

Japan's Future Development : An Outsider's View

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(October 6, 1994 to September 30, 1995)



al Development and Cooperation, Vol.2, No.1, 1996, pp. 1-33

IDEC

chool for International Development and Cooperation)

Hiroshima University

JAPAN

『国際協力研究誌』

広島大学大学院国際協力研究科

1996年3月

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Abstract

This paper attempts to analyze the development of Japanese economy systematically using English materials only written by both Japanese and foreigners. In order to understand future development of the Japanese economy, the paper traces factors contributed to the rapid growth period during 1950-73, the period approaching economic maturity (1974-86), the period of inflated assets (1986-91), and the current period of stagnation (1991-95). The results seem to indicate that current stagnation of the Japanese economy has been fundamentally caused by the continuation of pro-growth policies while the economy has already reached the stage of maturity. Like any matured person who is expected by other members of the society to behave sensibly, a matured economy must also be designed to operate like one. The German experiences could prove to be relevant for Japan to find her way out of the existing economic crises.

1. Understand Japan from First Hand Experience

Before presenting Japanese economy systematically from my own analysis, as an outsider I shall start by presenting Japan from my own casual observations during my various visits to Japan since 1966. I personally find it necessary to do so, since they have formed part of my understanding and my analysis. Also, it will serve as a way to inform readers how I see the development of Japanese economy with my own eyes periodically since then.

I visited Tokyo for the first time in April 1966, on my way to study in the United States. From my personal recollection now, Tokyo was a modern city much bigger than Bangkok at that time. My impression then was that, Tokyo was a much more dirty city compared with Bangkok. Water in rivers was black and smelly. Smoke covered Tokyo's sky made it looked cloudy throughout the day. My room in one of the big business hotels was very comfortable, with outstanding modern facilities of that time, but it was incredibly small from the standard that I was experienced in Thailand, reflecting the high density of population and perhaps high land price too. I told myself that time that I would not like to see Bangkok developed the way I saw in Tokyo and I would never witness Bangkok developed to that level within my own life time, because things were moving in Thailand then at a

very slow pace and the average life expectancy of the Thai male then were rather short.

After 20 years, Bangkok began to look like Tokyo in the 1960's, the portion of the main river of Chao Phraya that passed through Bangkok is now virtually dead. The situation has been gradually deteriorated for more than a decade without any obvious sign of reversal. Bangkok's sky is now covered with smog resulting from heavy air pollution. It was reported recently that upon the death of one traffic officer. High percentage of lead was found in his blood. The severe air pollution was caused by the notorious problem of traffic jam of the city for almost 10 years now. Contrarily, the rivers and the air quality in Tokyo are now much cleaner than any cities of the same size in the world. Obviously, Bangkok did not enjoy the "advantage of backwardness" or else it must be a very slow learner. Equally obvious, Bangkok has developed too quickly or else I have lived too long.

The moral of the story discussed above reflects the fact that Tokyo or especially Japan has the ability to deal with problems of pollution must more swiftly than the Thai counterpart. Most established economists in Japan attribute such success to the rapid growth path in Japan especially during the two decades of the 1950's and the 1960's. Whether such theory will also be true for Thailand is a matter to be attested in the future. Such ability to turn around quickly, was formed a part of the so called Japanese "miracle". Please observe that I deliberately use past tense in my last sentence to express my personal bias against the concept of Japanese "miracle". Also, I shall add to the footnote that as a Buddhist I do not believe in any kind of miracle.

I returned to Japan from the United States on the way to Thailand in 1970 through Osaka while the EXPO's was held then. Returning from a small city in the South of the United States, Nashville, Tennessee, I was impressed by the level of advancement and very clean of the underground transportation system in Osaka then. At the EXPO's, I was also impressed by the level of high technological development reflected by most exhibitions which I believed they were designed as the main theme of the event. The impression I have at that time was that Japan was already on the trajectory of high technological development. At least the country was much more developed than part of the United States that I used to live. There was no question in my mind then that Japan already became one of the economic power.

In April 1975, I visited Japan again for one month in some official capacity, a little more than a year after the first oil price shock of 1973/74. The mood was completely changed. There was a sense of insecurity everywhere. I was told by many that the Japanese archipelago could be sunk, because of its too heavy reliance on supply of foreign energy that was beyond its control. There were many questions directed to me about the attitude of the Thai students and Thai people in general against the concept floating round during that time of "Japan as an economic animal" for the accusation of being too aggressive in her overseas trade, especially among Asian nations.

I supposed the real fear was their rapid growth path would be interrupted while the country did not accumulate hefty amount of foreign reserves as it has now. There was also a fear that the hostility against Japanese trade practices then would lead to the boycott of Japanese products as well as to halt supply of other vital raw materials. Of course, there is no fear for both insufficient supply of energy as well as trade boycott now, as Japan have already held very large amount of foreign reserves, and is one of the largest suppliers of capital globally. At the same time, there are endless invitations for Japanese investment from almost all countries, together with the fact that Japan now has much higher degree of trade liberation internally, than that of the early 1970's.

The main purpose of my trip then was to learn more about the educational system in Japan as I was

invited to go to observe the result of the reform of education in Japan. Compared with my personal experiences elsewhere, Japanese system of education then and it is still true until now to certain extent, was highly elitist, especially among higher education organized by the state. Japanese education played key role for her industrial development because it gave strong emphasis on competition, the expansion of knowledge base especially in sciences and technology, as well as discipline. One could rightly claim that the schooling system in Japan was also heavy regimented. The system was well designed to serve the national development's objectives. The distinctive product of the reform of education in Japan pointed out to me then was the establishment of Tsukuba University to be operated along the system of higher education organized in the United States.

I visited Japan again in 1979, and for the first time was exposed to few social ills or their potentials. I learned about the existence of Burakumin in Osaka, about the unsettled problem of the Minamata disease resulting from the disposal of harmful industrial waste into public water. I learned about the conflict between the farmers and the Japanese government in the process of the construction of the Narita airport. I learned from groups of fishermen in Hokuriku and Tohoku areas, their reasons for protesting against the proliferation of the nuclear power plants in Japan, not only because the plants were in direct conflict to their existing occupations but their potential harm for future generations to come.

I was told about the exporting of pollution to a developing country by a giant steel plant from Japan who set up a steel plant in one island of the Philippines and exploited the workers there severely. The story was told by the Japanese not the Filipinos. I was also informed about the unequal treatments of the aborigines of Japan, the Ainu. At that time I was not introduced to Mr. Masanobu Fukuoka, a world famous natural farmer who opposed any uses of chemical products yet achieving amazing results. Not many Japanese know him. I only found out recently that he lived not very far from Hiroshima.

The not so impressive stories reflected the fact that within the Japanese society the concept of growth and development was severely challenged and was developed into sporadic fights all over the countries. Fortunately or unfortunately, opposition groups were not strong then. Growth advocator had victory over their opposition with some modified procedure to reduce social ills.

I returned to Japan in October 1992 for one month, when the Japanese economy was already dipped into a recession, after a period of slowdown in growth rate of the 1980's, with the growth rate of 1.3 per cent, the lowest growth record of the Japanese economy after the War, with the exception of that in 1974. In 1989, while we had part of asset boom in Thailand, due in part to rapid purchase of lands from overseas investors especially, the ones from Japan, Taiwan and Hong Kong, my Canadian colleague from the University of British Columbia cautioned me that Japan was embarking on a very adventurous path by using money created from inflated properties domestically to invest in real estates overseas. The property boom in Thailand was in part created artificially. Later on I learned that the so called "bubble economy" was generated in Japan since 1987. The recession in 1992 was due to bursting of the bubble economy towards the end of 1991.

I read from some commentators in newspapers later that in 1989, many Japanese companies rushed out to buy a great deal of symbolic properties in the United States mostly at a rather inflated prices with the promise that they would turn those rather poor performing businesses, into vibrant ones through the so called "Japanese style of management". For example, Sazale Group bought Hotel Bell Air, a romantic retreat filled with lush ginger plants and bougainvillea for \$ 110 million. Mitsubishi

Estate Co. bought the symbolic Rockefeller Center in New York City. Matsushita Electric Industrial Co. bought Universal Studios and the Sony Corporation frightened Americans by purchasing Columbia Pictures.

Most of these purchases endured subsequently heavy loss. Many of them were later on resold at significant loss. The frantic sale of properties bought overseas during the down turn of the economy to pay banks' loans recalled, due to huge amount of non-performing loans resulting from sharp reduction in domestic prices of properties, after the bursting of the bubble economy resulted in part in current situation of the too strong value of the yen. At the same time, confidence in financial system has been shaken due to the fact, according to the report of Ministry of Finance in July 1995, that lending institutions were sitting on bad debts worth 40 trillion yen. The sagged confidence in system of financial institutions together with the strong yen brought the Nikkei down below the psychological line of 15,000 yen in the middle of 1995, shattered investment prospect and the hope for economic recovery.

My latest visit to Japan was to be with Hiroshima University for one year. I arrived Hiroshima on October 6 in the middle of the Asian Games, and was able to participate some interesting events. I also had witness a rise to the new position of yokozuna, the grand sumo champion, of the mighty Takanohana after his Kyushu tournament in December. In January I experienced the Great Hanshin Earthquake, fortunately not directly, that exposed inefficiency of the Japanese government and its bureaucracy. In February, the yen began to surge beyond the psychological exchange rate of 100 yen per one U.S. dollar with the record high of 79.75 yen per one dollar on April 19, 1995, chattering the remaining hope for the economic recovery in that year, after the long slump since 1992. In March, there were then mysterious sarin gas attacks of five underground stations simultaneously. After a few months of police drama and a lot of public frustration, police arrested leader and leading members of the Aum Shinrikyo cult with, the charge of involving in the crimes and many other sinister activities committed by the group earlier. Such exposition of the group's devious activities reflected yet another form of social ills in Japan.

In the meantime, there were grouping and regrouping among political parties in Japan after the end of the 1955 politics, whereby the two alternative political ideologies were rather clear cut represented by the Liberal Democrat Party and the Socialist Party of Japan. The former ruled Japan continuously for 38 years while the latter always served as the opposition during the said period. It was rather odd for an outsider to observe two parties used to be deadly enemies formed a coalition with the support of another small party, the New Party Sakigake (yet another group formerly defected from the Liberal Democrat Party). The unusually strange situation forced by existing political circumstances was that, the combined forces of both the Social Democrat Party and the New Party Sakigake still constituted the minority within the coalition. Yet, they have led the coalition and took important posts in the government.

The above fact reflected the nature of weakness of the Liberal Democrat Party and its leadership. The unexpected behavior of the leader of the Social Democrat Party of Japan resulted in the split within the party, while the split within the Liberal Democrat Party was not less obvious either. Under such circumstance, one would expect to witness the weak and very unstable government. After all the grouping and regrouping of few political parties, the New Frontier Party emerged as a major opposition against the coalition government, thought not very strong initially. The reason was that although carried the reformed platform, the new party was basically the combination of some former members

of the Liberal Democrat Party and Komei or the Clean Government Party. People felt that the new opposition party did not offer any real alternative.

Meanwhile, the economy suffered the great set back resulting from the continuous strength of the yen and a problem of debt ridden of most banks in Japan, due to significant amount of the non performing loan resulted from the fall in value of land for the last three consecutive years. It was recently reported that the land value in 1995 fell by 13.3 per cent from previous year and was fallen by 16.6 per cent last year while the fall in 1993 was 18.1 per cent. Small and medium sizes manufacturing industries, a backbone of Japanese manufacturing development in the past keep moving out from the country in order to enhance their competitive ability. Unemployment rate kept increasing, and reached the record high since 1953, at the rate of 3.2 per cent. There were continuous calls in the media especially in news papers by people from various circles particularly those from businesses for the reform of politics, decentralization and deregulations. The calls were met with little improvement due to the nature of instability of the coalition government.

Fed up with the mainstream politics, Japanese voters casted their ballots to elect former television celebrities as well as former upper house members who were independent candidates, Yukio Aoshima and Knock Yokoyama (Isamu Yamada) for the key posts of governors of Tokyo and Osaka, respectively, on Sunday, April 9, of the nationwide local government election. So far, both of them seem to perform their roles satisfactorily and appear to be better than those of professional politicians, especially for Governor Aoshima. The voters expressed their dissatisfaction against the established politics, targeting their anguish this time more against the coalition government on the election of members of the upper house by very low percentage of turnout of only 44.52 per cent on Sunday, July 23, the lowest turnout in the history of election at a prefectural constituency level, with the Social Democratic Party of Japan suffered a crushing lost. The Party gained only 16 seats out of 41 that it had up for grabs. The other two coalition parties did not do very well either, though they did not lose in the race. The New Frontier Party gained more seats than originally expected. The result helped boost their moral as a much stronger opposition party, ready for the next round of the lower house election challenge.

Until the end of July, most Japanese complained that there was no good news since the beginning of this year, except that of Hideo Nomo, a baseball star upon leaving the national league in Japan last year has made his fame in the United States as a member of the Los Angeles Dodgers with the record of 10 wins and only 4 losses by August 20, 1995. Some said jokingly that it was a good news because Japan could then export baseball players to the United States as a new export items in addition to what the country already exported, so far. The other refreshing event this year was the beautiful wedding ceremony of Takanohana and his very beautiful bride.

As a junior member of the wartime generation, I felt very fortunate to be in Japan right at the 50th Anniversary of the end of the Pacific War, especially to be in Hiroshima on August 6, 1995 in order to learn from the experiences and to observe the mood of the people there. People in Hiroshima has clearly demonstrated their determination to continuously struggle for peace. They have done so during the past 50 years, and I am sure that they will continue to do so in the future, at least until the complete nuclear disarmament is achieved. The only unfortunate part was for some who did not realize, that they too were the victims of the war of aggression of the Japanese imperialism in the past. The failure to recognize such important fact, that made the United States looked like the real aggressor, had weakened their case substantially. Mayor Takashi Hiraoka of Hiroshima discovered this fact

himself, after his overseas trips to expose the horror of the A-bomb victims of Hiroshima overseas, especially in the United States.

For some specific cultural reasons that I still do not clearly understand, it took very long time for some Japanese, especially the conservative government from the Liberal Democratic Party who monopolized the Japanese government continuously for 38 years to recognize the simple fact that they were the aggressor in the last War, even before the start of the World War II by direct occupation of their Asian neighbor's territories of Taiwan, other parts of China and the whole Korean peninsula. This fact was reflected in the dragging debate of the lower house on the war resolution for the 50th year anniversary, to mark the end of the Pacific War.

Of course, the Liberal Democrat and the New Frontier Parties combined had the majority in the lower house. It took the real courage of the Prime Minister Tomiichi Murayama of the Social Democrat Party of Japan who made the clear statement on August 15, the 50th anniversary of Japanese official surrender, to admit clearly that Japan pursued a mistaken national policy and offered his heartfelt apology to all parties who are victims of the Japanese war of aggression. His part of the contribution is really significant for future development of Japan. Without his leadership as a Chairman of the Social Democrat Party of Japan and as the Prime Minister, this significant statement at the most opportune time would have never been made. With such open admission of the past guilt, future relationship between Japan and her Asian neighbors as well as the rest of the world is expected to be made in a much more sincere basis.

On the economic front, too strong yen also cause some concern for the United States. It has been a general concern on one hand that the high value of Japanese yen will boost the country's import prices causing inflationary pressure to the seemingly well performed economy. On the other hand the long depressed Japanese economy could pull the U.S. economy into depression as well.

Various attempts especially through the joint effort of the Federal Reserves of the United States and the Bank of Japan to absorb some amount of dollars out of the circulation and injection the yens into the market instead. The real joint effort began after the conclusion of the historic dispute on automobile between the United States and Japan on the June dead line. The market immediately responded to the action by reducing the yen value from the one close to 80 yen per one dollar to lower value that was closer to 85 yen per one dollar. With sentimental change in the market, the joint effort by the two government to weaken the yen further began to take effect. After the announcement of the Finance Minister Masayoshi Takemura a nine-item package featuring deregulation that could encourage Japanese institutions such as insurance companies to invest more heavily overseas, possibly in U.S. Treasury bonds, and to extend more loans to borrowers in foreign countries, on August 2, had caused further surge in dollar to the new record of higher than 90 yen per one dollar. The weak yen stimulated the Nikkei to surge almost 250 point to the new level of close to 17,000 yen on the same date.

Since then, the dollar continued to climb over the rate of higher than 90 yen per one dollar. On Wednesday, August 16, the dollar at one time hit the record high of 99.05 yen per one dollar pulling the Nikkei up to a new record of 18,158.73, the surge of 706.01 point in one day. It was explained later that such rapid increase in that particular day was due to the coordinated dollar buying by the authorities of Japan, the United States and Germany. Major export industries especially those of automobile welcome such favorable change. There has been some renewal of optimism about the chance for the economy to move out of the existing recession. Some analysts predicted the dollar may surge

further to 100 yen mark, and perhaps move a little further beyond the point, then sagging again to finish the year at around the range of 95 to 99 yen per one dollar.

Contrarily to the new resumption of hope by some business analysts, academic economists do not normally give much weight to the strength of the dollar through government intervention by buying up dollars. The reason is that the foreign exchange market is now too big for even a combined effort of economically powerful governments like those of the United States, Japan and Germany. Such combined action basically does not amount to any significant change in the existing nature of the problem, namely, the chronic trade surplus of Japan and chronic trade deficit of the United States.

The current situation is hampered further by the fact that most Japanese banks are now suffering from very weak financial positions, due to the accumulation of huge amount of non-performing loans caused by asset deflation after the burst of the bubble economy in Japan, as well as the deflating market of properties overseas, a significant proportion of them owned by Japanese businesses and individuals who, in turn, borrowed money from the banks. As the banks must recall their loans back in yen, more dollars are forced to be released into the foreign exchange market, while the yen must be absorbed by the yen's hungry banks. As a result, the market is flooded with dollars while the yen must be accumulated by the banks. Occasional intervention of the foreign exchange market by coordinating purchase of dollars, by related governments in the long run will not alter the situation except to provide more yens and Deutsche mark, in case of the joint intervention by the German government too, into the hands of speculators. Such situation will enable them to make more profits in the next round of selling. Governments involved normally lose money in the longer run.

Differently from what I observed in 1975, in spite of much severe problems this time, the general mood of Japanese people in 1995 remains very calm without any sign of fear, uncertainty or insecurity and there has been no sign of panic what so ever. I guess, the Japanese economy and society have already developed to the point of maturity that the country already achieves a strong sense of confidence to overcome any kind of problems now, since the country has already amassed significant amount of property and wealth and already has a firm root as the leading economic super power as well as significant political power globally. These are sources of the strong confidence, currently.

What I have discussed so far, was sporadic experiences from my personal recollection from visiting Japan different times in the past until now, in various capacities. I feel that it is necessary to tell the story, because it gives me specific inside of the country I observed. My knowledge about Japan could have been different from reading what the others have said alone. These observations form the basis of my personal understanding of Japan.

To summarize what I have personally observed so far, Japan experienced rapid economic growth since the end of the War until 1973, with the average rate of growth close to 10 per cent consecutively for 16 years during 1955–1970. The said recorded growth was achieved not without problems and sacrifice. However, the problems such as environmental degradation and pollution were quickly overcome by succession of rapid growth. Since 1974, the country moved to the new stage of maturity in economic development with the average rate of growth during 1974–85, 4.3 per cent (Lincoln 1988). Such significant record of growth achieved during the 1960's was not without opposition, especially by sporadic groups who sought after alternative path of development. They were the ones who did not benefit as much from the growth or were harmed by the growth. Fortunately or unfortunately, they were tiny minorities and their voices of opposition were being suppressed very easily.

The gradually rise in value of the yen since the conclusion of Smithsonian Agreement in 1971, from

the pegged value after the War of 360 yen per one dollar to that of 308 yen per one dollar, and was peak after the G-5 Plaza Accord of September, 1985, to the record high of the average rate of 176 yen per one dollar during 1986, reduced the opportunity of domestic investment in plants and equipments significantly. The final result was further slump in the growth rate from 5.0 per cent in 1985 to 2.6 per cent in 1986.

The continued strength of the yen that reduced the option of domestic investment in plants and equipments, on the other hand, created a new opportunity for property investment, especially, overseas. This factor explained why Japan was heading for adventurous action in her investment behavior since 1987. Initial success in property investment overseas together with the desire to buy land properties domestically for future expansion of their businesses stimulated new sense of optimism, resulting in the inflated value of domestic property as well as value of stocks in the stock market. Such course of action originated the boom of what now known as the "bubble economy". The boom of the bubble economy reached its peak in 1988 with the recorded growth rate of 6.2 per cent and start to burst.

The completed burst of the bubble economy came in 1991 with the growth rate dropped to 4.0 per cent. Since 1992, the economy slipped into recession and it is stagnant until now, with some dim hope for revival after the recent upsurge in dollar, recently. Japanese economy virtually moved from maturity stage since the middle of 1970's to complete stagnation since 1992 with the rate of growth of 1.3 per cent that year followed by the rate of 1.1 per cent in 1993. The estimated rate of growth for 1994 was 1.0 per cent and the rate could be negative in 1995. Japan has now become a victim of her own past economic success. Actually, this phenomenon is hardly surprising at all. It is part of the economic forces globally, that make it much more difficult for any fast growing economy to continue growing at the same peak rate achieved in the past. They are the forces pulling towards global equilibrium. The forces accommodate more of the late coming ones in order to allow them to be able to catch up or at least to be able to move closer to the leading ones, the same way Japan was able to catch up with the United States from the much far behind position right after the War.

2. What's Next

Under the new circumstance, one may wish to raise the question of whether Japan can get out of the contemporary depressing situation and continue to grow at the steady rate of 2-3 per cent annually, without too much trouble of high unemployment rate, while being able to maintain good records on environment, as well as gradually improving the quality of life of majority of her people all the time. The wish stated above is actually the ideal path of development for a matured economy. Admittedly, without current depressing situation, Japan's economy is basically strong and healthy in comparison with most leading economies in the world. Right after the 1973/74 oil price shock, Japanese economy did very well in terms of her export performance, pulling herself out of the recession, creating trade frictions with the United States and the European Community (Nakamura 1981).

Against this background, Professor Lawrence Klein from the University of Pennsylvania then, who advocated for the locomotive theory and considered Japan as one of the three locomotives, the United States and Germany included, called for Japan along with the other two locomotives to strive to increase its domestic economy and contribute to the expansion of world trade by increasing their imports. Among the three Japan performed this role rather poorly in the past. Not less significance, Japan supported the development of the NIE's as well as many developing countries in Asia in the

past and is continuing to do so, by being a major provider of direct foreign investment and some degree of technological transfer, as well as to provide huge amount of capital to most capital starving nations especially in the area of infrastructure investment.

These roles contribute to growth stimulation of relevant countries greatly. Unfortunately, the end results may not be without problems. Those who did well, achieved such desirable results while major importing countries, especially to the United States has faced increasing problems of trade deficit. This situation, in turn, added more pressure to the existing trade problems between Japan and the United States. The only case that direct foreign investment will benefit all parties, in both short and long runs, is the one that generate production and consumption in the invested nation or the region, and does not result in hollowing out problem for Japan. For the capital imported nations of the long term loans, the continued rise in the value of yen resulted in increased debt burden. Such increase in the burden would be counterbalanced if the countries did well on the borrowed capital. Unfortunately, if they did poorly, the burden would be onerous. This is why the former role of being a locomotive for Japan can be more appreciative than the latter one, that can also be viewed as equally necessary. However, the latter measure should be more of the stopgap nature rather than a longer term one. Unless, the process has been carefully administered.

On the other hand, the United States used to play such useful role of being a locomotive to facilitate Japan's development right after the War, until the end of the 1960's. Without understand much of the underlined nature of the Japanese economy and its constraints, one inclines to question why Japan cannot perform the similar task at least for her other developing Asian neighbors the way the United States did for Japan in the past, as her economy now also reaches the state of maturity. Unfortunately, before Japan is able to perform such a useful role, she must first be able to rise from the current depressing situation. It now becomes very clear that any solutions for Japan are not only meant for her own economic good but it must be part of the global solution to economic ills. Any solutions for Japan, if they are aimed at achieving longer term economic stability globally, they must at least not cause any undesirable side effects to the rest of the world. At the same time the rest of the world must also try to understand some intrinsic problems of the Japanese economy, if any. Such problems may serve as significant constraints in preventing or preempting Japan from pursuing the course that seems to be best for her own development as well as that of the global economy.

Equally clear, is that the most desirable future for Japan and the rest of the world lies on her ability to get out of current situation not through the expansion of exports the way that she used to know and did well in the past, but through some forms of domestic expansion that she also used to perform well in her initial period of the development and the time between various export booms. The question of whether she is able to do that, or in the position to do so, requires more systematic analysis.

3. Factors Explained the Rapid Growth Period (1950-73)

Factors explain rapid economic growth can be classified into three major groups, domestic environment, international environment and growth stimulating factors. The groupings are designed to distinctive factors according to their prominent nature, in order to help sharpen further analysis on the subsequent development as some factors still hold true while the others have already been changed. Neither the factors classified are mutually exclusive nor they are not overlapped. The classification is only meant to facilitate the understanding of the development process more or less on sequential

basis.

4. 1. Domestic Environment

Domestic environment will be divided into economic factors, other related factors, factors imposed on Japan by outside forces of the Supreme Commander for the Allied Powers(SCAP) led by General Douglas MacArthur of the United States, and political factors.

Economic Factors: According to Professor Ryoshin Minami (1988), the industrialization of Japan began since the mid 1880's. The word industrialization implies the growth of mining, manufacturing, construction and infrastructure industries (transportation, communication and public utilities) and the increase in their share of the total economy. The pre-War average rate of growth of these industries combined during 1889–1938 was 6.34 per cent compared with 2.59 and 1.34 per cent for primary and service sectors, respectively. During 1930–38, the share of mining and manufacturing alone was already 50.5 per cent of all industries followed by construction 11.2 per cent, transportation communication and utilities 8.0 percent, while the share of service sector and agriculture was only 25.4 and 4.9 percent, respectively (Minami 1988). This set of figures indicate that Japan was already a strong industrialized country before the War. Otherwise, she could not have gotten into the War in the first place. During the War, many of these manufacturing industries were converted into armed, ammunition, and munitions industries. The war normally results in rapid improvement of technology. Industries which were expanded during the War became major postwar export industries; wartime technology was reborn in the postwar export industries (Nakamura 1981)

Other Related Factors: There have been arguments that “Japanese style of management” consisting of lifetime employment as well as continuous training for skilled improvement; and optimum scale of production together with complete flexibility to adapt new technology and to improve production quality, are among the unique quality of Japanese industries. This latter point is the whole industrial development thesis of David Friedman (1988) explaining a much greater ability to compete in the international market of the Japanese industries in comparison with their American counterparts. He cites examples of the machine tool industry, automobile industry, banking industries and oil industry. He argues that during the high growth period, small and medium-sized manufacturers increasingly assumed larger roles in Japanese industry. Japanese competitive strategy in domestic and global markets was shaped by an effort to break up mass market into smaller, specialized segments through continuous product modification and new product development. The fact that there was dramatic expansion of smaller producers, because they were able to implement more flexible strategies than the firms that pursued mass production alone (Friedman 1988).

The fact is that Japan has all ranges of firm sizes, few very large ones, a little more of large sizes, and a lot more of medium and small sizes. The subcontracting systems link all sizes of firms together as part of the “Japanese style of management”. According to Professor Nakamura, it was part of a wartime phenomenon. Large firms in the military industries had at first made it a rule to produce everything in-house, including parts. They developed a system of subcontracting parts and other work out to small and medium-sized firms as an emergency measure to facilitate production increases. This practice honed the small firms' skills and was an opportunity to raise production standards (Nakamura 1981).

The seniority wage system and lifetime employment system first took shape during the depression

following World War I, primarily in the chemical and heavy industries; but their expansion into nation-wide system was due to the implementation of wage controls in 1940–41 (Nakamura 1981). This system allow firms to adjust wages much more flexibly especially at the time of depression when downward adjustment or at least wage fixed is required. This fact explains why Japanese firms can compete vigorously during depression and right after. Lifetime employment together with loyalty to the firms by employees make it practical for the firms to provide all kinds of training to employees, in order to improve their productive skills, the source of continued improvement of Japanese manufacturing industries, especially during the rapid growth period.

All factors discussed above explain the continual improvement of productivity of industries in Japan, required to maintain their up front position in competition in global markets. Last but not least is the Japanese system of education, especially at the secondary level. Heavy regimentation of the educational system with strong emphasis on competition, discipline and sciences and technology has continuously turned high school graduates to be best inputs into Japanese industries, especially during the rapid development period.

Factors Imposed from Outside : Imposition by the Supreme Commander for the Allied Powers (SCAP) was aiming at democratization of Japan. In Part Four of the Post-Surrender Policy, entitled “Economy”, the following can be summarized.

First, in the interest of “economic demilitarization”, the suspension and prohibition in future of military production, a ban on fleet and aircraft facilities, restrictions on the nature and scale of heavy industries, and restrictions on merchant vessels are set forth (Nakamura 1981). This clause resulted in significant amount of military expenditures being saved for the whole period of after the War until the end of cold war in the late 1980's. Under such circumstance, Japan was able to enjoy Pax Americana without participating. Japan was automatically covered by American nuclear umbrella for defense, a very effective deterrence for her very low military cost. This must be amount to trillions of dollars of savings for Japan (Woronoff 1992). Such amount of money can be used for infrastructure investment and other activities directly or indirectly to stimulate growth.

Second, in the interest of the “promotion of democratic forces”, provision was made for the promotion of labor unions and agricultural associations. The next step is the “elimination of concentration” in production and in property rights in the broad sense (Nakamura 1981). The main purpose is to eliminate monopoly in order to generate more competitive environment as well as more even distribution of wealth. Effective actions were in the form of breakup of the *zaibatsu*, the practice of few oligopolistic firms before and during the War, and land reform. The breakup of the *zaibatsu* set the scene for more intense competition among industries, particularly chemical and heavy industries. This produced good market mechanisms and was powerful factor generating rapid growth after the War. In case of land reform, it contributed to the reduction of tenant farmers from nearly 50 per cent down to about 10 per cent. Also the land reform had the effect of rapidly increasing the productive capacity of rice growing land in such area as Hokkaido, Tohoku, Hokuriku and Tozan generally the northeast half of Japan where landlords had been especially powerful (Nakamura 1981). Rapid increase in agricultural products, especially rice, through rapid increase in productivity contributed to stimulation of industrial growth in two ways. First, increased purchasing power of farm population implied larger domestic market for manufacturing products. Second, more farm workers could be released for the expansion of non-farm sectors.

Apart from major interventions engineered by the SCAP discussed above, there were one abstained

action by the United States and two other forms of intervention that contributed to rapid growth that should also be mentioned. Unlike Germany, Japan was only asked to pay a token sum for war reparations. Such exemption enabled Japan to use the funds to generate her own growth (Woronoff 1992). The other was the implementation of the Dodge Plan in 1949 that imposed strict fiscal and monetary measures on Japan in order to stop the likely course of runaway inflation gathering strength right after the War (Nakamura 1988). Not less significant was the quelling of potential strong labor movement and the acquiescing of political firings the “red purge” in 1949, after promoting freedom for unionization right after the War (Nakamura 1981). Such actions allowed management to regain control over their employees as well as more stable political environment. All the interventions and one absence of it mentioned above, have set the scene for subsequently rapid development of the Japanese economy until the mid 1970’s.

Political factors : Strong group spirit has been a part of Japanese cultural heritage for quite some-time. This spirit must have been most strong after being defeated in the War. The inner desire to unite and rebuild the country from terrible war torn situation must have been very strong. Rapid revival economically in order to make up for the loss of time during the War might have been the strongest aspiration among the Japanese then. Naturally, strong growth attitude prevailed among Japanese people as national consensus should come with no surprise. Any government that could maintain good record of growth must be very popular for the Japanese at least for some initial period of time. As a result, Japan had at least four strongly pro-growth governments in the past led by three leaders that were closely connected politically. They were Shigeru Yoshida (1946–47) and Shigeru Yoshida (1948–52), Hayato Ikeda (1960–64) and Kakuei Tanaka (1972–74). While Ikeda was Minister of Finance during the second period of Yoshida premiership, Tanaka was the Minister of Finance of Ikeda.

Since the 1955 political realignment and reorganization, there was a clear emergence of a two party system, the Japan socialist Party (JSP) and the Liberal Democrat Party (LDP). The pro-growth party of the LDP always won the election and formed the government leaving the JSP became natural opposition. The LDP enjoyed monopolizing power as government until the collapse of the 1955 structure in 1993, as Prime Minister Kiichi Miyasawa failed to implement electoral reform coupled with cases of corruption within the LDP. The incidence resulted in the passage of the vote of no confidence in the government proposed by an opposition supported by a revolt reformed faction of the LDP led by Morihiro Hosokawa. Hosokawa later formed Japan New Party, seizing the opportunity that the LDP did not win the majority to form the coalition government supported by seven-party/one-faction grouping on August 9, 1993 (Sakura Bank 1995). The LDP was in power for the total of 38 consecutive years. Such phenomenon reflects the long standing of pro-growth attitude of the majority of Japanese people as well. T. J. Pempel (1982) called this type of politics as “creative conservatism”.

In his book of *Policy and Politics in Japan : Creative Conservatism*, Pempel (1982) explained how conservative politics in Japan could attribute to growth by way of international comparison with other advanced countries such as Britain, the United States, Germany, Sweden and France. In Japan, the state took much more aggressive role in enhancing industrial development than most industrialized countries, to be justified by the notion of state-led capitalism, while Germany, Britain, Sweden and France to a certain degree were more inclined to pursue the policy of welfare state. The United States, on the other hand, was more inclined to follow a policy of free enterprise limiting the role of the government to only regulating fair plays.

Because of the said role committed by the Japanese government, and the so called “red purge” since 1949, the role of labor movements were confined only to the area of improving their own welfare such as higher wage, better working condition and environment, more social securities and benefits. Workers had never been so strong as to have any share of government political power. Not like their counterparts in Europe, where labor did gain some control over the government, in the form of Labor Party as the case of Britain and some forms of socialist parties in other European countries. The relatively weak labor movements in Japan resulted in the re-enforcement of the policy of state-led capitalism of the government, without much chance of occasional reversal to that of the welfare state, experienced by most leading European nations. As a result, the Japanese government had comparatively poorer social welfare records in comparison with its European counterparts. Similar things can be said on its spending on higher education and its environmental records.

With some exception on its environmental record, the LDP was initially very slow to react definitively to solve the problem. Itai-itai disease caused by cadmium in rice was first noticed in 1955 in Toyama Prefecture in 1955. Yokkaichi asthma, a lung ailment, was the result of complex smoke and soot emissions in the city of Yokkaichi. Minamata disease, which destroys the brains and nervous system, was first recognized in 1956 in the city of Minamata (Pempel 1982). Factory effluent, smoke and foul odor could easily be detected in industrial areas in most parts of Japan, in the 1950's. The government asked people to contemplate the problems as necessary costs for growth.

The fight against all forms of pollution was in the form of citizens' movement, organized pressure groups united by place of residence and/or common suffering from specific pollutant were the key elements. The media, the courts, and local governments were often important channels through which these groups could exert their political influence (Pempel 1982). As the mass media continued its drumbeat for action and as the LDP continued to lose seats in what were once considered invulnerable areas, the government once again seized the initiative in the so called pollution Diet in 1970. During a special session, fourteen major pieces of environmental legislation were passed at the government's behest (Pempel 1982). Once it decided to tackle the problem, the Japanese government did so well to surpass record of most industrial nations in terms of pollution free industries. This attempt resulted in strong competition of exports from Japan, at the time the world has been more conscious about environmental protection in the 1980's. At the same time, the increasing costs of pollutant prevention in Japan partially caused the slowdown in development of the economy in the 1980's as well.

Slightly different explanation made on similar point by Chalmers Johnson (1982), who explained the main factor responsible for rapid growth for Japan was due to the fact that the Japanese government followed the policy of “economic nationalism”. Differently from any totalitarian regime, that the state directly engages in production and distribution, being a democratic country operated under capitalist system, the Japanese state only engages in production and distribution some key industries and public utilities. The rest are allowed to function competitively through market mechanism. The main function of the state is to guide or coordinate them to “cooperate” with each other as well as with the state in order to avoid excessive or wasteful competition. This form of guidance by the state is known as a “plan rational”. The state can achieve the objective of this plan rational through its most talented and able bureaucrats in coordinating government and private activities according to the plan. Unique system of education and specific cultural practice contribute to the success of the plan rational.

All human relations in Japanese society are based on four kinds of “function” (*batsu*): *keibatsu* (family and locality), *kyodobatsu* (clansmen, or person from the same locality), *gakubatsu* (school and

university class mates), and *zaibatsu* (factions based on money). Within the Japanese bureaucracy the first two are of minor importance (Johnson 1982). The said relations are exploited by the bureaucrats to coordinate plan rational approved by the government and closely followed by private sectors. Among these networks, the most importance of all is the “old boy” or clique of Tokyo University classmates (*Todaibatsu*), particularly, the top elites of them are the alumni of the Tokyo University Law School (Johnson 1982). These top elites normally work their way up to top positions in various ministerial posts of the Japanese bureaucracy upon their graduation from the University. Among the top ones who control Japanese economic policy are Ministry of Finance, Ministry of International Trade and Industries, the Economic Planning Agency, Bank of Japan and the Ministry of Foreign Affairs.

After reaching their top careers as government officials, some will seek to move further into political profession, running for the election as members of the LDP and normally secure various positions of the Cabinet Members afterwards. Many Japanese prime ministers in the past like, Yoshida, Kishi, Ikeda, Sato, Fukuda and Ohira reached their top posts this way (Johnson 1982). The others may *amakudari* (descent from heaven) to top positions in state enterprises and private sectors prior to or after their retirement as bureaucrats from various ministries. The whole process explained how the Japanese government, the bureaucrat and the private sector are cooperated closely in their economic activities. Under these specific relations and institutional setting that the plan rational under the system of democratic capitalism can function smoothly, according to Johnson (1982).

Among various concepts of rational often used in government official rhetoric, the most important one according to Johnson is the so called “industrial rationalization policy”. The term industrial rationalization implies state policy at the micro level allowing state intrusion into the detailed operations of individual enterprises with the measures intended to improve those operations or, on occasion, to abolish the enterprise (Johnson 1982). Of course, the powerful Minister of International Trade and Industry (MITI) has been responsible for this policy. The successful performance of Japanese industries during the rapid growth period (1950–75) led Johnson to conclude that the MITI played significant role contributing to rapid growth of the Japanese economy. Consequently, top elites of the MITI’s bureaucrats deserve the credit.

Unfortunately, the Johnson’s thesis did not stand up to the test to explain why Japan did moderately during the maturing age of development (1976–1991) and has done rather poorly since then until now. However, his elaboration on the nature of close connection among the government, the bureaucrats and the private sector as a result of unique institutional and cultural factors in Japan under specific situation, apart from other factors, explains why the LDP could held on to the power as the government in Japan for too long period of time. Their obsessive concerns on growth performance of Japan backup by the work of MITI’s bureaucrats as well as big business organization, apart from other problems to be discussed later, has caused constant trade frictions against the rest of the world that has led to too rapid increase in the value of the yen resulting in current situation of a rather long recession. Yet, there seems to be no simple measures to solve the existing problems. Part of the reasons is simply because the same set of policies has been carried out repeatedly far too long.

For more interesting analysis that can actually explain the performance of Japanese economy during the rapid growth period (1950–1975) and its aftermath, the overall implication of Pempel’s thesis of the so called “creative conservatism” will be now discussed. One of the main consequence from the said government policy during the 1950’s and 1960’s was that, in addition to spend little portion of

the budget for defense, the government did not have to deal with militant labor unions. It did not spend much on social welfare, higher education and the costs for anti-pollution measures, at least before 1970.

As a result, the government could spend more time concentrating on its growth objective as well as to be able to invest much more physical infrastructure and other related activities to stimulate growth and exports of manufacturing goods. Meanwhile, most Japanese with only little benefits of social welfare and must cope with increasing costs of education and housing with very low rate of pension after the compulsory retirement age of 55 then, had no other alternative but to save as much as they could while working. They could not afford to be unemployed because they would be paid only little sum from unemployment benefit. They had no other choice but to work hard and save a lot, to fend themselves against any unforeseen eventualities. This fact explains why the rate of personal savings in Japan is the highest among most advanced nations.

The high rate of savings, on one hand, was siphoned back by various forms of financial institutions, a well known one is the post office, mutual savings bank (*sogo ginko*), and credit association (*shinyo kinko*). Together with the government policy to encourage these institutions to lend money to industries of all sizes by receiving the strong backup from the Bank of Japan and the government. While the Japan Development Bank has been established to help finance key industries, small and medium scales industries never suffered from the problem of lack of funds. They have been financed by People's Finance Corporation and Small Business Finance Corporation, respectively (Nakamura 1982). This fact explains why many of them have been thriving in Japan. On the other hand, high rates of savings will only function well for Japan and the rest of the world, when it is supplemented by high rate of investment in plant and equipments domestically, together with equally high rate of imports when the rate of exports is also high. Soon as exports flourish while imports cannot keep pace with them, foreign exchange surplus will be inevitable.

This policy is known as beggar thy neighbors or simply as exporting unemployment to the others. As foreign exchange surplus becomes chronic, there will be strong political pressure from the rest of the world to buy more, or else Japan must appreciate her currency. This has been a chronic problem for Japan with the rest of the world since the beginning of the 1970's. While the yen has been upward adjusted constantly, there has also been continuous pressure overseas for Japan to open up more of her supposedly "close" markets, since 1970. As the policy by the conservative government did not change much, every time there was significant upward adjustment in the value of the yen, Japanese manufacturers must improve their efficiency further by improving energy efficiency, replace human employees by robots, slow down the wage increase, exploit their subcontractors heavier. In the end, they always came up with more exports in spite of the appreciation of the currency. The logic for the said adjustment of Japanese manufacturers was that with the system of lifetime employment, if they wanted to survive in the longer run, they had no choice but to keep the businesses. Otherwise they must be out of businesses altogether. This practice in the long run only exacerbates the problem.

The so called creative conservatism policy of the Japanese government certainly worked well during the rapid growth period of the 1950's and the 1960's, because during that time, imports also grew at roughly the same rate as exports. Soon as imports grew at a much slower rate than exports, the problems explained above emerged. The main feature of the functioning of Japanese economy discussed above, has been basically responsible for the slowdown in growth of the Japanese economy since 1974 and the currently long recession, starting from 1992.

This study by no means suggests that Japan should trade off the nature of her forced saving virtue for the so called welfare state which is also proven to be less efficient, economically. Also, the concept of welfare state could also invite whole host of many social problems never experienced in Japan, to name a few, welfare induced unemployment, a problem of young single parent-young women in particular, the problem plagued American people currently. There are problems of loneliness and alcoholism caused by the complete break down of communal and family relationship, because personal security financially is guaranteed by social insurance. These problems alone will result in many forms of criminal acts and many other forms of social diseases. At the same time, Japan cannot afford to allow the protracting problem ruin her economy and the welfare of her own people. Solution that will be useful for Japan as well as the rest to the world, must be sought after finally.

4. 2. International Environment

From 1950 to the early 1970's Japan's economy was also stimulated by the following series of external events, the Korean War during 1950-51, the general rapid growth environment internationally especially from 1950 to the mid-1960's, and the Vietnam War from the mid-1960's until 1975.

Korean War : The broken out of Korean war during 1950-51 provide significant boost to the Japanese economy at the time the country was in badly needed. After a series of high rate of inflation after the War, due to rapid fiscal expansion as part of the government effort to pull the country out from the war torn situation, together with the Dodge Plan in 1949 with the aim control inflation through strict fiscal and monetary measures, the country was almost swung back into recession. The Korean war resulted in 23 per cent rise in the unit price of world exports. Exports from Japan jumped in response to the rise in international prices, and along with them production, employment, and business profits all rose rapidly as the economy surged forward into a boom (Nakamura 1982).

Favorable International Environment: The 1950's and the 60's were generally known as the golden age of global development. According to the United Nations statistics, the global gross domestic product (GDP) from 1950 to the mid-1960's grew at a rate about 5 per cent; even when Eastern Europe and the former Soviet Union were excluded, the rate was still high, about 4.4 per cent. Such rapid growth globally was due mainly to the revival of most economies right after the War spurred by very low cost of energy especially oil, and also relatively low resource costs. Developed economies normally gained more from the low prices of both energy and resources. The accession of advanced technology worked to their advantage. After Korean war Japan was able to catch up with advanced technology and was in a good position to compete with other developed nations for cheap manufacturing products then. Hence, she also benefited from such globally favorable environment.

Vietnam War : Soon as the brisk global performance began to subside, the United State had started full scale military operation in the Vietnam war. Such evil war lasted for at least 10 years, ending in 1975 with the complete withdrawal from the war by the United States. During the war, massive outflows of the U.S. dollars floated into global economy at accelerated rate as the war became intensified. By that time, Japan was able to catch up with most advanced technology. At the same time, the yen was already undervalued because of the pegging rate of exchange of 360 yen per one dollar. The German government already made upward adjustment of the Deutsche mark since 1961. Japan, then, had the competitive edge over the relatively low value of her currency as well as the technological edge. She was ready to compete in markets of quality products worldwide. Such massive influx of

the U.S. dollar into the world economy, helped perpetuate growth of the Japanese economy further into the early 1970's.

4. 3. Growth Stimulating Factors

Under such favorable environment both domestically and internationally, Japan must bound to perform well. Nevertheless, without some crucially intrinsic factors, the country could have missed the good opportunities. As already pointed out the pro-growth Japanese government of the LDP that enjoyed strong support from Japanese people for long period of time, should also received credit for the country's growth performance. Among its past activities already discussed, were its policies and effective measures to squeeze massive amount of savings from its people and to transfer the savings into very useful investment without any waste. The series of tax reform during 1951-53 resulted in the promotion of plant and equipment investments, and exports. The foreign exchange allocation system inaugurated in 1949 designed to restrict the value of imports turned out to be one of the good protective measures of local industries, while they were still not strong enough for external competition. The government also played decisive role in promoting of imports of foreign technology at the time needed by engaging in technological cooperation overseas and giving protection for the imported technology to related firms (Nakamura 1982).

The study of Denison and Chung (1976) on sources of growth of Japan during 1953-71 revealed interesting pattern.

Table 1 Japan's Economic Growth

<i>Sources</i>	<i>Contribution to growth</i>
National income growth rate	8.77
Labor	1.85
Employment	1.14
Hours	0.21
Age-sex composition	0.14
Education	0.34
Unallocated	0.02
Capital	2.10
Inventories	0.73
Nonresidential structures and equipment	1.07
Dwellings	0.30
International assets	0.00
Land	0.00
Productivity change	4.82
Advanced in knowledge and "not elsewhere classified"	1.97
Improved resource allocation	0.95
Economies of scale	1.94
Irregular factors	-0.04

Source : Hugh Patrick and Henry Rosovsky (eds.), *Asia's New Giant: How the Japanese Economy Works*, Brookings, 1976, p. 94.

The results in the table above indicate that labor contributes to the total growth rate of 8.77 per cent by 1.85 percentage points. Capital contributes 2.10 percentage points while land do not contribute to any. The biggest item of all is productivity change 4.82 percentage points. As for the sub-item of labor, employment contributes to 1.14 percentage points as a result of reduction in unemployment as well as increase in labor forces of a post war baby boom. The largest sub-item of the contribution of capital is non-residential structures and equipment, with the total contribution of 1.07 percentage points. Inventories play subsidiary role, and the contribution of housing is only moderate.

The most interesting sub-item of productivity change is advances in technology or what Denison and Chung call advances in knowledge, with the total contribution of 1.97 percentage points, followed by economies of scale 1.94 percentage points. The improved resource allocation, or the ability to move labor out of the less productive sector of agriculture to the higher one of non-agriculture, or manufacturing in particular, contributes to growth during the said period by 0.95 percentage points.

In conclusion, the stars of the growth performance during 1953–71 for Japan were rapid improvement in technology, a wide range of firm size allowing for more flexible in production resulting in economies of scale, investment in plants and equipments, and the ability to increase labor productivity by constant drawing labor from agricultural sector. Not much contribution was from investment in housing and education. Contribution from foreign asset was nil, since Japan had little amount of foreign asset then. The above findings are quite significant because it does not only explain the factors contributed to growth during the rapid growth period, it can also explain why growth has been slow down in subsequent period, the matter to be discussed more comprehensively later on. At this point the figures are only use to draw attention on growth stimulated factors.

The true growth engine in this case is the fact that Japan lagged far behind the industrial countries in technology in the 1950's and 1960's and her ability to absorb new technology from abroad (Ohkawa and Rosovsky 1973). In order to explain the process sequentially, one must start from the Korean war boom. The boom resulted in the surge of export from 510 million dollar in 1949 to 820 and 1,355 million dollar in 1950 and 1951, respectively. The new source of foreign exchange was from the expenditures of the U.S. Army and military personnel-the special procurement reached the sum of 590 million dollar in 1951 and over 800 million dollar in both 1952 and 1953, or 60 to 70 per cent of total exports (Nakamura 1982).

The two items combined enabled Japan to spend about 2 billion dollar annually on imports. Part of the money was used to buy cheap raw materials and energy, the rest was spent on imported technology in the forms of royalty fees and new plant and equipment investment. With strong encouragement by the government and aggressive business management practice among the rising new generation of business managers resulted in continuous inflows of new technology and continuous expansion of businesses through more investment in plants and equipments. During 1951 to 1973, plant and equipment investment grew at the rapid rate of 22 per cent annually (Nakamura 1982). Excessive surplus of foreign exchange was not a problem during that time because it was used mostly for imports. This fact was also captured in Denison and Chung's study (1976) in that there was no contribution from foreign asset. The flexibility in scale of production, a unique feature of Japanese industries enhanced their competitive edge further. Rapid expansion of industries especially manufacturing industries enabled more labor to be drawn out from the agricultural sector, another significant factor contributed to growth during the rapid growth period.

Having discussed most significant factors contributed to rapid growth for Japan during 1950–73, it

is no longer difficult to understand why economic maturity finally set in. This can be done simply by checking the list of pro-growth factors and find out which ones are still true and which ones are not in subsequent period. The more the growth generating factors are weakening, the closer to maturity of the economy. Obviously, when the economy reaches the level of maturity, the government policy must also change accordingly. Otherwise it will result in wasteful usage of energy and resources. At worse, it will cause more economic problems as well as economic depression resulting in welfare losses to the public in general.

5. Reaching Economic Maturity (1974–86)

Japan did well on her growth performance up to 1973 as the rate of growth that year was still as high as 7.9 per cent. Sharp reduction took place in 1974 as the impact of the oil price shock of the 1973/74 affected her economic performance, severely. The growth rate turned to be negative for the first time after her long growth experiences (1950–73) at the rate of –1.4 per cent and consumer prices were up 24.5 per cent (*Nihon Keizai Shimbun* 1974). The situation was hardly surprising since most developed countries suffered the same consequence at the same time. However, for Japan she fell from a much higher platform.

Japan had experienced hyperinflation of 200 per cent a year and higher right after the War. Such experience still haunted her in 1974. Inflation was quickly contained in 1975. This unpleasant experience affected Japanese policy later, with greater weight given to controlling of inflation as less to stimulating demand (Lincoln 1988), one of the factors that led Japan to depend more on export led expansion, than rapid expansion of government expenditures at the time stimulation policy is needed. Such general attitude added extra pressure on exports that resulted in more of that to the already existing problem of trade surplus, the source of excessive balance of foreign exchange reserves, that lead to the perpetuated problem of the appreciation of the yen.

Since 1975, growth rate in Japan never increases beyond the rate of 6.2 per cent which is the highest rate achieved in 1988. Most of the time growth rate bounces between 4 and 5 per cent annually (ASEAN Centre 1995). However these rates should be considered much better than those of most matured economies in Europe and North America. Anyway, the sharp break from the high growth path of the 1950's and the 1960's in 1974 is not unexpected. The only unexpected part is the oil price shock. Without such a shock, the trend for eventually slowdown of the Japanese economy can clearly be detected from some factors in the check list discussed above. For the sake of consistency in the analysis, the said check list will be re-examined again.

5. 1. Domestic Environment

Again starting from economic factors, the star performer of Japanese industries before the War as well as during the rapid growth period has always been manufacturing industries. During matured economic period, this sector remain to be the most important sector for the development of the Japanese economy but its significance decreases gradually. After the post-war peak of 34.6 per cent of the GDP in 1970, its share reduced to 29.8 in 1980 (Minami 1986).

For other related factors, especially the one under the heading of Japanese style of management, senior wage system and lifetime employment may no longer be the advantage. Senior wage system

can induce inefficiency. However, in the past this system was a good substitute to government welfare system inadequately provided. Private sectors were implicitly asked to shoulder the cost while the government could concentrate its effort in promotion of growth. During the period of slowdown in growth, it is no longer good idea to ask private sectors to shoulder this implicit cost. Unfortunately, the absence of proper welfare scheme on part of the government, will result in welfare loss to affected individuals directly.

Lifetime employment is still relevant if it provide extra flexibility for the firms to make adjustment during the slowdown period as well as the aftermath. Similarly, it is also a good welfare system when unemployment benefit provided by the government has been rather insufficient. The overall merit of this system of lifetime employment to the firms involved during the slowing down period is rather unclear.

Another part of the so called Japanese style of management through the system of subcontractors taking the advantage of wide range of firm sizes, is obviously still the advantage that contribute to the flexibility of the whole industries as well as the economy of scale. This factor is still a strong contributor to the overall industrial performances of Japan.

Factors imposed from outside is no longer relevant in the discussion, after the conclusion of the Peace Treaty of San Francisco in September of 1951. However, the conclusion of the Japanese-American Security Pact of May 1952, resulting in very small portion of the government budget allocated for military purpose is still an effective tool enabled the Japanese government to use the remaining sum for stimulating the economy.

As for political factors, the policy of creative conservatism is no longer relevant. Deliberated government policy aiming at massive amount of forced savings from the general public results in too high rate of savings especially during the slowdown period. Too much savings while plant and equipment investment slow down to the rate of 3.9 per cent annually during 1974-85 (Lincoln 1988), coupled by conservative fiscal policy, creates a great deal of pressure on exports, followed by continuous problems of excessive surplus of foreign exchange balance. In sum, the policy is more harmful than useful. The close and strong link between government as well as political parties, bureaucrats and private sectors explained by Johnson (1982), makes it much more difficult for such conservative policy of the government to be changed. As a result, in 1976 and 1979, the LDP could no longer retain its majority position but was able to form the government by the support of independent candidates elected after the election (Lincoln 1988). The complete setback of the LDP took place in 1993.

5. 2. International Environment

Series of war that will directly benefits growth of the Japanese economy in the future is not likely. The more likely scenario on wars in the future is that at least Japan will be asked to share the costs. Also with continual deterioration of global environment, relatively more scarce of supplies of resources and energy, and economic maturity of most developed nations, it is hardly conceivable that the golden age of global development experience during the 1950's until the mid-1960's will ever return in the future. Although trade relations with other East Asian nations and Japan are increasingly important for Japan in the future, given the fact that these countries are now fast growing, the trade volume still cannot be matched with that of Japanese trade with the United States alone, at least in the near future. For example, in 1993 the value of Japanese exports to the United States was 106.9

billion dollar, while total exports to the whole ASEAN in the same year was only 55.7 billion dollar (ASEAN Centre 1995).

Not in a far distant future, these countries must be in direct competition with Japan in acquiring resources and energy for their own countries' development. They also wish to sell more than to buy from Japan. This scenario will make the policy of export led growth for Japan, in the future, become much more difficult than it is now. Other fact to be noted is that when Japan was economically small in the 1950's, her exports could expand rapidly without making much difference in world markets. But by the 1970's her exporting industries were important enough to represent a significant factor in the world markets (Lincoln 1988). This factor will severely limit the export led growth of Japan now, and more so in the future.

5. 3. Factors Explaining the Slowdown

The true growth engine of the 1950's and the 1960's of rapid advancement in technology did not prevail any longer, as Japan has been very close to most technological frontiers since the beginning of the 1970's. According to *Japan Marketing Handbook* (1988), Japan has already achieved two major areas of technological progress: firstly, highly systematized technologies such as nuclear fusion reactors, the construction of ocean-based cities, and the use of super-conductive materials in macro-engineering field; secondly, life sciences such as biotechnology and bio-electronics (Euromonitor Publication Limited 1988). Unfortunately, these high-tech industries only accounted for 6.1 per cent share of industrial output in 1985 and expected to increase to 8.5 per cent in 2000. Contribution to growth of these industries will be only minimal. While the cost of research and development is rather high, the net contribution to growth of the development of new technology will be very small. Unlike the time of technological lag, the gain from improvement was substantial, especially for Japan, while the cost for imported technology was still very low in comparison with the cost for the development of her own. The fact that Japan already reaches most technological frontiers is the major factor explaining the reaching of maturity of the Japanese economy.

Reconsidered the factors contributed to growth by Denison and Chung (1976), and assumed the period to be the 1980's instead, one will anticipate that most figures of growth contribution will be less than before, except some. Starting from the figure of employment, because of the slower growth in birth rate since the early 1950's, labor force participation rate during 1974-85 reduced to 1.2 per cent from the earlier rate of 1.8 per cent from 1955-73 (Lincoln 1988). Under such circumstance, the contribution of employment must be less than 1.14 percentage point during the 1980's. Contribution by hours of works should also decrease due to general trend of less hours of works, although not so rapid reduction in case of Japan. The other sub-groups under labor are not so important. The total contribution from this group must be lower than before.

As for capital, the slowdown of plant and equipment investment discussed earlier must definitely result in the reduction of the contribution to growth of the nonresidential structure and equipment item. The contribution of dwellings and international assets on growth would definitely increase in the 1980's. As a result, the total contribution of capital to growth may be close to the previous figure of 2.10 percentage point.

Under the item of "productivity change", there must be considerable reduction. The sub-item of advanced in knowledge and "not elsewhere classified" which represent contribution from rapid techno-

logical progress would reduce significantly. The contribution from improved resource allocation would simply disappear, because further reduction of labor in agricultural sector was no longer possible. The part of the economies of scale could be unchanged, because Japan still maintain the said advantage. However slight reduction due to increasing competition from other Asian nations was also possible. In sum, the total contribution to growth from productivity change must be less than half of the 1953–71 figure of 4.82 percentage point.

The new sum of the contribution to growth of all the factors discussed should be in the range of 4 to 5 percentage point, the same as the average rate of growth achieved during 1974–1985. This rough re-estimation of the Denison and Chung's figures for slow growth period help explain how the Japan's economy moves from the rapid growth period of the 1950–73 to the new position of 1974–1985.

5. 4. Other Related Factors

The gradually decline in its popularity due to the Party's poor records on environment resulting in losing seats in many used to be safe districts since the late 1960's, made the LDP to reconsider its strongly pro-growth position. There were also demand for increased investment in better roads, better housing, and other amenities (Lincoln 1988). There was a great shift in basic development goal during Sato's Cabinet (1964–72) in May 1969 from the one of the Ikeda government (1960–64) where the emphasis was on twofold increase in income. The new goal was the creation of nice living environment: (1) harmony between man and environment, conservation of nature, (2) preparation of basic conditions for development of all regions, (3) more efficient use of land and utilization of local advantages, (4) development for safe, comfortable, and cultural environment (Cheung 1994).

Since the Diet passed the pollution control legislation in 1970, the government expenditures for this purpose increased four times in 1973 from the 1970 figure, the total amount of 430 billion yen. Regional and local government spending rose to 954 billion yen. Expenditures by private sectors also rose by twofold during the same time. The distance of road paralleled by side walked doubled between 1970 and 1975, and almost doubled again by 1981. Total area of local parks doubled from 1970 to 1981. The percentage of households with telephone service between 1970 and 1980 tripled from 25 per cent to 77 per cent. In the area of housing, the amount of space per person increased steady from 14.5 square meters per household member in 1958 to 25.6 square meters by 1983 (Lincoln 1988). Housing improvement appeared to be the slowest of all, due to high price of land resulting from the nature of general limitation land space of the country.

With significant amount of resources devoted to activities that would directly improve the quality of life of most Japanese people by both the public and private sectors, fund available for direct expansion of production must be greatly reduced. Nonetheless, expenditures on the said items were necessary at the time for the real reasons, not only for the government to regain the losing support. They can be viewed as the effort to maintain high productivity of the Japanese workers before it could be greatly reduced from exhaustion resulting from overwork, poor living conditions, foul air, and polluted water. In terms of growth record, expenditures on the said activities will reduce growth by conventional calculation. However, it should be viewed also as long term investment in quality the country's human resources. No doubt, present generation of Japanese people have absolutely, better quality of life than the one right after the War. This must be the most worthwhile trade off than for

that of the growth pursuing objective only. The net result must be the slowdown in growth in exchange for much longer term improvement in quality of life of most Japanese people.

6. Continued Foreign Exchange Surplus followed by Asset Inflation (1987–1991)

The structure of Japanese political economy such that massive amount of private savings generated by conservative policy of the government, without sufficient domestic expansion, growth can only be achieved through good performance of exports. Given strong competitive edge of Japanese products resulting from continued improvement in quality in terms of efficiency and environmental record, soon as international environment tilts to their advantage, exports normally perform well as expected. This process has always been the main source of foreign exchange surplus for Japan during the whole period of the 1980's. The continual flows of foreign exchange surplus has eventually led to excessive surplus resulting series of appreciation of the value of the yen. Without proper policy instruments planned to tackle the problem in advance, among many possible consequences, an undesirable outcome of asset inflation cannot be avoided.

6. 1. Continuation of Foreign Exchange Surplus

Rapid increase in government expenditure to create nice living environment matched to a certain extent by business enterprises, during 1970 to 1973 resulted in only moderate surplus in current account balance at 2.0, 5.8, 6.6, and –0.1 billion dollar, respectively. Rapid oil price increase in 1974, caused deficit balance of –4.7 billion dollar. Small deficit of –0.7 billion dollar continued in 1975. Competitive edge in energy efficiency of Japanese automobile industries contributed to rapid increase in exports during 1977–78, with surpluses in the current account of 10.9 and 16.5 billion dollar, respectively. Long term capital investment overseas began to increase significantly since 1978 with the net balance of –12.4 and –13.0 billion dollar in 1978 and 1979, accordingly. The second oil price shock of 1979/80 resulted in deficit in current balance of –8.8 and –10.7 billion during 1979 and 1980, respectively. Until 1980, excessive surplus of foreign exchange reserves did not seem to cause any problem to both Japan and the rest of the world. The new development then, was Japan began to emerge as a significant capital exporting nation.

The trouble began in 1983 and continued until 1986 as the current account balance surged to the new record of high level. The surpluses increased continuously from 20.8, 35.0, 49.2, to 85.8 billion dollar from 1983 to 1986, respectively. This phenomenon increase can be explained by three factors. The decline in oil price stimulated economic expansion for the United States. At the same time Japan enjoyed the advantage of the under value of the yen, caused by the fact that Japan began to use her surplus to invest in assets overseas. Since transactions were made in dollar, in the process the dollar must be first bought by the yen in large amount. This action resulted in the artificially over value of the dollar. Consequently, the price of Japanese exports became relatively cheap for the American. During the period of economic expansion in the United States, the situation finally resulted in more imports from Japan by the United States. The problem was also compound by the fact that during the Reagan administration, the United States ran large government deficit especially on defense.

Strong influence from the said three factors, exports from Japan to the United States increased very rapidly. In 1981, exports from Japan to the United States was 25.4 per cent of total exports from

Japan. In 1983, the share rose to 29.1 and increased further to 38.5 percent. In comparison with the share of imports from the United States, the share increase from 17.7 to that of 19.5 and 23.0 per cent during the same period. In terms of bilateral balance, Japan had trade surplus of 13.3 billion dollar over the United States in 1981. The surpluses increased to 18.2 and 51.4 billion dollar in 1983 and 1986, respectively (Lincoln 1988). This situation explained how the protracted trade war between Japan and the United States was originated. It should be also noted that the surplus in the yen value was not as high as the dollar figure, because the strong appreciation of the yen in 1986, since the G-5 Plaza Accord in September 1985. In September 1985, the exchange rate was 273 yen per one dollar. By the end of 1985, the rate increased to 203 yen per one dollar and reached the record high of almost 150 yen per one dollar by the summer of 1986 (Lincoln 1988). Rapid appreciation of the yen in 1986 resulted in significant drop in growth rate for Japan from 5.0 per cent in 1985 to only 2.6 per cent in 1986. Sharp appreciation of the yen also resulted in the subsequent asset boom.

6. 2. Asset Inflation (1987-1991)

Sharp appreciation of the yen in 1986 made property investment overseas become much more attractive, especially when export prices from Japan became less competitive. Nevertheless, high valued assets overseas especially in the United States were bought during 1989. The process started after the event of adventurous undertaking had already taken place in Japan. Asset inflation originated from easy money policy of the government in its attempt to counter the severe effect of the yen appreciation. A typical monetary measure to ease out the pressure in this case was to reduce the rate of interest in order to stimulate domestic investment, as well as to discourage the inflows of foreign currency from outside. At the same time, the measure also aimed to encourage the yen to flow out into international market in order to reduce upward pressure on the yen. Normally, monetary policy alone is not sufficient to ease severe contraction in investment caused by the yen appreciation, a supplement measure of fiscal expansion is also needed.

Actually, when one accuses the U.S. government for running huge budget deficit, a person should also be reminded that the tract record of the Japanese government has been much worse. In 1977 when the ratio of fiscal deficits to expenditures for Japan was close to 35 per cent that of the United States was only about 10 per cent. While the U.S. government was accused of running high rate of budget deficit of close to 22 per cent in 1985, the rate for the Japanese government was still slightly higher of around 22.5 per cent (*Nihon Keizai Shimbun* 1986). Because of this fact the debt servicing cost in the 1986 budget alone was already as high as 10.7 of total government expenditures. This amount of money would basically go to the hands of the government financial asset holders, whose propensity to save would be very high already. This amount of money normally would not generate investment in productive activities. It would more likely go to more savings or speculative activities. In order to generate domestic expansion, given the existing situation of tight money, sizable supplementary budget was required in spite of the original intention of the government to tighten the belt as part of the effort to reduce the deficit gap by the government (*Nihon Keizai Shimbun* 1986).

As a result, asset inflation in the late 1980's was originally spurred, in part, by the government fiscal expansion. As firms were flood with money but little opportunity to invest in plants and equipment, they started buying land in preparation for future physical expansion. The rest of the general public who could afford to do so follow the suit. Without support from the banks and other related financial

intermediaries, such activities would not have gone so far. It is generally known that financial institutions in Japan are basically spoiled by the practice of Ministry of Finance. They know that if they fail in their operation the government will come to bail them out, finally. In the past, the banks had become accustomed to distributing money along the industrial policy lines. They never learn how to take intelligent risks. As Japan became a creditor nation with an excess of savings, banks had to search out parties to lend money to. Ultimately, they clung to the myth of profit-turning real estate and the asset-inflated economic growth of the late 1980's-growth in which property and stock prices spiraled-was their last hurrah (Yamada 1995).

The following set of figures may be use a rough indication on how land price increases compared with stock price, wage, and consumer price index.

Table 2 Stock Market and Residential Market

year	consumer price	nominal wage	stock market index	residential land price 6 major cities
1955	100	100	100	100
1985	700	2,000	4,000	8,000
1990	800	2,500	9,100	21,000

Source: Jon Woronoff, *Japan: The (Coming) Economic Crisis*, Yohan Publication Inc., 1992, p. 198.

Starting from 1955, as the base year, by 1985 consumer price index rose 7 fold, wage rose 20 fold, the stock price index rose 40 fold, residential land price of 6 major cities rose 80 fold. By 1990, consumer price index rose 8 fold, while wage rose 25 fold, 5 fold increased from the one of 1985. The stock price increase 41 fold, while the land price increased 130 fold during the same period. The figures indicate that land price increases 23 times of the wage and that the stock price increases 8.2 time of the wage. Profits gained from stock and land prices' hike, were, in turn, reinvested in assets overseas. The collapse of asset prices overseas and land price domestically has been responsible for the long period of recession in Japan (since 1992). Most financial institutions in Japan are now suffered from significant amount of non-performing loans. During the second half of 1995 the Tokyo base of Cosmo Bank, the Kobe base of Hyogo Bank, and the Osaka base of Kizu Credit Union were all close down. These financial institutions required significant assistance from the Bank of Japan.

7. Current Recession (since 1992)

As everyone now knows that the current recession was originally caused by the combination of steep fall in asset prices both domestically and overseas since 1992, and further appreciation of the yen value. The appreciation of the yen is caused basically by the continued surplus of the current account balance starting from 1981. The new peak of more than 1,250 billion dollar in both 1993 and 1994 results in the cumulative surplus ratio to shoot up close to 20 per cent (Sakura Bank 1995). The more worrying aspect is that the continued surplus of current account balance is no longer due to strong export performance alone, as before. The value of the yen by itself, in part, is responsible for

current account surplus calculated in dollar value. The continuous sale of overseas assets to pay for bank loans borrowed during the time of inflated assets is also another contributory factor. Lastly, but also increasingly significant in the future is dividend from overseas investment.

The fact that current account surplus is no longer the result of strong exports while domestic savings is still very high are factors explaining long period of the current recession. Gross domestic savings for Japan in 1994, was still as high as 33.6 per cent while those of Hong Kong and Australia were only 30.2 and 16.5 per cent, respectively (The Asian Wall Street Journal 1995). The said figure is rather high by the standard of advanced countries. The figure implies that the ability to recover from recession through domestic expansion without aided by fiscal expansion, is rather limited. As for fiscal expansion, first there is a question of the limitation of its application since Japanese government already has a record high of budget deficit. Second, there is also a question of whether fiscal expansion will not result in inflated assets experienced in the late 1980's.

While there are both political and economic uncertainty at home, small and medium scales manufacturing industries start to migrate out of Japan, more to the rapid growth region of Asia than North America and Europe. This phenomenon is known as the hollow out of Japan, causing more unemployment problem domestically and slowing down the process of recovery. Most of these firms must take the said options for their own immediate survival. The whole situation is nicely summarized by Sakura Bank (1995) as follows: The weakness of the present recovery is attributable to the after effects of aggressive capital investment during the late 1980's, which remain a burden on the economy, and to the existence of a huge current account surplus, which has prevented Japan from achieving renewed economic vitality through exports. Other factors include the corporate sector's shift to overseas production. The Japanese economy is undergoing a structural realignment from export-led growth to domestic demand-led growth, and the frailty of the present recovery phase is a reflection of the transitional state of Japan's economic structure.

The key answer to this difficult situation lies in the ability to transform to the new economic structure, the quicker the better. Whether Japan's economy is ready for such transformation is the matter to be discussed further.

7. 1. Weak Structure?

According to Jon Woronoff (1992), Japan is having a weak economic structure and is either in a crisis or heading for a crisis. Among many factors outlined by him, only a few obvious ones will be reiterated here. They are a declining of the leading sector or manufacturing industry, low level of productivity by the standard of advanced countries, complex system of distribution resulting in high cost caused by low efficiency, and low productivity in agricultural sector. Of course, all these factors are interrelated.

Before discussing each factor, three sets of interesting figures produced by Woronoff will be presented here.

If all figures above are correct, their implication is that the manufacturing industries, the star of Japan's growth performer is now diminishing in its importance. In terms of productivity, the manufacturing sector of Japan is the only sector that performs better than that of Germany and France. However, its performance is still poorer comparatively to that of the United States at least in 1987. The rest of them are the lowest among the four advanced nations with the minor exception of finance, insur-

Table 3 Gross Domestic Product by Industry (per cent)

	1976	1982	1988
Primary	5.2	3.2	2.3
Secondary	37.7	35.3	34.9
Manufacturing	28.0	26.0	25.9
Construction	9.2	8.9	8.6
Tertiary	57.1	61.5	62.8

Table 4 Comparative Productivity 1987

	Japan	United State	Germany	France
Manufacturing	100	112	84	88
Agriculture, forestry and fishery	100	337	135	226
Construction	100	118	135	142
Wholesale and retail	100	167	137	171
Transportation and Communication	100	155	128	131
Finance, insurance and real estate	100	119	98	127
Overall	100	134	124	131

Table 5 Distribution System: Number (thousands)

	1958	1968	1978	1988
Wholesale establishments	193	240	369	436
Wholesale employees	1,551	2,697	3,673	4,328
Retail establishments	1,245	1,432	1,674	1,620
Retail employees	3,273	4,646	5,960	6,851
Distribution employees	4,824	7,343	9,633	11,179

Source: Jon Woronoff, Japan: *The (Coming) Economic Crisis*, Yohan Publication, Inc., Tokyo, 1992, p. 64, 78, and 67.

ance and real estate over that of Germany. Given the poor performance of the sector recently, it is doubtful whether such minor exception still held. Overall, Japan's productivity was the lowest among the four advanced nations in 1987. Given the depressing trends since then, it is rather doubtful if there should be any change in such ranking of productivity, currently.

In terms of distribution system, Japan has a very complex system. On the paper, Japan has already liberalized her trade. Import taxes are already low, and there are not many effective quota systems of import quota. However, her effective self-defense is the distributive system. The system is designed

to discourage competition from imported goods through their added costs of distribution. This explains why domestic consumers benefit from their consumption of imported goods only slightly after the steep rise of the yen. The distributive system has also been designed to absorb extra work forces released from the shrinking sector of manufacturing. This fact explains why distribution employees increased from 4.8 million in 1958 to 11.2 million in 1988. In a country designed to keep open unemployment at very low level like Japan, the distributive system is very effective tool.

Therefore, the distributive system has been designed to perform two important tasks, to prevent excessive competition domestically from abroad and to absorb workers released from shrinking sectors. The distributive system in Japan performs both tasks very well, of course, at the cost of the lowest productivity among the non-agricultural sectors in comparison with the other three countries shown in the comparative productivity table above. While the overall productivity ratios in 1987 for Japan: the United States: Germany and France, are 100: 134: 124: 131, the ratios for wholesale and retail are 100: 167: 137: 171.

Of course, the poorest performed sector among all because heavy government subsidies as part of the country's food security policy, is the agricultural sector. Its comparative productivity ratio, again among the four advanced countries, was the lowest in 1987. The following are their productivity ratios for Japan: the United States: Germany: France, 100: 337: 135: 226. It should be observed also that among them, Japan has the lowest agricultural land per farmer. In terms of scale of production, if agriculture in Japan carried out the same way as the one in the countries mentioned, it will suffer from the scale advantage from the beginning.

The overall implication from the sets of fact discussed above, is that if manufacturing sector of Japan is the only locomotive pulling the whole Japanese economy, the size of the locomotive is getting smaller each time, though it may become more powerful than before. Unfortunately, other cars are getting much bigger and heavier, the distribution system and the agricultural sectors in particular. This study does not intend to suggest that Japan should scrap the two loaded sectors altogether. For obvious reasons, the distributive system still perform its assigned task quite well, while the agricultural sector still provides food securities for Japan. The toilet paper panic in Japan in the recent past was bad enough. Imagine the rice panic in Japan that can happen in the future without the food security policy, how severe in terms of national confidence would it be? Besides, the policy also help preserve more green areas needed in Japan as well.

All discussed so far in the last two sections, are designed to pin point specific problems encountered by Japan that make the her efforts to overcome the current recession, the most difficult ones. Anyhow, the country must finally rides out of the trouble one way or the others. It is now the time to contemplate on whether there is any less painful way to get out of the problem, and what will be the likely longer term prospect for Japan. Perhaps, it will be more helpful to discuss future prospect first as part of method to probe for solution from existing problems.

8. Future Prospect for Japan

If the levels of economic performance and technological development of the United States are set as the goals for Japan to achieve and surpass finally, the first one is already doubtful, if Woronoff's figures of productivity are correct. On technological development, the limitation does not lies in economic area alone. In fact, economic factor is the least of the problem. Culturally, Japan is still a

basically inward looking country and Japanese language while being used widely outside Japan is still not as much popular as English. Fortunately or unfortunately, the inward looking part carries much more weight.

Japan is basically a conformed society with strong sense of nationalism (Fukurai and Alston 1992). To this extent, not like the United States, Japan will not be able to gain as much from the development of her own technology from foreign nationalities, rather than her own people. In the United States most of the new frontier in technological development is actually carried out by foreign migrants or their second generation. That from the third generation and after is the least. Given a rather restricted nature of Japanese immigration policy because part of the social norm and other real necessities for the country, intellectual contribution from migrants will be rather limited in comparison with that of the United States. This makes the process of surpassing in technology over the United States become untenable. Nevertheless, Japan will always benefit from the new technology developed in the United States. At the same time Japan is also capable at reaching new technological frontier in some areas on her own.

Under such constraints, it is still a good idea for Japan to move closer to the United States in the area of technology while gradually taking a more outward looking attitude as well as reducing her strong sense of nationalism. It is best for Japan to play accommodating role for both the United States and Asian nations, economically and technologically. This will bring Japan back in line with the role suggested by Professor Lawrence Klein, namely, to be part of the world locomotives. In order to fulfil the expected role, Japan must be less aggressive on her attempt at exports and open the country for more imports from developing countries especially the ones in Asia. In the area of technology, she should also share the development of technology both at home and abroad based on mutual benefits. This can be done through joint development with other nationalities both at home and abroad.

At the same time she must try to achieve the said international objectives, while maintaining full or at least high level of employment domestically. As well, the welfare level of her people must also be gradually improved or at least maintained at current level. All the said objectives sound like a formidable task to be achieved under currently depressed situation. Nonetheless, they are one of the most sensible sets of objectives. The real challenge remains whether those who are involved in finding solutions for the existing problems clearly perceived the said set of objective in common or not. The challenge to a society with typical consensus is to see if the consensus can be reached on the said objectives. Suppose the consensus is reached, the first logical thing to be done is to open the country up little by little for sincerely mutual exchanges as well as mutual understanding. After the said objectives are set, the way to get out from existing problems can be consequentially discussed.

8. 1. Ways out from the Existing Problems

The word “ways” used as plural to recognize the fact that there are more than one way to be out of the problems. However, before many different ways are suggested, it must be first agreed if the problems perceived are commonly acknowledged. Equally necessary, all suggested solutions must incorporate some forms of structural change. The existing problems basically stem from the pursuit of growth strategy by the Japanese government far too long, resulting in excessive surplus of foreign exchange reserves, the major cause for continual increase in the yen value. Its impact has been more difficult for exports, the main growth engine for Japan. Slowdown in exports results in slowdown in

investment in plants and equipments, a typical factor used to absorb massive of savings in the past. Massive surplus of domestic savings has also been part of the pro-growth policy of the government in the past.

The purpose of this policy is for the government to have full control over its own development strategies while having private sectors had full responsibility on both savings and investment. The policy to create massive amount of savings, by creating the environment of insecurity for each individual member of the society, has been with the intention to provide sufficient supply of capital to firms of all sizes without taking any risk of having inflation that can also upset investment. Under investment depressed atmosphere, it is very difficult to convince those who save to consume, for fear of future uncertainty. Easy money policy by the government in the past amid dim prospect of investment in any productive areas, coupled by discouraged consumption, resulted in more fund available for speculation, the main cause of asset inflation in the past. Therefore, government deficit must be handled with great care in this case. Unemployment is generated as a result.

Under the new circumstance, that exports cannot be used as a potent measure to pull the country out of depression any longer. The solution must lie in the combination of proper measures of increase government expenditures, encourage domestic consumption that will directly result in reduction of savings, as well as significant efforts aiming at effective reduction of excessive foreign exchange reserves. At the same time exports cannot be written off completely. Encouraging exports in the areas of strong advantage comparatively is still very much necessary. If the suggested set of solutions are commonly agreed, then as many ways out of the problems should be discussed. In this study only some "ways" consistent with the long term objectives discussed above will be suggested.

Measures to encourage exports to a certain extent will not be discussed here, since the manufacturing sector in Japan is very much capable in taking care of its own problems given the situation that the yen value only gradually appreciated. Next question is how to deal with excessive foreign exchange reserves. There were at least two outstanding experiences in the past, the American and the German experiences. The American experience was through troops overseas. The notoriously successful result of wasting significant sum of the U.S. dollar, is the U.S. spending in the Vietnam war. Of course to reduce the excessive amount of foreign exchange reserves that way is a bad example, but the underlined principle is to heavily engage in overseas activities. On the other hand, the German experience as well as experience of most advanced European nations has been for the government to spend more on welfare programs. A combination of high consumption ratio and less restriction on imports will easily take care of the excessive surplus of foreign exchanges.

Both examples are bad for Japan for exact duplication, but the essence is to demonstrate how the underlined principles operate in both cases. Sending troops overseas is not much desirable in most cases except the recent experience of the dispatch of the self-defense forces from Japan to help refugees from the Rwanda's conflict. The better one is to send some kind of volunteers to be engaged in constructive development actions for appropriate length of time to less fortunate countries. Such action will be more positive as well as more appreciative. At the same time, too much welfare spending will induce inefficiency as well as social problems. Nevertheless, its useful principle is to improve the quality of life of those involved as well as a good method for long term investment in human resources. Similar actions accomplished in Japan are many kinds of facilities provided for handicap persons. Most directly relevant to the discussion, is its ability to generate consumption mostly needed for Japan.

It is now appropriate to consider what kinds of welfare plan or spending, that do not induce social problems and at the same time generates consumption. One must look into the area that is severely lacking in Japan. In Japan, people are forced to save because of high cost of housing, high cost of higher education, too little amount of pension after retirement and too much time to spend at work places. In order to stimulate consumption, much more attention must be paid in these areas. Welfare spending in these areas will not induce any social problem. In fact increased pension is most appropriate for Japan, as aging population now increase rapidly.

In the area of high cost of housing, the real culprit is the high cost of land. Land price should be kept as much low as possible, for long term sustained development of Japan. This can be achieved through the combination of high property tax especially the one used for speculative purpose and high rate of tax on profit from property transaction, especially land. However, the measures must be applied gradually but constantly. Otherwise the country will risk the massive collapse of banking institutions now are very weak due to too much acquisition of inflated properties, and land in particular.

In other studies, for example the one of Lincoln (1988), suggestion made for the reduction of land price is by deregulating land uses so that more land will be available for residential purpose. This study is not in agreement with more land being used for housing purpose by deliberate policy of the government. In Japan one of the most precious resource of the country is water supply. Being a country consisting of a long strip composed of four main islands, the only source of supply of fresh water must be obtained from the existing space of water catchment within the country. Import of fresh water from elsewhere if not possible, must be very much costly. The argument also applies to the attempt at conversion of sea water into fresh water. Expansion of land uses for other purposes than to keep it for water catchment will directly affect the amount of water supply needed in the future. Problems are already emerged now in many regions in Japan where long spell of dried season hit the areas. Therefore, it is not advisable to deregulate land uses that may results in further reduction of water catchment areas.

In the area of higher education, obviously, the Japanese government did not spend as much money for it by a standard of advanced countries. This practice creates financial strain on individual family in providing higher education for their off springs. The government should try more to alleviate such burden. The most appropriate measure is to provide higher education voucher to a high school graduate and float the tuition fees collected by state universities to the level collected by private institutions. The main idea is to keep both private and state institutions in strong competition. At the same time, more students should be encouraged to move on for higher level of education. The success of this effort will bring two more desirable results, to help the currently ailing private institutions because reduction in numbers of enrollment, as well as to reduce the problem of unemployment of high school graduates, by delaying the time for them to enter job markets. Significant by-product from this practice would be to enhance long term development of the country's R&D increasingly needed in the future.

If people spend most of their time at their work places, they will not have much time for leisure as well as for spending. Simply being at work places does not necessarily mean that more works are done efficiently. In fact, more leisure time and more flexible work hours can result in more efficiency from work. Japan should now try to move away from the so called workaholic society to less and more flexible hours of works. The said practice alone can generate more employment but it is still not good enough. The main purpose of this exercise is to help generate spending as well. If the

Japanese government do not like the idea of having its people spend too much money on imported goods too quick, it should encourage more domestic travelling. From Hokkaido to Okinawa, Japan has so many interesting places to visit. Apart from insufficient amount of time to spend, domestic transportation costs and lodging are also quite high. In order to propagate domestic travelling, a policy directed at the reduction of individual traveller's transportation and lodging costs are necessary. The final outcome if the said scheme is successful, will be at least more consumption spending, more generation of local economy, and more employment generation.

Apart from government expenditures and related measures aiming at increasing consumption spending, reducing the problem of unemployment and generating more employment, as well as directly and indirectly improve welfare of the people, more government spending aiming directly at welfare improvement of the general public is needed. More government spending to improve physical infrastructure in the areas of amenities and environmental protection lagged behind other advanced nations must also be stepped up.

In the area on international relation, in order to reduce too strong sense of nationalism as well as to enhance cooperation and exchanges, Japanese government should spend more to encourage more of international exchange, in forms of more exchange of teaching and research scholars as well as more active programs of student exchanges, especially more training of overseas students in Japanese academic institutions.

In addition to sending a team of self-defense forces overseas occasionally upon being called for, the Japanese government should also seriously giving aids to Japanese based NGO's for various overseas development and self-help programs, the way at least the Australian and Canadian government have already done so for quite sometime. It is more constructive and direct to the point when aids are given directly to local grass-root organizations in order to help people in developing countries solving their own problems. This kind of assistance ,in general, will generate positive impact within short period of time if properly organized. It will generate friendship atmosphere among people in the countries involved as well as those in Japan. It will encourage Japanese people to take a more outward looking view. Finally, it will also generate employment among Japanese youths to alternative profession apart from the tradition of being salary-men.

All the suggestions made above are only meant to be tentative and do not claim to be exhaustive. The main idea is to give some indication for solving the existing problems in Japan in a more constructive way, that is to get Japan out of the current depression, solving her unemployment problem as well as improving the welfare of her own people at the same time. Meanwhile the suggested solution will also help to improve international environment especially in the area of easing potential trade conflict as well as accommodating international development. The suggested path of development will certainly direct Japan to more stable path of maturity in her development effort. Like any matured person who is expected by the society to behave accordingly, a matured economy of Japan must also be designed to function like one. German experiences with proper modification could be more relevant for Japan in her attempt to find the way out from existing crises.

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