United States Direct Investment in Japan: Studies in Government Policy and Corporate Strategy

Mark Mason[1]
Center for International Affairs
Harvard University

Foreign direct investment (FDI) is not a new topic for business and economic historians. Indeed, many scholars have written about the role of FDI in the economic histories of China, India, Russia, and a host of other nations, and they have often judged that role to be highly important. Yet the comparatively low levels of FDI in modern Japan have led scholars and others to conclude that FDI played an insignificant role, at best, in that country's economic development [2, p. 323]. Many of these same observers also contend that foreign multinationals' indifference toward the developing Japanese economy provides the chief explanation for the small quantity of direct investment undertaken by foreign business in modern Japanese economic history.[2]

This doctoral dissertation examines the history of United States direct investment in modern Japan to assess these and other claims. The thesis analyzes in particular the critically important interactions between Japanese government policies and the corporate strategies of U.S. multinationals in Japan from 1899 through 1952.[3] I document and evaluate in depth the experiences in Japan of Ford, General Motors, Otis Elevator, RCA Victor, and International Business Machines, which together account for a significant proportion of all U.S. direct manufacturing investment in Japan during these years, and supplement these accounts with discussions of other foreign multinationals which also operated in Japan in the prewar and early postwar

[1] This dissertation was written at Harvard University under the supervision of Professors Albert Craig, Dennis Encarnation, and Henry Rosovsky. It will be published, subject to revision, as *Access Denied: American Multinationals and Japan, 1930-1980* (Cambridge, MA, forthcoming 1990).

[2] A typical statement of this viewpoint regarding the postwar era can be found in Ozawa Terutomo [3, p. 147]. Other observers, clearly in a minority, attach much greater significance to restrictive Japanese policies towards inward direct investment. See, for example, Dan Fenno Henderson [1, p. 14].

[3] Examination of Japanese government policies does not imply necessarily that such policies originated with the government. Indeed, much evidence suggests that private-sector initiative motivated many public-sector policies. The relationship between Japanese business and government actions, particularly with respect to the entry and development of foreign multinationals, is a topic of my current research.

BUSINESS AND ECONOMIC HISTORY, Second Series, Volume Eighteen, 1989.
 ISSN 0849-6825.

periods. The study draws on a wide range of primary sources, including information never before used in scholarly research, or never previously presented to a Western audience. These sources include internal Japanese and U.S. government documents, interviews with current and former American and Japanese business and government officials, and over a dozen public and private archival collections in both countries as well as in England.

Japanese government policies and American corporate strategies proceeded through four distinct stages during the years covered in this study, and in at least three of these periods U.S. firms had a considerable impact on the development of the local economy. The first stage began in 1899, when the Japanese government, as a partial concession to Western countries who agreed to revise their so-called "unequal treaties" with Japan, opened much of the previously-closed interior of the country to foreign direct investment. The domestic economy was not, to be sure, entirely open to such investment: there remained, for example, important restrictions on foreign participation in the Japanese banking, mining, railroad, and telegraph industries. Yet such regulations were not unusual in other nations during this period; and, at least compared to its own past, the Japanese government had created a less restrictive regulatory environment for the overseas direct investor. In a metaphorical sense, then, Japanese government policies from 1899 can be likened to a Door Ajar of relatively relaxed controls over American and most other foreign direct investment.

Numerous American companies responded to these newly-liberalized public regulations by entering Japan as direct investors. Victor Talking Machine, acquired by RCA in 1929, is a case in point. An exporter of records and phonographs to Japan since the company's establishment in New Jersey at the turn of the century, Victor decided to set up a Japanese affiliate in 1927 to avoid a rise in local tariff rates and to challenge on an equal footing a British competitor that had organized a subsidiary in Japan. Not only did the Japanese government permit Victor's entry, but official policy to increase tariffs on certain Victor imports actually *encouraged* the U.S. firm to establish a local subsidiary.

American direct investors substantially influenced the development of industry in Japan during the era of the Door Ajar. To turn once again to the case of Victor, the American company brought to Japan its latest methods of record and phonograph manufacture. These included the firm's advanced techniques for grinding, sifting, and mixing ingredients to produce records, and its latest methods for designing and equipping factories to manufacture phonographs. In addition, Victor contributed to the development of local industry by hiring and training more than five hundred Japanese workers in this advanced industrial sector.

Japanese government policy entered a second stage from the early 1930s. Departing from their earlier tolerance of many American and other foreign businesses in Japan, local authorities placed increasing restrictions on inward direct investment throughout the prewar decade of intensifying nationalism and militarism. These restrictions included application to overseas investors of the 1933 Foreign Exchange Law, together with the imposition of a host of specific measures designed to curtail foreign participation in a wide range of industries. Public policy had become analogous to a Sliding Door of increasing controls.

These changed policies frustrated the designs of American investors eager to develop and expand their operations in Japan. The experiences of Ford and General Motors well illustrate this point. The two U.S. automakers, which had established local assembly operations in the mid-1920s and together had managed to gain control of some 95% of the Japanese motor vehicle market by 1930, found themselves increasingly threatened by hostile government policies as the prewar decade progressed. Government enactment of the 1936 Automobile Manufacturing Industry Law in particular prompted the two companies to shift from development to survival strategies in Japan. As war approached, severe government controls forced GM and Ford virtually to abandon their local operations.

Despite growing restrictions on their Japanese affiliates during the era of the Sliding Door, however, U.S. direct investors such as Ford and GM contributed to the development of the Japanese economy in numerous ways. Ford, for example, introduced to Japan the assembly line method of motor vehicle manufacture. General Motors, forced by government policies to curtail its local activities, indirectly promoted the development of wholly domestically-owned auto manufacturers when leading Japanese employees, hired and trained by GM, moved to Nissan and Toyota. And both American automakers actively encouraged the development of local companies to supply vehicle parts and other inputs.

Japanese policies towards American direct investors entered a third stage from the outset of World War II. Having already frozen most U.S. assets in Japan in July 1941, the authorities moved after Pearl Harbor to expropriate the local operations of American multinationals through enactment of the Enemy Property Control Law. Officials then assisted in the exploitation of these same assets through selective application of the Wartime Law on Industrial Property (WLIP) and other measures. Government policy had shifted to a Closed Door regime of virtually total control over U.S. and other direct investment from abroad.

IBM Japan and the local affiliates of other American enterprises had little choice but to cooperate with the authorities in wartime. Increasing tensions between Japan and the U.S. already had forced IBM to repatriate its non-Japanese managers before Pearl Harbor, and, when war began, the parent company completely lost control of its local subsidiary. The Japanese government then moved quickly to designate this American subsidiary an enemy organization, and assisted in the transfer to a wholly Japanese-owned organization of IBM Japan workers, managers, equipment, and technology. IBM Japan could do little but cooperate with Japanese officials.

Even during this period of the Closed Door, the local affiliates of IBM and other U.S. firms made significant contributions to Japanese industry. Under government direction, for instance, the mandatory transfer of IBM-trained engineers and other expert personnel to a Japanese-owned competitor directly benefitted the development of local interests in the tabulating field. The authorities forced the American subsidiary to contribute still further to domestic industry when officials invalidated IBM-registered patents through invocation of the WLIP, and transferred these patent rights to Japanese hands.

Official policies toward direct investors from abroad entered a fourth stage during the Allied Occupation, which lasted from 1945 until 1952. Government directives, now controlled by both American and Japanese officials, prohibited virtually all FDI at the outset of the period, but permitted the entry and development of modest amounts of such investment-- subject to rigorous case-by-case screening-- starting late in the decade. These directives were codified in Japan's Foreign Investment Law of 1950, whose regulations and subordinate measures fully elaborated Japan's Screen Door regime of detailed and comprehensive controls over direct investment from abroad.

American companies such as Otis Elevator reassessed their strategies for the Japanese market during the era of the Screen Door. Initial Occupation rules allowed Otis to do little more than re-establish contact with its former affiliate, and register claims with the authorities for its seized assets. Later in the Occupation period, however, new rules enabled Otis officials to travel to Japan and re-examine the market's potential. Despite initially chaotic economic conditions, Otis and many other U.S. companies chose to re-enter Japan as direct investors after government policies permitted them to do so.

As the Occupation drew to a close, American multinationals were preparing once again to make important contributions to the development of the Japanese economy. Otis Elevator, for example, committed fresh resources to its Japanese affiliate after the authorities permitted the U.S. firm to operate in the postwar market. These resources would include the transfer from the American parent of Otis engineers trained in the latest methods of elevator manufacture and repair, together with new infusions of capital necessary to rebuild the local organization. As it had before the War, the local subsidiary of this U.S. company would soon achieve a highly influential position as the leader of the Japanese elevator industry during the postwar period as well.

The history of United States direct investment in Japan challenges at least two common interpretations of the relationship between FDI and the developing Japanese economy. First, the activities of RCA Victor, Ford, GM, IBM, Otis Elevator, and other American firms in Japan demonstrate that foreign direct investment made highly significant contributions to the local economy. Second, the character and impact of official policies strongly suggest that restrictive Japanese government practices, rather than indifference on the part of American and other foreign multinationals, provide the principal explanation for the relatively limited amount of foreign direct investment in the modern Japanese economy.

References

1. Dan Fenno Henderson, *Foreign Enterprise in Japan: Laws and Policies* (Tokyo, 1973).
2. William Lockwood, *The Economic Development of Japan: Growth and Structural Change, 1868-1938* (Princeton, 1954).
3. Ozawa Terutomo, "Japanese Policy Toward Foreign Multinationals: Implications for Trade and Competitiveness" in Thomas Pugel, ed., *Fragile Interdependence* (Lexington, MA, 1986).