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Spirit of the Samurai

Shady land deals brought down Premier Kakuei Tanaka in the biggest political scandal in Japan's postwar history. But Tanaka is important not because he can be added to the long list of corrupt people who exploited the wealth of others to his own ends through the monopoly of land; he has more general significance in the quest to understand the malfunctionings of the industrial economy.

Kakuei Tanaka embodied the spirit that betrayed the aspirations of the Japanese who, in 1867, liquidated the parasitic class of feudal land lords. The mechanism which was selected to achieve this result was simple, and it was executed reasonably smoothly. Rent which had formerly been levied upon the rural peasants to support the warrior class and its conspicuous consumption was switched into the coffers of the nation's exchequer and used to finance an industrial revolution.

Two hundred and fifty *daimyo* (feudal lords) were rendered redundant, and Japan embarked on the path of industrial growth until, finally, she attained supremacy in the field of modern economic enterprise. This was achieved, at the outset, on a foundation of land value taxation. Something, however, ultimately went wrong. Our study of Japan will analyse the processes that created the opportunities for the Japanese to industrialise, and will reveal how land monopoly undermined that grand determination and left the people living in a miserable physical environment even while they stacked up the material goods that poured out of their factories.[1]

But at the outset we must note that, to the leading Japanese land speculators, there was nothing mysterious in the forces that served to unhinge attempts at harmonising the process of modernisation with a civilised social system and stable ecological environment. Their appreciation of their power to hinder the creation of new wealth and higher living standards, in the pursuit of unearned rental income, is neatly summarised in the book which sold a million copies and helped its author, Kakuei Tanaka, to become Prime Minister of Japan.

The contents of the book, *Building a New Japan*[2], are summarised in its subtitle: A Plan for Remodeling the Japanese Archipelago. In it, Tanaka describes objectively how the process of land monopoly dislocated the growth of urban centres like Tokyo, priced decent homes out of the reach of wage-earners, deterred the creation of new factories, distorted the locational pattern of industries, and inhibited the development of agriculture. In this one book, then, Tanaka affirmed the essential features of the thesis that land monopoly is the major agent blocking the creative efforts of people and their capital. And yet, ironically, modern Japan was built on a fiscal foundation that provided her leaders with the unique opportunity for avoiding the destructive path of the land values cycle that manifested itself in other industrial nations. What were the distinctive contributions and promises of the Japanese land tax, and how were they eclipsed by the grasping claims of the land monopolists?

The political power of the Tokugawa *shogun* and his supporting structure of *daimyo* and their dependent *samurai* was wiped out by the restoration to power of the Emperor in 1867. This transformation of the Japanese political system was the prelude to a rationalisation of the economy, a programme specifically designed to industrialise an agrarian economy to meet the challenge from the Europeans and Americans who demanded that there should be free trading access to the Japanese market.

Japan, at this point, was in a backward state. The agrarian society operated on a configuration of traditional values and loyalties which were no match for the thrusting merchants who threatened to follow Commodore Perry's gunboat. To resist this threat, Japan had to modernise her political and economic institutions. But to build a new superstructure, she had to change the method of extracting agricultural surplus. Rents and taxes had up until then been paid in kind by peasant cultivators. This was unsuitable for a modern economy. Taxes, to facilitate the creation of a new economic infrastructure, had to be paid in cash. Marx feared the worst:

> If the foreign trade, forced upon Japan by Europeans, should lead to the substitution of money rents for rents in kind, it will be all up with the exemplary agriculture of that country. The narrow economic conditions under which that agriculture is carried on, will be swept away.[3]

Marx's prediction proved to be wrong. Agriculture did not fare any worse than under the feudal system; indeed, within two decades Japan had completed the transition to modern economic growth[4] and was ready to take on all-comers!

The Meiji reformers reconstructed the land tenure system through the Land Tax Revision Act (1873). They had no axe to grind. They were technicians determined to produce solutions to the problem of strengthening the economic base of their society, rather than rigging the results in favour of the landlords. Nonetheless, the law which they enacted suffered from a number of shortcomings. These — and their effects — we need to examine in detail.

The Meiji land tax, as we shall see, has been criticised on a number of counts. These criticisms, however, have been misdirected; they imply, or explicitly state, that the land tax *per se* is a deficient instrument for accomplishing the desired goals. But on the contrary, problems arose in Japan because the tax was technically inadequate and incomplete. These concessions, however, far from counting against land taxation, provide those who formulate policies today with a clearer understanding of what they need to accomplish if they wish to maximise the prospects for constructive development.

The Meiji reformers devised a formula which led them to believe that their tax fell on net produce (in contrast to the Tokugawa land tax, which was a proportional levy on gross farm produce). Net produce, correctly defined, is economic rent. The tax is still commonly regarded as falling on land values by modern scholars.[5]

The law required that a *standard value* of cultivated land should be established. To arrive at this figure, certain costs were deducted. These were the cost of seeds and fertilizers (15% of the value of gross output), and the national land tax (3%) and local land tax (1%). Income was calculated by taking local market prices averaged over the previous five years.

It is evident from this that the Meiji formulation of taxable income made no allowance for the wages of farmers to compensate them for their labour inputs. The tax, then, fell on both rent *and* wages, and was evidently not a tax on net produce. Few students of this crucial fiscal feature of early modern Japan have noted, let alone elaborated upon, the consequences. Ranis, for example, settled for parenthetically noting that 'implicit wages not deducted' in a footnote to his otherwise excellent quantitative study.[6]

Yet the authorities realized that their formula failed to untax wages, for they had a second method for determining the value of land.[7] This was to capitalise the rent actually paid to landlords, that is the surplus *after* allowing for the wages (and other overheads) retained by a tenant farmer. The problem for the authorities was that, using this method of arriving at net income, there would be a disparity in taxable income. For — using the same rate of interest to capitalize income, to arrive at the value of land — they would get two different figures, depending on whether a piece of land was owner-occupied or farmed by a tenant. Instead of imputing the cost of wages under the first formula, they dealt with this problem by using two different rates of interest. They assumed that the income of the tenant was one-third and the rent was two-thirds of taxable income. So they decided that rental income should be capitalised by using a rate of interest which was two-thirds (4%) of the figure used to capitalize owner-cultivated land (6%). This ensured that the 'land' value would turn out to be identical on the same property whether that land was owner-occupied or cultivated by a tenant.

Now, while a tax on wages has an obvious effect on family incomes — reducing purchasing power, and so restricting the domestic market for consumer goods — the overall effects on owner-occupiers need not have been serious, given that the land tax did not take away the whole of economic rent. This state of affairs, however, held true only for so long as the price of rice remained buoyant. As soon as it started to come down it had a serious effect on incomes. This was what happened in the mid-1880s. The price of rice rose steadily until 1881, then started sliding, reaching its lowest point in 1887.[8] From 1883 to 1890, over 367,000 producers suffered forced sales for arrears in the payment of the land tax. The total amount in arrears was 114,178 yen , and the area of land auctioned or confiscated was nearly 116,000 acres.[9]

The distress in the countryside was the product of an imperfectly formulated land tax. The payments were inflexible obligations even compared with the Tokugawa system. In the feudal period, if harvests were poor (leaving a smaller economic surplus), the official who was charged with the duty of collecting the taxes told the farmers how much the payments would be reduced: this provided immediate relief. There was no administrative reason why the centralised Meiji bureaucracy could not have emulated this procedure.

The sale of all or part of a farm in the 1880s, then, provided more than just the cash with which to discharge immediate tax obligations. For the farmer, as a tenant, could deduct his wages from the gross product before paying the remainder, as rent, to the landowner. This shifted the tax burden onto the landlord: he, however, was destined for long-run prosperity as the price of rice recovered. The Meiji land tax, however, was levied at a uniform rate 'without regard to bumper or lean years',[10] which meant that tenants and landowners retained part of the economic surplus in the bumper years, but the landowning farmers had to dig into their wages to meet tax obligations during lean years.

The limitations placed on the land tax guaranteed that, at the macro-economic level, the 'miracle' of the Japanese model was to be betrayed by the 18-year cycle of destruction. The first cycle will be examined here because it lays bare the defects in the Meiji land tax. The last cycle, which brought to a close the major phase of unimpeded growth in the decades after the Second World War, will then be fully investigated in Chapter 12. This will demonstrate that, without a 100% tax on annual land values, the hard work and high-level entrepreneurial skill of the Japanese workers and managements, their flexible working practices and adaptive institutions, are ultimately defeated by those who monopolise the earth's natural resources.

How do we date the beginning of any 18-year cycle in land values that might have been present in the early Meiji period? The obvious starting point would be 1873 (rather than the first year of Restoration, 1868), for this was the year of the great land settlement which established new rural relationships and provided secure legal title to land for those who formerly held it by custom. Money rents and legal titles ensured the creation of a market in land.

If there *was* a cycle of land values, it ought to have brought its palsied hand down in 1890: and that is precisely what happened. Rents rose to an extraordinarily high proportion of total factor income,[11] and in 1890 the people were confronted with what Norman characterised as 'this first economic crisis of modern Japan'.[12]

How did the Meiji reformers unwittingly hand over their economy as a hostage to fortune?

TABLE 11:I

Relative Shares in Japan's Agricultural Sector

	Percentage of Total Product		
	Landowners	*State*	*Tenants*
1868	18	50	32
1873	34	34	32
1874-76	55	13	32
1877	50	18	32
1878	56.5	11.5	32

	Percentage of Net Agricultural Product		
	Rent	*Taxes*	*Tenants*
1878-82	60.4	16.9	22.7
1888-92	56.0	15.5	28.5
1898-1902	50.7	12.1	37.2
1908-1912	55.1	12.5	32.4
1918-22	59.1	9.2	31.7
1928-32	57.9	9.7	32.4

Source: G. Ranis, 'The Financing of Japanese Economic Development', *Econ. Hist. Rev.*, XI, 1958, Table 5, p. 448. Norman [*op. cit.*, p. 150, n. 29] gives 56% to landowners and 12% to the state for 1877.

When the 3% land tax was instituted, payable in cash, the state took about one-quarter of the produce from farmland.[13] Thereafter, however, the distribution shifted in favour of landowners. From Table 11:I, we can see that landowners received an increasing proportion of agricultural income at the expense not of the tenant, but of the state.

This re-distribution of income, in an opposite direction to the one which we would have advocated, ensured that all the speculative motives and structural dislocations associated with the European land market would be at work in Japan.

The state unwittingly conspired with the landowners in the interests of the latter. R. P. Dore has emphasised that those who controlled policy after the Meiji Restoration were not landed gentlemen — unlike the situation in England at the comparable state of industrialisation — but were bureaucrats who depended for their income on salaries.[14] 'They had, therefore, no personal interest in protecting agricultural incomes at the cost of slowing the growth of industry.'[15] But with the growth in the demand for democracy, the landlords were able to drive a wedge ihto the disinterested administration of the affairs of State:

> As soon as they were allowed representation in the national Diet their main interest was directed towards reducing their tax burden. This pressure on the national budget slowed the growth of agricultural research and extension services and of the developmental subsidy system. If the voice of the villages in the Diet had been the voice of practising farmers these things would not have been neglected.[16]

In 1878, the land tax was reduced to 2.5%, but rents were not lowered for tenant farmers.[17] In 1884, the government abandoned the original plan to reassess land values every five years: this meant that, with the rising price of rice, an increasing proportion of economic surplus remained with landowners. By 1889, the economic privileges of the new landowning class were institutionalised in the political system. In that year, the franchise in national elections was granted to men over the age of 25 years. Of a total electorate of 453,474, only 13,491 qualified to vote on the basis of income tax payments. The majority, 97% of the total, were landowners who qualified on the basis of land tax payments.[18] Appropriately enough, the economic crash the following year, in 1890, bore witness to the underlying influence exercised by the landlords over the economy.

The transfer of political power to the landlords was accompanied by a reduction in the contribution of land taxes to total government revenue. In 1872, land taxes were 72% of revenue. This share declined to about 46% in 1890, and sank to 15% just before the outbreak of the First World War.

When we dig behind the statistics, we find a pattern of behaviour which has now become depressingly familiar. There was corruption; local governors who learnt, in their official capacities, of intentions to build railways, bought land and re-sold at inflated prices to the construction companies.[19] Land was the most secure investment, yielding a rising income: it therefore attracted money and entrepreneurial skills from both the rural and urban sectors that would otherwise have been devoted to fixed capital formation in industry.[20]

The 'extremely high rent' demanded by landlords reduced the domestic market for factory-produced consumer goods.[21] Even more serious, however, was the impact on investment. For during this period construction (excluding military investment) accounted for over 50% of gross domestic capital formation,[22] and there came a point where buying or renting land for erecting buildings, roads, bridges and railways reached deterrent levels.

Thus, the level of the land tax, although significant from the point of view of landowners, was a declining proportion of gross rents and was ultimately insufficiently high to deter the land monopolists from influencing the process of economic growth. The incorrect interpretation of these facts, then, would be to arrive at the conclusion that a land tax cannot ultimately thwart landlords from having a causal influence on the directional growth of the economy. The correct interpretation is that a 100% recovery of annual rental income is a necessary pre-condition for stable, sustained development.

The Meiji leaders had a perfect opportunity to realign their policies in the 1890s. The onset of the first severe structural recession induced by the termination of the 18-year cycle in land values was the beginning of five years of severe hardship.[23] There were demands for reforms. One of the options was the establishment of a consistent and thorough-going programme of land value taxation. Henry George's *Progress and Poverty* appeared in translation in 1891, and it created a considerable impression.[24] The virtues of the tax were vigorously promoted, and one of its advocates was an American missionary, C. E. Garst — affectionately known as Tanzei Taro ('Single-tax Joe'), 'who stumped the country with a proselytizing zeal primarily directed towards the propagation of the gospel according to Henry George'.[25] The landowners, however, were by now exercising power in the political system, and the idea of capturing the full value of land for the benefit of the community — offset by a reduction in taxes on wages and consumption — was not adopted.

Recovery began in 1895. Was this the start of the second of the 18-year cycles? The peak in the new cycle should have been in 1913. This was, indeed, the case.[26] But although land values began to slump, the structural recession did not occur: the preparations for World War I intervened to provide the economy with an extraordinary buoyancy. Had this influence not come into operation, report Ohkawa and Rosovsky, 'it is entirely possible that 1909-12 would have developed into a full-fledged downswing' in the economy, for in that period the growth rate of private capital formation 'falters'.[27]

And so the price of ignoring Henry George's solution was not paid. A world war saved the economy from the effects of the land values cycle — as it did in Britain in the 1930s — but few would deny that mass slaughter and a profitable munitions industry are high prices to pay for neutralising the influence of land monopoly. Land values quickly recovered, and were on course for a termination in the early 1930s, neatly dovetailing the deficiencies of the domestic economy with the identical problems that were converging in the leading industrial systems. It was the same story in the postwar years, as we shall now see.

Notes

1 J. Woronoff, *Japan: the Coming Economic Crisis*, Tokyo: Lotus Press, 1979.
2 K. Tanaka, *Building a New Japan*, Tokyo: Simul Press, 1972, first English edition, 1973.
3 *Capital, op. cit.*, Vol. I, p. 140.
4 H. Rosovsky, 'Japan's Transition to Modern Economic Growth, 1868-1885', in *Industrialisation in Two Systems*, editor: H. Rosovsky, J. Wiley & Sons, 1966.
5 E. H. Norman, *Japan's Emergence as a Modern State*, New York: Institute of Pacific Relations, 1940, p. 141; R. P. Dore, *Land Reform in Japan*, London: Oxford University Press, 1959, p. 15, and T. Fukutake, *Japanese Rural Society*, Ithaca: Cornell University Press, 1967, p. 10.
6 G. Ranis, 'The Financing of Japanese Economic Development', *Economic History Review*, Vol. XI, 1958, p. 445, n. 1.
7 J. I. Nakamura, *Agricultural Production and the Economic Development of Japan 1873-1922*, Princeton: Princeton University Press, 1966, p. 190.
8 Norman, *op. cit.*, p. 144, n. 15.
9 Norman, *ibid.*
10 Norman, *ibid.*, p. 142.
11 C. Clark, *The Value of Agricultural Land*, Oxford: Pergamon Press, 1973, p. 88.
12 *Op. cit.*, p. 166.
13 Norman, *op. cit.*, p. 141, n. 10, and p. 143, n. 14.
14 R. P. Dore, 'Land Reform and Japan's Economic Development', *Developing Economies*, Special Issue, Vol. 3, 1965; page references are to the reprint in *Peasants and Peasant Societies*, editor: T. Shanin, Harmondsworth: Penguin, 1971.
15 *Ibid.*, p. 381.
16 *Ibid.*, p. 385.
17 A. Waswo, *Japanese Landlords*, Berkeley: University of California Press, 1977, p. 22, and Dore, *op. cit.*, p. 17.
18 Waswo, *op. cit.*, p. 33, n. 65.
19 W. W. McLaren, *A Political History of Japan during the Meiji Era 1867-1912*, London: George Allen & Unwin, 1916, p. 129.

20 Waswo, *op. cit.*, p.76, Norman, *op. cit.*, p.111, and Dore, *op. cit.*
21 Norman, *op. cit.*, pp.165-166.
22 K. Ohkawa and H. Rosovsky, *Japanese Economic Growth*, Stanford, California: Stanford University Press, 1973, pp.16-17.
23 Dore, *op. cit.*, p.63.
24 Y. Jamasaki, 'The Influence of Henry George's Ideas Upon Modern Japan', *The American Journal of Economics and Sociology*, Vol. 21, 1962.
25 Dore, *op. cit.*, p.67.
26 *Ibid.*, p.20, for the price of rice land, and Clark, *op. cit.*, p.99, Table 39.
27 *Op. cit.*, p.33.