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## *Money, Employment, and Liberalism: in Memory of Professor Masayuki Otaki*



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## Introduction

SSJ newsletter No. 60 features one of Japan's outstanding macroeconomists, Professor Masayuki Otaki. For over 20 years he was our colleague but passed away unexpectedly last summer. Horiuchi Akiyoshi and Tamura Masaaki introduce innovative Otaki model, which critique and offer alternatives to Robert Lucas's quantity theory of money. Horiuchi focuses on the background to the development of the model, and Tamura takes an in-depth look at its mathematical basis. Kuninori Morio shows us Otaki's passionate concerns about the environment, especially global warming. Cato Susumu and Mamiya Yosuke examine Otaki's life and work, revealing the influences that formed his profound thoughts on economic theory. Takeshita Keisuke and Uno Shigeki sketch out the many intellectual exchanges Otaki had with researchers in other fields. Takeshita gives us an interesting view of aspects of international law that underlie Otaki's economic theory. Uno sheds light on Otaki's wide-ranging knowledge of political thought and intellectual history from the view point of a historian of European political thought.

In the ISS Research Report, Meredith Shaw outlines her intriguing research on cultural elements in the persistence of dictatorship as a form of rule. Lastly, we are providing you with an update on recent lectures by the ISS Contemporary Japan Group, recently published books by ISS staff, and the Focus on ISS, which introduces the Tokyo Conference on the Economics of Institutions and Organizations which will be held at ISS on March 18 and 19, 2019.

Unfortunately, SSJ Newsletter will cease publishing with this, our last newsletter. We would like to take this opportunity to thank you for all your contributions to the 60 issues of the Newsletter.

Maki Yokoyama  
Managing Editor

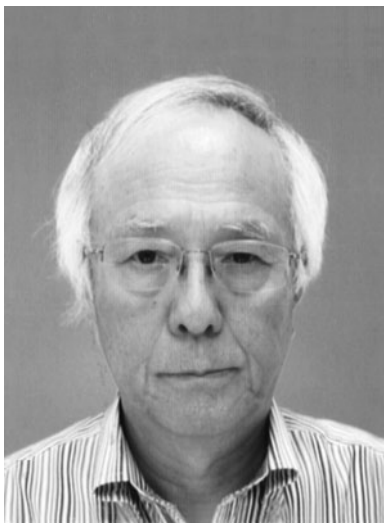
## Table of Contents

### Money, Employment, and Liberalism: in Memory of Professor Masayuki Otaki

HORIUCHI Akiyoshi The New Economics of Otaki Masayuki.....	p.3
TAMURA Masaaki Revisiting the "Otaki Model" .....	p.6
KUNINORI Morio Global Warming and Intergenerational Concerns: Masayuki Otaki's Contribution to Environmental Economics .....	p.10
CATO Susumu Challenges of Professor Masayuki Otaki .....	p.13
MAMIYA Yosuke Mathematics and Humanities .....	p.17
TAKESHITA Keisuke Prof. Otaki as a Humanitarian – Law and International Relations .....	p.20
UNO Shigeki In Memory of Professor Otaki Masayuki .....	p.24
<b>ISS Research Report</b>	
Meredith SHAW The Cultural Struggles behind Autocratic Regime Change .....	p.27
<b>ISS Contemporary Japan Group</b> .....	p.30
<b>Recent Publications by ISS and ISS Staff</b> .....	p.34
<b>Focus on ISS</b>	
NAKABAYASHI Masaki.....	p.36

# The New Economics of Otaki Masayuki

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Between his time as a graduate student in his 20s and his death at the age of 60, Otaki Masayuki produced an extraordinary quantity of research. I would like to speak specifically about the idiosyncratic but extremely important theoretical research which he accomplished in the very final stage of his life. I feel that this research is a fitting way to sum up Otaki's life as a scholar.

I would like to begin this outline of Otaki's achievements by explaining an idea put forward by the historian of science Thomas Kuhn. As many of you will know, Kuhn formulated the concept of the "paradigm," which refers to a theory that is dominant within a certain academic discipline. A "paradigm shift" occurs when a dominant theory changes over time, in most cases radically. Kuhn's idea is that the evolution of scholarship, regardless of the discipline, comes about not as new theories accumulate on top of old ones, but rather as old theories are utterly discarded and new ones are accepted into the mainstream. Kuhn says that such shifts, whether large or small, have taken place in every discipline.

Let us use archeology as an example. In the mid-nineteenth century Charles Darwin put forward a completely new theory that fundamentally altered the ideas that had dominated archeology up to that point. Pre-Darwin theories were discarded and, as is well known, Darwin's theory of evolution greatly advanced the study of archeology thereafter. If we apply this same frame to the field of economics, it is undoubtedly John Maynard Keynes who played a role equivalent to Darwin. With the release of his *General Theory of Employment, Interest and Money* in 1936, Keynes completely overturned the neoclassical approach that dominated the discipline of economics at the time. Keynes' new theory utterly transformed the approach to economics, and especially macroeconomics, and furnished new policy tools, for example, to governments struggling to tackle a grave poverty crisis. Today it is impossible to talk about the economy without invoking Keynes' ideas.

I have brought up this general pattern of the advancement of scholarship because I believe that the theories put forward by Otaki Masayuki are capable of causing a paradigm shift in macroeconomics. Looking at the recent state of the economy, especially in the field known as macroeconomics, in Japan we see a protracted economic downturn and a series of recovery policies instituted by the Bank of Japan, specifically efforts to raise the rate of increase in money supply in order to lift price levels. In spite of these efforts, however, Japan has not experienced the kind of recovery that was hoped for. There has been no increase in price levels, which have remained virtually stagnant over a long period of time, regardless of the major increases in money supply made by the Bank of Japan. In other words, the relationship between changes in the real economy and changes in price levels are completely different from the relationship based on the quantity theory of money that has constituted the mainstream of economic thought. Despite this fact, however, there has been essentially no major change in the Bank of Japan's policy approach since around the year

2000. In fact it is fair to say that this approach is a faithful application to the Japanese context of the new type of quantity theory put forward by Robert Lucas Jr. in the 1970s.

It is worth mentioning that Otaki's own teacher, Uzawa Hirofumi, had been critical of Lucas' quantity theory of money and endeavored to expose the flaws in its theoretical coherence, but ultimately failed to do so. Uzawa was a theoretical economist well-known throughout the world for his contributions to the development of a variety of new models from the 1950s through to the 70s. Uzawa worked to develop and advance neoclassical macro-models, but above all his major challenge was to present the world with a new model formulated independently. When the new neoclassical macro-model, including Lucas' quantity theory of money, was created and gained currency, Uzawa saw it as his role to critique this Lucas Model and build a new alternative. In university classrooms and in his office at the Research Institute of Capital Formation, Uzawa presented us with his attempts at such a critique on many occasions. Ultimately, however, he did not succeed. "It seems that Lucas is right after all": these words we heard Uzawa utter on several occasions as his attempts drew to an end.

Otaki Masayuki, however, persisted with the attempts begun by Uzawa, and finally succeeded in developing a new Lucas critique model. It is clear that this critique was also directed to the financial policies advanced by the Bank of Japan from the 1990s onward. This is most vividly demonstrated by his final book, *Speculative Bubbles and Monetary Policy*. He used a relatively uncomplicated dynamic macroeconomic model in this book and, I believe, succeeded in formulating a framework that offers an integrated account of the ostensibly contradictory relationship I mentioned earlier, whereby price levels fail to rise and real GDP growth remains low despite increases in money supply.

Otaki makes use of a macro-model that is comparatively simple to comprehend, but also incorporates the orthodox quantity theory of money outlined by Lucas. At the same time, however, Otaki shows the difficulty of achieving the conditions demanded for the quantity theory to work in

practice, and argues that what prevails generally is an anti-quantity theory of money; in other words, the Keynesian model of rational expectation. The macro-economic equilibrium is unstable, and while in some cases price levels will rise limitlessly, in others they will stagnate. The results derived from this Otaki model have the potential to explain the situation that has confronted the Japanese economy for so long, whereby prices fail to rise despite additional monetary supply. I believe that this achievement is worthy of being called a paradigm shift.

Otaki's scholarly achievement is not adequately known among general audiences at this stage. It is my belief, however, that it will eventually gain widespread recognition and enter the mainstream of macroeconomics in Japan. I also suspect that in the not too distant future it will attract much support from experts outside Japan. In this way, I feel that the work which Otaki devoted himself to in the final stage of his life will come to be accepted as the new paradigm. Otaki accomplished that which Uzawa Hirofumi had pursued for so many years but ultimately was unable to achieve.

As something of an aside, I would like to mention that at the end of last year, I had the opportunity, together with Hanazaki Masaharu who is also present today, to attend a dinner with the CEO of a certain financial institution. In the course of our conversation I mentioned Otaki's new book that would shortly be released, and suggested that the model it explained would be extremely useful in understanding the conditions prevailing in Japan recently. I naturally had no idea that Otaki would be leaving us so soon, and thought as a matter of course that Otaki himself would be around to receive feedback on the book and apply himself to further advancement of his discipline. In this sense I feel the passing of Otaki with particular sorrow. I was able to see him just one week before his death, and at that time he was in relatively good spirits, commenting that he would like to be able to finish off one remaining task at least. I suspect that the task he was referring to was that of presenting his great achievement to the world and seeing the response.

In this sense, I believe that it now falls to us to complete the task of demonstrating to the world

the true value of Otaki's scholarly accomplishment – the new macroeconomic model he created – and achieving a paradigm shift in macroeconomics. I therefore conclude by expressing my sincere hope that all of you here today, especially scholars of a younger age, will apply yourselves to further development of Otaki's work.



# Revisiting the “Otaki Model”

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## 1. Introduction

The “Otaki Model” was completed by Professor Otaki Masayuki in the recent years and used by him as the basis for discussing macroeconomics. This article addresses: (1) the implications of the model and (2) the changes in its assumptions. The context for the article is as follows. While the basic framework of the Otaki Model remained unchanged, as time passed, Otaki himself manifestly adjusted the model’s assumptions and his account of its implications. This point will be well understood by readers familiar with Otaki’s books and articles. Those coming to Otaki’s work for the first time, however, may well feel confused by the changes in assumptions and explanatory approach, and not fully appreciate the intent and significance of the Otaki Model. It is this concern which served as my motivation for penning this article.

## 2. What the Otaki Model Demonstrates

I believe that the most important theme for Professor Otaki over the course of his career was the expression of Keynesian economics using a

dynamic general equilibrium model. The model that he produced was first unveiled in its entirety in Otaki (2007). A Japanese-language explanation of this Otaki Model was provided in Otaki (ed., 2008). Subsequently, Otaki (2011a) and Otaki (2012) employed slightly different assumptions, and this led to new commentary on the Otaki Model from somewhat different angles, which were reflected in the Japanese works Otaki (2011b) and Otaki (2013). Otaki (2015) is thus a solidly-built and extremely dense volume that could be called Otaki’s most important work. Chapter 2 of this volume contains the consummate explanation of the Otaki Model. In this article I refer to the model in the period from 2007 to 2010 as the Early Otaki Model, and that from 2011 to 2018 as the Late Otaki Model.

In broad terms, the model revealed the following three things:

- ✓ The effectiveness of fiscal and monetary policy
- ✓ The non-neutrality of money
- ✓ Imperfect competition and price rigidity are not the core of Keynesian economics.

I discuss each one of these below, with a focus on how they are related to changes in the assumptions employed by Otaki.

### 2-1. The effectiveness of fiscal and monetary policy

Mankiw (1988) and Reinhorn (1998) are among authors prior to Otaki who expressed the general equilibrium model using the Keynesian Cross. They showed that under imperfect competition, fiscal policy could generate a multiplier effect, but economic welfare would decline. The multiplier effect mechanism was presented in these papers as follows:

Fiscal policy

→ Increase in company profits → Increase in personal income → Increase in personal consumption

→ Increase in company profits → Increase in personal income → Increase in personal consumption

→ ... cycle continues indefinitely

Note that imperfect competition is important in this mechanism in the sense that it guarantees the existence of positive profit.

In contrast, the Otaki Model added to imperfect competition the assumptions of money (employing the Overlapping Generation Model, OLG) and indivisible labor. With these assumptions, fiscal policy generates a multiplier effect but also increases economic welfare. To be more precise, the conclusion of Otaki (2007) is that fiscal policy financed by issuing money yields a multiplier effect, and economic welfare will improve even if fiscal expenditure does not provide direct utility. In other words, the model shows the effectiveness of fiscal and monetary policy.

To shed light on another assumption that plays a decisive role in yielding this result, let us look more closely at one part of the construction of the Otaki Model. The firm's profit maximization problem leads to:

$$p_t = \frac{W^R}{1 - \eta^{-1}}$$

Here  $p_t$  represents prices in period  $t$ ,  $W^R$  is reservation wage, and  $\eta$  the parameter. This can be regarded as markup principle. The reservation wage is determined by the labor supply of consumers and, hence, current and future price. So it can be transformed into:

$$P_t = \left( \frac{A^{-1}\beta}{1 - \eta^{-1}} \right)^{\frac{1}{1-\alpha}} P_{t+1}$$

Here  $A$  and  $\alpha$  are parameters,  $P^t$  is current price level,  $P_{t+1}$  is the future price level. From this it can be said that the inflation rate is determined solely on the real side. But however much the inflation rate is fixed, actual price levels remain unfixed. Generally, the problem of multiple equilibria is known to arise with the OLG model, and this indeterminacy of price levels can be seen as another part of the OLG model's distinct multiple equilibria problem. To determine prices within the model, it is necessary to add other assumptions: in prior research, these assumptions included end point conditions and "not insignificant" interest rates.

The Early Otaki Model addresses the problem of multiple equilibria by implicitly adding the assumption: **"If government can arbitrarily control the real money balance ( $m_{t+1} = \frac{M_t}{P_t}$ ) in**

**the current period."** Here,  $m_{t+1}$  is real money balance,  $M_t$  is money supply. Equation (15) in Otaki (2007) describes the multiplier effect as follows:

$$\frac{Y_t}{P_t} = \alpha \frac{Y_t}{P_t} + \rho m_{t+1}$$

Here,  $Y_t$  is output. We can see that real money balance affects  $Y^d$  through the multiplier effect. It is still undetermined, however, whether the government can control  $m_{t+1}$  or not. This is because the policy variable is not  $m_{t+1}$  but  $M_t$ .

Professor Otaki seems to have recognized that it is an assumption, and an additional assumption (one example is the assumption above) is required to solve the model.

Is this an appropriate assumption? Perhaps Otaki himself was not convinced. In fact the Early Otaki Model does not highlight this assumption, but rather emphasizes the points of divergence from the aforementioned work of Mankiw (1988), Reinhorn (1998) and others, and its success in expressing the multiplier effect.

## 2-2. The non-neutrality of money

In his search for a more appropriate assumption, Otaki set his sights on the formation of expectation. While the assumption of the Early Otaki Model was that government can arbitrarily control the real money balance ( $M_t/P_t$ ), in the Late Otaki Model from 2011 this was changed to **people have the expectation that money supply ( $M_t$ ) will not influence prices ( $P_t$ )**. Under this assumption, which Otaki calls the **"credibility of money,"** the expectation is self-realizing and money supply does not influence prices (= **the non-neutrality of money**), so the government can choose the real money balance ( $\frac{M_t}{P_t}$ ) arbitrarily. This assumption has essentially the same effect as the Early Otaki Model assumption, so the conclusion is identical.

In other words, the post-2011 Late Otaki Model changes the assumption to "the credibility of money." There is no change whatsoever in the conclusions produced by the model. The emphasis, however, is different. The new assumption, that people trust money, is at the heart of Keynesian economics. This was Otaki's key argument.

To summarize, the Late Otaki Model lays empha-

sis on the following points:

- ✓ Fiscal policy financed by the issuing of money improves economic welfare even if not directly for the utility of consumers.
- ✓ The assumption used to deal with the existence of multiple equilibria, i.e., the expectation that the value of money is credible (which leads to the non-neutrality of money), is at the core of Keynesian economics.

In order to test whether the latter assumption is one that is generally “usable,” Otaki (2012) explored what happens if the assumption of the credibility of money is applied to the Lucas (1972) model of the neutrality of money. The result, that money loses its neutrality even under the Lucas model, successfully shows that the assumption of credibility of money is a generally applicable concept that functions even in other models.

### **2-3. Imperfect competition and price rigidity are not the core of Keynesian economics**

Otaki (2015) looks at what happens when people have expectations other than the credibility of money, revealing that:

- ✓ Under the “credibility of money” expectation, the theory of non-neutrality of money and effective demand (multiplier effect and Keynesian cross) holds true
- ✓ Under the “quantity theory of money” expectation, the neutrality of money holds true.

Otaki (2011b), meanwhile, shows that the same conclusions are valid in conditions of perfect competition (except that economic welfare differs). In other words, it cannot be determined whether a Keynesian equilibrium or a neoclassical equilibrium will be reached, regardless of whether competition is perfect or imperfect. On the other hand, fixing the expectation will determine which of the two equilibria is reached. In this sense, Otaki argues, the core of Keynesian economics does not lie in imperfect competition or price rigidity.

### **3. Conclusion**

The Early (2007-2010) and Late (2011-2018) Otaki Models have the same conclusions, but place emphasis on different facets. The Early Otaki

Model (2007-2010) emphasizes the effectiveness of fiscal and monetary policy, while the Late Otaki Model (2011-2018) highlights the “credibility of money” and the “non-neutrality of money.” This is because Otaki altered his assumptions to address the problem of multiple equilibria.

The most concise explanation of the Late Otaki Model can be found in Chapter 2 of Otaki (2015).

Finally I would like to look beyond the content of Professor Otaki’s research, and comment on his approach as a researcher. The Professor was my supervisor in graduate school. At that time, the Otaki Model was on the verge of completion, and I was fortunate to be able to watch the completion process at close quarters. What impressed me most was Otaki’s tenacious attitude to his work, which demonstrated an astonishing and unparalleled degree of enthusiasm and sincerity toward his own critical consciousness as a scholar. He was unwavering in his pursuit of the ambitious goal of adding microeconomic foundations to Keynesian economics, continuing to tackle it head-on even as he struggled with ill health. He was a truly “fighting” scholar. To engage sincerely and unremittingly with the problems that you consider to be most important: this, alongside the Otaki Model itself, was the greatest thing that I learned from Professor Otaki.

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# Global Warming and Intergenerational Concerns: Masayuki Otaki's Contribution to Environmental Economics

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## 1. Introduction

Apart from his pioneering work in macroeconomics, since the turn of the last century, Masayuki Otaki has shown a great interest in advancing environmental economics, especially in the field of global warming—a truly distinct environmental problem, encompassing many generations to come. One of his earliest contributions to environmental economics is found in [1], where he addressed the commons, or social common capital. There, he stressed that it is extremely difficult to manage the commons soundly when it is affected by intergenerational negative externalities. It is virtually impossible for later generations to protest earlier generations because later generations do not exist when negative externalities are created. Thus, environmental problems such as accumulation of CO<sub>2</sub> in the atmosphere have an inherently dynamic nature, posing an extremely baffling question to humankind.

## 2. Social Discount Rate and Carbon Tax

In combatting an intergenerational externality problem, a research agenda on how to weigh each

generation in the consumption-utility stream inevitably arises. Under the constraint of sustainability, which was proposed by Pezzey [2] and others, Otaki showed in [3] that “the weight of each generation’s utility in the social welfare function should be allotted equally in a planning economy” [3, p.4] on a stationary state path. Applying the setting of optimal growth theory, he articulated that the imposition of a zero discount rate on the generations’ utilities over time in a planning economy is equivalent to the situation where an optimal carbon tax is fully imposed in a decentralized market economy. This equivalence is an application of Negishi’s theorem [4]. Conversely, if a positive discount rate is applied to a stationary planning economy, it means the imposed carbon tax is lower than the optimal carbon tax rate in the market economy. Thus, imposition of an optimal carbon tax rate under the stationary economy allows for a desirable social decision when we apply a zero rate of discount. These arguments enrich the discussion of discount rates in a stationary economy.

As we have seen in the discussion of the commons, it is extremely difficult for a generation to deal with the CO<sub>2</sub> problem since it is intrinsically a dynamic problem. We humans live for only one generation whereas the CO<sub>2</sub> problem lingers over many generations. Is there a solution to tackle this problem? To give a constructive answer to this problem, Otaki makes the following suggestion in [5]. If each generation altruistically cares just about the subsequent generation’s welfare, and this kind of behavior, called parentage, is repeatedly applied to bridge the generations, it leads to the optimal solution. Here, “parentage is defined as the action of applying zero social discount rate to its subsequent generation, and discounting the utility of generations thereafter infinitely” [5 p. 433]. With this kind of behavior under a stationary state, it is possible to reach the first best solution.

In optimal growth theory, the Ramsey rule is well known. To find an appropriate relationship

between the rate of time preference and the real interest rate, this rule has been used extensively (See [6]). The ordinary Ramsey rule, however, does not consider the existence of negative externalities in its formulation, which causes us to adopt a modified Ramsey rule to find the following proper relationship among the endogenous variables and parameters [7]:

$$\rho = r_t - \psi^* \pi_t - \eta \frac{\dot{c}_t}{c_t},$$

where  $\rho$  is the rate of time preference,  $r_t$  is the real interest rate,  $\psi^*$  is the optimal carbon tax rate,  $\pi_t$  is income per capital,  $\eta$  is the elasticity of marginal utility, and  $\frac{\dot{c}_t}{c_t}$  is the increased rate of consumption.

With this new formula, the social rate of return of capital accumulation stays lower than the real interest rate because the former rate takes the negative externality into account in the production function. In addition, the rate of time preference is lower than the real interest rate in the stationary state where the growth rate of consumption is zero. The article also indicates that the real causality in the Ramsey rule stems from  $\rho$  and  $r_t$ , which results in  $\frac{\dot{c}_t}{c_t}$ , not vice versa. This has been sometimes overlooked in the interpretation of the Ramsey rule in environmental economics. The article also states the usual application of the rule often implicitly presumes the existence of exogenous, autonomous technological improvement.

The next article calculates the carbon tax rate from a modified Ramsey rule for the case of a stationary economy in the following expression [8]:

$$p = \frac{1}{\beta(\alpha + \rho)},$$

where  $p$  is the optimal carbon price in terms of unit emissions reducing cost,  $\alpha$  is the absorption ratio of CO<sub>2</sub> by the Earth,  $\beta$  is the efficiency of production measured by the amount of production (consumption) that can be produced by unit emissions, and  $\rho$  is the rate of time preference. In [7], negative externality is introduced in the production function. In [9], he checked if the difference occurs where the negative externality arises in the production or consumption side. Negative externalities on the consumption side, such as abrupt changes in the environment that directly influence

people's living standard, postulate a direct effect on utility. It has been shown that in the neighborhood of the stationary state, either approach to incorporating the externality is proven to provide the same level of optimal carbon price. In this environment, as the social discount rate approaches zero in the neighborhood of the stationary state, resource allocation improves accordingly because lower discount rates extend the scope of future considerations. Lower discount rates also increase the carbon price.

### 3. Offset Trading: An Alternative Environmental Instrument

Devising a simplified but sufficiently elaborated model where there are  $n$ -paired two country economies, [10] calculates the optimal offset prices for emissions trading between two countries – advanced and developing countries – and also obtains the optimal rate of carbon tax in the world, which is Pareto efficient and higher than the offset price. Here two things are emphasized. First, a worldwide carbon tax system is superior to other systems. Its realization, however, is rather difficult because of its relatively high rates and the corresponding obstacle of international income redistribution. Therefore, instead of arguing for the adoption of a universal carbon tax in a non-cooperative context, it is more realistic to seek the adoption of some type of emissions trading scheme. Second, the diffusion of emissions-saving technologies such as energy-saving investments will lead to the softening of carbon prices, which will affect the increase of CO<sub>2</sub> emissions. Such general equilibrium effects are hard to ignore, and the diffusion of energy-saving technologies is not enough to overcome the release of CO<sub>2</sub> emissions.

With the same setup as [10], [11] provides one piece of a rationale for the Clean Development Mechanism. That is, corporations in advanced countries make direct investments in developed countries and acquire the revenue from the investment, deducting the payment of the emissions trading scheme. The paper shows theoretically how the CDM functions in depressing the emissions of CO<sub>2</sub> in a second-best way. At the same time, offset mechanisms such as the CDM, having a redistributive effect on income, do not work self-reliantly, and need outside institutions such as governments to operate effectively in the market.

#### 4. Concluding Remarks

Masayuki Otaki's passionate concerns about the environment, especially global warming, appear throughout his papers. His deep understanding about optimal growth theory enriches discussions on discount rates of utility in an intergenerational setting and related rates of optimal carbon tax, especially in stationary states. Both modification of the Ramsey rule and a proposal of "parentage" give a hint as to how to tackle the intergenerational difficulty of CO<sub>2</sub> accumulation and increase the intellectual knowledge necessary to counter global warming. In addition, his theoretical treatment of offset mechanisms, exemplified by the Clean Development Mechanism, provides us with another practical environmental instrument against global warming. One of the remaining agenda items will be to study the transition process leading to the stationary state. Since such "an analysis is beyond analytical procedure," meaningful "numerical analysis or simulation" backed by theoretical foundation is envisaged [3 p.6]. Otaki's sudden passing has left us with a theoretical "arsenal" to fight against global warming, but we will also greatly miss his unfinished contributions since he passed away before compiling them from an original viewpoint.

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# Challenges of Professor Masayuki Otaki

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Professor Masayuki Otaki passed away on July 2<sup>nd</sup>, 2018 at the age of 60. He was an outstanding macroeconomist working on monetary economics, growth theory, labor economics, and environmental economics. He also had done much work on environmental economics. His deep understanding of economic theory was rooted in his strong interest in the history of economic thought and political philosophy. This is a brief bibliographical essay.

## 1. Early days

Professor Otaki was born in Iwaki, Fukushima prefecture in 1957. After graduation from Iwaki High School, he entered the University of Tokyo. He spent fruitful days on the Komaba Campus reading the classic novels of Soseki Natsume, Ogai Mori, Ryunosuke Akutagawa, Kazumi Takahashi, and others and then joined the Hongo Campus and started studying economics under Hirofumi Uzawa, who was a giant in the field of economic growth and general equilibrium theory. A pioneering work by Lucas (1972) was an assignment in the first year of Uzawa's lecture course, and he

started to read Keynes's *General Theory*. Later, these two works, which represent different intellectual traditions, became his academic foundation.

In 1981, he joined the Graduate School of Economics at the University of Tokyo. Otaki (1996) admitted that he struggled with developing his own new ideas on macroeconomics in this period, not just in the graduate school. He spent a period of time in the Research Institute of Capital Formation in the Japan Development Bank as a research fellow. He received helpful advice and experiences from people in the institute, and Professor Akiyoshi Horiuchi was an important influence on him in this period (Otaki, 1996).

In 1986, Kanagawa University hired Otaki as an associate professor. He often held long discussions with his colleague, Professor Yosuke Mamiya, an expert on the history of economic thought, especially the ideas of J.M. Keynes and F.A. Hayek. Professor Otaki then moved to Aoyama Gakuin University in 1991. In the Kanagawa-Aoyama period, he began constructing his unique models of dynamic macroeconomics.

With Professor Kyoji Fukao of Hitotsubashi University he wrote a distinguished early paper "Accumulation of Human Capital and the Business Cycle" (Fukao and Otaki, 1994). The paper was based on an earlier paper (Otaki, 1988), which examined the kinked adjustment cost of employment. By introducing training costs in a general equilibrium model with a representative household, Fukao and Otaki (1994) showed that a continuum of equilibria exists with the Japanese type as one special case and the US type as another special case. This work is regarded as a theoretical foundation of new institutional economics or modern comparative institutional analysis.

Professor Otaki next published *Theory of Business Cycles: A Structural Analysis of the Contemporary Japanese Economy* (Otaki, 1994, 『景気循環の理論』)

in Japanese) in which he put his paper with Professor Fukao at its core. *Theory of Business Cycles* is an elegant combination of his theoretical thought and practical treatments of the Japanese economy. It pioneers mathematical formulations of path dependency (or hysteresis), which is the central concept of a modern economic history (North, 1990). Indeed, he could show a non-ergodic property of equilibria in the presence of sunk or adjustment costs. This book received the Nikkei Economics Books Cultural Award.

## 2. A Shift to Monetary Economics

In 1996, Professor Otaki joined the Institute of Social Science at the University of Tokyo as an associate professor (in 2001, he became a full professor) and started a new fruitful endeavor in his academic career. After accomplishing his elegant work on a dynamic general equilibrium model with a representative agent, he shifted his interest to monetary theory. To examine the role of money, he introduced heterogeneous agents. Although there are many ways to introduce heterogeneity, he believed in the relevance of an overlapping generation model (OLG model). Indeed, his starting point of this was Lucas's (1972) work on the neutrality of money, which is based on an OLG model.

From the mid-2000s, Professor Otaki started publishing works on monetary theory. For example, in Otaki (2007, 2009), he demonstrated Keynesian policy implications from an extended OLG model with indivisible labor. His main finding is an equation that describes a movement of prices (we call it *Otaki's fundamental equation of money*), i.e., the relationship between  $p_t$  and  $p_{t+1}$  is given by:

$$p_t = \frac{W(p_t, p_{t+1})}{\gamma}$$

Here,  $\gamma$  is the productivity of labor and  $W$  is the wage level, which is dependent on current and future prices. Given this equation, we can see that the determination of prices is independent of the quantity of money.

He synthesized his works on money in *Keynesian Economics and Price Theory: Re-orientation of a Theory of Monetary Economy* (Otaki, 2015). In this book, he introduced the concept of the "credibility" or

"confidence" of money. Money is said to be confident if "individuals believe in the future intrinsic value of money, and rationally anticipate that the future value of money will not be affected by monetary policy" (Otaki, 2015, p. 20). Assuming credibility, Otaki argued how Keynesian policies can improve the functioning of an economy and social welfare. The point of his result is a multiplicity of equilibria. According to Professor Otaki, Lucas's neutrality result is an extreme case in his set of equilibria: neutrality happens only when there is no credibility of money and people have a certain type of belief. Further, Professor Otaki argued that, although equilibrium with neutrality is technically possible, credibility is a natural presumption of human nature. We believe in the non-neutrality of money in our real lives.

## 3. Welfarism and Liberalism

Professor Otaki had a deep interest in the history of economic thought. He did not publish a monograph on the subject as a sole author, but he edited several books on political philosophy and economic thought (see, for example, Uno, Otaki, and Cato (2015)). Thus, we can understand his basic ideas from pieces of his work.<sup>1</sup>

First, he believed in welfarism, a weak form of utilitarianism (Professor Otaki did not distinguish welfarism and utilitarianism, but I follow the usual distinction in political philosophy here). He criticized modern political philosophers, such as John Rawls and Michael Sandel, based on his own reinterpretation of the writings of Edmund Burke and G.E. Moore (Uno, Otaki, and Cato, 2015). According to Professor Otaki, each individual develops his/her own goodness alongside his/her own particular life and, thus, the nature of goodness is path dependent. Because of this developing process, each individual changes all the time and makes many mistakes. In this sense, human beings are vulnerable. One way to protect people is employing the Paretian approach, which does not allow for interpersonal comparability of individual well-being. Under this approach, the government or any other agents cannot intervene in individual values. For Professor Otaki, path dependency serves as a justification of the Paretian approach.

<sup>1</sup> In the following two paragraphs, I incorporate personal conversation with Professor Otaki along with Chapter 5 of Uno, Otaki, and Cato (2015).

Second, related to the first point, Professor Otaki emphasized the importance of liberalism. The fundamental value of liberalism is the freedom of individuals. He argued that a basic conception of the Paretian approach is “humanism” because all agents, including natural persons, corporations, and the government, must respect each human being’s own values, and any activity undermining the values is not allowed under this approach,<sup>2</sup> which also means that each human has a certain set of freedoms. For Professor Otaki, however, this is totally different from the idea of neo-liberalism: a society must be liberal in the sense that each person can pursue his/her own goodness *as long as* his action is consistent with social existence. He considered that this is a consequence of welfarism or the Paretian principle (Uno, Otaki, and Cato, 2015).

#### 4. Final Remark

In May of 2018, Professor Otaki gave his last presentation in a University of Tokyo ISS seminar. It was a summary of his several works on reinterpreting *The General Theory*. He tried to understand Chapters 1-3 by using a simple extension of the golden cross of demand-supply. According to Otaki (2018) in this Newsletter, “Keynes does not abandon the second postulate of classical economics but extends it” (p. 21). This was a quite new understanding of the meaning of Keynes’s revolution<sup>3</sup>. His idea was amazingly simple because he based his entire argument on a static model. He also showed a fundamental problem of the standard model of investment that Uzawa (1969) developed.

His academic achievements can be understood as challenges to the three giants of economics in the 20<sup>th</sup> century: Keynes, Uzawa, and Lucas. Through these challenges, Professor Otaki had many new ideas and perspectives. Almost 90 years ago, Keynes wrote the following remarks at the end of *The General Theory*:

“if the ideas are correct...it would be a mistake, I predict, to dispute their potency over a period of time....the ideas of economists and political philosophers, both when they are

right and when they are wrong, are more powerful than is commonly understood. Indeed the world is ruled by little else. Practical men, who believe themselves to be quite exempt from any intellectual influences, are usually the slaves of some defunct economist. Madmen in authority, who hear voices in the air, are distilling their frenzy from some academic scribbler of a few years back. I am sure that the power of vested interests is vastly exaggerated compared with the gradual encroachment of ideas. Not, indeed, immediately, but after a certain interval; for in the field of economic and political philosophy there are not many who are influenced by new theories after they are twenty-five or thirty years of age, so that the ideas which civil servants and politicians and even agitators apply to current events are not likely to be the newest. But, soon or late, it is ideas, not vested interests, which are dangerous for good or evil.” (Keynes, 1936, pp 383-384)

Professor Otaki believed in the importance and power of economic theories and he repeatedly encouraged us to work on new theories and ideas. What I believe is that theories and ideas are necessary for making social progress and moving toward a better society, and Professor Otaki’s challenges give us one such idea.

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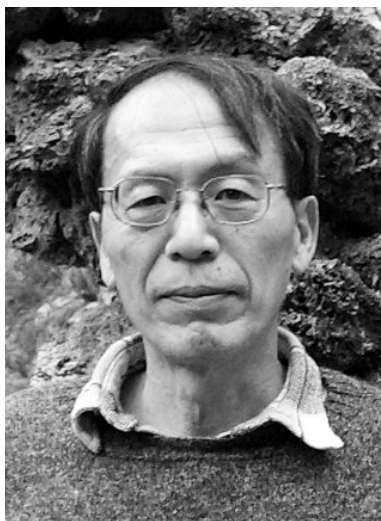
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# Mathematics and Humanities

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### 1

Because our specializations differed, Professor Otaki and I almost never locked horns over individual topics that he was researching in areas such as economic theory, fiscal policy, and environmental economics. Nonetheless, over a period of 30 or more years, I met with him frequently and greatly enjoyed our discussions. Especially at his first place of employment, Kanagawa University, where I was also based, we used to meet for a drink at a pub near the campus almost every day, and I would lend an ear to his concerns in both research and life in general.

Although we were both economists, Otaki employed the techniques of quantitative economics to explore economic theories and realities, while I examined the genesis and evolution of politics, economics, and society through the ideas of various great thinkers. Put simply, Otaki inhabited a world of mathematics, while my domain was in the world of humanities. There were virtually no points of contact between these two worlds, and naturally our two names never appeared in the same magazines or books. In the

last five years of Otaki's life, however, our names did at last coincide in no fewer than four such publications. This was nothing short of a miracle; some act of providence. It was as if the gods had foreseen his death, and arranged a last-minute snapshot of the two of us.

The publications to which I refer are as follows, in chronological order:

(1) Horiuchi Kozo, Uchida Katsuhisa, Yosuke Mamiya, eds. 2014. *Nihon Keizai: Shakaiteki kyōtsū shihon to jizokuteki hatten* (The Japanese Economy: Social common capital and sustainable growth). University of Tokyo Press.

Kuninori Morio & Otaki Masayuki, "Kōkatekina Nisankatanso Haishutsu Seigyō" (Effective Control of Carbon Dioxide Emissions)

Mamiya Yosuke, "Gyojō no Kyōdō Riyō to Jichiteki Kanri" (Communal Use and Autonomous Management of Fisheries)

(2) *Gendai Shisō* (Uzawa Hirofumi special issue, February 2015)

Otaki Masayuki, "Uzawa Hirofumi Sensei to Keinzū Keizaigaku" (Uzawa Hirofumi and Keynesian Economics)

Mamiya Yosuke, "Shakaiteki Kyōtsū Shihon no Shisō" (The Idea of Social Common Capital)

(3) Otaki Masayuki, Uno Shigeki, Kato Susumu, eds. 2015. *Shakai Kagaku ni okeru Zen to Seigi* (Good and Justice in the Social Sciences). University of Tokyo Press.

Otaki Masayuki, "Riron Keizaigaku ni okeru Zen to Seigi: Kojin to shakai no sōgo sayō" (Good and Justice in Theoretical Economics: Interplay of Individual and Society)

Mamiya Yosuke, "Bunkatsu no Seigi to Fuseigi" (Justice and Injustice of Segmentation)

(4) *Social Science Japan Newsletter* No.58 (March 2018)

Otaki Masayuki, "Has the Second Postulate of Classical Economics Been Abandoned or Extended?"

Mamiya Yosuke, "The Ideological Background of Keynesian Economics"

Some of the publications listed above are designed for general readers rather than experts. The magazine *Gendai Shisō* (number 2 above), for example, is well-known for introducing the latest trends in scholarly thought, and enjoys a wide readership among students and working adults. The issue mentioned above was a special memorial issue for the world-renowned economist Uzawa Hirofumi, who had passed away in September of the previous year. It comprised essays by a variety of people associated with Uzawa, not all of whom specialized in economics. Otaki allowed me to read his manuscript before it was sent off for publication, and I was surprised to find that it contained a highly comprehensible explanation of Uzawa's quantitative paper on "Time preference and Penrose effect in a two-class model of economic growth" from 1969. When I say comprehensible, it was of course necessary to use mathematics, and I do not think there has been an article in *Gendai Shisō* before or since which contains differential equations. But looking at the article in its published form, there is no sense of incongruity. It is a prosaic essay backed by a solid mathematical edifice, conveying the distinctive style of Uzawa's own work.

What impressed me even more was Otaki's interpretation of Keynes in the fourth item on the above list. In Keynes' discussion of involuntary unemployment in the second chapter of *The General Theory of Employment, Interest and Money*, there is a section that perplexes many readers. It is the definition of involuntary unemployment, which reads: "Men are involuntarily unemployed if, in the event of a small rise in the price of wage-goods relatively to the money-wage, both the aggregate supply of labour willing to work for the current money-wage and the aggregate demand for it at that wage would be greater than the existing volume of employment."

Rational workers, as envisaged by economics, would surely reduce their supply of labour if the real wage decreases. According to Keynes, however, when workers are in a state of involuntary unemployment, their supply of labor actually increases if the real wage is lowered. Keynes asserts that this is what occurs in reality. It is here that the reality of labor and the mathematical

theory of economics come into conflict. Otaki's means of resolving this conflict was to eliminate it, by expanding the mathematical theory in line with reality.

If the money wage is  $w$ , the price level  $p$ , labor quantity  $N$ , and the function of disutility of labor  $\psi(N)$ , then the usual labor supply curve would be expressed as  $(N, w/p)$  satisfying  $w/p = d\psi(N)/dN$ ; that is, real wage = marginal disutility of labor. According to Otaki, however, real wage and labor supply do not correspond value-to-value. Any marginal disutility of labor is tolerated, provided it is lower than the prescribed real wage. Economics has traditionally taken labor supply as the maximum volume at that point, but in Otaki's account, where real wage is  $w/p$ , labor supply is an aggregate determined by  $\Omega(w/p) = \{N \mid w/p \geq d\psi(N)/dN\}$ . In other words, Otaki expanded labor supply from a value-to-value function into a value-to-set correspondence, thereby furnishing a graceful mathematical expression of Keynes' definition of involuntary employment.

## 3

Otaki was also well-versed in literature and philosophical thought. As a young scholar, he published a magazine essay under the title of "My Heart is Not Made of Stone." This title was taken from the novel by Takahashi Kazumi which had sent many young people, myself included, into a frenzy at the time. When I saw the essay, I was deeply impressed to learn that Otaki had read the novel as well. In the fourth publication listed earlier, Otaki built on works such as G.E. Moore's *Principia Ethica* and Hanna Arendt's *The Human Condition* in his discussion of the meanings of "good" and "justice" in economics. If Otaki's outer appearance was that of a theoretical economist, inwardly he was a moral philosopher who enjoyed exploring ideas and novels.

When I look back on Otaki's scholarly career, one that was brought to a premature end by his death, I cannot help but think of the short story *Meijinden* (The Legend of the Great Master) by Nakajima Atsushi.

---- Long ago in a certain city in China, there was a young man who had no equal as an archer. This archer could unfailingly pierce the heart of a

louse bound up in hair, yet he still felt something was missing. The archer hid himself away in the mountains to train with an old hermit who had developed the art of shooting without shooting (in other words, the ability to shoot animals and birds without even using a bow and arrow). After nine years the archer had mastered this art and returned to his home town. Hearing the rumors about his training, people gathered around and implored him to demonstrate his wondrous skill. But the archer had forgotten about the very existence of the object he once called a bow, let alone how to use one.

The bow for Otaki was mathematics. Just as that young archer in ancient China had full mastery over his bow, Otaki displayed a complete command of mathematics in his specialized academic papers. But for him that was not sufficient, and he began roving through the forest of the humanities. We do not know whether or not, like the archer, he ultimately lost sight of the very existence of mathematics. But if he had been allowed just ten more years on this earth, he may well have crafted a new form of harmony between mathematics and humanities.

# Prof. Otaki as a Humanitarian – Law and International Relations

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## Preface

In his book *Fundamentals of the Theory of Money and Employment* (Otaki 2011), Professor Otaki described the humanitarian character of Keynes's theory. In this short essay, I will describe Otaki's humanitarianism through an analysis of his other-than-economic thoughts. As a scholar of private international law, I will particularly focus on his thoughts on law and international relations. In my understanding, Otaki based his thoughts on his exquisite recognition of the reality and possibility of human beings.

## Prof. Otaki and Law

Concerning Otaki's thoughts on law, I would like to introduce his ideas on law-making in order to describe his humanitarianism. In his discussions with me on legal issues, he often, but not always, argued against including detailed provisions in legislation simply because it is impossible for a legislator to foresee what will happen. In his opinion, judges, as artisans of the interpretation of law, are responsible for realizing the appropriate

application of laws to individual cases. Judging from my experience, the current practice of Japanese law-making—detailed and clear provisions, which are usually preferred for their predictability—is quite different from what Otaki regarded as desirable. His ideas focused on both the limited ability of legislators and trust for judges. At the same time, it seems to me, he argued that the application of excessively detailed provisions of law increased the danger of unintended consequences affecting ordinary people.

Otaki's position was compatible with Friedrich August von Hayek's idea of *nomos*, the law of liberty for the "spontaneous order." *Nomos* consists "of rules regulating the conduct of persons towards others, applicable to an unknown number of future instances and containing prohibitions delimiting the boundary of the protected domain of each person (or organized group of persons)" (Hayek 1973, p. 122). Concerning the legislation of rules relating to *nomos*, he wrote:

Although legislation can certainly increase the certainty of the law on particular points, I am now persuaded that this advantage is more than offset if its recognition leads to the requirement that only what has thus been expressed in statutes should have the force of law. It seems to me that judicial decisions may in fact be more predictable if the judge is also bound by generally held views of what is just, even when they are not supported by the letter of the law, than when he is restricted to deriving his decisions only from those among accepted beliefs which have found expression in the written law (Hayek 1973, p. 116).

Pointing out the problems of legislation, he leaves it to judges, as an organ of the "spontaneous order," to uncover the existing order and articulate and improve the rules of *nomos*. In this respect, we see similarities between Hayek and Otaki, though there may also be differences.

There is another similarity between them con-



cerning the concept of liberty. Otaki explains that, under Hayek's liberty, people need to exercise their freedom in accordance with their common sense rejecting antisocial conducts (Otaki 2018, pp. 178-179). From his perspective, the liberty is people's freedom limited by the sense of responsibility that should be shared in a society. I think liberty with a sense of responsibility is essential for Professor Otaki's humanitarianism in that he trusts that human beings, who live in society, recognize their social responsibilities. He argues for the acceptance of such a form of liberty through a "social contract." While the relationship of Hayek's "rule of law" as a meta-legal doctrine to Otaki's "social contract" should be further considered, it is certain that lawyers who take Otaki's messages seriously should pay more attention to Hayek's ideas.

### **Professor Otaki and International Relations**

Concerning international relations, it is well known that he argued against current globalization, which he called Americanization. Otaki (1996) critically noted that today's contacts between cultures are unusually frequent, and arguments supporting such contacts are an innocent form of antirealism. Otaki argued that "sufficient distance" between cultures is essential for co-existence because of the strong narcissism of human beings, echoing Claude Lévi-Strauss.

Lévi-Strauss (1962) strongly criticized the ethnocentrism of European culture in his book, *La pensée sauvage*. Concerning "sufficient distance" that Otaki mentioned, he noted in another article:

"...it is true, as the example of so-called primitive peoples teaches us, mutual tolerance presupposes two conditions that contemporary societies are farther distant than ever from experiencing: a relative equality and sufficient physical distance from one another." (Lévi-Strauss 1985, p21)

He pointed out the two conditions for a reciprocal tolerance between societies: relative equality and sufficient physical distance. He analyzed the current world of rapid transportation and communication in which the fusion of different cultures progresses:

"...I have repeatedly emphasized that the gradual fusion of groups previously sepa-

rated by geographic distance as well as by linguistic and cultural barriers has marked the end of a world: the world of human beings who, for hundreds of thousands of years, lived in small and durably separated groups, each evolving differently on both a biological and a cultural level. The upheavals unleashed by an expanding industrial civilization, and the rising speed of transportation and communication, have knocked down these barriers. At the same time, we have lost the possibilities offered by these barriers for developing and testing new genetic combinations and cultural experiences." (Lévi-Strauss 1985, p. 23)

If we recognize the current situation of information technology, it should be evident that we need to pay serious consideration to these texts. The following passage explains the difficulty – or impossibility – of maintaining a diversity of cultures and an originality of individuals in days of unusually rapid and frequent communications:

"For one cannot fully enjoy the other, identify with him, and yet at the same time remain different. When integral communication with the other is achieved completely, it sooner or later spells doom for both his and my creativity. The great creative eras were those in which communication had become adequate for mutual stimulation by remote partners, yet was not so frequent or so rapid as to endanger the indispensable obstacles between individuals and groups or to reduce them to the point where overly facile exchanges might equalize and nullify their diversity." (Lévi-Strauss 1985, p. 24)

It seems that Lévi-Strauss's words influenced Otaki's thoughts. Otaki argued for the variability of co-existing societies and against the antirealism of a coercive fusion of societies. Especially, he pointed out the necessity of keeping international society "inter-national," that is, a society of independent nations. It should be highlighted that Otaki's humanitarianism includes a positive acceptance of patriotism. He wrote, strictly distinguishing patriotism from chauvinism, that a person can be a humanistic cosmopolitan only when he/she is a patriot of his/her country. From his point of view, appropriate international relations

can be constructed only when each country is firmly established by people attached to their country. Recognizing the sensitive balance between patriotism and tolerance for other countries, he seemed to conclude that sufficient distance is necessary for international society.

In addition, if we look at Otaki's arguments on the environment, we can also find a linkage with Lévi-Strauss. Both professors held quite similar thoughts on the relationship between human beings and nature, which is clearly described by Lévi-Strauss as a basis for his humanism:

"...a wisely conceived humanism, which does not center on man but gives him a reasonable place within nature, rather than [sic] letting him make himself its master and plunderer, without regard for even the most obvious needs and interests of later generations." (Lévi-Strauss 1985, p. 14)

Otaki's humanitarianism is based on a sincere recognition of human beings and the world/nature around them. In this respect, it seems to me to coincide with the ideas of Lévi-Strauss. It can be said that Otaki's humanitarianism held a warning for current globalization.

### Conclusion

Although I am not capable of evaluating Professor Otaki's achievements in the field of economics, I believe the same humanitarianism was behind them. Reading his recently published textbook (Otaki 2018), I think it is evident that he strongly

argued, as reflected in his discussions of "homo economicus" and "artisans," for a diversity of lifestyles. It should be also noted that he loved books, such as the work of Trevelyan (1942), that had a warm and deep sympathy for ordinary people. In my understanding, he made us aware that many of our future tasks should be undertaken based on his humanitarianism. Keeping in mind our tasks, I would like to express my deepest condolences on the loss of Professor Otaki, who truly loved karaoke, artisanally produced Japanese cuisine, and his family.

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# In Memory of Professor Otaki Masayuki

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It was in July 2018 that Professor Otaki Masayuki passed away so suddenly. When I heard this news I was on foreign soil, giving lectures at the Free University of Berlin. While deeply regretting that we would never again be able to engage in conversation, as someone who had engaged with Otaki Masayuki at close quarters, I was driven to set down a few words about both his research and his character.

My research is on the history of Western political thought, and especially the 19<sup>th</sup>-century French political philosopher Alexis de Tocqueville. In that sense, I may seem to have little in common with Professor Otaki, who specialized in macroeconomics. The University of Tokyo's Institute of Social Science (ISS) is characterized by collaborations in social science research that transcend the barriers between different specializations, but I must admit to feeling rather distant from Professor Otaki's research in my early days at the ISS. For some reason, however, the Professor himself took the initiative to approach me very soon after I arrived.

One of the places I often saw the Professor at that time was in the Journal Editorial Board. The committee was undertaking a major review of the ISS's Japanese-language periodical, the *Journal of Social Science*. How could we make this bulletin into a true peer-reviewed academic journal? What steps could be taken to make its existence known to a wider readership, such as having it on sale at bookstores? It was Professor Otaki who consistently took the lead in these wide-ranging discussions about the journal's character.

Not all of the committee's ideas necessarily came to fruition, but Professor Otaki continued his efforts to reinvigorate the journal unstintingly. In the course of this work he encouraged me to plan a special issue, which was eventually published under the title of "Representation in Crisis" (Vol. 52 Issue 3, March 2001). Planning a special issue was a real challenge for a newcomer like me, but I managed it thanks to Professor Otaki's encouragement. This experience was the starting point for my research career at the ISS, and I still remember it as if it happened just yesterday.

Subsequently Professor Otaki came to me with many different proposals for joint research in the *Journal of Social Science*. One example is the project on John Rawls. As an economist, Professor Otaki had a deep interest in Rawls' work, and indeed in questions of good and justice in the social sciences generally. At the time, my own interests were expanding from the history of political thought into contemporary political philosophy, so Professor Otaki's proposal came as a godsend. The joint research culminated in a special issue of the *Journal of Social Science* titled "Good and Justice in the Social Sciences" (Volume 64 Issue 2, March 2013). Later the special issue was republished as a stand-alone volume by the University of Tokyo Press (Otaki Masayuki, Uno Shigeki, Kato Susumu, eds., *Shakai Kagaku ni okeru Zen to Seigi* [Good and Justice in the Social Sciences], May 2015).

I continued to publish joint research with Professor

Otaki in the *Journal of Social Science*, including a project on John Maynard Keynes. It was at the end of March this year that the Professor called on me again to say, "let's get together to do another interesting project soon." When I recall those words, I still find it hard to believe that he is no longer with us.

As mentioned at the outset, my initial impression was that Professor Otaki's research was rather distant from my own. But as I interacted with him, I gradually came to realize that I was mistaken in this regard. Allow me to relate one especially memorable episode. Professor Otaki and I had just boarded the same elevator in the ISS when the Professor accosted me with the question: "so, what do you think of Hannah Arendt?" Startled to hear the name of a political philosopher uttered so unexpectedly by a macroeconomist, I was incapable of answering with much adroitness. I clearly remember Professor Otaki's rejoinder: "I am very fond of her phrase, 'that a beginning be made, man was created'" This phrase, which to be accurate Arendt had borrowed from St Augustine, is today one of my personal favorites.

I also learned a great deal from the research I did with Professor Otaki on John Rawls. The point of departure for Rawls' theory of justice is a critique of utilitarianism, but the Professor had his doubts about Rawls' understanding of utilitarianism itself. Might Rawls be using utilitarianism as a straw man? Does not utilitarianism have a deeper thought? Little by little, I began to comprehend what the Professor meant when he talked of the importance of utilitarianism.

Despite being a scholar of economics, or perhaps because of it, Professor Otaki had an exceptionally well-developed sense of justice and equity. I came to appreciate that this sense was the underpinning of the Professor's research in economics. In that sense, it was naïve of me to think that macroeconomics and the history of political thought were disparate fields of research. In the Professor's mind, macroeconomics and political philosophy, or macroeconomics and the history of political thought, were extremely close neighbors. It took nearly twenty years of working with the Professor for me to grasp this fact, a delay that can only be put down to my own obtuseness. I can just imagine

the Professor smiling as he says: "Uno, you're starting to cotton on at last."

Another thing I learned from Professor Otaki was the value of reading biographies. One time when we were chatting in the Professor's office, the conversation turned to a biography of Keynes. The Professor commented that when studying economists, it is also important to know more about the lives that they led. The Professor read many biographies, not only of economists, and I remember that they were always in English.

Once I saw him reading a biography of the conservative thinker Edmund Burke. I read the same volume, and soon understood why he found it so interesting. Purchasing that book myself out of a desire to emulate the Professor proved to be the starting point for my book, published several years later, titled *Hoshushugi to wa nanika [What is Conservatism?]* (Chuko Shinsho, 2016).

A feature of the United Kingdom, even in comparison to France and other European nations, is its wealth of excellent biographies, which has helped establish biographical writing as a distinct genre of literature. In the UK there are numerous biographies that are rich in content and stand up well to scholarly reading, yet are also written in simple language and can be enjoyed by lay readers. Professor Otaki enjoyed reading such biographies; he often introduced them to me, I gained much from those introductions. I once suggested to the Professor that there aren't many good biographies in Japan. A few days later he came back to me with the response: "What about Agawa Hiroyuki's *Inoue Shigeyoshi*?" That turned out to be the last conversation we ever had.

Professor Otaki was often very candid in his views. If he thought something to be correct, he would not hesitate to offer forthright criticism of others' arguments. This, I believe, was an indication of his intellectual integrity. Most of his criticisms were grounded in sensitivity and a sense of justice. The fact that the Professor was so widely loved despite his sometimes severe manner is surely attributable to his intellectual integrity, together with his warm smile. At times he would laugh merrily and effusively, but at others he would just give a wry smile tinged with irony.



But what he offered most frequently was a kind, welcoming smile. It fills me with sadness to think that I will never again see that smile.

When I think back on the scholarly gifts that Professor Otaki bestowed on me, I regret always being so slow to grasp his meaning and unable to respond adequately to his questions. Yet I have a

sense that the Professor is always nearby. In the future I hope to be able to move a little closer to his ideas, guided by the words that he shared with me.

Professor Otaki is my intellectual companion for eternity. May he rest in peace.

## The Cultural Struggles behind Autocratic Regime Change

**Meredith SHAW**



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### **Cultural Policies in Autocracies**

One subject that has always intrigued political scientists is the question of why some autocracies fail and others persist. Studies of autocratic resilience have typically focused on two types of explanations: economics (how autocrats extract rents from their citizens and reward their supporters) or repression (how autocrats surveil and control the population and punish dissenters).

My research considers the influence of another element: cultural policies, meaning government efforts to directly manipulate the direction of a nation's culture. State-imposed cultural manipulations are a pervasive feature of modern autocracies across all regions and time periods. In the name of "culture," autocratic governments have sought to change how their constituents dress, eat, write, read, talk, sing, dance, worship, raise

children, and style their hair. Autocrats often invest considerable resources toward ensuring that their "approved" culture succeeds and all "unapproved" culture fails.

The costs of state-imposed cultural policies are varied and often hard to measure. Among the most obvious economic costs we may consider the cost of enforcement, losses in consumer spending, damage to trade relationships, and loss of national prestige. Additionally, state efforts to outlaw certain fashions, music, movies, and food-stuffs often lead to the expansion of black markets where such items can be obtained, disrupting the government's control of the economy. The East German authorities' prohibitions against blue jeans and rock music have been frequently cited as a driving force behind the waves of immigration and illegal trade that ultimately brought down the iron curtain.

This contradicts our leading economic models of autocracy, which predict that successful autocrats only spend as much public money as necessary to keep their minimal supporting coalition happy and repress dissent, and keep the rest for themselves. Why, then, do so many autocrats spend valuable resources enforcing unpopular cultural policies?

Through a survey of cultural policies in a variety of 20th century autocracies, I found that cultural policies generally fall into two categories: those that impose modernization (often with the aim of spurring economic growth) and those that seek to forcibly preserve or restore perceived "traditional" culture. The Soviet bloc countries and colonial-era Korea are good examples of the former; Iran, Saudi Arabia and North Korea are good examples of the latter.

This led me to reconsider the past failures of Modernization Theory. This oft-debunked line of political theory has undergone several waves of revision, but the general idea is that societies will be more likely to embrace democratic norms as their economies develop and their societies embrace secular/modern (i.e. Western) values (Inglehart and Welzel 2005). But even the newer incarnations of Modernization Theory have never bothered to distinguish between those societies whose modernization occurred organically and those upon which it was imposed by an autocrat eager for economic growth. I decided to explore the question of how populations respond to state-imposed cultural modernization.

### **Two Model Cases: Mongolia and South Korea**

Two cases of state-imposed, rapid, modernizing changes that I examine closely in my dissertation are communist Mongolia under Soviet influence from 1924-1990 and Yushin-era South Korea under military dictatorship from 1963-1986. I was fortunate to be able to interview many Mongolians and South Koreans who had actively participated in their countries' democratization movements.

What struck me was the similarities between these two groups – one operating under a stagnating, communist, Soviet-backed regime and the other under a high-growth, capitalist, US-backed regime – in the way they used cultural symbols to attract public sympathy and support for their cause. Both were able to draw on deep social anxieties from decades of watching their traditional ways of life and distinctive cultures being eroded in the name of “modernization” and “progress.”

For instance, in the 1970s in South Korea, young democracy activists in the cities were able to reach out to poor factory workers who had migrated from the countryside through political theatre performances called madangguk that incorporated the rhythms, language and movements of peasant folk dances. In this way they communicated some simple political messages while simultaneously forging a common identity as traditional-minded Koreans struggling against a modernizing government. Similarly, in Mongolia young protestors wore traditional clothing and sang songs of Genghis Khan to communicate that they were defending Mongolian traditions that had been

swept aside by the pro-soviet government. After democracy, winning coalitions in both countries acted quickly to pass laws restoring traditional arts and revering forgotten cultural figures, even when the political and economic situation was still uncertain.

### **Hypothesis Formation**

Through observations of these and other case studies, I have begun developing some hypotheses for how different cultural policies affect regime stability. In short, I predict that governments will be inherently more prone to encounter recurrent, grass-roots, regime-change-seeking popular opposition if:

- A) They are perceived to be foreign-imposed or based upon foreign ideologies;
- B) The ruling regime pursues policies that impose rapid cultural transformation in a modernizing/Westernizing direction.

As a corollary, I hypothesize that successive governments in the aftermath of a popular revolution will be more likely to stabilize into democracies if they take action early on to undo the cultural policies of the preceding autocrat.

The principle innovation of this approach is that it allows us to consider a new angle on the classic collective action problem: in culturally oppressive regimes, protest groups can signal their affiliation and attract a larger and more diverse following by making use of cultural symbols – singing banned songs, breaking official strictures on dress and hairstyle, praising officially condemned historical figures, etc. (Scott 1990). Cultural protests are more difficult for a regime to suppress than overtly political acts, and thus provide a safer method of signaling to like-minded followers.

This idea borrows some concepts from the extensive literature on political coalitions and class-based models of political revolutions, but also considers the idea that coalitions may line up along cultural lines as well. The Mongolian and South Korean cases suggest that cultural preferences tend to form along class lines, and thus a government's cultural policies can work to either unite or divide class coalitions.

One important caveat is that this model only applies to ethnically homogenous states that have

a large degree of popular consensus on their cultural identities. The canonical literature on democratic transitions has long assumed a negative relationship between cultural chauvinism and democratic consolidation. Much of this research is based on the ethnically diverse states of Eastern Europe and the Middle East, where extant nationalist forces, formerly held in check by a strong dictator, fractured with the advent of democracy and disrupted fragile democratic institutions. Western democratic theorists rarely consider how, in a more homogenous state such as Mongolia or Korea, resurgent cultural nationalism might actually be conducive to the political stability of a young democracy – particularly if that democracy immediately follows a culturally revisionist autocracy.

I chose to focus on East Asian societies because they share certain important similarities: they all began encountering “modern” (Western) culture at a time when they already had relatively established borders and concepts of their own cultural

identity, at least compared to Africa and the Middle East. They all share Buddhist and Confucian heritages that influence their understanding of just rule and correct citizenship. Also, East Asian autocracies are not greatly affected by the political dynamics of the so-called “resource curse” which complicates models of autocracy elsewhere. Through these characteristics, East Asian autocracies provide a set of conditions quite distinct from most previous studies of autocracy and democratic regime change. By incorporating the oft-overlooked element of cultural policy, I believe that this research can shed new light on the sources of autocratic stability and failure.

### Sources

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- Scott, J. C. 1990. *Domination and the arts of resistance: Hidden transcripts*. Yale University Press.



## ISS Contemporary Japan Group at the Institute of Social Science, The University of Tokyo

ISS Contemporary Japan Group seminar series provides English-speaking residents of the Tokyo area with an opportunity to hear cutting-edge research in social science and related policy issues, as well as a venue for researchers and professionals in or visiting Tokyo to present and receive knowledgeable feedback on their latest research projects. Seminars are open to everyone. Admission is free and advance registration is not required. For further information, please consult the CJG website: <http://web.iss.u-tokyo.ac.jp/cjg/>.



### Florentine Koppenborg

(Post-doctoral Research Fellow at the Chair of Environmental and Climate Policy at the School of Governance, Technical University of Munich)

September 20, 2018

#### *The Art of Change by Crisis: Japan's nuclear policy after the Fukushima nuclear accident*

The Fukushima nuclear accident eroded trust in the safety of nuclear power plants in Japan. In response, nuclear safety administration was reformed in a bid to strengthen nuclear safety and regain public trust. After similar efforts following the Mutsu nuclear powered ship accident in 1974 and the 1999 Tokaimura criticality accident, nuclear power promotion continued unabated. This time, however, the creation of the Nuclear Regulation Authority (NRA) inadvertently put Japan on a path towards a nuclear phase out. Despite pressure from a powerful coalition of actors pushing for restarts, dubbed the “nuclear village” by critics, five years after Fukushima, nuclear power made up only two percent of the electricity generated in Japan. Why was the outcome of nuclear safety reforms different this time?

In answering this question, the presentation focusses on two things: the nature of the newly established NRA, and the reform process itself. As an independent regulatory agency, the NRA proved able to defy pressure from the pro-nuclear coalition. It forced an internalisation of safety costs and broke the information monopoly pro-nuclear actors had held for decades. Moreover, this time the reform process included new agents of change, which were able to steer the outcome in a different direction. These include the DPJ government in 2011/12 as well as international actors that had not participated in previous Japanese safety reforms. The findings presented are the result of a three-year research project on nuclear safety governance reform in the wake of the Fukushima accident.

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### Mary Alice Haddad

(Professor of Government, East Asian Studies, and Environmental Studies at Wesleyan University)

October 18, 2018

#### *Environmental Advocacy in East Asia: A New Policy Network Model*

East Asia is hostile to environmental advocacy. It is home to developmentalists, pro-business governments, not all of which are democratic. It has few professional advocacy organizations, and weak Green parties. And yet, Japan has been a leader in emission standards for decades, China has recently become the world's largest producer of photovoltaic panels, and Korea and Taiwan have both embarked on major green initiatives that involve not just green business development but also new national parks, widespread energy conservation, and comprehensive recycling efforts. This presentation will lay out new evidence showing that activists across East Asia, indeed across the world, utilize a relatively small number of strategies (e.g., make a friend on the inside, make it work for business, make it work locally, contribute to education, art, and radical innovation) that are particularly successfully in achieving pro-environmental behavior change among governments, businesses, and citizens. The presentation will develop a new model of how networks influence policymaking to explain why these strategies are particularly effective.

**Iwona Merklejn**  
(Associate Professor at the School of Cultural and Creative Studies, Aoyama Gakuin University, Tokyo)



### Jan Wislicki

(Assistant Professor at the Department of Formal Linguistics, University of Warsaw, Poland)

November 22, 2018

#### *News headlines and ethnic minorities in Japan: Reporting the `hate speech law` of 2016*

In this talk we present the results of the first stage of a long-term project: `News media and ethnic minorities in Japan: representation, discrimination, diversity`. The final aim is to provide a more precise, nuanced

analysis of media discourse about ethnic minorities than existing qualitative (critical discourse analysis) and quantitative (statistical analysis) methods allow, and to develop a machine learning tool instrumental in that kind of analysis. We intend to reveal a variety of subjective attitudes towards minorities that media implicitly promote, such as indifference, reluctance, hostility, aggression, favour, and enthusiasm. We start with a selective analysis of the media debate surrounding the so-called `hate speech law` (Anti-Discrimination Act) enacted in Japan in 2016. We take a closer look at the types of facts relevant to both hate speech and the Act reported in Japan's five leading national newspapers. The analysis is based on a sharp distinction between facts, reports and opinions. This distinction turns out to be challenging when applied to precise analysis of media texts. Nevertheless, we argue that it is a proper starting point for investigating how news media shape the gradation of attitudes towards minorities—an urgent topic for all contemporary societies, including Japan.

### **Yves Tiberghien**

(Professor of Political Science at the University of British Columbia)

December 13, 2018

#### *Japan's New Leadership in Liberal Economic Governance*

Japan has long been seen as a solid but rather stolid pillar of the global liberal order, more inclined to follow the US than take the initiative. This has changed over the last two years. Japan has grown more active in both regional leadership and global governance (IMF, reform of global architecture, G20, WTO, global climate negotiations). In trade, Japan has undergone a revolution from reluctant TPP joiner to the leader of the post-US TPP-11, complementing that feat with a Japan-EU FTA and other ongoing negotiations. At the G20, Japan is taking the helm in 2018-2019. In infrastructure and development, Japan is leading new international initiatives. And at the UN, PM Abe recently spoke boldly about the importance of upholding the global liberal order. What explains this dramatic shift?

In this talk, I explain Japan's behaviour within a larger model of truncated strategic interactions. Drawing upon the cases of trade, G20, climate change, and development governance, I argue specifically that Japan's new behaviour is driven less by domestic politics than by a reaction to the crisis of the liberal order caused by the election of President Trump and the emerging risk of a China-led order in Asia.



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### Steven K. Vogel

(Chair of the Political Economy Program, the II Han New Professor of Asian Studies, and a Professor of Political Science at the University of California, Berkeley)

January 11, 2019

#### *Japan's Ambivalent Pursuit of Shareholder Capitalism*

Modern-day markets do not arise spontaneously or evolve naturally. Rather they are crafted by individuals, firms, and most of all, by governments. Thus “marketcraft” represents a core function of government roughly comparable to statecraft. This talk builds upon the recognition that all markets are crafted, and then explores the implications for understanding the evolution of the Japanese market model. As the Japanese economy descended from boom to bust in the early 1990s, government and industry leaders called for a decisive move toward U.S.-style shareholder capitalism. But a funny thing happened on Japan’s way to the U.S. model – it never got there. In practice, the government gave firms more options for restructuring, but did not make them more beholden to shareholders. And firms favored superficial adjustments to prop up share prices rather than fundamental changes. In fact, Japanese government and industry were probably wise to be ambivalent of the shareholder model, for some of the core features of that model – such as stock options, share buybacks, and mass layoffs –have not proven to improve long-term corporate performance in the United States.

### Jaemin Shin

(Thyssen post-doctoral research fellow at the German Institute of Global and Area Studies)

February 7, 2019

#### *Gender and Politics in Northeast Asia: Female Legislators in Korea and Taiwan*



Drawing insights from the literature on the effect of gender on legislators’ priorities and preferences, this project examines whether and how the increased number of female legislators



(descriptive representation) in Korea and Taiwan over the past two decades has led female legislators to act on behalf of female electorates (substantive representation). Based on bill sponsorship, co-sponsorship, and newspaper data, the project examines i) the effect of three political factors—seat share, political institutions, and legislator characteristics—on substantial representation of women, ii) how the quality of female representatives' legislative networks affect legislative and electoral success, and iii) how mainstream media in each country have portrayed gender-promoting activities by female legislators.

**Rieko KAGE**

(Associate Professor of Political Science at the Department of Advanced Social and International Studies, University of Tokyo)

February 21, 2019

*The Politics of Judicial Reform in Japan*

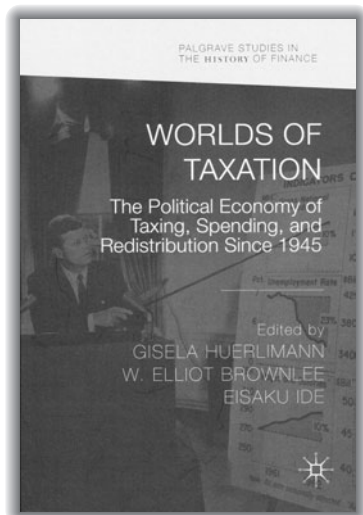


The delivery of justice is a core function of the modern state. The recent introduction of jury/lay judge systems for criminal trials in Japan, South Korea, Spain, and perhaps soon Taiwan represents a potentially major reform of this core function, shifting decision making authority from professional judges to ordinary citizens. But the four countries chose to empower their citizens to markedly different degrees. Why? Drawing on detailed theoretical analysis, original case studies, and content analysis of fifty years of Japanese parliamentary debates, I show that the relative power of 'new left'-oriented political parties explains the different magnitudes of reform in the four countries. The talk also offers a comparative analysis of the Japanese lay judge reform and another major reform that was enacted in the early 2000s, administrative litigation reform.

# Recent Publications by ISS and ISS Staff

Gisela Huerlimann, W. Elliot Brownlee, Eisaku Ide (Eds.)  
(Mari Osawa)

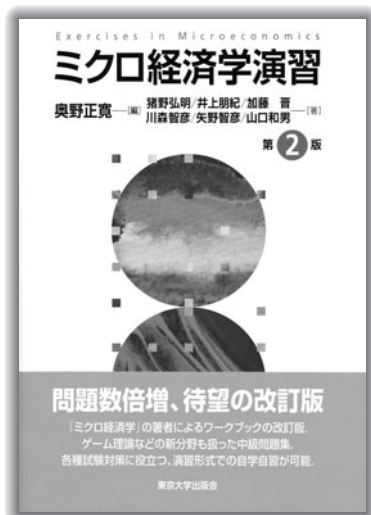
『WORLDS OF TAXATION The Political Economy  
of Taxing, Spending, and Redistribution Since 1945』  
(Palgrave Macmillan) 2018年9月



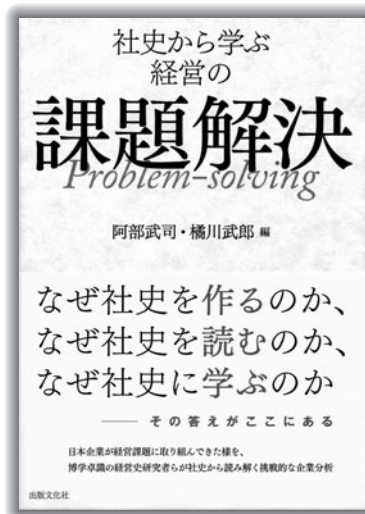
東大社研・玄田有史・有田伸（編）  
『危機対応学 明日の災害に備えるために』  
(勁草書房) 2018年9月



奥野正寛（編） 猪野弘明・井上朋紀・加藤晋・  
川森智彦・矢野智彦・山口和男（著）  
『ミクロ経済学演習 第2版』  
(東京大学出版会) 2018年9月



阿部武司・橋川武郎（編）（中村尚史）  
『社史から学ぶ経営の課題解決』  
(出版文化社) 2018年9月



宇野重規（著）  
『未来をはじめる  
「人と一緒にいること」の政治学』  
(東京大学出版会) 2018年10月



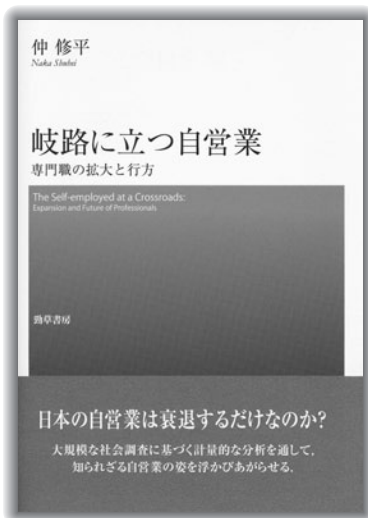
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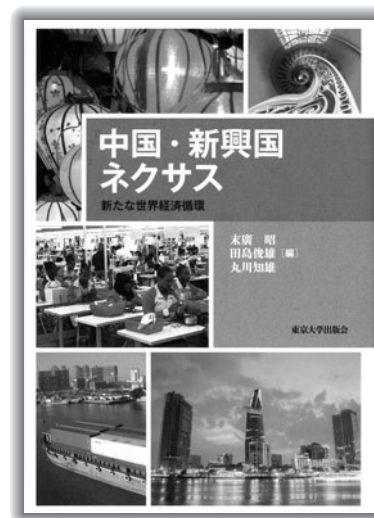
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『30代からの働く地図』  
(岩波書店) 2018年10月



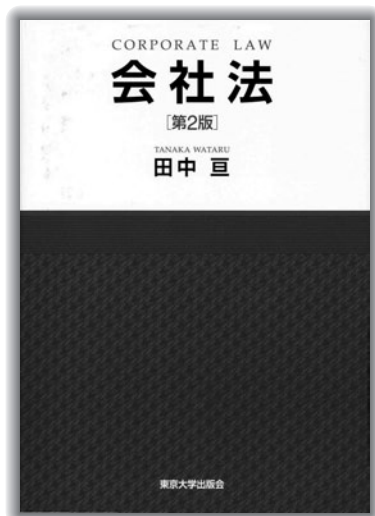
仲修平 (著)  
『岐路に立つ自営業』  
専門職の拡大と行方  
(勁草書房) 2018年11月



末廣昭・田島俊雄・丸川知雄 (編)  
『中国・新興国ネクサス』  
新たな世界経済循環  
(東京大学出版会) 2018年12月



田中亘 (著)  
『会社法 第2版』  
(東京大学出版会) 2018年12月



廣井亮一・中川利彦・児島達美・水町勇一郎 (著)  
『心理職・援助職のための法と臨床』  
(有斐閣) 2019年2月



# Focus on ISS

## The Tokyo Conference on the Economics of Institutions and Organizations

NAKABAYASHI Masaki

If information is symmetric and contracts are complete, free transactions lead to the optimal resource allocation. Each individual joins the market and trades with each other as a price taker.

In the real world, however, symmetric information is not easy to attain. Even worse, a dynamic and growing economy almost depends on asymmetries of information.

In geographically or socially distant communities, trade between communities increases the aggregate welfare of the communities. However, by construction, essential information for trade is asymmetric between either geographically or socially distant communities. Trade that could improve resource allocation must inevitably overcome the challenge of asymmetric information.

If a firm finds a new idea to produce the same goods more cheaply or to differentiate products, the firm can earn excessive returns until the other market participants have caught up with it. It is why firms conduct research and development and differentiate products. Firms, in essence, strive to make information asymmetric. Only by capitalizing on information unknown to other market participants, such as knowledge for innovation and product differentiation, can a firm earn excessive returns. If a firm cannot earn excessive returns, the firm earns the profit at the same level at the wholesale price of capital, that is, the market interest rate. However, nobody would invest in a firm whose profit rate is the same as the market interest rate. Thus, surviving firms create informational asymmetry every day. Households invest only in such firms whose core competence is in knowledge unknown to other market participants, including, alas, by construction, households themselves. Therefore, in any thriving capitalist economy, asymmetry of information between firm managers and investors is inevitably severe.

In short, we cannot remove asymmetric information unless we accept stagnation. Either for trade expansion or productivity improvements, we need to accommodate asymmetric information every day. An economy whose institutions and organizations handle asymmetric information grows. So, the quality of institutions and organizations matters to our growth.

We call our activities workshops and conferences “The Economics of Institutions and Organizations.” Our community includes organizational economics built on contract theory and new institutional economics that are motivated by but not limited to game theory. We have theorists specializing in industrial organization, game theory, contract theory, economic growth, and social choice. Development economists, labor economists, and economic historians are also fellows. In sum, economists who somehow share interests in the implications of institutions and organizations for economic development are our friends.

Since 2006 we have organized monthly workshops during semesters at Osaka University. Starting in 2008, we have also organized twice yearly conferences—The Tokyo Conference on the Economics of Institutions and Organizations—on spring and summer breaks at the Institute of Social Science, The University of Tokyo. The upcoming conference is to be held at ISS on March 18 and 19, 2019, which will be the 125th meeting.

We started our activities at Osaka when I worked for the Graduate School of Economics, Osaka University. Participants included: Shingo Ishiguro, who specialized in contract theory, Takashi Shimizu (game theory), Kazuhiro Yamamoto (urban economics), Ryoji Ohdoi (growth theory), Katsuya Takii (growth theory and organizational economics), and Junichiro Ishida (organizational economics). Usually, professional economists present their works in field associations or field sessions in large conferences and do not necessarily construct research ideas while interacting with each other. We wanted this cross-fertilization to understand economic institutions and organizations better.

In a monthly workshop, we have two 90-minute presentations. In our twice-yearly conference, we allocate 60 to 70 minutes for presentations. We reserve plenty of time for strengthening ideas by presenting and listening to work in its early stages instead of displaying and appreciating the developed muscles of almost completed research.

While we often present our own work, speakers at the monthly workshops are invited. While most presenters at the twice-yearly conferences were invited, we switched in 2018 to competitive selection through the Conference Maker.

Fortunately, we have met scholars who find our approach interesting. Now core members include Noriaki Matsushima (industrial organization), Keisuke Kawata (development and labor economics), Akifumi Ishihara (organizational economics and contract theory), Ryuichi Tanaka (the economics of education and labor economics), Toshihiro Matsumura (industrial organization), Eric Weese (political economy and spatial economics), and Mayo Morimoto (economic history). Some were invited speakers, and some were students who sat in on workshops and conferences.

To learn more about our activities, please visit <https://sites.google.com/site/theoeio/Home>

If you are interested in presenting your work at our conferences, please check the Conference Maker <https://editorialexpress.com/cgi-bin/conference/cm.cgi>