JAPAN

The rise & decline of industrial Japan

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INDUSTRIAL supremacy does not usually last *very* long. "All industrial curves seem to take off vertically and to decline equally dramatically," the French historian Fernand Braudel writes in his great work *The Mediterranean and the Mediterranean World in the Age of Philip II.* "There was a distinct relationship then between industrial expansion and decline in places often very far apart. The last player to arrive is always the favorite."

Braudel was commenting on the shift of the center of textile production from Italy to northern Europe some four hundred years ago, but be could have been talking about Japan today. For most of this century, Japan has been leading one of the most momentous shifts in the geographical distribution of industrial production that the world has seen.

Japan's share of all industrial output has leaped from 1 percent in 1913 to 11 percent today, more than doubling over the past decade alone. Over the past two decades, its manufactured exports multiplied from $4 billion to $150 billion, accelerating a rise in per-capita income since 1952 from $188 to more than $10,000, now roughly equal to the other major industrial countries.

While Japan is most famous for its cars and consumer electronics, more than two-fifths of its exports are now production machinery and other capital goods, including whole factories, contributing to the extension, cheapening, and upgrading of industrial processes in many other countries. Japan is not merely inflicting heavy damage on U.S. industry with exports of steel and automobiles; it is also building steel mills in Brazil, Korea, China, Qatar, Nigeria, and Venezuela, and setting up electronics factories throughout Southeast Asia and in such remote places as Manaus, on the Amazon river, and Tierra del Fuego, at the edge of the Antarctic in South America.

Along with all this, Japan has gradually been taking up the slack left by the declining importance of the United States as what might be called a matrix economy: the source of new products and new designs, components for assembly and spare parts, and the creator of new industries in other countries. As high domestic costs have made certain items too expensive to produce, or when direct export has been blocked for political reasons (as with color-TV shipments to the U.S.), production often has been farmed out by Japan's matrix economy to factories elsewhere, first to Korea and Taiwan (former colonies), then throughout the world, often in ways akin to the subcontracting of production between large and small Japanese firms.

Japan's recent conquest of new markets has provoked fear and rage among Western businessmen, union leaders, and politicians concerned with maintaining employment and productive capacity, and threatens to disrupt the postwar system of international trade. Yet according to the latest World Bank figures, Japan exports a smaller share (15 percent) of its national product than most industrial countries, coming closer to the low export profile of the U.S. economy (10 percent) than those of most European nations, which exceed 30 percent. Moreover, Japan's manufactured exports are less than its share of population among the industrial countries, and less in absolute terms than the manufactured exports of the U.S. and Germany. Indeed, with half the population of Japan. Germany exports considerably more manufactured goods.

No doubt Japan still is and will remain one of the world's leading industrial economies. Yet unperceived by most Westerners, Japan's economy is entering a phase of "maturity" akin to that of the older industrial nations. Thus since the 1975 oil crisis, despite Japan's extraordinary achievements in energy conservation and in maintaining the competitiveness of its manufactured exports, real economic growth has declined to 3 percent yearly — according to Japan's Ministry of International Trade and Industry (MITI), the minimum needed "just to insure the stability of Japanese society" — and to about one-third to one-fourth the levels of the previous "boom decades." Annual gains in labor productivity have declined in the same proportion. While these rates are higher than those of the Western economies, that is because Japan still is younger industrially. On the other hand, Japan foreign competition, we must develop a firm solid basis to fight it off, they say. All this economic growth, that's it. The growth of the economy has gone so far that the balance of — what do you call it? — the balance of payments has got a big balance in the black — billions of dollars — and that means the pressure's on Japan internationally speaking. Trade protection won't do any more. We've got to be internationally minded. It's going to be a tough time for us Japanese from now on.

One of the West's old masters of Japan studies, Dore first visited. Shinahata in 1955 while preparing an earlier book, *Land Reform in Japan.* When he returned two decades later, he found the villagers' "sense of modern prosperity underpinned by a certain sense of guilt. It's just not quite *right."* The villagers were being massaged lovingly and continually with government services and public works. Their benefactors were politicians of the ruling Liberal Democratic party (LDP), which has governed Japan continuously since 1955 and has become more and more dependent on votes from overrepresented rural districts to stay in power.

"You can say what you like about these politicians, but they certainly know how to run the country; they must be smart," a farmer tells Dore:

I don't know how it's done, but at any rate here I am, doing much the same as I was doing 20 years ago; I don't get much bigger yields from the rice fields. I do about the same amount of work on construction sites, but our whole style of life is different; everything's mechanized, we don't have to work nearly as bard and we can afford things we'd never dreamt of a few years ago.

The LDP has been ruling with the support of. what one might call a business-peasant alliance formed gradually in the postwar years in response to General Douglas MacArthur's 1945 call for "revival and strengthening of democratic tendencies" in Japanese villages. The most spectacular benefit to businessmen and peasants from this alliance has been a series of luxurious public works.

Some of these works in Shinohata are in the great tradition of land-reclamation projects going back at least four centuries: the area of rice paddies in Japan was doubled between 1550 and 1650 by construction of dikes and diversion of rivers. But today there is a difference. In *Shinohata* Dore remarks, "Nowhere else are rice fields banked with such expensive concrete blocks." Fields that were "entirely recreated after a typhoon washed them away 15 years ago — at a cost to public funds of $2,400 an acre — [are now] left to grow weeds throughout the year." He adds:

Older people remember the days when what one earned from a day's casual labor would buy less than a couple of kilograms of rice, not the 20 kilograms that the 4,000-yen daily wage would buy today — not to count the fact that rice was then far cheaper relative to other goods. To many of them the sudden prosperity seems too good to last. It can't be true. It has a hollow ring. It is built on sand.

I harbored similar thoughts during my visit last October to the village of Ushiroyama, cradled among the hills of the snow country of central Japan. The village's 51 houses, with curved, pagoda-style roofs, are threaded by a narrow paved road that winds downward past flower gardens and the soft greens and browns of terraced rice fields into a quiet ravine where the government has built a small dam to control soil erosion. Because the cold and snow of Ushiroyama make these hills marginal for rice production, the villagers used to specialize in growing silk — Japan's main export until 1929, with 97 percent going to the U.S., until prices collapsed under competition from synthetics during the Great Depression.

Today Ushiroyama produces little but votes for the LDP. In return, nine-tenths of all farm families now earn most of their money off the farm, much of it on construction projects that increasingly defy the imagination: hot-water sprinkler systems embedded in local highways to melt falling snow; or the tunnel now being dug so the villagers of Ushiroyama, at a cost of $500,000 per family, can leave their valley more easily when it snows; or the new Tokyo-Niigata bullet train built at the staggering cost of $60 million per mile. It all comprises an enormously expensive welfare system for rural Japan.

IN SEPTEMBER 1936 *Fortune* magazine published a special issue on Japan, one of the unremembered (and anonymous) masterpieces of American journalism, ascribing "the great competitive superiority of the Japanese" to

a homogeneous, highly integrated, and beautifully adapted social organization permitting a unification of national effort not possible in any other country ... *The Japanese can still get along without more things than any other industrial people* [emphasis in original]... The Japanese family system — which, whatever it was in the old days, is now merely another name for self-help among the Japanese workers — absorbs its unemployed not by absorbing them but by dividing with them. Every tiniest crumb of possible activity will be kneaded into employment of a sort. A man will make a living out of carrying a kettle of steam along the country roads from farm to farm to scald out the brass tobacco pipes of the farmers. Another will exist by showing paper drawings to children and explaining their story. Each fraction of economic life is subdivided to further fractions.

In Ushiroyama a farmer named Kazuju Yamamoto was telling me how things have changed:

My children go to the village school that the government maintains, even though there are only 12 pupils. Next year my daughter will be soon will have the oldest workforce of all industrial countries because (thanks to a bulge in its birth rate during the early postwar period) its population is aging faster than any other nation on earth.

At the same time, we are witnessing the erosion of the economic viability of some of Japan's key "strategic" industries — shipbuilding, aluminum, oil refining, petrochemicals, nonferrous metals — that were favored with priorities and subsidies over the past half-century in Japan's drive toward heavy and chemical industrialization. In these and other industries, the domestic Japanese market is increasingly being penetrated by imports. "Despite a widely-held view that the Japanese economy is 'closed,' " says a new Hudson institute report. "the cases of declining industries on record to date show that at some paint Japanese companies, like those in other countries, are unable to sustain price/cost differentials with the rest of the world." In the official view of MITI: "Just as Japan is being admired for the strength of its economic power, major changes are taking place within its industrial structure. The very foundation of that industrial activity which must support Japan's future economic performance is in danger." Thus, while Japan was the world's leading steel producer two years ago, a sudden rise in cheap imports in 1982-83 has taken away one-fourth of the home market from Japanese companies which are now pressing the government for protection.

In addition to all this, Japan since 1975 has been running the largest government deficits of any major industrial country, eating steadily into the huge pool of personal savings — highest in the world — that once could finance both government deficits and industrial investment. Thus savings has been following investment on a downward path, while Japan's international competitiveness is being undermined gradually by rising consumption at home, the closing of overseas markets, and the challenge in its home market of imports from abroad.

II

ACCORDING to Braudel, "industrial functions are called into existence by commercial activity, which creates the demand for them; they therefore presuppose a certain level of economic maturity." Yes, trade breeds manufacturing, and Japan was forced to trade again with the West after the visit in 1853 of Commodore Perry's "black ships," ending more than two centuries of seclusion imposed by the Tokugawa shoguns. But how was Japan able to overwhelm its Western trading partners with a flood of cheap manufactured goods, of ever-increasing sophistication and quality, so soon after the reopening of trade?

Scholars of many different stripes have been chewing on that question for a long time. in his new book, *MITI and the Japanese Miracle; The Growth of Industrial Policy, 1925-1975,* Chalmers Johnson of the University of California tells how the elite bureaucracy of MITI rode piggyback on the militarization of Japanese politics and society in the 1930's to carry out a transition from low-class industry (silk, cotton textiles, toys) to high-class industry (steel, chemicals, motor vehicles, airplanes). Building on this foundation, Japan in the postwar decades became a "plan-rational state." Johnson explains:

The United States government has many regulations concerning the antitrust implications of the size of firms, but it does not concern itself with what industries ought to exist and what industries are no longer needed. In the plan. rational state [Japan], the government will give the greatest precedence to industrial policy....The real equivalent of the Japanese Ministry of International Trade and Development in the United States is not the Department of Commerce but the Department of Defense, which by its very nature and functions shares MITI's strategic, goal-oriented outlook.

Other scholars — including Takafusa Nakamura of the University of Tokyo — have taken Johnson to task for exaggerating the importance of MITI, for underrating the role of the private sector, and for stating that Japan's first priority since 1925 has been economic development. Nakamura has just published two major works in English on the prewar and postwar Japanese economy that provide a much more far-reaching view. Nevertheless, he shares Johnson's fascination with the embarrassing and often unpalatable linkages between warfare and economic development, and he elsewhere actually reinforces Johnson's analogy between M1TI and the Pentagon. In his *The Postwar Japanese Economy,* Nakamura argues that present systems of lifetime employment, industrial investment, forced mergers, industrial subcontracting, and sweeping bureaucratic powers over industry all developed in the wartime emergency that began with the 1937 invasion of China and ended with the surrender to the United States in 1945. "To a great extent, the system which was created during the war was inherited as the postwar economic system," he writes. "The industries which were expanded during the war became the major postwar industries; wartime technology was reborn in the postwar export industries; and the postwar national lifestyle, too, originated in changes that began during the period of conflict."

THE TROUBLE with interpretations like these is that they concentrate too much on recent events and not enough on the underlying strengths that bred the great flowering of Japanese economic development in the half-century before 1929. Perhaps Japan's success, both in the prewar and postwar decades, would have been easier for Westerners to understand if Japan were not so far, culturally and geographically, from the "white men's club" of nations along the two great industrial belts that, until 1929, produced four-fifths of the world's industrial goods. The first was the European belt that spread over the centuries along an irregular series of iron and coal deposits that stretch from the British Midlands to the Ruhr, Silesia, and Russia's Don basin. The second was the North American belt that followed both shores of the Great Lakes from western New York, Pennsylvania, and Ontario into the huge but now depleted Mesabi iron range of Minnesota. While these two industrial belts developed as men learned better use of their coal and iron, Japan groped along the path of a resource-poor seafaring nation, Holland, in nurturing trade and industry.

Indeed, the Dutch were the Japanese of the 17th century. Like the Japanese three centuries later, the Dutch built upon an early trade in bulk commodities to introduce new methods of making ships and textiles — the advanced products of the time — in the service of a trading network that spanned the world. "The Dutch had a genius, if not an obsession, for reducing costs," writes the Italian historian Carlo Cipolla:

The Dutch succeeded in selling anything to any. body anywhere in the world because they sold at very low prices, and their prices were competitively low because their costs of production were more compressed than elsewhere. The Dutch decidedly moved toward mass production. In an increasing number of activities they endeavored to maximize their profit by maximizing the volume of sales. Even Dutch painters produced their masterpieces at low prices and in prolific quantities.

Like the Japanese centuries later, Dutch entrepreneurs thrived on low domestic interest rates — 3 percent in Amsterdam against 6 percent in London — which made it easier to invest in trade and industry. And like the Dutch before them, the Japanese thrived as interlopers on other peoples' trade. Just as the Dutch aggressively cut themselves into the established business of the city-states of Italy and the North German Hanseatic League, the Japanese became suppliers of cotton fabrics to Europe's Asian and African colonies during World War I, while the colonial powers were otherwise distracted. The momentum thus gathered enabled Japan to overtake the British as the world's leading textile exporter by 1933.

By then, too, Japan was further irritating and embarrassing the industrial powers by selling beer to Germany, silk to silk-making Italy, and American flags to the American Legion. Meanwhile, as the Dutch did centuries before, the Japanese were creating new markets by selling a bewildering variety of manufactured products so cheaply that they were within the reach of people who never could afford them before. In Chile, for example, they were marketing handsome English-style bicycles in 1934 for $8 each, half the price of the competing German model. American microscopes wholesaled at $7.50, while Japanese copies whole. saled for 61 cents in Japan in 1935 and were landed in Boston, duty-paid, for $1.95. By the 1930's U.S.-Japanese "trade frictions" were beginning to take the shape of the disputes of the 1970's.

In 1955 the U.S. got Japan to agree to "voluntary" restraints on textile imports and then imposed "here and there" controls on imports of wool-knit gloves, zippers, rubber shoes, electric bulbs, toys, matches, brushes, carpets, pottery and porcelain, imitation pearls, canned fish, and pencils.

TODAY, the mix has changed. However, even as Japan in 1980 became the world's leading producer of steel and automobiles, overtaking depressed U.S. industries and throwing overpaid U.S. workers out of work, the Japanese economy was beginning to yield to the same forces that governed the rise and decline of earlier powers.

Thus the Dutch encountered protectionist legislation in Russia, Prussia, Denmark, Norway, and Spain in the early 18th century: the Japanese today are facing the same kind of closing of their export markets. So, too, high wages and taxes began to undermine the competitiveness of Dutch products just as foreigners were beginning to make the same things and close their home markets, after many Dutch industries had expanded to meet export demand; the same thing is happening to Japan today. Again, just as cheap Dutch textiles previously invaded the home markets of Genoa, Venice, and Milan, wiping out their industries, cheaper English cloth later invaded the Dutch market — wiping out the workshops of Leyden and Utrecht in the 18th century almost as fast as they had mushroomed a century earlier; today, in the same way, the Japanese home market is being invaded by cheap Korean steel, textiles, machine tools, and electrical appliances.

The point is illustrated in Ronald P. Dare's jewel-like book, *Shinohata: A Portrait of a Jaanese Village.* "I'm afraid the [printed gift] towels are more expensive this year," apologizes an old cloth merchant quoted by Dore. "Luckily the dyers still had the plates from last year or the expense would have been terrible. They can't get people to do this kind of thing nowadays. They've even started sending work to Korea to be done. It's terrible the cost of labor these days.

The complaint of the cloth merchant in Shinohata bears witness to a sweeping change in the traditional economic system upon which Japan built in order to burst onto the world economy with so much force. Only recently have we come to appreciate the strength and character of that traditional system and the degree to which Japan's precapitalist development singularly paralleled that of Western Europe. In his newest book, *The Wheels of Commerce,* Braudel summarizes the recent work of many scholars by observing that Japan grew institutionally

in a kind of anarchy not unlike that of the European Middle Ages. Everything developed simultaneously in the diversified arena of Japan as the country gradually formed itself over the centuries: a central government, feudal lords, towns, peasantry, an artisan class, the merchants. Japanese society bristled with "liberties" like the liberties of medieval Europe, which were privileges behind which one could barricade oneself for protection and survival.

THE strength and adaptability of the traditional system are richly described in Nakamura's new book, *Economic Growth in Prewar Japan.* One-fourth of all farmers managed second business by the end of the Tokugawa shogunate (1603-1868). They ran small bars and eating houses, made bean curds and candies, sold tobacco, vegetable oils, and lumber, and hired themselves out as craftsmen and laborers, while their wives and daughters raised silkworms and wove cloth and straw matting when not working in the fields. Landlords were pawnbrokers and moneylenders, fertilizer and dry-goods merchants, and owned small *sake* and soy-sauce factories, whose number doubled between 1892 and 1899 alone.

According to Nakamura, Japanese industry adapted imported Western machines to make them cheaper and simpler to copy and to make factory operations more labor-intensive. For silk-reeling machines from France and Italy, capital costs were reduced by making parts from wood instead of copper, iron, and brass: wire replaced glass and earth replaced brick. Big cotton-spinning factories could not become profitable until they added night shifts, increasing the ratio of cheap labor to expensive capital. Power-weaving made little progress until a big hydroelectric construction effort began after 1910, enabling capital per worker to double during the 1920's in the textile industry.

Preindustrial Japan was not a poor country. Fisheries in its surrounding waters were so abundant that they provided not only a ready protein supply for the islanders, but also a supply (in the form of dried fish) of fertilizer, contributing to the large increases in farm productivity during the Tokugawa era. Japan's mineral wealth was such that it was a leading supplier of silver and copper to Europe in the 16th and 17th centuries. These exports continued through the Dutch trading station on an island in Nagasaki harbor even after trade with other Western countries was banned in 1637. By the 18th century Japan was one of the most urbanized societies outside Europe. In an earlier book, *Education in Tokugawa Japan* (1965), Dore estimated that 54 percent of males and 19 percent of females had been through primary school in 1875 (as compared with England at the height of the Industrial Revolution; when only one child in four or five was ever getting to school).

So much, then, for the traditional view of Japan making a sudden transition from feudalism to capitalism as it burst upon the world scene after the visit of Commodore Perry's "black ships." This interpretation, the product of the writings of Japanese Marxists, has until recently dominated the literature on their country's economic history. The newer view is crystallized in a pathbreaking study, *Economic and Demographic Change in Preindustrial Japan, 1600-1868* by Professors Susan B. Hanley and Kozo Yamamura of the University of

Washington, who marshal much new data to argue that Japan's sudden success upon reentering the world economy a century ago was due to

...the already high level of agricultural productivity attained by the end of the Tokugawa period, the existence of pools of potential capital and easily trainable industrial labor that could be tapped by emerging industries, the already developed economic institutions, and the importance of traditional manufacturing and commercial activities throughout the early phases of industrialization ... Tokugawa economic and demographic changes explain why Japan alone in Asia succeeded in industrializing so rapidly, making increasingly efficient use of its resources ... Since both the total output and per-capita income were rising during the second half of the Tokugawa period, the economy was able to generate both the capital required for industrialization and sufficient demand for new products during the first crucial decades of industrialization. A mid-19th century economy in which the per-acre yield of rice was as high as in most Southeast Asian nations in the 1950's cannot be considered a "backward" economy.

This portrait of Japan in the century or so before the arrival of Commodore Perry is more consistent than the Marxist view with the rapid economic development that followed. With trading and financial skills already well-developed before the arrival of the "black ships," it should be no surprise that Japanese entrepreneurs soon became alert to opportunities beyond the horizon. Japan's premodern economic system exploited those opportunities.

To consider how much longer Japan's modern system can continue exploiting those opportunities, we must return to the complaint of the old cloth merchant in *Shinohata.*

III

"SOON it will be all big enterprise," the cloth merchant says:

The banks and the big manufacturers: they're getting bigger all the time. That's the tendency. ...And now the next thing is capital liberalization. There are going to be foreign firms investing in Japan. Since we are now about to face going to the junior high school in town and sleeping in the dormitory they provide for village children. In the winter I earn money driving a snowplow along village roads for the government. When the weather's good I work on construction jobs.

That farmers living on handkerchief-sized pieces of land — the national average is one hectare (2.5 acres) — can live better than many U.S. farmers, the world's most productive, shows how much Japan has changed. But that is only part of the story. That these farmers can vacation in Hawaii, drive two cars, and load their houses with all the electronic conveniences one would wish (TV, telephone, washer, dryer, etc.) shows how far rural Japan has advanced into the age of superfluity, from which it may be hard to recede.

IV

MUCH OF the farmer's new prosperity is due to the fact that land prices and government spending rose in tandem by 19 percent yearly in the two decades before the 1973 oil shock, while the Japanese "miracle" was unfolding at a long-term rate of 10 percent annual economic growth.

Those "miracle" decades began in 1950 with the "special-procurements boom" of the Korean war, when the U.S. military gave contracts worth $2.4 billion (about $10 billion in today's money) to Japanese companies, including orders for 7,079 trucks that, Johnson says, were "the key to the revival of the Japanese automotive industry." These contracts, plus spending in Japan by U.S. military personnel, proved a foreign-exchange windfall for Japan in a dollar-scarce world economy, providing the means to import machinery that led to the 1953 investment boom.

Between 1954 and 1960 private investment quadrupled, while exports doubled, accelerating the parade of booms. In 1956-57 came the "Jimmu boom," so named by Japanese journalists because no such prosperity was remembered since the Emperor Jimmu ascended the throne in 660. Next came the 1959-61 "Iwato boom," bringing good times not seen since the even more remote period when the Sun Goddess Amatarasu Omikami was lured from her sullen seclusion in the Iwato cave.

By then, the historic Income-Doubling Plan had been launched by Prime Minister Hayato Ikeda (1960-64), one of Japan's legendary super-bureaucrats. In his book, *The Postwar Japanese Economy,* Nakamura tells how the Income-Doubling Plan — which outpaced all expectations, doubling personal income in seven instead of the planned ten years — was fueled by a "strikingly large budget expansion," with public-spending increases averaging 25 percent yearly in the early 1960's and plant and equipment investment averaging 40 percent. The "accompanying rising prosperity" led into the "Izanami boom" (1967-69), when the economy grew by 13 percent yearly, harking back to the still more misty past when the goddess Izanami coupled with her brother and gave birth to the islands of Japan.

Through all these booms, the main source of economic growth was not exports but investment. From 1952 to 1970 annual private investment increased more than tenfold, financed by an enormous growth in household savings, which peaked at 24 percent of disposable income in 1974 (as compared with only 6 percent in the U.S. today).

But this huge pile of savings — estimated at $550 billion in 1980 — soon began to be squandered. In his drive for the LDP leadership, former Prime Minister Kakuei Tanaka (1972-74) hastily converted an internal MITI report into a bestselling book, *Remodeling the Japanese Archipelago,* calling for what amounted to a second Income-Doubling Plan. Predicting that Japan's national product would rise to $1 trillion by 1985, Tanaka announced that the enormous new transport demand thus generated would require 5,600 miles of new bullet-train track crisscrossing the country, plus 6,000 miles of superhighways, and 4,000 miles of oil pipelines (which, incidentally, would benefit the real-estate and construction interests that backed his extraordinary political career). In the event, Japan's GNP reached $1 trillion as early as 1979, but only 1,120 miles of bullet-train lines have been built and, because they were so expensive, no more are planned.

Nevertheless, from the tracks already completed, one can see the need to remodel the archipelago: unending waves of densely-packed houses lapping against the mountainsides, masses of miniature dwellings fronting on miniature streets, sprawling and monotonous suburban cityscapes extending almost continuously between Tokyo and Osaka on the horizon dominated by Mount Fuji and by the big cages of golf driving ranges bulging up amidst the houses in the same imposing way that white church towers dominate the skyline of all New England towns.

We do not know why golf practice cages have come to dominate the visible profile of these suburban communities. We do know that the Japanese businessman is devoted to the company of other men, generally his clients and colleagues, with whom he spends long evenings of camaraderie in bars and restaurants on the company expense account. We know too that on weekends he gets up at 5 A.M. to drive two or three hours to play golf on a course he has to reserve a month in advance, at a cost of $500 for the day, including drinks and lunch, which the company routinely will pay.

His abandoned wife, meanwhile, will channel all her energies into driving their son to study, study, study so he can progress along life's endless and highly regulated competitions into a company job like his father's. "Will your two-year-old make it to a first-rate firm?" ask the ads on the Tokyo suburban trains. "Better start his education now, before he's too old!" Once hired, he can then endlessly complain, like his parents, that "we are economic animals living in rabbit hutches."

While the government spends lavishly on public works for peasants, large swaths of the Tokyo and Osaka areas are without piped sewage. Housing is expensive and of poor quality, which nobody can explain, given Japan's technological breakthroughs in other areas. Some of the blame is laid to the rising price of land, which in turn has helped drive up rents. Over the past decade, construction costs rose 2.5 times while housing-land prices rose sevenfold in suburban Tokyo and by more in other cities. Because interest rates have been held artificially low by the government, Japanese companies invest surplus cash in land, an asset that appreciates faster than financial paper. Land also is an important political stake. Tanaka, who is still Japan's most powerful politician, despite his prosecution for allegedly taking a $2.5 million bribe from Lockheed while Prime Minister, once said that if the LDP ever tried seriously to control private land rights, the party would go to pieces.

LIKE THE farmers, businessmen have become increasingly dependent on government spending. Between 1973 and 1981, Japan's government deficits averaged 8.1 percent of GNP (while U.S. deficits averaged 2.5 percent). Since 1973, as economic growth rates fell to one-fourth of the pace of the boom decades, government borrowing has multiplied .Japan's public debt fifteen-fold, from one-fifteenth to nearly two-fifths of GNP (while the U.S. federal debt remained stable at one-third of GNP through most of the postwar period). By 1979, these government deficits had become the central issue in Japanese politics as public borrowing reached 40 percent of government spending. However, so dependent had Japanese business become on public-works contracts that a new organization was born, with the backing of 1,076 cement, steel, engineering, and construction companies, under the slogan: "Higher above ground, deeper underground, and farther offshore."

Over the past five years the debts of Japanese National Railways (JNR) roughly doubled to $72 billion, rivaling the size of the foreign debts of Brazil and Mexico, primarily because of the railroads' role as a politically-guided welfare system. And indeed, Japan has caught up with the West in welfare commitments even faster than it previously caught up in production technology. Because Japan's population is aging faster than that of other industrial nations, its welfare bills will also multiply faster as its industries mature and its wage structure becomes top-heavy thanks to its seniority system.

In 1982 Japanese exports fell for the first time since 1955. According to the *Industrial Review of Japan / 1983,* published by Tokyo's leading business newspaper *(Nihon Kezai Shin bun):*

Foreign demand for Japan's mainstay export products has almost been filled and overseas inventories of these products have been piled up. It was no longer possible for the Japanese economy to fuel its growth via exports. Decreasing exports invited a decline in production which, in turn, resulted in a reduction in imports. This was compounded by increasing pressure from Western countries for Japan to open up its market or, failing that, to at least strengthen its voluntary export restrictions. As a result, exports have fallen and the domestic economy has been trapped in a vicious circle.

This "vicious circle" still has sustained a large trade surplus and the highest economic growth and lowest unemployment among-major industrial countries. If we were living in the 1930's, we might expect a peremptory Western response to cut off the Japanese exports that have been exploiting the weaknesses of Western industries. There indeed have been trade restrictions, but the restrictions have been themselves restricted by a delicate balancing of interests that reflects Japan's incorporation into an international system that has changed much over the past half-century.

Now as then, Japan is the largest overseas customer for U.S. exports, but the U.S. economy is much more dependent on exports today than it was a half-century ago. At the same time, Japan's two main markets and competitors in industrial exports, Germany and the United States, fearful of reviving the nightmare of the 1930's, are determined to maintain both free trade and their own home markets open to the degree permitted by domestic political constraints. Meanwhile, Japan itself has become a major exporter of capital as well as goods, with the Tokyo money market becoming the world's second-largest after Wall Street. Many foreign companies and governments raise funds there. Japan thus is following the historical path of the Dutch in the 18th century, Britain in the 19th, and the U.S. in the 20th, all of whom became capital exporters at the peak of their industrial ascendancy.

In this new role, Japan is cooperating intimately with banks and governments in other creditor-nations in attempts to manage today's international currency and debt difficulties. In addition, a fast-growing number of small and medium-sized Japanese companies have joined giants like Nissan and Matsushita (Panasonic-National) in investing in factories overseas. In some months of last year, investment income from abroad accounted for most of Japan's current international earnings. In this way the structure of Japan's balance of payments is changing from that of a developing country to something akin to Britain a century ago or the United States today.

Because of this change in Japan's balance-of-payments structure, many are beginning to see that Japan need not export as much as it does to sustain present living standards and, indeed, to retain a significant surplus for investment overseas. In 1981, the last year for which we have detailed statistics, three-fourths of Japan's imports ($109 billion) went to meet basic needs for food, fuel, and raw materials, about the same proportion as other industrial countries outside the lucky circle formed by resource-rich nations such as the United States, Canada, and Australia. In that year Japan exported $152 billion worth of goods, earning 40 percent more than its basic import needs.

One of the singular features of Japan's economic ascent over the past 130 years has been its intimate linkage with the United States. In the century that ended with the 1973 oil shock, Japan sent roughly one-third of its exports to the U.S., usually earning large trade surpluses. During the 1970's, however, Japan came to rely even more heavily on its growing trade surpluses with the U.S. to pay its way in the world economy, especially since the 1973 oil shock. While Japan's bilateral surpluses with the U.S. averaged only $1 billion yearly in 1970-76, they suddenly ballooned to $16.3 billion by 1981. Without this huge surplus with its biggest trading partner, Japan's international payments (including services) would be deeply in deficit.

Today, however, there is a growing awareness among Japanese (sharpened by the recent decline in oil prices) that large trade surpluses are not only becoming unnecessary for Japan but are also intolerable for its trading partners, and that Japan cannot continue to rely on expansion of the big U.S and European market to sustain its export and industries, in particular those large flagship companies that provide a minority of Japanese workers with guarantees of lifetime employment.

IN THE process of becoming more like us, the Japanese are finding themselves faced with the challenge of managing the same kinds of problems that also plague us. How they meet this challenge will be a fascinating and fateful story in the years immediately ahead. For the incorporation of Japan over the past century into what might be called the world system of capitalism and democracy has been the latest example of the recurrent mutual stimulation between distant cultural and industrial centers that is one of the most positive and painfully-sculpted features of human development.

We do not know whether it is still true, as *Fortune* observed a half-century ago, that "The Japanese can still get along without more things than any other industrial people." On the one hand, there is the huge increase in consumption of recent decades and the cost and welfare burdens imposed by tiny farms, tiny shops, and other inefficient economic units that have become net takers from the system. On the other hand, Japan over the centuries has shown a remarkable capacity to cut back consumption in different ways, from the practice of infanticide and abortion to maintain living standards in the 17th and 18th centuries, to its radical simplification of imported industrial machinery and processes early in this century, to its pathbreaking achievements in oil conservation in the 1970's. In its new role at the center of a much larger system, Japan now may either be trapped by its excesses or generate new ideas and patterns that could be very useful in insuring the continued vitality of capitalism and democracy not only in Japan itself but in the United States and the other Western countries as well.