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Title: **Trade, Corporatism, Clusters, and Japan as Bellweather**

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Remarks on the trend toward corporatism in the U.S. and outlines the latest developments, namely the MAI treaty, and examines how what we know about Japanese business and society does and does not signal what we can expect from increased corporatism in the U.S. Speculates on the effect of the new corporatism of the OECD countries on scientific progress, innovation and high technology clusters.

Keywords: international trade; high tech; innovation; corporatism; MAI treaty; Japan

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**Trade, Corporatism, Clusters, and  
Japan as Bellwether**

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## **Abstract**

The paper remarks on the trend towards corporatism in the United States, and examines how what we know about Japanese business and society does and does not signal what we can expect from increased corporatism in the U.S. It also speculates on the effect of the new corporatism of the OECD countries on scientific progress, innovation, and high technology clusters.

**KEY WORDS:** CLUSTERS; CORPORATISM; HIGH TECHNOLOGY INDUSTRY; JAPAN; MAI TREATY; TRADE.

## Introduction

Democracy, the nation-state, and the corporation: Which is the oldest? That's easy – everyone knows democracy dates to ancient Athens. For millennia after Athens, people lives in city-states (Athens was one), kingdoms, empires, colonies and so forth, their boundaries determined by continual war and shifting alliances. It was only after World War I that the modern nation-state – and entity governed by its natives, participating in international discourse, and with boundaries relatively fixed and recognized by international convention – came into being.<sup>1</sup>

As for corporations, I have heard that as late at 1900, there were only about thirty of them in the United States. Historically, of course, corporations (then synonymous with “patents”<sup>2</sup>) were granted at the pleasure of the sovereign, for limited purposes. Corporations did become effectively as powerful as governments in some cases, for example the Hudson Bay company in Canada and United Fruit in Central America. But these were for all practical purposes colonial situations, the post-World War I nation-state seemed incompatible with the idea of corporations as governing bodies. Nonetheless, in acknowledgement of the danger of expansionist corporations, the U.S. occupying forces dismantled the Japanese *zaibatsu*, the President Eisenhower warned us about the military-industrial complex.

As members of a mobile society, Americans demanded government protection from traveling snake oil scams and from the likes of Harold hill the music Man. We demanded it and got it, and in a dialectic that looks inevitable in hindsight, the Harold Hills, and their more honest cousins, had to protect themselves from the abuses of government protection, and formed the limited-liability corporations that are ubiquitous today. As legal quasi-persons, corporations cannot vote in political elections, but can and do lobby and make political contributions to further their interests.

Whose interests are those? We are the corporations and they are us. We are employed by them, we consume their products, and, through our investments and pension plans, we own them.<sup>3</sup> But individual Americans are also voters, and still expect the corporations to abide by the law of the sovereign (which is also us). We are increasingly at risk of being disappointed in this expectation. The well-intentioned NAFTA and World Trade Organization (WTO), and the not-so-well-intentioned Multilateral Agreement on Investments (MAI), potentially subordinate government power to corporate decisions. Most of us would think of this as putting the cart before the horse, to put it mildly. From a liberal-statist to a corporatist United States in less than fifty years – how would such a shift affect our lives? Our study of Japan helps us understand what life might be like in the corporatist regime that would result from MAI.

In this paper I will offer some introductory remarks on trade and corporatism in the U.S.; briefly outline the features of the latest development on these fronts, namely, the Multilateral

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<sup>1</sup> When did Japan become a nation-state? Historically, it fit most of the criteria mentioned above, except that until Admiral Perry, there was little “international discourse.” “Japan still has a feudal mindset,” according to professor Kenichi Arai of the University of Tokyo, referring to a tradition of fealty to *daimyo* and to the emperor rather than to the nation. And of course Japan suffers from defining itself in ethnic terms, a malady that is destroying nation-states elsewhere, viz., Canada, Israel, and Yugoslavia. Will the idea of the geographical-political nation-state (as opposed to the ethnic enclave) turn out to be a short-lived idealistic dream?

<sup>2</sup> The corporation and the patent both constituted sovereign permission to a private party to profit from some extraordinary activity.

<sup>3</sup> Unlike the Japanese, whose personal savings to date have mostly been in the postal savings system. The majority of Americans do not own stocks, and few have employer-funded pension plans. Unfortunately, a financial regime that encourages stock market growth at the expense of GNP growth exacerbates income inequality and is a social lever that gives stockholders a much different set of civic motivations from the remainder of Americans.

Agreement on Investment; take a look at corporatism in Japan; and examine how what we know about Japanese business and society does and does not signal what we can expect from increased corporatism in the U.S. I'll also speculate on the effect of the new corporatism of the OECD countries on scientific progress, innovation and high technology clusters.

### **Free Trade, Capital Regulation, and Corporate Influence**

Industrial enterprises use land, labor and capital to produce goods and services. Nowadays people add "technology" to the list of inputs, but as technology is useful knowledge residing in the heads of knowledge workers, we can regard technology as a certain kind of labor. What is the effect of free trade on these traditional inputs and outputs? Capital movements are freer than ever before. With negligible exceptions, land stays in one place. Labor obviously does not move freely, except within the European Community, and even affluent knowledge workers face formidable visa problems when travelling for work purposes between other nations of the world. On the output side, goods move reasonably freely. To the extent that services are provided by human service providers (or consumed by knowledge workers in another country, as in the case of Chinese professionals coming to the U.S. for graduate education), movement of services is restricted to the extent that labor movement is restricted. Only two of five or six factors of trade actually move freely, so "free trade," in the NAFTA sense, seems an exaggeration.

According to Noam Chomsky (1998), "It was realized even in the immediate post WWII years that financial capital can impose the social policies it chooses on governments and can punish those that deviate by capital flight.... for example, efforts to stimulate the economy or to create full employment or to use public resources for health or education or social welfare, for the environment, for improved working conditions and other ["inefficient"] purposes can be terminated and punished simply by flight of capital, which even these days rich and powerful states can't withstand."

The post-war Bretton Woods monetary agreement regulated capital very strictly. The economies of its signatories (including the U.S. and Japan) were characterized by high GNP growth, high productivity growth, and expansion of the social contract, if also by low profits. The U.S. and other countries abandoned the Bretton Woods regime in the 1970s; the result was lower growth and higher profits. But Japan kept up the high-regulation/high-growth/low-profit regime, ironically making that country look aggressive to American eyes.

"Historically, recession is the midwife of protectionism. In good times, peoples and nations are happy to enjoy the benefits of open trade," says *The Economist* (1999). Yet the magazine's 1999 survey shows that U.S. consumers, pleased with the current state of our economy, favor protectionism over free trade by about twenty percentage points. (Japanese consumers, hungry for cheaper imports, prefer free trade by about the same margin.) *The Economist* (1999a) also notes that "the profitability of companies is shrinking," and *Business Week* (Byrnes and Barrett, 1999) talks about "the deteriorating quality of corporate earnings," a reference to increasing use of funny bookkeeping. Doubtless, these contradictions of trend and theory have spurred corporations to lobby for trade agreements that give them greater latitude.

In addition, while WTO rules reduce national sovereignty, their enforcement of product standards can be good for consumers (Phillips, 1998).

### **The Multilateral Agreement on Investment**

A treaty that is as pro-corporation as the MAI naturally generates a lot of wild-eyed and ungrammatical populist response (e.g., Clarke, 1997). A more literate but no less impassioned viewpoint is provided by Chomsky (1998, 1998a). And the attorneys for the Western Governors' Association (1998) offer a sober but still critical analysis of the treaty.

In short, here are the main features of the MAI, as gleaned from these sources.<sup>4</sup> There can be no barriers to repatriation of foreign direct investment (FDI) or its profits. Trans-national corporations (TNCs) can sue government, but not vice versa. All TNCs, no matter where incorporated, will be free to bid for privatized government enterprises. Remaining state enterprises will be required to act solely in accordance with commercial considerations. No quid pro quo can be required from companies when localities offer tax incentives for location, and indeed such incentives may be banned. Signatory governments will be forced to deregulate all industries that ask for it. MAI gives corporations equal status with governments, in many arenas.

MAI opposes any government taking or giving that distorts private market allocation of capital. Companies may not be compelled to use domestic content, transfer new technology, or export a certain level of manufactured goods. There will be no exceptions for health, safety, or environmental standards, or local cultural content.

The only exceptions to MAI investor protections would be national security, public order, and international peace and security. This is much more restrictive than current NAFTA and WTO provisions. The Western Governors' Association (1998) notes, "The MAI may be more than merely a tougher NAFTA or WTO. Unlike those agreements, the MAI may protect investors by curtailing sovereign powers and sovereign immunity." While the WGA report cleverly concludes "...governors are again positioned to support the MAI in principle while pushing the federal government to take steps to protect state sovereignty in the MAI and in potential implementing legislation," the steps they recommend are so extensive that they amount to opposition to MAI.

Additional responsible opposition comes from the *Christian Science Monitor* (1997): "This treaty will transform government of, by, and for the people into government of, by, and for the corporations."

A Canadian book about the treaty is number seven on the best-seller list, five provinces refused to participate in the treaty by declaring themselves MAI-free zones, and the Canadian government announced that it could not sign the current treaty. In France, tens of thousands of protestors took to the streets, forcing the French government to call for a renegotiation of the treaty. In New Zealand, the parliament exploded into fury against the government when word leaked out (Taylor, 1998).

I could find no mention of MAI in the Japanese press, but there is some, generally negative, in the Korean press. There is no more in the Canadian press than in U.S. newspapers, perhaps not surprisingly.

The MAI is still under negotiation. Because of widespread popular resistance to the treaty, talks have stalled as of the date of this writing, and if resumed may take place within the WTO rather than within the Organization for Economic Cooperation and Development (OECD). Because OECD is not normally a treaty-making organization, MAI's genesis within OECD was regarded as a secretive move, contributing to the grass-roots resistance.

### **Japan, Inc. as Bellwether?**

Can Japan be called Corporatist? It is not for nothing that the press refers to the country as Japan, Inc. From its imperial expansionism in the first half of the century, driven by its military-industrial complex, to today's disempowered Japanese consumers and the neon and extravaganzas in Ginza and Kabukicho, the corporate influence on Japanese life seems overwhelming. Religion is not a major preoccupation of the Japanese, and governments rise and fall with frequency. But the companies and the *keiretsu* persist, and the increased international expansion of Japanese companies lessens the control of MITI and MOF<sup>5</sup> over their activities.

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<sup>4</sup> A good general information site is <http://www.igc.org/econwg/MAI.index.html>.

<sup>5</sup> The Ministry of Trade and Industry, and the Ministry of Finance.

What characteristics of Japanese corporatism might foreshadow what the U.S. would be like under an extreme free trade agreement (FTA) like the MAI? Some of them are Japan's

- passive labor force.
- emphasis on rote learning in school.
- much horizontal and vertical integration (cross-ownership) of companies.
- vulnerability to crashes in the economies of neighboring countries.
- construction industry favored by massive public works spending. (This is good for economic infrastructure, but has led to corruption.)
- weakness in entrepreneurship and venture capital.
- secrecy, with company records not easily accessible.

What current features of Japanese corporatism would *not* characterize the U.S. under MAI?

- Japan's "statist capitalism" (Brenner and Kunii, 1998) with industry taking direction from government ministries.
- Most personal savings in MOF (postal) deposit accounts, not with private brokers.
- Slowness to adapt to office automation and the Internet.
- Well-educated workforce.
- Japan does not have a social welfare structure like the U.S. or Western Europe.
- Corporate farming has not dominated Japanese agriculture, as it does in the U.S.

### **Capital Flows and Scientific Progress**

One of the most powerful ideas in technology management today is Fumio Kodama's (1992) notion of technology fusion. In days past, isolated research laboratories could develop expertise in any needed discipline. Advances were linear extensions of the lab's prior knowledge. Today's phone, fax and Internet connections mean that no lab is isolated. Nor could today's budgets support facilities devoted to wide expertise. The result is that profitable advances can be made cheaply by combining knowledge from different fields, different companies, different industries, and different geographies. This combination process is called technology fusion. The current base of scientific knowledge is such that combining existing ideas and technologies can generate profits for decades to come even with no new advances in basic science. Don Kash of George Mason University (1989) notes that improved engineering techniques, plus the above-noted increased interaction between established bodies of knowledge, are the current drivers of technology innovation.

These considerations may reinforce with smugness of certain scientists about the advanced state of physical and biological theories that has led to published discussion of the end of science. One thinks twice before disagreeing with Feynman and Hawking, but the "end of science" is a foolish notion. Consider the as-yet undiscovered "dark matter" that is said to make up the bulk of the universe's mass. People who have misplaced 90% of the universe's matter should not be saying they are close to knowing all there is to know (see Hawking, 1988). In any case, talk about the end of science plays into the hands of those who would limit the freedom of ideas.

Nobel Laureate Richard Feynman (1998) noted that Soviet Russia and Nazi Germany both showed impressive advances in technology – but that, due to the excessive official influence of Lysenko in Russia and Hitler's glorification of the supposed occult history of the Germans, and due to the general suppression of new ideas and their expression in both regimes, science did not

advance notably in either.<sup>6</sup> And of course modern science dates from Galileo, whose work was not exactly embraced by the then all-powerful arbiter of ideas, the Catholic Church.

The current international consolidation of the publishing industry could produce the same constriction of ideas as the repressive nation-states of the past. Last year, the entire press run of the British journal *The Ecologist* was burned, the publishers fearing that its distribution would bring a libel action from the Monsanto company (Harper's, 1999). A smaller publisher, with less to lose and much to gain in reputation, would not have burnt the run. But there are fewer small publishers each year (if you don't count Joe Oddball's Personal Web Page and its many cousins). It is easy to appear paranoid about this. But on the other hand, it is demonstrably true that U.S. domination of the Canadian press, and the economic incentive for filling Canadian editions with content originating in the U.S., have reduced the forums in which Canadians can share ideas and concerns with each other (Barlow, 1998).

Readers who have been in Japan will have drawn their own conclusions about the independence of the press there, but it is certainly a rarity (despite the huge variety of magazines for sale) to see a printed criticism of one of the large corporations. The easy explanation of this (and I don't know any harder ones) is the extensive cross-ownership of companies, known as the *keiretsu* system. Many of these cross-ownerships would be illegal in the U.S. under our antitrust laws. Some of them, under MAI, presumably would be compulsory.

One would think that the recent increase in Nobel prizes and basic research in Japan is not consistent with the notion of corporatist restriction of the flow of ideas. But only 14% of total public and private Japanese research expenditure is on basic research, compared to as high as 64% in the U.S. (Bremner and Kunii, 1998). I do not think there is sufficient evidence to conclude broadly that corporatism and so-called free trade are anti-innovation. But we do generally associate R&D expenditure and the resulting innovation with long-term growth, rather than with the short-term profits that impel corporations to seek deregulation.

### **Implications for High-Tech Clusters**

Theoretically, according to Michael Porter (1998), "companies' ability to source capital, goods, information, and technology from around the world... should not diminish the role of location in competition." Competitive advantage, Porter says, does not rest any longer on driving down input costs, but rather on making more productive use of inputs, which requires continual innovation. He notes the role of location is important, then, as geographical clusters of industries, especially technology-intensive industries, offer many conditions conducive to innovation. Extensive market, technical and competitive information accumulates within a cluster, and members have preferred access to it. In addition, personal relationships and community ties foster trust and facilitate the flow of information. Clusters thrive because of access to public resources, and companies "must engage locally, fostering good relationships with local government, schools, utilities, etc." Clusters arise and can thrive because of specific local characteristics having to do with the special nature of the population, the terrain, or the infrastructure.

Porter's argument is correct as far as it goes,<sup>7</sup> but it is trade agreements that dictate the availability of inputs, the disposability of outputs, and even the viability of industrial clusters.

Under MAI, no quid pro quo (corporate performance requirements) will be allowed in exchange for tax incentives, reducing the ability and incentive of localities to encourage cluster

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<sup>6</sup> Feynman, who died in 1988 (the cited 1998 publication is a reprint of lectures from the early 1960s) does not seem to realize the irony of touting the end of science while criticizing political regimes that stifle scientific advance.

<sup>7</sup> Porter's thesis is far from original, and his HBR paper not only fails to cite the work of Alonso (1972), Hansen (1972), Richardson (1969), and Hoover (1963), but offers no citations at all.

growth. Those of us who have witnessed the successes of public-private partnerships, including the Air Force-sponsored JIMT program that is host to this conference, must be skeptical about extreme FTAs.

FTAs affect the ability of state and local governments (the primary governmental facilitators of clusters) to regulate industry. For example, Japan is bringing suit in the WTO against Massachusetts' ban on companies that do business in Myanmar. As a result, some localities are declaring themselves MAI-free zones, including Edogawa Ward in Tokyo. Of course, this is of dubious legality, but it could accelerate the dissolution of nation-states throughout the world.

Japan's advanced industries are clustered not because of the natural advantages of regions, but because they have been government-driven and must be close to the seats of power. As MAI decouples industry from government, the rationale for this clustering disappears, and companies will disperse.

## Conclusion

I first went to Japan as an immature twenty-three-year-old, at a time (1975) before the "Japanese quality miracle" had visibly affected U.S. industry, and when the yen was four hundred to the dollar. In those days, Americans still went to Japan as tourists rather than pilgrims. But I understood that I was looking at the future. It was antiseptic, corporatist, and stifling. But in terms of urban crowding and the social, infrastructural and architectural ways of accommodating a dense population, it seemed both sensible and inevitable. About the latter, I was too optimistic. In the ensuing twenty-plus years, U.S. cities did not become more like Tokyo, but rather in their squalor, lawlessness, shrunken tax base, and pollution evolved into little (or not so little) free-standing third world countries.

Both extremes have unattractive features. How to ensure a happy medium? The answer is us. When employers oppressed labor, we formed labor unions. When the advertising machine turned is in to consumers, we formed consumer unions. Now, when PACs and religious blocs control Congress, we must exercise our rights as citizens and voters. And if MAI removes that sovereignty from our hands, we must exercise our right as stockholders. It places great demands on our character to play our many roles as producer, consumer, breadwinner, stockholder, and citizen.

When the cold war ended, it was predicted (*inter alia* in Phillips, 1994) that the difference in the kinds of capitalism practiced in the U.S. and Japan, previously ignored in the grand conflict between capitalism and communism, would become new arenas of disputation. But any conflict between flavors of capitalism now seems lost in the crisis of post-cold-war conservatism and a confused religious millennialism that both anticipates apocalypse and applies the language of good and evil to the economic debate. It now seems that democracy, federalism, and the nation-state face greater risks than capitalism does – and perhaps this shouldn't surprise us, as capitalism predates democracy, the nation-state, and the corporation. *The Economist* (1999) uses the word "liberalism" in connection with free trade. Lacayo (1998) points out that conservatives, ostensibly, dedicated to the preservation of traditional values, also seem dedicated to corporations that tend to "chew up every precious thing that stand in their way, including small towns, small farms, old institutions, and you." We cannot rely on old categories to resolve the issues of trade and technology that I have discussed today, but decisions must be made nonetheless.

As noted at the beginning of this essay, the dialectic of protection for all parties gives rise to agents and counter-agents. We can look to Japan for clues about how the dialectic might play out for us. Japanese corporations have perfected the use of *sokaiya*, tough guys who prevent stockholders from having their say at annual meetings. But Japanese corporatism is balanced, to some extent, by the powerful rural agriculture vote.

After seven years of JIMT, we can throw away what we learned about Japanese management – so much of it rested on a bubble that has now burst – except for the fact that these are inventive

and resilient people. The really interesting part begins in 1999, as we wait to see: What will the Japanese do now?

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