

COMMUNICATION FROM JAPAN

The following communication, dated 2 October 2000, has been received from the Permanent Mission of Japan with the request that it be circulated to Members.

1. Introduction

It has been agreed that discussion at this year's Working Group meetings will focus in particular on the relation between competition policy and economic development. At present, around 80 countries have already instituted competition laws. Contrary to the perception in some quarters that competition and competition policy would not contribute to a significant degree in the initial stages of economic development, the Government of Japan believes that both competition and competition policy serve crucial roles in economic development, and that the establishment of competition laws and policies is essential for the economic development.

A view was expressed at the June 2000 meeting that the very high growth of the Japanese economy was facilitated by the "subordination" of competition policy to "industrial policy". In this paper, we draw on a number of cases to demonstrate that both industrial policy and competition policy has played a central and indeed synergetic role in Japan's economic development.

2. Development of Competition Environment in the Post-War Period

A key point in considering the relation between Japan's industrial policy and competition policy is that the competition authority (the Japan Fair Trade Commission) was established from the initial stage of economic development. The Fair Trade Commission faithfully enforced competition policy, holding consultations, where necessary, with the Ministry of International Trade and Industry (MITI) as the main body in charge of industrial policy, and exercising considerable influence on industrial policy and industry trends from a competition policy viewpoint. If Japan had not instituted competition laws and policies from such an early stage, the development of the Japanese economy to date would have been extremely difficult to achieve.

Between 1946 and 1949, Japan's *zaibatsu* were dissolved and a number of monopoly companies broken up. More specifically, ten *zaibatsu* disappeared and 18 companies were reorganized, while 1947 saw the formulation of the Anti-Monopoly Act (Act concerning the Prohibition of Private Monopoly and Maintenance of Fair Trade), modelled on the US Anti-Trust Act. These measures provided a basic framework for competition, and also laid the foundations for very vigorous competition among business.

3. Economic Growth led by Competition Among Business

It should first of all be noted that Japan's post-war economic growth was the result of flourishing domestic demand encouraging plant and equipment investment and technological advance, boosting corporate competitiveness and creating very intense competition among business. This private sector dynamism proved to be a key factor behind economic growth.¹

Post-war Japan saw the development of many new industries, and many of these met with success as export companies. Initially, they produced sewing machines, cameras, motorcycles, pianos, zippers, and transistor radios, which were overtaken as of the mid-1960s by colour televisions, tape recorders, magnetic tapes, sound equipment, fishing equipment, watches, calculators, power lines, machine tools, NC machine tools, textile machinery farm machinery, insulators, communications equipment, ceramics, robots, etc. Companies in such growth industries were typically launched from zero in the post-war years or as extremely minor-scale enterprises, and developed on their own efforts without the assistance of any particular preferential measures. Their management would object strongly to the view of Japanese industrial policy as a powerful, systematic and universal force.²

The following two cases exemplify the way in which private sector dynamism laid the foundations for industrial development.

In the petrochemical industry, MITI raised the standard for establishing ethylene center to a high 300,000-ton annual production rate in 1967 as a means of restraining intense intra-industry competition and developing the industry through economies of scale. However, this did not prevent the entry of a succession of new players meeting the standards for new center establishment in terms of technology, market creation and fund procurement, with the original nine companies expanding to 17. The petrochemical industry is a typical process industry and is characterized by substantial scale merit and units of investment, as well as a relatively rigid production volume. Therefore there was concern that an over-proliferation of companies could unnecessarily exacerbate market confusion during economic downswings. MITI sought to prevent this by setting standards for the establishment of an ethylene center. But as the petrochemical industry developed, the entry of new players spurred the emergence of a competitive market even as plant scale surged, and the resulting multiplier effect pushed prices into a steep decline. The consequent market boom attracted more new entrants, while economies of scale reduced costs and expanded the market yet further, a virtuous cycle which set the petrochemical industry on a strong growth trajectory. Thus, the growth of the chemical industry was achieved based on the competition induced by the entry of a string of new market players.³

In the case of the automobile industry, the epitome of Japan's strong economic growth, the number of auto manufacturers was viewed as too great to withstand international competition, prompting the government to issue guidelines on the fostering of domestic vehicles in 1955, followed by the "three-group" initiative of 1962, in an attempt to concentrate the industry through mergers and groupings. However, the auto industry resisted these efforts, choosing a competitive market over industrial policy. The result was the emergence of a number of companies boasting world-class international competitiveness. A typical example was the participation by Honda, a motorcycle manufacturer, into car production. Overriding government opposition to the entry in the car market in 1963, Honda worked steadily on R&D and other strategies in order to compete with existing players. As a result of their effort, Honda grew so rapidly as to achieve the coup of having the small passenger Civic, launched in 1972, chosen as 'Car of the Year' from 1972 through 1974 in Japan and in 1972 in the United States.⁴ As from 1966, nine companies have been vying against each other in passenger

¹ NAKAMURA (1993).

² KOMIYA (1994).

³ KOMIYA (1994).

⁴ ITAMI (1988).

vehicle production, with this fierce competition contributing significantly to the development of the car industry and the fostering of competitiveness.

4. Roles played by Industrial Policy

Private sector dynamism has therefore served as a driving force behind Japan's rapid economic growth, and it would be erroneous to attribute Japan's post-war economic growth to competition-restricting industrial policy. Far from distorting the operation of market mechanisms, the ultimate goal of Japan's industrial policy has been to complement and facilitate competition.

A typical case is the R&D support provided to strengthen competitiveness. Technological advance has played an enormous role in the strong growth of the Japanese economy and the changes in industrial structure which have occurred along the way. This progress was spurred by rapid demand expansion, high rates of plant and equipment investment, and fierce inter-corporate competition, which in turn led companies to vigorously pursue R&D and the introduction of new technology. The private sector took the forefront in R&D efforts, with the government playing a supporting role by developing assistance schemes which included subsidies, tax breaks, and low-interest financing provided by government financial institutions.

However, there was fear that short-term economic downswings or the deterioration of the export environment which allowed no time for structural shifts could bring about heavy demand slumps and trigger a chain of corporate collapses not only in specific markets but also in related industries. In view of this fact, the government has on occasions, sought to forestall such economic chaos through adjustment measures such as temporary production restrictions (hence the anti-recession cartels provided for under the Anti-Monopoly Law). In particular, the government has been known to take special measures for small and medium enterprises (SMEs), which are disadvantaged in terms of management and fund procurement capacity, and therefore more vulnerable to changes in the economic environment. There are clear provisions for such special treatment in response to special cases written into the Anti-Monopoly Law and the various special laws. Furthermore, strict stipulations are made as to the conditions under which competition-restraining measures can be applied - namely, on a provisional basis and only to ensure fair competition in domestic markets, never as a means for excessive protection. Such principles have been strictly followed in the case of adoption of the exemption of the Anti-Monopoly Act for the SMEs as emergency evacuation measures in economic downswings.

Further, where specific industries lose their structural competitiveness and an industrial conversion must be undertaken, policies are sometimes needed to promote the redistribution of production factors and ensure the smooth disposal of facilities and labour transfers. There have been a number of such instances in Japanese history. When the coal-mining industry declined in the 1960s, certain policies were instituted to assist an employment shift and local development. The Bill of Temporary Measures for Stabilizing Specified Depressed Industries, which was formulated in 1978 and abolished in 1983, provided for three types of policies: a basic plan of stabilization, a depression fund, and directions for concerted action. The first industry to be designated under this law was aluminum refining. Its surplus plants and equipment were made out of operation or abolished in line with the basic plan of stabilization adopted in 1978.⁵

5. Roles played by Competition Policy

The two elements which ensured the adequate consideration of competition in developing industrial policy have been, naturally enough, competition law and the existence of the Fair Trade Commission (which administers this law). The Fair Trade Commission not only polices

⁵ TANAKA (1984), SEKIGUCHI and HORIUCHI (1984).

anti-competitive practices, but has also exercised its influence on industrial policy as well as on opinions of business circles from a competition policy perspective and thereby has created and ensured competition in industries.

This role was epitomized in the 1969 merger of two steel manufacturers, Yawata and Fuji, which held first and second place respectively in the industry. In terms of fostering the industry, the presence of leading companies was considered important to the sound development of the steel industry with its rapidly changing market conditions. However, the Fair Trade Commission judged that there was a fear that this merger could restrict effective competition in the steel industry and made a recommendation to ask them to call off the merger plan. As a result, the original plan was forced to make major adjustments. For example, the railroad rail production, which would virtually have become a monopoly under the original merger conditions, was completely split off and certain other facilities, stockholdings and technology were transferred to rival companies. Agreement was therefore reached at the point where competition policy considerations and industrial policy demands concurred. Since that time, companies have been battling to produce new products and develop new markets in the competitive climate of the steel industry; Sumitomo Metal Industries, for example, has built up a specialty in seamless pipes, Kawasaki Steel in steel plate - with international competitiveness improving across the industry as a whole.

While the Fair Trade Commission ensures appropriate enforcement of the law from a competition policy perspective, a system of exemptions of the Anti-Monopoly Act has also been established for specific activities in order to achieve certain economic policy goals. For example, as noted above in the context of the roles of industrial policy, where the majority of businesses in a certain industry are no longer able to continue operating, cartels have been allowed as an emergency means (Article 24.3). However, rigorous provisions are laid down as to the application of the system and operation is restricted, including limitations on the permitted duration of actual operation (in principle three months).⁶ Moreover, there were in fact very few anti-recession cartels. (The anti-recession cartel system was abolished in 1999 under the Omnibus Act to Repeal and Reform Cartels and other Systems exempted from the Application of the Antimonopoly Act under Various Laws.)

In terms of the operation of cartels based on special laws such as the Small Business Corporation Law, MITI and the Fair Trade Commission have engaged in detailed consultations on whether the case meets the necessary requirements and whether the duration of application is appropriate. Where economic conditions improve while a cartel is still in operation, immediate consultations are also held to review.

Anti-recession cartels and production adjustment cartels for small and medium enterprises, as well as concerted action to dispose of excess plants and equipment as part of industrial conversion are mainly advocated by MITI. However, requirements for such cartels are stringent, and detailed consultations held between MITI and the Fair Trade Commission ensure necessary competition policy viewpoints. As the views of the competition authorities define the cartel operation, cartels are never left to go indiscreetly. Given that SME cartels in particular have also fostered SME competitiveness within an appropriate range, it can be viewed as having stimulated competition across the market.

6. Conclusion

As is evident from the above, the competition policy introduced by Occupation Forces immediately after the war contributed significantly to the postwar economic development of Japan. One feature of the postwar Japanese economy has been the sheer intensity of intra-industry competition, with rivalry among companies maintained and strengthened as a basic trend, creating

⁶ SANEKATA(1987,1992).

favorable market mechanisms. The development of an environment conducive to free and fair competition among private enterprises as a result of both the tension and synergy which exists between industrial policy and competition policy has therefore been a major factor in Japan's rapid economic growth. According to the experience of Japan, it would be important to introduce appropriate competition policy at the early stage of development while taking necessary measures from the viewpoint of industrial policy in order to achieve the economic growth.

On the other hand, the development of e-commerce and similar trends promise even greater economic integration across borders in the years to come. It will, in turn, prompt the emergence of Internet industries and other increasing-returns industries as well as more mergers among major multinationals. At the same time, there might be increasing cases of anti-competitive practices that affect several markets. Such trends are likely to impact heavily on developing economies. In this sense, development and improvement of basic frameworks for competition laws and policies has become an ever more important task for developing countries for realizing stable economic development.

While industrial policies can certainly be utilized where necessary to respond to these new challenges, developing competition laws and policies will allow countries to provide competitive conditions, ensuring the sound development of domestic industry and restricting the abuses of dominant position of large companies including multinationals. The outcome of such efforts will be greater international competitiveness for the domestic industries.
