

On the Occasion of Faculty's 10th Anniversary

Economics Nobel Prize, Institutional Economics and Japanese Experiences

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Introduction

As a creditor country, England was the "Mecca" for modern economics and the world economy before the Second World War until the cost of financing the War forced it to sell most of its foreign assets to the U.S. government. After that war, its special significance was transferred to United States, which was practically untouched by the war. This transfer occurred because there is a strong relation between the centrality of an economy in the world context and the advances in the field of economics in that country.

When England was the leader of the world economy, her economy flourished because she was industrially a pioneer with all advantages at hand, and without any significant competitors in the world market. England also had foreign assets equal to almost 150 percent of its GDP in places such as the United States, Latin America, Australia, South Africa, India and other countries in the empire. The investment income from these assets encouraged England to adhere to free trade policies.¹ Therefore, the science of economics which by its very nature is rooted in nationalism helped solve her problems. Free trade was good because it was good for Great Britain not because it was good for the world.² Consequently, these solutions were considered the best remedy for the capitalist world and finally for the world economy and the Nobel Prize for economics was received mostly by those advocating these economic principles.

The global British eco-political domain was weakened by the war. America was the

successor of this heritage. Thus, solving the economic problems of America was considered to be solving problems not only for the other advanced capitalist economies, but also those of developing economies as well. The current normal science paradigm in orthodox economic thought emerged and was theorized after the Second World War by Neo-classical economists in the United States.

Today the global economic scene has changed. Japan's economy, in spite of its recent slow recovery situation, has proved very successful in the past few decades. What are some of the indicators of Japan's successful economy? Statistics answer: Japan's nearly \$100 billion trade surplus; 200 billion foreign currency reserve; \$500 billion foreign investment; the world's largest capital exporter; more than \$600 billion foreign net assets; the world's number one creditor and ODA supplier for five continuous years (15 billion in 1995); the biggest enterprises in term of annual sales in the world with \$184.4 billion in 1995 (but 284th in term of profit maximizing); the world's top 10 banks and even distribution of income. Why, then, has no Japanese scholar ever won the Nobel Prize for economics?

The simple answer is that Japan has still not become a "global pole" on the contemporary economic scene. Solving Japan's economic problems, with various national and institutional characteristics (which most Japanese economists take into account), it is considered, will not help solve the Anglo-Saxon capitalist world's problems. Addressing the economic problems of Japan has, on the other hand, been helpful as a catch-up or "developmental market economy" model for many non-western developing economies, especially in Asia.

On the other hand, a country may win several Nobel Prizes for Economics, while its real economy in spite of recent records fails, the country sustains huge deficits (current account deficits of \$150 billion to \$200 billion per annum and net international investment deficit exceeding 10 percent of GDP),³ and remaining the number one net debtor in the world with increasing expansion of income gap. The Noble Prize for Economics was established in 1969, and 40 prizes have so far (1996) been awarded, among which 25 have gone to American economists—more than 62 percent of the winners. Americans have also harvested many Nobel Prizes in natural science and rank higher than Germany, France, and Japan in this field. Yet, America's nobel prize winnings in natural science are fewer than its economics prizes.

A glance at the statistics from the pre-Second World War era up to the present day reveals that 20 scientists from only one British research institute have won Nobel Prizes. This exceptional experience demonstrates the general development of basic science in England. Yet the British stand second to Americans in economics with 4 prizes, Sweden and Norway with 2 each, France, Holland, the ex-Soviet Union and Canada with one for each. Even more astonishingly, the Germans, despite their strong economy and industrial strength got the Economics Nobel Prize for the first time last year (1995) and Japanese economists have never received the prize.

The example of these two countries (Germany and Japan) suffices to demonstrate that the Nobel Prize in economics is not necessary for economic and industrial development.

Conversely, the purpose of economics is not winning the Nobel Prize, but in sustaining economic development and solving real economic problems.

The factors involved in economic development differ depending on historical and institutional environments. The fundamental economic philosophy and various cultural phenomena should be taken into account when studying any given economy. Economic thought, households or firms behavior may have complementary or substitutional relationships with public or private capital accumulation and production, which are the fundamental factors in the economic development process.

One of the basic principles of economics is that the greater the differences between the current amount of output and the smallest amount needed for consumption, the more numerous the available courses of action for development of an economy and the easier it will be to achieve a wide range of industrial growth. Therefore, economic thought and behavior, (regarding production, consumption, profit, work habits) of a given household, firm, and state in this respect are highly important.

Art is also culture-bound (bound by ethnicity), yet it is appreciated and understood anywhere in the world, despite its original setting. Japanese *Kabuki*, *Noh*, *Ikebana*, Japanese garden style, and tea ceremony are relevant examples. Without nationality or localism, the emphasis on specific culture is impossible.

The natural sciences, on the other hand, are culture-free (not bound by ethnicity). Therefore, duplication and practical application of pure theory are relatively easy. But a real economy that is subject to economics which is theorized under a different set of social and value premises, unlike the natural sciences, is both nationally-bound and uncopiable in some of its dimensions.

The world appreciates and even duplicates Japanese arts, and culture, but they hate Japanese practices of *Keiretsu*, *Dango*, *Sogo Mochiai Kabushiki*, (mutual stock holding), *Shushin koyo* (the permanent employment) system, *Genchi seisanshugi* (adherence to localism in production), and so on. This is typical of the arguments against "the Japanese system" used by such so-called "revisionists" as Fallows,⁴ Johnson⁵, Prestowitz,⁶ and von Wolfen.⁷

During the cold war period, capitalist economies used to emphasize the liberal market economy as a unique system universal all over the world. But these days, there are many articles and books regarding the diverse aspects of market economies. "Capitalisme conter Capitalisme,"⁸ "Japan: the Pure Capitalism System,"⁹ "Capitalism, The Age of Cultural Clash,"¹⁰ "Look over Smith's Spirit Again,"¹¹ "Head to Head: The Coming Economic Battle Among Japan, Europe, and America"¹², "The Myth of Free Trade: A Plan for America's Economic Revival"¹³, and "Beyond Capitalism"¹⁴, are among the volumes which echo this theme. This means that the United States, England, Germany, France, Japan and other Western economies are all market-oriented economies, but each has its own specific characteristics. Thus it is not strange to say that their economies are culture-bound, with strong aspects of nationality. Of course these nationalities have some aspects of universality. Therefore, universality and a nation's economically unique aspects should be considered

and dealt with, especially during the early stages of the development process.

1 The Differences Between the Capitalist Economies: United States, Japan, Germany, and East Asian Countries

We all remember the embezzlement scandal in the Japanese stock market which started a wave of heated controversy a few years ago. The story in brief:

Some of the customers were remunerated by the stock companies for money lost due to the fall of the share values.¹⁵ Americans as well as Fulbright graduates in Japan denounced the act, calling it “the insider scandal deal.”¹⁶

It is true that using company secrets for those who have easy access to them in order to gain more money or escape from loss probabilities is unjustifiable. Yet, institutional variation must also be kept in mind. For instance, in Germany, unlike the United States, banks are closely integrated with the stock market. German banks sell shares and, as in Japan (but unlike England) they are in charge of allocating long-term financial support to companies.

This is exactly why these banks often have current and precise information about companies' inner advice and research programs. Banks feel, also, responsibility toward their own depositors. Since the banks in Germany are in charge of stock business, and like Japan provide long-term loans to companies, their business practices can also be labelled “insider transaction,” as the case was called in Japan.

Those in favor of American-style capitalism, which does not supply long-term loans to private companies, and which separates stock transaction from the banking system, denounce these two countries. Japan, on the other hand, with its increasing confidence, considers herself a true capitalist system and even calls for world economists to apply Japan's approach elsewhere. Eisuke Sakakibara, for example, the director general of MITI's International Finance Bureau, believes that Japan should be more assertive in promoting its form of capitalism over the Anglo-Saxon alternative.¹⁷ On the other hand, the Tokyo High Court upheld a Tokyo District Court decision that Nomura Securities' compensation of clients' investment losses, while a violation of the law, was carried out within the bounds of management obligations. The judge said the Nomura executives made the payments to maintain business relations with clients and to prevent damage and therefore they did not overstep their discretionary framework or renege on their managerial obligation.¹⁸

Historically speaking, the London Stock Market existed prior to the establishment of banks in England. At the time in Japan and Germany, in these then industrially under-developed countries, the banks, which were government owned, were used to back industries with long-term and low interest loans. This was seen as an indispensable element in any effective catch-up model. This is the “developmental market economy” strategy (in contrast to a liberal market economy) which led to Japan and Germany's industrial strength and economical achievement. Therefore, it can be said that economic development based on financial structure has some universality, at least regarding Japan and Germany,

which relevant economics has not yet theorized.

In most recent experiences, many East Asian countries, which according to a World Bank report are producing “miracles,” are incorporating many Japanese-style policies and other measures into their national economic management according to their social environments. According to the World Bank report, the success of the East Asian economies stems partly from the policies that were adopted by their governments, and partly from the institutional mechanisms they created to implement them.¹⁹ This means that East Asian Countries’ economic practices should be considered in the framework of new modern economics. Therefore, the diversity of experiences and institutions, and the great variation in policies means that there is *no single market economic model* for success.

2 Modern Economics and the Generation Gap among Japanese Economists

Current modern economics, which has developed from Western culture and ethics and contributed to the science of economics, has many aspects of universality. But this kind of economics is based on 19th century academics and does not consider specific nations and the reality of their economies according to time and particular stage of development. From Adam Smith to Keynes, economics was concerned with the problems of a certain country and the reality of its economy; England was the primary case study.

Universal economics tends to be constructed purely in mathematical terms. This kind of economics grew more and more in the post-war era in the United States, and some young Japanese economists were naturally attracted to it. Interestingly, these economists often emigrated to the United States, because there was less demand for their services in Japan than in America. They now teach in American universities.

When we look to the preceding generation of Japanese economists, we find that the first generation of post-war Japanese economists were educated before or during the war and were deeply influenced by the German historical school of economics (especially List’s²⁰ thesis of infant-industry protection),²¹ by non-communist Marxism, and by the ideas of neo-mercantalism. They found that late-coming Germany had managed to catch up with England as early as the 1870s in the area of heavy and chemical industries. This strategy was geared to accelerating capital accumulation and economic growth by suppressing consumption, by means of government finance and border protection, within the basic framework of market economies. The major figures from this generation were Hiromi Arisawa, the pioneer of “*Keisha Seisan Hoshiki*” (Priority Production System); during the reconstruction and stabilization period in Japan, Ichiro Nakayama and Shigeto Tsuru, who were responsible for the compilation of the first economic report on Japan in the *Keizai Antei Bu* (Committee of Economic Stabilization) after the war. This committee report is considered to be the first edition of today’s Annual *Tsusun Hyakusho* (Economic White Paper) of Japan.²²

All of these economists served as high government advisers on economic policy after World War II, until about 1965, just 3 years before Japan became the number two economy

in the capitalist world. Japan's industrial policy, implemented primarily by MITI, was based on ideological and institutional ground work laid by this generation. It means that critical Japanese post-war reconstruction economic policy and its "miracle" high growth rate was unaffected by the micro-and macro-economic theories that dominate the international academic scene today; theories and guidelines developing countries are forced to obey if they need World Bank assistance (for example SAL; Structural Adjustment Loan).

The first generation economists in Japan believed that government must exercise strong leadership, formulate plans, and guide and regulate the activities of private sector across the whole gamut of industrial activities. Most of them had little regard for, and less understanding of antimonopoly policies aimed at promoting competition.²³ According to William Lockwood,²⁴ this historical school of economics was even the basis for the establishment of faculties of Economics in Japanese universities.

The ideology of second generation economists like Ryutaro Komiya, Ryuichiro Tachi, Masao Baba and Hisao Kanamori, Komiya writes, was based on microeconomics, particularly general equilibrium theory, welfare economics, and industrial organization economics, developed mainly in United States.²⁵ This generation had much less influence on the operating branches of the Japanese government, although they did have an intellectual impact on the Economic Planning Agency. According to Ryutaro Komiya, one of the most influential academic economists, the propositions of welfare economics, to which second generation economists have addressed themselves (including Komiya himself) have had little to do with the realities of the Japanese economy.²⁶

Unlike the second generation, which believed that the markets of the Japanese economy function well on the whole, the third generation assumes that market failure occurs frequently.²⁷ This new generation is more interested than its predecessor in models of oligopoly and hence on how industrial policy works in advanced capitalist economies.

3 The Importance of Institutional Economics and Japanese Experiences

The importance of this trend is that the study of institutional aspects of Japanese economy and industrial policy is an exercise in economic science. But Nobel laureate Milton Friedman, talking on national television about Japan's achievement of global hegemony in the production of semiconductors in the late 1980's, asserted "the image of the Japanese having had an industrial policy which explains their success is a myth. The fact of the matter is that the most successful components of Japanese development proceeded against the advice of the government."²⁸ Friedman does not read Japanese and has made no study of the Japanese economy. He does not have to because he is speaking as one of the world's most eminent economic theorists. Those, like Friedman, who believe that Japan does not have an industrial policy, or who critique institutions used in the Japanese economy just because of its incompatibility with modern economics theory, or says that its industrial policy differs little from that of, for example, the United States, have only managed to cloud the history of Japanese economic development and to prevent others from understand-

ing the real nature and dimensions of the Japanese economy.²⁹

Members of the senior economics faculty of the West prefer to study theory; and they warn members of their department not to undertake applied or comparative research, since it might reveal the large number of anomalies that have developed in neoclassical oriented theory. For example, the Western economic theory of labor as a separate input into production and of the free-flowing labor market external to the firm clearly is irrelevant to Japan. It cannot explain why Japanese managers have been more interested in internal labor markets, in "human capital," and in measures to retain such human capital within the firm in spite of recent slow recovery situation. Another anomaly concerns Japan's failure to transfer saving and other financial resource allocation via capital markets. "There were no markets for either corporate or government short-term securities, the sale of corporate bonds within Japan was prohibited, and the MOF (Ministry of Finance) encouraged financial resource allocation through the banking system rather than capital markets."³⁰

Moreover, these Japanese practices are increasingly cited as one of Japan's most effective competitive innovations. As Peter Drucker concluded, Japan's economic success since World War II, has largely rested on its having been the only country that had both the low labor costs of a developing nation and the high labor productivity of a fully developed one³¹. It also seems that the world today is moving in Japan's direction and away from uncontrollable labor markets to fill skill needs. Especially in knowledge-intensive production, the cost of the hardware is only a fraction of the total investment in skilled personnel and effective institutions to make the system work. It is Japan's favorable balance of skill,...a highly educated, skilled, adaptable, flexible, and innovative and disciplined work force, that makes it more likely to master the knowledge-industries than many of the nations that invented them.³²

The sources of Japanese economic growth have been studied by many scholars. The important issue of the role of the "residual" among the components of the Japan's economic growth has been addressed by Ohkawa and Rosovsky, among others. Their analysis follows the conventional approach, which specifies capital and labor as principal inputs into the productive process and then attempts to identify the effect on national product of changes in input. For 1955 to 1964, this method of calculation attributes approximately one-third of the growth rate of "output" to increments of capital, one-third to increments of labor, and one-third to the residual, the last constituting "a measure of our ignorance."³³

In another elaborate analysis of the sources of Japan's economic growth, Denison and Chung likewise attempt to calculate the residual.³⁴ Their procedure is to identify the determinants of growth in as fine detail as they can and evaluate the respective contributions each. They specify the following: Input of land, labor, and capital; and changes of output per unit due to improved resource allocation, economies of scale, irregular factors, and "advances in knowledge and n.e.c. [not elsewhere classified] items," the last calculated as a residual. With the exception of the residual, these in turn are broken down into subcategories. They find that the most important source of growth of national income was increase in capital, which contributed 26.9 percent of growth rate during 1961-1971. Of almost equal

importance was the residual factor which accounted for 25.4 percent.

These results are more or less consistent with the Ohkawa-Rosovsky residual: Both are very large. The Denison-Chung calculations are interesting because, instead of declining, their residual rises steadily during 1952-71.³⁶ This conflicts with the observed progressive exhaustion of the "catching up" process as well as with the chronology of the application of domestic wartime production advances to civilian output after the war. In my opinion, what substantially accounts for the remarkably high value of the unexplained residual in these two major studies is the neglect of Japanese institutional and cultural factors, which were excluded from the analysis.

These institutional factors were actually the major sources of the growth for more than 100 years in total productivity. For example the importance of institutional aspects of agricultural development in Japan can be attributed to 1) evolution during the Tokugawa period, especially Kokusan economic policy (encouragement of local production); 2) economic thought and philosophy of Meiji government; 3) land tax revision; 4) early effort toward agricultural improvement; the dominant sector of the economy, by the developmental state of Meiji; 5) farmers' initiative and cooperatives, (*Gono*,³⁶ *Nodankai*,³⁷ *Hinshukokankai*,³⁸ *Rono*,³⁹ *Dai Nippon Nokai*⁴⁰); and 6) agricultural experimental stations. According to the Hayami and others, "The growth in agricultural output and productivity began to accelerate at the beginning of this century. The reason should be sought in the existence of indigenous technological potential that could be further tested, developed, and refined at the new experiment stations, combined with a strong aspiration among farmers to innovate."⁴¹

Uniformity of technological progress among farmers is one of the most important factors in total productivity. In this respect, "1) the emerging effects of comprehensive agricultural extension work, begun in 1949 and continuously carried out since, and 2) the wide practice of cooperative works, such as rice cultivation and rice protection activities, which have facilitated the exchange of technology among farmers, has played an important role in this homogeneity in Saga Prefecture."⁴²

Of course the "residual" contains factors other than technological progress. Quality of labor and capital are among them. Unfortunately, because of difficulties in quantifying quality we cannot obtain independent estimates of the importance of changes in the quality of labor and capital over time. But it should be remembered that the social capability to absorb modern technology which contributes to the quality of labor and capital is of high importance. The availability of unexploited technology in itself does not, of course, guarantee the emergence of a modern economy. As Kuznets pointed out, it is necessary to have the capability to absorb new technology.⁴³ The successful introduction of western technology and its contribution to economic development of Japan can be understood only through the study of this capability.

Japan's capability to absorb modern technologies resulted from a number of cultural and institutional factors. Morishima shows how a strongly-held national ethos has interacted with religious, social and technological ideas imported from elsewhere to produce highly

distinctive cultural traits.⁴⁴ In terms of human resources, engineers are very important.⁴⁵ At the beginning of industrialization, and the policy of encouragement of local industry (*Shokusan Kogyo*), Japanese industry needed some foreign engineers (*Yatoi Gaikokujin*) as live learning machines. But Japan is different in two ways. First of all Japan relied far less than European countries on the skills, knowledge, and enterprise of foreigners.⁴⁶ Secondly, these engineers were very soon replaced by Japanese engineers trained at factories and educational institutions in Japan and other countries. The Kōbu University (University of Engineering established in 1877),⁴⁷ and the Tokyo Artisan School (established in 1881)⁴⁸ are among them. The unusual feature of Japan's experience was not her failure to draw heavily on such assistance from abroad, but the speed with which she was able to dispense with it over wide areas of technology. In the other words, foreign experts were in Japan to teach Japanese how to replace their teachers. For example, when Japan's premier shipping company, the *Nippon Yusen Kaisha*, was organized in 1884, it employed 174 foreigners in operating its modest fleet of 74 steamers aggregating 60,000 tons. During the Sino-Japanese War the number of foreign officers rose to 224. Thereafter it declined, as the Japanese themselves learned the science and business of navigation. By 1920 not a single foreign officer was employed on a Japanese vessel.⁴⁹ The engineers studied foreign technical treatises and the functioning of imported machinery, and then copied what they saw, often adding modifications.

Research and development (R&D) which took place before the actual application of modern technology is another important factor regarding the social capability to absorb modern technology. However, only after the outbreak of the Second World War was R&D conducted on a large scale. The R&D of small-scale enterprises was also important; they were often members of trade associations, which had research institutions for developing technology appropriate for small-scale enterprises.

In this respect and as a result of Japanese experiences some concluding comments are appropriate. First, Japan's "cultural and institutional receptivity" which developed through her long history of introducing culture and technology from China, facilitated the introduction of Western technology.⁵⁰ Second, as a result of educational progress, Japan's social capability to absorb new technology increased. Therefore, the level of R&D activities was boosted a great deal. The last comment is related to the most important lesson that can be derived from the Japanese experience for present-day developing countries. Those countries which are struggling to achieve economic development and have a large "backlog" of unexploited technology must strive to increase their social capability to adopt it. Many oil producing countries with huge amounts of capital have spent several hundred billion dollars each for technology import and hired thousands of foreign experts in the past four decades. But, in spite of that, none of them have achieved their goals. It means that it is not enough to land machinery and equipment at the ports of some developing countries, even if political conditions are favorable for their use. Without broad social capability based on producer economics, these cargoes may easily rust away like so much junk. What substantially accounts for these defaults, is the neglect of institutional and cultural factors which are ex-

cluded from the Western-oriented economic thought and economic models adopted by these countries.

In contrast to the mandatory attitude of the abstract economic theorists represented by John Eatwell who says, "if the world is not like the model, so much the worse for the world,"⁵¹ Shigeto Tsuru remarks that, "institutional economists set store, above all, on the empirical studies of the subject matter...which undergoes evolutionary changes in the course of historical development."⁵² The disability of abstract conventional economics in identifying the sources of growth and development process in a perfect fashion, and the tremendous impact of technological changes on the structure and functioning of the economic system have contributed to the emergence of new trends for the institutionalism. For this reason Tsuru says that, "institutional economics in the condition of disarray⁵³ which the discipline of economics finds itself today, I feel, that institutionalism needs to be reappraised as a school of thought with promises of greater relevance to the task which our profession is called upon to wrestle with today."⁵⁴ Gunnar Myrdal, John Kenneth Galbraith and William K. Kapp, as the modern institutionalists echoed the warning that conventional mainstream economics was no longer able to meet the requirements for an effective tool of analysis for the problems with which modern society is confronted.⁵⁵

Myrdal confesses that when "he first came to America at the very end of the 1920's...the wind of the future was institutional economics... At that time I was utterly critical of this new orientation of economics. I was in the theoretical stage of my personal development as an economist. I even had something to do with the initiation of the Econometric Society, which was planned as a defense organization against the institutionals."⁵⁶ After, the study of race relations in America, he found himself writing a book about the entire American civilization. From then on, as he writes, "more definitely I came to see that in reality there are no economic, sociological, psychological problems, but just problems, and they are all mixed and composite... The problems are regularly also political and have moreover to be seen in historical perspective."⁵⁷ Myrdal spoke, at the American Economic Association meeting in December 1971, saying "economic science is in a serious crisis, in my view very much more revolutionary for our research approaches than was the Keynesian revolution three decades ago."⁵⁸

Galbraith referred to the situation as the "disconcerting obsolescence in the profession of economics," evidenced by the fact that "economics becomes progressively more inadequate as a basis for social judgment and as a guide to public policy."⁵⁹ Kapp, also, has raised a similar point, by describing the traditional doctrine as a case of "conceptual freeze" and predicted that "it is not unlikely that this freeze will be broken in the calculable future under the impact of new facts, new evidence of environmental disruption, new catastrophes and an increasing public opposition to the deterioration of the physical and social environment."⁶⁰

As Myrdal, had forecasted many years before⁶¹ the institutional economics has blossomed as a new field located in a interdisciplinary approach. The basic concept of institutional economics is that a market is not something that even exists in a disembodied state

or without a history. Pure competition and perfect information not only in developing economies but also in advanced market economies never occurs. Nor is the assumption of an economic entity or a culture-free individual, which acts "only" as a profit-maximizer valid as a universal phenomena. Therefore, the economic activity and all economic decisions take place within the context of an institutional structure and all are governed by the nature of that structure.⁶² Thus the institutional structure determines the economic development process of the nations. Therefore, the institutional structure can be changed through political process for the sake of the creation of a "Developmental State".

Institutionalists are those who, while they consider the national and universal aspects of economy of a given society, inquire into problems such as the logic of the process of industrialization, the power relations among economic interest groups with their various institutions, the impact of the technological changes and equality on the structure and functioning of the economic system, and the determination of national goals and priorities through industrial policy. Accordingly, institutionalists do not pose themselves as value free social scientists; for them economics remains a moral science.⁶³

All markets have rules and institutions in order to function at all. Institutions or rules traditionally existed informally in society or as formally instituted sets of regulations. Formal rules are constitutions, statutes, common laws, tariffs and the tax system and other governmental regulations which are externally enforced. These rules and institutions define the political system (the hierarchical structure, decision-making powers, the individual's rights), the economic system (property rights in scarce resources, contracts), and the protection system (judiciary, police, military). Informal rules have their origins in the experiences, traditional values, ethos, religious beliefs, ethnicity and other factors that influence the subjective perceptions individuals form to interpret reality. They are part of the heritage or culture, which is transmitted from one generation to another via teaching and imitation. Economic thought prevailing in society and among leaders,⁶⁴ consumption behavior, traditional marketing agreements and transactions, all follow these informal rules. The world around us is full of examples of informal rules that affect human behaviour differently from one area to another and from one culture to another. Evidence shows that informal rules matter, that similar formal rules imposed on different societies produce different outcomes, and that informal rules have frequently outlived formal rules.⁶⁵

But contemporary economic theory is the study of how economic forces would interact if institutions did not exist. On the other hand, institutional economic theory is the study of how economic theory is actualized through institutions and on the process of various changes such as technology. "Institutions are like fortresses: they must be well designed and properly manned,"⁶⁶ to achieve the sustainable development process of a society.

Western-oriented students of the Japanese economy have tended to miss this dimension of Japan's achievement because the study of institutions has been slighted in postwar Western scholarship. Until very recently, the study of Japanese economy by English-speaking social scientists was thought of as mere "area studies."

Area studies in their traditional form meant the application of various social science

theories to some exotic non-Western case, or the collection, through sheer mindless empiricism, of new data for later theorist to explain.⁶⁷ This understanding of the relationship between theory and area studies is now dead.

4 The Nobel Prize for Economics, Economic Thought, and the American Experiences

The first Nobel Prize for Economics was granted in 1969 to the founder of econometrics, Jan Tinbergen of the Netherland's National Collage of Economic Science, and Ragnar Frisch, the Norwegian founder of the new methods of measuring marginal utility in 1969. This trend became mainstream in economic studies. The neoclassical mathematical approach, based on 19th century academicism, continued its evolution toward maturity mainly in America.

One of the reasons America has received 25 prizes within 26 years was the emphasis on positivism, which is based on neoclassical consumer-oriented economic thought. The profit-maximizing Anglo-Saxon economic thought is derived from the rational utility-maximizing individual, to whom consumption and leisure are the sole economic elements of satisfaction. Higher productivity at work is desired since it gives individuals higher income to buy more goods for consumption and the ability to reduce work to obtain more leisure without sacrificing consumption. Work and saving are both disutilities, tolerated solely because the future income that flows from these activities provides the economic resources needed for future consumption.

It is true that man is a consumer, but is also a producer. Therefore, a producer's work is not a disutility. Those remembered in human history are not the great consumers. They are the conquerors, the builders, the producers.⁶⁸

Natural science is based on the academics of the 19th century. Neoclassical economics is the same. Most Nobel Prize economists are from this category, and their theories are supported by mathematical proof. Keynes is a great economist. His ex-assistant, professor Hahn, currently at Cambridge University, believes that because Keynes theory is based on intuition, sometimes it is very difficult to prove. However, the economist who was able to prove the consumption function (the relation between income and consumption) within the framework of Keynes's theory won the Nobel prize.

Logical deductions are impossible if economic statistics are not released for the public in comprehensible statistical language. American society takes advantage of such an effective tool, because it is a disclosure society, based on its traditions and value system. Economic institutions often release all the required information that investors and shareholders might need, except for top secret data. The public, thus, has easy access to this type of information. The American government, too, acts openly when it comes to economic data. Researchers in America have easy access to up-to-date statistic, information, and current government policies anytime they need them.

In Japan, getting up-to-date information about companies is impossible, especially in

large private companies. It is impracticable to know the real situation of Japanese firms, and it is very difficult to believe the reports provided by the firms' accountants. The attested public accountants are appointed by the president of the company in Japan. Thus, if these accountants release any information to the managing directors' disliking, they will risk their relationship with them or even be fired.⁶⁹

In America, the situation is different. A certified public accountant covers all the companies' transaction, from managing directors to the lowest level, and then reports them in the company's general assembly for all shareholders. The managing directors in America are part of a team that makes crucial decisions, just like football or baseball coaches who have to consult with trainers and other team managers.

In Japan, the general assembly of shareholders is ceremonial and takes only 10 to 30 minutes each year. The managing directors are often comparable to professional team owners whose only duties are watching the financial performance and changing a coach or two if the outcome is unsatisfactory. They may know little about the procedure and perhaps can not play the game.⁷⁰

American companies were originally established by the British, which might partially explain the roots of these differences. The companies had to invite foreign inspectors or accountants, who were usually British and neutral.

These differences make the United States an environment for positive-style economic studies. Economics based on the actual data of American society, with its economic behaviour and cultural-based value premises, became an effective tool for neoclassical researchers. Thus, United States was assumed to be the world wide universal model by the neoclassical economists.

For economists, the reality of various economies with their historical and institutional aspects and their future sustainable development, is of high importance. But if the current environment for the awarding of the Nobel Prize in economics prevailed before World War II, it is not clear whether Keynes would have been awarded a prize. He was an intuitive economist and as a nationalist was concerned with a specific country (England) and a specific period of its economy (the inter-war years). It is interesting to note that none of Keynes followers have been awarded a prize either.

5 Who Will Win the First Nobel Prize in Economics for Japan?

Until now, several Japanese economists have been nominated for the Nobel Prize. Shigeto Tsuru, Michio Morishima, and Hirofumi Uzawa are among them. Tsuru is the only Japanese economist who has advanced to the semi-final stage of this competition, along with John Kenneth Galbraith of America. Both of them have been eliminated in the final stage.

At present, the Nobel committee in Sweden systematically discriminates against labor-oriented economists like Michio Morishima, Hahn or John Robinson (who have had close relations with the British Labor Party). Shumpeterian, Marxist economists and Insti-

tutional economists, except Myrdal for his previous works have not gotten the prize either. Therefore, a highly mathematical and positivist approach with neoclassical economic thought has been the norm for the Nobel Prize in economics.

The Japanese have been sensitive to winning the Nobel Prize during the past few years. They have established a committee exclusively for strengthening ties with the Nobel Prize committee in Sweden. A large number of the prize winners are invited to Japan by this committee every year. They participate in large ceremonies. These ceremonies are broadcast by Japanese television to encourage young researchers. The press, too, engages in heated debate on the issue.

Under the current situation mentioned above, the question is: Who will win the Nobel Prize first for Japan? For now, it seems an economist like Masahiko Aoki, an ex-professor of economics at Kyoto University who is presently teaching at Stanford, is the frontrunner. Aoki has explained the characteristics of Japanese firms, their unique economic behaviour and their phenomenal achievements (reality aspects) through the mathematical language of the Game Theory (universality aspect). But it might be remembered that behind the scenes activity for the Nobel Prize is very important and sophisticated. It is said that Mishima Yukio lost the chance for the Nobel Prize due to the lack of this kind of activity. On the contrary, Eisaku Sato the former Japanese prime minister, was awarded the Peace Nobel Prize because of successful behind the scenes activity all over the world. The lack of Nobel Prizes for economists in Japan does not mean that Japanese economists are not among the leading world's economists. Some critics say Takashi Negishi from Tokyo University had a higher standing than Frank Hahn from Cambridge University, who is a world renowned figure. The problem is that, first of all, ideological belief and cultural environment play an important role in the Nobel Prize Committee's Selections. Secondly, it is very difficult for non-Anglo-Saxon economists under the current circumstances of economic science to be able to receive the prize. Therefore, "the Nobel Prize had better be given in such fields as the Natural sciences and perhaps to the peace activist as well, which we hear a lot about nowadays" says Mitsuharu Ito, the emerituse professor of Kyoto University.⁷¹

Some Concluding Remarks

Institutions, in their broadest sense, were actually the major sources of the growth and development for more than 100 years, not only in Japan, but many other developed countries. The disability of abstract conventional economics in identifying the sources of growth and development process in a perfect fashion, the tremendous impact of technological changes on the structure and functioning of the economic system, the diverse aspects of market economic systems based on different institution and cultural backgrounds among the market-oriented countries, in the face of underdevelopment, energy, food and environment crisis, has revealed many anomalies of the neoclassical synthesis which caused the current crisis in economic thought.

Institution refers to a configuration of power and a constellation of beliefs. Any society

contains a power structure or set of control groups that have the discretion to make and implement decisions. The powerful operate in the context of a culture that provides them with guiding principles and speaks to the legitimacy or illegitimacy of their power and its use. An institution is then a cluster of mores that distribute power or authority. Culture, as an informal institution, is a set of significant meanings that arise from and structure interpersonal relationships. Any society carries on a culture by means of the stories told and models of, and for, reality that are displayed within it. Therefore culture in this sense significantly influences the individual personalities and its behavior and social character of a society. The world around us is full of examples of informal rules that affect human behavior differently from one area to another and from one culture to another. Therefore, the preconception of the autonomous cultural-free individual as a rational manager of a bundle of resource, services, and as an utility calculator in orthodox economics is invalid. Individuals' perceptions of the real economy are colored by their values, experiences, traditions, observed successes and failures, and reason. Dedication to ideologies, sacrifice in defense of abstract causes, depth of religious beliefs, and many other observed behaviors of individuals, households and even firms can be neither expressed in term of neoclassical theory nor dismissed as ad hoc events.

The behavioral assumptions of neoclassical theory rests on the assumption that competitive forces assure an efficient outcome, and that the system can best be understood in terms of the analysis of predetermined equilibria. However, it is difficult to reconcile neoclassical theory with the performance of various economies. Why are inefficient alternatives surviving? Why do the same set of rules imposed in different countries for their development, produce different outcomes?

As, was mentioned earlier in this paper, area studies in their traditional form of the application of abstract theory to the exotic (non-western) case is now dead. The reason for this is because the study of the Japanese economy and many other economically successful non-western countries is today in need of further theorizing. Therefore, institutional economics or social economics which is concerned with the reality of economics and examines the interaction of economy and society as a whole, is highly important to the Faculty of International Studies; a faculty which is devoted to Japanese Studies, Area Studies, and developing economies. As a result, this interdisciplinary approach rightly serves as the main pillar of the department's educational colloquialia and research activities and is the standard-bearer for the new theoretical forces challenging the established paradigm in orthodox economics at the department's 10th anniversary and in the "Age of Mega-Competition" which is actually the 「Age of CIA」 (Comparative Institutional Analysis) for the institutional economist.

Footnotes

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- 11 Mizuta Hiroshi, "Sumisu no Seishin Minaoshi o", *Nihon Keizai Shinbun*, 1992, July 13.
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- 18 Japan Times, Sept.27, 1995.
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- 22 Keizai jisso hokoku sho, (Economic Reality Report) Fu, Keizai kinkyu taisaku, (Appendix: Emergency Economic policy), Keizai Anrei Bu, S.22.7.4, (July 4, 1947).
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- 26 *Ibid.*, p.24.

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- 61 “I foresee that within the next ten or twenty years the now fashionable highly abstract analysis of conventional economists will lose out. Thoughts logical basis is weak—it is founded on utterly unrealistic, poorly scrutinized, and rarely even explicitly stated assumption—its decline will be mainly an outcome of tremendous changes which, with crushing weight, are falling upon us.”, Gunnar Myrdal, “The Meaning and Validity of Institutional Economics”, in Kurt Dopfer, *ibid.*, p.86.
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