

# National Foundation for American Policy

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## **New Research Finds Japanese Industrial Policy Was Not An Economic Success**

### **Industrial Policy In Japan Did Not Raise Productivity Growth In The Technologically Advanced Parts Of The Economy**

**Arlington, Va.** – Industrial policy in Japan was not successful and was not responsible for the country’s economic achievements in the post-war era or the international performance of leading sectors, including autos and electrical machinery, according to [new research](#) from the National Foundation for American Policy (NFAP), a nonpartisan policy research organization.

“There is no evidence that industrial policies raised productivity growth among the more rapidly growing or technologically advanced parts of the Japanese economy between 1955 and 1990 when industrial policy was utilized in Japan, raising doubts that industrial policy would be effective today in other countries,” concluded the study’s author, Richard Beason, a Professor of Business at the University of Alberta and a leading expert on Japanese economic policy.

“Overall, Japanese industrial policy did not succeed in producing economic results and was ultimately abandoned by the Japanese government,” according to Beason, who is the author of two books and more than two dozen journal articles on the Japanese economy, with a particular focus on Japanese industrial policy.

Japan discontinued industrial policy targeting, starting in the 1990’s, due to a growing consensus that such policies were unsuccessful, pressure from the United States and growing budgetary pressures on the government from the 1990’s onward as economic growth stagnated.

The study, “Japanese Industrial Policy: An Economic Assessment,” can be found at <https://nfap.com/>.

There is no evidence to support the claim that Japanese industrial policy during the 1955-1990 period enhanced growth rates by sector, industries with economies of scale (greater efficiency when produced in increased amounts), productivity growth or competitiveness. “The reality of the political process and government spending priorities makes it very difficult for such policies to be effective,” according to the report. “Furthermore, even if political pressures had not intervened, it seems questionable to suggest that government policymakers would be better than actual market participants in determining the most efficient allocation of resources to produce the best economic outcomes.”

Among the key findings of this research:

- The industries that we associate with Japan during the high growth period, electrical machinery (most of the “tech” sector), general machinery (most capital goods industries) and the transportation equipment sector (which includes autos) were generally toward the bottom in terms of government support between 1955 and 1990. What these and other sectors received in quantifiable public policy was largely unrelated to growth or productivity

growth, and government policy acted as an impediment to the more rapidly growing sectors because such sectors had higher rates of effective taxation than the slow growers. This result arises from two facts: Actual resources are allocated according to the political preferences of lawmakers, and actual patterns of growth and productivity during the period were largely determined by market forces. That the policies might have affected the product mix and possibly harmed consumer welfare as a consequence is difficult to measure but quite likely. However, this was not the desired result of policymakers, and certainly not what is claimed by industrial policy supporters.

- Even during its zenith, industrial policy in Japan was not executed in a way that favored the rapidly growing sectors.
- The data show industrial policy tools were disproportionately allocated to the slower-growing industries. Governments in most countries provide some support to virtually every industry, rapid and slow growers alike. Slower-growing industries are likely to be more active in securing government funds, and some of the slow growers are likely to be situated in certain geographic regions, and politicians from those regions have an incentive to push for more government funding for those industries.
- While many advocates attributed rapid growth among the leading industries to Japanese industrial policy policies, the problem with such analyses is they ignore that both “winners” and “losers” were the beneficiaries of such policies. A breakdown of the government-sponsored benefits by industry is necessary to determine whether the “winners” actually benefitted disproportionately from such policies. Policies that benefit all industries cannot correctly be described as “industrial policy,” nor can the usual “pork-barrel” style policies that benefit the losers in politically sensitive regions or declining industries be described as industrial policies designed to promote high growth or high productivity sectors.
- To address the issue of the actual allocation of government policy by sector, we identified quantifiable policy measures undertaken by the Japanese government at the time and considered the relationship of these policy measures growth rates by sector. While various measures might be used by governments to promote some industrial sectors relative to others, the key (and quantifiable) measures of industrial policy used by the Japanese government during the 1955-1990 period included 1) subsidized government loans to industry, 2) subsidies, 3) tariff protection and 4) tax relief.
- The actual distribution of industrial policy tools was the outcome of the political process such that implementation in Japan was unfocused and arbitrary. The data show it was often the case that an industry might benefit disproportionately in terms of some measures but not others. Mining, for example, was the number one recipient of cheap loans, government subsidies and tax relief for the 1955-1990 period, undoubtedly because it was such a slow grower and employment in the sector was concentrated in particular geographic regions (where unemployment in the sector would have been politically problematic). However, it received the least amount of tariff protection. Japan is a resource-poor country, and high tariffs on mining products would have crippled other industries.
- Other than the mining example, however, the distribution of these policy tools was arbitrary and inconsistent. Not at all what we would expect if the Japanese government had been dispassionately executing growth-oriented industrial policies. However, it is what one would expect if political pressure and political maneuvering actually determined the distribution of government policies toward industry. It should not be surprising that the allocation of industrial policy tools was the result of the political process and not purely in line with the policy prescriptions of the then Ministry of International Trade and Industry (MITI). Indeed, it seems highly unlikely that the actual allocation of industrial policy tools

would have been apolitical, even though many advocates of industrial policy at the time argued the allocation was apolitical.

- There seems to be no evidence that Japanese policy was aimed at promoting industries exhibiting economies of scale. Industrial policy advocates of the 1970's through 1990's seldom, if ever, mentioned this or other policy goals. On the issue of promoting scale economies, the correlation coefficients between estimated scale parameters and policy tools by period show most of the measured coefficients are negative, and those that are positive are very small.
- Industrial policy tools generally also had no positive and significant impact on productivity growth ("competitiveness") for the various sub-periods from 1955 to 1990. One exception to this finding is for Japanese Development Bank loans, though the impact on productivity growth is small. Furthermore, this very small positive impact of JDB loans on productivity growth was driven by one sector alone: mining. Mining was a declining and economically insignificant sector, but it was politically significant and was undergoing mechanization and downsizing of the labor force during the period. Overall, Japanese industrial policy did not enhance the competitiveness of key sectors during the period.
- There is no evidence that any help to declining industries via industrial policies allowed those industries to achieve long-term success. Declining industries, such as textiles and mining, were previously heavily supported in Japan. Mining and textiles were the two slowest growing sectors over the period 1955-1990 in Japan but were the number one and three largest recipients, respectively, of government subsidies during the period for the 13 primary two-digit industries under the Japanese industrial classification system. In general, the four types of policy tools (JDB [Japanese Development Bank] loans, government net subsidies, tariff protection and taxation) were more favorably geared toward the slower-growing sectors, though the application of the tools appears to be generally unsystematic. Application of the tools of industrial policy does not appear to follow the pattern suggested by proponents of the statist view of Japanese economic development during the period (i.e., the view that economic growth was the result of government industrial policies).
- The two sectors that received so many resources during the high growth period, mining and textiles, have gradually faded into insignificance since such policies were unwound during the 1990's. The trade surplus in textiles was \$1.13 billion in 1970. It steadily moved into deficit from the mid-1980's, reaching a deficit of \$28.4 billion in 2016. Similarly, employment in the sector eroded from 719,814 in 1985 to just 109,064 in 2011. When it comes to the mining sector, it is difficult to understand why so many public resources were dedicated to promoting such an uneconomic sector. Employment in the mining sector was less than 20,000 persons in 2020.
- Japanese policymakers did not experiment with strategic trade policies. Strategic trade policies would include identifying industries that are experiencing economies of scale (greater efficiency), then protecting those industries from imports while they achieve scale and subsidizing exports so to achieve economies of scale in foreign markets as well. Not only is there is no evidence that Japan ever engaged in such policies but most of the discussion centered on the use of such policies *against* Japan, especially in autos trade.

Japanese industrial policy lies essentially dormant as a "positive example" of industrial policy measures, according to the study. Policymakers in Japan abandoned industrial policy because such policies were unsuccessful, the public finance resources needed for such a policy eroded and international relations mitigated against it. However, the emergence of China and Japan's declining semiconductor sector has changed that, and industrial policy, at least with respect to semiconductors, has gained renewed interest in Japan. That renewed interest does not change the historical economic record: Industrial policy in Japan was not successful and was not responsible

for the country's economic success in the post-war era or the international performance of leading sectors, including autos and electrical machinery.

**About the National Foundation for American Policy**

Established in 2003, the National Foundation for American Policy (NFAP) is a 501(c)(3) non-profit, non-partisan public policy research organization based in Arlington, Virginia focusing on trade, immigration and related issues. The Advisory Board members include Columbia University economist Jagdish Bhagwati, Ohio University economist Richard Vedder, Cornell Law School professor Stephen W. Yale-Loehr and former INS Commissioner James W. Ziglar. Over the past 24 months, NFAP's research has been written about in the *Wall Street Journal*, the *New York Times*, the *Washington Post* and other major media outlets. The organization's reports can be found at [www.nfap.com](http://www.nfap.com). Twitter: [@NFAPResearch](https://twitter.com/NFAPResearch)

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