

【Article】

Market Order and Intermediate Organizations;
“Inclusive Growth” in the Perspective of
Japanese Economic History

市場秩序と中間組織：日本経済史の視点から見た「包括的成長」

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1. Introduction

This paper explores the role of intermediate organizations against the backdrop of the economic history of Japan, and tries to derive implications for Africa. It is argued that in Japan typical form of intermediate organization changed from regional coalitions in the prewar to industrial associations in the postwar period, and that intermediate organizations based on inter-industrial adjustment of interests of the postwar period, a mutually inter-related system of industrial associations, was especially effective in contributing to inclusive growth. It is asked whether it is possible to reorganize ethnic and regional groups in Africa, interpreted as intermediate organizations, as a smoothing mechanism of income distribution, and not as a mechanism to monopolize benefits of modernization by winning coalitions.

It is composed of five sections. Section 2 tries to examine intermediate organizations from a broadest framework of political economy, and discuss how intermediate organizations function in establishing and improving market orders together with or substituting the role of the state or human ethics. Quoting the materials from the history of political-economic thought, three types of market order are compared; market order with human ethic, market order with the state, and market order with intermediate organizations. It will be suggested that intermediate organizations have been considered to be a factor to affect the quality of market order or democracy, complementing or substituting the role of the state or human ethics.

Section 3 deliberates on the role of intermediate organizations in socio-economic aspects in two respects; self-enforcing governance of contract enforcement and informal mechanism of income redistribution among various groups. With respect to the first point, it will be argued that the mechanism of informal contract enforcement functions when a group or an intermediate organization has indefinite life. In other words, for the informal mechanism to function, it is not necessary to have specific utility function that value the future higher than the present, but group altruism and notion of immortality of the group will suffice to enforce contracts effectively.

With respect to income redistribution, it is pointed out that the conventional model of income redistribution policy comprising a comparison between Heckscher-Ohlin model and specific-factor model is misleading in the sense that the properties of latter model are derived in a two-industry framework without any consideration about input-output interaction among industries. As a result, not only in Heckscher-Ohlin model, but also in specific-factor model, rivalry among industry is over-emphasized. As is shown in the experience of the postwar Japanese system, the interests of various industries are

interdependent through technological input-output relationship, so that interaction among industries with industry-specific production factors is usually characterized by negotiations representing inter-related interests, not by sheer rivalry among industries. While the solution in Heckscher-Ohlin model results in outright antagonism between capitalists and workers, that of factor-specific model, in a multi-industry setting, is smoothing of income distribution among competing industries. The intermediate organization system of postwar Japan organized according to a set of industrial associations representing inter-industrial interests resulted in inclusive and equitable income distribution in this sense, while the system organized along a set of labor and employers' unions representing class interests quite often ends up in a serious trade disputes and social unrests as was frequently seen in the history of Latin American economies.

Section 4 discusses the typology of intermediate organizations. Following Tocqueville, this paper identifies two types of intermediate organizations. First is "associations", where exit from the organization is free because of the absence of organization-specific investment by members, and another is "intermediate corporations", where it is not easy for the organization members to quit from the organization because of the sunk-cost nature of investment in organization-specific human capital. In his analysis of American democracy in the nineteenth century, Tocqueville emphasized the role of intermediate associations (association) organized by the initiative of individual citizens, as a mechanism for protecting American democracy from falling into tyranny of majority. Later on, in his analysis of French revolution Tocqueville deplored the elimination of intermediate corporations (*corps intermédiaire*) due to the enactment of Le Chapelier Act in 1791, with a consequent prevalence of individualism in France. Generally speaking, associations have a tendency to develop multi-dimensional interest representation, while such a tendency is rare to be observed in the case of intermediate corporations.

Section 5 provides a brief historical overview of the evolution of intermediate organizations in the Japanese economic history, and investigates how and why the mechanism to adjust income distribution through a set of industrial associations emerged after the Second World War. In the prewar Japan, regional coalitions functioned as a key set of intermediate organizations enabling informal redistribution of income and resources necessary for economic development. Each regional coalition was led by rich landlords and merchants called *Meiboka*, engaged mainly in indigenous economic activities.

As modern industries developed and indigenous industries stagnated in the interwar period, *Meiboka* tried to invite factories of modern industries to their regions. Agglomeration effects of modern factories gave rise to various supporting industries in the regional economies through Marshallian external economy. The nascent supporting industries organized industrial associations at national level, and this had the effect of cross-cutting of existing regional ties. There also emerged class conflicts during the interwar period. Representation of distributive interests through class conflicts, however, did not develop fully in Japan because of the spread of Japanese-style firm system

organized on firm-specific skill formation. With the reduced mobility of labor under lifetime employment system, distributional interests came to be represented by a set of industrial associations. In the postwar period the government utilized this system in order to realize inclusive growth of society. Both input and output prices of each industry were subject to interest group activities of industrial associations. Owing to the input-output inter-relationship among industries, a higher or lower product price of any industry had spillover effects on other industries. The government intervened in the interacting process of industrial associations through adjusting the competitive conditions of each industry, effectively shifting part of the value-added from growing industries to declining industries. Sharing fruits of modernization among growing as well as stagnating industries was a major outcome of the system.

Section 6 discusses the implications of the analysis for ethnic groups in Africa from the viewpoint of intermediate organizations. First, it will be argued that ethnic groups in Africa bear characteristics both of associations and of intermediate corporations. At the same time, we will note that the characteristics as intermediate corporations, together with the sunk costs in the form of human tolls paid through violent ethnic conflicts, make it difficult for Africa to develop multi-dimensional interest representation. Second, it is pointed out that the main aim to organize intermediate organizations along the line of ethnic groups was distributional. However, in Africa, distributional conflicts among ethnic groups quite often end up generating monopoly of resources by winning groups, unlike the postwar Japan, where distributional conflicts among industrial associations resulted in inclusive growth through smoothing of income distributional disparity. Finally, we will deliberate on whether it is possible to convert ethnic competition system in Africa into inter-industrial income adjustment system *a la* Japan. Quite tentatively, a three-stage strategy is proposed in order to reorganize intermediate organization system in Africa; first, to convert ethnic rivalry based on regional and other identities into genuine regional rivalry by use of subsidy policy, second, to apply industrial policy in order to exploit the benefits of regional agglomeration, and finally to develop multiplicity of distributive system along inter-industrial interests.

2. Role of Intermediate Organizations in Market Order

Market is a powerful mechanism to convert the free play of self-interested individuals and firms into an optimal resource allocation. The conversion is neither costless nor automatic, however, because individuals under a *laissez faire* rule could indulge in opportunistic activities as a rational behavior whenever there exist information asymmetry and conditions that lead to incomplete contracts. Market cannot exclude the possibility of falling into failures such as moral hazards, adverse selection or hold-up problems. It is true that, with the development of social infrastructure and information and communication technologies, market could give rise to private activities to overcome information asymmetry and impediments to contracts. Rating companies, second-hand car

dealers, and security analysts are such examples. While these devices could reduce market failures in the areas concerned to some extent, they cannot eliminate information asymmetry as a whole in a society: proliferation of new magazines to judge the quality of security analysts is good evidence here.

Let us examine existing theories about market order or democracy in a framework of three dimensions: individuals and firms (the private), the state (the public), and intermediate organizations (the society). Individuals could be irrational and immoral especially when they are left in a “natural state”. However, individual might learn through education or from experience. The state under the rule of the philosopher-king could set someroprite rules and direct the market system so as to achieve fair and efficient performance. Since those who hold power usually maximize their own rents, however, the outcome could be either the tyranny of the majority or capturing by privileged minorities. Intermediate organizations sometimes bridge the private and the public adequately and attain a proper balance between freedom and equality. However, whenever competition among intermediate organizations gets too intensive, capturing of the state by powerful interest groups could result in inefficient and unstable outcomes.

With this framework, it could be argued that three types of solutions have been pursued in the history of economic thought to realize desirable outcome of market order. First is the market order with ethical behavior by individuals, where individuals and firms with sufficient ethical view restrain from opportunistic behavior for themselves. Second is the market order with state interventions, where the state is endowed with the right to regulate the behavior of individuals and firms and leads the performance of market. Third is the market order with intermediate organizations, where informal rules are provided by intermediate organizations to induce individuals and firms to restrain from opportunistic behavior. The first-type market order with individual ethics was examined by Adam Smith (1723-1790), the second by Jean-Jacques Rousseau (1712-1778) and Friedrich August von Hayek (1899-1992), and the third by John Locke (1632-1704) and Alexis de Tocqueville (1805-1859), among others. Let us compare the theories of these economists or political scientists briefly in order to understand the role of intermediate organizations in the market order. It will be suggested that intermediate organizations had been considered to be a factor to affect the quality of market order or democracy complementing or substituting the role of the state or human ethics. In other words, freedom of behavior of self-interested individuals is not sufficient to bring about desirable outcome in market order or democracy; along with the quality of the state and the ethic level of individuals, intermediate organizations could have positive or negative influences on the quality of market and democracy.

(1) Market order with human ethics

Adam Smith tried to see whether and how market order leads to desirable resource allocation with the help of human ethics. As is well known, with the help of the notion of invisible hand, he arrived at an affirmative conclusion in this respect.

With respect to the quality of individuals, he was rather optimistic. At first, he considered that the performance of an individual has two parts---a part governed by self-love and another part composed of behavioral norm as a fair observer of himself, and that an individual's behavior based on the principle of self-love is monitored by the latter part (the principle of sympathy). Later on, learning process of individuals was incorporated into the principle, and it is argued that through repeated experience in markets, individuals learn to behave ethically in order to keep reputation. Smith hated intermediate organizations (interest groups) composed of manufacturers and merchants, who had captured the government under mercantilist regime. His policy recommendation of minimizing the room for government intervention (*laissez faire* rule) was the natural consequence of the reliance on individual ethics and the abhorrence of intermediate organizations.

(2) Market order with the state

Rousseau aimed at establishing democracy in which the state and society are merged. The society is conceptually dissolved into individuals with equal right and the state is considered to be established representing the “general will” of those individuals.

Individuals are considered to be immoral and irrational before integrated into the state system, and requested to surrender totally their private rights and interests to the state. The state has absolute power over individuals (citizens) as a body representing the general will of the people¹. Any intermediate organization (associations) is considered to be inimical to the public interest, merely because it is private (Sabine 1952). Associations were relics from the feudal period, where associations were basic instruments for the rulers to give rise to discrimination of status and hierarchy.

Hayek proposed spontaneous market order under the aegis of a strong state. He did not have any rosy image about the ethical behavior of individuals either. Individuals are considered to be lazy, indolent and irrational originally, and the concept of “economic man”, a consistent and rational optimizer in the market with sufficient information, was completely denied in the Hayek's model. Based on the understanding that the *laissez faire* policies before the Second World War had given rise to socialism and totalitarian regimes, he emphasizes the need for a strong state to bring up efficient markets. Cautious of capturing of the state by powerful interest groups, he denies the role of intermediate organizations. Collective behavior was condemned as a characteristic of tribe societies, while roles played by custom and tradition are not denied.

(3) Market order with intermediate organizations

Locke envisaged democracy in which the state and subjects enter into a subordinate contract, and the latter have basic freedom including rebellion against the former if necessary. Individuals (subjects) are considered to be able to make their own autonomous judgments, and to manage most of their affairs for themselves. The compulsory power of the state is stipulated by the law within the confines of the constitution and moral rules established in the society. The society is composed of a maze of private relationships and a multitude of intermediate organizations (associations) that pursue their own interests and make their own rules. The state is requested to protect diverse intermediate organizations and the right of individuals to participate in them.

Tocqueville acknowledged the value of democracy with active roles played by intermediate organizations (associations). Individuals are considered to foster habits of heart to appreciate public good through the active participation in intermediate organizations, while they are liable to fall in individualism without such opportunities. A state is considered to tend to be an arena for the tyranny of the majority under democracy, so that intermediate organizations are indispensable for the proper functioning of democracy; people could pursue freedom from the state through collective actions by means of associations.

3. Economic Roles of Intermediate Organizations

Intermediate organizations have been a research subject either of political science or sociology by and large. For example, political scientists argue that intermediate organizations work as a protector of citizens against coercive policies by the government, or that capturing of the government by particular intermediate organizations leads to inequality; sociologists examine how intermediate organizations strengthen social ties through enhancing considerations toward others by individuals.

In the classification above, the roles of intermediate organizations have been explored only in the political relationship with the state. Both Smith and Hayek criticized intermediate organizations because they act as selfish interest groups trying to capture the state, and consequently distort the motivation of the state. Rousseau was also against intermediate groups because they were feudal rulers' instruments for creating discriminatory status, giving rise to inequality of political rights between the privileged and the rest. Locke was more lenient with intermediate organizations and, instead, valued their positive roles at the interface between the private sector and the state. Tocqueville also points out the positive aspects of intermediate organizations, emphasizing the effects on political freedom from the state secured and enjoyed thorough collective behavior by associations and regional coalitions. their economic roles.

(1) Informal Mechanism of Contract Enforcement

The analysis on the roles of intermediate organizations from the economic aspects has begun only recently and the research is still actively ongoing. The first part of the study is concerned with the role of intermediate organizations as an informal mechanism of contract enforcement. Greif (1993, 1994) was pioneering in analyzing the role of business ties among medieval merchant groups in enhancing the efficiency of market order. Kandori (1993) conducted theoretical research in contract enforcement mechanism based on community relationship. Dixit (2004) integrated related researches and explored their implications.

Whenever an intermediate organization is a stable and cohesive group, self-governance mechanism works to enforce contracts and hence helps to enhance the optimality of market order. Let us explain this in two cases; transaction between the same partners and between different parties. When the same party interacts repeatedly, the concerns about the collapse of long-term relation would restrain participants from pursuing short-term gain obtained by violation of a contract. This happens when participants value the future sufficiently highly relative to the present (i.e., subjective rate of discount for the future gain is low)² or when transactions are expected to be repeated infinitely³. The first condition, which is usually assumed in theoretical models, seems to be rather clumsy because it assumes specific forms of utility functions. Precisely in this regard lies the importance of intermediate organizations as informal governance mechanism. Although, at first glance, it might be considered that the latter condition is also hardly satisfied, because any individual is mortal and any transaction could not be accomplished without consuming time, in the case of an intermediate organization, this condition could be satisfied because an organization such as a church or a temple could be immortal or of infinite life-span even if members in the group have only finite life-span. A sort of group altruism assures that each member behave for the sake of long-term benefits accruing to the group⁴. Temporal coalitions like the one formed for the purpose of vote mobilization by ethnic groups could also be viewed as having infinite life potentially, because a new coalition could be formed at any time in the future whenever necessity arises, although the composition of member may not be the same.

When different partners of each group interact, a credible multi-lateral punishment mechanism could prevent opportunistic behavior (Dixit 2004). If any one member of a group cheats his trading partner, and the information is conveyed smoothly among group members, this could lead to ostracization or other punishment because any other member of the group could be the cheater's future partner. With stable membership and good information networks, the loss of reputation is a deterrent to opportunistic behavior, even with limited life span of the members.

It follows that a stable and cohesive intermediate organization functions as a provider of informal contract enforcement mechanism in two senses; through its indefinite horizon making repeated transactions credible and through its effective information exchange and the resulting punishment mechanism.

(2) Redistribution of Income

Intermediate organizations fulfill the role of enhancing the quality of market order in another dimension; informal adjusting mechanism of income redistribution among various groups⁵. A competitive market cannot necessarily realize desirable income distribution in the society. Moreover, as is emphasized by Hayek, it is difficult to define fair and equal income distribution, and hence to design formal political system to realize it. Nevertheless, it is well understood that stable economic environment for the successful working of market order requires income distribution that is regarded at least reasonably fair by most of the participants. Intermediate organizations at the interface between the private sector and the state could fulfill the role of adjusting income distribution informally. That could bring about income distribution among different socio-economic groups difference, which would be considered to be “fair” by most of the participants and effective in establishing stability of the political-economic system among groups.

A well-known starting point of the analysis of the role of intermediate organizations in alleviating inequality in income distribution was provided by the theory of endogenous tariff, in which two models, Heckscher-Ohlin model and specific-factor model, are compared within a 2-factor (labor and capital), two industry (labor intensive and capital intensive industry) framework.

In this comparison the difference in the pattern of representation of distributive conflicts is closely related to the nature of factor markets, especially mobility of labor market. In Heckscher-Ohlin model, where factors are assumed to be perfectly mobile, a policy which increases the price of labor-intensive product will benefit workers in the industry, because wage rate is increased by the policy and the rate of increase in wage is higher than the rate of increase of product price. Capitalists will suffer by that policy, so that interests of workers and those of capitalists diverge and a coalition of labor and capital will not be realized. However, workers in the capital intensive industry will also benefit from the policy (the Stolper-Samuelson theorem), so that labor as a whole has an incentive to lobby the state against the interests of capitalists as a whole. Representation of distributional interests by economic class is a natural outcome in this case.

On the other hand, in the specific-factor model, it is assumed that skills of workers are industry-specific and workers cannot move across whereas capital can move freely. In this setting the policy to raise the product price of labor-intensive industry will definitely benefit workers because wage rate of the labor-intensive industry increases more than the increase in product price (Krugman and Obstfeld 1988, Ch.3). While profit rate will also increase by this policy, it is not certain whether profit rate increases in real term. Rate of increase in profit rate is lower than the rate of increase in the product price of the labor-intensive industry. (Real profit rate decreases in labor-intensive industry while it increases in capital-intensive industry.) Workers with industry-specific skills in labor-intensive industry will have incentive to form a coalition to advocate policies favoring their industry. Since the workers in capital-intensive industry definitely suffer from the

policy, there tend to occur significant conflicts between two industries with workers possessing industry specific skills. Representation of distributive interests by industrial associations is a reasonable institutional arrangement in this case⁶.

While this theory of endogenous tariff seems to be a reasonable description of distributional coalition formation, it is important to note that the reasoning regarding the specific-factor model contains serious ambiguity and misleading implications in the following two senses. First, this model is presented in two-industry framework, in which only possible outcome is a winner-loser solution. When one industry is successful in lobbying for a policy that benefits the industry, the other industry automatically fails and become a loser. A fierce antagonism between the two industries is an inevitable outcome, just as the Heckscher-Ohlin model results in class struggle between two classes. Moreover, the model does not take into account the technological input-output relationship among industries. As a result, the model overemphasized the inter-industry competition. It is shown below that in the postwar Japan interrelated interests among industries resulted in smooth division of value-added among industries, not causing monopoly of policy rents by the winning industry. Second, the model does not offer persuasive explanation about the coalition formation in labor-intensive industry. Although wage rate increases in real term in this industry, the real profit rate does not necessarily increase in this model, so that it is not certain that capitalists of labor-intensive industry has an incentive to take part in the coalition with workers. Although it needs to build a completely new model to present a convincing explanation on this point, it seems to be certain that coalition formation in this case is motivated by the fact that workers in this model are partly residual claimants because they are not simply wage earners but owners of human capital. In this sense, the interests of capitalists who are owners of real capital have something in common with workers, and payments of bonus to workers has a nature of paying part of residuals to the contributors of human capital. Without noting this point, it is not easy to explain the formation of industry-level coalition in this model.

4. Two Types of Intermediate Organization

(1) Associations

This paper identifies two types of intermediate organizations⁷. First are intermediate organizations called associations, where exit from the organizations is free because of the absence of investment in organization-specific skills by members. Some of associations are standing organizations, and others, frequently called coalitions, are non-standing and organized on an *ad hoc* basis. Based on his observation of the nineteenth century United States, Tocqueville asserted that the healthiness of American democracy owes significantly to the prevalence of associations organized freely by the initiative of individual citizens. In particular he noted the important role played by associations in protecting democracy from falling into tyranny of majority.

It is well documented that the origin of business corporations in the United States could be traced back to associations, which have their roots in religious sects organized by Puritans during the seventeenth century. One of the basic characteristics of associations is easiness of establishment and resolution. This property of associations was expected to lead to the growth and proliferations of interest representation by intermediate organizations in multi-dimensional areas. As is emphasized by Truman (1951), Galbraith (1952) and Dahl (1982) among others, the American society was expected to preserve healthy competitiveness and freedom for citizens in spite of the growth of monopoly in the private sector and the coercive power of the government. These authors predicted a bright future for the American democracy based on proliferation of multi-dimensional associations. Focusing on the activity of associations as political interest groups, Becker (1983) presented a theory of competition among pressure groups. In a model in which political influence is produced by political pressure groups using real resources and assuming that aggregate political influence satisfies a zero-sum condition because of interdependence among influences, Becker asserted the existence of socially efficient equilibrium of interest group activities⁸. Skocpol (2003), however, points out that the development of association seems to have reached a turning point after the 1960s. He ascribed it to the increase in the costs required to establish and manage efficient associations. Many more associations have become established by large-scale funds and managed by specialists, and traditional-style associations established by members only are getting out of date.

(2) Intermediate corporations

Another type of intermediate organization is intermediate corporations, where it is not easy for the organization members to quit from the organization. Basic reason for the difficulty in leaving organization lies in the sunk-cost nature of investment in organization-specific human capital by members. Members of intermediate corporations are willing to pay the costs of investment in organization-specific human capital whenever hold-up problem is negligible, and the level of such investment will increase in an economy where alternative investment opportunity is scarce and where more emphasis is given to organizational efficiency than to allocation efficiency.

In his pioneering book on human capital, Becker introduced the distinction between firm-specific and general skills and deliberated on the financing of investment in human capital (Becker 1975). It is interesting to note that while Becker developed a detailed argument as to why workers are willing to pay the expenses for training to obtain general skills, with respect to the training to obtain firm-specific skills he simply assumes that only firms pay the training expenses, and neglect the possibility of training costs paid by workers. This seems to reflect the fact that individual initiative and freedom with respect to the entry and exit decision is a basic principle of forming intermediate organizations, and that firms in the United States are established in the tradition of associations, where

hold-up problem is ubiquitous. In other words, it seems that Becker did not feel any necessity to pay attention to a situation in which hold-up problem is avoided and workers are willing to pay the costs to acquire firm-specific skills.

Perhaps the United States is special in the sense that intermediate organizations are mainly composed of associations there, and intermediate corporations defined above do not have any significant roles. Locke seems to have paid significant respect to the roles of intermediate corporations that had been inherited historically. In his analysis of the French revolution Tocqueville deplored the elimination of intermediate corporations (*corps intermédiaire*) due to the enactment of Le Chapelier Act in 1791, that had resulted in the prevalence of individualism in France. In Japan where modern business firms have their origin in *ie* system, in which the possibility of hold-up problem is reduced to a minimum and firm-specific skill formation and organizational efficiency constitute major source of business competitiveness, intermediate corporations have significant importance. As has been noted already, it is interesting to see that the origin of modern corporate firms in the United States lies in the religious associations (covenant churches) during colonial days⁹.

Two of the properties of intermediate corporations are worth mentioning. First, intermediate corporations seem to be more persistent compared with associations. Second, while associations have a tendency to develop multi-dimensional interest representation, such a tendency is rare to be observed in the case of intermediate corporations. There is no need to say that these properties are closely related to the investment in organization-specific skills and the related difficulties in leaving organizations by members.

5. Intermediate Organizations in the Japanese Economic History

This section examines how income distributional interests came to be represented through industrial associations in the postwar Japan in a long-term perspective from the beginning of modernization. When Japan began to modernize, the interface between the state and the private sector was represented by regional communities. This section discusses how regional coalitions were established at first, and why and how this representation pattern changed over time, eventually leading to the establishment of a system of intermediate organizations representing inter-industrial interests.

(1) Emergence of Regional Communities as Intermediate Organizations

(1-1) Natural villages

During the pre-Meiji feudal period, Japan was composed of 261 feudal territories. In each district, the revenue of a feudal government came mainly from agricultural tax, which was levied in proportion to annual amount of production of each village. Villages had been formed gradually through hundreds of years, and were inhabited by a hundred of

independent farm households on average¹⁰ mainly engaged in family-based rice production. These villages, natural villages, were the basic units of daily life, production and the payment of taxes.

(1-2) Government policy

The Meiji Government established in 1868 integrated the feudal districts into 46 prefectures¹¹ and changed the governance system in two respects. First, it reorganized the local government system so as to meet the necessity for central government control as well as to accommodate democratizing demand by the Freedom and People's Rights Movement that erupted in 1874¹². The new system was a hierarchy system composed of prefectures, county, and towns and villages. A prefecture had an officially designated governor and an assembly, whose members were representatives of counties. A prefecture was usually composed of 3-5 counties. A county also had an officially designated chief and an assembly, whose members were representatives of towns and villages. A county was usually composed of tens of towns and villages¹³. It is important to note that towns and villages were established on the basis of natural villages¹⁴ and were conferred (public) corporate status¹⁵, and that their chiefs were elected by popular vote¹⁶. Moreover, town and village offices were allowed to be involved in their own activities related to daily consumption and production of the inhabitants, so that their budgets were comprised of two parts; administration-related part under the control of the government and daily-life-related part¹⁷ left to the free hand of the people. In other words, the basic stance of the Meiji Government toward regional communities was to leave natural villages intact.

(1-3) Introduction of land tax

Second, the government introduced a new taxation system on agriculture in order to secure government revenue. While the tax revenue from agriculture in the feudal period was unstable because the tax rate was related to annual production, the tax system introduced by the new government in 1873 was related its tax rate to estimated land prices¹⁸ held by each farmer. Since the estimated land prices were changed only occasionally, the new taxation system realized much more stable revenue for the government. At the same time, the government clarified land as private property. The regulation on the use of land was lifted in 1871. The feudal ban on land transaction was abolished, and certificates for the ownership of land were issued in 1872, followed by the enactment of collateralized lending act in early 1873. The promulgation of the revision of land tax act in July 1873 marked the finalizing of this entire process.

These policies entailed enormous changes in the socio-economic structure of the rural sector. There emerged a significant income inequality among farmers. Those farmers with good cultivating conditions and technology expanded their production and hence land holding. Partly due to the depression policy around mid 1880s (Matsukata deflation), there

occurred significant concentration of land ownership, and successful farmers emerged as a land-owning class. With the rapid expansion of domestic and international markets caused by the abolition of feudal regulations and the development of communication and transportation systems, it was natural that rich landlords became absentee landowners and embarked on commercial or industrial activities. Because of the underdevelopment of financial markets, the best way for the landlords to invest in non-agriculture was to be involved in indigenous manufacturing and related commercial and service activities in the region they lived.

(1-4) Inequality among counties

Rich landlords became political-economic leaders of regions and were called *Meiboka* (men of reputation). Usually counties composed of tens of towns and villages or areas with the space of one-third or fourth of a prefecture comprised the basis of their commercial and industrial activities. Most of them became members of county or prefecture assemblies, and some even became members of the Imperial Diet.

The domestic and international expansion of markets caused fierce competition among regions for the sales of region-specific products. In order to win the competition, construction of infrastructure such as roads, railroads, ports, hospitals and schools was crucial. Utilizing their political position, many of *Meiboka* were involved in the competition to invite national infrastructures or to obtain subsidies from the central government (Ariizumi 1980).

Regions that succeeded in obtaining the government support developed more rapidly than other regions. Within the same region or county the effects on economic activity of an infrastructure could be different among towns and villages (Matsuzawa 2009), and this frequently triggered rivalry among towns and villages. Income inequality among counties or inequality among towns and villages were the consequence of the process. The gains through regional agglomeration triggered the economic growth of Meiji Japan under the condition of rapid expansion of domestic and international markets. When there had existed significant inequality among regions before the introduction of government support, the extension of support towards poor regions had equalizing effects among regions. Meiji government leaders such as Kaoru Inoue and Aritomo Yamagata were eager to utilize the resource allocation mechanism based on *Meiboka*-order to stabilize and strengthen the grip on rural communities. Keeping the internal harmony within natural villages and manipulating of favors at the county level were their basic strategy in this respect.

(2) Emergence of Industrial Associations

(2-1) Weakening of *Meiboka* Order

After the end of the First World War the growth rate of agriculture and the related indigenous industries declined because of stagnation of productivity growth¹⁹. Moreover, the government implemented a policy of lowering rice price in order to prevent a rise in real wages of urban factory workers. Tenancy disputes increased after 1921 drastically in the number both of cases and participants. Regional ties were no longer monolithic. The commitment of landlords to farming decreased and they converted their portfolio composition from land and related indigenous industries to investment in modern industries in large cities (Teranishi 2000). The development of financial markets facilitated landlord to implement the investment by means of financial intermediaries and financial instruments. All of these factors worked to weaken the *Meiboka* order.

(2-2) Cross-cutting Regional Ties

In view of the decline of indigenous industries, *Meiboka* also tried to invite factories of modern industries to their region. Modern industries responded this in order to reduce wage costs. Company towns spread rapidly all over the national territory. The newly established modern factories induced the growth of supporting industries through Marshallian external economy caused by the agglomeration effects of modern factories. In various regions there emerged similar supporting industries. As time goes on, the nascent supporting industries began to organize industrial associations. In the interwar period the number of newly established associations (including non-industrial associations) increased sharply from 57 during 1868-1893, and 72 during 1894-1913 to 195 during 1914-1931, and the share of economy-related associations was highest during 1914-1931 (Tsujiyama Yutaka 1988, p 61). The purpose of establishing industrial associations might have been diverse, ranging from informational needs to mobilizing of power to work on the government for support. It is conjectured that the organization of national-level industrial associations had effects in weakening the existing regional ties, although serious research is left as future agenda.

(3) Class Conflicts

(3-1) Socialism and Class Conflicts

In the modern industries labor disputes increased significantly after the First World War reflecting the spread of Marxism among activist workers, the impact of the establishment of Soviet Union as well as the stagnation of large manufacturing concerns in industries such as shipbuilding. It is worth noting, however, that class conflict was not

established to any significant extent in Japan despite the surge of labor disputes in the interwar period. There are several reasons for this. First, socialist movements were seriously oppressed by the government, and the frequent changes in the strategy of Comintern (Communist International) caused confusion of the communist party strategies. Second, Japan did not have a tradition of class conflicts in agriculture in the sense of conflicts between those who have production means and who do not. Tenancy system did not cause this kind of conflict, because tenant farmers were not hired laborers but “managers” of agricultural production firms. There did exist a small number of large-scale farming utilizing hired labor in Japan around the turn of century, but overwhelming portion of agricultural production was implemented by household farming with family labor.

The third and perhaps the most important reason was the gradual development of the Japanese-style firm system after the interwar period and the consequent tendency towards labor immobility across industries. Afraid that intensification of labor disputes might endanger smooth capital accumulation, owners and managers of large firms extended long-term employment and seniority-based wage system towards middle managers. Because credible promise of long-term employment prevents hold-up problem, firm-specific skill formation started to prevail among middle-managers and, then, among white-color workers in the interwar period. The long-term employment system and firm-specific skill formation diffused among blue-colors after the Second World War, as is discussed in detail in Teranishi (2007). With the consequent disappearance of differential status between white and blue-color workers, labor union came to be organized for each firm irrespective of differences in occupation. In this Japanese-style firm system, workers, management and shareholders share the value-added of a firm within a stakeholder society framework, and class conflicts disappeared. Teranishi (2005) presents a detailed explanation about the process in which intense class conflict flared up during the occupation period²⁰ after the Second World War was replaced by inter-industrial conflicts

(4) Inter-industry Conflicts During the Postwar High-Growth-Period

With the establishment of Japanese-style firm system and the sharing system of value-added among stakeholders at individual firm level, a mechanism to determine the value-added for each firm and to distribute it between labor and capital was needed. During the high-growth period after the Second World War, this was accomplished by the inter-industry conflicts, accompanied by intervention by the government in the competitive conditions of industries through industrial associations and the collective wage bargaining (Teranishi 2005).

The government controlled competitive conditions of industries through various measures applied on industrial associations such as intervention in cartel agreements, capacity and equipment adjustment in declining industries, and manipulation of infant industry protections. Regulation of competition resulted in prices that were higher than a

competitive level. When competition in almost all industries was controlled in this way, both input and output prices were at higher-than-competitive levels for each industry. The level of output was thus a function of the controlled prices. It follows that the value-added of each industry was controlled by the competition-preventive measures. Both input and output prices were affected by the policy-induced rents caused by regulations. If the rents included in the output prices were higher than the rents in input prices, the value-added of the industry would be higher than a level determined through perfect competition, and lower if the rents were less.

The collective bargaining system determined the wage level for each industry. More exactly, the standard base-up rate for each industry was determined at the bargaining that took place in spring every year. The collective bargaining system and the government intervention through industrial associations together functioned as a mechanism to determine the value-added of each industry and to distribute it between wages and profits. That is, because the system's competition preventing policies yield policy-rents, the value-added determined in this way was higher than a competitive level in industries with stricter regulations, and lower than a competitive level in industries with milder regulations.

During the high-growth-period, the competition preventing regulation was stronger for declining industries such as agriculture and much milder for rapidly developing industries such as auto-industries. This meant that through this process of inter-industrial conflicts innovation rents accrued in auto-industry was spilled over to agriculture. With the role of intermediate organizations fulfilled by industrial associations, smoothing of income distribution was pursued in this system. There was no monopolization of the benefits of modernization by rapidly developing industries and, at the same time, no monopolization of regulation rents by the winning coalition.

(4-1) The Johnson-Noguchi Theory

As far as the historical experience until the high-growth-era is concerned, the hypothesis of Japan as a development-oriented state is the most popular idea that was considered to capture the essential characteristic of the Japanese economy. This hypothesis was most eloquently spelled out by two authors; Chalmar Johnson and Yukio Noguchi. Johnson (1982) derived this hypothesis through tracing the historical experience of MITI going back to the Ministry of Agriculture and Commerce in the Meiji period, and Noguchi (1995) by way of a comparison of the economic system of high-growth-era with that during the Second World War. The logic of Noguchi is much more cautious than that of Johnson in the sense that Noguchi was aware that the high-growth-era system was introduced as a system to solve income distributive problems. However, for the sake of simplicity we will not touch upon the difference.

The impact of these two literatures had been enormous, partly because it was congruent with the Marxian view of the Japanese economy that emphasizes planned and

bureaucracy-driven development. This hypothesis, however, is wrong with two important respects; first, regarding the methodology of reasoning about the way in which the political decision mechanism chooses an economic system, and second, regarding the purpose or basic philosophy of establishing the high-growth-era system.

Let me explain the first point. Both Johnson and Noguchi argue that the development-oriented bureaucrats who had carried out wartime planned economy survived until the postwar growth period, and since they had enormous power in the implementation of industrial policy, Japanese economy had become development-oriented. Ostensibly, this logic is analogous to the controversy about which of politicians and bureaucracy has stronger power in policy implementation. This analogy, however, is wrong because in the democratic society both politicians and bureaucrats are agents against the real principal, the constituents. The decision about to what degree market mechanism is utilized in an economy is the theme decided by the constituents or the median voters of the society. Both politicians and bureaucrats must obey the decision of the constituents. In other words, unlike the political decision regarding local public goods such as the tariff rate of particular product, this issue is the area for the general-interest politics. In this sense, the fact that development-oriented bureaucrats had strong power in policy implementation has nothing to do with the issue why Japan has become development-oriented. The logic of both Johnson and Noguchi is based on complete misunderstanding in this regard.

(4-2) The Purpose of the High-Growth-Era economic System

The drawback of the hypothesis, Japan as a development-oriented state, is more serious with respect to the second point. The hypothesis implies that the high-growth-era economic system of Japan was established with the purpose of facilitating economic growth thorough growth-oriented industrial policy. Let us explain why this assertion is wrong. There are two reasons; first, the regulations are mainly targeted toward declining industries, and second, the system was established so as to avoid the failures of prewar system based on almost pure market principle without any formal measures to improve income distribution.

Let us start with the first point. As is explained above, the regulation system of the high-growth-era economy could be summarized as a system to control competitive conditions of each industry so as to determine the value-added of each industry and the division of the value-added into profit and wages. It is important to note that in this system, competitive conditions were most severely regulated in declining industries. In the case of growing industries, value-added could be high enough without any control of competitive conditions. There is no denying that bureaucrats in such bureaus as MITI tried to use this system of controlling income distribution among different industries as a tool of industrial policy. Although they were eager to apply the policy toward growing industries, however, such efforts were by and large ended in failures as was typically seen in the case of

Temporary Measures Law for Special Industries in 1962.

The second reason why the assertion that the high-growth-era system was established for the developmental purpose is wrong is that the actual process of the establishment did not underline this assertion. In this regard it must be noted that the postwar economic system was established so as to avoid the instability of socio-economic system due to the aggravation of income distribution and the fragility of the banking system. The banking system just after the war was on the verge of death because of the huge loss caused by the moratorium of wartime loans. In order to save banks from bankruptcy, control of various interests including the prices of national and corporate bonds were introduced. Although such controlled interest rates were utilized by bureaucrats for credit rationing purpose, it is important to note that the original purpose of interest rate control lied in securing the safety of the banking system, not in the developmental credit rationing (Teranishi 1993).

With respect to the improvement in income distribution, there had been three alternatives to represent conflicting interests of people about income distribution. The first alternative was to revive the prewar-style order based on the interest representation by regional communities. The second alternative was western-type socio-democratic mechanism, in which distributive interests of the people is represented by classes such as labor and capitalist class. For the reasons explained above, these two strategies to attain equitable growth was not attainable, and the third alternative of representing distributive interest by each industry emerged as the workable distributive mechanism congruent with the Japanese-style firm system.

In sum, the postwar economic system was established with the purpose of realizing an equitable and stable socio-economic system. Although the competition-preventing mechanism introduced for that purpose was utilized by some development-oriented bureaucrats by means of industrial policy, it was not the original intention of the system. Two qualifying reservations should be added here. First is the role of the state. Although I have argued that intrinsic mechanism that gave birth to intermediate organizations realizes income distribution-smoothing effect, neither the role of inter-regional rivalry nor inter-industry adjusting mechanism are sufficient to bring about income smoothing. For the sake of effective working of intermediate organization role of the state to use the intermediate organization to utilize the mechanism to the realization of smooth income distribution and at the same time the bureaucrats who are in charge of this mechanism should be motivated to pay attention to income distributional aspects to some extent. In this regard prevailing economic thought might play an important role for the successful working of the system. For the sake of simplification of the model this paper did not touch upon this issue, but it is certainly an important task undertaken in the future research. The author owes this point to the comment by Satoshi Miyamura. Second, it is important to note that we are not talking about redistributive aspect of income distribution but touching upon the issue of direct determination of income distribution, which is the direct result of the working of the economy equipped with intermediate organizations. The author is also greatly thankful to Michael Carter for pointing out this. In fact many of

comments regarding the applicability of postwar Japanese experience to African ethnic issue are related to the misunderstanding regarding this point. This paper is not talking anything about income redistribution. Further, it is extremely important to note that the model of postwar Japan is not a zero-sum but positive some game, in which innovation rents accruing to growing industries play crucial roles. In this sense we are talking about inclusive growth strategy within the framework of a pro-growth model.

(5) A Digression; Failure of Koizumi Reform

(5-1) Defects of the High-Growth-Era System

The competition-preventing system of the high-growth era has come to suffer from various defects after the 1980s. First, the coordination of regulations across various industries had come to face difficulties. Responsible for this were international criticism against non-tariff trade barriers, and dissatisfaction of the middle class, who were eager to pursue affluence in consumption and denounced the system that caused high prices of consumption goods. Second, there occurred sentiments of anti-Japanese firm system in the form of criticism against “company man” or “over-work death”, leading to weakening loyalty to the system by the rapidly expanding new middle class. Third, excessive intervention by pork-barrel politicians and bureaucrats also invited criticism of the system.

Unless we move to the Western-type socio-democratic system, the best and the most practical solution for these problems is to carry out repairs of the government-private sector interface in order to alleviate or correct various defects. In view of the experience during the interwar or period just after the war, it would be best to present multi-dimensional system of interest representation and social solidarity. In those periods there were three alternatives; region (interest representation through local communities), industry (adjustment of inter-industry income differences and solidarity based on industries and firms) and class (interest representation by the ownership of production factors; labor and capital). In the future, considerations of historical path dependence would dictate that industry remains to be an important axis for interest representation focusing on weak side of industrial structure. In view of growing criticism against the excessive centralization of economic system, local communities could again be a core of interest representation; competition among regions with respect to living conditions, social welfare and employment opportunities is expected to activate the economy. Moreover, in view of the increasing conflict of interests among different generations, it would be necessary to incorporate a system of representation of inter-generational interests, which alleviates the distributive conflicts over public works, social pension system and environmental issues.

(5-2) The Logical Structure of Koizumi Reform

The Koizumi reform implemented during 1998 and 2002 when Japan was struggling to overcome the shocks caused by bubble burst and ensuing stagnation, however, was based on entirely different logical ground, and in the author's judgment, ended up with serious negative legacies. It is not the intention of this paper to assert that the postwar system of inter-industrial representation was the best and optimum system as a system of intermediate organization, but the paper merely wants to suggest the system evolved as an only possible practical path-dependent solution in the circumstances faced by Japan. In order to understand this point, it is useful to note how Koizumi reform failed.

In the Koizumi reform, reform policies were introduced as a measure to revitalize the economy, after all the orthodox macro policy measures to rehabilitate the economy have turned out to be ineffective. The core policy, deregulation and structural reform, was justified by neo-liberalism, the dominant approach at the time, coupled with almost groundless theory that claimed Japan was a developmental state. Let us examine the logical structure in this regard.

As is well known, neo-liberalism was the pragmatic policy philosophy of Reagan administration in the US and the Thatcher administration in the UK. In the US, this theory was born as an anti-thesis toward populist policy of Roosevelt administration, biased toward labor protection (Shlaez 2007), and in the UK, neo-liberalism emerged from the criticism of the corporatism policy by socio-democratic administrations. The theory obtained popular support owing to the stagflation during the 1970s, caused by labor union activism and real wage rigidity (Bruno and Sachs 1985). In this sense neo-liberalism was a political philosophy in the context of class conflicts or interest representation by means of various classes. This was perfectly adequate for Western countries with strong tendency toward socio-democracy. In Japan, however, as already seen, we have discarded socio-democracy as a solution for distributive conflicts, and in the case of stagflation triggered by the Oil Shock, Japan had weathered it by means of flexibility of real wages by use of distributive mechanism related to inter-industry interests.

Let me expand the above point. The neo-liberalism maintains that the freedom of business activity in competitive markets is the best way to maximize the wealth of each country and the world (Harvey 2005). Free business activity means unfettered pursuit of profits, and this makes it inevitable for the labor to be repressed. The weak side in this model is the labor class, who do not have fixed capital (Roemer 1986), and hence, are subject to capitalistic exploitation by means of monitoring and coercion of efforts (Bowles and Gintis 1986). The central social welfare policy is the social safety net, which target at individual losers in the competition. On the other hand, in the case of Japanese model, the economy's weak side was firms in declining industries and small and medium-sized firms. This is completely different from the Western model. The high-growth-era system protected weak industries, hence firms in it as well as small and medium-sized firms. The labor market reform carried out by the Koizumi reform destroyed employment system in

declining industries and small and medium-sized firms, giving rise to massive dispatched workers and non-regular employees. This policy, however, was based on complete misunderstanding of the economic system in Japan.

Moreover, the doctrine of neo-liberalism gave rise to the so-called Washington Consensus in its application to developing countries, development-oriented states of Latin America among others: The Washington Consensus was IMF-World Bank campaign based on neo-liberalism against development-oriented states. Because of the strong influence of Johnson-Noguchi thesis, the policy prescription of Washington Consensus found a golden opportunity for its application in Japan.

However, this application was also based on an easy and wrong reasoning. During the 1960s and 1970s, there occurred rapid expansion of state enterprises in Latin-America in order to implement import-substitution policy. It was considered that government involvement was the most effective way to accomplish the policy, because the government was considered to have grips on the best technology and human resources needed in the policy. The strategy, however, incurred serious inefficiency and macro-economic instability. The labor disputes, most radical in case of state enterprises, caused serious inflation, which induced policy to overvalue exchange rates in order to keep urban CPI low. In this way inflation together with the inefficiency of state-enterprises due to the lack of competition led to balance of payment deficits, leading to the eruption of foreign debt crisis in the early 1980s. It must be noted that the inflation in Latin America was invariably triggered by the labor activism led by state enterprise employees. Their request for wage hike was quite often accommodated by budget deficits, directly leading to an increase in money supply, fuelling further inflation. Neo-liberalism was applied to this situation as a criticism of the over-expansion of government activity in the economy or over-presence of state enterprises which squeezed out private business activities (Kuczynski 2003 and Williamson 1990). This diagnosis was perfectly adequate in the case of Latin-American economies where class conflicts were major mechanism to adjust distributive issues and state enterprise had huge share in the economy. The situation of Japan, however, was quite different from this, where most of important economic activities were carried out by the private sector, and inter-industry adjustment, not inter-class confrontation and labor movements, were major mechanism to resolve distributive conflicts.

It seems that the transplanting of neo-liberalism by the Koizumi reform was carried out to the soil entirely different from Western world and in particular from Latin America. A basic reason for this was the popularity of the Johnson- Noguchi hypothesis about Japan as a developmental state, and the expansion of the neo-liberalism doctrine as an anti-development oriented policy. Another was the tactful strategy of the Koizumi administration to propagate neo-liberalism as the global standard. Finally, the attitude of economists in Japan was also responsible for this. Most of the major economists have taken accommodating stance in this regard. The stance of economists reflects the change in economic theory; as the criticism of Keynesian economics by monetarism

gained increasing support among the economists, the opposition toward neo-liberalism built on anti-Keynesian philosophy became weak.

6. Ethnic groups in Africa as Intermediate Organizations; Concluding Remarks

The initial system of intermediate organizations in Meiji Japan based on regional rivalry has a great resemblance to Africa, where ethnic rivalry based on tribal and regional coalitions is the typical system of intermediate organization. In Japan, the inter-regional system was converted into the inter-industrial system of the postwar period over time. It seems to be interesting to ask whether it is possible to convert the African system into inter-industrial competition system *a la* Japan.

Let us start from the examination of the nature of ethnic rivalry from the viewpoint of intermediate organization. Ethnic rivalry in Africa does not necessarily mean tribal rivalry. In the formation of ethnic groups, there are many identity-lines (basis) for division other than tribal division such as regional, religious, linguistic and so on. Having noted this, let us discuss the characteristic of ethnic groups in Africa as intermediate organizations.

Bates (1983) defines ethnic groups as coalitions which have been formed as part of rational efforts to secure benefits created by the forces of modernization (p.152); benefits that are desired but scarce. This definition implies two things. First, current ethnic on conflicts are of relatively recent origin, although in every civilization clan or tribe based conflicts are usually seen in primordial period. Second, it implies that ethnic groups are organized on an *ad hoc* base whenever it becomes necessary to secure benefits of modernization policies. In this sense, ethnic groups in Africa as an intermediate organization have characteristics that are pertinent to be classified as associations. This characteristic is most clearly seen at the time of voting, when formation of coalition or, more concretely, choice of identity line is quite flexibly made so as to attain maximum possibility to gain benefits after voting. In his interesting study about Zambia, Posner (2005) has shown that during periods of multi-party rule language group cleavages serve as the central axis of coalition-building, whereas during periods of one-party rule, tribal cleavages play this role.

This, however, is not the end of the story. In the formation of ethnic groups, we frequently see group identity is persistent and, despite the seemingly *ad hoc* choice of division line, involvement in a group means some kind of sunk cost investment. In this regard, ethnic groups in Africa have characteristics to be classified as intermediate corporations, whose basic characteristic is investment in organization-specific human capital. A readily noticeable investment in group behavior is related to the securing of benefits or acquiring of spoils of modernization. Posner (2005) notes that policies of colonial states generated incentives for people actively to invest in and cultivate the social distinction defined by the state. Wide range of formal institutions (including land tenure regulations, labor policies, civil service hiring practices, local government structure, and even the organization of judicial system) created incentives for Africans to invest in their

identifications as tribe people and language speakers (p.25). However, another important investment in the group behavior seems to be human tolls paid at the time of ethnic conflicts, which quite often involves serious violence. Historical experience or memory related to this point seems to be necessary to be taken into account. Bates notes that Clifford Geertz emphasized the role of consummatory behavior as opposed to instrumental view, which led to ethnic conflicts over issues other than the material advantage. In other words, ethnic conflicts occur even if it “didn’t make sense” i.e., even when costs exceed benefits of the action. Whenever organization-specific investment is significant, the development of an intermediate organization becomes path-dependent, and the emergence of multi-dimensional interest representation could not be readily expected.

(1) Purpose of Ethnic Groups in Africa

It seems that the purpose of formation of ethnic groups lies mainly in income distributional gain. As is emphasized by Bates, ethnic competition has rational basis and the rationality is invariably related to the securing of benefits of modernization. Considerations of other effects of intermediate organization such as efficiency with respect to contract enforcement do not seem to be a major motivation for the formation, even if it is highly possible that such effects do exist actually.

It is important to note that in the African system distributional conflict is a monopoly game. The rule of game is frequently expressed as formation of “minimum winning coalition” (Bates 1983 and Posner 2005). It is claimed that the purpose of group formation is maximization of individual benefits. In order to become a winning coalition different criteria of inclusion and exclusion are invoked on each occasion, and the size of the coalition or association that would insure maximum individual benefits to its members is chosen. A winning group tends to monopolize the gains extracted from the modern sector, exerting maximum efforts to secure benefits to members. In this way, ethnic favoritism works at its maximum; politicians in a winning coalition are forced to channel patronage resources to their supporting ethnic groups by resorting to legal as well as illegal measures. “Horizontal inequality” (Stewart 2008), inequality among culturally defined groups or among groups sharing common identities, is a natural outcome in this case.

(2) Experience of Japan and Ethnic Groups in Africa

The examination on the experience of Japan above suggests that a system of intermediate organization is not static even if the type of intermediate organization is intermediate corporations, but could be changeable over time, and that policies to improve a system could be effective. As a system to exert some influence on income distribution resulting from the free play of the market, African system of ethnic competition seems to be seriously unsatisfactory, involving harsh rivalry that tends to lead to monopolization of benefits by one group and exclusion of others. It seems to be desirable to dispense with

African-style resolution of distributive conflicts, and transplanting of Japanese-style resolution is an option worth exploring. As a concluding remark, let us discuss one possible strategy to convert African-style system into Japanese-style system. The proposed strategy assumes that the type of intermediate organization is that of intermediate corporations, and is in line with the recent emphasis on the development policy based on geographical agglomeration proposed by Otsuka, Sawada and Sonobe²¹, and the one based on human capital accumulation.

Our proposal is composed of three stages. First, ethnic rivalry originating various identity lines should be stream-lined into one that is mainly based on regional identity. Since regional identity is a most prominent identity line in ethnic competition, this stage could be supported by many policies. The policy similar to One-product One-village movement adopted in Japan could be one promising policy option. Second, a powerful industrial policy needs to be introduced so as to make the maximum of the benefits of agglomeration such as spillover of industry-specific information, promotion of the division of labor, and accumulation of industry-specific skills (Sonobe and Otsuka 2004). Economic development through agglomeration will give rise to Marshallian external economy, leading to the birth of various industries complementary to the region-specific industries. Third, as the sufficient accumulation of industry-specific human capital in each region proceeds and the proliferation of various supporting industries is accomplished, it would be possible to organize the representation system of inter-industrial interests, which could fulfill the role as a system of income distribution smoothing, inclusive growth *a la* Japan. A concrete procedure is to induce the organization of an industrial association for each supporting industry at national level, to let the industrial associations to cross-cut existing regional and ethnic economic ties, and finally to reorganize the system so as to be able to control competitive conditions of industries.

We have already touched upon the defects of the Japanese system that were brought to light during the 1980s. Let us conclude the paper by pointing out some of the merits of the system. First, competition and lobbying occurs at industry level, so that bureaucratic intervention is confined to competitive conditions, and hence to prices and value added at the level of each industry. This implies that the room for collusion or interlocking interests between individual companies and politicians /bureaucrats is usually kept to a minimum. Second, the intervention by government is implemented mainly by controlling competitive conditions, so that subsidies are not indispensable policy tools. It follows that the effects on macro-level government budget is almost zero, or budget deficits and their monetization are not necessarily accompanied by the policy. Third, since the policy of controlling competitive conditions targets only declining industries, its influence on growing industries is very negligible, so that usual fierce competition in the latter industry could lead to healthy growth of the economy as a whole. Alis Sindzingre and others raised various helpful suggestions regarding the usefulness of the concept of ethnicity in the framework of intermediate organization; especially important is the suggestion that the membership in ethnic group is determined by birth. To this comment, two tentative

responses are as follows; first, the role of education is most important to diffuse the birth-bounded nature of ethnicity, and second, actually African people seem to be quite flexible in utilizing various identifying lines in their economic and political activities, as is suggested in Posner (2005).

(Notes)

- 1) Rousseau was not only the father of French revolution but also the father of modern totalitarian democracy (E.H. Carr 1946).
- 2) Cooperation occurs when net present value of the gain from violation of the contract and the implied reward stream in the following periods be less than the present value from cooperating.
- 3) When a transaction is repeated indefinitely and if participants place a high weight on the future periods' rewards, cooperation can be sustained by conditioning future cooperation on past cooperation (Folk Theorem).
- 4) Theoretically, this is the end-game problem in finite-horizon games. Greif (2006 pp. 434-437) suggests two solutions to achieve cooperative solution in this case. The first is by altering the time profile gains from cooperation. Increasing the share of gains toward the end of the transaction or payment of a bonus upon retirement correspond to this. The second is by endogenously linking the reputational considerations of individuals from different generations. The case of intermediate organizations corresponds to this case. Like dynasties and family firms, this kind of social units serve as entities with infinite life-spans that mitigate the end-game problem.
- 5) This aspect is related to bargaining power among economic groups, which was first pointed out in Galbraith (1952). Concept of countervailing power was introduced representing the role of intermediate organizations offsetting the effects of market power of large firms. The study on pluralism by Truman (1951) and Dahl (1982) parallel this argument in political science.
- 6) It is shown in Teranishi (1998) that Brazilian case corresponds the former, and the Japanese case to the latter. In Brazil, concomitant with the intensification of the tendency to represent distributional conflicts by class struggle, the mobility of labor market seems to have increased during the 1960s and 1970s. In Japan, the emergence of the system of representing distributional interests by industrial associations seems to be accompanied by the prevalence of the workers with firm- and industry-specific skills or spread of lifetime and seniority wage system. In Japan during the postwar high-growth-period, intermediate organizations representing the distributive interests among people were a set of industrial associations; people lobbied the state in order to realize favorable policies for their industries through industrial associations. The government responded to the demand by intervening in the determination of value-added for each industry. In Brazil during the 1960s and 1970s, on the other hand, such interaction regarding income distribution took place

mainly through the representation of class interests; people lobbied the state in pursuit of better income distribution through class representation in the form of labor unions or employers' unions. The response of the government took the form of direct intervention in wage determination or wage-profit sharing mechanisms.

- 7) In his study about the trade relationship in late medieval Europe, Greif (2004) calls standing intermediate organizations as “corporations” and intermediate organizations organized as coalition as “segregation” in the society. When merchants get into informal contract relationships based on reputation building, such contracts are called “coalitions”. “Corporations” are considered to be characteristic organizations in individualistic society like Western Europe and “segregation” in collective societies like Islam countries and developing countries.
- 8) The Virginia school economists such as Tullock and Brennan and Buchanan, on the other hand, pointed out negative side of interest group equilibrium such as the conflict of interests between rent-seeking politicians and voters. For more on this point, refer to Persson and Tabellini (2000).
- 9) Okada (2003) examines literature on this point extensively.
- 10) Oishi (1961) p.386.
- 11) Since 1888. The number of prefectures (*huku*) had been 305 in July 1872 and 75 after November 1872.
- 12) At first, the Meiji government tried to introduce oppressive system neglecting previous customs (*daiku-shouku* system) in 1873, which did not work because of resistance by farmers.
- 13) Along with counties, in prefectures, there were also several administrative areas called cities (*ku*, *shi*), which comprised of 5 towns and villages usually. *Ku* was introduced in 1880, and came to be called *shi* after 1884.
- 14) *Gunkuchouson-hensei-hou* promulgated in 1878. Refer Oishi (1961), p.79 on this point.
- 15) By *Gunkuchouson-hensei-hou*, and officially by *Shichouson-sei* promulgated in 1888.
- 16) Officially stipulated in *Shichouson-sei*.
- 17) Revision of budget system in 1884 (Oishi 1961, p.388).
- 18) Land prices were estimated as discounted future revenue from the land (Arimoto 1959).
- 19) The basic reason for this was the end of diffusion process of high-yielding varieties and related technologies of rice production.
- 20) The occupation force, largely composed of ex-New Dealers or sympathizers of the New Dealers, was eager to promote labor union movement in Japan.
- 21) Refer to Sonobe and Otsuka (2004) and Sawada and Sonobe (2006) among others.

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