was changed to 33.3 percent, and the official life of equipment shortened from 16 to 13 years. The rate was further reduced in three stages before being terminated at the end of 1975. Special depreciation also was included for research and development equipment and was divided into equal parts of 33.3 percent over a three year period. This was modified in 1961 and then eliminated in 1967. For example, between 1952 and 1955 Nissan concluded purchases of 271 machine tools totaling 3,629 million yen (\$10,080,555) under the special depreciation system.⁵⁴

Machinery needed to rationalize the industry was unavailable from domestic suppliers. Therefore, equipment was imported primarily from the United States. The government provided special foreign currency allocations and exempted the imports from the 15 percent (CIF) tariff. The automobile industry was the foremost user of this program, and its imports peaked in 1954. For example, Toyota imported from the United States 28, 44, 78, 24, and 60 machine tools in 1952, 1953, 1954, 1955, and 1956, respectively, which constituted 43.3 percent of its machine tool imports through

these years. After the early 1950s, the program was not as necessary because the earlier imports were in place and increased domestic production could fill new demand. The government accelerated this process by providing subsidies to domestic machine tool makers.

Direct subsidies to the automobile industry were not pervasive and seem to have been concentrated in the area of technology development. Hiroya Ueno and Hiromichi Muto estimate that during the 1950s the automobile industry received only about 369 million yen (\$1,025,000) in direct subsidies, which came from funds derived from bicycle races and appropriated for machinery promotion.⁵⁵ This money was dispersed through organizations like the Automobile Technology Association and the Japan Small Automobile Industry Association. The Automobile Technology Association, for example, set up a research committee, composed of both private and government representatives, that analyzed the performance and efficiency of imported foreign cars.

The final important area of government support was approval of technology imports. The government realized that imported technology was essential to quickly overcome the gap between Japan and more advanced industrial nations, but it added provisions to ensure that the technology would be domesticated. The most important technology imports arrived through the tieups approved for Nissan, Isuzu, Hino, and Shin-Mitsubishi. In addition, there were thirty tieups with foreign makers approved for the auto parts industry between 1951 and 1963.⁵⁶ The basis for these tieups was the Policy Relating to the Treatment of Technical Tieups and Assembly Contracts in the Passenger Car Industry released by MITI on October 3, 1952.⁵⁷ Its major provisions were:

1. Foreign capital for sales operations is not permitted in Japan.
2. Foreign capital for production, if it contributes to the development of the domestic industry, will be approved.
3. The remittance of royalties and patent fees will be guaranteed for foreign producers.
4. Within five years of the initiation of the technology contract, at least 90 percent of parts must be produced domestically (the parts were listed in accordance with their importance).
5. Manufacturing rights for foreign cars must be transferred to domestic companies.

6. The importation of raw materials not produced in Japan will be permitted.

In addition, MITI limited the number and the type of Japanese companies that could enter into technology agreements to two or three chassis makers. Four makers ultimately received approval: Nissan, Isuzu, Hino, and Shin-Mitsubishi. MITI clarified that foreign cars produced without meeting the domestication requirement would be treated as imports.

The process, while successful, was not without its problems. By 1955, MITI believed that the parts domestication process was proceeding too slowly, especially in the case of Hino and Isuzu, which were more inefficient and not as technologically experienced as Nissan. MITI suspected that Renault and Rootes were purposefully causing delays in approving Japanese-made parts in order to increase brand loyalty, hoping to someday enter the Japanese market independently.⁵⁸ In March, therefore, MITI issued "New Guidelines on the Domestication of Foreign Passenger Cars" (*Gaikoku Joyosha Kokusanka no Shinhoshin*), which stated that the foreign currency allotment given for KD production would be shortened to cover only 200 vehicles a month if the domestication progress was behind schedule.⁵⁹ If domestication was proceeding ahead of schedule, the foreign currency allotment would be increased. The guidelines then set up a concrete schedule for the completion of parts domestication. Hino, Isuzu, and Shin-Mitsubishi agreed to meet the schedule. Eventually, MITI agreed to extensions of the contracts for two years for Hino and Isuzu, and five years for Shin-Mitsubishi, with three conditions: the foreign partner allow export of the KD car, the Japanese company be allowed to buy the manufacturing rights to avoid patent royalties, and the Japanese company must be making a durable and exportable car at the end of the extension period. Total production of these cars was 165,630.

Conclusion

In the early 1950s, government and business objectives coincided to a greater degree than in later periods due to the severity of external threats, the uncompetitiveness of the industry, and the need for innovative policies after Japan's defeat in World War II.

The government-business relationship in the automobile industry was cooperative during this period. Business needed

government to take actions to protect it from imports and foreign capital. It could not protect itself in the area of passenger cars because of the immaturity of the industry; this same concern was not evident in the area of truck production. Without protective measures, Japan's passenger car industry would have been dependent on foreign manufacturers longer, and the development of domestic technology would have been slower. Foreign automobile companies, especially European firms, were very interested in Japan and posed a real threat.

The automobile industry convinced MITI that its development would help Japan achieve broader economic policy objectives such as saving foreign exchange and developing the machinery industry. MITI then strongly supported the industry over the objections of other segments of the Japanese government. MITI, in a trade-off for industry support from opponents, agreed to the sale of Occupation used cars to temporarily fill the demand that domestic carmakers as yet could not satisfy.

Support did not mean that the government took control of the industry or created a national company. It simply set perimeters limiting what companies could enter into technology tieups and what types of cars could be produced (small not large), provided minimum survival security through protection from imports and foreign capital, and enacted generic support measures from which the automobile industry benefited.⁶⁰

John Campbell has stated that the automobile industry was not "designated to play a key role in this long-term restructuring strategy [the evolution of the industrial structure from lower to higher value-added]."⁶¹ It is true that support, especially financial support, was not as pervasive as in basic infrastructure industries such as steel and electric power. But a consensus was reached to provide minimal survival security, and that support was indeed provided. It is impossible to ascertain how much the support measures (as opposed to the protective measures) helped the dynamic entrepreneurs working in the automobile industry obtain their goals. Certainly, the entrepreneurs would have tried to develop passenger cars even without government support, but they could not have developed them as rapidly.

The governmental policies of the early 1950s were developed in conjunction with the private sector—indeed often at their instigation—and were designed to promote the development of passenger car production. The greatest impact of this period, an impact that the government and the private sector helped create, is that the automobile industry "established itself firmly through special

procurement during the Korean Conflict, investment for equipment and facilities, and the introduction of foreign technology.”⁶² The success of this joint effort can be measured by the successful development of the industry, which in turn helped change the way government and business interacted.

Finally, it has to be remembered that the developments of the 1950s occurred in an international environment that was conducive to the type of policies and interactions that were used to launch the passenger car industry. Other countries, especially the United States, were willing to tolerate protectionist barriers because of Japan's chronic balance of payment problems and relative insignificance in world trade. Multilateral arrangements governing trade, such as the General Agreement on Tariffs and Trade (GATT) and the International Monetary Fund (IMF), recognized the legitimacy of protective actions to resolve balance of payments problems and aid in reconstruction after World War II. Article XIV of the IMF provided for the transitional period after the war. Section 2 of this article states:

In the post-war transitional period members may, notwithstanding the provisions of any other articles of this Agreement, maintain and adapt to changing circumstances (and, in the case of members whose territories have been occupied by the enemy, introduce where necessary) restrictions on payments and transfers for current international transactions.⁶³

The United States sought to strengthen Japan's weak and vulnerable economy. For Japan to be a counterweight to Communism in Asia and serve as a U.S. military base, the Americans looked favorably on Japan's rebuilding program. Therefore, the United States was tolerant of restrictive practices except of those on products such as umbrella frames, wood screws, and cotton textiles. Restrictions on these products created trade problems that were resolved through voluntary export restraints. As the Japanese economy strengthened, American and international tolerance diminished, forcing changes in Japan's public policies and straining the government-business partnership.

NOTES

¹Koichi Shimokawa, "Entrepreneurship and social environment change in the Japanese automobile industry: On the key elements of high productivity and innovation" (Paper presented at the International Conference on the Incidence of the External Environment on the Global Automobile Industry, Breau-sans, France, 27-29 April 1981), pp. 273-92.

²Naokazu Yamamoto, *Nihon no jidosha: Toyopeto seichosi* [Japanese automobiles: history of the growth of the Toyopet] (Tokyo: Tokyo Sogensha, 1959), p. 227.

³In addition, Tama Denki Jidosha K.K. was producing a small number of four-wheeled electric-powered passenger cars.

⁴Ministry of International Trade and Industry, Machinery Bureau, "Kokusan joyo jidosha no rikai no tame ni [In order to understand domestic passenger cars]" (Handwritten, Tokyo, April 1952), p. 13.

⁵Ibid.

⁶Ibid., p. 16.

⁷Ibid., p. 24.

⁸U.S. Department of Commerce, *Japan, The Government-Business Relationship*, ed. Eugene J. Kaplan (Washington: Government Printing Office, 1972), p. 109.

⁹"Yushutsu no mitoshi—Ichimada sosai shachu dan" [Export forecast—interview with President Ichimada while in moving car], *Nihon Keizai Shimbun*, 13 April 1950, p. 1.

¹⁰Interview with Mr. Akira Kawahara of Toyota Vista, formerly of MITI, Tokyo, September 1984.

¹¹C.S. Chang, *The Japanese Auto Industry and the U.S. Market* (New York: Praeger Publishers, 1981), p. 49.

¹²MITI, Machinery Bureau, "Kokusan joyo jidosha," p. 16.

¹³"Kokusan jidosha: obei yori sunen okureru" [Domestic cars: several years behind the United States and Europe], *Nihon Keizai Shimbun*, 15 December 1951.

¹⁴Shuichi Takamina, "Showa 27-29 nen no jidosha gyosei" [Automobile policy from 1952 to 1954], in *Nihon jidosha kogyoshi gyosei kiroku shu* [Collection of articles on the administrative history of the Japanese automobile industry], *Nihon Jidosha Shinko Kai* (Tokyo: Nihon Jidosha Shinko Kai, 1979), p. 179.

¹⁵Yamamoto, *Nihon no jidosha: Toyopeto seichosi*, p. 228.

¹⁶Taizo Yakushiji, "Dynamics of Policy Interventions: The Case of the Government and the Automobile Industry in Japan"

(Ph.D. diss., Massachusetts Institute of Technology, May 1977), pp. 201-4.

¹⁷Shigenobu Yamamoto, "Showa 25-26 nen no jidosha gyosei" [Automobile policy from 1950 to 1951], in *Nihon jidosha kogyoshi gyosei kiroku shu* [Collection of articles on the administrative history of the Japanese automobile industry], Nihon Jidosha Shinko Kai (Tokyo: Nihon Jidosha Shinko Kai, 1979) p. 175.

¹⁸Yakushiji, "Dynamics of Policy Interventions," p. 203.

¹⁹Yamamoto, "Showa 25-26 nen no jidosha gyosei," pp. 175-76.

²⁰*Ibid.*, p. 176.

²¹Ministry of International Trade and Industry, Library Division, "Chuko gaikoku jidosha no yunyu nisuite" [Concerning the import of foreign used cars] (Handwritten, Tokyo, 1949), p. 1.

²²Yakushiji, "Dynamics of Policy Interventions," p. 211.

²³MITI, Library Division, "Gaikoku jidosha," p. 30.

²⁴*Ibid.*

²⁵Yakushiji, "Dynamics of Policy Interventions," p. 218.

²⁶Diet records from 1952, various committee records.

²⁷Nissan Motor Corporation, *Nissan jidosha sanjunenshi* [Thirty-year history of Nissan Motor Corporation] (Tokyo: Nissan Motor Corporation, 1965), p. 222.

²⁸Yakushiji, "Dynamics of Policy Interventions," p. 222.

²⁹"Kankochō wa gaikokusha ga osuki" [Government agencies like foreign cars], *Mainichi Shimbun*, 4 March 1956, Tokyo Evening Edition.

³⁰"Gaikoku jidosha Nihon e shinshutsu" [Foreign cars advance into Japan], *Nihon Keizai Shimbun*, 27 April 1952.

³¹*Ibid.*

³²"Shihon no shinshutsu nerau gaisha kosei" [Foreign car offensive takes aim through advancing capital], *Nihon Keizai Shimbun*, 29 May 1952.

³³*Ibid.*

³⁴"Kokusai jidosha kogyo ni kiki" [Crisis in the domestic automobile industry], *Nihon Keizai Shimbun*, 7 June 1952.

³⁵U.S. Department of Commerce, *Japan, The Government-Business Relationship*, p. 112.

³⁶"Honkakuka shita gaikoku jidosha no shinshustu" [The advance of foreign cars is proceeding at full speed], *Nihon Keizai Shimbun*, 18 June 1952.

³⁷The motivation behind Japan's local content rules in the 1950s differs from the motivation for American local content proposals during the 1970s and 1980s. The Japanese sought to

ensure that domestic manufacturers would develop the requisite skills to produce automotive parts and assemble passenger cars without depending on foreign partners. Penalties were instituted to insure compliance within five years. The provisions both pushed the industry to a higher level of technical competence and saved foreign exchange. The American local content bills arose from a very different motivation. The local content provision that stated captive imports could not be counted when calculating a company's degree of compliance with the standards enacted as part of the Energy Policy and Conservation Act in 1975 represented an attempt by labor to ensure that the American manufacturers would not meet the fuel economy standards by importing small fuel-efficient cars. The purpose was to save American jobs. The local content bills of the 1980s sought to encourage foreign—primarily Japanese—automobile manufacturers to establish assembly plants in the United States and to prevent American companies from moving to offshore assembly sites. Again, the purpose was to save American jobs. Thus while the Japanese local content provisions were technology-pulling in an infant industry, the American local content bills sought to preserve labor's status quo in a mature industry.

³⁸“Gaikoku shihon shinshutsu mitomesu” [Observations on the advance of foreign capital], *Nihon Keizai Shimbun*, 26 October 1952.

³⁹*Ibid.*

⁴⁰Michael A. Cusumano, *The Japanese Automobile Industry* (Cambridge: Harvard University Press, 1985), p. 116.

⁴¹“Hino Diesel Renault to no teikei naiyo” [Content of the Hino-Renault tieup], *Nihon Keizai Shimbun*, 17 October 1952.

⁴²Shogo Amagai, *Nihon jidosha kogyo no shiteki tenkai* [Historical development of the Japanese automobile industry] (Tokyo: Akishobo, 1982), p. 127.

⁴³Nissan Motor Corporation, *Jidosha kogyo handobukku* [Automobile industry handbook] (Tokyo: Nissan Motor Corporation, 1984), pp. 98–99.

⁴⁴Yakushiji, “Dynamics of Policy Interventions,” p. 218.

⁴⁵Takashi Kawazoe, ed., *Nihon jidosha sogo nenpyo* [Comprehensive chronology of Japanese automobiles] (Tokyo: Nihon Jidosha Kaigisho, 1967), p. 32.

⁴⁶MITI, Machinery Bureau, “Kokusan joyo jidosha,” pp. 49–52.

⁴⁷Interview with Masami Tamaoki, Tokyo, March 1984.

⁴⁸Cusumano, *The Japanese Automobile Industry*, p. xix.

⁴⁹Tariffs also were used to protect the infant American automobile industry from European exports. Under the Dingley tariff of 1897, automobiles were classified as “manufactured steel” and subject to a 45 percent tariff rate. Early auto manufacturers in New England took advantage of the tariff to sell high-priced luxury cars. However, attempts to lower the tariff were first made by Midwest-based companies such as Ford Motor Company that produced vehicles for the mass-market (rather than luxury cars that competed with European products) and sold them overseas. In 1908, James Couzens, Secretary of the Ford Motor Company, protested efforts to raise the tariff further. In a petition to the U.S. House of Representatives, Committee on Ways and Means, he stated that “we are unalterably opposed to any increase in this tariff. We believe that this so-called infant industry is fully protected . . . and, in fact, we believe that the present tax is a greater protection than this industry should have.” (Mira Wilkins and Frank Ernest Hill, *American Business Abroad* [Detroit: Wayne State University Press, 1965], p. 37.)

⁵⁰In the United States, a differential was created in the tariff rate in 1911 with a 30 percent duty imposed on automobiles costing less than \$2,000 while the 45 percent duty remained for automobiles costing \$2,000 or over. In addition, in the case of imports from countries with higher duties, the U.S. duty would be equal to the foreign duty but not exceed 50 percent. This stipulation was repealed by the Trade Agreements Act of 1934. By the 1920s with the successful dissemination of assembly-line technology, the American automobile industry as a whole was internationally competitive. Therefore, the American industry in the 1930s, because of its growing international interests, opposed the Smoot-Hawley tariff law that threatened to instigate retaliatory action by foreign governments that would cut off overseas markets. Until the 1970s, the industry’s leaders continued to be strong advocates of free trade. In 1948, the tariff was lowered to 8.5 percent *ad valorem* and gradually reduced until in 1984 it stood at 2.7 percent for passenger cars, 3.4 percent for buses, and 8.5 percent for trucks.

⁵¹MITI, Machinery Bureau, “Kokusan joyo jidosha,” p. 27.

⁵²Takafusa Nakamura, *The Postwar Japanese Economy* (Tokyo: University of Tokyo Press, 1981), p. 45.

⁵³Japan Development Bank, *The 25 Year History of Japan Development Bank* (Tokyo: Toyo Keizai Shimbun Kai, 1976), p. 462.

⁵⁴Toshio Kimura, *Nihon jidosha kogyoron* [The Japanese automobile industry] (Tokyo: Nihon Hyoron Sha, 1959), pp. 165-66.

⁵⁵Hiroya Ueno and Hiromichi Muto, "The Automobile Industry of Japan," *Japanese Economic Studies* 3.1 (Fall 1974): 16-17.

⁵⁶Tadahiro Iwakoshi, *Jidosha kogyoron* [The automobile industry] (Tokyo: University of Tokyo Press, 1968), p. 93.

⁵⁷William C. Duncan, *U.S.-Japan Automobile Diplomacy* (Cambridge, MA: Ballinger Publishing Company, 1973), pp. 145-46 and Takamina, "Showa 27-29 nen no jidosha gyosei," p. 179.

⁵⁸"Showa 29-31 nen no jidosha gyosei [Automobile policy from 1954 to 1956]," in *Nihon jidosha kogyoshi gyosei kiroku shu* [Collection of articles on the administrative history of the Japanese automobile industry], Nihon Jidosha Shinko Kai (Tokyo: Nihon Jidosha Shinko Kai, 1979), p. 186.

⁵⁹*Ibid.*

⁶⁰MITI, Machinery Bureau. "Kokusan joyo jidosha," p. 12.

⁶¹John Campbell, "The Automobile Industry and Public Policy," Joint U.S.-Japan Automotive Study Working Papers Series 16 (Ann Arbor: Center for Japanese Studies, The University of Michigan, August 1983), p. 4.

⁶²C.S. Chang, *The Japanese Auto Industry*, p. 53.

⁶³J. Keith Horsefield, ed., *The International Monetary Fund 1945-1965: Twenty Years of International Monetary Cooperation*, vol. 3, *Documents* (Washington: The International Monetary Fund, 1969), p. 203.

CHAPTER 5

CONSOLIDATION AND EXPANSION

Introduction

By the mid-1950s, Japan's overwhelming concern with imports and foreign capital in the auto sector changed to attempts to expand domestic demand and build strong foundations for the passenger car industry. The long-term threat from imports and foreign capital still existed, but the enactment of protective policies changed the focus of interactions to the domestic market. The consensus that developed in the early 1950s to support the industry reinforced MITI's mandate to develop the industry and helped create a more stable economic environment.

The prominent policy issues, creating domestic demand and enhancing competitiveness, were issues that required adjustments at the national and company levels. The industry started to take a more independent stance vis-à-vis the government on some of these issues, issues that required their action rather than just that of the government. Because the industry was also growing in competitiveness, it was less dependent on financial and other government incentives. As a result, while agreement existed on what constituted the major problems facing the industry, there were no clear-cut solutions.

There were two major auto-specific policies in the late 1950s: the People's Car Project and attempts to develop the automotive parts industry. Conflict between the government and the industry characterized the People's Car Project, while cooperative relations prevailed in the auto parts program until the parts industry became competitive in the 1960s.

Creating Domestic Demand

The passenger car industry could not be competitive until domestic demand increased sufficiently to make mass production possible. Until this time, demand for passenger cars had come almost entirely from the business sector—primarily taxis—and the public sector. The potential demand from these groups was not sufficient to support mass production. In 1957, hired cars and taxis accounted for 53.9 percent of passenger car sales, with sales for personal use at 3.6 percent. By 1966, hired cars and taxis had fallen to 9.6 percent of sales, while sales for personal use increased to 30.3 percent.

Government and business realized that private demand had to increase to support mass production, but they could not agree on how to reach this goal. The government increasingly favored the development of a small passenger car that ordinary people could afford and that was suited to Japan's crowded conditions. The private sector favored decreasing the price on slightly larger small cars already planned. This difference of opinion resulted in the first major conflict after independence between MITI and the auto industry. MITI unwittingly created this conflict, which centered on a government project that sought to promote the development of a small four-wheeled vehicle suitable for everyday use by ordinary people—the *Kokuminsha* or "People's Car."

The People's Car Project

Mr. Akira Kawahara, a member of MITI's Automobile Bureau, developed the People's Car Project in conjunction with three Tokyo University engineering professors, including Dr. Hirao and Dr. Watari. Mr. Kawahara's aspiration was to allow the Japanese people, like people in other advanced nations, to enjoy owning passenger cars¹:

In an editorial in the *Economist* it said that British automobile manufacturers should produce a people's car. I thought we should not miss out on this new trend in car production. Fortunately, the Japanese automobile industry was still on the starting line, the number of cars was very limited. We could see and follow the trends of car production in the industrialized countries. In other

words, we could take lessons from the industrialized countries, and then we could study and consider the production of automobiles in a new way. That was my motivation for the study.²

MITI had been very interested in the development of the Volkswagen in West Germany and published an analysis of it in 1956.³ MITI felt that producing a small, cheap popular car as a consumer item suitable for Japanese conditions was the best approach to expanding the market for passenger cars (as opposed to production for business use only). This type of car would help create a mass market and provide automobiles for those who wanted their own "personal" car.

Toshimasa Tsuruta states that MITI's motivation was to concentrate the production of an exportable passenger car in one company.⁴ While exports might have been seen as a side benefit, the main reason for the project was to expand domestic demand. MITI was not seeking to create an automobile industry centered on a single company. Instead, the tentative plan revolved around only one company because MITI did not have either the personnel or the funding to support more than one company. This did not mean that other companies were not welcome to produce cars on their own.

Disagreement surfaced abruptly on May 18, 1955 when *Nihon Keizai Shimbun* published a very detailed article on the development of MITI's plan for a people's car.⁵ This article was published while the plan was still tentative and before the government was able to informally approach industry to garner support. The plan quickly became controversial because it stated that MITI would chose only one company to mass produce the proposed car. The companies also felt that the proposed price was too low. The proposal's main provisions were⁶:

Requirements for a People's Car

1. Maximum Speed - 100 km/hr.
2. Seating Capacity - 4 persons or 2 persons plus 100 kg of cargo.
3. Fuel Consumption - between 60 km/liter and 30 km/liter.
4. Durability - 100,000 km.
5. Exhaust Volume - 350 to 500 cc.
6. Vehicle Weight - 400 kg.

7. Production Price — less than 150,000 yen [\$416] on a production scale of 2,000/month.

Proposed Production Schedule

1. July 1, 1956. First Performance Test of Test Models.
2. July 1, 1957. Second Performance Test and Decision on a Single People's Car.
3. September 1957. Decision on a Single Manufacturer.
4. October 1958. Production Start.

According to the preliminary plan, MITI would provide financial support to the companies making test models so that they could make improvements through additional research. If a company were unable for some reason to produce the resulting car, the MITI minister would have the right to transfer the manufacturing rights to another company. After the second performance test from which a single model and company would be chosen, MITI would provide additional funding and act as a go-between to secure loans from city banks. In addition, MITI would ask other relevant government agencies to make any necessary changes in the traffic and tax laws to promote the small People's Car.

During the summer, MITI and the automakers formally began discussing the plan. On July 7, the head of MITI's automobile section explained the People's Car Project to staff members of the Automobile Manufacturers Association, and on July 17 he conducted a similar discussion with the association's executive committee.⁷

While these discussions were taking place, the association began a feasibility study of the plan. On July 12, it sponsored a meeting of top engineers from nine companies. These engineers undertook the feasibility study and released their report on August 23.⁸ The report concluded that it was impossible to produce the specified car at the specified price.

The industry's formal response was determined at a directors meeting of the Automobile Manufacturers Association on September 1. The directors, basing their comments on the engineers' study, stated⁹:

1. The specified levels of cost and efficiency make the manufacture of the cars proposed by MITI impossible.

2. Even if the efficiency requirements could be met, the cost of the car would be 50 percent higher than specified.
3. The People's Car idea is worthy of further industry research.

The controversy dissipated briefly but resumed in early December when the president of Komatsu Seisakusho, Mr. Kawai, announced that his company would make a test model.¹⁰ Mr. Kawai wanted to enter the passenger car field earlier but failed to receive government approval for a technical tieup with Volkswagen because Komatsu was not a chassis manufacturer. He now proposed to manufacture the car with assistance from Mr. Porsche, the German developer of the Volkswagen and other cars. Mr. Porsche stated that MITI's proposed plan was not impossible to achieve. This new development perturbed the major automobile manufacturers since other motorcycle and three-wheeled vehicle producers also expressed interest in the People's Car Project in September.

The five major manufacturers—Nissan, Toyota, Isuzu, Hino, and Prince—agreed on December 25 to cooperate and fight the plan.¹¹ They also agreed among themselves that none would betray the others by producing a test model. They reasoned that domestic demand did not yet warrant a new type of car and that potential export demand existed only in Southeast Asia. They also were concerned that the new car might simply take sales away from their current models.

These views were presented to MITI Minister Tanazan Ishibashi.¹² The manufacturers told him that they would work hard to bring the cost down and raise the quality of their existing passenger cars in order to meet private consumer demand, but that the selection of a single manufacturer would violate the principles of free competition. Minister Ishibashi replied: "We never thought of assisting any private companies financially in regard to the People's Car."¹³ This statement dealt a strong blow to the project.

The plan was not implemented for two reasons. First, the major automobile companies opposed the project. They were not willing to cooperate in producing the car or to let one company gain a competitive advantage in the production of small cars. (However, some companies, including Toyota Motor Sales, announced in 1956 that they would try to produce test models.¹⁴) Second, the government, in the new postwar environment, did not have the power to enact its programs unless it had support from the major

producers in the industry. In this case, support was not forthcoming.

Even though the project was not carried out, the program had some positive effects. Hiroya Ueno and Hiromichi Muto state:

Though this program ended up as a desk plan, its objectives have been well incorporated into MITI's subsequent policies, such as preferential taxes for mini 4-wheel cars, selective financing, and encouragement of production concentration by reorganizing automobile manufacturers into two groups.¹⁵

C.S. Chang also sees some positive effects:

The car was not produced because it was almost impossible to develop. However, this outline stimulated motor vehicle manufacturers to develop small passenger cars henceforth.¹⁶

The plan especially stimulated the entry of two- and three-wheeled vehicle producers into the four-wheeled passenger car market (and out of production of three-wheeled vehicles), helping to create what MITI termed "excessive competition" problems in the 1960s, which it believed would keep the industry too weak to compete with foreign producers.¹⁷ Instead, it sharpened competition and spurred development. The publicity given the People's Car also helped change the attitude of ordinary people toward passenger cars.¹⁸ No longer were passenger cars perceived just as taxis.

Toshimasa Tsuruta cites the People's Car Project as evidence that the Japanese government's relationship with the automobile industry is adversarial and that MITI's industrial policy has been a failure.¹⁹ He is correct in viewing the People's Car controversy as a conflict. The major producers were not interested in following MITI's technical specifications because they appeared unprofitable and might have given one company an unfair advantage over the others. Because it was impossible to predict which company would receive that advantage, the major companies were motivated to work together to defeat the plan. After additional companies entered the market around 1960, this type of consensus was harder to achieve. Because the small companies saw the project as an opportunity to break into the market with a product suited to their production capabilities, they did not have the same reaction as the five existing manufacturers.

Taizo Yakushiji states that this program “revived prewar teaching of government control of the automobile industry in the use of technical specifications.”²⁰ Certainly the standardized “Isuzu” and the People’s Car were based on government technical specifications, but there the similarity ends. MITI’s plan was fundamentally different from earlier military policies because it did not seek to impose controls on the industry. Rather, the People’s Car Project represented MITI’s attempt to use its leadership to influence production trends. In the late 1930s, the government succeeded in unilaterally imposing its need for trucks on the manufacturers, but in the postwar period it could only attempt to influence. The final decisions remained in the hands of the private companies.

Other Public Policies

Other public policies affected the level of consumer demand for passenger cars in postwar Japan. These included policies related to road construction and taxation.

The policy governing road construction increased demand indirectly. Japan’s roads at this time were inadequate. Dr. Ralph J. Watkins, an American brought to Japan by the government in 1956, said, “The roads of Japan are incredibly bad. No other industrial nation has so completely neglected its highway system.”²¹

This issue did not involve much interaction between government and the automobile industry. The government and business favored the creation and upgrading of roads. MITI, the strongest advocate for the auto industry, was not in charge of road construction; it was under the jurisdiction of the Ministry of Construction, which catered more to its clients—construction companies—and local politicians than the automobile industry. The auto companies had to compete with everyone else to obtain improved roads around their factories to facilitate supplier deliveries.

The first postwar recognition of the importance of a road network occurred in 1948 when SCAP outlined a five-year plan.²² This plan was to be carried out by the Ministry of Construction’s Road Bureau but was never implemented because of the Dodge Line. Road construction that was done during the Occupation progressed slowly because of conflicts over where the roads should be built and the lack of materials.

Interest in roads revived in 1952 when the Japanese government made a survey of existing road conditions and established a classification system for public roads.²³ The government in 1953 passed the Temporary Measures Law Concerning the Source of Funds for the Improvement of Roads (Doro Seibihi no Zaigento ni Kan Suru Rinji Sochi Ho) in response to the survey. This law established a five-year construction program that began in 1954 and was financed by a gasoline tax.²⁴

Other laws were enacted in the 1950s that further expanded the road network: the Law Concerning Special Measures for Road Improvement (1955), the Japan Highway Public Corporation Law (1955), the National Expressway Law (1957), the Law Concerning Emergency Measures for Highway Construction (1958), and the Metropolitan Expressway Public Corporation Law (1959). Five additional types of special road taxes were also established to aid road construction: the Local Road Transfer Tax (1955), the Light Oil Transactions Tax (1956), the Liquefied Petroleum Gas Tax (1965), the Automobile Acquisition Tax (1968), and the Automobile Weight Tax (1971).

The impact of the road construction program was favorable. Takafusa Nakamura states that the upgrading of roads since the latter half of the 1950s had a tremendous influence, increasing the potential for automobile transportation.²⁵ Masaki Koshi similarly states that "the rapid diffusion of cars starting from the second half of the 1950s is attributable to the government's policies of achieving high economic growth and improving the nation's road network."²⁶

Although MITI's policies helped expand demand for passenger cars, other government policies were inconsistent with this goal. John Campbell and Masaki Koshi state that the huge increases in consumer demand for passenger cars in the 1960s sometimes occurred in spite of, not because of, government policy.²⁷ Masaki Koshi states:

It would not be an exaggeration to say that various related government agencies have been implementing their respective policies in accordance with their own interests and circumstances. The impact of such policies has frequently inhibited, rather than encouraged, car ownership and use.²⁸

The policies that were unfavorable to passenger car demand included difficult driver's license tests, restrictions on consumer financing, parking and garage regulations, inspections, high tax burdens, emission controls, and strict traffic safety regulations.

Those restrictive measures did not mean that the internal opposition to passenger cars that existed earlier was still prevalent. Rather, they exemplified a different type of government-business interaction: regulation to minimize social costs. With the exception of tax policies, the other policies were primarily enacted during the 1960s after consumer demand had increased to a level that created environmental and safety problems. Regulations tended to be more controversial than developmental policies.

In regard to tax policies, the majority of automobile taxes were used either to finance safety inspections (a social cost issue) or road construction. The exception was the high commodity tax, which was essentially a revenue tax on luxury goods, that had been applied to passenger cars since before World War II. Although the tax remained high, it was lowered considerably during the early 1950s and included a differential that favored the small cars produced by the Japanese companies. The fact that it was not eliminated does reveal the bias that existed in Japan against consumer consumption. To this extent, the automobile industry was not seen as central to economic development in Japan as were industries such as steel or fertilizer. The auto industry was provided only with minimum survival security that left most of the initiative up to the private sector.

The inconsistencies in government policy did exist, especially after 1960. John Campbell states that the restrictive policies had "the net effect of holding down demand, certainly well below the level that would [have been] be reached if American-style [less restrictive] policies had been implemented."²⁹

While it is difficult to determine the full dampening effect of these policies, increased consumer demand due to road expansion, general economic growth, and rising incomes outweighed the restrictive policies' negative effects. Even if demand had been higher, the auto industry might not have been able to meet it since its manufacturing capacity did not take off exponentially until the 1960s. Registrations of new passenger cars then increased over fifteenfold from 145,777 in 1960 to 2,379,128 in 1970.

Automotive Parts Industry Promotion

A major reason why Japanese automobiles were not competitive was the high price and low quality of domestically produced parts.³⁰ In an attempt to remedy this problem, the government's major program to upgrade the automobile industry's competitiveness in the latter half of the 1950s involved the automotive parts industry. The major automobile companies had achieved a degree of stability, so attention shifted to the automotive parts industry, and automotive parts became the major focus of government and private sector interactions during this period.³¹

The Industry's Early Development

The parts industry began to expand in the late 1920s, primarily to make aftermarket repair parts. A few firms, including Toshiba and Teikoku Spring, supplied parts to the domestic manufacturers and to the onshore assembly plants of Ford and General Motors. These companies trace their present subcontracting relationships with the major assemblers to this period. The market grew further after the passage of the Automobile Manufacturing Law in 1936, which required the domestication of parts production. By the eve of World War II, Japan possessed a rudimentary independent parts industry, but much of the parts production was still done inside the car companies.

A Ministry of Commerce and Industry survey in 1935 found that 202 factories had automotive parts as their major products (excluding businesses such as general machine tool producers and shipyards, which produced automotive parts but not as a primary line). The survey found that production totaled 53 million yen (\$1.9 million), of which 26.7 million yen (\$933,566) was tire production.³²

The government first became involved with the automotive parts industry in conjunction with the "Isuzu" project. Studies on standardizing automotive parts were carried out in 1931 and 1933 by the Research Committee on the Standardization of the Size of Industrial Goods.³³ No substantive action was taken until the passage of the Regulation for the Registration of Qualified Auto Parts and Materials (Yuryo Jidosha Buhin Oyobi Zairyo Nintei Kisoku) in 1938 and the formation of the Committee on Automobile Technology in 1939. The law's purpose was to establish an authorization system for quality parts for use in the production of

standardized military trucks. If parts were authorized for use, the companies could obtain scarce raw materials and their parts would be bought by the authorized auto manufacturers. The authorizing authority was MCI's Machinery Experimental Bureau.

Auto parts companies could also be authorized under the Automobile Manufacturing Law. Only one auto parts company, Motor Wheel Industry (a predecessor of Topy Industries), was authorized under the law. It was created by a forced merger of three stamping companies³⁴ and obtained a monopoly on the production of wheels during World War II.

The Automobile Control Association regulated the distribution of automotive parts during the war. After November 1942, the Regional Automobile Maintenance and Distribution Corporation (JIHAI), the operational arm of the control association, was responsible for day-to-day supervision.

Prior to 1945, little information is available on how the parts companies interacted with the government. As in the case of the assemblers, they had no choice but to cooperate with the military, and specific companies did benefit from procurement contracts and participation in munitions production.³⁵

Technology Tieups

At the end of World War II, the automotive parts industry was backward and uncompetitive. Immediately after the war, existing suppliers underwent extreme economic hardships forcing them to restructure and cut employment. Some suppliers survived by receiving a limited amount of aid from the major assemblers along with income from the Korean War special procurement programs.

The automotive parts industry did not become a focus of government attention again until around 1953, when the major assemblers began KD production under technology tieups with foreign firms. Because MCI, and later MITI, continued on a limited scale after 1945 to certify parts' quality and engage in technical research, the administrative apparatus needed in 1953 was already in place.

One reason attention focused on the parts industry at this time was because the contracts signed by the assemblers in the tieup agreements required the domestication of parts production. MITI refused to approve tieup contracts without this provision. Domestic production of parts, including engines, was required to be 90 percent within five years. For example, Hino's initial production plan for

KD production of the Renault 3CV stated that in 1953 sixteen parts, including tires, would be domesticated. The domestication percentage would then rise to 25 percent in the second year, 50 percent in the third year, 75 percent in the fourth year and 100 percent in the fifth year.³⁶ Thus, MITI's policy ensured that foreign passenger car technology would be quickly internalized.

In order to qualify under the contract's domestic content provisions, a part had to be approved by the foreign partner as meeting specified quality levels.³⁷ Once approved, MITI would also authorize the part, and it could qualify as domestic content.

The automobile companies at this time did not have the funds to subsidize parts production. In 1952, MITI, foreseeing this problem, diverted some funds originally intended for the assemblers to the parts industry as loans to finance the required parts.³⁸ In addition, MITI recommended that JDB extend loans to viable major parts suppliers of the four major assemblers. Most smaller parts suppliers did not have the staff to fill out the extensive government loan applications, so the benefits of these programs went primarily to the larger companies.

Despite the loan program and some subsidization from the assemblers, the primary burden of fulfilling the domestication schedule fell on the parts suppliers themselves. The companies had to scrounge for the capital to upgrade their products (or in some cases produce entirely new lines of products) to meet the high standards of the foreign partners. This was especially true for Hino and Isuzu suppliers, who only had experience with truck parts.

Some of the larger parts producers also entered into technology agreements with foreign firms in order to upgrade quality. These agreements were subject to review by the government, which decided whether or not to allocate the foreign exchange needed. The first such postwar agreement was signed in 1951. (A few of the largest parts producers, including Diesel Kiki and Nihon Air Brake, had technology agreements with foreign companies in the 1930s.) There were eight agreements from 1951 to 1956.³⁹ Ueno and Muto describe the evolution of the agreements:

For instance, technology imports ranged from basic technology to design, increasing from eight in 1951-1956 that centered around product technology (brake boosters and electrical devices), to twelve in 1956-1960 that centered around mass production technology (continuous casting, etc.), fifty-one in 1961-1965 that centered on newly developed technology (air spring, automatic clutch, etc.),

and eighty-three in 1966-1968 that were mainly accessories (sun visor, tire pressure indicator, etc.) and technology-bypassing registered patents (wiper blades, fan clutches, etc.).⁴⁰

The advances brought about by these tieups benefited more than just the individual companies involved. The assemblers helped encourage the spread of technology, especially new industrial engineering and quality control techniques, through the cooperative associations of parts producers and specific assemblers that began to form in the mid-to-late 1950s for prewar vehicle manufacturers and in the 1960s for later entrants. Because the parts companies often supplied more than one major auto assembler and assemblers bought the same part from more than one supplier, the new technologies spread throughout the industry.

Operation Roll-Up

The technological development of the Japanese auto parts industry in the 1950s also was enhanced by the U.S. military's rebuild program, known as Operation Roll-Up. The program helped increase parts quality, upgrade manufacturing techniques, and provide a stable market. It also trained workers in automotive skills.

In 1948, the U.S. military started a program to rebuild trucks and jeeps left behind in Asia after World War II.⁴¹ These vehicles were then reshipped all over Asia to support U.S. military and United Nations forces. Compared to the cost of new vehicles, the U.S. government saved an estimated \$4,000 on every rebuilt 2.5 ton truck and \$2,000 on every rebuilt jeep.

The U.S. Army Ordnance Depot at Oppama and the U.S. Army Logistical Depot at Tokorozawa procured parts to repair these vehicles and contracted for the complete repair of vehicles.⁴² Fuji Motors Corporation was the primary contractor for the complete repair of vehicles. The major Japanese contractors for parts included Nihon Seiko at its Oppama Plant near Yokohama and Victor Autos Company at its Tokorozawa Plant in Saitama.⁴³

The program required numerous parts that were procured from small- and medium-sized Japanese parts companies. These parts included products such as brake shoes and linings, piston rings, electrical parts, shield beam headlamps, starters, crankshafts, springs, hoses, and tires.

Because the quality of the parts was poor, Japanese and American engineers were assigned to work with the Japanese suppliers.⁴⁴ Special teams were frequently sent to the suppliers' factories to teach them how to read SAE (Society of Automotive Engineers) standards and military specifications and how to use statistical process control. The U.S. military also specified as a condition in the contracts the establishment of quality controls and inspection systems.

By August 1958 when the program began to be phased out, 176,653 vehicles had been completely rebuilt and 7,000 more had been repaired.⁴⁵ In addition, almost 102,000 engines, axles, and transmissions had been rebuilt. The rebuild program turned out 699 vehicles in 1948 and peaked at 37,722 in 1955. The number of rebuilt vehicles and required parts is significant when compared to 828,249 domestically produced vehicles (passenger cars, trucks, and buses) between 1948 and 1958 because it expanded demand for parts and provided a stable source of income at a critical time in the industry's development.

Machinery Promotion Act

The most extensive Japanese government program to increase the competitiveness of the auto parts industry began in 1956. The government felt that the assemblers' and parts companies' own efforts were proceeding too slowly. Therefore, it designated automotive parts in 1956 for promotion under the Machinery Industry Promotion Act (Kikai Kogyo Shinko Rinji Sochi Ho).

The commerce and industry committees of both houses of the Diet held hearings on this act in the spring of 1956. The hearings dealt primarily with the overall level of specialization, rationalization, and the lack of maturity within the machinery industry, with the auto parts industry as one example.⁴⁶ This act was passed on June 5, 1956 and extended twice, each time for five years, first in 1961 and then in 1966.

The Machinery Industry Promotion Act helped industry to overcome the technological gap it faced in relation to foreign producers. Koichi Shimokawa states that the law allowed "eminent specialized parts manufacturers" to grow up.⁴⁷ In particular, he points out that the law allowed companies to acquire technology patents, to receive priority in foreign exchange allocation to buy new equipment, and to obtain special fiscal privileges. In addition,

there were special rules for the depreciation of new equipment and the promotion of rationalization technology.

The machinery promotion act complemented the vehicle assemblers' corporate price reduction plans. Nissan established the Original Price Reduction Committee, while Isuzu had a similar Rationalization Committee.⁴⁸ Toyota conducted a comparative study of the prices of 300 parts in Japan and the United States and found that Japanese products were on average 45 percent more expensive.⁴⁹ The other major companies had similar committees and conducted similar surveys in the late 1950s.

The assemblers were concerned not only with obtaining low-cost products but with establishing integrated production systems. The companies needed to rationalize parts production to secure efficient mass production for successful competition—the overriding concern during this period. The “just-in-time” or *kanban* system of inventory management (in which parts arrive at the assembly line from suppliers as needed rather than being stock-piled) began during the 1950s in part as a way to better integrate parts production with final assembly.⁵⁰

Intensified domestic competition was created by a large number of new entrants into the parts industry between 1955 and 1956. This competition provided motivation for parts companies to take part in the price reduction and rationalization plans of the vehicle assemblers and the government.

The act was administered by the Automotive Parts Committee, an *ad hoc* group with members from MITI, the major automotive parts associations, and the Automobile Manufacturers Association.⁵¹ MITI and the committee agreed on the policy approach pursued during the first ten years of the plan because all sides had similar objectives.

The privileges extended under the act were the same benefits earlier extended to the major automobile assemblers: technology imports, tax benefits, and loans. The industry benefited from technology tieups and technology imports, but the impact of the loans was more controversial.

Loans were extended through the Japan Development Bank, and the Small and Medium Companies Finance Corporation. The JDB loans went to primary parts makers (companies with direct relationships with the assemblers), and the Small and Medium Companies Finance Corporation loans went to secondary parts makers (companies with indirect relationships with the assemblers and direct relationships with primary parts makers). While the JDB and the Small and Medium Companies Finance Corporation were

responsible for granting the loans, the Automotive Parts Committee approved their decisions.

The initial criteria for the loans stated that they had to involve products that represented substantial costs to the final assemblers.⁵² MITI listed ninety-five categories of parts, from which forty-five categories would be promoted for modernization and rationalization.⁵³ Nine products were designated to begin the program: wheels, carburetors, shock absorbers, horns, gauges, metal cable, switches, chassis coil, and evaporators. Loan conditions announced in 1964 were broader and reflected the growing concern with the liberalization of the Japanese market.⁵⁴ The new criteria required that loans had to help prepare the passenger car industry for liberalization, had to contribute to future exports, and had to be given to companies with a substantial share of the domestic market.

The total amount of loans extended to the auto parts industry by JDB under the Machinery Promotion Act was 30.642 million yen divided among 139 companies (1956 to 1970).⁵⁵ The Small and Medium Companies Finance Corporation's loans under the act totaled 4.147 million yen and were received by 161 companies (1961 to 1970). The auto parts industry also received loans after 1970 under the Machinery Electronics Act (1971 to 1977) and the Machinery Information Act (1978 to 1980), totaling 33.7 million yen from JDB and 959 million yen from the Small and Medium Companies Finance Corporation.

Koichi Shimokawa sees the loans as important and bases his conclusions on the total loan figures and price reductions to show increases in efficiency rather than defining success simply as the industry's growth.⁵⁶ John Campbell states that impact of the government loans was ambiguous given that both firms receiving and not receiving JDB loans grew at impressive rates.⁵⁷ In addition, he notes that if JDB used "normal banking criteria" to decide who should receive the loans, the stronger companies would have benefited in any case. He concludes that "the impact of public policy should be seen as helpful rather than determining."⁵⁸

The evidence suggests that Campbell is more correct in his evaluations. The loans could not by themselves determine which companies would be successful but helped to reinforce and somewhat hasten trends that were already being pursued privately. Because Japan was subject to time constraints imposed by pending merchandise and capital liberalization, acceleration of growth was essential to long-term competitiveness.

Parts Company Mergers

In the mid-1960s, MITI's attention turned to promoting mergers within the parts industry. This program sought to encourage the consolidation of the parts companies in order to strengthen the industry so that it could withstand the impact of capital liberalization. The attempt lasted from 1966 to 1971. MITI wanted to encourage mergers on a horizontal level to support its plan to reorganize the automobile assemblers into three groups. It tried to create a small number of horizontally integrated companies—similar to the American structure—strong enough to withstand the impact of capital liberalization.

MITI's attempts to encourage mergers were strongly opposed, primarily because they disturbed the industry's emerging subcontracting practices, in which major parts companies were quasi-integrated with a major assembler and smaller parts companies were similarly integrated with the major parts companies. In addition, the mergers would have disrupted efforts to encourage new entries needed in certain product lines and would have discouraged the rivalry within supplier groups that permitted prices to be held in check.⁵⁹

Few mergers resulted from MITI's efforts.⁶⁰ Some companies did enter into joint manufacturing agreements, which resulted in the grouping of third and second tier suppliers around a primary supplier that handled formal agreements with the assembler. These subcontracting relationships emerged because Japan did not have a strong existing parts or machinery industry, from which a passenger car industry could develop. The major assemblers, who were still weak themselves, had to develop a production system that shared capital and labor costs and transferred the brunt of labor problems to the suppliers. The resulting production system depended on a vertical division of labor that was reinforced by cultural proclivities toward groupism and the vertical structuring of social relationships.⁶¹

The industry also was not motivated to accept MITI's merger policies during the 1960s because the very success of the first ten years had created vigorous, more independent parts producers. The growing competitiveness of the industry first became apparent in 1964 when the parts producers rebelled against increased pressure to further reduce prices while facing rising raw material costs.⁶² In the fall, the parts suppliers announced that they had reduced prices to the lowest limit possible without going into debt. The confrontation was accentuated by a recession that lasted through 1965.

On November 25, 1964, the relationship between the assemblers and the parts makers was discussed at a conference chaired by Katsuji Kawamata of Nissan and attended by representatives of the major assembler and parts companies and MITI and the trade associations, as well as by representatives from other related industries.⁶³ Prior to the conference, the top executives of the parts industry compiled a twelve-point demand, the most important point being that if raw material prices rose, the prices paid for parts must also rise. Evidently, the assemblers took the position that they were "buying the parts not the materials," thus putting the burden of price increases on the parts makers. The parts makers, by taking a unified stand, were able to "obtain the full understanding of the assemblers." Their demands were formally accepted on December 17.

Conclusion

The mid-to-late 1950s was a period of consolidation and expansion for the Japanese auto industry. Because the immediate threat from the international arena had been eliminated, the companies gained competitive strength and were ready to build mass production facilities. Toyota completed construction of its Motomachi plant in 1959. Toyota's lead was followed by the other companies in the early 1960s. The new mass production plants included: Nissan's Oppama plant, Isuzu's Fujisawa plant, Hino's Hamura plant, and Prince's Murayama plant.

Domestic demand expanded primarily because of rising incomes and Japan's rapid growth. Policy initiatives to develop domestic demand also had an impact in reinforcing a trend that already had begun with Korean War special procurements. The Peoples' Car Project, although it was never implemented, encouraged the entrance of new producers and quickened the existing companies' small car projects.

The most important government-business interaction during this period involved the automotive parts industry, the weakest link in the drive toward competitiveness. Interactions and policies in this area mirrored those with the vehicle manufacturers. The industry's uncompetitiveness and the existence of shared objectives initially facilitated cooperation. The industry worked with the government and received government subsidies. Later, cooperation dissipated as the industry became more competitive, and MITI tried to change the industry's structure through mergers.

By the early 1960s, increased demand resulted in a promising passenger car market that attracted new entrants like Honda and Mazda, who previously produced motorcycles or three-wheeled vehicles. The new entrants sharpened competition and helped set the stage for the next round of government-business interactions. Concern over internationalization intruded and again became the central theme of relations between the government and the assemblers.

NOTES

¹Interview with Mr. Kawahara, Tokyo, September 1984.

²"Showa 29-31 nen no jidosha gyosei" [Automobile policy in 1954-1956], in *Nihon jidosha kogyoshi gyosei kiroku shu* [Collection of articles on the administrative history of the Japanese automobile industry], Nihon Jidosha Shinko Kai (Tokyo: Nihon Jidosha Shinko Kai, 1979), p. 188.

³Naomitsu Shirai, "Jidosha bu no ayumi" [Steps of the Automobile Section], in *Nihon jidosha kogyoshi gyosei kiroku shu* [Collection of articles on the administrative history of the Japanese automobile industry], Nihon Jidosha Shinko Kai (Tokyo: Nihon Jidosha Shinko Kai, 1979), p. 120.

⁴Toshimasa Tsuruta, *Sengo Nihon no sangyo seisaku* [Japan's postwar industrial policy] (Tokyo: Nihon Keizai Shimbun Sha, 1982), pp. 168-74.

⁵"Kokuminsha ikusei yokoan matomaru" [Decision on plan to promote a People's Car], *Nihon Keizai Shimbun*, 18 May 1955, p. 3.

⁶*Ibid.*

⁷Takashi Kawazoe, ed., *Nihon jidosha sogo nenpyo* [Comprehensive chronology of Japanese automobiles] (Tokyo: Nihon Jidosha Kaigisho, 1967), p. 57.

⁸Taizo Yakushiji, "Dynamics of Policy Interventions: The Case of the Government and the Automobile Industry in Japan" (Ph.D. diss., Massachusetts Institute of Technology, May 1977), p. 267.

⁹"Kokuminsha seisan wa fukano" [The production of the People's Car is impossible], *Nihon Keizai Shimbun*, 9 September 1955.

¹⁰"Seinen shita kokuminsha mondai" [People's Car issue raised again], *Nihon Keizai Shimbun*, 15 December 1955.

¹¹"Kyokai gai no ugoki ni hanpatsu" [Repelling movement from outside the industry], *Asahi Shimbun*, 25 December 1955.

¹²Yakushiji, "Dynamics of Policy Interventions," p. 269.

¹³Akira Hirotani, *Toyota no shinjitsu* [The truth about Toyota] (Tokyo: Diamond Sha, 1983), p. 101. Hirotani states that Shotaro Kamiya of Toyota Motor Sales discussed the possibility of jointly producing a test model with Mr. Kawai of Komatsu. Evidently, Toyota Motor Corporation was not informed of these decisions. When the negotiations were discovered, Toyota Motor Corporation blocked them and then hastened development of their own small car (ultimately produced as the Publica) under Seisi Kato.

¹⁴"Fuji Seimitsu no taishusha" [Fuji Seimitsu's popular car], *Nihon Keizai Shimbun*, 23 October 1956. Three companies announced plans for a People's Car: Toyota Motor Manufacturing, Ota, and Fuji Seimitsu. Evidently, Toyota Motor Manufacturing had not been informed about the plan of Toyota Motor Sales, and the project was terminated.

¹⁵Hiroya Ueno and Hiromichi Muto, "The Automobile Industry of Japan," *Japanese Economic Studies* 3.1 (Fall 1974): 19.

¹⁶C.S. Chang, *The Japanese Auto Industry and the U.S. Market* (New York: Praeger Publishers, 1981), p. 48.

¹⁷Michael A. Cusumano, *The Japanese Automobile Industry* (Cambridge: Harvard University Press, 1985), p. 21. Cusumano states that the main impact of the People's Car Project was the acceleration of the end of three-wheeled vehicle production.

¹⁸Hiromi Arisawa, ed., *Nihon sangyo hyaku nenshi* [History of 100 years of Japanese industry] (Tokyo: Nihon Keizai Shimbun Sha, 1981), p. 183.

¹⁹Tsuruta, *Sengo Nihon no sangyo seisaku*, pp. 168-74.

²⁰Yakushiji, "Dynamics of Policy Interventions," p. 265.

²¹Masaki Koshi et al., "Japanese National Policy toward the Automobile," *Transport Reviews* 3.1 (1983): 2.

²²John A. Black and Peter J. Rimmer, "Japanese Highway Planning: A Western Interpretation," *Transportation* 2.1 (March 1982): 30-31.

²³Black and Rimmer, "Japanese Highway Planning," p. 31.

²⁴*Ibid.*

²⁵Takafusa Nakamura, *The Postwar Japanese Economy*, trans. Jacqueline Kaminski (Tokyo: University of Tokyo Press, 1981), pp. 134-36.

²⁶Koshi et al. "Japanese National Policy," p. 3.

²⁷John Campbell, "The Automobile Industry and Public Policy," Joint U.S.-Japan Automotive Study Working Paper Series 16 (Ann Arbor: Center for Japanese Studies, The University of Michigan, August 1983), pp. 6-7 and Koshi et al., "Japanese National Policy," pp. 2-3.

²⁸Koshi et al., "Japanese National Policy," pp. 2-3.

²⁹Campbell, "The Automobile Industry," p. 7.

³⁰For the best and most complete review of the history of the Japanese auto parts industry and the development of subcontracting practices see Michael Smitka, "Competitive Ties: Subcontracting in Japanese Industry" (Draft Ph.D. diss., Yale University, 1989).

³¹It has to be remembered that, beginning in the 1950s and throughout the 1960s, the automobile companies placed strong pressure on their parts companies to rationalize production, cut prices, and become part of subcontracting networks. This pressure helped to condition the environment in which the policy actions described in this chapter occurred and in which global competitiveness was achieved.

³²Masami Tamaoki, "The Protective System of Domestic Car Production in the War Time," in *Keizaigaku-Kiyo*, no. 9 (1974): 27.

³³Chang, *The Japanese Auto Industry*, pp. 79-80.

³⁴Fumihiko Adachi, Keinosuke Ono, and Konosuke Odaka, *Ancillary Firm Development in the Japanese Automobile Industry—Selected Case Studies*, vol. 3 (Tokyo: Hitotsubashi University, 1981), p. 56.

³⁵Adachi, Ono, and Odaka, *Ancillary Firm Development*, pp. 137-40. One example, NGK Company, a manufacturer of spark plugs, benefited from two government policies during the 1930s and 1940s. The Japanese army and navy bought spark plugs and provided the company with testing devices for free. The government instituted a protective tariff, which was set at 10 percent in 1930 and then raised to 35 percent in 1932, subsequently eliminating foreign brands from the market.

³⁶"Gaiasha no kokusanka naru ka" [How will the domestication of foreign automobiles be accomplished?], *Nihon Keizai Shimbun*, 13 April 1953.

³⁷"Showa 29-31 nen no jidosha gyosei," pp. 186-87.

³⁸U.S. Department of Commerce, *Japan, The Government-Business Relationship*, ed. Eugene J. Kaplan (Washington: Government Printing Office, February 1972), p. 117.

³⁹Tadahiro Iwakoshi, *Jidosha kogyoron* [The automobile industry] (Tokyo: University of Tokyo Press, 1968), p. 93.

⁴⁰Ueno and Muto, "The Automobile Industry of Japan," p. 73.

⁴¹U.S. Army, "Army Ordnance Marks 10 Years at Oppama," *The Ordnance Press*, 20 August 1958, pp. 4-5.

⁴²*Ibid.*

⁴³Interview with Tetsuo Okamoto, Tokyo, February 1988.

⁴⁴*Ibid.*

⁴⁵U.S. Army, "10 Years at Oppama," pp. 4-5.

⁴⁶Hearings on the Machinery Promotion Act, House of Councillors, Commerce and Industry Committee, 23 May 1956, Record number 37.

⁴⁷Koichi Shimokawa, "Entrepreneurship and social environment change in the Japanese automobile industry: On the key elements of high productivity and innovation" (Paper presented at the International Conference on the Incidence of the External Environment on the Global Automobile Industry, Breau-sans, France, 27-29 April 1981), pp. 22-23.

⁴⁸"Jidosha gyokai, jiyuka taisaku isogu," *Nihon Keizai Shimbun*, 28 March 1960.

⁴⁹*Ibid.*

⁵⁰For an explanation of the *kanban* system and its origins, see Kenichi Sekine, *Toyota kanban hoshiki* [Toyota's *kanban* system] (Tokyo: Nikkan Kogyo Shimbun Sha, 1981).

⁵¹U.S. Department of Commerce, *Japan, The Government-Business Relationship*, p. 117.

⁵²"Jidosha buhin no kyushu o tanjunksu" [Simplification of five automobile parts], *Nihon Keizai Shimbun*, 29 December 1958.

⁵³*Ibid.*

⁵⁴Nikkan Jidosha Kaigisho, *Jidosha nenkan* [Automobile year-book] (Tokyo: Nikkan Jidosha Shimbun Sha, 1960), pp. 157-59.

⁵⁵Koichi Shimokawa, "The structure of the Japanese auto parts industry and its contribution to automotive process innovation" (Paper presented at the International Policy Forum, Hakone, Japan, 16-20 May 1982), pp. 22-23.

⁵⁶*Ibid.*, p. 6.

⁵⁷Campbell, "The Automobile Industry," pp. 9-12.

⁵⁸*Ibid.*, p. 12.

⁵⁹Smitka, "Competitive Ties," pp. 40-41.

⁶⁰*Ibid.*

⁶¹For an explanation of the cultural basis for vertical relationships see Chie Nakane, *Japanese Society* (Berkeley: University of California Press, 1970).

⁶²The following account is taken primarily from Nikkan Jidosha Kaigisho, *Jidosha nenkan* [Automobile yearbook] (Tokyo: Nikkan Jidosha Shimbun Sha, 1965), pp. 157-58.

⁶³*Ibid.*

CHAPTER 6

INTERNATIONALIZATION

Introduction

Liberalization of trade and capital flows was the major factor affecting the relationship between the Japanese government and the automobile industry in the 1960s. The pressures and fears surrounding liberalization strongly influenced the way in which the government viewed its role vis-à-vis the business community. The government had to balance Japan's need to enter fully into international trade through complete access to foreign markets with the need to ensure that Japanese industry would be competitive enough to export and not be overrun by foreign competitors.

Liberalization was necessary because Japan had to have access to the international market in order to survive and expand. By 1960, Japan's access began to be jeopardized by export and import practices that did not comply with rules and procedures established under multilateral trade arrangements: the General Agreement on Tariffs and Trade (GATT), the International Monetary Fund (IMF), and the Organization for Economic Cooperation and Development (OECD). Japan did not yet have the ability to affect the contents of such arrangements; therefore, it had little choice but to adapt, although it did so more slowly than other nations wanted. As Japan accepted the conditions of various trade arrangements and its industry adapted to liberalized trade, interactions between government and business changed.

Arrangements For Liberalization

During World War II and immediately thereafter, the United States established a system to manage and regulate international economic relations. This system developed from the experiences of

the two world wars, the Great Depression, and the excesses of economic nationalism, experiences that had threatened economic stability and thereby threatened world peace. These experiences gave birth to a new guiding principle: the international economic environment affected the stability of the international political environment. A stable international economic system would enhance the chances for peace. Cordell Hull, the U.S. secretary of state from 1933 to 1944 and one of the founders of the new system, stated:

Unhampered trade dovetailed with peace; high tariffs, trade barriers, and unfair economic competition, with war. . . . If we could get a freer flow of trade—freer in the sense of fewer discriminations and obstructions—so that one country would not be deadly jealous of another and the living standards of all countries might rise, thereby eliminating the economic dissatisfaction that breeds war, we might have a reasonable chance of lasting peace.¹

Supporters of the new system believed that the desired stability could only be achieved through the establishment of a liberal international economic order. They established multilateral arrangements to carry out this objective.

As Japan became bound by the rules and regulations of the new postwar multilateral arrangements, the government-business relationship revolved around controversies over whether the domestic economy could withstand national competition and, if it could not, what steps should be taken to ensure it would become internationally competitive as quickly as possible. Japan first faced this issue when it tried to join GATT.

GATT is a complicated set of agreements applying reciprocal rights and obligations to each country with a differing degree of rigor.² It became effective on January 1, 1948 and since has been expanded by numerous international agreements. It was originally intended to complement the functions of the ill-fated International Trade Organization (ITO). When the charter of the ITO was not ratified, GATT by default became one of the major international instruments for regulating international trade, with the following objective:

The contracting parties recognize that their relations in the field of trade and economic endeavor should be conducted with a view to raising standards of living, ensuring full employment and a large and steadily

growing volume of real income and effective demand, developing the full use of the resources of the world and expanding the production and exchange of goods, and promoting the progressive development of economies of all the contracting parties.

The contracting parties desire to contribute to these objectives through this Agreement by entering into reciprocal and mutually advantageous arrangements directed to the substantial reduction of tariffs and other barriers to trade and to the elimination of discriminatory treatment in international commerce.³

Japan quickly moved to join GATT at the end of the Occupation and submitted a membership application on July 18, 1952.⁴ Japan was not immediately granted membership because of stiff objections from several nations led by the United Kingdom and Australia. Because of these objections, Japan was granted only associate membership (observer status) in October 1953, with full membership delayed until February 21, 1955. Japan, like the European nations, initially had transitional status in GATT, which meant it did not have to accept the obligations of full GATT membership under Article XII because the IMF had given it transitional status under IMF Article XIV. This status was important because IMF Article XIV allowed the use of quantitative restraints to control imports for balance of payments purposes in order to complete reconstruction and settle international debts arising from World War II, while full status under IMF Article VIII did not.

G.C. Allen states that the objecting countries feared Japanese trade “would take its prewar form,” which they believed was based on “social dumping,”⁵ described as “the use of prison or sweated labor to produce goods which could therefore be sold at very low prices.”⁶ The United Kingdom, whose prewar cotton goods industry had declined as India and other colonial possessions began domestic production, believed that as Japanese exports of cotton goods expanded, British industry would be hurt further. At GATT’s preparatory discussions on dumping, several countries wanted to make four types of dumping—price, social, exchange, and service—dutiable. The American position that the definition should be limited to price dumping that causes injury in the importing market was finally accepted.⁷ The limited definition of dumping helped make the objecting countries reluctant to permit Japan’s full membership because social dumping would not be actionable under GATT.

Whether or not the dumping accusations were true, Japan's prewar trade had particularly hurt producers of textiles, and such nations objected to Japan's admittance into GATT. James E. Landes attributes the British objection, in addition to the economic motives, to a basic distrust of Japan arising out of wartime experiences as well as to frustration over American domination of the Occupation, especially its decision to rearm Japan.⁸ Warren Hunsberger further states that the United Kingdom discriminated against Japan in favor of similar imports from low-wage areas of the Commonwealth, while Australia discriminated because of "a residue of political resentment."⁹ Like Allen and Landes, he states that the strongest motivation for opposing Japan's membership in GATT was a fear that a "sudden spurt of cheap [not necessarily dumped] manufactures [would] seriously disrupt markets and damage domestic producers who [had] not been given the time to adjust themselves to the new competition."¹⁰

The value of Japan's GATT membership was reduced when several nations refused to grant most-favored-nation (MFN) status to Japan for several years for the same reasons. The refusals were based on a clause in Article XXXV that stated if a contracting party does not wish to grant GATT treatment to a newcomer for political, economic, or welfare reasons, it need not until bilateral tariff negotiations are undertaken.¹¹ Japan's major trading partners, including the United Kingdom and Australia, had disinvoked Article XXXV by 1963. This episode's significance is that in the 1960s many Japanese felt that Japan would be refused equal treatment in world trade until the obligations of full status in the IMF, GATT, and the OECD were accepted.

GATT was especially pertinent in interactions between government and business in the 1960s because Japanese tariffs were lowered as a result of GATT negotiation rounds. The overall reduction in tariff rates affected the motor vehicle industry because the tariff rates on automotive products were high. The first step to lower tariffs to comply with GATT occurred in January 1968 when the tariff was lowered on large passenger cars from 40 percent to 36 percent and on small passenger cars from 35 percent to 28 percent.¹² In April 1971, all tariffs on passenger cars, as well as on trucks and automotive parts, fell to 10 percent, eliminating the differential between large and small cars and bringing the tariffs in line with those of other major auto producing nations. These tariffs were eliminated in 1978.

The IMF was the major institution forcing Japan to undertake liberalization in the 1960s. The IMF was created in 1944 under the

Bretton Woods Agreements to organize the conduct of international monetary affairs through the elimination of exchange controls and the restoration of reasonably stable exchange rates combined with national independence in monetary and fiscal policy. It began to play an important role in the mid-1950s when the United States no longer needed to finance European and Japanese reconstruction.

Japan joined the IMF on August 13, 1952. It initially held transitional status, as did the European nations, under Article XIV. After the last European nation, Italy, shifted from transitional status to full status under Article VIII in 1959, Japan came under increasing pressure from the IMF to accept full status. In addition, Japan's balance of payments position had improved, eliminating the reason for transitional status. At the IMF's 1959 annual meeting, Japan was urged to hasten its liberalization process. Japan entered into negotiations with the IMF and agreed to switch to Article VIII status in April 1964.

When Japan accepted Article VIII status, it relinquished the right to impose foreign exchange restrictions for making payments and transfers for current international transactions, to engage in discriminatory currency arrangements, to establish multiple exchange rates without consultation with the IMF, and to apply restrictions on the convertibility of yen held by nonresidents.¹³ In addition, it automatically switched to full status in GATT under Article XII.

Japan also joined the OECD on April 28, 1964, which was founded on September 20, 1961 as a transformation of the Organization for European Economic Cooperation (OEEC) established in the context of the Marshall Fund at the end of World War II. After 1949, the OEEC became increasingly involved in an effort to form a free-trade area in Western Europe. The OECD's formation reflected French dissatisfaction with efforts to include Britain in the free-trade area as well as American dissatisfaction with the growing trade imbalance and its role as "donor nation."¹⁴ In addition, the United States wanted to encourage Europe to adopt global liberal trade policies that would not discriminate against itself and Canada. The United States planned to include Japan to further expand the scope of the organization. Thus while the OEEC was to stabilize Europe, the OECD was to be a new international forum for highly developed, market-economy industrialized nations.

The significance of Japan's admittance to the OECD is twofold. First, OECD membership required Japan to fully conform to OECD codes. In return, membership gave Japan greater access to the European market through the receipt of MFN status.

Second, Japan had particular trouble accepting one OECD provision, the Code of Liberalization of Capital Movements, that required the freeing of foreign capital transactions. Japan was permitted by the "Memorandum of Understanding Between the OECD and the Government of Japan" to temporarily maintain seventeen reservations to the Code of Liberalization of Capital Movements in order to prevent capital flight and to control capital penetration. Japan also was allowed to maintain ten reservations on technical assistance to the Code of Liberalization of Nontrade Transactions that controlled technology imports. Other countries were permitted reservations, but none had as many as Japan. In the late 1960s, Japan was strongly criticized for delaying the abolition of these reservations and was forced to abandon most of them in the early 1970s.

Japan embarked on a capital liberalization program to comply with the OECD codes. Prior to Japan's admittance into the OECD, all foreign direct investment required government authorization, and foreign companies were not guaranteed the right to transfer income overseas.¹⁵ In 1963, investment was liberalized to the point that if a transaction received authorization, income could be freely transferred. In 1964, Japan permitted the free transfer of funds for short- or medium-term credits for exports or imports, for current income and liquidation proceeds of direct investment, and for portfolio investments listed on the stock market.

Heated debate occurred within Japan over the pace and implications of capital liberalization. In 1965, the first capital liberalization program was announced to take effect in 1967 and be completed by 1972. This plan divided industries into two groups. Industries in Group 1 could be 50 percent foreign owned, while those in Group 2 could be 100 percent foreign owned. Some industries that were considered too weak to withstand liberalization were excluded from both groups.

Manufacturers of motor vehicles (all kinds of vehicles, motor vehicle chassis and accessories, and motor vehicle parts and accessories) initially were excluded and then placed in Group 1 in April 1971 and in Group 2 in May 1973. The liberalization of capital had especially strong implications for the motor vehicle industry because American auto companies historically entered overseas markets via capital rather than by exports.¹⁶ The initial exclusion of motor vehicles, along with delays in liberalizing imports of engines, parts, and used cars, became part of a major trade controversy between the other OECD nations and Japan. This controversy, as it affected automobiles, mainly involved the United States.

Japan, with the concurrence of the IMF, adopted the "Plan for Trade and Exchange Liberalization" in June 1960 to prepare for its full membership in GATT, the IMF, and the OECD. This plan established four liberalization stages for merchandise imports that ranked products according to the degree of effect they would have on the economy.¹⁷ Examples of items in each liberalization stage were: stage one, raw materials such as mineral ores; stage two, synthetic fibers and glass; stage three, machine tools and automobiles; and stage four, agricultural products such as rice. In mid-1961, the Japanese government decided on a liberalization target of 90 percent by September 30, 1962. This goal was reached by August 31, 1963 when liberalization reached 92 percent.¹⁸

The OECD designed a liberalization ratio based on the licensing procedure under which imports were allowed into Japan.¹⁹ Merchandise was classified by four-digit numbers covered by the Brussels Tariff Nomenclature (BTN) system. If a good was imported under the Foreign Exchange Allocation (FA) system, which required consideration on a case-by-case basis to obtain import authority and the right to purchase needed foreign exchange, it was not considered to be liberalized. However, if an import arrived under either the Automatic Fund Allocation (AFA) system, which permitted automatic approval and allocation of foreign exchange but still required applications to be submitted to MITI, or under the Automatic Approval (AA) system, which automatically granted import licenses, it was considered liberalized. Warren Hunsberger explains how the liberalization ratio was set:

The Japanese use 1959 as the basis of calculation so the importance of liberalizing any particular item is measured by its share in imports of that year. Items that were important then, like raw cotton or crude petroleum, carry heavy weight in measuring liberalization. Items whose import was small in 1959 carry little weight.²⁰

In addition, some items were placed on a negative list and so were still subject to quantitative controls even after the Japanese accepted Article VIII status. Takafusa Nakamura states that the reasoning behind this list was that liberalization would not be authorized until genuine competitiveness had been achieved.²¹

In the case of the motor vehicle industry, three- and four-wheeled truck imports were liberalized in October 1960 as they had little foreign competition. Completed passenger car imports were liberalized five years later, in October 1965. Restrictions on

engines, engine parts, chassis with engines, and used cars were not lifted until February 1970.

Japan's membership in these multilateral organizations affected government-business relations in two ways. First, the government lost many tools it had used to regulate and aid business during the 1950s. Japan could no longer use (except for agricultural products) strong foreign exchange controls, quantitative quotas, high tariffs, and some export subsidies. The close government-business relationship that existed in the early 1950s had been possible in part because a supportive international environment had allowed and even encouraged Japan to use these tools to reestablish and protect its industries. After these tools were taken away, the government had fewer methods to facilitate business compliance.

Second, the controversy over how Japan should prepare for liberalization and what power the government, particularly MITI, would have to structure the economy affected the government-business relationship. It facilitated cooperation because government and business sought to delay the implementation of liberalization measures as long as possible to enable industry to become competitive. At the same time, it created tension in the relationship when the government sought to implement reorganization programs in many industries, including automobiles. The tension that resulted from MITI's attempt to pass the Special Measures Law for the Promotion of Designated Industries and its later efforts to promote mergers exemplified this relationship.

Reorganization Plans

The primary government program to prepare Japanese industry for liberalization was industrial reorganization based on the Japanese concept of "excessive competition" or *kato kyoso*. Excessive competition, defined as existing when too many firms engage in competition, was believed to result in overproduction, price cutting (especially on exports), loan defaults, and the bankruptcy of major companies. As Michael Cusumano states, "Too much competition would not have mattered so much if MITI had felt confident that it could isolate Japan's automobile market from the rest of the world indefinitely."²² Because of the pressures from GATT, the IMF, and the OECD, MITI knew that it could not.

Martin Brofenbrenner, while dismissing the validity of excessive competition when used "as a tainted cover for monopoly or

cartelization," describes the economic reasoning behind its application to various types of cases.²³ He relates the most frequent usage "to decreasing-cost and excess-capacity firms and industries, where there are large economies of scale." Brofenbrenner provides an excellent description of how this reasoning was applied to the automobile industry.²⁴ He states that if only one company produced automobiles, it would be able to produce and sell enough units to reach an economy of scale that would be competitive internationally. It could export without any, or only a minimal, need for government protection. However, if too many companies produced automobiles, they could not produce at a level that would be competitive internationally in the absence of protective tariffs and quotas. The latter situation would prevent exports except when dumped. The reasoning follows then that if the Japanese automobile industry had only two or three large producers, they could each produce enough to be competitive enough to withstand liberalization. If only one producer existed, unit prices would drop even lower, exports would increase, and Japan's overall trade balance would improve. He further states that if such a program is carried out and if trade liberalization is accomplished, the argument "includes the promise to compensate the consumer for reduced competition among Japanese firms by increased competition on the international level." This line of reasoning was behind MITI's attempts to reorganize the automobile industry in the 1960s through mergers and tieups.

Brofenbrenner was not happy with government-imposed solutions to excessive competition based on organizing Japanese exports, disciplinary price-fixing, or various types of competition-reducing practices. He preferred strict enforcement of antimonopoly regulations that would allow the market to eliminate excessive competition. He felt that Japanese governmental controls themselves were the chief culprits in causing excessive competition by creating expectations that profits would be protected. In some industries, profits were protected through various cartels. In the auto industry, the expectation that profits would increase came from the protection of the market and the rapid growth of the economy. As a result, companies increased output and capacity. Thus, during the 1960s, the Japanese government sought to impose solutions on the automobile industry through its various industrial reorganization programs, which the industry rebelled against.

Often, excessive competition is depicted as a unique Japanese phenomena related to the market-share maximizing behavior of

Japanese companies. Yasusuke Murakami and Kozo Yamamura in their analysis of market-share maximizing behavior during the 1950s and 1960s claim that excessive competition is really profit-maximizing behavior that only seemed to be market-share maximizing because it occurred when firms faced decreasing long-run average costs.²⁵ In turn, decreasing long-run average costs occurred because of rapid growth in domestic demand and world trade, various favorable environmental conditions (e.g., large supply of trained labor and a high savings rate), and government policies designed to prevent "unstable equilibrium" (e.g., administrative guidance on investment and various cartels). While in partial agreement with Brofenbrenner that government policies helped create "excessive competition" that resulted from market-share maximizing behavior, Murakami and Yamamura—with hindsight unavailable to Brofenbrenner in 1966—disagree that the attempted policy solutions were misguided. Rather, they believe such solutions helped permit "the orderly growth of innovative large firms," although they also entailed political costs arising from the creation overseas of the "Japan, Inc." image, an image that became synonymous with the Japanese auto industry. They hasten to add that while these policy approaches were necessary and effective in the 1960s, they are no longer valid.

Other scholars stress additional motives for the reorganization program. William Duncan, in a discussion limited to automobiles, states:

The government both during the 1930s and the 1960s sought to reorganize the industry in order to insure that its future growth would be domestically controlled. In other words, though a prosperous and competitive industry was of top priority, the reorganization policy came to center on a political objective, i.e., management control. By 1962 the issue among MITI planners was not how to maximize automobile production but rather how to maximize domestically controlled automobile production.²⁶

Duncan is stressing Japanese opposition to foreign ownership, which, in the case of automobiles, can be traced back to Ford's and General Motors's dominance before World War II. Duncan asserts that the Japanese concept of "reorganization" is different from the Western idea of "infant industry protection" because it is associated with maintaining domestic control of industries rather than being a temporary measure to aid import substitution.

Chalmers Johnson raises yet another valid motivation for the reorganization program, especially in terms of the Special Measures Law for the Promotion of Designated Industries. He believes that the reorganization effort was a power play by MITI, or at least some MITI officials, to maintain their control over the economy and their *raison d'être*.²⁷ He states that MITI felt that it would be left "without any continuing function" if liberalization exposed that it was the weakness of Japanese industry that was disrupting the economy and allowing the large increase in foreign ownership.

These explanations taken together make clear the motivations behind the policy and demonstrate the complexities of policy making. Japan was faced with a time limit in which to develop an internationally competitive automobile industry. The Japanese government did want an automobile industry composed of domestic manufacturers. Because the economy was rapidly growing and the auto industry was becoming competitive, the automobile manufacturers increasingly were able to assert their independence. Because MITI's loss of control over foreign exchange decreased its power, it did seek new avenues for control. But these concerns were only part of the broader policy context that sought the best way to protect the country's industries by meeting the challenges of liberalization through the elimination of excessive competition.

The Selection

The passenger car industry was an obvious candidate for reorganization. MITI believed the industry had economic potential. Production was increasing steadily and, importantly, the industry was beginning to export. Because it had just reached the stage of mass production, policy makers could not imagine that it was ready to compete internationally, especially with such giants as General Motors and Ford.

MITI felt the industry could be strengthened through reorganization to eliminate excessive competition. Conventional wisdom stated that the successful production of passenger cars was tied closely to mass production. The government felt that existing excessive competition inhibited mass production, and mass production was needed to achieve competitiveness.

The loss of market share by Nissan and Toyota to new entrants—the creation of excessive competition—lent urgency to reorganization plans. More producers entered the market as economic growth increased domestic demand for passenger cars

during the late 1950s and early 1960s. In 1950, Toyota and Nissan accounted for 83.3 percent of passenger car production, and they had only one major competitor, Ota Jidosha.²⁸ By 1955, the Big Two's market share had fallen to 69 percent as Isuzu and Hino started KD production, and Prince began passenger car production. By 1960, three additional competitors—Mazda, Mitsubishi, and Fuji Heavy Industries—had entered the market, although Ota had ceased producing vehicles. Toyota and Nissan's market share fell even further, to 58.8 percent. The final three Japanese passenger car producers—Daihatsu, Honda, and Suzuki—(Suzuki produced forty-three passenger cars in 1955 and 1956 but halted production until 1961)—entered the market by 1964, raising the number of producers to eleven.

The number of producers remained relatively stable at five throughout the 1950s and then suddenly increased at the beginning of the 1960s. This trend was considered an alarming side effect of protectionism and economic growth by many who felt it would potentially have a negative impact on competitiveness. In retrospect, Toyota and Nissan were able to retain a combined market share of approximately 60 percent from the mid-1960s on, and the increased competition forced domestic producers to be more innovative. But around 1960, it appeared that their market share was steadily declining and that their competitiveness might also.²⁹

The renewed threat from European manufacturers, especially Renault and Rootes, in 1960 and 1961 also precipitated plans for reorganization. Although the potential impact from Europe was never permitted to materialize, it lent credibility to those arguing that the smaller passenger car producers were vulnerable to foreign takeover if not protected or merged. Foreign small cars were still of higher quality and lower price than domestic models.

This threat developed just prior to the expiration of the KD contracts between Hino/Renault and Isuzu/Rootes in 1962. Renault and Rootes, anticipating the liberalization of the Japanese market, attempted to get a head start over other foreign companies by maintaining their relationships with Hino and Isuzu. Renault wanted to continue cooperation in the area of sales and also possibly invest in Hino.³⁰ It was rumored that Renault might keep its patent fees from Hino inside Japan to gradually buy Hino. Rootes tried to negotiate an extension for KD production of the Hillman. By proposing to allow production without requiring any remuneration, Renault hoped to avoid any need for government approval of the extension.³¹ This scheme would effectively circumvent foreign exchange controls. Rootes would lose income under such a proposal

but would retain free advertising for its nameplate and would be able to use Isuzu's sales network after liberalization. Isuzu, by continuing to have access to Rootes technology, would have a safety net in competing with Nissan and Toyota.

The new arrangements failed to materialize. Rootes and Isuzu did organize on paper a joint sales agency named Yamato Motors (later Shinsei Motors). In 1967, Chrysler would gain control of Rootes and try to use Shinsei Motors as an operations base in Japan.³² Renault was stymied by MITI when Hino became affiliated with the Toyota Group in 1966. In the same period, attempts by Mitsubishi and Kawasaki to import passenger car technology from Fiat and Benz, respectively, failed to win government support.³³

Increased domestic competition and concern about foreign capital investment reflected the environment in which the decision to reorganize the automobile industry took place. The combination of these problems and the financial, labor, and cultural difficulties inherent in horizontal mergers set the stage for changing government-business interactions during the reorganization period.

The Three Group Concept

MITI's first attempt to reorganize the automobile industry was the "three group concept." This concept was developed in 1960 and was the focus of policy discussions until late 1963.

The three group concept was designed to limit the number of manufacturers of passenger cars—excessive competition—in order to stimulate the mass production thought to be crucial to competitiveness. The plan sought to establish three groups of passenger car producers; a given manufacturer could only produce cars within one group. The three proposed groups were: two conventional passenger car manufacturers (Nissan and Toyota), two or three specialty car producers (high quality, minidiesels, sports), and two or three minicar producers.³⁴ A manufacturer of minicars could not make conventional passenger cars or vice versa. Individual companies were not named, but this plan, if passed, probably would have left only Nissan and Toyota as conventional passenger car manufacturers.

This concept was announced at a meeting of the Industrial Structure Investigation Council's (Sangyo Kozo Chosa Kai) Subcommittee on Capital in June 1961. The Council was created on April 1, 1961 to prepare for Japan's overall liberalization. The concept was

entitled the "Guideline of Policy Hereafter for the Motor Vehicle Industry" and was delineated further by Mr. Manabu Sasaki of MITI's Machinery Section at the Conference on Liberalization Policy for the Machinery Industry on August 4.³⁵

The August announcement outlined a plan to strengthen the passenger car industry and included more than just the three group concept³⁶:

1. Production Measures
 - a. Obtain a waiver from the liberalization of engines and engine parts.
 - b. Revise the foreign capital law.
 - c. Establish a special production system (three group concept).
2. Technology Measures
 - a. Support specialized promotion through financial aid.
 - b. Construct a high-speed test course.
 - c. Establish departments of automotive engineering in universities.
3. Materials Measures
 - a. Cost down the cost of steel, specialty steel, glass, etc.
 - b. Standardize parts production.
 - c. Stabilize iron scrap prices.
 - d. Promote low-cost nickel imports.
4. Rationalization
 - a. Set up special rationalization funds in JDB and the Small and Medium Companies Finance Corporation.
 - b. Extend depreciation life on equipment.
 - c. Expand depreciation system.
 - d. Revise the tax system.
 - e. Revise the sales system, especially to promote the formation of consumer finance companies.

By early 1962, MITI was preparing legislation that would empower it to implement the three group concept. The law was tentatively titled the Passenger Car Industry Promotion Law (Joyosha Kogyo Shinko Ho). While this law was discussed in various incarnations until late 1963, it was never submitted to the Diet for consideration.³⁷ Its failure was partially due to its subsequent inclusion in the Special Measures Law for the Promotion

of Designated Industries, which the Japanese business community strongly opposed. Discussions of the Passenger Car Industry Promotion Law included these points:

1. Mass production would be promoted within the context of the three group concept.
2. MITI's permission would be required for new production.
3. MITI would allow companies to work together to concentrate production and, if necessary, would provide financial aid.
4. The auto parts industry would not be included since it was covered by the Machinery Industry Promotion Law.

The next major step in the development of the three group concept occurred on April 12, 1962 when a Passenger Car Subcommittee was set up within the Heavy Industry Section of the Industrial Structure Investigation Council.³⁸ The subcommittee was headed by Katsuji Kawamata, president of Nissan Motor Company, and included representatives from each passenger car company, middle and upper level staff from financial institutions, and scholars. Ultimately, this subcommittee only dealt with technical issues. Its reports centered on the status of the Japanese passenger car industry relative to foreign producers. The first interim report was published on October 11.³⁹

MITI felt that it needed a second subcommittee to serve as a forum to develop a policy consensus rather than simply discuss the status quo and technical issues. The Passenger Car Subcommittee had been unable to hold such debates because of the low rank of most of its members. After overcoming industry's initial opposition to the new committee and obtaining agreement from the Automobile Manufacturers Association, a Special Subcommittee on Passenger Car Policy of the Industrial Structure Investigation Council was established on September 12.⁴⁰ The special subcommittee was to use the findings of the Passenger Car Subcommittee to develop policy alternatives for the automobile industry. It was chaired by Koki Imazato, the president of Nippon Seiko K.K., and included the presidents of the major auto companies.⁴¹

In October Mr. Sasaki stated why the special subcommittee was necessary:

The passenger car problem cannot remain in the mist of vagueness. The passenger car is able to become the center of future motorization. The motor vehicle industry has under it a large number of related industries and it prides itself on being a core industry for economic development. Such an important industry cannot be allowed to decline because of liberalization. And also, in order to develop it in the future and place it under national control in a broad sense [control by domestic producers not the government], it cannot be left under the control of foreign currency. Because it is a core industry, it cannot exist where the nation's control cannot reach it.

On the other hand, IMF's liberalization advice inevitably will come. If so, this is really the time to decide a concrete strategy for the passenger car by directly researching its problems. With this in mind, a policy subcommittee that examines only liberalization policy for the passenger car was established.⁴²

He admonished the membership in an effort to force the subcommittee to make policy decisions:

I would like you to debate thoroughly standing on a high level and decide what the Japanese passenger car industry should be. After that, the development process for individual companies should be considered along with this great direction. This is no longer an intellectual problem like control or free economy or cooperative adjustment. In this time of liberalization, this is an actual problem, simply live or die, develop or maintain the status quo. It is a mistake if you think such *amae kangae* [dependent thinking] as "anyway the government will do it properly." I really strongly wish that this problem will be resolved by the manufacturers as it is their own problem.⁴³

The special subcommittee released its final report on December 18, 1962 outlining the fundamental direction for passenger car policy. The report conceptually endorsed MITI's earlier policy proposals:

The motor vehicle industry contains a vast number of related industries and workers so its development will

greatly influence the expansion of the people's economy as a whole. And in the future, they should try to develop to be an expert industry inasmuch as it is an important industry. However, it cannot yet be fully equipped with international competitive power in the production system, it's not yet established a sales system, and roads and surrounding conditions are remarkably behind compared with the United States, Europe and advanced countries. In these, international competitive power is not yet fully acquired.

Therefore, on the premise that liberalization will be achieved by the end of fiscal 1964, we should at this time promptly establish a production system for the passenger car industry and at the same time try to upgrade its physical plant, prompt adjustment of the sales system and surrounding conditions and wherewith strengthen its international competitive power and try to establish its basis as an export industry.⁴⁴

The report presented possible policy initiatives⁴⁵:

1. Establish a mass production system in order to achieve widespread cost-down by the time of liberalization. In order to do this:
 - a. Check the increase in kinds of cars.
 - b. Decrease the current number of kinds of cars.
 - c. Promote tieups and mergers.
2. Vigorously invest capital in those enterprises that are expected to be mass producers and strong exporters.
3. Increase imports of foreign cars by the time of liberalization.
4. Quickly decrease the price of domestic cars and promote their quality by the time of liberalization.
5. Strongly promote the rationalization of the parts industry by promoting
 - a. unification and simplification of parts standards,
 - b. concentration and planning of parts ordering, and
 - c. amendment of the excessive quality of parts.
6. In combination with the move to adjust the production system in order to prevent the negative effect chaotic building will have on such adjustment,

statutes are to be enacted for the purpose of checking the advance of new manufacturers and at the same time ensuring the effectiveness of earlier points.

7. Promote the adjustment of the sales financial system in combination with the adjustment of the production system and an ordered sales system.
8. Epoch-making policy is to be practiced given the influence of roads and the surrounding environment on passenger car demand and cost. At the same time, promote the adjustment of various legal requirements as well as changes in the tax system.

Industry Reaction

The presidents of the companies, under pressure to write a report and conceding in principle that the industry faced excessive competition, had written a report supporting MITI's position. When it came time to implement specific recommendations early in 1963, they balked.

Nissan and Toyota took a neutral stance. This stance revealed that, although they understood they would be the primary beneficiaries of legislation to limit the number of automobile producers, they still had misgivings about the proposed degree of government involvement in the industry.⁴⁶ Instead, they decided to direct their energies toward delaying commodity and capital liberalization. Hino, having just completed a mass production factory, expressed support for keeping new companies out of the market.⁴⁷

The Small Car Industry Association stated their views on the policy in January 1963:

Our committee consists of three companies who are members of the policy committee [MITI's special subcommittee] and four other companies who are actually producing or are going to produce passenger cars. They were obliged to examine their opinions about the report. Therefore, a Board of Directors' meeting was held on January 25 and also a meeting of members producing passenger cars for an exchange of opinions.

Some of them expressed opinions in direct opposition to this report from the international viewpoint, and also

some of them expressed opinions in support, saying it is a necessary policy to maintain the motor vehicle industry as a national industry. Opinions were expressed from various angles and our committee's views below are based on this.

1. We will fundamentally cooperate with this report. That means that for the time being we won't produce the kinds of cars (over 1,000 cc) that are problematical from the standpoint of international competitive power.

2. But, some margin should be left [for us]—high technology development should be left (gas turbines, rotary engines, etc.). Tentatively, our committee's funds and mental cooperation will be given. And, we will carefully weigh how various areas would respond.⁴⁸

Honda Motor Corporation voiced strong opposition to the report and MITI's three group concept. Since Honda was not yet producing passenger cars, they would be frozen out of the market if MITI's policy were implemented. Honda was able to object to the policy because of its position as the largest producer of motorcycles and as one of Japan's largest exporters.

Shoichiro Honda, the founder of Honda Motor Corporation, had planned to enter the passenger car field since the late 1950s.⁴⁹ Mr. Honda felt that this could be done with ease given the company's experience producing engines. In late 1962, Mr. Honda received an unofficial inquiry from MITI asking if his company were planning to produce a specialty passenger car. This request was motivated by the exhibition of a prototype sports car (S-360) and a lightweight truck (T-360) by Honda Motors at the 1962 Tokyo Motor Show in October. The proposed legislation was one reason Honda had hastened to display vehicles at the show. MITI's question caused Honda to accelerate production plans since it appeared that if it did not enter the market soon, it never could. In the long run, MITI's opposition caused a delay in Honda's plans because its first passenger car was put on the market in October 1963 (a truck had been marketed the previous August) before being fully tested. The car had to be withdrawn and redesigned due to technical problems.

On January 18, 1963, Mr. Honda told newspaper reporters that "free competition should be practiced without restraining the types of cars."⁵⁰ Mr. Honda described this confrontation in an interview in October 1983:

After we succeeded in the motorcycle race at the Isle of Man [December 1961], we gradually became confident and enthusiastic about starting the manufacture of passenger cars. We had a letter from customers saying that they wanted to use a Honda-made passenger car. And many younger Honda men pushed me to start passenger car manufacturing. Therefore, we made a prototype and then we dared to enter a very severe car race. In these circumstances, we had encountered a serious problem posed by MITI. They tried to establish a new regime authorized by new legislation, the so-called Special Measures Law. In their regime, they insisted that manufacturers who were not manufacturing at that moment should not be able to start manufacturing passenger cars. We, our plan, suffered significantly from this guidance. Then I resisted (revolted against) MITI vigorously. "We have a right to manufacture what we want to!" "We are free!" I do not know whether because of my revolt or because of their own common sense the new legislation, or rather their attempt at new legislation, was cancelled. But our plan was delayed at least one year.⁵¹

In early 1963, it appeared that a partial consensus (the most prominent exception being Honda) had been reached between government and business over the future direction of policy. The consensus was only on the general policy direction, not on how each specific company would be affected. Ultimately, the policy failed because no company was willing to be the one eliminated. William Duncan quotes one company president who was a member of the special subcommittee: "In the council I am a member, but when I return to my company I am president. The adjustment between conception and reality is difficult."⁵² The differences between conception and reality fully emerged with the introduction of the Special Measures Law for the Promotion of Designated Industries.

Special Measures Law for the Promotion of Designated Industries

MITI's major legislative initiative in 1963 was the Special Measures Law for the Promotion of Designated Industries (Tokutei Sangyo Shinko Ringi Sochi Ho). This bill was MITI's attempt to

obtain legal authority to promote reorganization in industries it felt were especially vulnerable during the liberalization process. It was also an expression of the concept of "public-private cooperation" or *kanmin kyochō*. This concept was based on a relaxation of antitrust laws to permit various types of cooperative behavior. Industries "designated" as "vulnerable" included specialty steel, petrochemicals, ferro-alloys, machinery, tires, and automobiles. The earlier debate on the three group concept was subsumed in the broader discussion that resulted from this bill. Legislation affecting only the automobile industry continued to be discussed during 1963 but would have been redundant with the passage of the Special Measures Law.

The bill specified development measures that could be used to help the vulnerable industries. These measures included standardization, specialization of production, establishment of joint capital enterprises, organization of industrial complexes, rationalization of plant and equipment investment, mergers, and the conversion of businesses to other fields of activity in line with the reorganization of industrial structure. Takafusa Nakamura states: "The bill would have obligated businessmen to comply with these standards while the government devised the requisite monetary and tax measures and made exceptions to the Anti-Monopoly Law as necessary, with banks also supplying funds."⁵³

The Special Measures Law is often called the "Bill Without A Sponsor."⁵⁴ This nickname explains why it failed to win the support of business. The bill was written within MITI's Enterprises Bureau without industry consultations except for reports such as that by the Special Committee on Passenger Cars. There was disagreement over the bill even within MITI.

On February 1, 1963, the Enterprises Bureau announced the final draft of the bill, which was titled the Draft Law of Special Measures for Strengthening the International Competitive Ability of Designated Industries.⁵⁵ During the next two months, amendments designed to weaken its impact were added to overcome opposition from the Japan Fair Trade Commission (JFTC), the financial community, and business leaders. The JFTC feared that the bill would impair the Anti-Monopoly Act (antitrust regulations). The financial community felt that it would interfere with the operation of their financial *keiretsu* (company groupings around a principal bank). Keidanren, the major business federation, opposed giving MITI, in particular, and the government, in general, more power to intervene in the economy.

On March 22, a Cabinet conference changed the title to the Special Measures Law for the Promotion of Designated Industries, which was then presented to the 43rd session of the Diet on March 25.⁵⁶ In the Diet, the Japan Socialist Party and others opposed it. At the same time, the financial community and the JFTC continued strongly to oppose the bill. Ultimately the opposition of these groups made the bill too controversial. The Diet session ended on July 6 without any action taken.

The bill ceased to be a threat as of July 23, 1963 when its main supporters in MITI's Enterprises Bureau were transferred to new jobs and opponents of the bill moved into their positions. The bill was reintroduced at the 44th session (October 17 to October 23, 1963) and the 46th session (January 30 to June 26, 1964) of the Diet. It failed to be considered both times.

The automobile industry's stance on this bill and on the reorganization program stayed combative during this period. The major producers continued to take a neutral position and stated through the Automobile Manufacturers Association that it was unnecessary to arrive at any "unanimous opinion."⁵⁷ The Small Car Industry Association established the System Research Committee in May 1963 to study the implications of the bill.⁵⁸ The members of this committee had divided opinions: some felt that the bill would hinder technological progress and infringe on the freedom of the companies, and others felt it was a necessary evil to prevent the advance of foreign capital. The association finally decided that MITI had not presented a "positive approach."

After the bill failed to gain support for the third time, MITI dropped it. MITI had failed to gain any legal authority to implement its industrial reorganization concept "for reasons not particular to the auto industry" but related to business and financial opposition in general.⁵⁹

Koichi Shimokawa argues that MITI's ultimate failure to win business support for its automotive reorganization program was due partially to underestimating the competitiveness and dynamism of its own industry.⁶⁰ Given the deep-seated fear of internationalization, it is easy to understand why MITI felt the automobile industry—in terms of the mass production of passenger cars—was uncompetitive. Companies, wanting to maintain their independence and perhaps in a better position to know their own strength, rebelled against MITI's reorganization programs. As with the People's Car Project, the industry fought to maintain its independence when MITI attempted to control rather than work as a partner.

The failure of the bill did not mean that the concept of reorganization was entirely abandoned. Instead, MITI attempted in the latter half of the 1960s to use administrative guidance and financial aid to induce voluntary compliance. The major positive result of the reorganization movement, according to Katsuji Kawamata, was the industry's increased awareness that it had to take steps to prepare for impending liberalization.⁶¹

Preparation for Capital Liberalization

After Japan liberalized passenger car imports in June 1965, the major issue facing the automobile industry was the liberalization of capital imports. This issue was one of the most controversial in the context of interactions between government and the automobile industry.

In consultations with the Automobile Manufacturers Association on March 15, 1965, MITI Minister Yoshio Sakurachi enumerated three items that needed attention before liberalization was enacted.⁶² The technical and financial strength of companies had to be enhanced through business mergers. Companies had to refrain from excessive sales competition and had to prepare quickly to export. The assemblers also needed to pursue close cooperation with, and the strengthening of, the parts industry. At the same meeting, the Automobile Manufacturers Association stressed that, while they were not concerned about the impending liberalization of completed passenger car imports, the liberalization of parts and capital was not yet possible.

The issues raised at this meeting formed the focus for policy debates in the second half of the 1960s. In particular, the debates focused on the potential takeover of weak firms by foreign capital as capital liberalization approached and as the major American automobile companies showed an active interest in Japan. The high degree of controversy surrounding this issue resulted in a wide range of policy makers, including the Liberal Democratic Party, which established the Automobile Industry Policy Conference in 1966, and major business federations, becoming involved in the automobile issue.⁶³

In 1964, Ford and General Motors began negotiations with Japanese companies; Ford was in contact with Nippon Oil Seal and General Motors with Nittsu, a distribution company.⁶⁴ The continuing rumors and press reports, some true and some not,

about U.S. interest in Japan's auto industry added to the tension. MITI was alarmed by the reports. It was true that the American companies were interested in Japan because U.S. imports of Japanese automobiles had increased from 1,806 in 1960, to 34,441 in 1965, and to 422,464 in 1970. When asked if Japanese imports bothered him, Henry Ford II stated:

They sure as hell do. They're turning out mighty good cars and I don't like the way they're cutting into the American market. I haven't got anything against open competition. If they can build a better car and sell it for less money, let 'em do it. But what burns me up is that I can't go into Japan. We can't build, we can't sell, we can't service, we can't do a damn thing over there. Ford Motor Company still owns land in Japan, and we still have a building there that was put up before the war. I understand it leaks like a sieve but it's still there, built with our money, and we can't use it. I'd be in there tomorrow if the Japanese would let me. I'd be manufacturing cars and I'd give the Japanese a run for their money. But they won't let me in and that's why the whole thing is unfair. I think this country ought to have the guts to stand up to unfair competition.⁶⁵

Concern about foreign capital also grew because increased fragmentation of the passenger car market appeared to make the industry conducive to takeovers. Because Toyota and Nissan had achieved a measure of competitiveness by 1965, their existence was not directly threatened by capital liberalization. This was not true for the smaller and newer auto companies.

In 1965, there were eleven Japanese producers of passenger cars and thirteen producers of trucks. The passenger car companies' market shares were: Toyota (33.9%), Nissan (24.4%), Mazda (11.7%), Prince (6.8%), Mitsubishi (6.6%), Fuji Heavy Industries (5.4%), Isuzu (4.4%), Hino (3.8%), Daihatsu (1.6%), Honda (1.3%), and Suzuki (0.3%). When production of trucks and buses is included, the smaller companies' market share position improved: Toyota (25.2%), Nissan (18.4%), Mazda (14.6%), Mitsubishi (8.8%), Daihatsu (7.9%), Isuzu (5.2%), Prince (4.9%), Fuji Heavy Industries (4.9%), Honda (3%), Hino (2.7%), Suzuki (2.2%), Aichi Trucks (1.8%), and Nissan Diesel (0.3%). The last two companies were closely tied to Nissan.

Finally, a recession began in late 1964. Unlike the early 1960s when all the automobile companies were growing and profitable, the recession quickly strained the resources of the financially weaker companies.⁶⁶ The problems faced by the smaller companies increased the possibility that they could be taken over by foreign capital.

MITI's major policies from 1965 to 1969 reflected these problems. The policies sought to induce voluntary mergers and to postpone capital liberalization for as long as possible. The auto industry rebelled against the former policy but worked closely with the government to ensure the success of the latter.

The Merger Movement

MITI's major domestic policy involving the automobile industry in this period was the promotion of mergers. As with the earlier reorganization policies, the automobile industry was not the only industry in which MITI tried to induce mergers. This policy grew out of the three group concept and the Special Measures Law. It differed from earlier reorganization programs because MITI did not have, or attempt to obtain, a legal mandate to enforce its views.

Financial aid was the major tool the government possessed to encourage mergers. The financial aid available included tax deductible allowances for merging companies and, most importantly, loans from the Japan Development Bank (JDB). Beginning in Japan Fiscal Year 1963, JDB established a special fund for promoting mergers between large companies in strategic (potential export) industries, including the automobile industry.⁶⁷ The first merger to receive these funds was the Nissan-Prince merger in May 1966 (JDB was already supplying funds to aid mergers of small- and medium-sized companies, including the automobile parts companies).⁶⁸ Toyota's merger with Hino in 1966 and with Daihatsu in 1967 were also mergers funded under this program. Altogether, JDB loans for mergers amounted to 11.9 billion yen (\$33 million).

The automobile industry did not draw heavily on the loan program because the size of the loans was too small to make a substantial difference in the companies' total financial picture. One source suggests that the size of these loans could not outweigh the longer-term obligations that might have been incurred from being "indebted" to MITI.⁶⁹ This situation was very different than that which existed in the early 1950s when capital was scarce and the

amount of capital needed was smaller. MITI claimed that even a small amount of government financing was meaningful because it created easier access to private financing.⁷⁰ This claim was more true in the 1950s than in the 1960s when capital was more readily available and the auto industry had proven its potential.

MITI's other major tool to encourage mergers was administrative guidance. Administrative guidance is "the use of influence, advice, and persuasion to cause firms or individuals to behave in particular ways that the government believes are desirable."⁷¹ The effectiveness of this tool is related closely to how individual companies perceive their interests and competitiveness. The effectiveness in this case is revealed by the two major merger negotiations that occurred in the late 1960s. The first, between Nissan and Prince, succeeded while the second, among Mitsubishi, Isuzu, and Fuji Heavy Industries, failed.

The merger of Nissan and Prince is often cited as the first and only successful example of MITI's merger program.⁷² While MITI was instrumental in arranging it, the merger actually was precipitated by Prince's poor financial condition in late 1964. Prince had failed in its attempt to challenge Toyota and Nissan in the 1,500 cc and 2,000 cc passenger car market. In addition, although it had a good reputation in technology, its sales network was weak.

The president of Prince's principal bank, Shozo Hotta of Sumitomo Bank, was worried about Prince's financial status and sought to arrange a merger in 1964. Mr. Hotta approached Mazda with the merger plan since Sumitomo was also Mazda's principal bank. This proposal did not succeed because Mazda, based in Hiroshima and controlled by the Matsuda family, was too hampered by regionalism.

MITI became involved in Prince's merger plans through the intervention of MITI Minister Yoshio Sakurauchi and Vice Minister Shigeru Sahashi. They met with the chairman of Prince, Shogiro Ishibashi, to discuss a possible merger with either Toyota or Nissan. Initially, Mr. Ishibashi was troubled about such a merger because he owned Bridgestone Tire Company, which he wanted to keep as an independent supplier not connected with either Toyota or Nissan. Minister Sakurauchi's father, Ukiyo Sakurauchi, who was an old friend of Mr. Ishibashi, was called upon to mediate. At this point, Minister Sakurauchi flew to Nagoya in January 1965 to discuss a possible merger with Toyota's Taizo Ishida. Toyota decided that it preferred to "go it alone" and informed MITI in March.

Minister Sakurauchi thereupon approached Katsuji Kawamata of Nissan, who quickly agreed to the merger because it would expand Nissan's product line to match that of Toyota. Mr. Kawamata stated: "This merger has been decided on the basis of strengthening international competitive power."⁷³ The two companies and their respective banks settled the details of the merger. The agreement was sealed in May and stated⁷⁴:

1. Nissan will take over Prince and continue to exist as an entity; Prince will be dissolved.
2. The merger's stock ratio will be 2.5 to 1.
3. The company's capital after the merger will stand at 39.8 billion yen (\$111 million).
4. The date for the formal merger will be August 1, 1966.
5. Nissan and Prince will both ask for approval of the merger at regular stockholders' meetings to be held on May 28.
6. A general stockholders' meeting will be held in September after the merger.

Although the impetus for the merger was financial, it "did give a boost to MITI's prestige and set the precedent for further reorganization."⁷⁵ MITI's major contribution to the merger was to seek out and arrange for a merger partner. In addition, MITI gave Nissan the first JDB reorganization loan of 8 billion yen (\$22 million).

Toyota and Hino entered into a business merger on October 15, 1966.⁷⁶ As with Prince, it was precipitated by Hino's financial position. Hino failed to prosper in the passenger car market despite its technological tieup with Renault and stopped production of passenger cars in 1969. Because Hino's continuing strength in truck production complemented Toyota's strength in passenger cars, a merger was mutually advantageous. It was arranged through Mitsui Bank. This was not a true merger like that of Nissan and Prince since the companies maintained separate identities while cooperating in new production, technology promotion, and the purchase of raw materials. MITI's role in this arrangement was limited. Mr. Yoshifumi Kumagaya of the Heavy Industries Bureau acted as one of the go-betweens, which resulted in the merger receiving a JDB reorganization loan of about one billion yen (\$2.8 million).⁷⁷ In 1967, Toyota also entered into a business agreement with Daihatsu, whose minicar production complemented Toyota's

production of larger passenger cars. JDB again provided a loan of about one billion yen.

The second major merger attempt involved three companies: Mitsubishi, Isuzu, and Fuji Heavy Industries. It initially appeared that some combination of these companies would form a third major automotive company to challenge Toyota and Nissan. However, these proposals failed to materialize, demonstrating the limitations of MITI's administrative guidance and the various economic pressures working against the merger program.

In December 1966, Isuzu and Fuji Heavy Industries formed agreements in technology research, the purchase raw materials, new production, and sales.⁷⁸ The companies retained separate identities but established six joint committees to discuss proposed areas of cooperation. Toward the end of 1967, Isuzu decided that a production level high enough to be internationally competitive would be impossible to achieve by cooperating just with Fuji. Thus, when Mitsubishi began making overtures, Isuzu was interested.

Mitsubishi's involvement in the motor vehicle industry began in the 1930s but did not extend to the passenger car market until after 1964. In 1964, the three companies that had been formed out of the breakup of Mitsubishi Heavy Industries by U.S. Occupation authorities in 1950 were remerged. One of these companies, Shin-Mitsubishi, had a motor vehicle division. The merger gave this division a stronger financial base to support its efforts to become the third largest Japanese motor vehicle producer. In order to accomplish this goal, Mitsubishi invested 75 billion yen (\$208 million) in the motor vehicle division from 1966 through 1969.⁷⁹ Mitsubishi, however, needed a partner with experience in passenger car manufacturing in order to expand rapidly before capital liberalization. (Mitsubishi had failed to win government approval for a technology tieup with Fiat in 1962.) Mitsubishi decided to approach Isuzu and Fuji Heavy Industries in December 1967. It received MITI's support for the proposed tieup.

The negotiations quickly ran into trouble. In May 1968, Fuji Heavy Industries ended its agreement with Isuzu in order to enter a tieup with Nissan in October. There were several reasons behind Fuji's action. Fuji and Nissan shared the same principal bank, the Industrial Bank of Japan, which wanted to strengthen the Nissan group and pushed the agreement. Fuji feared it would lose its independence in a tieup with Mitsubishi, given the huge resources of the Mitsubishi group. And, some antagonism remained between Fuji and Mitsubishi from World War II when Mitsubishi and Fuji's

predecessor, Nakajima Aircraft, had competed in aircraft manufacture.

Mitsubishi and Isuzu proceeded with negotiations without Fuji. They agreed to a merger in June 1968, but this agreement also ran into problems. Mitsubishi and Isuzu, rather than complementing each other, made competing products; both were strong in truck production and weak in passenger car production. Most importantly, Isuzu agreed to the tieup on the premise that Mitsubishi Heavy Industries would make its motor vehicle division an independent company. When the motor vehicle division experienced financial difficulties after the imposition of a new purchase tax on automobiles in 1968, the creation of the separate company was delayed. At the same time, consumer complaints that Mitsubishi passenger cars drove like trucks contributed to stagnant sales. Isuzu, like Fuji, started to worry that it would be absorbed by Mitsubishi Heavy Industries and decided not to move forward with the tieup.

Other tieups that were discussed during the late 1960s but never implemented included Isuzu/Nissan and Suzuki/Toyota.⁸⁰ In addition, the Automobile Manufacturers Association and the Small Car Industry Association, at MITI's suggestion, merged in April 1967 to form the Japan Automobile Manufacturers Association (JAMA).⁸¹ The new association represented the convergence in product lines—and the interests—of the former two- and three-wheeled vehicle producers of the Small Car Industry Association and the four-wheeled vehicle producers of the Automobile Manufacturers Association.

The failure of most of the tieups was due to economic pressures and the strong separate identities of the companies involved. The government supported the concept of mergers but provided few incentives and did not have enough persuasive power to overcome the disincentives present. In addition, MITI floated a two-group concept in the late 1960s that contributed especially to the failure of the proposed Mitsubishi-Isuzu tieup. The two-group idea was MITI's last plan to reorganize the industry before capital liberalization and was closely tied to the progress of U.S.-Japan negotiations on automotive trade and investment from the fall of 1967 to October 1969.

The U.S.-Japan Negotiations

After the capital liberalization program excluding automobiles was announced in July 1967, the United States began to pressure Japan to open the automobile sector to direct investments.⁸² Although the issue of automotive liberalization had been raised earlier by the United States and other countries, the July announcement intensified the debate. While the automobile industry was only one of several industries about which the United States expressed concern, it rapidly became the most politicized and symbolic because of strong lobbying by the U.S. auto industry, especially Ford and Chrysler.

Informal negotiations on automobile trade took place on December 12 and 13, 1967 in Tokyo.⁸³ The U.S. delegation was led by Philip Trezise, U.S. Ambassador to the OECD. The Japanese delegation was led by Katsuji Kawamata, the president of Nissan and chairman of JAMA. Although he was made a temporary MITI advisor for the meeting, Mr. Kawamata was not a government official. Thus, the Japanese responses to American demands were necessarily—perhaps purposely—vague. The meeting accomplished little except to clarify the positions of the two countries. The United States made three demands: reduce tariffs and taxes (commodity, road, and various prefectural) that discriminate against large cars; liberalize imports of engines and parts; and permit foreign capital investment. The Japanese delegation took the position that taxation was a domestic, not international, issue and that tariffs had been addressed in the Kennedy Round of GATT. Tariffs on passenger cars were to be reduced from 40 percent to 36 percent on small cars and 35 percent to 28 percent on large cars in July 1968, with further reductions in 1969, 1970, 1971, and 1972. In regard to the liberalization demands, the delegation did not set specific dates but indicated the issues would be considered with a forward-looking attitude.

The issue was raised again at the Japan-U.S. Joint Economic Subcommittee meeting in Hawaii on January 23–26, 1968, but no progress was made. Soon after, MITI Vice Minister Shigenobu Yamamoto stated: “We will decide MITI’s attitude after a conclusion has been reached by the automobile industry around March concerning capital liberalization and engine liberalization.”⁸⁴ JAMA released its views in a March memorandum to MITI:

We have no objection to liberalizing engines, etc. which are included within foreign trade liberalization. We

understand that capital liberalization and trade liberalization are not the same thing. But, the time to start capital liberalization must be thought about carefully. Because it would be embarrassing for us in the future if foreign capital gained ground in Japan, monopolizing patents, we hope that the United States and Japan will discuss this and come to an agreement. In regard to tariffs, we agreed to the Kennedy Round. In regard to the commodity tax, etc., we expect the government will consider them.⁸⁵

MITI's own position was clarified by MITI Minister Etsusaburo Shiina's May 21 press statement:

The liberalization of major automobile parts such as engines cannot be dealt with separate from capital liberalization. There is fear that if we were to liberalize engines in advance this would create confusion at a time when the reorganization of the domestic industry is progressing. I think that both engine liberalization and capital liberalization should be carried out together.⁸⁶

The most noteworthy point about these statements is the omission of a timetable for liberalization. The positions of MITI and JAMA were closely aligned in favor of delaying liberalization because of the weakness of the domestic industry compared to Ford and General Motors. Executives from Nissan and Toyota were especially vehement on this point. The statements also tied together the liberalization of capital and engines. Duncan states the reason for this stance was that Japan saw engine imports as the first step toward comprehensive foreign onshore assembly operations. This position was maintained through the early summer of 1968 in Japanese government proposals to the U.S. government during June and in JAMA's position paper, the Hakone Declaration, released in July.⁸⁷ The United States separated the two issues for negotiation purposes. In the long run, the separation allowed Japan to concede on the less important issue, engine liberalization, rather than on the much more critical issue of capital liberalization.

By March 1968, MITI and the automobile industry agreed on a liberalization policy. Nissan and Toyota directed their energies toward working with the government on liberalization while maintaining a neutral position on reorganization. In fact, one study states that "during the ensuing eight months [December 1967 to August 1968] of discussions between the two countries, MITI and

the domestic producers demonstrated their most complete unity during the postwar period."⁸⁸ Toyota and Nissan continued to work with MITI until 1969 when the decision was made to liberalize engine imports. The smaller producers increasingly disassociated themselves from this policy.

During the spring, certain domestic groups voiced support for capital liberalization in the automobile industry. These groups feared the United States would penalize all Japanese exports to the United States if the automobile issue were not resolved. This period was generally a time of strong bilateral trade tension. Keidanren, the major business federation, became the strongest advocate of early liberalization of the automobile industry.⁸⁹ In February 1969, Keidanren reached an agreement with the automobile industry and MITI in which it conceded that while it was impossible to set a specific date for capital liberalization, it felt the automobile industry would be able to survive liberalization in Japan Fiscal Year 1971.

Mounting pressure from the United States and domestic groups forced two developments in August. On August 20, the Japanese government agreed to liberalize engine and parts imports by the beginning of 1970 with considerable increases in quotas occurring earlier. This concession, combined with the fact that Japan and the United States were on the verge of national elections, created a temporary lull in bilateral tensions. The timing of capital liberalization still remained undecided, and this issue ultimately revived bilateral tensions.

On August 21, 1969, MITI Vice Minister Setsuo Takashima of the Heavy Industries Bureau once again raised the reorganization issue, referring to a two-group idea in a press conference.⁹⁰ MITI had considered a plan during 1968 that sought to reorganize the passenger car industry into two groups around Toyota and Nissan. A possible third group would concentrate on bus and truck production. The August decision on engine liberalization combined with the failure of the Mitsubishi/Isuzu/Fuji tieup—and the problems developing in the Mitsubishi/Isuzu merger—accelerated MITI's interest in a two-group idea. It is unclear how committed MITI was to this plan but Takashima's public reference to it greatly disturbed the smaller passenger car producers, who immediately attacked it with varying degrees of intensity. Commenting in 1983, Shoichiro Honda stated:

MITI insisted that Japanese automobile manufacturers could not compete with the United States. Therefore, MITI said you manufacturers should merge to make two

or three larger manufacturing units. . . . I went to MITI and shouted at them "Even though you insist that we cannot compete with large U.S. auto companies, history teaches us that it is the newcomer who makes good progress. You [MITI] don't have the right to order us like that. If you want to do that you should be an owner of Honda stock. You can say that as a Honda stockholder at the Honda stockholder meeting. We follow, we are prepared to listen to stockholder's comments, but we never will be ordered by the government."⁹¹

The two-group idea, even though it was abandoned quickly by MITI after the strong industry protests, helped split the automobile industry's unanimity by creating an additional incentive for the smaller manufacturers to seek limited tieups with American automobile companies to maintain their independence. Between August 1968 and May 1969, the smaller makers had gradually backed away from supporting an indefinite delay in capital liberalization. This movement culminated in Mitsubishi's announcement in May 1969 that they would tie up with Chrysler.

The Chrysler/Mitsubishi announcement was a shock. It was viewed by MITI—as well as Toyota and Nissan—as a betrayal. Isuzu and Mazda followed Mitsubishi's lead and concluded tieups with General Motors and Ford. Honda and Suzuki chose to remain independent and draw on their strength in motorcycles to support their passenger car programs.

Mitsubishi's announcement, combined with the need to resolve other tense issues between the United States and Japan such as the Okinawa reversion and the textile negotiations, finally forced the government to establish a timetable for the automobile industry's capital liberalization. On October 14, 1969, the Japanese Cabinet decided to permit direct investments of up to 50 percent in the automobile industry as of October 1971. Capital investment in the automobile industry was liberalized completely in 1973.

Conclusion

The liberalization policies of the 1960s reflected both change and continuity in the government-business relationship. The relationship was adversarial on some issues but had strong elements of cooperation on others.

Domestic opposition was no longer a factor in the 1960s. As the automobile industry gained strength, it did not have to struggle continually for survival and recognition. The rapid increases in exports and the emergence of new producers best exemplified its newfound competitiveness. The industry unquestionably was important to the economy in terms of the government's economic development policies and the contribution made by the individual companies' corporate growth and profits. Hence, MITI was concerned about the competitiveness of the industry in relation to foreign producers and the smaller companies' determination to begin production of passenger cars.

The absence of domestic opposition affected the industry's lack of incentive to cooperate with government policy. Koichi Shimokawa and Toshimasa Tsuruta correctly stress the limitations of government policy when the industry and its market were strong.⁹² These limitations were especially evident when the government in the 1960s lost its strongest controls over the industry because of the limitations imposed by the multilateral arrangements. In addition, the tools the government still possessed consisted of incentives that increasingly were less attractive. Small-scale JDB loans were not very enticing when capital needs were large and capital easily obtainable.

This view is useful in understanding the failure of MITI's industrial policies and of the various reorganization attempts. It is also the primary reason that relations between the automobile industry and the government during the 1960s are characterized by a majority of scholars as one of the foremost examples of antagonistic government-business relations. This reasoning is behind John Campbell's emphasis on the failure of the reorganization program and Koichi Shimokawa's emphasis on the refusal of smaller companies such as Honda to accept government policies.⁹³ While this characterization of interactions as adversarial is true, it remains incomplete even in the context of the reorganization programs. These programs produced many types of reactions among the producers, depending on their size and on the specific reorganization program. More importantly, this characterization considers only one part of liberalization policy; the other part was closely related to threats posed by imports and foreign capital.

The policies to liberalize imports and foreign capital investment were still potential threats to the industry's development. Foreign capital investment was the most substantive threat in the latter half of the 1960s since passenger car imports had ceased to be a problem by the time of their liberalization in 1965. European

small-car imports had been delayed until Japanese products were competitive. The American companies produced the wrong type of product and were primarily interested in capital investment.

Fear of foreign capital was a factor in the reorganization programs and, obviously, in the delay of capital liberalization. The automobile industry initially had strong incentives to cooperate with the government on this issue. The automobile companies did tend to support the conceptual reasoning of the possible impact of excessive competition behind the reorganization programs. However, the strength of the domestic market and the refusal of the smaller companies to bow out of the market overwhelmed the government's ability to extend agreement on the concept to agreement on a specific policy to solve the problem and on which company would be eliminated.

Cooperation prevailed on capital liberalization policies until the public announcement of the two-group idea and Mitsubishi's decision to tie up with Chrysler. It is important to note that this cooperation was able to last as long as it did given the strong pressure to liberalize from powerful domestic organizations, such as Keidanren, and from foreign countries, especially the United States.

It is possible to be critical of MITI for delaying capital liberalization longer than the competitive strength of the automobile industry indicated. In hindsight, the industry was more competitive than imagined. In addition, the delay reveals the government and automobile industry's congruence of interest, and that their interactions were based on a partnership designed to provide minimal survival security.

NOTES

¹Richard N. Gardner, *Sterling-Dollar Diplomacy in Current Perspective* (New York: Columbia University Press, 1980), p. 9.

²For a detailed description of the evolution of GATT, see John H. Jackson, *World Trade and the Law of GATT* (Indianapolis: The Bobbs-Merrill Company, 1969).

³General Agreement on Tariffs and Trade, *Basic Instruments and Selected Documents, Volume 1* (Geneva: The Contracting Parties to the General Agreement on Tariffs and Trade, 1955), p. 7.

⁴Details of the following section on GATT are primarily taken from James E. Landes, "Japan and the Contracting Parties to the

General Agreement on Tariffs and Trade: A Case Study in Postwar Commercial Policy" (Ph.D. diss., University of Colorado, 1965).

⁵G.C. Allen, *How Japan Competes: A Verdict on Dumping* (London: Institute of International Economics, 1978), p. 23.

⁶Jackson, *World Trade*, p. 404.

⁷*Ibid.*, p. 404 and pp. 810–11. Service dumping referred to "the use of subsidies or other discriminatory pricing to enable an exporter, through minimal freight rates, to be able to offer his product in foreign markets at a very low price," and exchange dumping referred to "the manipulation of exchange rates to achieve competitive advantage for exports." Price dumping is defined in GATT Article VI as when the price of an exported product "is (a) less than the comparable price, in the ordinary course of trade, for the like product when destined for consumption in the exporting country, or, (b) in the absence of such domestic price, is less than either (i) the highest comparable price for the like product for export to any third country in the ordinary course of trade, or (ii) the cost of the production of the product in the country of origin plus a reasonable addition for selling cost and profit.

⁸Landes, "Japan and the Contracting Parties," p. 152.

⁹Warren S. Hunsberger, *Japan and the United States in World Trade* (New York: Harper and Row, 1964), p. 234.

¹⁰*Ibid.*

¹¹Clause XXXV was originally added to the GATT in March 1948 to allow India to boycott South Africa.

¹²Michael A. Cusumano, *The Japanese Automobile Industry* (Cambridge: Harvard University Press, 1985), p. 24.

¹³Alfred K. Ho, *Japan's Trade Liberalization in the 1960s* (White Plains, NY: International Arts and Sciences Press, 1973), pp. 25–26.

¹⁴Miriam Camps, "*First World*" *Relationships: The Role of the OECD*, Council Papers on International Affairs 5 (Paris: Atlantic Institute for International Affairs and New York: Council on Foreign Relations, 1975).

¹⁵Ho, *Japan's Trade Liberalization*, pp. 25–26.

¹⁶American automobile manufacturers have traditionally entered foreign markets via foreign capital investment rather than exports (except sales to Canada, which are handled as an extension of the American market). Ford Motor Company established its first overseas assembly plant (excluding Canada, which had been entered earlier) in 1911 and General Motors in 1925. There were four major reasons for this approach. First, it was much more expensive to ship finished cars than parts. By assembling in the foreign market,

the U.S. makers saved on transportation costs. It was not until the Japanese invented specialized ships to carry cars after World War II that transportation costs were lowered sufficiently to be competitive with foreign assembly. Second, Europe (the primary overseas market for the United States) was a labyrinth of protective tariffs before World War II. For example, England in 1915 under the McKenna duties enacted a 33.3 percent tariff on motor vehicles and their parts. American companies, in order to surmount the tariff wall, established foreign assembly plants. After World War II, Ford and General Motors were already tied to foreign assembly, and Chrysler soon followed by buying the existing European firms Simca and Rootes. Local content requirements in many nations as well as the formation of the European Economic Community also encouraged the establishment of local assembly plants. Similarly, all the major Japanese manufacturers in the 1980s established passenger car assembly plants in the United States, spurred by fears of U.S. protectionism. Third, American cars have been differentiated by size from those in most other major markets because of lower gasoline prices and geography. The product built at home for American customers was not the same one overseas customers wanted to buy, so exports of large cars had limited appeal. It was simpler to build a different product overseas for foreign customers. And fourth, because foreign currencies were cheap relative to the dollar after World War II, U.S. companies could build foreign assembly plants economically under the Bretton Woods system. Therefore, it remained wise to assemble overseas rather than export.

¹⁷Hunsberger, *Japan and the United States*, pp. 135-36. (1) Imports were to be liberalized as quickly as possible for certain raw materials and finished products that raised no serious problems, notably mineral ores, pig iron, cotton and silk manufactures, optical goods, and textile machinery. (2) Imports of commodities that Japan could sell on a competitive basis abroad or that did not compete in the domestic market were to be liberalized within three years. Among these commodities were synthetic fibers, wool manufactures, plate glass, special steels, and some machinery. (3) Commodities that would not be removed from the quota list for more than three years included products of industries in which technical development is being fostered, for example, machine tools, automobiles, heavy electrical equipment, some fertilizers, metals, and forestry products. (4) The fourth group consisted of items whose "liberalization appears to be difficult for a

fairly long period of time," including rice and wheat, dairy products, vegetable oils, and most fruits.

¹⁸Ibid.

¹⁹Ibid., pp. 133-34.

²⁰Ibid., p. 136.

²¹Takafusa Nakamura, *The Postwar Japanese Economy*, trans. Jacqueline Kaminski (Tokyo: University of Tokyo Press, 1981), p. 81.

²²Cusumano, *The Japanese Automobile Industry*, p. 22.

²³Martin Brofenbrenner, "Excessive Competition," *Monumenta Nipponica* 21.1-2 (1966): 114-24.

²⁴Ibid., pp. 118-19.

²⁵Yasusuke Murakami and Kozo Yamamura, "A Technical Note on Japanese Firm Behavior and Economic Policy," in *Policy and Trade Issues of the Japanese Economy*, ed. Kozo Yamamura (Seattle: University of Washington Press, 1982), pp. 113-22.

²⁶William C. Duncan, *U.S.-Japan Automobile Diplomacy* (Cambridge, MA: Ballinger Publishing Company, 1973), p. 83.

²⁷Chalmers Johnson, *MITI and the Japanese Miracle* (Stanford: Stanford University Press, 1982), pp. 255-56.

²⁸Japan Automobile Manufacturers Association, *The Motor Industry of Japan* (Tokyo: Japan Automobile Manufacturers Association, 1967, 1980).

²⁹Ibid.

³⁰"Hino-Runo oboegaki kokan" [Hino and Renault exchange memorandum], *Nihon Keizai Shimbun*, 17 May 1960 and "Hino-Runo teikei kyoka" [Hino and Renault strengthen technology agreement], *Nihon Keizai Shimbun*, 28 December 1961.

³¹"Isuzu-Rotsu teikei encho" [Extension of Isuzu/Rootes tieup], *Nihon Keizai Shimbun*, 10 October 1961.

³²For further details on the Chrysler takeover of Rootes see Stephen Young and Neil Hood, *Chrysler U.K.: A Corporation in Transition* (New York: Praeger Publishers, 1977), pp. 77-85.

³³"Gijitsu kyotei, musho de encho, Isuzu jidosha to Rutsu" [Technology tieup, extension without cost, Isuzu and Rootes], *Asahi Shimbun*, 6 October 1961.

³⁴U.S. Department of Commerce, *Japan, The Government-Business Relationship*, ed. Eugene J. Kaplan (Washington: Government Printing Office, February 1972), p. 122 and "Hanbai kinyu gaisha o setsuritsu—jidosha no jiyuka taisaku" [Establishment of sales finance company—impending automobile liberalization], *Nihon Keizai Shimbun*, 5 August 1961.

³⁵Duncan, *U.S.-Japan Automobile Diplomacy*, p. 84.

³⁶“Hanbai kinyu gaisha o setsuritsu—jidosha no jiyuka taisaku,” *Nihon Keizai Shimbun*, 5 August 1961.

³⁷“Shinki seisan ni kyokasei” [Licensing new production], *Nihon Keizai Shimbun*, 12 January 1962 and “Shashu betsu ni seisan chosa ‘Joyosha Kogyo Shinko Ho’ kento” [Production control depending on model—consideration of the “Passenger Car Industry Promotion Law”], *Nihon Keizai Shimbun*, 24 June 1962.

³⁸Duncan, *U.S.-Japan Automobile Diplomacy*, p. 84 and Honda Motor Corporation, “Toku shin ho” [Special measures law] (Handwritten, Tokyo, n.d.), p. 4.

³⁹Japan, Industrial Structure Investigation Conference, Committee on Heavy Industries, Passenger Car Subcommittee, *Hokoku an shingi shiryō* [Investigative report materials] (Tokyo: Ministry of International Trade and Industry, 1962). Additional reports were published on 7 June 1963 and 17 September 1963.

⁴⁰Honda Motor Corporation, “Toku shin ho,” p. 4.

⁴¹“39 nendosei made ni jiyuka” [Liberalization as 1964 approaches], *Nihon Keizai Shimbun*, 19 December 1962. The company representatives included: Katsuji Kawamata (President, Nissan), Naomichi Kusunoki (President, Isuzu), Shigeru Komatsu (President, Prince), Fukio Nakagawa (President, Toyota), Torao Hayashi (President, Auto Parts Industry Association), Fukazo Fujii (President, Shin-Mitsubishi), Masanobu Matsukata (President, Hino), Kouji Matsuda (President, Mazda), and Takao Yoshida (President, Fuji Heavy Industries). The expert members from outside the industry included: Hiromi Arisawa (Hosei University), Jiro Enjoji (*Nihon Keizai Shimbun*), Kiyoshi Tsuchiya (*Asahi Shimbun*), Sohei Nakayama (President, Japan Industrial Bank), Iwane Hamaguchi (President, Long-Term Credit Bank), Keiichiro Hirata (Vice President, JDB), and Hisaji Tokunaga (Fuji Steel).

⁴²Nikkan Jidosha Kaigisho, *Jidosha nendan* [Automobile year-book] (Tokyo: Nikkan Jidosha Shimbun Sha, 1962), p. 12.

⁴³Ibid.

⁴⁴Honda Motor Corporation, “Toku shin ho,” p. 10.

⁴⁵Ibid.

⁴⁶U.S. Department of Commerce, *Japan, The Government-Business Relationship*, p. 122 and Honda Motor Corporation, “Toku shin ho,” p. 5.

⁴⁷“Yonrin bumon ni warikomu, ni-sanrinsha maka” [Two- and three-wheeled vehicle makers break into four-wheeled field], *Asahi Shimbun*, 24 January 1962.

⁴⁸Honda Motor Corporation, “Toku shin ho,” p. 6.

⁴⁹Michio Nishida, *Katari tsugu keiei: Honda totomo ni 30 nen* [Management passed on: thirty years at Honda] (Tokyo: Kodansha, 1983), pp. 96-98.

⁵⁰Honda Motor Corporation, "Toku shin ho," p. 1.

⁵¹Nihon Hoso Kyosai (NHK), "Shogen, gendaishi" [Testimony, present day history] (Videotape, October 1983).

⁵²Duncan, *U.S.-Japan Automobile Diplomacy*, p. 87.

⁵³Nakamura, *The Postwar Japanese Economy*, pp. 81-82.

⁵⁴Johnson, *MITI and the Japanese Miracle*, pp. 255-60.

⁵⁵This discussion of the debate on the draft law is taken primarily from Johnson, *MITI and the Japanese Miracle* and Honda Motor Corporation, "Toku shin ho."

⁵⁶*Ibid.*

⁵⁷Honda Motor Corporation, "Toku shin ho," p. 9.

⁵⁸*Ibid.*

⁵⁹U.S. Department of Commerce, *Japan, The Government-Business Relationship*, p. 123.

⁶⁰Koichi Shimokawa, "Sengo Nihon jidosha sangyo keisei shi nisuite [Management history of the postwar Japanese automobile industry]," *Business Report* 31.2 (1983): 57-58.

⁶¹Diamond Company, *Nissan jidosha shacho, Kawamata Katsuji* [The president of Nissan Motor Company, Katsuji Kawamata] (Tokyo: Diamond Company, 1966), pp. 62-64.

⁶²Nikkan Jidosha Kaigisho, *Jidosha nendan* [Automobile year-book] (Tokyo: Nikkan Jidosha Shimbun Sha, 1966), p. 3.

⁶³U.S. Department of Commerce, *Japan, The Government-Business Relationship*, p. 130.

⁶⁴Nikkan Jidosha Kaigisho, *Jidosha nendan* [Automobile year-book] (Tokyo: Nikkan Jidosha Shimbun Sha, 1965), p. 40.

⁶⁵Booton Herndon, *Ford: An Unconventional Biography of the Men and Their Times* (New York: Weybright and Talley, 1969), p. 242.

⁶⁶Leon Hollerman, *Japan's Dependence on World Economy* (Princeton: Princeton University Press, 1967), p. 155.

⁶⁷Japan Development Bank, *The 25 Year History of Japan Development Bank* (Tokyo: Toyo Keizai Shimbun Kai, 1976), pp. 463-64.

⁶⁸U.S. Department of Commerce, *Japan, The Government-Business Relationship*, pp. 124-26.

⁶⁹Nikkan Jidosha Kaigisho, *Jidosha nendan* [Automobile year-book] (Tokyo: Nikkan Jidosha Shimbun Sha, 1967), p. 6.

⁷⁰*Ibid.*

⁷¹Gardner Ackley and Hiromitsu Ishi, "Fiscal, Monetary, and Related Policies," in *Asia's New Giant*, ed. Hugh Patrick and Henry Rosovsky (Washington: The Brookings Institution, 1976), pp. 236-37.

⁷²U.S. Department of Commerce, *Japan, The Government-Business Relationship*, pp. 124-26 and Nikkan Jidosha Kaigisho, *Jidosha nendan* [Automobile yearbook] (Tokyo: Nikkan Jidosha Shimbun Sha, 1966), pp. 4-5.

⁷³Nikkan Jidosha Kaigisho, *Jidosha nendan* (1966), p. 5.

⁷⁴Nikkan Jidosha Kaigisho, *Jidosha nendan* (1967), p. 12.

⁷⁵Duncan, *U.S.-Japan Automobile Diplomacy*, p. 87.

⁷⁶Nikkan Jidosha Kaigisho, *Jidosha nendan* (1966), p. 5.

⁷⁷U.S. Department of Commerce, *Japan, The Government-Business Relationship*, p. 126.

⁷⁸Detailed descriptions of the Mitsubishi/Isuzu/Fuji tieups can be found in Duncan, *U.S.-Japan Automobile Diplomacy*, pp. 88-95 and Nihon Keizai Shimbun Sha, *Kokusansha wa doko e yuku* [Where are domestic motor vehicles going?] (Tokyo: Nihon Keizai Shimbun Sha, 1969), pp. 1-45.

⁷⁹Nihon Keizai Shimbun Sha, *Kokusansha wa doko e yuku*, pp. 10-11.

⁸⁰U.S. Department of Commerce, *Japan, The Government-Business Relationship*, p. 127.

⁸¹Hideko Magara, "Changing Relationship Between the State and Business Associations: Is the Japanese Automobile Industry Corporatist?" (Master's thesis, University of Chicago, 1984), p. 22.

⁸²Duncan, *U.S.-Japan Automobile Diplomacy*, pp. 3-42. Duncan provides details of the development of the informal automobile negotiations between the United States and Japan.

⁸³*Ibid.*, pp. 4-5.

⁸⁴Quoted in Duncan, *U.S.-Japan Automobile Diplomacy*, p. 6.

⁸⁵Katsuji Kawamata, *Waga kaiso* [My reminiscences] (Tokyo: Nikkei Kigyo Shuppan, 1983), pp. 133-34.

⁸⁶Quoted in Duncan, *U.S.-Japan Automobile Diplomacy*, p. 18.

⁸⁷*Ibid.*, p. 27. The Hakone Declaration had three main points:

1. Concerning the engine liberalization problem we support the attitude of the Japanese government in gradually expanding the amount of engine imports.
2. Concerning capital liberalization, because there exists various internal problems within the industry, we oppose deciding a date at this time;

hereafter the government should keep an eye on the course by which these problems are resolved and skillfully confront them.

3. Keeping in mind the fact that the government has heretofore fostered the automobile industry as an essential industry, the industry will in the future endeavor to develop on a national basis.

⁸⁸U.S. Department of Commerce, *Japan, The Government-Business Relationship*, p. 130.

⁸⁹Keidanren, *Keidanren sanjunenshi* [Thirty-year history of Keidanren] (Tokyo: Keidanren, 1978), pp. 564-66. Keidanren had strong ties to basic industries, especially steel, which stood to lose heavily if the United States enacted strongly protectionist legislation. The automobile industry, on the other hand, was relatively new and so still outside Keidanren's power structure. In later years, Keidanren expanded its ties with the automobile industry, with Nissan an especially strong supporter of Keidanren.

⁹⁰Duncan, *U.S.-Japan Automobile Diplomacy*, pp. 90-95.

⁹¹Nihon Hoso Kyokai (NHK), "Shogen, gendaishi."

⁹²Toshimasa Tsuruta, *Sengo Nihon no sangyo seisaku* [Japan's postwar industrial policy] (Tokyo: Nihon Keizai Shimbun Sha, 1982), pp. 168-74 and Shimokawa, "Sengo Nihon jidosha sangyo keiei nisuite," pp. 54-58.

⁹³John Campbell, "The Automobile Industry and Public Policy," Joint U.S.-Japan Automotive Study Working Papers Series 16 (Ann Arbor: Center for Japanese Studies, The University of Michigan, August 1983), pp. 8-9 and Shimokawa, "Sengo Nihon jidosha sangyo keiei nisuite," pp. 53-66.

CHAPTER 7

COMPETITIVENESS ACHIEVED

A new era began for Japan's automobile industry in the first half of the 1970s. The changes of the 1960s combined to create another stage in the relationship between the government and the industry. The industry was now globally competitive. It had survived the competitiveness test by exporting; the home market was secure.

The international environment continued to be important, but not as a source of vulnerability. Rather, Japan's competitiveness was a challenge to other countries. Interactions therefore concentrated on regulatory issues and trade problems that led to a relationship that was more adversarial and distant.

The Final Transition

Foreign Capital Tieups

The new stage began on May 12, 1971 when Chrysler and Mitsubishi signed their tieup agreement, which symbolized the auto industry's maturity and independence. The agreement revealed that the international challenges to the industry's survival had evaporated.

While the government-business relationship during the capital liberalization negotiations had great unanimity because of the perceived danger in the renewed interest of the American automobile companies in Japan, the unanimity disappeared in the 1970s when the smaller producers realized that foreign capital tieups, rather than threatening their independence, presented an opportunity to preserve it.

The tieups gave the smaller makers access to the growing American market for imports. Nissan and Toyota already had established sales networks in the United States and had begun to

replace European companies as the dominant imports. Most of the smaller Japanese makers, however, did not have the financial resources to establish extensive sales networks in the United States.

The sequence of events leading up to the Mitsubishi/Chrysler tieup demonstrates the transition in the government-business relationship.¹ This tieup proved to be more important than the later General Motors/Isuzu and Ford/Mazda tieups because it directly challenged MITI's wishes and established precedents for the others.

Chrysler took the first step toward the tieup on June 8, 1968 when Vice President A.N. Cole, together with other Chrysler executives, arrived in Tokyo.² The visit's purpose was to find a Japanese automobile company that could supply Chrysler with a small passenger car. Ford and General Motors were investigating the Japanese market at this time, but Chrysler was the most aggressive because of the three it was the only company that did not have a small car ready for production. General Motors and Ford had the Vega and Pinto, respectively. During his visit, Mr. Cole conducted interviews with a wide range of people involved in the automobile industry: Mr. Shozo Hotta of Sumitomo Bank, Mr. Katsuji Kawamata of Nissan, Mr. Eikichi Ohashi of Isuzu, Mr. Kohei Matsuda of Mazda, and Mr. Yaichiro Makita of Mitsubishi. He was especially interested in the three smaller companies that were not tied to either Toyota or Nissan: Mazda, Isuzu, and Mitsubishi.

Mazda and Isuzu turned down the overtures because they feared that even if Chrysler began as a minority shareholder it would eventually attempt to take full control, as happened in Chrysler's acquisition of Rootes in England and Simca in France.

Mitsubishi decided to conduct preliminary negotiations with Chrysler. Mitsubishi initially did not seriously consider Chrysler's offer because it was attempting to become the third major Japanese automobile manufacturer through tieups with other domestic firms.³ It was not until after the proposed tieups with Isuzu and Fuji failed and MITI announced its two-group idea that Mitsubishi's interest in Chrysler's proposal heightened. Unlike Mazda and Honda, Mitsubishi was not afraid of being absorbed by Chrysler because, as part of Mitsubishi Heavy Industries, it had access to tremendous resources. And unlike Ford and General Motors, Chrysler was willing to accept minority ownership.

The negotiations accelerated after January 1969 and then climaxed in May when Mitsubishi Vice President Yaichiro Makita arrived secretly in Detroit for discussions with Chrysler's top executives, including Mr. V.E. Boyd and Mr. Lynn Townsend as well as Mr. A.N. Cole.⁴ Mitsubishi suggested an investment ratio of 70

percent/30 percent in its favor. Chrysler wanted 40 percent. The difference between the two figures was split, giving Mitsubishi 65 percent and Chrysler 35 percent.

Mr. Makita returned to Japan on May 18 and announced the agreement. In addition to the investment ratio, Mr. Makita announced the following points⁵:

1. Mitsubishi and Chrysler would conduct joint research and development.
2. Mitsubishi would separate from Mitsubishi Heavy Industries and Chrysler would invest in the new company, Mitsubishi Motor Corporation.
3. Initial cooperation would be in sales. Chrysler cars would be sold through Mitsubishi and the Mitsubishi Gallant (Dodge Colt) would be sold by Chrysler.
4. Local assembly of Chrysler cars in Japan might be considered in the future.
5. A trading company would be established to import Chrysler engines for use by Mitsubishi.

MITI was stunned by the announcement, although there had been rumors earlier in the year that negotiations were being conducted. Mr. Makita's American trip had been undertaken and the announcement made without prior consultation with MITI. The announcement, combined with the ongoing foreign capital negotiations, forced the government to finally announce a date for capital liberalization—October 1971. It had no choice but to approve the final tieup agreement.

MITI made a final attempt to establish limits for foreign investment in the automobile industry. This move was extremely crucial because the Mitsubishi agreement set precedents not only for the automobile industry but, because it was one of the first such agreements, for foreign capital investment in general.⁶ MITI suggested that it would only approve foreign investment when the share was less than 35 percent to ensure domestic control. Under the Japanese commercial code at that time, anyone with more than 25 percent of outstanding stock had the right to vote in the selection of directors, but anyone with more than one-third had the right of veto. Thus, if Chrysler obtained at least 35 percent in the tieup with Mitsubishi, it would have greater influence in decisions about the management of the company. Thirty-five percent was finally accepted by MITI after negotiations with Mitsubishi since it still constituted a minority share.

MITI suggested stockholder safety measures, which attempted to consolidate and stabilize the domestic share owners by encouraging banks and other major institutions to become permanent shareholders by buying out potentially weaker shareholders. Some controversy arose over what institutions constituted proper permanent shareholders—institutions that could be counted on not to sell their stock even if it declined in value. For example, at first MITI wanted to eliminate life insurance and casualty insurance companies as permanent stockholders, but later allowed their inclusion. Although the automobile companies did not have to abide by MITI's proposals, they also favored limiting the percentage of foreign ownership in order to maintain their independence, which was the motivating factor behind the tieups.

Between May 1969 and October 1971, Mitsubishi and Chrysler completed the details of their formal agreement. Chrysler would pay \$100 million over three years to Mitsubishi, acquiring a 15 percent share in the first year, 25 percent in the second year, and 35 percent in the third year. Chrysler, however, announced in June 1972 that it was indefinitely postponing any investment over the 15 percent acquired in 1971 due to its own overall financial difficulties.⁷

Isuzu followed Mitsubishi's lead and decided to negotiate a tieup with General Motors.⁸ General Motors asked a Japanese trading company, C. Itoh (with whom GM had earlier dealt), in September 1968 to help locate an affiliate in Japan to produce trucks and buses. At the same time, General Motors approached Mitsubishi through Mitsubishi Shojii and later in January 1969 initiated a survey of Mazda. Neither Mitsubishi nor Mazda was interested. In March 1970, C. Itoh suggested that it might be possible to arrange a deal with Isuzu and negotiations began in August. C. Itoh was evidently instrumental in persuading General Motors to abandon its initial attempt to obtain 100 percent ownership. Isuzu, unhappy in its 1968 preliminary tieup with Nissan and especially upset about rumors that Nissan wanted it to merge with Nissan Diesel, agreed to negotiate the tieup with General Motors. This agreement, signed in July 1971, gave General Motors a 34.2 percent share of Isuzu. The companies agreed to collaborate in safety and air pollution technology, and Isuzu would produce trucks for General Motors. Because the share was less than 35 percent, the government accepted the tieup.

Negotiations began between Mazda and Ford.⁹ These talks proceeded slowly, partly because Mazda was involved in a patent controversy over its rotary engine with the Dutch automotive

company, NSU. Mazda also wanted to try to establish a sales network in the United States on its own. Later, management problems revealed by the 1973 oil crisis caused further delays in the negotiations with Ford. Ford did negotiate various sales agreements with Mazda in the 1970s and then acquired 24.7 percent of Mazda in 1979 for \$55 million in cash and \$80 million in property located in Yokohama, which Ford had acquired prior to the war.¹⁰

The tieups are depicted as results of the failure of MITI's reorganization program. Ira Magaziner and Thomas Hout state that by the end of the 1960s it was clear that MITI's reorganization program had failed and that the effect of this failure was the accelerated flow of foreign capital into the industry.¹¹ The failure of the reorganization program did create an opportunity for foreign capital in the Japanese automobile market. But, importantly, the smaller producers were able to retain their independence by using the tieups to become more competitive while limiting foreign capital to a minority position.

The smaller firms' ability to retain majority ownership was a surprise to many Japanese. Katsuji Kawamata stated: "It was unexpected that American capital affected the Japanese automobile industry less than we had anticipated."¹² He was especially surprised that the Americans did not build assembly plants in Japan.

Because the Japanese companies were competitive enough to retain control and the government supported the minority ownership policy, it was possible to impose limits on foreign ownership. And, because the foreign ownership share was kept low, the Japanese companies were able to retain management control. More importantly, limited foreign ownership was also a result of U.S. corporate policies that, at least in the early 1970s, saw the tieups primarily as a source of captive imports rather than as a method to move aggressively into the Japanese market.

The Mazda Bailout

Even though the smaller firms did not present a serious challenge to Nissan's and Toyota's dominance, their survival was no longer in question after the early 1970s. Therefore, their relations with the government could be distant. Mazda was the sole exception.

Mazda had built its passenger car program around the Wankel (rotary) engine, which was not as fuel-efficient as conventional

engines. After the 1973 oil crisis, Mazda found itself with a high inventory of undesirable products, poor managerial practices, and inefficient production. By late 1974, Mazda faced bankruptcy.

Unlike the Chrysler bailout in the United States, the government did not assume the primary responsibility for helping Mazda.¹³ Instead, Sumitomo Bank with the help of Sumitomo Trust Bank took the initiative and the operational responsibility for the bailout. Because it was one of Japan's strongest banks at the center of one of the major financial *keiretsu*, Sumitomo Bank was able to gain the confidence and cooperation of smaller creditors. In December 1974, it sent a group of its own staff led by Tsutomu Murai, head of Sumitomo's Tokyo office, to Mazda to revamp managerial practices and to obtain assistance and cooperation from labor, suppliers, dealers, and other related parties. Mr. Murai and his colleagues encountered some opposition and problems but managed to make progress despite the fact that Keiji Matsuda continued as president until 1978 (Matsuda's managerial style had drained the company's resources, hurt supplier relations, and stifled the development of strong managers). Upon Mr. Matsuda's resignation, Yoshiki Yamasaki, who had been chosen by Mr. Murai to streamline production, became president.

Even though Sumitomo Bank was in charge, the government expressed its concern and became involved by lowering the risk involved in the venture. As with Toyota's near bankruptcy in 1949, the government had to be supportive because of Mazda's regional economic importance. Pascale and Rohlen estimate that Mazda accounted for approximately one-quarter of all manufacturing employment in the Hiroshima area.¹⁴ In addition, the Hiroshima economy was already having difficulties because of the decline of its major industry, shipbuilding. Unlike conditions in 1949, the private financial sector in the 1970s was strong enough to help Mazda without direct financial assistance from the government.

The government thus assumed an indirect and supportive role, with the most active government agency being the Ministry of Finance (MOF). Besides informal consultations and discussions, MOF implicitly guaranteed the solvency of Sumitomo Bank. Pascale and Rohlen state:

This [implicit guarantee] does not imply that the Ministry of Finance would have compensated Sumitomo directly for any losses. Rather, presumably it would have cared for the bank and restored it to health by granting it special

business favors (e.g., shifting larger portions of the government's cash account to Sumitomo).¹⁵

The implicit guarantee enabled Sumitomo to "take an energetic response" to Mazda's problems.

MITI advised competitors and large suppliers not to take advantage of Mazda's problems and publicly expressed its support for the company. Evidently, it tried to limit negative media coverage to help restore consumer confidence. Pascale and Rohlen see MITI's support as somewhat incongruous since MITI "viewed the industry as overcrowded and due for an adjustment." Thus, it should have viewed the loss of one competitor as favorable.¹⁶ However, by 1975 the justification for MITI's earlier rationalization programs had disappeared. The Japanese automobile industry was internationally competitive, and Mazda, before the oil crisis, had proven to be a successful exporter. In addition, while high officials in MOF had opposed the development of a domestic passenger car industry in 1949, they still helped Toyota because of its importance to the economic strength of the Nagoya area. In 1976, the same reasoning applied to MITI's and MOF's support for Mazda. Finally, MITI wanted to assist Sumitomo, which had just been weakened by the bankruptcy of another client and could have been seriously hurt by Mazda's failure.

The Mitsubishi/Chrysler tieup and the Mazda bailout demonstrate that the relationship between the government and the automobile industry became increasingly indirect during the 1970s because there was no need for protectionist and developmental policies. The relationship, and with it government policy, had evolved and changed as the industry reached healthy maturity and the international threat disappeared. The demise of the earlier relationship did not mean that interactions completely ended. Rather, they changed direction to deal with newly emerging issues, which included regulation to achieve social goals and the negotiation of export restraints.

Emission Control

Regulation to achieve social goals became a major focus of attention during the 1970s. While regulation existed earlier, it was not until the 1970s that it began to dominate the government-business relationship in the automobile industry. This trend represented an economy-wide modification of national goals as well

as the maturity of the automobile industry. A Japanese government report in 1976 stated:

In view of the fact that the automobile has already become indispensable to the Japanese and that motorization has been approaching its saturation point in Japan, it is necessary to implement traffic and environmental policies answering the needs of the Japanese people. In addition, the Japanese automobile industry must recognize its role in society and appropriately cope with the requirements of society such as those associated with the environment and the conservation of natural resources.¹⁷

The rising concern about the social and environmental costs of high growth gained in importance. Japan was not able to focus on these concerns until economic success and competitiveness lessened the preoccupation with achieving economic growth regardless of its social costs.

The relationship between the government and the automobile industry was part of this trend. Several regulatory issues had high visibility, including safety and fuel economy problems. The environmental problem of automobile emissions was the most volatile regulatory issue during the 1970s and therefore serves as the best example of the new regulatory relationship.¹⁸

The regulation of automobile emissions was only one aspect of a strong environmental movement in Japan. The environmental movement began in the 1960s as the public became increasingly aware of health problems caused by industrial pollution. Incidents such as the mercury poisoning Minamata disease, cadmium-induced *itai itai* disease, and the lethal Yokkaichi asthma resulting from industrial smog created a powerful citizens movement opposed to pollution. Local government officials, many of whom represented minority political parties, responded to and supported the citizens movement, as did the mass media. The automobile emissions issue arose when this movement was at its height and the health effects of photochemical smog were widely publicized. The public outcry over all types of pollution increased the legitimacy of government attempts to regulate the automobile industry and added to the industry's fear that negative publicity would adversely affect sales.

Automobile emissions did not become a major policy issue until 1970 although concern had emerged in the late 1960s. Before 1970, air pollution policy centered on controlling stationary sources such as factory smokestacks. In 1970, public interest focused on

widely reported incidents of lead poisoning and photochemical smog that many scholars traced to automobile emissions. The automobile companies' initial response was that automobile emissions were not the only cause of photochemical smog and that it was preferable to control such emissions through various secondary policies such as the establishment of bus lanes and parking regulations.¹⁹ After similar incidents in 1971, the need to solve the problem became urgent. Public outcry over other types of pollution was high, forcing the automobile emissions issue into the public arena. Both houses of the Diet formed Special Standing Committees on Industrial Pollution that served as platforms for heated discussions on pollution, including automobile emissions. The formation of these committees was unusual and demonstrated the political sensitivity of the pollution issue.

The Ministry of Transportation (MOT), which had jurisdiction over automobile emissions as well as other regulatory issues such as safety, took the first step to control emissions.²⁰ (MOT had managed to retain some power over the automobile industry out of the jurisdictional dispute with MCI in 1945-1946. Its control was limited to areas such as parking and licensing regulations.) By July 1970, MOT had drawn up emissions proposals to be implemented by 1975. The automobile manufacturers had been consulted while the proposals were being written, and by 1970 the companies had already begun research to meet them.

Japan's automobile emissions standards are often linked to the passage of the U.S. Clean Air Act in 1971, implying that Japan only enacted emissions regulations to ensure that exports would meet American standards. However, MOT's standards were proposed prior to any action in the United States and were in response to incidents of photochemical smog in Japan in 1970 and 1971. American regulations became an added incentive to strive for stronger emissions standards but were not actually responsible for the Japanese government's enactment of the regulations.

In September 1971 MOT's jurisdiction over the automobile emissions policy was transferred to the newly created Environmental Agency, although MOT retained authority for implementing regulations.²¹ The Environmental Agency, under intense political pressure, immediately requested the Automobile Subcommittee of its Central Committee—an advisory group or *shingikai*—to draw up long-term automobile emissions control standards. The subcommittee's membership consisted of three professors, two industry association members (automobile and oil), five government representatives from MOT, MITI, and the Ministry of Health and Welfare,

and a traffic specialist from the Policy Science Institute. Because the Environmental Agency drew its initial staff from competing ministries, it was feared that infighting would diminish its authority. The Environmental Agency was able, however, to act strongly on the emissions issue backed by public outcry over pollution in general and the forceful personalities involved.

The subcommittee released its interim report in August 1972 to the Central Committee, which in turn formally submitted it to the Environmental Agency on October 3. The subcommittee members had only two precedents on which to base emission allowance standards: the U.S. Clean Air Act and the earlier MOT recommendations. The subcommittee decided to accept the stricter 1971 U.S. standards in its interim report, albeit with some differences in testing methods.²² Julian Gresser explains that the subcommittee chose the U.S. standards because they believed that the U.S. government would never establish a standard for an industry of this importance without firm evidence that the industry's compliance was possible and because Japanese exporters would have to comply with U.S. emission standards.²³

The stricter standards helped satisfy the political demands of environmental activists. The draft regulations went into effect on October 5, 1972 with the final regulations scheduled to take effect a year later. The Environmental Agency asked MOT and MITI to urge the industry to comply.

Criticism surfaced at a series of Environmental Agency hearings on the 1975 emissions standards held from May 21 to June 6, 1973.²⁴ All the automobile companies stated that these standards were attainable, although Toyota and Nissan demurred somewhat saying that they would be difficult to achieve in all their models. But the Environmental Agency held to its stated position of implementing the 1975 standards. The smaller companies, particularly Mazda and Honda, were so enthusiastic that they stated they would attain these standards ahead of schedule. None of the car companies were enthusiastic about the 1976 standards and criticized the stricter 0.25 gram/kilometer standard for nitric oxide. The standards for carbon monoxide and hydrocarbons would remain the same as in 1975.

In 1974, a heated controversy began on the nitric oxide provision of the 1976 standards. The year opened with a January 9 press conference by Eiji Toyoda for the purpose of detailing four reasons for loosening the 1976 standards.²⁵ First, the technology for emissions reduction was not reliable or durable. Second, emissions reduction increased cost. Third, there was not enough time

allowed to apply the standards to all types of cars. And fourth, the new technology would cause a 10 percent increase in gasoline consumption. He further stated that even meeting the 1975 standards would be harmful for the nation and that he would ask the Japan Automobile Manufacturers Association to present a new proposal to the Environmental Agency. The manufacturers' position drew a great deal of criticism and accusations from environmental activists and opposition party politicians.

In the summer of 1974 the Diet's Special Standing Committee on Industrial Pollution held hearings on the 1976 standards.²⁶ At the same time, the Environmental Agency began closed hearings with the manufacturers. At the Diet hearings, all nine automobile manufacturers again spoke in favor of postponement. Shoichiro Toyoda said, "There is no prospect for fulfilling the technological development required for the 1976 standards."²⁷ When asked what temporary limit for nitric oxide would be acceptable, most of the companies, including Toyota and Nissan, said that they could not answer the question. Honda and Mazda suggested a figure of 0.6 to 0.7 grams per kilometer. Ikuo Kobayashi, head of the Automobile Subcommittee, stated that if the smaller makers could meet a temporary level the larger makers (Toyota and Nissan) could also. He implied that the larger makers refused to suggest a temporary standard because they wanted a complete postponement. In September, MITI supported the automobile manufacturers, stating that the standards would create unemployment and cause GNP growth to slow down.²⁸ MITI was never able to seriously challenge the authority or position of the Environmental Agency on the emissions question, however, partially because the issue had become politicized through the hearings in the Diet.

The Environmental Agency decided to ask the Central Committee in August to reconsider the 1976 standards. The Central Committee set up an "Expert Advisory Committee on Automotive Production," which began to study the standards. The Environmental Agency and the industry immediately came under attack from environmental activists, including the *ad hoc* Diet Environmental Committee and the mayors of seven major cities (Tokyo, Kawasaki, Yokohama, Nagoya, Kyoto, Osaka, and Kobe). The mayors not only held their own hearings in September but began their own study of the standards' feasibility.

The mayors' report, entitled "The Seven Cities' Investigative Report on the Automobile Emissions Regulations Issue," was released in October.²⁹ The report gave a brief history of local government actions on automobile emissions and related problems

such as noise pollution. It concluded that the 1976 standards were technologically feasible and urged local governments to take action. Although the report was criticized for technological inaccuracy by the Environmental Agency and others, it, along with the formation of the *ad hoc* Diet committee, clearly demonstrated how the issue had become politicized and helped put pressure on the manufacturers. The report resulted in an agreement "in spirit" by the expert committee on the compliance question.³⁰

The expert committee managed to retain control of the issue by keeping some company data confidential while releasing to the public a great deal of information. Concentrating on technological rather than policy considerations increased the committee's credibility.

The committee's final report in December concluded that the 1976 standards should be postponed until 1978 because they were technologically infeasible in view of the small amount of preparatory time given to the industry.³¹ Thus, the government returned to a position closer to the original MOT suggestions. The report supported tax incentives for pollution research and the enactment of stricter traffic regulations. The final report was accepted by the Environmental Agency in February 1975 after a small delay caused by opposition from environmental activists.

During 1975, additional research was conducted on the technology needed to meet the new 1978 standards. Disagreement remained on the issue of technological feasibility, but by early 1976, the debate resolved itself. Several smaller manufacturers, sensing an opportunity to finally cut into Toyota's and Nissan's market shares, announced that they would meet the 1978 standards.³² These companies included Mitsubishi, Fuji Heavy Industries, Honda, and Mazda. Within several months, this announcement forced Toyota and Nissan to agree to meet the 1978 standards.

The emissions issue illustrates two aspects of the government-business relationship. First, the regulatory relationship differed from that created by developmental policies in that it was more antagonistic and politicized. More importantly, the government had to take a stronger role to force compliance as government and industry interests diverged. The administrative tradition of resolving conflicts, while ultimately prevailing, faced a challenge from opposition Diet members and local governments. Chalmers Johnson states that nations have either a predominate regulatory or developmental policy orientation producing

two different kinds of government-business relationships. The United States is a good example of a state in which the regulatory orientation predominates, whereas Japan is a good example of a state in which the developmental orientation predominates.³³

This distinction is useful if, as in the case of the automobile industry, it is clear that as domestic and international environments change, a nation's predominate orientation can also change. In addition, its orientation can be different depending on the industry involved.

Second, although the government-business relationship in the 1970s revolved around regulatory issues, it differed from the regulatory relationship that existed in the United States. Julian Gresser states that Japanese "viewed the emission standards more as administrative targets than rigid, inflexible, legal requirements."³⁴ Because the standards were implemented administratively rather than legislatively, the Environmental Agency was able to be more flexible in coordinating the disparate interests of the industry and the environmental activists than if it had simply been an implementing agency. The Environmental Agency, although sensitive to the position of the automobile industry, was able to avoid direct challenges to its authority and to maintain a strong position because of the large number of competitors in the domestic environment. Thus, because the smaller makers saw emissions standards as an opportunity to expand their market share, the two dominant makers were forced to comply.

The Export Takeoff

Export policy had been part of the government-business relationship in the Japanese automobile industry since 1948 when MCI's Five-Year Plan targeted the Asian market for future exports. By 1949, the motor vehicle industry had formed an Export Promotion Association, headed by Kiichiro Toyoda, that received some funds from MCI to do market research.³⁵ The Korean War stimulated exports of trucks in 1950 and 1951. And, MITI's 1952 report on passenger cars alluded to the automobile industry's potential to directly contribute to machinery exports. However, the automobile industry's export capability was limited in the early 1950s to trucks and three-wheeled vehicles. It was difficult to

foresee that four-wheeled passenger cars could become a major export, let alone become Japan's largest export earner by 1976, just thirty years after the end of World War II.

The industry's export potential was clearer by 1955. Toyota and Nissan decided to explore the American market in 1955 and launched American sales companies in 1957. MITI added a motor vehicle section to its Heavy Machinery Export Council in 1955.³⁶ The justification for developmental policies was no longer primarily to save foreign exchange and fill domestic demand but to encourage the industry's export potential. Therefore, export policy during the late 1950s and 1960s concentrated on export promotion.

However, in the 1970s, export policy changed drastically from focusing on export promotion to export restraint. Government and business found it necessary to cooperate in order to cope with the international repercussions of export success—an issue that continued to dominate the relationship in the 1980s.

Until the 1970s, the relationship between the Japanese government and the automobile industry revolved around the development of a competitive industry. This focus existed throughout the post-World War II period in protectionist, reorganization, developmental, and export promotion policies. But by the 1970s, the Japanese automobile industry was competitive; the goal that dominated the relationship in the 1950s and 1960s had been achieved, and attention shifted from industry growth and protection (the Japanese automobile industry was now "protected" by its competitiveness) to how government and business would cope with the international tensions resulting from competitiveness. Ironically, at a point in time when there was little need for government and business to interact except on various social goals, a new area of interaction developed in response to demands from trading partners for export restraints.

Export Promotion

Exports initially consisted primarily of trucks, but four-wheeled passenger cars quickly became an export commodity, increasing from only one in 1954 (19 passenger cars had been exported during the Occupation but none from 1951–1953) to 4,884 in 1959. By 1965, passenger cars had surpassed trucks in total export numbers. Total exports of four-wheeled vehicles did not surpass the 100,000 level until 1964, while passenger car exports alone surpassed the same level in the next year. Similarly, when

total exports of four-wheeled vehicles surpassed the one million mark in 1970, passenger car exports followed suit one year later.

C.S. Chang states that a basic tenet of Japanese government-business relations in export promotion is a division of labor between the Japanese government and the motor vehicle industry with the government controlling import policy and the industry playing the most important role in exports.³⁷

This tenet does not imply that the government was not active or interested in exports. Rather, the government consciously promoted exports by supporting the domestic growth of industries with export potential. In the 1950s and 1960s, the government provided export incentives that were generally available to all industries. The government did not provide direct support through specific market research, nor did it help design grand strategies for export offensives. This was done at the corporate level.³⁸ The Japanese auto producers developed their marketing strategy in the United States based on Volkswagen's early success and their own failures in the late 1950s.

The government's export policy in the 1950s and 1960s concentrated on general export promotion accomplished through tax advantages and subsidized interest rates as well as trade promotion and information provided through the Japan External Trade Organization (JETRO) to the auto parts industry. None of these measures were automobile industry specific with the exception of a few JETRO programs. However, the automobile industry was not sufficiently developed to take advantage of export incentives that were available before 1964.

The establishment of the Japan Export Bank in December 1950 (the name was changed to the Export/Import Bank in 1952) was the first export incentive. The bank's purpose was to encourage or assist ordinary financial institutions in facilitating international commerce by underwriting exports, imports, and overseas investments.³⁹

Although the motor vehicle industry's (including motorcycles and parts) percentage of total Export/Import Bank loans to the manufacturing sector peaked at 28.8 percent (5.18 million yen) in 1953 because of Korean War procurement, it relied most heavily on the bank during the late 1960s, peaking in 1968 at 13.2 million yen. The number of loans then fell before increasing again in the 1980s.

One major export promotion program was the special accelerated depreciation allowance for exporting firms.⁴⁰ Prior to 1964, this program involved tax write-offs and later switched to a

five-year tax deferral scheme when Japan entered GATT. This allowance gave companies the greater cash flow they needed to expand into international markets. Up until 1971 there were two depreciation schemes available to businesses. There was a "basic" accelerated depreciation scheme and a "supplemental" accelerated scheme. The basic accelerated depreciation scheme was computed from the company's export ratio multiplied by a stipulated export percentage figure that changed every few years. The supplemental depreciation scheme was available to companies who qualified as "export contributing companies" because of their strong export performance.⁴¹ The supplemental depreciation provisions were ended in 1971; the basic depreciation scheme was abolished in April 1972.

The Export Income Deduction Provision was effective from 1953 to 1964, when it was abolished as contrary to the export subsidy provisions of GATT.⁴² This program provided for a tax deduction based on export performance. The more a company exported, the greater the tax advantage. Ira Magaziner and Thomas Hout estimate that fewer than 150,000 passenger cars were exported under this deduction. The programs did not have a significant effect because it was abolished before the industry's export drive began.

The Reserve Fund for Overseas Market Development was enacted in 1964 to replace the Export Income Deduction Provision.⁴³ The fund allowed companies to maintain a reserve for market development through a five-year tax deferral scheme available for "export contributing companies." The law was revised in November 1972 to exclude all companies capitalized at over \$3.3 million (1 billion yen), which effectively excluded the automobile industry with the exception of the smaller parts manufacturers.

JETRO was organized to provide market information and technical assistance primarily to small- and medium-sized exporting companies. The automobile manufacturers were not targeted by these programs as they had sufficient resources to undertake the same type of activities on a corporate level. JETRO did establish automotive parts promotion centers in Chicago and Bangkok in 1966.⁴⁴

A dearth of statistical data makes it impossible to determine exactly how much the automobile industry benefited from these programs during the 1950s and the 1960s. By the 1970s, the export incentive programs were abolished for all except very small firms. From available evidence, it appears that the industry did take some advantage of the programs, especially the Reserve Fund

for Overseas Market Development. Thus, the companies had extra funds for maneuvering during the critical period of overseas market development, but not during the period of accelerated export expansion in the 1970s.

Export Tension

After becoming a full member of IMF and GATT, Japan was not permitted to use many export subsidies. By the 1970s, export incentives were no longer necessary. Instead, Japan needed policies that would address repercussions resulting from the impact its growing market had on other countries' industries.

Textiles were the first major Japanese product after World War II to strain multilateral trade relations and so served as a precursor of later trade tension. The textile issue was important in the controversy over Japan's admittance to GATT. Textiles also were the first product to strain the U.S.-Japan trade relationship.⁴⁵ By 1955, Japanese textile exports were increasing and taking domestic sales away from American producers. The Japanese government responded in December 1955 with voluntary restraints, which were expanded in a five-year bilateral agreement negotiated in January 1957. U.S. imports of Japanese textiles decreased in the late 1950s. U.S. imports again increased in the 1960s, not just from Japan but from other textile exporters such as Hong Kong. Additional restraint agreements were negotiated. Textiles remained a problem and various restraint agreements continued to be imposed throughout the 1960s, eventually resulting in 1969-1971 in a major dispute and the Arrangement Regarding International Trade in Textiles (the Multifiber Arrangement) in 1974. This dispute brought for the first time economic and product-specific tensions to a level that threatened to overwhelm the bilateral relationship. Japan now appeared not as a weak, vulnerable economy but as a powerful exporter.

Bilateral tension that began with textiles and expanded to encompass many other products continued to escalate in the 1970s, exacerbated by the 1973 oil crisis and the 1974-1975 recession. It did not flare up again until 1977, when American concern about Japan's current account surplus and the U.S. current account deficit spilled over into an increasing number of product-specific conflicts. The U.S.-Japan trade conflict intensified during the Carter Administration not only because of the policies pursued but, more importantly, because the time was right.

During 1977, two highly visible product-specific conflicts developed between the United States and Japan—color televisions (settled by an orderly marketing agreement in May) and steel (settled by the announcement of the trigger price mechanism in December). The dispute over the trade imbalance, however, received the most attention. Official U.S. attention focused on how America trading partners could reduce their surpluses with the United States—surpluses caused by “unfair or overzealous trading.”⁴⁶ Because of these highly visible product-specific conflicts, Japan was depicted as the major culprit in disturbing the international economy.

The United States called upon Japan to restrain exports, to open the Japanese market to U.S. exports, and to accelerate the growth of its economy. Increasingly, the policies generated by the trade imbalance were used by Congress and industry to obtain restraints on specific products. During 1978 and 1979, the U.S.-Japan relationship extended from U.S. charges of Japanese unfair trading practices on products ranging from seafood to semiconductors to Japanese promises to liberalize their economy and correct the trade imbalance. By 1980 when the automobile crisis surfaced, a pattern had developed in the solutions of product-specific issues: Japanese investment in the United States, voluntary restraint agreements, and import relief.

Development of the Automobile Issue

The automobile export restraint issue developed in the broad context of multilateral and U.S.-Japan bilateral trade relations. The auto issue was primarily bilateral because the United States was Japan's major trading partner and major market for its car exports. Initial bilateral export tension and attempts to curb motor vehicle exports began in the 1970s.⁴⁷ Japan exported less to Europe because of various import restrictions and the similarity in product size. Other areas of the world did not have competing domestic automobile industries.

The Japanese government's first attempt to restrict motor vehicle exports to the United States occurred in October 1972 as part of a broad export control program adopted in the “third yen policy.”⁴⁸ This policy was an attempt to lower Japan's trade surplus to help prevent the collapse of the Smithsonian Agreement.

Japan's bilateral relations with the United States greatly deteriorated after 1969 due to the growing trade imbalances, the

textile dispute, and problems associated with the reversion of Okinawa. These tensions, combined with the problems in the international monetary system and the undervaluation of the yen, strained the bilateral relationship (as well as Japan's relationships with other advanced industrial nations).

Economic tension came to a head with President Richard Nixon's announcement of his "New Economic Policy" on August 15, 1971.⁴⁹ The main provisions of the policy suspended the convertibility of the dollar, imposed a 10 percent import surcharge, froze domestic wages and prices, and enacted a tax cut to stimulate the American economy. While this policy was primarily a response to multilateral monetary problems, it spilled over into the U.S.-Japan relationship. The multilateral repercussions of the program, however, were the farthest reaching and led to the Smithsonian Agreement. This agreement, signed on December 19, 1971, devalued the dollar and revalued upward the currencies of other advanced nations, including Japan.

The Smithsonian Agreement immediately began to collapse. The direct result of the collapse on the U.S.-Japan relationship was a progressive deterioration in the American trade balance with Japan. The United States, reversing its previous approach in resolving trade imbalances, pressed Japan to correct the situation.⁵⁰

Prior to the collapse of the Bretton Woods system when the United States had a surplus in its trade balance, it urged deficit countries to assume the burden of adjustment by decreasing domestic consumption and expanding exports. However, by 1972 when the United States was in deficit, it had begun—and has continued so to the present—to demand that the surplus countries, that is, Japan, assume the burden of adjustment. Part of the Japanese response to the new American demand was the third yen policy.

In December 1972, MITI announced details of the export control plan, which sought to restrict exports of twenty groups of commodities retroactively from September 1972 until August 1973.⁵¹ The commodities chosen had export values in the January to July 1972 period that had increased by more than 20 percent over the same period in 1971. Commodities already regulated, that is, textiles, were exempted. The exports were to be restricted either through "voluntary" export cartels or by invoking the compulsory Export Trade Control Order (*Yushutsu Boeki Kanri Rei*). The automotive products covered by the plan included:

1. regular passenger vehicles, excluding buses;

2. special passenger cars and trucks;
3. automotive bodies and chassis; and
4. motorcycles and motor bikes and parts.

The automobile industry was shocked by the government's plan since they had expected only another yen reevaluation, not to be "singled out" for export controls.⁵² They had not been consulted. Although the plan was never implemented, it created antagonism between the industry and the government, which continually resurfaced during export disputes in the following years. Importantly, these controls were a response to the general bilateral trade problem and not to the conflict over automobile exports.

The first oil crisis in October 1973 again brought the export restraint issue to the forefront. The growing American demand for small cars increased imports of Japanese passenger cars by 17.1 percent and trucks by 32.1 percent in 1974 over 1973 levels. Japanese products overtook those of West Germany (primarily Volkswagen) as the top imports. Indeed, imports from several countries continued to increase in the first half of 1975. In reaction, Representative John Dent of Pennsylvania and the United Automobile Workers (UAW) independently lodged formal complaints with the U.S. Treasury Department and the International Trade Commission alleging that eight countries—Belgium, Canada, France, Italy, Japan, Sweden, the United Kingdom, and West Germany—were dumping (selling their products in the U.S. market at less than fair value, i.e., at a price lower than in their home markets).⁵³

The American automobile manufacturers did not lodge complaints, preferring to take a neutral stance. Mr. William D. Eberle, president of the Motor Vehicle Manufacturers Association and former special trade representative, testified before the International Trade Commission in August 1975 that the import increase resulted from a switch in consumer preferences due to gasoline price increases associated with the oil embargo, and new safety and pollution regulations, rather than less than fair value sales.⁵⁴

On August 7, 1975, the U.S. Treasury Department preliminarily decided that there was "substantial doubt" that any less than fair value imports were the cause of injury to the U.S. industry.⁵⁵ Upon receipt of this decision, the U.S. International Trade Commission decided on September 8, 1975 that it could not determine that there was "reasonable indication that the imports

were causing injury to the U.S. industry." The U.S. Treasury Department arrived at a final determination on May 4, 1976, supported by Representative Dent and the UAW, that conditionally discontinued the investigations of dumping by all eight countries "so long as certain specialized assurances are received from . . . exporters concerning future prices to be charged on their products in the U.S." The major Japanese exporters—Toyota, Nissan, and Honda—were cleared of all charges, but Fuji, Mitsubishi, and Mazda were found to have made some sales at less than fair value. The latter three companies received conditional discontinuances after they made price assurance commitments that were monitored by the U.S. Treasury Department.

The Japanese automobile manufacturers reacted to the investigation by asserting that there were no grounds for the charges. Shotaro Kamiya of Toyota stated that he was "totally convinced" Japanese cars were not being sold at less than fair value.⁵⁶ The companies then quietly waited for the investigation to end, anticipating correctly that the final decision would be in their favor. MITI, on the other hand, reacted with more alarm, fearful that even a favorable decision might precipitate import barriers. Their anxiety increased because of various proposals in 1975 to enact local content requirements on automobiles by members of Congress and the AFL-CIO. One such proposal passed, inserting local content requirements into the Energy Conservation and Conversion Act of 1975, which was intended to prevent U.S. manufacturers from meeting energy conservation requirements through captive imports. At a GATT conference in October, MITI demanded that the United States immediately end the investigation.⁵⁷ Later, because of the potential import barriers, MITI informally came out in favor of voluntary curbs on export shipments. The industry did not agree and antagonism increased. The issue cooled as U.S. domestic car sales rebounded in the 1976 and 1977 model years, overshadowing the continued, though more modest, increase in import sales.

By late 1977 and in 1978, rumors surfaced again that Japan might curb automobile exports to the United States.⁵⁸ In March 1978, MITI asked the automobile industry to voluntarily restrain sales to the United States and in April began to require auto manufacturers to file their export shipment programs with the government.⁵⁹ The government expressed its fears that if U.S. automobile imports exceeded 20 percent of the market there would be repercussions, and it warned the automobile industry to export cautiously.

As in 1972, the government's request was part of a larger program designed by MITI to reduce Japan's trade surplus with the United States. U.S.-Japan trade tension had begun to escalate in early 1977 centering on imports of Japanese color televisions and the United States's establishment of a 200-mile fishing zone. As the year progressed, the dispute increasingly focused on U.S. demands that Japan reduce its current account surplus.

The automobile manufacturers again opposed MITI's position, calling export restraints unnecessary.⁶⁰ Importantly, the manufacturers were in a better position during 1978 and 1979 to challenge the validity of MITI's opinions because the major companies had opened their own offices in Washington, D.C. Honda opened an office in May 1978, followed by Toyota in August 1978 and Nissan in August 1979. The Japan Automobile Manufacturers Association had opened a Washington office in 1976.

The adversarial government-business relationship that developed out of increased export tension reflected the divergence of the perceived interests of government and industry, and the competitive strength of the industry. While Japan had negotiated and implemented voluntary restraint agreements since the 1930s to forestall the enactment of tougher restrictions by foreign countries, it was not until the 1970s that the concept of export restraint rather than export promotion began to dominate the relationship between the government and the auto industry.

The now mature automobile industry believed that the export market was important for corporate vitality since the domestic market was becoming saturated. This belief was especially strong among the smaller manufacturers who found it hard to compete in Japan with Nissan and Toyota's already well-established sales networks. On the other side, the government under pressure from overseas was interested in reducing international trade tension. Automobile trade, politicized in the United States because of the automobile's high visibility as a consumer product and the mystique surrounding the industry, became a major issue in the redefined Japanese government-business relationship.

The Voluntary Export Restraint Agreement

The final crisis leading to the imposition of the voluntary restraint agreement began in January 1980. In the aftermath of the second oil crisis, American consumer demand again shifted to small imported cars. Foreign imports in the United States recorded

a new high in 1980 of 2.4 million vehicles, 28.2 percent of the U.S. market. Of this number, Japanese makers sold 1.9 million vehicles for 20.8 percent of the U.S. market. At the same time, American manufacturers were experiencing their worst year since 1961, and Chrysler was on the verge of bankruptcy. Automobiles became the hottest issue in U.S.-Japan trade as well as in Japanese trade with Europe.

The year opened with a speech on January 13 by UAW President Douglas Fraser stating that Japanese automakers must build assembly plants in the United States or face import restrictions.⁶¹ He followed this speech with a trip to Japan in February during which he reiterated his warnings. The American executive branch was conspicuously quiet but supported Japanese investment in the United States.

MITI took the lead in fashioning the Japanese government's response, since it felt that government intervention either directly or through administrative guidance was necessary to avert trade friction. In early 1980, MITI asked Japan's automakers to undertake "orderly" export practices with the United States and to invest in the United States.⁶² The manufacturers agreed in principle to restrain exports but opposed foreign direct investment. Each maker, fearful that the others would try to increase their market share and aware of American disagreement on the import issue, pushed export levels in the first half of 1980 to record levels.

During early March, high-level negotiations began between members of the Carter Administration and MITI Vice Chairman Naohira Amaya, which revolved not around export restraints but around Japanese investment in the United States and imports of American automotive parts by Japan. MITI made concessions on parts imports but failed to persuade the Japanese automobile makers to invest in the United States. The sole exception was Honda, which was already planning to build an assembly plant in Marysville, Ohio. The investment issue dominated discussions into the summer, but it soon became obvious that Toyota and Nissan were not going to open plants in the United States. Even if Toyota and Nissan disagreed, it appeared that such plants would probably produce only trucks and would have no immediate effect on either American unemployment or the trade imbalance.

Bilateral tension resumed in June. The UAW and its congressional supporters, frustrated with the lack of action from either Japan or the Carter Administration, filed a 276-page petition with the International Trade Commission under Section 201 of the Trade Act of 1974 (the escape clause) seeking temporary relief from

import competition through higher tariffs and quotas.⁶³ The Carter Administration responded with a \$1 billion relief program that included some regulatory relief on emissions, loan guarantees for car dealers, and eligibility designations for certain workers and communities to receive trade adjustment assistance.

In Japan, tensions between MITI and the automobile industry intensified. MITI ordered the automobile industry to practice disciplined behavior and insinuated that they might impose export controls under the Export-Import Transactions Law.⁶⁴ In addition, they publicly censored the automobile industry for their lack of cooperation. Again, the automobile manufacturers responded negatively, continuing to stress that imports were not responsible for the American automobile industry's problems.

The U.S. import situation continued to escalate during the summer and early fall. The most significant event of the summer occurred on August 4 when Ford filed a petition with the International Trade Commission supporting the position of the UAW. The Ford petition went further than the UAW petition, calling Japanese imports a "continuing source of problems" rather than only one source of current problems. The pending American presidential election further politicized the issue.

At the beginning of September 1980, MITI Minister Rokusuke Tanaka with the support of Prime Minister Suzuki summoned the top executives of Toyota, Nissan, and Honda to a meeting. He strongly urged that they practice voluntary restraints during the final months of 1980 in order to preempt an orderly marketing agreement.⁶⁵ By this time, the automakers believed that the situation was deteriorating and agreed to cooperate. Minister Tanaka announced publicly on September 5 that automobile exports would decrease in the last quarter of 1980. Keeping in mind possible antitrust charges, the Japanese automakers announced that they were not voluntarily restricting exports but that exports would decline "simply because of market conditions in the U.S."⁶⁶

The International Trade Commission announced its final decision on November 10, when it ruled by a three-to-two vote that imports were not a substantial cause of actual or potential serious injury to the American motor vehicle industry. This decision made it legally impossible for the Carter Administration to implement an orderly marketing agreement. Nevertheless, the UAW, members of Congress, and the automobile manufacturers continued to pressure the Carter Administration and later the new Reagan Administration to seek stronger import restraints.

The Japanese manufacturers made a final bid in January 1981 to convince the incoming Reagan Administration not to impose restrictions. Nissan President Takashi Ishihara, who was also president of JAMA and thus a spokesman for the entire industry, stated:

Curbing car imports from Japan cannot be helpful to solving unemployment of American auto workers. The new U.S. cabinet should work out a broader industrial policy of promoting industries other than automaking to relieve the unemployed.⁶⁷

He also pointed out that import restraints would not help vitalize the American industry in the short, medium, or long term.

The Reagan Administration established an interagency task force on automobiles at the end of January to resolve the problem, but the task force found itself divided on the issue of import restrictions. Ironically, MITI helped to resolve the split in favor of export restraints by indicating in January, and again in February, that it would support a negotiated voluntary restraint agreement. The Japanese government was also divided over restricting automobile exports. The Foreign Ministry opposed the restrictions, but MITI's position prevailed.

March and April were devoted to completing an agreement before Prime Minister Suzuki visited Washington, D.C. in May. These negotiations occurred on a government-to-government level and within Japan as MITI had to persuade the manufacturers to accept its plan.

By March, the Japanese automobile manufacturers realized that some type of restraint was inevitable. Toyota's Vice President Shigenobu Yamamoto urged the government not to make any hasty decisions since opinion on this issue was divided in the United States. The real issue however between the government and the automakers was the size and duration of the impending limit.⁶⁸ On April 25, MITI Vice Minister Amaya met with the heads of the automobile companies. During the meeting, the companies would only agree to hold exports to the 1980 level of 1.82 million vehicles.⁶⁹ MITI considered this too high and again mentioned the possibility of statutory limitations on exports.

Japan and the United States reached a final agreement on May 1 after negotiations in Tokyo between Amaya and U.S. Trade Representative William Brock. MITI offered and Brock accepted a two-year restraint with exports limited to 1.68 million vehicles in the first year and 1.68 million vehicles plus 16.5 percent of any

growth in the U.S. market in the second year. In addition, a third year of restraints would be considered if conditions so warranted.

After the announcement, Japan's automakers expressed their strong dissatisfaction with the volume and duration established in the proposal. Takashi Ishihara stated:

The three-year restraint plan will seriously hurt the motor industry, related material and component industries and the nation's whole economy.⁷⁰

The only choice was to consent, and they voluntarily agreed to MITI's three-year restraint plan on the grounds that otherwise the government would enact statutory limits. The automakers based their decision on these grounds in order to avoid possible antitrust actions in the United States. MITI and the automakers then jointly, but with much conflict, determined the quotas of the individual companies, which were announced by MITI on June 24 and reflected the market share held by each company in 1980.⁷¹

The export restraint issue increased the level of tension in the relationship between the automobile industry and the government. An uneasy truce was not declared until 1981 when industry became convinced that the situation in the United States had progressed to the point that local content legislation was likely. Later, the majority of Japanese automobile companies decided to build assembly plants in the United States only after it became clear that the restraints and the swell of protectionist sentiment would continue.

Impact of the Restraints

The imposition of the restraints is depicted as a symbol of a new government-business relationship in Japan. Chalmers Johnson states that MITI began to reassert its control over industry after the 1973 oil crisis when it "successfully redefined its mission" and became more "internationalist."⁷² MITI, believing that a valid part of this "new" mission was to negotiate export restraints and encourage overseas investment to ease trade tension, had urged the automobile industry to agree to voluntary export restraints.

Two studies on the Japanese automobile industry appropriate Johnson's depiction of a more "internationalist" MITI. Although both studies focus on government-to-government interactions, they

extend the "internationalist" argument to government-business relations. Gilbert Winham and Ikuo Kabashima state:

However, over the years, the MITI has become much more internationalist, in the sense that it is now more willing to accommodate the interests of Japan's major trading partners instead of trying to defend the narrow and immediate interests of the industries under its jurisdiction.⁷³

A University of Michigan study edited by Robert E. Cole contains a similar description.⁷⁴ These studies indicate that a more internationalist MITI is better able to handle trade conflicts on a bilateral level than it was in the case of the textile dispute. At the same time, because MITI is less inclined to defend the automobile industry's interests, these studies suggest that interactions are more antagonistic.

The interactions that occurred between government and industry during the U.S.-Japan auto dispute also resulted from the industry's competitiveness and the fact that the problem involved an external threat. Thus, the relationship, unlike the close interactions of the 1950s when industry and government goals were synonymous and international threats to the industry's existence strong, contained powerful tensions hidden behind the cooperation and the heightened government control seen during the implementation of export restraints. These tensions reappeared each time the restraints were extended.

Conclusion

During the 1970s, the relationship between the government and the automobile industry was more adversarial and distant, yet there were moments of mutual agreement.

The final shakeout of domestic producers characterized the decade's start. The shakeout occurred as the industry became competitive and overcame three final challenges to its existence. The challenge of foreign capital was resolved when three of the remaining small producers negotiated tieup and sales agreements with American firms. The second and third challenges, the reevaluation of the yen and the 1973 oil crisis, were weathered fairly easily by all the companies except Mazda. Eventually, Mazda

also was able to overcome adversity and to survive as a viable manufacturer.

Regulatory issues, especially the inflammatory automobile emissions issue, gained prominence as Japan achieved a high level of industrial development. With the internal and external threats to the industry's survival eliminated, it was possible to redress the undesirable social and environmental implications of earlier economic policies. Costs imposed on the industry would no longer significantly affect its international viability. These regulations were opposed by the industry, which had to bear increased costs. Some of the overt antagonism was deflected by cultural predispositions toward consensus. The use of the regulations by the smaller makers as a method to increase market share and the use of administrative rather than legislative methods to design and implement regulation were also important in encouraging compliance and cooperation.

The industry's international competitiveness led to skyrocketing exports. Increased world demand for small passenger cars following the oil crisis created new and different problems that had to be resolved within the context of the government-business relationship.

The relationship was more adversarial and distant than in earlier decades because the goals of the government and the industry diverged. The industry was competitive and felt it was able to oppose those government policies it thought undesirable. The ability of Mitsubishi and Isuzu to disassociate themselves from MITI's reorganization plans and negotiate tieups with American automobile companies was evidence of their new independence, although each held majority control of its venture primarily because of MITI's policies covering foreign capital investment. Later, the companies' competitiveness was evident in the role private listening posts played in monitoring developments in Washington and in the vocal disagreements between the industry and the government on the export restraint issue. The industry no longer relied on the government's perception of the severity of international problems.

Because the automobile industry was competitive, its existence was no longer threatened by either imports or foreign capital. The government's role as a buffer was no longer required. Again, this decreased the incentive of the industry to work with the government on issues where there was a conflict of interest. It was only after the new threat of protectionist legislation overseas became serious enough to threaten the profits of the industry that the two sides were again forced by external circumstances to cooperate.

The two sides did work together at times when there were similar goals to achieve. The Ministry of Finance provided support for Sumitomo Bank and its client, Mazda. MITI supported delaying the implementation of the 1976 emission standards. And, the government and the industry accepted voluntary export restraints to retain access to the U.S. market.

NOTES

¹For further details on the Mitsubishi-Chrysler tieup, see William C. Duncan, *U.S.-Japan Automobile Diplomacy* (Cambridge, MA: Ballinger Publishing Company, 1973), pp. 43-52; U.S. Department of Commerce, *Japan, The Government-Business Relationship*, ed. Eugene J. Kaplan (Washington: Government Printing Office, February 1972), pp. 131-34; and Nihon Keizai Shimbun Sha, *Kokusansha wa doko e yuku* [Where are domestic motor vehicles going?] (Tokyo: Nihon Keizai Shimbun Sha, 1969), pp. 1-45.

²Nihon Keizai Shimbun Sha, *Kokusansha wa doko e yuku*, pp. 8-11.

³Ibid., p. 12.

⁴Ibid., pp. 6-8.

⁵Nikkan Jidosha Kaigisho, *Jidosha nendan* [Automobile year-book] (Tokyo: Nikkan Jidosha Shimbun Sha, 1972), p. 54.

⁶Ibid.

⁷Duncan, *U.S.-Japan Automobile Diplomacy*, p. 50. In June 1985, Chrysler increased its share of Mitsubishi Motor Corporation to 20 percent by buying an additional 5 percent of stock held by Mitsubishi Heavy Industries, Ltd. Chrysler since bought an additional 4 percent.

⁸This account is taken primarily from Kazuaki Kajiwara and Toshiyuki Tagaki, "GM in Japan," *Zaikai*, December 1971, p. 10 and Nikkan Jidosha Kaigisho, *Jidosha nendan* (1972).

⁹Henry Scott Stokes, "If You Can't Beat 'Em . . ." *Far Eastern Economic Review*, 7 August 1971, pp. 7-8.

¹⁰"Toyo Kogyo-Ford Venture Near?" *Journal of Commerce*, 30 December 1981, p. 1.

¹¹Ira C. Magaziner and Thomas M. Hout, *Japanese Industrial Policy* (Berkeley: University of California, 1981), p. 77.

¹²Katsuji Kawamata, *Waga kaiso* [My reminiscences] (Tokyo: Nikkei Jigyo Shuppan, 1983), pp. 130–31.

¹³The most detailed description of government involvement in the Mazda bailout can be found in Richard Pascale and Thomas P. Rohlen, “The Mazda Turnaround,” in *Journal of Japanese Studies* 9.2 (1983): 230–33. In addition, Yoshi Tsurumi comes to a similar conclusion about the indirect role of government in “The U.S. vs. Japan: Business-Government Relations in the Automobile Industry,” *Pacific Basin Quarterly*, no. 5 (Spring/Summer 1980): 10–14 as does Robert Reich in “Bailout: A Comparative Study in Law and Industrial Structure,” *Yale Journal on Regulation* 2.163 (1985): 179.

¹⁴Pascale and Rohlen, “The Mazda Turnaround,” p. 220.

¹⁵*Ibid.*, p. 231.

¹⁶*Ibid.*, p. 232.

¹⁷Japan External Trading Organization, “The Automobile Industry in Transition,” *Now in Japan*, no. 21 (May 1976): 1.

¹⁸The automobile emissions issue is also an important example of regulatory interaction in the United States. American automobile emissions standards were first established in California in 1964, while national standards were not established until the 1970 Clean Air Act Amendments. Beginning in 1962, the American companies repeatedly obtained delays and relaxations in the implementation of standards from both the Environmental Protection Agency and Congress. As a result, government and public interest groups charged that the companies were colluding to delay the implementation of standards. Industry countercharged that the regulations were technically impossible, costly, and discouraged innovation in alternative technology.

Several scholars have pointed to the difference in the implementation of emissions standards between the United States and Japan as representative of the differences in the two countries’ government-business relationships—the U.S. as adversarial, Japan as cooperative. In reality, the case study shows that the Japanese case was also adversarial but did not experience as open a conflict as in the United States because (1) the industry was divided with the smaller producers sensing an opportunity to gain market share by complying with the standards; (2) public support of the environmental movement in Japan was at a peak, placing additional pressure on the industry to comply; (3) the existing product structure stressing small cars made the regulations easier to implement; (4) the automobile industry was unable to obtain delays by lobbying the Diet; and (5) there was a great deal more interaction between the

industry and government. Only the last two conditions point to an institutional structure more conducive to cooperative rather than adversarial relations. It is impossible to say, however, whether if in the absence of the first three conditions, Japan's experience would have been closer to that of the United States. Certainly, there would have been less incentive for the industry to cooperate.

¹⁹Japan, Ministry of International Trade and Industry, Automobile Section, *Showa 60 nen no jidosha sangyo* [The automobile industry in 1985] (Tokyo: Nikkan Kogyo Shimbun Sha, 1975), p. 36.

²⁰Interview with Michio Hashimoto of the University of Tokyo, formerly of the Ministry of Transport, Tokyo, December 1984.

²¹Unless otherwise noted, information on the emissions controversy is from Julian Gresser, Koichiro Fujikura, and Akio Morishima, *Environmental Law in Japan* (Cambridge: MIT Press, 1981), pp. 268-74 and Shigeru Hongo, *Documento 0.25* [Document 0.25] (Tokyo: Seibun Sha, 1978).

²²Details on the technical differences in testing methods can be found in Gresser, Fujikura, and Morishima, *Environmental Law in Japan*, p. 475.

²³*Ibid.*, p. 269.

²⁴"Kankyochō chobun owatta Nihonban musuki ho" [The environmental agency finishes investigation of Japanese muskie law], *Asahi Shimbun*, 7 June 1973.

²⁵"Kanwa yobo o koshiki hatsugen" [Formal decision on relief request], *Nihon Keizai Shimbun*, 10 January 1974.

²⁶For example, see records of the *ad hoc* Diet Environmental Committee's hearings held on 21 August 1974 and 11 September 1974.

²⁷"Zantei tekina kisoku wa kano" [Temporary regulations approved], *Asahi Shimbun*, 8 June 1974.

²⁸"Tsusansho ga gyokai yogo" [MITI on business's request], *Asahi Shimbun*, 11 September 1974.

²⁹Seven Cities Investigative Group, *7 daitoshi jidosha haiki gasu kisei mondai, chosadan hokokusho* [The Seven Cities investigative report on the automobile emissions regulation issue] (Tokyo: Seven Cities Investigative Group, October 1974).

³⁰Gresser, Fujikura, and Morishima, *Environmental Law in Japan*, p. 271.

³¹"Kuruma no haigasu chukoshin-i ga hokokusho" [Central Committee report on automobile emissions], *Asahi Shimbun*, 6 December 1974.

³²Gresser, Fujikura, and Morishima, *Environmental Law in Japan*, p. 271.

³³Chalmers Johnson, *MITI and the Japanese Miracle* (Stanford: Stanford University Press, 1982), p. 19.

³⁴Gresser, Fujikura, and Morishima, *Environmental Law in Japan*, p. 272.

³⁵Magaziner and Hout, *Japanese Industrial Policy*, p. 78.

³⁶C.S. Chang, *The Japanese Auto Industry and the U.S. Market* (New York: Praeger Publishers, 1981), p. 92.

³⁷*Ibid.*, p. 94.

³⁸For information on Japan's corporate strategies for entering the U.S. market see Chang, *The Japanese Auto Industry*; James Rader, *Penetrating the U.S. Auto Market: German and Japanese Strategies 1965-1976* (Ann Arbor: UMI Research Press, 1980); and John B. Rae, *Nissan/Datsun: A History of Nissan Motor Corporation in the U.S.A. 1960-1980* (New York: McGraw-Hill, 1982).

³⁹*The Export-Import Bank of Japan, Its Object and Functions* (Tokyo: The Export-Import Bank of Japan, 1964).

⁴⁰U.S. General Accounting Office, *United States-Japan Trade: Issues and Problems* (Washington: Government Printing Office, 1979), pp. 178-82.

⁴¹*Ibid.*, p. 180. After qualifying as export contributing companies, the firms would be placed in one of two categories, which determined whether they could increase their accelerated depreciation rate by 60 percent or 30 percent of the basic accelerated depreciation rate. The objective of these schemes was to give companies a large cash flow advantage that in turn allowed increased plant and equipment investment. Exporting contributing companies were divided into two categories based on whether they met one or two conditions: (1) export sales in the latest accounting period is to absolutely exceed by 1 percent export sales in the immediately preceding accounting period and (2) the export ratio in the previous accounting period or the increase in the export ratio is at least two-thirds of the percentage increase in the nation's total exports.

⁴²Nissan Motor Corporation, "Sengo no jidisha sangyo hogo seisaku" [Protective policies for the postwar automobile industry] (Handwritten, Tokyo, n.d.). A company could deduct from 1 to 3 percent of its export income or up to 80 percent of their net operating income derived from exports.

⁴³U.S. General Accounting Office, *United States-Japan Trade: Issues and Problems*, pp. 182-83.

⁴⁴Nikkan Jidosha Kaigisho, *Jidosha nenkan* [Automobile year-book] (Tokyo: Nikkan Jidosha Shimbun Sha, 1967), p. 201.

⁴⁵A comprehensive review of the textile issue can be found in I.M. Destler, Haruhiro Fukui, and Hideo Sato, *The Textile Wrangle* (Ithaca: Cornell University Press, 1979).

⁴⁶This characterization is found repeatedly in press accounts, congressional hearings, and executive branch statements, especially in 1977 and 1978.

⁴⁷The vulnerability of the American automobile industry was first apparent in 1960 when small-car imports took 10.1 percent of the market, up from only 1.7 percent in 1956. The imports lost ground with the introduction of captive small-car imports and compact cars by American manufacturers, with the recovery of the economy, and by the failure of all foreign companies except Volkswagen to set up adequate marketing networks. The import share fell to only 4.9 percent in 1962, which caused the 1959 situation to be summarily dismissed as a fad and American cars to grow even larger. The import share again rose in the 1960s, reaching 10.5 percent in 1968. This second challenge was led by Volkswagen and was harder to dismiss because the importers had finally built strong marketing networks. The American companies again tried to stem the imports by using captive small-car imports and building new subcompacts—the American Motors Gremlin, the Ford Pinto, and the General Motors Vega. Again, the growth of imports was temporarily halted by marketing mistakes by Volkswagen. The American companies returned to producing larger cars since the subcompact sales eroded the much more profitable large-car sales. While small cars appealed to many buyers, the American market was still fundamentally protected from imports by product differentiation: a market bias toward large cars accentuated by low gasoline prices and an extensive road network. The oil crisis of 1973 exposed the American companies to international competition for the first time since the early 1900s by expanding the small-car domestic market, an area that foreign companies could readily penetrate.

⁴⁸Tatsuro Uchino, *Japan's Postwar Economy*, trans. Mark A. Harbison (Tokyo and New York: Kodansha International, 1983), p. 194.

⁴⁹*Ibid.*, pp. 169–98.

⁵⁰For a discussion of the policy reversal see Leon Hollerman, "Locomotive Strategy and United States Protectionism: A Japanese View," *Pacific Affairs* (Summer 1979): 193–209.

⁵¹U.S.-Japan Trade Council, "Japanese Export Control Program, Council Report No. 73" (Washington: U.S.-Japan Trade Council, 19 December 1972), pp. 1-3.

⁵²Ibid.

⁵³U.S.-Japan Trade Council, "International Trade Commission Holds Hearing on Automobile Dumping Case, Council Report No. 52" (Washington: U.S.-Japan Trade Council, 28 August 1975), pp. 1-6.

⁵⁴W.D. Eberle, "Statement Before the U.S. Trade Commission," Typewritten, 19 August 1975, pp. 1-12.

⁵⁵U.S.-Japan Trade Council, "Treasury Discontinues Automobile Dumping Cases, Council Report No. 25" (Washington: U.S.-Japan Trade Council, 14 May 1976), pp. 1-3.

⁵⁶A.E. Cullinson, "Japan to Demand that U.S. End Probe," *Journal of Commerce*, 10 September 1975.

⁵⁷Ibid.

⁵⁸"Toyota Will Curb Exports to U.S. in October-December," *Japan Economic Journal*, 25 October 1977.

⁵⁹A.E. Cullinson, "Japan Acts to Restrain Car Exports," *Journal of Commerce*, 30 March 1978.

⁶⁰Ibid.

⁶¹Japan Economic Institute of America, *Yearbook of U.S.-Japan Economic Relations in 1980* (Washington: Japan Economic Institute of America, June 1981), pp. 47-49 and *Yearbook of U.S.-Japan Economic Relations in 1981* (Washington: Japan Economic Institute of America, June 1982), pp. 38-45. Further details of the negotiations that are beyond the scope of this section are found in Gilbert R. Winham and Ikuo Kabashima, "The Politics of U.S.-Japanese Auto Trade" in *Coping with U.S.-Japanese Economic Conflicts*, ed. I.M. Destler and Hideo Sato (Lexington, MA: Lexington Books, 1982), pp. 73-119.

⁶²Keisuke Okada, "Gov't Talks With Japan Car Firms on U.S. Ventures Making No Progress," *Japan Times*, 1 March 1980.

⁶³Japan Economic Institute, *Economic Relations in 1980*, pp. 51-54.

⁶⁴Ibid., p. 53.

⁶⁵Ibid.

⁶⁶"Passenger Car Export to U.S. Will Drop in October-December Period," *Japan Economic Journal*, 23 September 1980.

⁶⁷"Curbing Japanese Cars Cannot Be Relief to U.S. Unemployment," *Japan Economic Journal*, 27 January 1981.

⁶⁸"Toyota Asks Gov't of Timely Reaction to Washington," *Japan Economic Journal*, 17 March 1981.

⁶⁹"Ishihara Seeks 1980 Level and 'Just for One Year,'" *Japan Economic Journal*, 21 April 1981.

⁷⁰"Japan, U.S. Agree on Curb of Car Export," *Japan Economic Journal*, 5 May 1981.

⁷¹David Halberstam, *The Reckoning* (New York: William Morrow and Company, 1986), p. 40.

⁷²Johnson, *MITI and the Japanese Miracle*, p. 275.

⁷³Winham and Kabashima, "U.S.-Japanese Auto Trade," pp. 111-12.

⁷⁴Robert E. Cole and Taizo Yakushiji, eds., *The American and Japanese Auto Industries in Transition* (Ann Arbor: Center for Japanese Studies, The University of Michigan, 1984), p. 72.

CHAPTER 8

CONCLUSION

The relationship between the Japanese government and the automobile industry consists of complex interactions. The relationship is like controlled chaos; it has shape and form, but inside is a labyrinth of obligations, responsibilities, and pressures. It has many players seeking their way through its corridors, sometimes walking together and sometimes alone, but always aware of the presence of others.

Interactions varied considerably depending on the situation, but at the same time there were elements of continuity. The interactions also reveal that no monolithic government or private sector controlled the relationship; rather, many actors shaped the relationship including Japanese government agencies, Japanese and foreign companies, foreign governments, multilateral organizations, and individuals. Most importantly, each of these actors precipitated interactions within the relationship that resulted in public policies. The overall effect of the interactions was to help create a dynamic situation that led to the development of a competitive automobile industry in Japan.

Understanding that government-business relationships are complex interactions and contain elements of continuity and change is not sufficient to comprehend the ramifications of these relationships in global competition. But this understanding does lead to three further questions. What are the major factors that shape the relationship by creating change and providing continuity? How did the government-business relationship contribute to the automobile industry's competitiveness? And, does this case provide any insights into the development of policies that would cope with the government-business relations issue in international trade?

The Factors

Many factors exist that affect government-business interactions. While it is impossible to delineate precisely the impact of each factor or to even uncover all of them, four factors most strongly influenced government-business relations in the Japanese automobile industry and can account for the form the interactions took. These factors are distinct but often overlapped in their effects.

Cultural and Historical Lessons

Culture and history provided continuity in the relationship. Culture helped reinforce the constant of negotiation in the government-business partnership. History provided policy makers in government and business with lessons they remembered and created common preceptions of the competitive environment that were reflected in policy.

Japanese culture, through its emphasis on harmony, promoted consensus building. Consensus building in turn reinforced a policy-making pattern based on negotiation, negotiation being the recognition of the interdependence between government and business that resulted in formal and informal bargaining and accommodation. Thus, while there was much disagreement, conflict did not result in polarized positions and rarely in open confrontation. Each side accepted the other's right to a role in policy formation even if it was not enamored of the other's position. Ultimately, compromises were worked out that helped grant a certain legitimacy to public policies. Several scholars, including Richard Samuels and Ellis Krauss, also see a pattern of negotiated policies in Japan.¹ The effect of this pattern was directly apparent in relations between the Japanese government and the automobile industry in the development of emissions policies and the role of advisory commissions (*shingikai*), and indirectly evident in the acceptance of the right of all parties to have a role in policy formation.

In contrast, cultural tendencies toward vertical relationships heightened adversarial relations when MITI attempted to create horizontal mergers in the 1960s. The industry rebelled even though the businessmen who were members of the relevant advisory committee agreed in principle with the government's concern over excessive competition. They rebelled partially because horizontal mergers went against the cultural tendency toward vertical value

order and because no company wanted to be the one shut out of the market.²

Policy implementation through administrative rather than legislative means reveals another indirect effect of culture. Culture reinforced the tendency to avoid the direct confrontations more common with legislative methods of policy implementation, especially with regulatory policies. Thus, while culture did not create administrative guidance, it reinforced the industry's responsiveness to the Japanese government's frequent use of it.

History, through the lessons it taught, also provided continuity in the relationship. Japanese government and business policy makers remembered their lessons about the possible negative impact of foreign capital and unrestrained imports on an uncompetitive infant domestic industry. These lessons grew out of experiences common to all of Japanese industry during the Meiji era, and those specific to the automobile industry in the 1930s.

Because government and business learned the same lessons, they sought, and cooperated in creating, policies that lessened the vulnerability of the industry through protective measures or technological innovation. These experiences led to a widespread awareness of the international environment's role in creating and in undermining competitiveness. Michael Cusumano points out that the international environment also affected Japanese industry and government through the use of foreign technology and industrial practices in their development plans.³ Everyone knew General Motors, Ford, and other foreign companies were not only competitors but also models to emulate.

History also taught that Japanese exports might be discriminated against and denied access to foreign markets. Discussions over Japan's membership in multilateral organizations reinforced this lesson in the 1950s. It helped shape protectionist and developmental policies during the internationalization period and created a sense among policy makers during the export crisis, especially in the Ministry of Foreign Affairs and eventually in MITI, that Japan would have to compromise to preserve its overall market access.⁴

While culture and history provided continuity in the relationship, other factors, especially administrative rules and competitiveness, often overrode them to create change.

Administrative Rules

The administrative rules under which the government operated affected the relationship—rules being the perimeters agreed to by consensus or imposed by force within which the government made and carried out policy.⁵ The rules arose from the domestic environment (e.g., military or civilian government) and from the international environment (e.g., the Occupation authorities and multilateral trade agreements). The rules changed throughout the history of the Japanese automobile industry. Changes in the rules affected the amount of leeway industry had to influence public policy and the amount of control government had to enforce its ideas.

Effects of changes in the rules on interactions are most apparent when comparing the wartime and postwar periods. From approximately the time of the Manchurian Incident in 1931 to 1945, the relationship was characterized by the subordination of industry to military needs. Subordination did not mean that interaction and negotiation did not occur; Toyota's and Nissan's discussions with the Ministry of Commerce and Industry about the Automobile Manufacturing Law and the formation of the Survey Committee for the Establishment of the Automobile Industry are evidence to the contrary. However, subordination did place strong constraints on business by specifying what type of cars could be produced, what companies would produce them, and who would get raw materials. Nissan and Toyota used this period to gain entrance into the Japanese automobile market, but they had to develop production plans within the boundaries set by what the government felt was important. Most importantly, the government did not permit them to make passenger cars and forced them to work through the control associations to obtain materials and to sell.

Beginning in the Occupation, industry was able to exert greater and more direct influence over public policy. The wartime control associations became voluntary trade associations. Regulations prohibiting passenger car research and production were repealed. Companies no longer had to be authorized in order to produce, which allowed new companies to enter the industry. The government worked more closely with the industry, and sought its advice, when developing policy options. Industry also suggested policies and played a large role in developing initiatives to propose to SCAP. MITI's 1952 policy paper on the automobile industry also incorporated industry's views. In fact, in the 1940s one of the first tasks of the Automobile Manufacturers Association (the predecessor of the Japan Automobile Manufacturers Association) was to lobby

SCAP and the Japanese government to support the industry—a role it continued to play during liberalization, the negotiation of the export restraints, and up to the present. When industry's views were overlooked, as occurred during the People's Car Project, business was likely to oppose government policies.

Japan's parliamentary structure also affected interactions. It helped reinforce the tendency, along with culture, to use administrative rather than legislative methods of policy implementation. It also was responsible for the existence of an elite bureaucracy, rather than the legislature, that took the governmental lead in policy formation. This structure permitted more cooperation and negotiation because issues were not politicized as often. When issues were politicized, as in the case of emissions, there was much less room for government and business to maneuver in their negotiations. In addition, the bureaucracy had more respect and influence under Japan's parliamentary system, which made close and continuous consultation with industry possible.

Frank Upham shows that administrative rules need not be formal.⁶ He suggests that attributes of informality and verticality, and the broader political and social context of which they are part, affect the Japanese government's ability to control the pace and direction of change. While his case studies do not include the automobile industry, his conclusion that informal, consultative actions rather than compulsory edicts account for the preponderance of government actions also holds for automotive-related actions from the development of protective policies in the 1950s to the implementation of emissions policies in the 1970s.

The rules continued to change after independence, albeit more subtly. The changes in the rules in the 1950s and 1960s reflected constraints put in place by the international environment more so than any change in domestic institutions. In the 1950s, the government controlled foreign exchange allocation, which gave it leverage in its negotiations with business. It threatened to cut off foreign exchange for those automobile companies that did not fulfill the domestic content provisions of the technology tieup agreements, but at the same time it allocated companies foreign exchange to buy machine tools. It was able to enact protective policies that restrained imports and developmental policies that promoted demand and technological innovation because of its transitional status under multilateral arrangements and because the United States wanted Japan to be a bulwark against Communism in Asia. Business, especially the larger companies, benefited from these

controls that kept imports (and some smaller Japanese companies) out of the market.

After Japan joined the IMF, the OECD, and the GATT, the government lost some control over foreign exchange and had to liberalize its market. These changes lessened the government's leverage over industry. The government sought new forms of influence, which resulted in the ill-fated Special Measures Law for the Promotion of Designated Industries. Thus, because the international environment created changes in the administrative rules in Japan, in spite of the endorsement of the concept by the special committees, the government could not force business to accept the merger schemes, and it lost much of its control over foreign capital investment in the early 1970s. As a result, even though the government preferred mergers among domestic companies to tieups between domestic and foreign companies, Mitsubishi, Isuzu, and Mazda concluded partnerships with foreign firms.

The administrative rules constrained how government and business interacted to create policy and affected the amount of leverage government had over business. Again, interaction and negotiation remained, but they operated under different constraints at different times.

Competitiveness

The automobile industry's competitiveness strongly affected its relationship with government—competitiveness being the ability of industry to compete globally without government protection or, in other words, the industry's vulnerability in the international environment.

A competitive mature industry with wide-ranging influence on the economy and a vulnerable infant industry with potential can both be perceived as economically important. However, the government-business relationship differs in these two cases because of competitiveness.

The competitiveness of the Japanese passenger car industry was low and its vulnerability high through the 1950s. In the 1930s, General Motors, Ford, and Chrysler had onshore assembly plants. Japanese domestic production was small and of bad quality. The industry survived primarily because the American companies were forced out of the market. In the 1950s, European small-car exports and foreign companies' attempts to establish subsidiaries threatened the Japanese domestic producers again.

The still uncompetitive passenger car industry needed and accepted protective and developmental incentives that involved a high level of government direction but gave it room to experiment with new technology and to adapt industrial practices to meet local conditions.⁷

As the automobile industry became competitive, its interactions with the government grew more adversarial. During the 1960s and 1970s, companies increasingly opposed government policy initiatives that they felt were not in their best interest even though they still often agreed on the basic problems being addressed. The Mitsubishi/Chrysler tieup and Honda's decision to manufacture passenger cars are clear examples of industry opposition to government wishes. However, even in this period, industry cooperated with the government in forming policies to delay liberalization. This cooperation continued until some companies saw that it was not in their best interest, a decision possible because of changes in competitiveness and administrative rules.

The industry's competitiveness affected public policy options. Initially, government and business used protective and developmental policies to help the automobile industry grow. After the industry matured, policies expanded to include regulatory controls on emissions and safety and restraints on exports. There were fewer incentives for the industry to cooperate with these intrinsically restrictive regulatory policies than with the earlier developmental policies. (It is always easier to cooperate when someone else is being penalized, i.e., a foreign producer, and when someone else is responsible for implementing an agreed upon policy, i.e., the government.) After much hesitation the industry did cooperate with the government on emissions controls, but only after the smaller companies perceived an opportunity to use the controls to increase market share. The industry strongly opposed export controls. It accepted them only to prevent the threatened enactment of restrictive American local content legislation. The industry's competitiveness in the 1970s also allowed it to have its own listening posts in Washington, adding an independent source of information and yet another dimension to its negotiations with the government over export controls.

Economic Importance

The automobile industry's importance—real or perceived—to the economy also influenced how government and business interacted. Those who argue that industrial policy did not affect the

industry's economic development point out that the automobile industry was not at the center of economic development plans and was only one of many "key" industries. However, these facts do not negate the relationship or the possibility that assistance, even if not as large as in some industries, was provided because the industry was perceived as important.

Prior to the 1930s, the industry was so small that interaction was limited to the military subsidy program. As the industry proved crucial to foreign exchange conservation and to military strength, the relationship became more active. The government attempted to create a national vehicle, the Isuzu. When this attempt was unsuccessful, the government worked with Toyota and Nissan to create a domestic truck industry.

After World War II, the industry lobbied the government to support the industry's interests with the Occupation authorities. The government cooperated but did not place the same importance on the automobile industry as it did on other more basic industries. Toward the end of the Occupation, the discussion between MITI and the financial community on the feasibility of developing a domestic passenger car industry revolved around different perceptions of the industry's economic importance. Ultimately the potential for economic development in the passenger car industry swayed those who had previously been unenthused. The government then supported the industry through a variety of protective and developmental policies. These policies in turn created an atmosphere conducive to cooperation.

The industry, however, still was not at the center of economic development plans and received just enough assistance to provide minimal survival security. The decision to provide only minimal financial support did not lessen the amount of interaction that occurred, it just occurred on other issues. By the mid-1950s and even more so by the 1960s, the government agreed with the industry that it was central to economic development and, so, sheltered the industry from liberalization for as long as possible.

The industry's and government's similar goals in the initial postwar period contributed to a cooperative relationship and to the economic development of the industry. Agreement on the economic importance of the industry, however, could not sustain a cooperative relationship when substantial disagreement developed about specific methods and policies at the same time competitiveness had increased industry's leverage and the administrative rules had changed.

Summary

The major factors that affected interactions between government and the Japanese automobile industry were (1) cultural and historical lessons, (2) the perimeters or rules agreed to or imposed by force within which the government can make and carry out policy, (3) the competitiveness of the industry, and (4) the importance, real or perceived, of the industry to economic development. Each factor affected the relationship by creating tendencies toward continuity or change, and by interacting with one another to create a dynamic environment. The potential effect of each factor must be carefully evaluated in relation to the others to discover how it affected any particular situation.

Cultural and historical lessons provided continuity throughout the relationship. Two such lessons were especially important. First, government and business accepted that they each played a role in policy formation. Both suggested policy initiatives, although the government drafted the actual policies. Each side's acceptance of the other's role helped create a tendency to formulate policy through negotiation. Second, government and business were aware of the close association between the international environment and competitiveness. Their awareness of this connection created a sense of urgency and provided an incentive to work together.

Continuity did not mean that business and government always cooperated and agreed; quite often they did not. Continuity also did not prevent change because factors that created change often overrode it. The industry's competitiveness, and thus its ability to oppose government policy initiatives, changed. The rules of the international environment, and thus the government's ability to enforce policies, changed. And, the industry's importance to the economy changed, altering in turn the type of policies needed.

One reason American policy makers are interested in the Japanese government-business relationship in the automobile industry is that they see it as more effective than that of the United States in creating a competitive industry. This perception recognizes the dynamism that existed in the relationship. It is important, however, to understand that the effectiveness of the relationship grew out of its interactiveness and out of the way in which the various factors affected each other.

Competitive Implications

The government-business relationship and the policies it engendered facilitated the development of Japan's automobile industry by protecting the industry in its formative stages and by providing developmental incentives. These measures gave industry the minimal security it needed to experiment and to grow before it had to test its competitiveness in export markets against foreign producers. These measures grew out of interactions among many governmental and private actors, not simply from a prescient government or a competitive market.

Given this, it is necessary to remember that, just as the government-business relationship reflects the interaction of several factors, many factors contributed to the creation of a competitive automobile industry. The Japanese automobile industry grew because of strong entrepreneurs, a competitive market, an innovative subcontracting system, an educated population, and developmental timing. The list of possible factors is infinite.⁸ The industry also benefited from programs rooted outside Japan such as special procurement during the Korean War and Operation Roll-Up, and tieups with foreign companies. Thus, the industry's successful development did not occur as a result of one factor, be that factor the market, government direction, process technology, or the government-business relationship. Rather, it occurred out of the dynamic interaction of many factors.

However, just as certain factors are more important than others in shaping government-business interactions, some factors are more important in economic development. In the case of Japan's automobile industry, one of the important factors was the government-business relationship.

The relationship was important to economic development first because the acceptance of negotiation, and thus the acceptance of the involvement of both government and business, facilitated the development and implementation of policies of which both industry and government approved. There were instances in which consensus could not be achieved, but most of these occurred after the industry was competitive.

Negotiation existed in Japan before the postwar period but did not lead to as dynamic an industry because business initiative was inhibited during wartime and because the industry was still in an early formative stage. The creation of a market economy and changes in administrative rules removed the restrictions on business

and gave it a stronger role in the partnership. In addition, as the industry took on economic importance, the government was more responsive to its needs, leading to more interaction and more negotiation.

The relationship that evolved contributed to successful growth and to the implementation of protective and developmental policies by creating a negotiated set of public policies that provided minimum survival security for the industry. Without this security, it is likely that foreign companies would have controlled the market through imports and onshore assembly plants. The developmental measures, while insufficient by themselves to create the industry, accelerated its progress—how much so compared to actions the companies took themselves is impossible to quantify.

The negotiated set of public policies is the aspect of the relationship often cited by those seeking protectionist policies. They see these policies as evidence of a collusive partnership to overtake world markets. Rather, the partnership was one that recognized a mutual interest in developing a competitive industry to protect the home market, which resulted in the added benefit of competitive exports.

The relationship also was important after World War II when awareness of the industry's vulnerability to the international environment, together with a consensus that the industry was economically important, contributed to, and indeed necessitated, government and industry cooperation. Cooperation was needed to build a competitive industry that abided by multilateral agreements and operated within the constraints of a market economy. Both government and business were aware of the industry's vulnerability in the international environment, but, at the same time, they knew that it was this environment that would provide the stimulus to become competitive.

Finally, without the acceptance of negotiation in policy formation, important viewpoints from government and business would have gone untapped in developing policies to meet the competitiveness challenge. Without government interest in ensuring that Japan met its obligations under multilateral agreements, the industry would not have felt pressured to become competitive so quickly.

The policies that resulted from the partnership eliminated the industry's vulnerability by helping to create a competitive industry. These policies and this solution were not systematically planned but resulted from negotiation, an awareness of the international environment, and the perceived economic importance of the industry. If the factors affecting the relationship had interacted

differently, different policies with different effects might have occurred. The interaction of these factors in the case of Japan's automobile industry was dynamic: a democratic market economy forced to become competitive by adapting to the international environment—an adaptation aided by policies growing out of a government-business partnership that was not constrained by adversarial positions or stifled by the exclusion of either party in policy formation.

In the 1970s and 1980s, some of the factors affecting the Japanese government-business relationship in the automobile industry changed. The elements of continuity remained, but competitiveness increased and the administrative rules changed. In consequence, policies changed to stress the achievement of broader societal goals such as a clean environment and decreased bilateral trade tension. It is too early to predict if the relationship's dynamism remains to help meet new challenges to the industry, such as those posed by its obligations to help insure a free international trade environment.

In the United States, the impact of factors affecting government-business relations were quite different. The American automobile industry until the 1973 oil crisis was protected by product differentiation and believed itself to be competitive. Cultural and historical lessons did not encourage negotiation and consensus. Although it became a cliché in the United States that government and business must work together to build competitiveness and to formulate effective public policy, often the concept was not practiced in reality. As a result, even though the industry was perceived as economically important, there was little reason or incentive for government and business to cooperate in policy formation. This situation changed in the 1980s, resulting in the growing interest in industrial policy.

Policy Implications

This study concludes that trade friction will remain as long as nations' industries are at different levels of competitiveness. Interactions between government and business will continue to take place affecting competitiveness and in turn being affected by it. And, factors will combine differently in each nation to produce unique relationships.

The study's findings help to specify the perimeters within which policy makers should take government-business relationships into account when making trade policy decisions. The study demonstrates that relationships do have implications for global competition that need to be factored into policy decisions. If nothing else, knowing why different relationships exist and how they interact helps policy makers develop better methods to influence behavior and to reach solutions acceptable to all parties.

Michael Blumenthal was right in stating that government-business relationships are different in different situations but wrong in stating that they are not relevant. They are relevant because they affect economic development, which in turn affects global competition. Global competition then in turn affects every country's government-business relationship. Therefore, unless a country exists in total isolation, other nations' relationships are important to understand for their effects on the global economy, on domestic government-business relationships, and on policies being considered to influence other countries' behavior. Since government-business relationships have implications for global competition, what lessons can be drawn from the history of the Japanese automobile industry's interactions with its government?

First, ideologically based explanations of government-business relationships are invalid and culture bound. The trade debate over industrial policy and the role of government-business relationships tends to use such explanations to justify policy actions. However, such explanations fail to reveal the interactiveness of relationships and fail to take into account differing situations among countries. Since government-business relationships are interactive, they reveal the ability of both government and business to influence each other. More importantly, they reveal that many actors influence policy through their complex interactions. Ideologically based explanations miss the richness of these interactions. And, policies based on them will be fundamentally flawed because they will not address the real problems.

Policy makers should recognize that ideologically based explanations restrict the range of policy alternatives just when imaginative policies are needed to deal dynamically with new situations. They need to adjust policies to the fact that relationships change as the factors surrounding them change. Therefore, they should seek out those factors that promote continuity and discover how, or if, they will be overridden by other factors that create change. They should not base policy decisions on outdated conceptions of past relationships or on idealized relationships.

Factors can change, and this implies that nations can gain, lose, and regain competitiveness. It also suggests that each nation, because of differences in how factors combine, has to discover the government-business relationship that best promotes competitiveness in its situation. This implication does not mean that policy makers cannot learn from other nations' experiences, only that these experiences need to be analyzed and adapted carefully. Just as there are differences between nations, there are also similarities.

Second, different government-business relationships lead to different policy choices and to different degrees of success for policy implementation. Whether or not the resulting policy choices and their implementation will encourage or discourage competitiveness is highly dependent on the interaction of many factors, including the international environment. In the case of Japan's automobile industry, it was effective and dynamic.

Policy makers need to be aware of these differences in formulating policy options. Understanding how the government-business relationship developed in Japan's automobile industry and how it affected global competition offers the opportunity to discover what factors affect each nation's government-business relationship and how it in turn affects competitiveness. It also provides the opportunity to see what can and cannot be changed in relationships.

Differences also point out the need to decide whether certain policies are equally permissible in advanced and less-advanced nations. These decisions are value based and depend upon the perceived importance of maintaining certain relationships and aiding less-advanced nations.

Third, the dynamic combination of factors in Japan's automobile industry that fostered the creation of a fully competitive industry included a strong awareness of the international environment. The emphasis by government and business on exporting and on competitiveness reflected this awareness. The international environment acted both as a dependent and independent variable; it affected the government-business relationship and in turn the relationship affected it.

Policy makers who seek to build competitiveness should not only recognize international forces but also use them as a challenge to reinforce competitiveness. They should not use them to justify permanently limiting an economy's international exposure. True competitiveness increasingly is found and tested in the global arena, not the domestic market.

The government-business relationship is an increasingly significant issue in international trade but remains complex and

value ridden. In the short term, it is most feasible to continue to ameliorate the welfare effects of specific sectoral trade conflicts by using insights into government-business interactions to become effective players in influencing policy formation. There are some who might argue that this is one reason why Japanese lobbying, including that done by the Japanese automobile industry, has been effective in the United States. Multilateral arrangements continue to be appropriate to establish perimeters for when, and at what level of economic development, specific types of policies are permissible.

Conclusion

This study has delineated the factors shaping the government-business relationship in the Japanese automobile industry. It found that the relationship was interactive and consisted of many players whose actions are bound by factors creating change and providing continuity.

It demonstrated that the relationship was one important factor in economic development. The partnership that developed helped in the creation of policies that protected and supported the industry's development. These policies allowed companies to experiment with innovative practices that made them competitive and leaders in the world market.

It showed the relevance of government-business relationships in trade policy. The creation of a competitive Japanese automobile industry reinstated strong competition in the world market, disturbing existing automobile industries in other countries and creating trade friction. This change has challenged the Japanese government and automobile industry to use their partnership to take on global responsibilities and to cope innovatively with their effects on global competition in a manner than benefits all nations and all competitive companies worldwide. Also importantly, it has challenged the long-held assumption by many in the United States that government-business relationships arise purely out of domestic issues and that these relationships are not pertinent to trade policy formation.

NOTES

¹Richard Samuels, *The Business of the Japanese State* (Ithaca: Cornell University Press, 1987), p. 288.

²Examples of studies that include culture as a factor include Johannes Hirschmeier and Tsunehiro Yui, *The Development of Japanese Business, 1600-1973* (London: Allen & Unwin, 1981) and Ronald Dore, *Taking Japan Seriously* (Stanford: Stanford University Press, 1987).

³Michael A. Cusumano, *The Japanese Automobile Industry* (Cambridge: Harvard University Press, 1985), pp. 6-7.

⁴David Halberstam, *The Reckoning* (New York: William Morrow and Company, 1986), p. 615.

⁵Several studies stress the importance of institutional structures in policy formation including Chalmers Johnson, *MITI and the Japanese Miracle* (Stanford: Stanford University Press, 1982).

⁶Frank K. Upham, *Law and Social Change in Postwar Japan* (Cambridge: Harvard University Press, 1987), pp. 164-204. This book provides general insights into the legal context of industrial policy and interest group behavior in policy formation that are useful in understanding policy actions specific to the automobile industry.

⁷Cusumano, *The Japanese Automobile Industry*, p. 7.

⁸Two studies that contain lists of factors that affect economic development are Samuels, *The Business of the Japanese State* and Dore, *Taking Japan Seriously*.

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