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The Founding of Mitsubishi: A Case Study in Japanese Business History

By Kōzō Yamamura (1967)
Associate Professor of Economics, San Diego State College

The founder of Mitsubishi Zaibatsu, Yataro Iwasaki, was born in 1834 as the eldest son of a peasant who lived "scraping the bottom of the rice bowl". As his father was rarely sober, his hard-working mother and the financial assistance of his maternal relatives made it possible for him to attend village schools. His education consisted of Chinese classics and ethics taught by his relatives and by other lower class samurai of Tosa-han (a feudal domain, the present Kōchi Prefecture). Little is known of his childhood, but sources agree on his native intelligence and extreme mischievousness.

When Commodore Perry came to Japan in 1854, Yataro was 20 years old and the tempo of anti-Shogun sentiment was gaining momentum. It was in this historic year that Yataro, upon the recommendation of his relatives, and with their financial aid, bought the title of goshi (a low-class country samurai) in order to become a jūsha (aid to a samurai) of a samurai who accompanied the daimyo (feudal lord) of Tosa to Edo (Tokyo).
In Edo, he continued to study Chinese classics on a part-time basis along with his duties, but his stay was out short when he left for Tosa. to help win freedom for his father who had just been imprisoned following a fracas in one of his drinking bouts. Yataro not only failed to achieve his end, but also managed to get himself imprisoned after insinuating that the prison officials had hoped for a

bribe. After a brief stay in a village prison, he emerged jobless and without prospects. He resorted to eking out a meager living as a village school teacher.
It was during this period that he came to know Tōyō Yoshida, a high-ranking samurai then under house arrest on the charge that he had struck a fellow samurai. Yoshida had held several important positions in the han administration and had been known for his progressive views, which included promotion of the han industries, international trade, and the adoption of new knowledge from abroad.

In the political reshuffle of 1859, Yoshida was restored to the han hierarchy. He appointed Iwasaki to a minor position in the bureaucracy. Now 25 years old, Iwasaki had thus benefited from his acquaintance with Yoshida to emerge from four years of enforced inactivity. To overcome his humble origin he worked diligently, and when his meager finances permitted he “wined and dined” his colleagues to earn promotions. These two ingredients - ability and "public relations" - were to become the staples for much of his later success. In the more peaceful years of the early Tokugawa era he would perhaps have had ended his life as an inconsequential bureaucrat of Tosa-han, but this was one of the most turbulent eras of Japanese history. In 1862 his benefactor Yoshida was assassinated by the conservative extremists of Tosa-han for his progressive and strongly cosmopolitan views. Iwasaki, as a protege of Yoshida, was chosen to search and kill the assassins of Yoshida. Though accounts differ in details, it would be correct to say that Iwasaki had little interest in this mission of revenge. After a stay of a few months in Osaka and Kyoto, where most of his time was spent in inns and tea-houses, he returned to Tosa to face a chilly reception from his former colleagues.

Disenchanted with the fruitlessness of the samurai code and the lowliness of his position, he abandoned his samurai status altogether to become a lumber merchant in spite of much derision on the part of his former colleagues. Though no record is available, one can guess that the venture was started on the modest capital obtained by selling his title of goshi. However, the lumber business proved a total failure and Iwasaki at 28 again found himself unemployed.

In 1865, after four more years of idleness, Iwasaki obtained a low-ranking job with Keiseikan (Industry Promotion Agency) of Tosa-han. This had been established in 1852 by the daimyo of Tosa-han upon the recommendation of Tōyō Yoshida. The Agency's function was to promote sales and production of han-controlled products to alleviate the financial deterioration which threatened all han in the last years of the Tokugawa period. Iwasaki, however, found the job dissatisfying and even humiliating, and left the Position within a year. Nevertheless, in retrospect this was far from a wasted year, for during this period Yamasaki, who was the head of the Agency, noted Iwasaki’s diligence and ability. A year later, when Yamasaki was appointed head of the Nagasaki office of the Keiseikan to handle the rapidly increasing volume of arms purchases, he called upon Iwasaki to join him.

This was in 1867 when the ancien régime was on the verge of collapse and "the wind smelled of blood". The Nagasaki office was buying all the arms it could find for the militant Tosa-han. As a consequence of the reckless purchase of arms, and through mismanagement, the office accumulated by the end of 1867 a large debt of over 200000 ryo. Confronted by this crisis, Yamasaki now recommended to the han that Iwasaki be promoted to head the Nagasaki office. The undesirability of the task and Iwasaki's now recognized ability to deal with arms merchants (especially foreigners) proved sufficient to overcome his humble origin which, in the last years of feudalism, had become easier to overlook.

Shortly after this promotion, Iwasaki found himself called upon to assist with the fund-raising in Osaka, which had become a staging center for the Restoration forces against the Shogun. Tosa-han, which was massing its troops there, was on the verge of bankruptcy and could not even provide rations for its army. Though the available sources as to whether the idea originated with him or someone else are not clear, Iwasaki soon became involved in the counterfeiting of Shogun coins and the printing of supposedly convertible han notes to expedite the march of troops. He had, in effect, become a financial trouble shooter of the han. In the topsy-turvy condition of the Restoration War, the former jige-ronin came to the attention of the han for his ability. About the same time he had also succeeded in refinancing the debts of the Nagasaki Agency by borrowing 300000 ryo from an American merchant in exchange for the exclusive rights to deal in the han’s naphtha (petroleum). The means which Iwasaki used to consummate these transactions were typical: coaxing, cajoling, the hint of non-existent rivals, bribes to the American’s interpreter, flowing champagne (sic), and geisha.

Iwasaki busily occupied himself for the next few years in managing the Nagasaki office and the han monopolies, as well as performing the services of a trouble-shooter - the role he was frequently called on to play in those years of rapid political and economic transformation. Thus, when Haihan-chiken (Abolition of Han) came in 1871and Tosa-han withdrew from all former economic activities, Iwasaki was the logical choice to inherit the business of Tosa-han.

To extricate itself from its large debt of 300000 ryo, the han presumably gave Iwasaki 230000 ryo in cash, all the assets and privileges connected with the han business in naphtha, tea, silk, lumber, coal mining, and its eleven ships (six steamships and five sailboats). If this is correct, no one can accurately estimate the worth of the transaction to Iwasaki. For one thing the value of these han assets was unknown; for another the value of the former monopoly rights of han business now depended entirely on Iwasaki's ability to manage them competitively. Perhaps it is more accurate to say that Iwasaki did not benefit by this transaction per se, but he was able to gain a strategic foothold that could be exploited. Immediately following the acquisition of the former han business, Iwasaki, exploiting the knowledge and connections acquired as a

han official, began to deal in ships of all sizes sold by former hans and foreign merchants. Those who were inexperienced and eager to sell became easy prey for Iwasaki, and those who were experienced and shrewd often found themselves outwitted by him. These sharp dealings, which would have made a Jay Gould or Daniel Drew envious, were reported to have earned Iwasaki a small fortune in addition to his efficient management of former han business. However, this was nothing compared to what he earned in the conversion of former han-notes into government notes. The new government, assuming responsibility for the depreciated former han currencies, converted the notes of Tosa-han at face value into Dajōkansatsu (Privy-Councillor's notes). Iwasaki, obtaining the information before it reached the holders of former han-notes, bought up a large quantity and made a considerable fortune.

On the strength of these profits and the successful operation of the former han business, Iwasaki founded the Mitsubishi Shokai (Trading Firm) in 1873, and his major interest turned to shipping. The Japanese shipping business at this time was entirely coastal and fiercely competitive. Iwasaki's competitors were a large number of small firms with a few vessels each, specializing in short distance hauls, and the Yūbin Jōkisen Kaisha (Steamship Mail Co.). The latter was organized by the joint capital of wealthy merchants (Mitsui, Ono, and Shimada) enjoying a subsidy from the government, which, under the leadership of high-ranking officers of the Ministry of Finance such as Kaoru Inoue and Eiichi Shibusawa, wanted to see Steamship Mail grow. Iwasaki destroyed most of the small firms by under-cutting prices and offering longer and better-connected shipping schedules; his only competitor now was the Steamship Mail Co.
To all appearances the duel seemed unfavorable to Iwasaki. Steamship Mail was “the favorite of the Ministry of Finance and enjoyed the protection and prestige of the new government”, and had a fleet of fifteen steamships which were bought from the government on a fifteen-year credit basis and a subsidy. Iwasaki’s fleet was smaller and older and had no subsidy. However, appearances were deceiving. During 1873-1874, after a fierce rate war which all but ignored safety, Iwasaki managed to defeat his rival. His victory was due to a thorough exploitation of his competitor's vital weakness and its samurai management. Steamship Mail was operated “in the most bureaucratic fashion of the old han mentality”. The officials, still carrying swords, advertised that "those wishing to be granted permission to use the ships, who request the permission and pay a proper stun, may then be granted the privilege". The high-handed attitude of the samurai was evident in "their (ships' officers’) impolite and often rude manner toward passengers".

Iwasaki, on the other hand, was the very image of a chonin. He instructed his subordinates (most of them samurai) to “worship the passengers” as they were sources of revenue. In short, the modern attitude of "the customer is always right" became the major weapon of Mitsubishi Shokai. The result was a loss of patronage for Steamship Mail, and provided Iwasaki with victory in his first contest.

However, the struggle cost Iwasaki clearly. Far from secure in its financial foundation, his shokai in 1874 was barely on its feet when the Formosan Incident occurred. This affair resulted from the killing of fifty-four Japanese fishermen who were shipwrecked on Formosa (Taiwan). Preliminary discussions with Qing Dynasty China, which owned the island, were fruitless. China dismissed the incident as mob violence and rejected all responsibility for the incident. Japanese public opinion immediately became inflamed. The cabinet thereupon decided to embark on punitive action on Formosa. With five large steamships borrowed from an American and an English shipping firm as its core, the government readied in Nagasaki a convoy to carry 3650 soldiers to Formosa. Learning of the impending attack on Formosa, China appealed to the United States and England to help avert the attack. The two Western powers reacted by declaring their neutrality in the matter and by ordering their respective firms to withdraw the ships. This action by the United States and England dismayed the Japanese cabinet, which by then was politically committed to the attack.

To replace the ships withdrawn by the American and English shipping companies, the government in May hastily bought thirteen ships at a cost of $1506800 from those Western companies who were willing to sell, while the Japanese expedition forces waited in Nagasaki. Soon afterward the contract to operate the government ships and transport men and material was given to Iwasaki. There were two major reasons for favoring Mitsubishi Shokai over Steamship Mail. One was a change at the top level of the government, which had taken place following a political dispute on the question whether or not to invade Korea. Shigenobu Okuma had become the new Minister of Finance. This meant that the former Minister of Finance, Inoue, a staunch supporter of Mitsui interests and Steamship Mail, had been replaced along with Eiichi Shibusawa, who also left his position in the Finance Ministry. The second reason was that, given the political antagonism of the two factions, Okuma was forced to support a shipping firm other than Steamship Mail which his political opponents supported, and this meant support for Iwasaki.

Iwasaki had also worked feverishly to win the friendship of Okuma in anticipation of the latter's political role, and after Okuma had become the Minister, Iwasaki intensified his efforts to get the most favorable terms for his contract. Or, as one writer put it, "after a great deal of campaigning behind the scenes - mostly at famous inns and geisha houses - Iwasaki succeeded in talking these two (the Prime Minister and the Minister of Finance) into giving him the contract on his terms". Though there is no agreement among the sources on the details of Iwasaki's profits resulting from the contract, no one disputes the fact that this contract solidified the Mitsubishi Shokai.

The Formosan Incident, and the "friendship" of Okuma to Iwasaki changed the face of the Japanese shipping industry overnight. This exceedingly unprofitable expedition for Japan benefited

Iwasaki in more ways than one. Steamship Mail, now on the verge of bankruptcy because of sharply reduced patronage and loss of the government subsidy, asked the government to buy up the company's eighteen ships at 325000 yen. The government obliged and resold them to Iwasaki on a loan of fifteen years at 3 per cent. In addition, the government gave Iwasaki the thirteen ships it had bought for $1506800 earlier, plus an annual subsidy of 250000 yen. The major condition of this windfall for Iwasaki - stipulated in the so-called First Decree - was that the recipient was to open a route between Shanghai and Yokohama.

Ostensibly this was to promote the Japanese shipping industry, but in examining the terms of “protection of infant industry” it would be extremely difficult to deny that Iwasaki's “wine-and-dine” policy, and his financial contributions to the Okubo-Okuma alliance were not important reasons for such a policy as "protecting a Japanese company". Iwasaki, now owner of thirty-seven ships amounting to 23385 tons, became a virtual monopolist of coastal shipping and stood ready to compete for international routes.

For the next two years (1874~1876), the government's “protection” and Iwasaki's interests appeared to coincide sufficiently to stifle any open public opposition to the nature of “protection”. When Mitsubishi Shokai began to operate the Shanghai-Japan route in 1874, Iwasaki met stiff opposition from the American Pacific Mail Steamship Co. which had had a virtual monopoly of the route since 1870. The American shipping firm, having four large (over 1000 tons) steamships, and offices in major Japanese ports, fought Iwasaki vigorously throughout the summer and fall of 1874. However, Iwasaki's price-cutting (supported by a government subsidy of 250000 yen), a newspaper campaign for Japanese patronage of "Japanese ships", and other government supports, resulted in a request by the American firm to be bought out. As a result, Iwasaki was able to borrow $800000 from the Ministry of Finance, overcoming Okuma's astonishment at the former’s “thick-skinned” request. With this loan, Iwasaki bought six ships and associated warehouses and wharves from Pacific Mail Steamship.

Immediately following this duel, Iwasaki faced another challenge by the Peninsular and Oriental Steamship Co. (P&O) early in 1876. This English adversary was stronger than its American predecessor, and the Hong Kong-Shanghai-Yokohama route became an arena of competitive price-cutting and patronage promotion. The competition proved costly tor Iwasaki. His tenacious rival fought on from March into August of 1876, forcing Iwasaki to cut all salaries in half. But P&O finally yielded in August as it began to realize the futility of challenging a well-subsidized Japanese firm which had begun to benefit from the new and cumbersome regulations imposed on those Japanese who desired to use foreign ships. Iwasaki was rewarded for his efforts by a fourteen-year extension of the subsidy. The so-called Second Decree, which granted this extension, stipulated his responsibility to open a Korea-Japan route and “strengthen” coastal shipping.

In 1877 Iwasaki reaped large profits from his part in the Satsuma Rebellion. The most critical element of this civil war was coastal shipping, and Iwasaki controlled it. Knowing his power, Iwasaki was in a position to dictate the terms of his service to the government which had just aided him through two competitive struggles against foreign firms. He not only was awarded the contract to ship men and material to Kyushu at a large profit, but also succeeded in getting a government loan of $700000 on a fifteen-year term at virtually no interest. By the end of 1877, Iwasaki owned over 80 per cent of all ships in Japan and controlled her coastal trade.

The following few years were Iwasaki's golden years in profit and in social status. He extended his business into marine insurance and warehousing, which customers of Mitsubishi ships were required to use. During the post-Rebellion inflation, he decreed that payments be made in Mexican dollars. This had the effect of raising the price of his services by 60 to 70 per cent as the Japanese yen had rapidly depreciated. He also eliminated middlemen in producing areas and wholesalers in consuming areas by means of forward-and-backward integration. However small the remaining shipping firms might be, Iwasaki continued to weed them out by price-cutting and by refusing to transship goods handled by other companies. Socially he dined with cabinet members, and the Minister of Finance frequented his house. Some began to call him "Gozen-sama", or the equivalent of His Excellency, an expression normally reserved for Privy-Councillors and former daimyo.

In 1880, what could be termed the Mitsui group attempted to challenge the Mitsubishi Shokai. Led by Inoue and Shibusawa, the Mitsui Zaibatsu, which had been forced to use Iwasaki's services, organized Tokyo Fūhansen Kaisha (Tokyo Sailboat Co.) with the modest capital of 300000 yen. Though the firm could not have become a serious threat to Iwasaki's monopoly, Iwasaki made it known that anyone who contemplated joining this new firm by capital subscription or use of its services would be penalized by any means at his command. Nor did he hesitate to resort to libelous statements about the highly respected Shibusawa's personal conduct in order to discourage support of the new company. Under these circumstances, Tokyo Sailboat disbanded soon afterwards.

Iwasaki, confident of his power, intensified his efforts to integrate his business backward and forward. The rate structure was set and reset - in modern jargon - to exploit price elasticity of the respective commodities and other characteristics. His services deteriorated, and much of his profits were diverted to his other business activities rather than in the maintenance of his ships. Popular resentment was clearly evident as newspaper articles during 1880-1882 indicate. For example, Ukichi Taguchi, a close associate of Shibusawa wrote in Tokyo Keizai Zasshi (Tokyo Economic Journal) that:
"
Yataro accumulated wealth and his luxuries were unparalleled. Frequent dinners given by Iwasaki in the company of dignitaries boasted the best of geisha, of amusements and delicacies of both land and sea. Much was

spent on such occasions, but much was gained later because these dinners returned profits in friendship - the friendship of those who could favor him.
"

and that:
"

Mitsubishi fails to repair its ships, but is not shipping its business? Is there not a subsidy for repairs available also? Is the large subsidy insufficient? The answer is that Iwasaki, since 1878, has diverted a large amount of his funds for other activities. His interests (in banking, mining, newspapers, and marine insurance) are reported to exceed one million yen. This wealth explains the use to which government subsidies have been put.
"

These smouldering resentments soon resulted in the beginning of the celebrated Umibōzu (Sea Monster) Affair. Reminiscent of the “muckraking” literature in America, the attack on Iwasaki by the press became wholesale and unsparing. He was charged with reducing the number of ships by six since 1875 in spite of the rapidly rising demand for shipping, with charging exorbitant rates, and with indulging in all sorts of predatory and monopolistic practices such as tie-in sales and backward-and-forward integration. The writers of these articles were especially incensed by Iwasaki's use of the Mexican dollar as a means of payment for his services. In these journalists’ minds this indicated "Iwasaki's total lack of respect for the nation which helped him to become the largest ship owner in Japan". These journalists toured the nation with the political opponents of Okuma condemning Iwasaki, and the latter was hung in effigy at well-attended "Eliminate the Sea Monster" rallies.
"On the podium were paper models of ships, and an effigy of a sea monster made of straw. Speakers castigated the evils of Mitsubishi. When a succession of orators had succeeded in arousing the feelings of the audience, the paper ships and the effigy were burnt in the midst of the yelling crowd."

In the meantime Okuma, who had left the Ministry of Finance at about this time, grew increasingly anxious to dissociate himself from Iwasaki. Okuma himself was in a series of political difficulties and faced charges of corruption. The government then came under the control of the faction displaced earlier by the Okubo-Okuma coalition. During these years, too, the public, championed by the emerging political parties, began to demand an elected gikai (Diet). The Kyodo Unyu Kaisha (Cooperative Transport Co.) was formed under these circumstances. The new shipping company, formed explicitly to challenge the Iwasaki empire, was capitalized at 6000000 yen, a huge sum by the standards of the time. The government contributed to this venture twelve large steamships and a new cruiser, originally built for the Navy and valued at 1700000 yen. The steamships were rented to the new company for the extremely low fee of 3 per cent of the net profit of the company.

The year 1883 saw one of the fiercest competitions in the history of the Japanese economy. While the newspapers and public watched with partisan concern, both companies competed for speed and

service, and rates began to tumble. The pre-competition passenger rate of 5.5 yen between Kobe and Yokohama, for example, soon fell to 1.5 yen and by the middle of 1884 dropped to 55 sen, one-tenth of the original price (100 sen = 1 yen). Both companies gave gifts (towels and fans), often valued at around 30 sen, to their customers, and speed and punctuality were competitively advertised while explosions of over-taxed boilers increased.

The competition was dangerous and costly. As the number of sea accidents multiplied, losses sustained by both participants mounted. In the last six months of 1884, Mitsubishi suffered losses totalling 680000 yen and Cooperative 1000000 yen, one-sixth of its original capitalization. By the end of 1884 it was clear to both that further struggles meant bankruptcy for one or even for both. The first move for a possible merger came from Cooperative which was an ally of the government, a group led by Mitsui interests, and other anti-Iwasaki elements whole sole interest was to spoil the monopolist's profits rather than to fight tor the principle of "killing the sea monster for the good of the country". After a series of stormy discussions among the shareholders of Cooperative, the two competitors finally concluded merger negotiations in January of 1885. The new shipping company was named Nippon Yūsen Kaisha (N.Y.K.) and Mitsubishi Shokai became its largest shareholder.

While the outline of the merger was taking form, lwasaki's health deteriorated. On February 7, 1885, he died of stomach cancer at the age of fifty-two, only twenty years after he had joined the Nagasaki office of the former Tosa-han. The funeral of the erstwhile jige-ronin was "attended by 50000, including all who counted at all in the political and economic circles of japan in the early Meiji years".