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In this issue:

Japan, Refutation of Neoliberalism

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No-one wants to talk about Japan these days. The conventional wisdom is that the bloom went off Japan's economic rose around 1990 and that the utter superiority of neoliberal capitalism was vindicated by the strong performance of the American economy during the 1990s. Furthermore, everyone is now convinced that China – whose economy is 1/8 the size of Japan's – is the rising economic power and therefore the appropriate object of attention.

But Japan is, despite everything, still one of the master keys to understanding the future of the world economy, because Japan is the clearest case study of why neoliberalism is false. Simply put, Japan has done almost everything wrong by neoliberal standards and yet is indisputably the second-richest nation in the world.

This doesn't mean that neoliberalism is wholly meritless as an economic theory or as a development strategy, but it does mean that its claim to be the *only* path to prosperity has been empirically falsified. Japan's economy is highly regulated, centrally-planned by the state, and often contemptuous of free markets. But it has thrived.

What follows is for space reasons necessarily a sketch and exceptions, subtleties, and refinements have been left out. Facts have been homogenized and caricatured to make structural fundamentals clear. But a reader who bears this in mind will not be misled, as detail analyses are available elsewhere.

Are We Lied to About Japan?

Contrary to popular opinion, Japan has been doing very well lately, despite the interests that wish to depict her as an economic mess.

The illusion of her failure is used by globalists and other neoliberals to discourage Westerners, particularly Americans, from even caring about Japan's economic policies, let alone learning from them. It has been encouraged by the Japanese government as a way to get foreigners to stop pressing for changes in its neo-mercantilist trade policies. It has been propagated by corporate interests who gain from free-trade extremism with respect to Japan. And it is promoted by ideologues committed to the delusion that only a *laissez-faire* economy can prosper.

This is a formidable set of potential liars, equipped with money, technical expertise, transnational reach and state power. The Japanese government is centralized, elitist, and quite capable of fudging statistics if it wants, particularly since there are few Westerners who understand Japanese accounting. National accounting is notoriously susceptible to creative accounting anyway, as the world learned at the time of the Asian Crisis of 1998. So the assumption that the standard published figures about Japan's economy are true is dubious at best.

Japanese culture puts a premium on maintaining "face" and other forms of polite public presentation that constitute literal falsehoods, or at least fictions, so it is a natural instinct for the Japanese to tell the West what it wants to hear about Japan's economy. Japan's government is heir to a Confucian tradition in which the public is told only what the rulers deem it should know. Journalists and academics, who in America or Europe would have challenged its version of the economy by now, are loyal collaborators of the system, not its critics. So from a Japanese point of view, there is nothing immoral, unusual, or terribly difficult about misrepresenting Japan's economic performance. In fact, because it is in the national interest, it would be unpatriotic not to.

A Crisis Invented to Fit a Theory

The idea that Japan is thriving is not so different from the received wisdom as one might think. The Western press has over the last few years been full of stories about Japan's deep gloom, but in point of fact, the *admitted* state of the Japanese economy – let alone its actual state – is simply not that bad and in any other country would be producing mild expressions of concern, not brazen crowing about a crisis sufficient to force change in the fundamentals of the system.

Even the Japanese government admits that Japan is not actually declining economically, but rather growing at about 1% a year (which has ticked up to 2% since these words were first written.) This is a better performance than many other nations in recent years. So even if one accepts the official statistics, Japan is not in anything like the death-spiral that *laissez-faire* mythology supposes. It is, at *absolute* worst, accepting all the public mythology, stuck in a gentle stagnation of slow growth. And that it may now be emerging from this simulated rut (partly because the truth was getting too hard to conceal between the cranes on the Tokyo skyline) only reinforces this argument.

And this stagnation, even if one believes in it, is (or was) at the top of a very high plateau of aggregate and per-capita GNP, so Japan is hardly suffering by any reasonable international standard. It is, *even according to the official figures*, the second-richest country in the world. It is doing far better than other economies which get better press because they conform more closely to the globalist model of what an economy ought to be. It is a vastly richer nation, for example, than Britain, which globalist magazines like *The Economist* like to depict as an economic leader because it genuflects, at least in theory, to the right neoliberal theories.

Furthermore, the Japanese system is deliberately designed to contain the usual forms of economic stress that produce shocks to the political system, like inflation and unemployment, so Japan's (quite mild, really) economic problems are miles away from having the political consequences needed to cause the radical revision of the system that see-what-they-want-to *laissez-faire* ideologues suppose. Is 5% unemployment, in the context of a family structure more intact than in any Western nation, a crisis? In what other nation would 5% be considered a crisis level?

Nevertheless, we are fed a neoliberal fantasy that Japan is in a state of economic crisis and that this crisis is forcing her to revise her economy to conform to the world-conquering American version of capitalism.

Penetrating the Illusion of a Failing Japan

It is not hard to see through the illusion of a failing Japan if one knows where to look. The key is to look at indicators not susceptible to manipulation by the Ministry of Finance in Tokyo. First among these are export statistics, which are hard to conceal as they show up as imports in the statistics of other nations. Some key facts, not denied by the mainstream media, that make clear that Japan's economy is thriving:

1. Japan's net exports for the decade of the 1990s, when she was supposedly in decline, were 240% of those in the decade of the 1980s, when everyone admits she was booming. How is this possible if her economy is falling apart? We are being asked to believe that in an export-centered economy, exports are booming and yet the economy as a whole is failing.

2. The standard of living in Japan rose significantly during the supposedly stagnant 1990's, so that the Japanese are now among the world's greatest buyers of high-end consumer goods of all kinds, a fact visible in the shopping districts and parking lots of every Japanese city.

3. Japan's foreign assets have continued to grow rapidly. IMF figures indicate they nearly quadrupled in the 11 years to 2000, an inevitable consequence of her relentless trade surpluses.

4. Although a declining Japanese economy would imply a declining yen, the reverse has been the case.

5. Japan is the world's largest exporter of capital, enabling her to play the leading role in shaping the development of other nations. Americans ideologues who crow about the "spread of capitalism" ignore the fact that in large areas of the world, including its fastest growing region, East Asia, it is Japanese-style capitalism that is spreading, largely through the subsidiaries and suppliers of Japanese corporations.

6. Japan's supposed problems with its government budget are in a category all their own when it comes to misunderstanding. First, Japanese government accounting is very different from European or American government accounting, and that what have sometimes been reported as deficits are in fact surpluses. Second, although Japan's ratio of national debt to GNP is indeed somewhat large, it is not grossly out of line with other nations whose economies are not characterized as being in crisis, and given Japan's higher savings rate, she can finance this debt easily.

7. Western press reports about the supposed crisis in the Japanese banking system are based on the false assumption that Japan's banks are similar to banks in the US and Europe. Because of their complex structural relationships to Japanese industry and to government, explained below, they are nothing of the kind. They have sources of stability to tide them over temporary difficulties that Western banks do not, and their rare failures cause far less disruption.

Japan's Economic System Only Makes Sense as a Whole

The Japanese economic system does not make sense when viewed in parts, as the significance of any one part of an economy is determined by its relations with the other parts. Westerners naturally assume, when looking at one part, that it exists in a context similar to the one it would inhabit in the American capitalist economy. But in Japan, it frequently does not.

For example, the Tokyo stock market, unlike the New York one, is an economically-minor sideshow to the real action, because most capital is allocated by banks, even when they use the stock exchange as a forum to execute this. Its failure to be a real capital market is made clear by the fact that the Ministry of Finance has on occasion forced the shares of individual companies to hover at arbitrary levels for various reasons.

The key to understanding the Japanese economic system is that it is not just a system of economics, but a system of *political economy*. This term – Adam Smith never used the word "economics" – is an older one and enjoys the key advantage of not covertly implying that the economic system is an autonomous sphere of human activity operating, at most, within a loose cage of politically-enforced property rights. This erroneous conception tends to further the *laissez-faire* delusion that state power is something alien that intrudes upon economic activity from without, and that the only important economic choice is between more and less state control.

A Non-Socialist Centrally Planned Economy

Japan is something that is virtually impossible by definition within the frame of reference of neoliberal economics: a non-socialist state-directed system. To over-simplify a bit, it is a centrally-planned capitalist economy.

Neoliberal economists are dimly aware of the fact that fascist and Nazi economics were centrally-planned but not socialist, but they tend to dismiss these economic systems because of the attendant political horrors and have made precious little effort to develop rigorous theoretical accounts of how they worked. As we shall see, the Japanese system has achieved many of the things the fascists wanted.

Modeling the Japanese System

The best way to model the Japanese system is to start from the conventional models of free-market capitalism and centrally-planned socialism and discuss how it differs from both.

In order to grasp what the Japanese have done, it is worth comparing it to Western attempts to achieve the same thing. For example, the Japanese have understood that the ambition of the advocates of the "mixed economy," like Hugh Gaitskell in the UK, to socialize the "commanding heights" of the economy, has some rational basis, in that it embodies the desirability for some government direction of the economy without a total Gosplan-style takeover.

But this aspiration was misinterpreted in classic socialism, which understood the commanding heights to be basic industries like coal, steel, and railways. The problem with this, however, is that these industries do not *command* anything. Important though they are, they do not constitute a lever by which the economy as a whole can be controlled; they do not issue orders to the rest of the economy which determine how it behaves. The supply of capital to business, however, does, and this is under state control in Japan. One way to think of the Japanese system is as a capitalist economy with socialized capital markets.

Capitalism Without Plutocracy

Another case in point: does capitalism require plutocrats? The classic capitalist answer is that somebody has to own productive assets with a view to maximizing their profit, some of those who do will succeed brilliantly, therefore somebody must be rich.

But the Japanese see this as wasteful, so their system is designed so that corporations, in essence, largely own themselves. Even when there are nominal outside owners, corporations are managed so that the bulk of the wealth generated by the corporation flows either to the incomes of present workers or to investment in the future competitive strength of the company, making the workers and the company itself the *de facto* or beneficiary owners.

Most corporate capital in Japan is owned by banks, and the banks are principally owned not by shareholders, but by other companies in the same *keiretsu* or industrial group. And who owns these companies? Although there are some outside shareholders, majority control is in the hands of the *keiretsu's* bank and the other companies in the group. So in essence, the whole thing is circular and private ownership of the means of production has basically been put into the back seat.

Actually nationalizing the means of production would produce all the problems that led to the wave of privatizations in many nations in the last 20 years, and is unnecessary anyway. The Japanese system makes a sly mockery of both capitalism and socialism.

Forcing Growth by Forcing the Accumulation of Capital

One key way in which the Japanese system differs from American capitalism is that it squarely faces a fact that neoliberal economists admit, but tend to do nothing about:

The rate at which any economy – capitalist, socialist, feudal, fascist or what have you – can grow is dependent on how much of its production is saved and invested, rather than consumed.

America does almost nothing to increase its very low savings rate. Japan has a very high savings rate and this is a result of deliberate government policy and the lynchpin of the entire system.

How do they do it? The architects of the Japanese system understood that the socialist and communist way to produce high savings, i.e. outright confiscation of wealth, is destructive of people's incentive to work (not to mention its other problems) so they did not implement it. They understood that by definition, savings = production – consumption, so they focused on repressing consumption.

This means, for example, deliberately restrictive zoning policies that keep Japanese houses small, and it means not having the various devices in place by which America subsidizes borrowing and makes debt easy to assume. As a result, the populace of Japan is forced to save a far higher percentage of its earnings than Americans do.

It is a mistake to attribute Japan's savings rate, or many of its other key aspects, to "culture," as Japan had the same culture before WWII, when her savings rate was low. It is the interaction of culture with deliberate state policies, *not* culture itself, that is key. The use of "culture" as a catch-all explanation by foreign analysts of Japan is an evasion of serious analysis.

Controlling the Economy by Controlling the Accumulation of Capital

The Japanese government deliberately channels savings into a limited number of financial institutions under its control simply by making sure there is nowhere else to put the money. For example, it has seen to it that the Japanese cannot just open a brokerage account at Merrill Lynch and invest their money in the American stock market.

This huge torrent of savings flows to a handful of major banks, which the government has under its thumb because banking is extremely regulated in Japan, enabling regulators at the Ministry of Finance (MOF) to crack down on any bank at any time they see it doing something they don't want it to. So the banks are subject to the whim of the government, which then controls the economy by controlling how the banks allocate all this capital.

The net result is that the world's second-largest pool of private investable capital is subject to the control of a few hundred elite bureaucrats in Tokyo. The leverage they exert by controlling where this capital goes is the key to all their power.

How Japan Avoids the Problems of Soviet-Style Central Planning

The real genius of this system is that it is so indirect. These MOF bureaucrats are not stupid. They have read von Hayek, watched the Soviet Union struggle, and understand perfectly well that classic Gosplan-style central planning is unworkable. So they do not even remotely attempt this.

They understand quite well that the day-to-day detailed operation of the economy is best left to the invisible hand, just like Adam Smith said. They do realize, however, as Adam Smith didn't, that it is possible to manipulate an economy that is 99% capitalist into being, essentially, a centrally-planned economy *if* the state controls the right 1%. And this "right 1%" is the allocation of capital, especially big capital.

The MOF uses its stranglehold on the allocation of capital to make the banks into willing servants of its mission to control the Japanese economy. The banks, which in this respect (but not others) function similarly to the classic universal banks of Germany, handle almost all the detailed work of figuring out which companies should be loaned money and for which projects. The MOF essentially sits back, audits their performance, and rewards or punishes as appropriate.

This elitism in the MOF's control of the Japanese economy explains why so many outside observers fail to see it at all, though if one approaches the literature on Japan with this in mind, one quickly sees which observers have grasped the game.

In the early days of the Japanese system, the government had to be more involved in the details of deciding which industries to finance, because the banks had not developed the necessary sophistication, and so a far larger role was played by the Ministry of International Trade and Industry, the famed MITI, which actually did perform the classic industrial-policy functions of picking winners *et cetera*. But as Japan's private-sector banks have become more sophisticated, the need for this has diminished, and the MOF has become the key to the system. (MITI is still around, because there are some more speculative parts of the economy that the banks are not expert in and so the government still needs it sometimes.)

What is All This Capital Seeking?

As noted above, the MOF's key role is to audit the performance of the banks in allocating capital. But what counts as performance? In a conventional capitalist system, that's an easy question: maximizing return on capital. But in the Japanese system, this is not so.

For a start, the capital in question, although nominally privately owned, is "captive" capital in that it has nowhere else to go if it is unhappy with its return. This seemingly minor fact changes the whole dynamic of the entire economic system, because it means that capital, rather than chasing the highest return, can be made to obey political directives. Obviously, from the point of view of enriching individual investors this makes no sense, but this is not the MOF's objective. The investors don't have their money stolen from them – Japan is not a Marxist society – and they certainly get *some* return, but they do not get the maximum possible return.

What the MOF *does* want is to supply huge quantities of cheap capital to Japanese industry to build up its long-term productive capacity. The MOF *wants* capital to be paid a low return so that

Japanese companies will enjoy the competitive advantage of access of cheaper capital than their European, Asian, and American competitors. In capital-intensive industries like the advanced manufacturing in which Japan specializes, this is a huge advantage.

From the MOF's point of view, neoliberalism is designed to selfishly benefit the investors at the expense of the nation as a whole. And the investors themselves lose in the long run as their greed for high returns bleeds industry by imposing on it a high cost of capital, undermining these industries in the long run. In the Japanese analysis, the return to society as a whole of having strong industries (high wages paid, secure employment, a strong balance-of-payments) is more important than returns to individual investors, though these must be respected to some extent.

A Successful Planned Economy

The natural question a neoliberal economist asks at this point is, how can the MOF make rational capital-allocation decisions? Isn't it an article of faith, vindicated by years of experience, that governments are bad at this and markets good?

Well, yes, which is why the MOF intervenes at only the very highest levels of this process, most of the work being done by banks and the large corporations beneath them in this hierarchical system. Banks in Japan are attached to large industrial groups called *keiretsu,* meaning that they are both tied into sophisticated networks of industrial expertise and have several layers of administration below them to do the detail work.

Much of the Japanese system operates similarly to similar corporate structures in the West, though it faces a deliberately altered set of incentives. Because these incentives are just a fact of life to most of the corporate managers facing them, they don't even have to know where they came from or why. Most of the system doesn't even know that it's centrally-planned, and doesn't need to.

If there is any question as to whether they have been able to make these high-level decisions correctly for the last 50 years, one has only to look at Japan's relative economic performance, which has made her by all accounts the second-richest nation in the world and possibly soon to be the richest.

Simply put, *laissez-faire* theory is just plain empirically wrong: a planned economy can work. Period. Empirical facts trump abstract theories.

Unfortunately for the political left, Japan's success equally makes a mockery of socialism, which may explain why her system has attracted so little affection in the West. It does not flatter anyone's ideological religion, left or right.

Wall Street Works, But Isn't It Awfully Expensive?

Essentially, the architects of the Japanese system looked at the classic capitalist economy and reached the exact same conclusion as the average member of the Western world: that most of it is rational, but that an absurdly high proportion of national income is wasted rewarding the tiny elite that performs the capital-allocation function. Wall Street types do their jobs reasonably well, but why not replace them with elite bureaucrats who will perform the same function for $90,000 a year apiece, rather than people who earn ten, or even a hundred, times that? After all, one can teach bureaucrats the same technical skills of economic analysis.

In the Japanese view, investment banking is a business which, because of its structural monopoly on extremely valuable information, tends to produce grossly excessive returns for those engaged in it. The capital allocation function is irrationally priced because the intrinsic bottlenecks of information make it impossible for new entrants to drive down returns. Therefore the market cannot be relied upon to rationally price it. Capitalism, paradoxically, is rational except at its very pinnacle.

But Aren't All Bureaucrats Idiots?

At this point in the argument, neoliberal ideologues object in one of two ways:

1. By making some snide comment about the rule of elite bureaucrats.

An acceptable point, but one should not confuse the effectiveness of economic bureaucrats with the cultural and social mischief perpetrated by bureaucrats in other areas of government. The cold fact is that even the economies of those nations that most closely conform to neoliberalism, like the United States, are regulated by elite bureaucracies such as the Federal Reserve Bank, the Financial Accounting Standards Board, the Treasury Department, and the Interstate Commerce Commission.

2. By claiming that without paying the elite bureaucrats at the MOF huge returns directly proportional to the performance of the businesses they allocate capital to, they have no incentive to do their jobs well.

This is just empirically false. The performance of the Japanese economy shows that they do their jobs very well, and the key to this is something the architects of the Japanese political economy have understood that American economics tends to lose sight of:

Economic rewards are not the only effective incentives for economic action.

Exploiting the Power of Non-Economic Incentives

The Japanese are well aware that a successful economy requires the motivating effects of pay differentials and opportunities to accumulate private wealth. They are not living in a hippie socialist fantasy. But they have understood, as neoliberal economists, with their purely economic view of the economy, have not, that economic rewards operate in a social context and that social rewards for economic achievement can be as effective as cash.

In fact, because of the diminishing marginal utility of money, it is *irrational* for an economic system to rely on purely economic incentives. If all you pay people in is money, it gets awfully expensive to maintain their motivation as you go up the income scale. How much money does society have to dangle in front of a billionaire to get him to allocate another five hours a week from leisure to the work needed to run the part of the economy he owns?

That is to say, money is an efficient motivator (measured in terms of what society has to pay relative to what it gets for its money) under some circumstances, which is why we have capitalism, but inefficient under extreme conditions (which is why the Japanese deliberately limit it.) It is no accident that Japan has one of the lowest levels of economic inequality of any major nation at the same time as it has one of the most hierarchical cultures. The incomes of the top fifth of the Japanese population are only 2.9 times that of the bottom fifth, compared to 9.1 times in the US.

The income differential between a Japanese CEO and an assembly-line worker in his company is much less than in America, but the social-status difference is much greater. This does not consist in a system of static class differences not identical with economic differences, as in Britain, which the Japanese rightly see as producing class antagonisms which harm social cooperation. It consists in a *dynamic* social status system embodied in such oddities as the fact that Japanese grammar itself expresses the difference in status between the interlocutors, the Japanese reverence for hierarchy, and a lot else.

The Japanese have understood that what people are largely pursuing in the workplace is not so much money as the respect of the people around them, and therefore maintain a sophisticated – indeed, bizarrely over-elaborate to the Western eye – economy of *respect* in addition to the economy of money. They have understood that a large part of what money-seeking individuals really want is just to spend that money on purchasing social respect, though status display or whatever, so it is far more efficient to allocate respect directly.

Did you really think people as obviously intelligent as the Japanese were doing all those odd-looking bows for nothing? Sure, these behaviors are derived from tradition, but there's a reason they kept these traditions and the West hasn't. Interestingly, this understanding on their part of the need for unapologetic status differentials contradicts the emphasis in Western socialism on a *culture* of equality.

It also follows that if society is to maintain status differentials without suffering withdrawal of social cooperation due to the resulting resentment of low-status individuals, society must contain these status differentials within strong overarching sentiments of social unity. Naturally, the Japanese are famous for this, too. It all fits.

Platonic Guardians of an Eternal Japan

Why are Japan's bureaucrats so effective? Well, an American can start by looking at those American bureaucrats who are generally conceded by most people outside the far left to be effective: the military. The two salient characteristics of the military hierarchy in the US are that it has a governing ideology of nationalism and it is motivated by non-economic rewards. Japanese bureaucrats at the MOF are the same. Like 5-star generals, they are no more than reasonably paid, but their real reward is in the form of status: they are recognized everywhere as outranking people hundreds of times richer than they are. They can demand to be recognized as equals by anyone in their society and as superiors by all but a few.

Plato would have recognized such men as Platonic guardians, who were produced in his *Republic* by a process the Tokyo University men who run Japan would recognize: an elite education, followed by long apprenticeship and combined with relative material asceticism, ruthless scrutiny by the other guardians, a tight in-group *esprit de corps*, and a guiding ideology of nationalism. Anyone who knew the pre-1960s Jesuits will also understand what is going on here.

The Long Time Horizon

One of the key advantages of Japan's system is that it enables the imposition of an exceptionally-long time horizon on economic decision-making. Few American corporations think more than 5 years ahead; the Japanese routinely think 15 years ahead and the architects of the system obviously thought 50 years ahead. Because capital is allocated, at the end of the day, by MOF bureaucrats and not impatient shareholders and mutual funds, there is no pressure for short-term returns. MOF bureaucrats know they will be judged by whether they succeed in building up Japanese industry in the long term, so this is what they aim for.

What Does it Mean to Build up Industry?

The key thing the Japanese have understood, which America, among others, has forgotten, is that a nation's long-term ability to pay high wages to its citizens depends on its having a strong position in monopoly industries. Monopoly industries are industries that have the strongly-entrenched competitive positions that enable them to charge superior prices on the world market. Boeing and

Microsoft are the classic examples in the USA.

The core Japanese belief is that the benefits to society at large – in the terms of classical economics the positive externalities – of having these industries are so large that the free market on its own will misprice their value and not produce enough of them. Therefore it is rational for government to artificially direct capital into them, whether or not they produce the best short-term return to investors.

The Usefulness of Cartels

If one's objective is a strong competitive position for the industry as a whole, cartels immediately recommend themselves as a means to this end. Cartels are a device of industrial policy that has essentially been repudiated by neoliberal economics, for two reasons:

1. Within a neoliberal framework, profits from a cartel will just be captured by private interests, so there is no public interest in allowing them.

2. Neoliberal economics has an *a priori* obsession with vindicating free competition as the best policy.

Because the Japanese system, as noted above, forces the profits of monopoly industries into either paying its workers well or building up the industry so it can do so in future, reason #1 is inoperative, and reason #2 simply never interested them. Once one has these two factors out of the way, the many benefits of cartels can be tapped into:

1. They enable the individual firms in a monopoly industry to avoid fratricidal competition that would only benefits foreign customers, not the Japanese producers.

2. They enable the extraction of additional investment capital from the domestic consumer market by imposing higher prices.

3. They enable scale economies in research and development and standards-setting, crucial advantages in high technology.

4. They enable Japanese industry to avoid bidding wars in buying foreign technology and raw materials.

5. They enable Japanese industry to share out scarce sales in times of recession, avoiding bankruptcy of weaker firms. Naturally, these firms will pay a price in terms of losing control and will be whipped into shape, but they, and their workers, will not incur the traumas and layoffs of bankruptcy.

6. By enabling government-led control of prices and profits, they enable the government to pump in subsidies to favored industries with the confidence that these will go to building up the industry and not simply "wasted" as private profits to the shareholders.

Naturally, the Japanese are wise enough to the benefits of some competition that they don't simply agglomerate entire industries into "national champions," as several European nations have sometimes tried to do. A regulated cartel delivers the best of both worlds.

Manipulating Corporate Behavior Through Corporate Structure

Japan's key banks each sit at the apex of a pyramid of cross-shareholding companies called a *keiretsu.* This has a number of important consequences, each coordinate with the overall aims of the system.

1. Because each *keiretsu* links companies with their upstream suppliers and downstream customers, this biases customer-supplier relationships towards long-term relationship-based, rather than short-term transaction-based, profit-seeking. The former is a key advantage in high-tech industries in which companies must make huge irrecoverable investments in research and development that will only pay off if they can count on stable relationships with customers and suppliers. Compare this to the American bias in favor of short-term business relationships, a bias that then leads to short-term business thinking that is mutually-reinforcing.

2. The *keiretsu* system helps force companies to select their suppliers from within the *keiretsu*, not from foreign companies who may offer lower bids. Although this is superficially inefficient, because it deactivates the “exit” option American-style companies have in their dealings with their suppliers, it is in the long term efficient because it enhances the “voice” option Japanese companies have to enlist the aid of the entire *keiretsu* in whipping an underperforming supplier into shape.

3. Because each *keiretsu* contains within itself companies in a wide range of industries, the bank at its apex can draw on a wide range of reliable and proprietary expertise concerning appropriate allocations of capital.

4. Because each company in the *keiretsu* is on a leash to its bank, policies that the bank (puppet of the Ministry of Finance) wants imposed, can be. For example, policies to keep desirable high-value-added jobs in Japan. When Japanese jobs move to China, they are jobs that the MOF wants Japan to shed so her workforce can move up into ones with higher value-added and thus higher sustainable incomes. Naturally, pressure from the bank alone isn’t enough to bring this about, and this policy depends on all the other policies that combine to make it economically feasible to pay Japanese wages for these jobs.

5. Because the *keiretsus* in effect create a monopsony for the purchase of elite executive labor, they can avoid the problem that American companies have of getting into expensive bidding wars for executive talent. This helps drive down economic inequality without all the problems of redistributing income through taxation. The emphasis in Japan on teamwork and consensus decision-making also helps prevent the accumulation of valuable proprietary knowledge inside any one head, which would then have excessive leverage to extract wealth.

Taking State Capitalism Seriously

State capitalism (of one degree and structure or another) is not unique to Japan. What is unique to Japan, or taken to its greatest extreme there, is serious thinking-through of what state capitalism means and what is required to make it work.

The French government, for example, would dearly love to be able to order companies to keep their plants in France open to serve its full-employment goals. But, consciously or unconsciously infected with a socialist class-struggle mentality, it considers the cost of doing this “the company’s problem,” not its own, with the predictable result that it barks orders at companies that simply cannot afford to do what the government wants them to.

The Japanese government, by contrast, understands that if it expects companies to provide full employment, it must provide them the wherewithal to achieve sustainable competitive advantage, and it does so by guaranteeing them a supply of cheap capital, as explained above, by protecting them from foreign competition, and by other means.

Sustainable Competitive Advantage In Hard Industries

I have thus far only described Japan's economy in the abstract. The concrete consequence of her policies is an emphasis on advanced manufacturing as a sector, because:

1. Advanced manufacturing is that sector which is most able to pay sustainably high wages to ordinary workers.

2. Advanced manufacturing is that sector which is most susceptible, because of the proprietary know-how involved, to the acquisition of sustainable competitive advantage.

3. Advanced manufacturing is that sector whose produce is most exportable, a key consideration for a nation that must import most of its raw materials and energy.

Lifetime Employment Aligns Incentives

Japan's famed lifetime employment system for core workers seems to the neoliberal eye inefficient, as it supposedly interferes with efficient hiring and firing. But it has a key benefit in a system designed around maximizing long-term rather than short-term success: it aligns the interests of the worker and the company to a much greater degree than under a hire-and-fire system. (Of course, Japanese companies have ways of disciplining bad employees short of firing them.) And since their long-term orientation leads to an emphasis on maintaining sales, not profits, in slack times, they tend to avoid the layoff cycles that Western companies endure.

Lifetime employment also gives companies an incentive to invest in giving their workers expensive technical training, since they know the workers won't just jump to a competitor once they have it. Since a highly-trained workforce is one of the absolute keys to success in any advanced sector of the economy, this is very important. And lifetime employment forces *executives* at the company to care about its long-term success, rather than just to pump the company for quick profits during the few years they are there.

Furthermore, the architects of the Japanese system understand that as a sociological and political matter, providing lifetime security to a core group of male "breadwinner" workers confers stability to society as a whole, especially when combined with a traditional male-dominated society that has stronger inter-generational obligations (to care for the old, for example) than most contemporary Western nations.

Ending the Marxist Curse of Alienation

Lifetime employment helps nourish the emotional bond between the worker and the company, which is also expressed by such things, which seem silly to Western eyes, as company songs. These make perfect sense within the context of Japanese culture.

Americans tend to forget that Marx wrote so much about alienation, (which we tend to associate with teenagers with purple hair, not with serious economic questions) for a reason: he saw this as the key *psychological* phenomenon, in the head of the individual proletarian, that makes him a revolutionary. Alienation is important.

The Japanese were acutely aware of the Marxist challenge to capitalism, and they internalized this problem by taking seriously the elimination of alienation. The West really has not, choosing to smother it with consumerism while doing nothing about the phenomenon itself, resulting in the central weirdness of Western culture since the 1960s: the fact that our culture, from rock music to academia, is centered on the institutionalization of rebellion.

Unsurprisingly, Japan had no “60s” on our scale, and maintains levels of traditional morals (their traditions, remember, not ours) and deference to authority that remind most Americans and Europeans of the 1950s. This achievement is under certain stresses, as Japan is not immune to the corrosive forces of modernity any more than any other society, but it remains intact to a remarkable degree.

Fascism Without the Fascism

If the use of non-economic incentives sounds familiar, it is because the last time this issue was seriously addressed in the West in the context of a modern economy was by Peter F. Drucker in his 1940 book *The End of Economic Man*, which discussed how the Nazi system was based on creating a non-economic power structure to resolve the social conflicts that had been irresolvable within capitalist European society. This, in his view, was the sick genius of Nazism and the reason it had been able to come within a hair’s breadth of creating a world-conquering social system.

The political economy described above is the product of thinking that originated among Japan’s colonial bureaucrats entrusted with the industrialization of Japan’s colony of Manchuria in the 1930’s. They published their *Economic New Structure Manifesto* in 1940 as a result of their experience of the inefficiency of traditional capitalism as a development strategy. In the short run, the elite *Zaibatsu* capitalists of Japan vetoed their ideas, but in the long run, partly as a result of the American occupation’s assault on the big property owners, a product of their New Dealers’ conviction that industrial concentration was an abettor of fascism, they were able to triumph.

One way to describe the Japanese achievement is to say that they have achieved what the Nazis wanted to achieve but didn’t, largely of course because they were mad serial killers obsessed with a lot of things other than economics. Ironically, Asiatic Japan comes closer than any nation on earth to what Hitler wanted. It is a socially conservative, hierarchical, technocratic, orderly, pagan, sexist, nationalist, racially pure, anti-communist, non-capitalist and anti-Semitic society.

Of course, it would be unfair to describe contemporary Japan as Nazi-like in any of the senses that are notorious (though one cannot help observing that she has never been contrite about her WWII actions the way Germany has.) More correctly, the architects of the Japanese system learned from their disastrous experience in WWII that the kind of society they wanted could not be achieved through a totalitarian predator-state and they calculated that it could be achieved through the forms, though not the content, of liberal democracy, which is how Japan presents itself.

The Japanese Model Makes Democracy (Almost) Irrelevant

One of the consequences of Japan’s long-term orientation that is least palatable to the Western liberal mind is that it has the effect of making democracy almost superfluous. The reason is simple: if the objective of the government is the long-term well-being of the nation, the means to this end have already been figured out, and execution has been entrusted to a bureaucracy with a track-record of success, then *there is very little for democracy to do*. What is there for the elected representatives of the people to debate? Particularly since serious debate about these questions turns on economic expertise they do not possess.

As a result, the Japanese Diet is essentially relegated to the “Tammany Hall” functions of a democracy: interceding with the bureaucrats on behalf of individual citizens and co-opting potential troublemakers by dispensing corruption. In fact, the bureaucrats, who control the spigot that dispenses the grease, like to keep the elected officials corrupt so that they can be disciplined at any time by the threat of running to the police. As a result, the supposed “democracy” in Japan is a trivial and compliant rubber stamp for the bureaucratic elite, who operate under enabling laws that give them the legal basis to do as they see fit. Since anyone seriously interested in running the country went into the bureaucracy long ago, there are few representatives in the Diet with any inclination to challenge this system, which gives them the perks and popularity that elected officials really want.

Japan is not Really a Liberal Democracy

In terms of the fundamentals of contemporary political philosophy, the key issue this all raises is whether Japan has refuted the idea that running an advanced society requires freedom. This assumption, which is not without evidence, is the absolute cornerstone of the contemporary Western assumption that the increasing economic development of the world may be presumed to have an ultimately benign political outcome. It impinges on a whole host of crucial issues too numerous to discuss here.

Japan has preserved, of course, the nominal forms of liberal democracy. But she has systematically drained them of content, just as she has drained capitalist institutions like the stock exchange of content. But if these forms are not necessary to the system, then both Peter F. Drucker, who has argued that an advanced society must be a free society, and Francis Fukuyama, who has argued that liberal democracy is the ultimate state of human ideological evolution, are wrong. The significance of this is incalculable.

Japan is thus a far more important example of the famous Asian “soft-authoritarian” model made famous by Singapore, and the challenge of this model is far more profound than people realize. This is particularly so given that China is desperately trying to construct a sustainable regime without risking the national disintegration that she quite reasonably fears attempted democracy would cause.

Theoretical Implications

Not only has economic history not stopped, but the range of alternatives exceeds the conventionally assumed one between capitalism and socialism. Perhaps the Japanese system is capitalism of a sort, but if so, it is a capitalism in which private capital is not the dominant organizing principle of the economy, so I would dispute this.

As nationalists, the Japanese only want their system to serve them and have no interest in winning ideological arguments. They will not make significant efforts to disabuse foreigners of their economic theories, especially when these theories make foreign nations accept their trade surpluses.

Japan’s economic achievement refutes the proposition that neoliberalism is the only route to economic success. This does not mean, however, than all neoliberal theory is false. Clearly, within rationally-defined limits, much of it is true.

Practical Implications

This does not all mean that nations setting economic policies can ignore neoliberal prescriptions willy-nilly and expect not to pay a price. The Japanese system is a sophisticated construct that requires some of the world’s most skilled economic managers. Outsmarting capitalism is not a game for amateurs.

The Japanese system is a *system*, so one cannot just copy any piece of it and expect it to work outside its original context. But some pieces depend upon things that are sufficiently similar in other economies that they are plausibly imitable. For example:

1. Any nation can usefully increase its savings rate, not necessarily by Japan's means.

2. Any nation can prop up working-class wages by not importing cheap foreign labor.

3. Advanced nations can benefit from carefully relaxing anti-cartel laws to allow cooperative R&D, as in the Sematech consortium in the US.

Other policies, like lifetime employment and cartel price-fixing, would clearly be a disaster if simply imposed, because they need constraints supplied by the rest of the system to ensure that the benefits are socially diffused and not just captured by narrow interests.

The lynchpin of the system, politicized capital allocation, probably cannot work in a democracy, as it would just result in plants being built in the districts of powerful parliamentarians and would not make investments whose payoff exceeded one election cycle. Naturally, kleptocratic oligarchies wouldn't be good at it either; politicized capital allocation is only likely to work under highly Platonic systems like the MOF. And even then, there is no guarantee: power still corrupts and one can easily imagine such a system becoming inbred and perverse. Japan's achievement is an empirical fact, not a guarantee to all eternity.

Other policies fall in between the imitable and the inimitable, like the emphasis on advanced manufacturing, an extremely complex topic.

Still other policies, like protectionism, can only be rationally evaluated in the context of a general debate on the topic of which the Japanese case is but an important part.

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Three Arguments for Pluralism in Economics[1]

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Is there a single correct alternative to neoclassical economics? The purpose of this short paper is to suggest that there is not, and to show that this fact is increasingly recognized by eminent practitioners of several varieties of heterodox economic theory.

For most mainstream economists, of course, there is only one way to do economics. It requires the construction of a model, collection of relevant data and subsequent testing. The model itself must be consistent with the fundamental principle of methodological individualism: that is to say, it must be based on the assumption of optimising behaviour by rational agents. The tests must employ the most advanced econometric techniques rather than – or at least in addition to – descriptive statistics. For the defenders of mainstream economics these simple rules are what make it a science, which is envied and increasingly imitated by the practitioners of less favoured disciplines in the areas of management and social studies (Lazear, 2000).

This is a seductive story, and it is widely believed, inside and outside economics (Fine, 2000). When applied to the more disreputable branches of business 'thought' there is probably something to be said for it. If, however, it is taken as mandating the liquidation of sociology, political theory, social psychology and anthropology as autonomous bodies of scholarly knowledge it is obvious nonsense. As a methodological prescription for economics it is, to say the least, very questionable. In what follows I examine three counter-arguments, each making a different case for pluralism in economic thought. Two of the authors I cite are followers of the Cambridge economist Piero Sraffa, one is an institutionalist, and two are Post Keynesians

Apart from Pierangelo Garegnani, Heinz Kurz and Neri Salvadori are the two most prominent and tenacious defenders of modern-day 'classical' economics, by which they mean the study of the laws governing the pace of accumulation and the way in which output is distributed between the social classes, by means of a rigorous long-period analysis of a competitive capitalist economy. In a recent collection of essays they turn, rather surprisingly, to the defence of pluralism. Economic reality, they note, is widely believed to be very complicated. The questions that economists ask are therefore inherently difficult, and it is unlikely that they have simple answers. Since no theory can consider all relevant factors in any particular economic context, there is a strong *prima facie* case for theoretical pluralism. Different theories will often be complementary rather than alternative, so that 'to seek dominance for one theory over all the others with the possible result that all the rival theories are extinguished amounts to advocating scientific regress. To paraphrase Voltaire: in a subject as difficult as economics a state of doubt may not be very comfortable, but a state of certainty would be ridiculous (Kurz and Salvadori, 2000:237). Even classical theory has its limits. Kurz, in particular, has long acknowledged that it must be married to Keynesian macroeconomics if a comprehensive understanding of capitalist society is to be attained (Kurz, 1990).

In his latest book the well-known institutionalist Geoff Hodgson argues that the notion of a single, 'general' theory applicable to human behaviour in all societies, at all points in time, is a dangerous delusion that has led astray not only neoclassical economists but also many heterodox theorists. Failure to appreciate the need for historical specificity in economic theorising has not only blighted the work of several generations of general equilibrium theorists, but also reduced the analytical achievements of some of their most vocal opponents, including Clarence Ayres, John Maynard Keynes and Joan Robinson. One does not have to agree with all the names on Hodgson's charge-sheet (see King, 2002) to accept the truth of his contention that 'there are several problems with general theorizing in the social sciences. One is of analytical and computational intractability. Facing such computational limits, general theorists typically simplify their models, thus abandoning the generality of the theory. Another related problem with a general theory is that we are confined to broad principles governing all possible structures within the domain of analysis. In practice, a manageable theory has to confine itself to a relatively tiny subset of all possible structures. Furthermore, the cost of excessive generality is to miss out on key features common to a subset of phenomena' (Hodgson, 2001:16). Hodgson's own proposal for the reconstruction of economic theory, putting the history back, is innately and profoundly pluralistic (ibid.:chapters 18-23).

The Post Keynesians Victoria Chick and Sheila Dow make an equally powerful, if largely implicit, case for pluralism in their penetrating analysis of what is implied by mathematical modelling in economics. Formalising an argument is not, they suggest, an unambiguous improvement, as neoclassicals believe. On the contrary, it is a matter of costs and benefits. Formalism entails a particular view of the world, namely that it displays event regularities strong enough for it to approximate to a closed system. It also requires that the meaning of economic terms be fixed rather than context-specific, and that these terms are separable rather than internally related. If these assumptions are rejected, classical or formal logic is inapplicable and Keynes's 'ordinary logic' may be needed in its place. Ordinary, common-sense or human logic 'generates knowledge which is imperfect, partial or vague', and provides 'reasoned grounds for belief which are nevertheless not conclusively demonstrable' (Chick and Dow, 2001:711, 714). Economic statements may therefore be true in some historical and institutional circumstances, but false in others. Here Chick and Dow share common ground with Hodgson, since their argument casts doubt on 'the possibility of finding immutable laws applicable to, say, feudalism and capitalism alike, or even to capitalism in various stages of its development. From this perspective, a theory can be "right" at one time and become "wrong" (more accurately, outdated) at another. The notion of imbuing a closed theoretical system with meaning is thus not an objective procedure; it requires the exercise of judgement' (ibid.:709). In this way their critique of formalism leads them to pluralism, not just in substantive theory but also in method, since Keynes's ordinary logic 'supports a methodology which encompasses a range of methods in order to build up knowledge' (ibid.:719; cf. Dow, 1997).

Note that Chick and Dow do not completely deny the legitimacy of formalism in economics, in all circumstances, for all purposes. On the contrary: some problems lend themselves to closed-system thinking and cry out for precise, formal solutions. They argue only that it is a serious mistake to suppose that all economic problems are of this type. They would certainly disagree with Kurz and Salvadori on the size of the contribution that can be expected from formal reasoning. The two Sraffians, Kurz and Salvadori, follow Garegnani in placing great emphasis on the so-called 'core' of classical economic theory, which consists of propositions that can be established with certainty about the relationships between inputs, outputs, prices and distributional variables in a closed economic system where the same rate of profit is paid in all industries (Kurz and Salvadori, 1995). The two Post Keynesians, Chick and Dow, see very little point in exercises of this type, while Hodgson, the proponent of institutional economics, seems to deny their validity altogether. Certainly he shows no sympathy for those self-proclaimed institutionalists who use prey-predator models, chaos theory and similar sophisticated mathematical tools derived from the biological sciences.

If pluralism does not (quite) rule out formalism, what does it exclude? Unqualified relativism, for one thing; logical incoherence, for another. Hodgson is the most outspoken in denying that 'anything goes', and the most sternly critical of postmodernist claims in this regard. 'An acceptable policy of pluralism', he suggests, 'concerns the policy of institutions towards the funding and nurturing of science. Such a policy involves "pluralism in the academy". But it would not extend to the individual practices of science itself. This confusion, between encouraging contradictory ideas in the academy and encouraging them in our own heads, is widespread in post-modernism….There is much to be said for tolerance of many and even antagonistic scientific research programmes within an academic discipline or university. But we should not tolerate the existence of inconsistent ideas within our own heads. The policy towards science must be pluralistic and tolerant, but science itself must be intolerant of what it regards as falsehood…Any failure of social science to erect an adequate and coherent general theory is not rectified by applauding incoherence' (Hodgson, 2001:35). Horses for courses, as Geoff Harcourt has always put it (see Comim, 1999), but they must each have four legs and a jockey and proceed anti-clockwise around the course.

Sheila Dow has also defended the principle of consistency against its postmodernist and constructivist opponents. Thus she proposes that a clear distinction be drawn between 'pure' and 'modified' pluralism. To be a pure pluralist entails 'a refusal to appraise methodologoies and thus also [a refusal] to advocate one method rather than a plurality'. This, she maintains, offers 'no scope for scientific (or indeed any) discourse'. According to modified pluralism, however, 'no one system of knowledge can claim to have captured reality; each is partial, reflecting one vision of reality. Each school can support its approach to knowledge with reason while recognizing the legitimacy of alternative approaches….World-view and theory of knowledge cannot be eradicated; yet recognition of differences at this level allows for more reasoned debate over appraisal criteria and analysis of different methodologies' (Dow 1996: 45-6).

Kurz and Salvadori also insist on the need for logical consistency in economic theorising. For them this criterion is enough to rule neoclassical analysis out of the race, since its conception of capital is fundamentally flawed. If the 'principle of substitution' is central to mainstream theory, they argue, it should be applied in a logically consistent manner. In the long period, this means that an increase in the price of one input induces a decrease in the quantity of that input per unit of output. 'All propositions of the theory can be traced back to this basic idea. If it is not true in general, the theory appears to be in trouble' (Kurz and Salvadori, 2000:238). But it has been known since the mid-1960s that it is, in general, false when applied to the collection of heterogeneous commodities known as 'capital'. From a quite different perspective the Post Keynesian Paul Davidson has criticised what he terms the 'babel' of New Keynesian economics, in which market imperfections that prevent downward price and wage flexibility are denounced as the fundamental cause of involuntary unemployment while in the same breath a falling price level ('deflation') is decried as a serious macroeconomic evil (Davidson, 1999; compare Solow, 1997 and Taylor, 1997 for graphic examples of this incoherence). Horses for courses, once again, but all four legs must be pointing in the same direction.

No single case for pluralism in economics emerges from this brief discussion, and indeed it would be a cause for concern if one had. Similarly, there is no single version of 'unscientific' heterodox economics to stand in opposition to mainstream economic 'science'. Sraffians, institutionalists and Post Keynesians do quite different things, often in radically different ways – as do Marxists, social economists, feminists, greenies and other schools of political economy. As Abbie Hoffman is supposed to have said, in the course of the 1968 Chicago conspiracy trial: 'Conspire? We couldn't agree on lunch'. But they did agree to keep on talking, which in the last resort is what pluralism is all about.

Notes

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2. I am grateful to Sheila Dow, Heinz Kurz and Frank Stilwell for comments on an earlier draft.

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Liberalisation and Social Structure:

The Case of Labour Intensive Export Growth in South Asia

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Introduction

Neo-classical theorists argue that discrimination is impossible in a competitive market economy. Any firm or individual with a 'taste for discrimination' will be driven out of business by lower cost competitors who employ, trade and produce according to the criteria of profit and productivity maximisation. By this logic, free markets and free trade will allow a developing country to exploit a comparative advantage in labour intensive manufacturing and agro-processing. Such labour intensive growth will inevitably draw women for the first time into employment outside the home. Employed women will achieve an independent income and higher social status.

Neoclassical economics forgets economics is a branch of social theory. The outcome of liberalisation will be crucially dependent on the social structure of values and institutions in which it occurs. Where there is a pre-existing ideology of gender subordination (India and Pakistan) business has utilised this social structure to cut costs and fragment formal labour institutions. More egalitarian Sri Lanka has witnessed women being drawn into formal sector employment and receiving the benefits of independence, mobility and independent income.

Liberalisation, Efficient Growth and Labour Markets

In Neoclassical economics growth in a free market will reflect the preferences of rational individuals, growth must then by definition be efficient[1], each exchange will reflect mutually beneficial gains by optimising economic agents. 'Getting the prices right' will allow developing countries to exploit a comparative advantage in labour-intensive production and exports. Overvalued exchange rates discriminate against labour-intensive agro-exports and reduce the cost of imported capital goods. Minimum wage and other labour 'rights' raise the cost of labour and reduce the elasticity of employment with respect to output growth. Sometimes synonymous with removing 'urban bias', liberalisation could be better described as removing capital bias.

Numerous authors have highlighted labour market rigidities as being a key factor in explaining poor developmental outcomes in India[2]. Employment protection[3] has hindered restructuring in union dominated public sector enterprises. It became more costly and time consuming for firms to adjust to changing market conditions and absorb new technologies, legislation encouraged firms to remain small and informal[4], trading off access to formal credit and scale economies in order to avoid the strictures of labour legislation. Firms in declining industries were prevented from shedding excess labour and piled up losses; those in expanding industries were reluctant to hire new workers and so substituted labour for capital. The jobless growth in the 1980s is cited as evidence for this proposition. Minimal expansion of formal sector employment between 1980 and 1989 coincided with an increase in annual earnings per worker of 3.5% and large-scale substitution of labour for capital[5].

The supposed potential of labour-intensive growth in South Asia is demonstrated by post-Mao China. China's labour markets have proved highly flexible in the non-state sector. Formal sector employment increased rapidly from 95m in 1978 (9.7% of the economically active population) to 148.5m in 1994 (19.2%). In India by contrast formal sector employment has increased from only 22.9m in 1978 (6.8%) to 27.4m in 1994 (5.4%)[6].

Labour Intensive Export Growth and Gender

The crucial 'optimistic' Neoclassical assumption is that markets reflect mutually beneficial voluntary exchange. The spread of markets is thus by assumption proof that the economy is becoming more efficient.

Discrimination in the sense of paying workers of identical productivity different wages will not persist over the long term in a capitalist economy. Any employer refusing to employ workers on the base of colour, creed, gender or caste will be less profitable than a non-discriminatory rival. Over time the dynamics of competition will drive out those with a 'taste for discrimination', the logic of the market will separate discrimination from the process of production. In a broader sense the dictates of the market separate society from the economy.

"The bourgeoisie, wherever it has got the upper hand, has put an end to all feudal, patriarchal, idyllic relations. It has pitilessly torn asunder the motley feudal ties that bound man to his 'natural superiors', and has left remaining no other nexus between man and man than naked self-interest, than callous cash payment'[7].

'Female Employment Intensive' Growth

Historically labour intensive export growth has been associated in many instances with a disproportionate increase in the employment of women. In the textile mills of nineteenth century Britain, silk weaving in 1920s Japan, and electronics factories in the post-war Tiger economies. Wood[8] found a strong relationship between increased exports and increased female employment in manufacturing, the largest increases occurring in Mauritius, Tunisia, Sri Lanka, Malaysia and the East Asian Tiger Economies. In Export Processing Zones (EPZs) most labour is female, eighty percent in the Caribbean and the Philippines; this bias is especially strong in the garments sector[9].

Drawing women into the formal labour market will improve their economic status and social position. The relative respect and regard of women is strongly influenced by their ability to earn an independent income, being employed outside the home and having ownership rights. These factors are linked by the positive impact they have on strengthening women's voice and agency through independence and empowerment. With independent waged employment the contribution of the woman to the family's well-being is more visible, she is less dependent on others, the exposure to ideas outside the home makes her agency more effective[10]. An ability to seek employment outside the home can contribute to the reduction of women's relative and absolute deprivation.

Really Existing Markets

Neoclassical economists are quick to generalise this optimistic scenario to support an exclusive focus on liberalisation. However, re-rooting economics as social theory reveals such outcomes to be context dependent. Markets as they really exist do not accord to this hypothesised ideal, rather, they are embedded in wider social structures of values and institutions.

"Real markets are permeated by power relations of various kinds; they are embedded in social processes which may, for example, involve class exploitation or gender subordination; and they are saturated by divergent institutions, ideologies, ethical and cultural values.[11]"

The idea that liberalisation will remove politics from the economy and lead to a more rational and efficient allocation of resources is false. Markets are not politically neutral but are embedded in social structures. Just as government intervention can be distorted by an underlying political economy so too can markets. There is no neat dichotomy between state-regulation and market, rather both are meshed into existing social structures of (among others) caste, religion and gender[12] in South Asia.

Liberalisation can remove market constraints but not structural constraints such as patriarchal values that prevent equal access of men and women to markets. These are not just imperfections of the market but deep-rooted characteristics of society[13].

Social Construction of Gender in India

In India employers have utilised a pre-existing and intensifying ideology of gender subordination to undermine male unionised labour and replace it with low cost ruralised, casualised, and informalised female labour. In 1985, 250,000 people were employed in the Bombay textile mills, by 1996 this had declined to only 54,000. Women then constituted only 0.01% of the cotton mill workforce while accounting for more than 45% of the unorganised cotton handloom sector[14].

The social environment in which 'labour intensive' growth occurs is a crucial determinant of its net impact on women's agency. The missing factor to be controlled for is the pre-existing social structure of gender relations. The experiences of Sri Lanka and Pakistan offer sharply contrasting responses to liberalisation.

Sri Lanka and Pakistan: Empowerment and Exploitation

Sri Lanka has had traditionally good human development indicators, a 90% plus literacy rate and, compared with other developing countries, minimal gender disparity in education[15]. There has been a persistent upward trend in the educational attainment of males and females. Female literacy in 1995 was 87%, only marginally lower than that of men. In this context, of relatively equal gender relations liberalisation has had an empowering impact.

Liberalisation policies were initiated in 1977. By the early 1980s there was economic growth of slightly under 6% per annum. The fastest growing sectors since 1977 have been unskilled labour intensive manufactures, mainly garments and textiles. The structure of exports has indeed shifted towards Sri Lanka's comparative advantage. The institution behind this growth has been mushrooming Export Processing Zones (EPZ's)[16], set up in 1978, 1984 and 1990. 80% of the employment in EPZ's is female. The female-male ratio in manufacturing has increased from 25% to 80% between 1963 and 1985, total employment of women in manufacturing increased by 50% between 1977 and 1995[17].

In Pakistan by contrast, gender relations have historically been highly unequal, the sex ratio at 910 being even lower than that of India. Literacy, school enrolment and a persistently high fertility rate all point to the low status of women. Female primary school attendance is around 35%, among the lowest in the world. Female labour force participation is only 3.5% and represents severe crowding into low pay, low-skill occupations[18]. The labour market is also highly segmented, especially in urban areas where there is also widespread segregation between sexes.

The structure of modern industry in Pakistan is similar to that of Sri Lanka, consisting mainly of labour intensive processing of agricultural products as well as textiles and clothing. In 1992/93 textiles and garments accounted for 64% of total export revenue[19]. However on a pre-existing base of gender discrimination the gender composition of employment in textiles and garments is very different. In Pakistan it is a male intensive sector; 88.3% of urban textile manufacturing workers are men. As in India there is evidence of widespread contracting by garment enterprises that employ poor and young women. Most of this work is done in informal sector workshops or home based work. Such work by itself will have little impact on bargaining strength or increasing the social status of women. In fact there may be a contradictory impact by implicitly devaluing the implied worth of unpaid domestic employment and further marginalising those women without paid external employment.

"[I]n South Asian countries, women are rarely able or willing to work outside the marital home. In that case, wage work outside the house increases her work load because she is not in a position to bargain with others about sharing her housework.[20]"

Gender and Fragmentation of Labour in India

Structural adjustment in the 1990s has given impetus to the long-term trend of increasing market relations in South Asia. There has been no long-term improvement in the status of women in Pakistan or India. The logic of capital is not dissolving discrimination but working within the social structure of a pre-existing gender ideology and *intensifying* female disadvantage.

Female-Male (population) ratios have been declining in India since the beginning of this century. The 1991 Census showed a further decline in this ratio to 927 women for every 1000 men[21]. Mortality levels of women are abnormally high from birth until the mid-30s. Increased urbanisation, modernisation and economic growth have not improved these trends. In fact the lowest ratios are recorded in the richest states, Haryana and the Punjab. Using the ratio for Sub-Saharan Africa, Dreze and Sen[22] calculated there were approximately 37 million missing women in India in 1986[23].

Economic change is working within a social structure of female disadvantage. The north Indian pattern of anti-female discrimination is spreading southwards by means of cultural assimilation, and is not being undermined by economic change. Even in North India there is a pronounced process of Sansrikisation[24]. The dominant castes in the north are the martial and patriarchal Rajputs and Jats. Traditionally they have a pronounced gender division and obsession with honour. Honour is to a large extent a function of the conservative behaviour of women[25]. Lower castes in the north have been traditionally more equal, female-male ratios among tribes and Scheduled castes having long been significantly higher. Over time lower castes have been emulating, not opposing, the ideology of dominant castes. Practices such as restrictions on widow re-marriage and dowry have been diffusing down the caste hierarchy. The fall in female-male ratios has been generated by a convergence of ratios in lower castes to those of dominant castes[26].

Conclusion

Liberalisation is context dependent, not a neutral and deterministic process. The social structure within which liberalisation occurs has a crucial impact on outcomes.

Despite having levels of female disadvantage of a similar if not worse magnitude to India and Pakistan, throughout the 1990s Bangladesh has enjoyed rapid labour (female) intensive employment growth in the export-orientated textiles sector. There is evidence to support the proposition that a prior restructuring of social relations (by NGOs among others) has enabled this favourable outcome[27].

Economics is social theory. Neoclassical theory forgets social structure at the cost of relevance.

Notes

1. For a longer exposition see Matthew McCartney, 'Driving a car with no steering wheel and no road map: Neoclassical discourse and the case of India', *Post-Autistic Economics Review*, 21, 13 September (2003) article 5, http://www.btinternet.com/~pae_news/review/issue21.htm

2. See for example Peter R.Fallon and Robert Lucas, 'Job Security Regulations and the Dynamic Demand for Labour in India and Zimbabwe', *Journal of Development Economics*, 40 (1993), pp. 241-75; Roberto Zagha, 'Labour and India's Economic Reforms', in J.D.Sachs, A.Varshney and N.Bajpai (eds) *India in the Era of Economic Reforms* (Oxford University Press, 1999), pp. 160-185; Montek S. Ahluwalia, 'Economic Reforms in India Since 1991: Has Gradualism Worked?', *Journal of Economic Perspectives*, Vol 16 No.3 (2002), pp. 67-88; Timothy Besley and Robin Burgess, 'Can Labour Market Hinder Economic Performance? Evidence from India', LSE, *STICERD* Working Paper No.33.

3. The 1976 amendment to the Industrial Disputes Act required state government permission to carry out any retrenchments in a firm of more than three hundred employees. An amendment in 1982 reduced this figure to one hundred. The constitutional validity of this change was challenged and the second reform reintroduced as a constitutional amendment in 1984, Zagha '*Labour and India's Economic Reforms*'.

4. Only 7% of a labour force approaching 390m are in the organised sector subject to social security and labour laws.

5. R. Nagaraj 'Organised Manufacturing Employment', *Economic and Political Weekly*, Vol 35, No 38 (2000), pp. 3445-8.

6. Nirupam Bajpai, 'Sustaining High Rates of Economic Growth in India' *Harvard Centre for International Developmen*t, Working Paper, No 65, March (2001).

7. Karl Marx and Friedrich Engels, '*The Communist Manifesto*', (Penguin, 1967), pp82.

8. Adrian Wood, 'North-South Trade and Female Labour in Manufacturing: An Asymmetry', Journal of Development Studies, Vol 27, No. 2 (1991).

9. Martin Rama 'Globalisation and Workers in Developing Countries', *World Bank Develop*ment Research Group, Working Paper No. 2958 (2003), pp. 15.

10. Amartya .Sen, '*Development as Freedom*', (Oxford University Press, 1999), Ch 8.

11. Gordon White, 'The Political Analysis of Markets: Editorial Introduction', Institute of Development Studies Bulletin, Vol 24, No 3 (1993) pp. 1.

12. Barbara Harriss-White, *India Working: Essays on Society and Economy*, (Cambridge University Press, 2003).

13. Indira Hirway , Economic Reforms and Women's Work', in *Employment*' in T.S.Papola and A.N.Sharma '*Gender and Employment in India*', (Vikas, 1999), pp 356.

14. Ushma Upadhyay 'India's New Economic Policy of 1991 and its Impact on Women's Poverty and AIDS' Vol 6, No. 3, *Feminist Economics*, (2000), pp.108

15. Marzia Fontana, Susan Joekes and Rachel Masika, 'Global Trade Expansion and Liberalisation: Gender Issues and Impacts', *Briefings on Development and Gender*, Report No. 42, University of Sussex (1998), pp.23.

16. An EPZ is geographical location where foreign and/ or local investors are allowed to set up 100% export-orientated facilities, usually an array of incentives are granted such as tax holidays, access to duty free imported inputs and superior infrastructure.

17. Wood, 'North-South Trade and Female Labour in Manufacturing: An Asymmetry', pp. 168-89.

18 Shahid. J. Burki, 'Pakistan: Fifty Years of Nationhood', Third Edition, (Westview, 1999), Ch 4.

19. Fontana et al, '*Global Trade Expansion and Liberalisation: Gender Issues and Impacts*', pp. 25.

20. Nirmala Banerjee '*How Real is the Bogey of Feminisation?*' in T.S.Papola and A.N.Sharma '*Gender and Employment in India*', (Vikas, 1999), pp. 314.

21. Satish.B.Agnihotri, 'Missing Females: A Disaggregated Analysis', *Economic and Political Weekly* (1995), 19th Aug.

22. Jean Dreze and Amartya Sen, '*India: Economic Development and Social Opportunity*', (Oxford University Press, 1995), pp. 141.

23. There are a number of explanations for these disturbing trends, see Harriss-White, '*India Working: Essays on Society and Economy*'.

24. A process whereby lower castes emulate the practise and rituals of higher castes.

25. See Jean Dreze and Haris Gazdar, '*Uttar Pradesh: The Burden of Inertia*', in J,Dreze and A.Sen (eds), '*Indian Development: Selected Regional Perspectives*', (Oxford University Press, 1996), pp. 33-128.

26. The female-male ratio among the dominant Rajput caste has remained stable at 890 for most of this century, there has been a general convergence among lower castes to this 'standard'.

27. See Petra Dannecker, '*Between Conformity and Resistance: Women Garment Workers in Bangladesh*', (The University Press Limited, 2002).

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Editor's Note

Gossip: PAE and the economics textbook industry

Recent conversation and correspondence with the head commissioning editors at three of the world's largest publishers of English-language economics textbooks reveal that they anticipate the need to make fundamental changes in their product lines as a result of the PAE movement. The growing view in the industry is that the nature of demand in the economics textbook market is changing, especially for entry level textbooks.

One editor reports that his firm is planning a book for the first-year principles market with "characteristics I would ascribe to a pluralistic approach . . such as a rejection of rote rehearsal of neo-classical theory just because that is always how it's been done, and a recognition that books must relate theory to the real-world and capture the imagination of students."

Another publisher who is already about to go to press with an explicitly pluralistic textbook for business economics, is actively seeking an author or authors for a new first-year principles textbook constructed on pluralist lines. "What we want", explained the editor, "is a text that begins with neoclassical economics, maybe the first two or three chapters, and then quickly moves on to introduce the student to other approaches."

It takes on average three years for a publisher to bring a new major economics textbook onto the market and then at least a second edition before it can hope to capture a significant market share. Commissioning editors are now doubly nervous about the future of this market. Economics textbooks have long been a big earner for these publishers, but now are increasingly less so as enrolments for undergraduate economics courses continue to fall. But there is also PAE and the perceived movement away from the neoclassical hegemony. Commissioning editors appear to regard this as the joker in the pack. It could save them or ruin them. If PAE inspired textbooks were widely adopted in universities it could bring back the students and raise textbook sales to previous or even higher levels. But if a textbook publisher holds back now from investing in pluralist and reality-based textbooks, it could find itself, as one editor put it, "without a product to sell" in a new market situation. The market for PAE textbooks may currently be small, but editors are mindful of the possibility that the movement away from neoclassical economics could at some point accelerate dramatically, especially as economics teachers scramble to save their jobs.

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