

Fettered by the past in the march forward : ideology as an explanation for today's malaise in Japan

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ABSTRACT

Japan's Lost Decade of the 1990s is more than 10 years of economic downturn. The fact that a further decade later the malaise continues suggests that this is more than just an extended bad patch. Measures have been implemented to revitalise the economy however, the Japanese economy continues to wither. Why is this the case? This is an historical institutionalist's argument drawn from D.C. North's work that reform measures fall short of their aims if they are not underpinned by a complementary ideology. And, effectively, Japan is a case in point. Japanese-language records of debates between policy makers in 1999, after a decade of reform, show that they continued hold to a mental model of a political economy that was of the preceding high growth period and, indeed, much further in Japan's past. Such key figures as Prime Minister Obuchi Keizō argued both for the inculcation of greater market

competition and, at the same time, lamented the loss of Japan's former 'virtuous capitalism'. In other words, fettered by the past, they prepared Japan for the future.

Keywords

D. C. North, historical institutionalism, Japan, ideology, 'Lost Decade', *shingikai*

Introduction

Accounts of the 'Lost Decade' identify that Japan's economy reached a critical point at the end of the 1990s when the effects of key reforms began to be realised (Amyx, 2004; Schaede, 2008). Turning to this juncture, this study focuses on the Japanese-language records of debates in 1999 between government and business during *shingikai*, or Council of Deliberation, meetings over proposed reform measures. This analysis is part of a larger longitudinal study of the linkages between how key stakeholders conceptualize and reconceptualize policy and the ramifications for Japan's current politico-economic transition. While much of the literature focusses on reform measures and their impact, the historical institutionalist interpretation provided here sees the Lost Decade as more than just an economic downturn. Drawing on D.C. North's work on the socio-cognitive underpinning of political economy, answers based on ideological grounds are provided to questions raised in the literature as to why reform measures in the 1990s fell short of their intended outcome. And, we extend the implications of these findings to the present. Notwithstanding whatever gains may be achieved by the reform measures to date, the prognosis is that Japan's economy will continue, at least in the short-run, to do poorly.

The malaise of the 1990s brought an end to Japan's remarkable postwar economic rise. For a decade, government and business debated alternative solutions and implemented policies to revitalize the economy. Nonetheless, today, some 20 years after the onset of the Lost Decade, Japan has not yet found its way. To be sure, Japan has changed and continues to change. However, in as much as Japan had struck upon an effective politico-economic framework to channel its drive for catch-up, it continues to look for a replacement. The transition for a nation engrossed in catching up to the 'what next' after having caught up is not necessarily easy or smooth. After all, what is at stake is not merely the rejigging of a few market institutions – which in itself is difficult enough – but rather something more profound and all encompassing.

From all quarters, Japan has been urged to find a way to rejuvenate itself. Yet, its search continues. The bifurcation of its economy between globally competitive multinationals and cosseted domestic small and medium sized firms signals that Japan has the wherewithal to be innovative, flexible and competitive at the highest standards. But, at the same time, Japan tolerates the opposite among its domestic firms. Given these strengths, that still after some 20 years of economic restructuring and political reform Japan continues to stagnate suggests that the matter is of a deeper nature.

At its most elemental level – and where the crux of the matter lies – this transition is not about the creation of new institutions, or the adoption of new rules for old institutions or the reconfiguration of their matrix. Analysis at this level is epiphenomenal. Ultimately, what fetters Japan's resurgence is not its rules of operation that govern the market but, in the Northian sense, the ideology that underpins these rules. To be sure, change in the rules themselves may

increase competitiveness and lead to growth but, as the last 20 years have shown, this is not enough. Japan's economy has lost its former vitality and tinkering on the edges will not cut the mustard.

It is telling that despite a decade of debate about reform measures, fundamental ideological conflict continued among key stakeholders about the very nature of Japan's future political economy. Among these discussions, a key concern was that of competition. Records of *shingikai* meetings in 1999 reflect their acceptance of the need to increase domestic market competition but also their concerns about some of the consequences. Before the participants stood a wide range of bills whose overarching aim was to put Japan on a new footing commensurate with the challenges, economic among others, of the new century. They accepted the need for change but framed it within a vision of a political economy inspired by the past. Underpinned by values more closely associated with a socio-economic framework of the high growth period, this vision was significantly different than neo-liberalists would have hoped for. Japan's post-transition political economy was on the one hand to be more competitive than its forerunner and, on the other, inspired by the tenets of the very one that it was to replace. With one foot in the past it tried to move forward.

Fundamentally, what Japan needs is to decide how it wants its market to operate. A market is about the allocation of resources. The regulations which dictate how that allocation will be determined is not, however, preordained but a humanly devised construct. It reflects the values of the nation. As history shows, in the long run, agreement by a people on how their resources, capital and wealth are shared is essential. Expressed in Northian terms, the contestation of the rules of the game, formal and informal, is part of the process of a nation

defining and redefining how its market will operate. In so doing, the market becomes a means through which a nation realizes its hopes and desires. In this sense, the Lost Decade was a period of reflection on what kind of market - and, indeed, nation – Japan wanted. This issue remains unresolved still today. And, until such time that this resolution is found, Japan will continue to wander through its ‘valley of transition’.

Theory and Hypotheses : Ideology and Institutional Rigidity

The term ‘Lost Decade’ is somewhat of an unfortunate epithet. The word ‘Lost’ suggests that something has gone astray, ‘Decade’ tells us the time period and, through usage, we have come to associate it with economic crisis. But, this term fails to convey the sense of the pivotal role that the Lost Decade plays in Japan’s history. That said, as part of the larger transition from the post-1945 high growth period’s politico-economic (cum-socio) framework to its following reconfiguration, the Lost Decade is but 10 years within the long run. That the origins of the bursting of the real estate bubble in 1991 reach into the 1980s and that the ensuing downturn is two decades long points to the severity of Japan’s *bouleversement*. The jigsaw has broken apart and its pieces are coming together in new ways ultimately producing a very different picture (Pempel, 1998 ; Hook, 2011). Although it is still unclear what this new institutional configuration will be, it is clear that research on the Lost Decade needs to appreciate the larger historical process at play.

The spectrum of approaches to institutional theory is vast spanning the social sciences, each offering a different vista on the process of institutional formation, continuity and changeⁱ. Similarly, the actor-structure issue remains a hotly contested issue. New Institutional

Economics a la North (e.g. 1990), New Institutional Organizational Theory (see Greenwood et. al., 2008), Structuration Theory (Giddens, 1984), Critical Realism (Bhaskar, 1989; Archer, 1995) and a Darwinian approach (Hodgson, 2004; Hodgson and Knudsen, 2010) each contribute to this discourse. Notwithstanding difference that bedevils greater convergence, it is fair to say that there is agreement that both actor and structure are two parts of a mutually constitutive whole. The dynamics of that interaction though, are at the frontier of the literature. With respect to the Lost Decade, as will be seen, the dominant perspective in the literature is that of ‘structure’. While it is not that the literature sees ‘actors’ as bereft of agency, it is rather by omission that they have been rendered largely silent. This is, though, a shortcoming. The contribution by Fletcher here in this collection of articles helps redress this and signals the importance of agency in decision making processes. By specifically looking at some of the very business actors who conceive and convey opinion, he underscores that reform measures are a result of previously conceived ideas and not the other way around. That said, one must be sensitive to the actor-structure dialectic and recognise that the very reforms that actors create, in turn, provide new structures which both facilitate and shape further decision making. We seek here an understanding of institutional change in terms of a process worked out through time in order not to lose sight of the on-going politico-economic meta-narrative and to draw into relief the trajectory of Japan’s economy. And, it is thus, that we turn to historical institutionalism to frame the ensuing research and findings.

Historical Institutionalism is often closely associated with path dependency, that is ‘once a path [decision] is taken, previously viable alternatives become increasingly remote, as the relevant actors adjust the strategies to accommodate the prevailing pattern (Thelen, 2004, p. 27). The point of origin of the path dependent trajectory comes at ‘critical junctures’ when a particular institutional configuration sets (Thelen, 2004). Although not necessarily impossible,

later radical change is difficult to realise until a further turning point or 'crisis' is reached. While this theoretical approach may provide good explanations for why an economy persists along a sub-optimal path, it is less useful at predicting when change will occur (Peters, 2005). However, in the case of the Lost Decade, the issue is understanding why, despite reform measures, little has changed. This, in turn, steers us towards the actors themselves to find answers raising questions about their motivation and ideas. The importance of the socio-cognitive in explaining institutional change and stasis has been recognised within institutional theory such as New Institutional Organizational Studies (e.g. DiMaggio, 1997) and as New Institutional Economics (e.g. North, 1990, 2005). It is, however, the work of D. C. North that, in particular, provides theoretical underpinnings for answers to why political economies underperform and key insights come from his work on the socio-cognitive.

A focal point of the life's work of Nobel Laureate, Douglass C. North, is the limits of orthodox frameworks to explain economic underperformance. In his early work, he discerned that the rationality premise of neo-classical economics needed to be relaxed in order to better explain the rationale and motivations that drove political decision making which led to poor growth. Over time, his thinking has incorporated aspects of sociology and psychology to provide a more balanced appreciation of the actor-structure issue. Although for North the actor remains the main driver of institutional change, said agent is also located within and shaped by an ideological framework.

Ideology, we can hypothesize, informs the actor of how, for example, a market should operate and shapes how decision makers respond to the need for change. Although a dialectic exists between the actor and the structure that allows for one to effect the other, in the main,

the ideological framework remains a constant in stable times. This constancy may give way in times of crisis when actors are forced to reflect on the very tenets that underpin their ideas of how things should operate. It is in such circumstances that opportunities emerge for fundamental shifts in thinking. While the door to radical change may be open, it is up to actors to grasp the opportunity.

North (2005) emphasized the institutional rigidities hypothesis as importantly linked to the grip of belief continuities and, in turn, path dependencies. In early work, (notably North, 1990; 1994; Denzau & North, 1994), he laid the foundation stones for the explication of ‘mental models’ which were defined as the ‘subjective perceptions (models, theories) all people possess to explain the world around them’ (North, 1990, p. 23). He identifies that subjectivity in human interpretation of reality is a key factor in understanding actor decisions (North, 1990, p. 23). Accordingly, North (2005) provides an ideological context for economic choices; to wit, he delves into the very sociocognitive foundations of choice. As he puts it, ‘we choose among alternatives that are themselves constructions of the human mind, (t)herefore how the mind works and understands the environment is the foundation of this study’ (North, 2005, p. 11).

Commencing with the central proposition that institutional change is the outcome of deliberate or intentional choices made by actors, North (2005) sets out to explain how humans come to make said choices. In so doing, he explicates the sociocognitive process by which intentionality emerges as humans construct beliefs that shape decisions to alter the process of institutional change. He posits that beliefs are mental constructs derived from learning, present and past, individual and cumulative, and embodied in a society’s culture.

As he says: ‘The focus of our attention, therefore, must be on human learning – on what is learned and how it is shared among members of a society and on the incremental process by which the beliefs and preferences change, and on the way in which they shape the performance of economies through time’ (North, 2005:, p. viii).

For North, institutions are not only part of our genetic evolution, but also part of our cultural evolution and so, institutional change derives from the complex interplay between genetic dispositions and widely varied human experience (North, 2005, p. 42). Humankind’s ceaseless efforts to gain control over their lives, to try and structure human interaction is constrained by the vestige of institutions accumulated from the past which ‘give rise to organizations whose survival depends on the perpetuation of those institutions and which hence will devote resources to preventing any alteration that threatens their survival’ (North, 2005, pp. 51-52). But it is also ‘that the belief system underlying the institutional matrix will deter radical change’ (North, 2005, p. 77). Understanding institutional change, then, necessitates an understanding of path dependence in order to appreciate the nature of the limits it imposes on change because ‘at any moment of time the players are constrained by path dependence – the limits to choices arising from the combination of beliefs, institutions, and artifactual structure that have been inherited from the past’ (North, 2005, p. 80).

For North, then, to understand institutional change requires an understanding of beliefs which, he believes, are at the heart of human consciousness. As he says:

We have not only a vision about the way an economy or society is working but a normative view of how it could be restructured to work better. Thus

consciousness can lead to the construction of a set of beliefs that induce players to believe that revolution is a preferred alternative to a continuation of what is perceived as a deteriorating condition. At the other extreme, consciousness can lead to the construction of a set of beliefs in the 'legitimacy' of a society. We need to explore under what conditions beliefs get activated to produce order and disorder (North, 2005, p. 103).

Disorder can result from changes, such as political and economic crises, resulting in a dilution of coercive enforcement of formal rules or from a weakening of informal norms of cooperation, inducing individuals, organizations, or nation-states to attempt radical change to the 'rules of the game'. In short, in explaining both the emergence and change of institutions over time, North details a chain of causality from individual genetic architecture, through to sociocultural heritage/context of cognition and belief formation, and finally to deliberate choice in changing formal and informal rules to convert uncertainty to risk. North emphasizes that the differential performance of societies makes it abundantly clear that the cultural component of the institutional scaffolding humans erect is central to the success or otherwise of societies (North, 2005). These observations are crucial to our understanding of why Japan finds the transition from its politico-economic framework to the next so difficult.

A key characteristic of realizing change in Japan is the relationship between state and society. For much of postwar Japan, an implicit pact existed between the Japanese people and government that, as long as they delivered economic growth, political matters would be left to politicians and bureaucrats. As Daniel Okimoto has argued, Japan is 'without question a societal state' (1989, p. 226). At the top of this interlocked relationship between how the market operates, how policy is formed and the support of society is the state. In its focal role,

as Maruyama Masao (1963) has argued, the state embodies the collective will of the people and, through the instruments at its disposal, it harnesses that will to achieve goals shared by society. By extension, then, the 'economy is of importance in providing the instrumental means of achieving larger, collective goals set forth by the polity' (Okimoto, p. 226). Taking this further, Okimoto argues that the 'secret to the power of the Japanese state is thus embedded in the structure of its relationship with the rest of society' (p. 226). Although corruption prior to and throughout the Lost Decade had sullied the reputation of the state's leading actors, to wit politicians, bureaucrats and big business, these actors continue today to play an essential representative, coordinative and directorial function in Japan.

Literature in the field

Their tripartite role is seen both as the recipe for Japan's impressive postwar growth record (e.g. Johnson, 1982) and an important factor in explaining Japan's lacklustre reform implementation (e.g. Amyx, 2004; Katz, 1998; Vogel, 2006; Ihuri, 2003). These two positions are not mutually exclusive. They are, effectively, part of a historical institutionalist's explanation for path dependency and continuity. Dependent on conditions and the stage of economic development, networks may either facilitate or hinder. As a fetter to change, coordinative roles over time tend to become embedded and key stakeholders' interests do not necessarily correspond to the imperatives of change. Current economic reform in Japan is one part of a larger picture and, given the extent of the requisite reform, necessarily requires adjustment elsewhere in the institutional matrix. Two important edited volumes both published following the Lost Decade in 2005 attempt to draw together the multiple strands of Japan's transformation to provide a comprehensive overview. The first of these (*Beyond the lost 10 years (Ushinawareta 10 nen wo koete)*) focuses on explanations for

the economic crisis and the reform years under Prime Minister Koizumi Junichirō (2001-06). The second, *Reviving Japan's Economy : Problems and Prescriptions*, addresses the 'profound transformation process', which the Lost Decade was one stage of, in terms of its 'economic, demographic, social, and political' facets (2005, p. 1). The multi-disciplinary approach of these volumes underscores that the Lost Decade can not be understood only in terms of its economic or financial dimensions. The multi-facted nature of Japan's long run economic malaise argues, in turn, that actors in coordinative roles fulfill key functions in steering the nation through the transition. Because their interests are shaped, in part, by their own beliefs of what should be, reform measures may fall short of expectations and needs.

Certainly, change did occur but it also clear that after a decade of downturn, far more was necessary to raise the economy from its moribund state (Amyx, 2004; Katz, 1998; Vogel, 2006). As Edward Lincoln questions

Is Japan really forging ahead with major economic restructuring, institutional reform, and deregulation? This study argues that the surface image of change is misleading. That 'something' is changing cannot be denied, and the pace of change has clearly increased from the stasis of the preceding two decades (2001, p. 5).

He follows then by outlining some of the essential characteristics of what he sees Japan's political economy to hold for the future. Among others, government in Japan will continue to be 'intrusive in the economy', general 'mistrust of markets' will remain and social considerations will 'temper the drive for efficiency' (Lincoln, p. 5). Japan will continue to adhere to the fundamental values that underpinned the social capitalist framework of the high growth period. This tendency is reflected, he continues, in the fact that though '*structural*

change' has occurred, this is 'quite different from *systemic* change' (Lincoln, p. 5, emphasis in original). And without this radical – as opposed to incremental – change, Japan's economy can not regain its former vitality.

In Lincoln's assessment of Japan's reform initiatives, he says that there is a widely held 'belief in the value of the existing system' (p.8). Although growth on average throughout the 1990s was barely 1%, it was growth nonetheless. For stakeholders, as long as growth continues, belief in the economic system outweighs economic underperformance. The cautious voice argues that old ways 'should not be carelessly abandoned in hopes of a better performance' (Lincoln, p. 221). Reflecting Japan's network economy, Steven Vogel posits that

If we want to know why the Japanese government made critical errors in fiscal policy, monetary policy, and banking regulation, then we must begin with the bureaucrats who oversee these policies and whose ideologies inform the substance of these policies. If we want to understand the politics shaping those reforms with the greatest potential to alter Japan's economic model... then we must look to industry preferences and how these preferences are aggregated by industry associations, political parties, and government ministries (2006, p. 50).

James Lincoln and Michael Gerlach argue that in the absence of the requisite political will, the 'trajectory of change [in Japan] is shaped by legacies of the past: idealized images of how business should be conducted, the slow and haphazard process of deregulation, and the residue of historical affiliations' (2004, p. 299). If a nation is incapable of mustering the will to realize reform, it falls on political leadership to lead (Amyx, 2004; Katz, 1998; Vogel,

2006, Ihori, 2003; Kumei, 2003). Thus it is not reform, *per se*, that is the issue but rather did the Japanese political and corporate elites really want to change?

Empirical Evidence

In January 1999, *shingikai* members were convened in preparation for deliberations on a wide spectrum of billsⁱⁱ which, ostensibly, would lead to sweeping change. This institution has a long-standing presence in Japan's policy formulation process whose role is to provide a formal, legislated forum for discussion. Membership varies according to the issue at hand often drawing on government, the ministries, business and academe for participants.ⁱⁱⁱ This *shingikai* was made up of 40 individuals some of whom, as we shall see, came from the highest ranks of government. As their discussions show, they believed that Japan stood at a critical point in its history and, reflecting the breadth of the bills before them, their task was no less than to bring about national transformative change. They argued that Japan remained a country of great promise but had become derailed in its pursuit of economic gain. It was thus their task, through these bills, to bring back the virtues (*toku*) that had formerly underpinned Japan and, in so doing, revitalize the nation. In this sense, the *shingikai* forum for them was not just a place to hash out the bills' details – that would come later – but also an opportunity to delve into and expose the very essence of Japan's malaise.

The fact that these discussions came at the end of the Lost Decade is significant. The participants' reflective, if not confessional, dialogues suggest that they understood that solutions to what ailed Japan would not be found in just passing more reform measures.

As the literature suggests, the alteration of rules to bring about change amounts to little without a commitment to realize them not only in letter but also in spirit. As North argues, rules frame how institutions operate and, by extension, if this is at variance with actor beliefs, problems of compliance may arise.

In May, *shingikai* members reconvened and so began discussions led by Ōta Seiichi, Director-General of the Management and Coordination Agency. Established in 1984, this institution's central aim was to restructure the organizations and functions of the Prime Minister's Office. Setting the tone for the deliberations, he turned to the first matter on the agenda, namely the revision of the Cabinet Law. The proposed changes, he argued, were based on four reasons:

- 1) the need to strengthen political leadership
- 2) to reduce the 'evils' of interministerial rivalry
- 3) to reduce the size of government, and
- 4) to enhance political transparency and efficiency. (*Shingikai* number 3, p. 4)

In its aim, the strengthening of the Prime Minister's Office was a direct challenge to the norms of Japan's political decision making. During the Liberal Democratic Party's (LDP) sustained postwar dominance, power was diffuse and spread across political factions, bureaucrats and business. Similarly, Ōta's emphasis on the importance of Prime Ministerial leadership signalled fundamental change. Responsive to the electorate which both raised him to power and whose trust was essential to the functioning of the Diet underscores the new realities brought by reform in the election process (see Rosenbluth and Thies, 2010; *Shingikai* number 3, p. 4). This, combined

with the call for greater transparency in political decision making, signals that transformative change was in their sights.

This gravity was reflected by the poignant historical references made by participants. These deliberations were seen as more than an opportunity to implement changes to lift Japan out of its decade-long rut. One surmises that if that were the case then the thrust of discussions would have been related to economic issues. Rather, they spoke in expansive terms of the truly momentous point at which they stood in Japan's history. At this juncture, theirs was to recast, not just the economy, but their nation. Ibuki Bunmei, former LDP Minister of Labour, believed that their decisions spelled change as portentous as those made by Bakumatsu leaders in the mid-19th Century to end Japan's isolationist policy or as transformative as the effect of the reforms of the Allied occupation after World War II. However, whereas change was previously forced upon Japan by foreigners, at this watershed point, the Japanese had the responsibility of and opportunity provided by self-determination (*Shingikai* number 4, pp. 9, 29). One participant characterized change as a matter of survival, warning that as dinosaurs found it impossible to adapt to their changing environment and so became extinct, Japan too must evolve (*Shingikai* number 4, p. 30). A different perspective was taken by Prime Minister Obuchi Keizō who argued that this was not just another turning point but a third in a series of steps towards the restructuring of the relationship between central and local government. Steps in this process of decentralization had been achieved under the guidance of Occupation forces but now Japan must finish the work (*Shingikai* number 4, p. 11). Ultimately, as Chairman of the Democratic Party of Japan and later Prime Minister Hatoyama Yukio reflected, discussion on the need for change

was fine but the time had come to answer the question ‘what form should Japan take?’ (*Shingikai* number 4, p. 44).

Although never fully elaborated, in broad brush terms participants spoke of the need to recreate their society as one that would be ‘free, fair and open’ with the implication that Japan did not now have those characteristics (*Shingikai* number 4, p. 41). What is clearer though is that among these law makers, bureaucrats and businessmen there was a need for a ‘new system’ (*Shingikai* number 4, p. 30). That which ailed Japan was, for these participants at least, not a matter that could be dealt with through economic reform measures. The roots of the malaise were deeper and a manifestation of something much more fundamental which had gone wrong. As Obuchi put it, the creation of Japan’s wealth enjoyed by its people was thanks to the efforts of those who came before. However, the world had changed and the values of the Japanese people too had ‘dramatically diversified’ (*Shingikai* number 4, p. 30). The issue remains whose values had changed and whether they could be reconciled with the imperatives of enhanced economic competitiveness.

The *shingikai* records reflect that the overarching sentiment expressed by participants was that Japan had lost its way. It had achieved wealth but, in its pursuit, had lost something far greater: virtue (*toku*). What is meant by this term is never explained. Whose virtue? What virtues? These are questions that were never squarely addressed. By the same token, though, participants neither questioned what they meant by the term. One surmises that however this term was interpreted by *shingikai* members, they believed that they shared a common understanding. Moreover, it was accepted that,

indeed, Japan lost its 'virtue' in the pursuit of wealth. Prime Minister Obuchi saw the problem as one of a balancing act as economic gain carried the seeds of mammonism and if left unchecked would be a country's undoing.

The pursuit of economic wealth is natural however, this can not be done at the sacrifice of the spirit [*kokoro*]. A balance needs to be maintained. To be frank, there is a problem of spirit in Japan and it stems from education. The critical issue is what that balance should be. Among our forefathers of the Meiji Period, Shibuzawa Eiichi stands out.... I was told that students of his time were taught how to use the abacus and, at the same time, the Annalects of Confucious [*rongo*]. In other words, students were made to understand the inherent conflicts between the pursuit of money and remaining a virtuous person. Students studied how to balance these two opposing ends which was extremely important. (*Shingikai* number 4, pp. 14-15)

This invocation of Viscount Shibusawa, perhaps modern Japan's greatest entrepreneurial pioneer, and his Confucian credo is significant. Beyond mere symbolic value, it is his role in Japanese history that gives this reference such weight. As entrepreneur-cum-reformer, he was a leading figure during an earlier watershed point in Japan's history, namely that of the Meiji Restoration (1868). In response to the Western threat, Restoration leaders introduced sweeping institutional changes that placed Japan's capitalism on a modern footing to help realise the aim of industrialisation. Johannes Hirschmeier makes the point that by the start of this transformative period the traditional prejudice against the merchant class had diminished. But, he adds, these gains were lost during its initial years due to the 'total disregard of the public interest' by the former merchant class in pursuit of personal financial gain (1964, p. 163). Shibusawa and Fukuzawa Yukichi, another leading figure

of this time, recognized that in order to foster entrepreneurship in Japan a new public image had to be created, distinct from that of the tainted political merchant. Although he himself benefited from close political contacts, Shibusawa remains characterized as an entrepreneur who rose above personal financial gain to show how capitalism was a virtuous means to serve the nation.

Echoing North's views on learning and its crucial role in shaping a political economy, participants believed that the root of Japan's malaise, then, was socio-cognitive. They understood that the solution was found in the very formative process of not only just shaping the mind in order to become an effective actor in the market but in the making of one who is also virtuous. In this sense, virtue is not just about obeying market rules of competition, for example, but to remain virtuous in that pursuit. One surmises that this was an oblique attack at the evils of consumerism and unbridled capitalism.

Although North does not specifically draw a link between 'virtue' and economic performance, he does make clear that another widely accepted 'evil,' to wit, corruption, can have detrimental effects. He observes, for example, that notwithstanding gains achieved through Russia's recent market reforms, corruption remains endemic in its economy. North makes the point that corruption has not only hindered Russia's growth but also, in its endemism, points to something more important, namely ideology.

History afforded Russia the opportunity to implement reform however a corresponding ideological shift not did occur and, in turn, the full economic gains from these measures have not been realized (North, 2005). Similarly, his research on Castilian Spain shows that regardless of how 'virtuous' market transactions may be, it is also necessary that the laws that shape the transactions be aimed at promoting national growth as opposed to furthering the personal aims of key policy makers (North and Thomas,

1973). While point number 4 of the Cabinet Law addresses the problem of the non-transparency of decision making and was discussed in the *shingikai* meetings, there is little evidence to suggest that they saw ‘corruption’ as the worm at the core of why Japan’s capitalism had gone bad.

Regardless, the point is that *shingikai* participants understood that the promotion of effective – as they defined it – market operation was not just about passing appropriate reform bills but about engendering an ideology embraced by actors that corresponded with approved values. In other words, their foremost task was to create an ideological underpinning in order to create a political economy as they deemed appropriate. By implication, if they limited themselves to just passing competition enhancing measures without concern the return of lost virtue, then Japan would dangerously slip into neo-liberalism.

Whatever form the disease may have taken, for Hatoyama ‘Japan’s illness manifested itself at the national, firm, and individual levels and resulted in the loss of Japan’s spirit, economic strength, self-reliance and self-respect’ (*Shingikai* number 4, p. 43). He lamented that the evils of capitalism were eating away the very fabric of Japan’s society as evidenced by the fact that ‘the community spirit [*kyōdōtai*] has been greatly weakened [and] so too its relationship with the family unit, regional community... and the relationship between the individual and the nation’ (*Shingikai* number 4, p. 15). In short, the concern of *shingikai* participants was at the ideological level of who *homo economicus* had become and before any serious discussion of economic reform could

be take place, it was necessary to understand the illness that had given rise to the Lost Decade.

It is critical to understand what the participants characterized as good and bad among the various activities and consequences of market based accumulation of economic wealth. To be sure, their discussions do not suggest that they thought the market or capitalism was bad, *per se*. Afterall, theirs was the postwar generation that had through sacrifice and labour pulled Japanese society from poverty to affluence. But, they also recognized that in the reconfiguration of their politico-economic framework, they must reincorporate that which they had lost, namely, virtue. In short, they sought to recreate a ‘virtuous capitalism’ – one inspired by the past.

There was little further discussion about the reconciliation of these often conflicting ends. But, it was clear that the accent of discussions fell on this topic which, indeed, seemed a preoccupation for some participants. A similarly emotive debate arose when the talks focused on the more specific issue of competition. In terms of national cases, Europe’s continental economies did not figure in their discussions. In what was tantamount to a rejection of neoliberalism, Ibuki turned to what he considered Japan’s exemplars of alternate political economies, namely those under former President Ronald Reagan and Prime Minister Margaret Thatcher. Acknowledging that under strong leadership their nations’ economies had grown, ultimately Ibuki deemed that the ideological tenets of how their market operated were unsuitable for Japan. He opined that the ‘1000, nay 1500 years of Japanese history had cultivated a sense of joint responsibility, family and a sense of unity of and sacrifice for the nation’ (*Shingikai*

number 4, p. 13). He accepted that though Japan's market needed deregulation, 'the principle of competition and the omnipotence of market economics for the survival of the fittest and mammonism leads to a spiritually desolate society' (*Shingikai* number 4, p. 13). Prime Minister Obuchi echoed these sentiments in his acknowledgement of the importance of market reform and his fears over the social problems from hypercompetition. Striking a middle ground, he urged reformers to find rules to ensure fair competition, a second chance for those who fail and a social security net to ensure that all enjoy a minimum standard of living. He exhorted those participating in *shingikai* meetings on economic reform that whatever shape the political economy may take, they must ensure that these criteria are maintained (*Shingikai* number 4, p. 13).

Although reform measures that were introduced did bring greater competition there was little sign at the end of the decade that the economy would return to growth rates similar to the benchmark of developed Western nations. Reform legislation was passed – the need was too pressing to be ignored – but implementation, as we know, is another matter. Without political will and the acceptance of the Japanese people to accept the attendant pains, change was contained within the framework of a political economy that reflected existing values. Authors have argued for greater competition but the records show a strong fear that what was perceived as unbridled competition in the US and Britain would undermine the fabric of Japanese society. It is argued here that the reason why reform was less efficacious than one would expect is because the full implementation of market reform cut across the beliefs held by political decision makers and the Japanese people.

Implications for Japan Today

With the announcement on 7 September 2008 that the two US government supported firms Fannie Mae and Freddie Mac would be nationalized, the global financial crisis was brought squarely into the forefront of the business world. For Japan, this came at a time when its economy was beginning to show signs of recovery from the 1990s downturn and the LDP was in turmoil from its rapid succession of prime ministers following the retirement of Prime Minister Koizumi in 2006 . Although the in-house ‘cleansing’ of Japan’s banks placed them in a comparatively healthy and less exposed position to weather the global storm, the economy as a whole was weak (Grimes, 2009, p. 107). The stimulus measures that followed have helped prevent what would have been far worse. But, the expenditures have also rendered further market restructuring politically unviable until, at least, economic recovery is in swing. This prospect is increasingly difficult given Japan’s tightening fiscal noose.

A legacy of Japan’s post-war growth strategy reliant on US bound exports is the current tepid domestic demand. Although this asymmetric trade relationship is changing with Japan seeking to stimulate consumers’ spending, declining real wages suggest that in the near future domestic demand will not be able to take up the slack. If the long-term forecast of 0.5 to 1% GDP growth is correct, then not only will government have to walk a tight-rope to be able to pay back its largesse but will also have to find new ways of expanding economic output. Richard Katz argues that without fundamental restructuring of the domestic market, Japan cannot achieve strong sustained growth (Katz, 2010). If growth is sought by freeing up the domestic market, a rise in unemployment would follow which potentially would be tolerable if new jobs were generated and government could afford the costs of dislocation and, at the same time, increase household income, support the aging population and pay back debt. This possibility is – at least for the moment – unrealistic. Under current economic conditions, firms will more likely continue to keep worker numbers above efficiency levels and fund

construction firms that otherwise would be forced to fold. Here, business and government need each other - as does this nation as whole - for this Catch-22 relationship is a key aspect of Japan's informal social safety net (Murphy, 2009). As long as gains from restructuring are less than the political backlash to change, the relationship will at least keep a foot in its past ways of the high growth period.

That said, the Japan at the outset of the Lost Decade and that of some 20 years later are different. In 1998, T. J. Pempel wrote that the 'socio-economic, institutional, and policy underpinnings of the old regime have shifted, and the change is irreversible... [but] no clear agenda commands comprehensive support' (p. 212). Three years later, Prime Minister Koizumi Junichirō came into power bringing hope for the seemingly moribund state. Being mediagenic and a consummate political tactician, he rose on a platform of reform assuring the electorate that Japan would be better for the attendant pains. Time will tell what his legacy will be. However, it is clear that following Koizumi's departure, neither the Liberal Democratic Party or the Democratic Party of Japan have demonstrated the ability to lead the nation through the painful change. Rather, the rapid succession of new prime ministers underscores the seeming absence of strong political leaders from which the parties can draw.

Part of the problem may be an issue of age. As the evidence here shows, there was reluctance among *shingikai* members whose values were formed during the high growth period – years of considerable personal sacrifice – to sweep them aside for something new. Attuned to this generational issue, a survey conducted in 2005 among 480 elected members of the House of Representative, the lower house of Japan's bicameral legislature, suggests that though attitudinal difference exist between generations, they are not radical. The authors point out

that the ‘younger cohorts may indicate an openness to neo-liberal policies... this result is not evidence that these younger generations have adopted such views to the same degree and extent as have leaders in Washington or London (Boyd and Samuels, 2008, p. 48). On the basis of this assessment, regardless of how diverse public discourse may become, future politicians will follow a path of incremental change.

However much the Japanese media associates the rise of right-wing nationalism and cultural conservatism in Japan with an angry and alienated youthful generation, this connection is not reflected in the distribution of preferences among Diet members. To the contrary this study finds that the distribution of preferences is far less extreme than many fear. Though democratic discourse remains active and vibrant in Japan, we find little evidence that either the midcareer generation or the youngest generation will stake out a radically new course for the nation. (Boyd and Samuels, p. 51)

Takanaka Heizō, academic and reform czar under Prime Minister Koizumi, argues in his recent book *What happened to ‘reform’? Is this the chance for the Democratic Party of Japan?* (*‘Kaikaku’ wa doko ei itta? Minshūtō ni chansu wa aru ka?*) characterises the nation today with the words ‘hope’ (kibō) and ‘despair’ (zetsubō). His central point is that while fundamentally the economy is strong (senzai teki ni tsuyoi), the impetus for reform has dangerously waned in the last years. Although there are numerous impediments, vested interests among others, which hinder change, the responsibility for driving the reform process, nonetheless, rests with politicians. The implication is that short of strong leadership a la Koizumi, it will be difficult for Japan to realize fundamental transformative change. He also

suggests that part of the problem is that, despite its prolonged nature, the economic malaise has not been so bad as to galvanize public demand for change (p. 4). This, in turn, raises the issue whether Japan really did experience a ‘crisis’ and what this term means. As Colin Hay argues:

[A] crisis is not merely a property of a system, it is a lived experience; it is a politically mediated moment of decisive intervention and structural transformation. Moreover, it involves the active display of agency by actors or bodies which have some autonomy *at the level at which the crisis is identified*. What this in turn suggests is that the very identification of a moment of crisis is an integral aspect of the process of state transformation (Hay, 1999, p. 323; emphasis in the original).

Thus, as an opportunity for transformative change, a crisis is not the point where the reading of economic indicators merely says so but the point when actors experience it as such. The distinction is important. The first assumes an automatic and direct causality link between economic conditions and human reaction; and the second argues that it is when stakeholders believe that the economy is in crisis that it is in crisis. As Blyth (2002) argues, a crisis occurs when stakeholders have run out of ideas on how to mend the economic problem so that they are prepared to accept a new ideational paradigm. In the case of the Great Depression, U.S. government and big business found themselves at the edge of the road map, as it were, and, in turn, embraced Keynesian economics. In abandoning a laissez-faire approach to market intervention and the acceptance that it was good and appropriate for government to be interventionist, stakeholders embraced the new values that underpinned the New Deal.

In the case of Japan, however, on the cusp of the new millennium, after a decade of economic decline, reform, and much reflection on ‘what next’, Japanese political and corporate leaders still showed few signs of having found their way. A paradox arises: given the once vaunted coordinative capacity of Japan’s economy and the pressing need for change, why did Japan not rise to the challenge this time? Vested interests and weak political will played its part, as authors have noted, but these factors do not bring us to the nub of the matter. They are, rather, indicators that answers lie elsewhere.

Conclusions

North’s concept of a ‘mental model’ is key to understanding why reform initiatives during the Lost Decade fell short of what observers thought they should achieve. It is also critical in interpreting the trajectory of Japan’s economy. As he hypothesized, we live in a non-ergodic world and institutions act as mechanisms by which we reduce uncertainty. As humanly conceived, they are also reflections of how we perceive the world should be. The institutions of a political economy are, in this sense, indeed constructs to organize the activities that lead to economic growth. And, by extension, their matrix is not only a macro level politico-economic framework but also a reflection of the values, or beliefs, of the policy makers. North is also very conscious of and, indeed, pointedly argues that key stakeholders implement policies that do not necessarily lead to economic growth either because their interests lie elsewhere or that they hold beliefs in how their political economy should operate that result in lesser growth.

Research on the government and business elites' response to the 1990s economic turmoil raises the question whether they really wanted to change. Recognizing the imperatives of the time, reform measures were implemented and have shaped how the market operates. But, as authors note, there was a lack of political will. The debates of key policy makers in 1999, after a decade of economic turmoil, show that they continued to hold on to values and beliefs of a political economy that resembled that of the high growth period. Indeed, in defence of these beliefs, speakers reached for examples of what they considered to be hypercompetition and invoked stories of Japan's past to buttress their positions.

The point to be made is not that the values of Japan's social capitalist system are wrong but that, if policy makers wish to hold on to this model of its political economy, they must find within this framework a solution that squares its particular circle of conflicting problems and, at the same time, achieve sustainable growth. Whatever the solution, Japan will need to accept the attendant pains which, in the foreseeable future is politically unrealistic. Expressed differently, at this juncture in Japan's history, the opportunity exists to reconceptualize its political economy. This is not merely a technical matter of reform measures but, fundamentally, about how political and market related institutions enmesh to produce growth and share the gains. To achieve this, policy makers need to decide what values they wish to hold on to and what ones to let go of in order to forge a political economy for tomorrow.

Japan is a 'sleeping giant'. Among its manifold assets most important is the dynamism and discipline of its people. As much as this was true of Japan as it emerged from the ashes of World War II, it remains true today. The politico-economic framework of the 'economic miracle' harnessed the national desire for 'catch up'. The attendant sacrifice was accepted as

it resulted in economic growth and that, critically, the sharing of the gains were considered by and large fair. A deal was struck. This deal was underpinned by shared beliefs and values that governed that distribution of wealth. Similarly, Japan today must come upon a new way of aligning the strength of its people with a new politico-economic system, one that is rooted in the past but also one that carries it into the future.

Former Chairman of Toyota Motor Corporation (1992 – 99) and Chairman of Japan Business Federation (1994-98), or Keidanren, Toyoda Shoichirō struck a similar cord in his popular book *The Creation of a Japan with Charm* ('*Miryoku aru Nihon*' no Sōzō). Writing during the Lost Decade, he lamented the current state of affairs and outlined, as he saw it, the multifaceted problem that confronted Japan. The economic, political and social framework which had served Japan well in its period of catch-up now required revamping from the ground up. And, importantly, this framework needed to be located within a new a 'vision' for the nation – one, he suggested, that had not yet been found (p. 2). Still, 15 years later, one is pressed to find that 'vision'.

Notes on Contributor

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Endnotes

ⁱ For an overview of institutional theory in political science see Peters. *Institutional Theory in Political Science* and for the field of political economy consult Weingast and Wittman, *The Oxford Handbook of Political Economy*.

ⁱⁱ The list included the following bills:

- Partial Revision of the Cabinet Law (Naikaku Hō no Ichibu wo Kaisei Hōritsuan)
- Partial Revision of the National Administrative Law (Kokka Gyōsei Soshikihō no Ichibu wo Kaisei Suru Hōritsuan)
- Establishment of the Cabinet Office (Naikakufu Setchhi Hōan)
- Local Government Reform (Chūōshōfutō Kaiaku no tame no Kuni no Gyōsei Soshiki Kankei Hōritsu no Setsubitō ni kan suru Hōritsuan)

Also, bills were submitted that deal with or the creation of the following ministries or agencies:

- Ministry of Internal Affairs and Communication (Sōmushō Setchi Hōan)
- Postal Services Agency (Yūsei Jigyōfu Setchi Hōan)
- Ministry of Justice (Hōmushō Setchi Hōan)
- Ministry of Foreign Affairs (Gaimushō Setchi Hōan)
- Ministry of Finance (Zaimushō Setchi Hōan)
- Ministry of Education, Sports, Science and Technology (Bunbu Kagakushō Setchi Hōan)
- Ministry of Health, Labour and Welfare (Kōsei Rōdōshō Setchi Hōan)
- Ministry of Agriculture, Forestry and Fisheries (Nōrin Suisanshō Setchi Hōan)
- Ministry of Economy, Trade and Industry (Keizai Sangyōshō Setchi Hōan)
- Ministry of Land, Infrastructure, Transport and Tourism (Kokudō Kōtsūshō Setchi Hōan)
- Ministry of Environment (Kankyōshō Setchi Hōan)

-
- Independent Administrative Cooperative Body (Dokuritsu Gyōsei Hōjin Tsūsoku Hōan)

ⁱⁱⁱ For further details on post-1945 *shingikai*, see Schwartz . *Advice and Consent*.

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