

PRESERVING JAPAN'S BALANCE OF PAYMENTS POSITION IN AN OPEN ECONOMY

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I

Japan acquired Article VIII status of the International Monetary Fund on April 1, 1964. As an Article VIII nation, it is incumbent on her not to impose restrictions on the making of payments and transfers in current international transactions except with the approval of the Fund. She also received the status of an Article XI nation of GATT in February, 1963, accepting the obligation of eliminating quantitative restrictions on her imports in principle, except for those goods which are specially designated by GATT. On April 28, 1964, Japan furthermore became a member of OECD and began to observe the liberalization code in both invisible trade and capital transactions. Thus Japan has been enjoying an "open economy" ever since last April. An "open economy" may be described as an economic system in which transactions of goods, services, and capital may be concluded with foreign countries, in principle, freely and without restriction.

Japan has not suddenly entered the stage of an open economy, but in the course of nineteen years since the end of the Second World War has gradually shifted from a closed to an open economic system. In the period immediately after the war's end Japan's foreign trade was entirely controlled by SCAP, but in 1947 private foreign trade was partially permitted, and in 1949 a uniform exchange rate was established at 360 yen per U.S. dollar. In 1953, Japan became a member of the IMF and IBRD. In 1955, she affiliated herself with GATT. In 1956, Japan joined the United Nations. In 1960, a programme of liberalization of foreign trade and exchange was adopted, aiming at increasing the liberalization ratio¹ to 80% or 90% within three years. As a result, the liberalization ratio which stood at 45% in April 1960 went up to 88% in October, 1962, and to 93% in April, 1964. It may well be said that the shift to an open economy through the acceptance of Article VIII of the IMF Agreement and the affiliation of OECD are the result of efforts towards liberalization, and that this is a starting-point for a period of new economic development.

The decision to shift from a closed to an open economy was not made because liberalization is a world-wide tendency, especially among industrial

¹ The liberalization ratio is based on imports in 1959.

nations, but because it could be beneficial to the economic development of Japan.

Theoretically, the open economic system has three advantages :

- (1) advantages derived from the international division of labour,
- (2) advantages derived from the stimulus of free competition, and
- (3) advantages derived from large-scale operation.

These advantages derived from the acceptance of an open economy can be fully appreciated, but it is a matter of great concern that the shift to an open economy should be made at this time, especially as a large deficit in the current account was registered in 1963, and this could cause a large excess of imports, decreasing foreign exchange reserves, and thus could oblige the country to resume trade and exchange controls. To avoid this, Japan's exports should be increased by fostering the international competitive strength of industry through rationalization and modernization on one hand, and, on the other, imports should be kept within due bounds by implementing proper and timely monetary and financial policies, and not by direct quantitative restrictions.

Since the end of the war, Japan has experienced balance of payments difficulties on several occasions, but she has been fortunate in being able to surmount them every time. In the early postwar years, especially before 1949, a large amount of trade and service deficit was covered by U.S. aid such as GARIOA and EROA (see Table 1).

Table 1. BALANCES OF GOODS & SERVICES AND U.S. AID
(In millions of U.S. dollars)

	1947	1948	1949	1950
Net Goods a/c (A)	-296.3	-284.3	-194.8	-0.7
Net Services a/c (B)	-82.1	-102.5	-111.6	70.9
Net Goods & Services a/c (A)+(B)	-358.4	-386.8	-306.4	70.2
U.S. Aid	404.4	461.0	534.7	361.3

Source: IMF, *Balance of Payments Yearbook*, Vol. 5, Washington, D.C., April, 1954.

United States aid continued until 1952, ceasing in that year. In place of this U.S. aid appeared a new receipt item, receipts from special procurements for the U.S. armed forces.

"After the outbreak of the hostilities in Korea (June 25, 1950), the United States and other U.N. countries agreed to reimburse Japan for the additional cost of supporting the U.N. Korea forces stationed in Japan. . . . In addition, the United States began to procure goods and services in Japan for direct use in Korea. This was done mainly because of Japan's unused industrial capacity and proximity to the theatre of operations, but considerations may also have been given to Japan's need to increase its foreign exchange earnings. . . .

"Since the Peace Treaty, which became effective on April 28, 1952, expenses incurred in Japan for the maintenance of U.S. Armed Forces are borne equally by the United States and Japan.

These special procurements "enabled Japan to acquire foreign exchange which could not be earned through more normal channels. In this respect, the special government receipts were, to some extent, similar to U.S. aid, which more than covered Japan's payments deficits in the early postwar years"¹ (see Table 2).

Table 2. BALANCE OF TRADE AND SPECIAL PROCUREMENT RECEIPTS
(In millions of U.S. dollars)

	1950	1951	1952	1953	1954	1955	1956	1957
Balance of Trade	-0.7	-291.8	-412.6	-791.8	-434.7	-54.5	-125.2	-395.5
Special Procurement Receipts	153.6	624.2	787.8	803.3	602.3	505.2	498.0	449.4
Net Current Account	475.5	329.1	224.7	-205.1	-50.9	224.4	33.7	-620.1

Source: IMF, *Balance of Payments Yearbook*, Vol. 5 (April, 1954), Vol. 6 (December, 1955), Vol. 7 (July, 1956), and Vol. 10 (April, 1959), Washington, D.C.

The amount of special procurement receipts reached a maximum in 1953 with an amount of \$803 million. Since then the yearly amount has been decreasing, and in 1963 it was estimated at \$356 million,² that is, less than half of the peak figure.

Since the Korean War, Japan's economy has undergone a conspicuous expansion, and by 1953 her industrial production and level of consumption came up to the prewar levels.

In 1953, for the first time in postwar years, there arose a balance of payments difficulty owing to stagnant exports and expanding imports. A stringent monetary and fiscal policy was enforced.

In 1953 exports fell slightly owing chiefly to the marked decline in sales to sterling area countries, although exports to other areas continued to rise. "The reduction of exports to the sterling area was in part due to restrictions on imports from Japan imposed primarily by Australia, New Zealand, and the U.K. colonies. Total Japanese imports, however, increased by more than 20% during the year, primarily because of larger domestic incomes and relatively higher domestic prices when compared with prices of imports. A crop failure of rice, which resulted in emergency imports of foodstuffs and the need to build up stocks which had been drawn down rather heavily in 1952, were also partly responsible for the increase in imports."

Special measures favourable to import finance which have been enforced since 1951 were also one of the causes of increased imports.

"Consequently the trade deficit almost doubled in 1953, and in spite of slightly larger special procurement receipts, there was a substantial deficit in the goods and services account."³

"This deficit was financed mainly by drawing down sterling balances and

¹ IMF, "Developments in Japan's Balance of Payments, 1947-1955," *Balance of Payments Yearbook*, Washington, D.C., Vol. 7, July, 1956, pp. 3-11.

² IMF, *Annual Report*, Washington, D.C., p. 94.

³ "Development in Japan's Balance of Payments, 1947-1955," op. cit.

using IMF resources to the extent of \$62.4 million (purchase of sterling, \$124.0 million, less repurchase of yen with U.S. dollars, \$61.6 million)."¹

During 1954 and 1955, exports increased steadily; from \$1,258 million in 1953, to \$1,611 million in 1954, and to \$2,006 million in 1955. Imports, on the other hand, fell slightly or remained steady; \$2,050 million in 1953, \$2,041 million in 1954, and \$2,061 million in 1955.

The increase of exports is due to "the relaxation of import restrictions in the sterling area, domestic measures to stimulate exports, and a general disinflationary policy at home."

"The volume of exports in 1955 was 62% above that of 1953, but the volume of imports rose by only 7%, in spite of a 19% increase in industrial production."

"Exports in 1955 were aided by a rising world demand, the removal of adverse discrimination, internal price stability, and a generally favourable competitive position."

Although special procurement receipts fell by about \$100 million, the current account registered a net surplus of \$224 million in 1955 as against a deficit of \$205 million in 1953.

In 1956 the investment boom continued, but a too fast rate of expansion brought about balance of payments difficulties in 1957. Imports increased by \$630 million, while exports rose by \$360 million when compared with 1956. The current account registered a deficit of \$620 million, the largest figure recorded since the end of the war. The balance of payments difficulty in 1953 was chiefly due to an increase in consumption combined with greater imports of foodstuffs owing to crop failures, but in 1957 the expanding investment in equipment as well as in inventory was the cause of a balance of payments crisis. The crisis was overcome by the implementation of a tight money policy.

In 1958, thanks to the results of this policy, imports decreased by \$742 million, while exports increased slightly. The balance of trade improved, registering a surplus for the first time in postwar years. In 1959 and in 1960, both exports and imports increased, the balance of trade showing a favourable surplus as in 1958 (see Table 3).

Table 3. BALANCE OF VISIBLE AND INVISIBLE TRADE

	1958	1959	1960	1961	1962	1963
Balance of Trade (A)	375.1	364.8	270.8	-558.5	401.6	-154
Balance of Invisible Trade (B)	-110.7	-3.5	-127.4	-423.9	-353.2	
(Special Procurement Receipts)	(403.7)	(380.5)	(412.6)	(389.2)	(376.3)	(356)
(Net Services)	(87.8)	(24.0)	(-105.5)	(-382.1)	(-479.9)	
Balance of Current Account (A)+(B)	264.4	361.3	143.4	-982.4	48.4	

Source: IMF, *Balance of Payments Yearbook* Vol. 15, Washington, D.C., November, 1963, p. 1 and IMF *Annual Report*, Washington, D.C., 1964, p. 94.

¹ Ibid.

In 1960, the services account recorded a deficit for the first time since 1950 in spite of special procurement receipts of about \$400 million. This deficit was attributed primarily to the transportation account. Since 1960, the services account has shown a deficit every year, with the amount of deficit growing larger every year (see Table 3).

In 1961, the balance of trade again turned unfavourable, registering a deficit of \$558 million. This was caused by a remarkable increase in imports, about \$1,000 million more than in 1960. This trade deficit, when combined with the services deficit, put the current account into the red. This was covered, however, by the inflow of foreign capital.

The large deficit in 1961 was caused, as in 1957, by a too rapid expansion of equipment investment and inventory accumulation. The Government adopted a tight money policy to restrain the investment boom.

In 1962, imports decreased and exports increased, once more bringing the trade account into the black, but the services account showed even a larger deficit than in the preceding year, more than offsetting the trade surplus.

As may be seen, the country's balance of payments difficulties have occurred at four years' intervals, that is, in 1953, in 1957 and in 1961. In 1963, however, after an interval of only two years, balance of payments difficulties arose once more. In 1963 exports increased by \$530 million, but imports increased by about \$1,100 million. In addition to the trade deficit, the increasing imbalance in services deteriorated to such a degree that the long-term capital inflow was not sufficient to cover the current balance, which was only financed by the inflow of short-term capital. A tight money policy has been in force since December, 1963, and in March, 1964 the official bank rate was raised by 0.73% per annum. These are the difficult circumstances surrounding Japan's entry into an open economy. At present the country's aim is to keep the basic balance of payments solvent, that is, current account plus long-term capital account. But the final objective should be to keep the current account in equilibrium.

There are three schools of thought regarding the pattern of the balance of payments. The first asserts that we should aim at an overall balance of payments, that is, a balance of current, long-term capital plus short-term capital account. The second states that we should aim at a basic balance of payments, that is, a balance of the current plus the long-term capital account. The third insists that we should aim at a balance of the current account, that is, a balance of the visible plus the invisible trade account.

According to the first group, the deficit in the basic balance of payments could be covered by short-term capital movement.

Indeed, short-term capital may be effective in offsetting a temporary deficit in the current account caused by cyclical changes, but it is not a sound policy to depend upon this as a means for financing a long-running deficit of the current account. An outflow of Euro-dollars in 1961 at a time when the balance of payments situation was in difficulties provides a good

example of this.

The second group considers that a deficit in the current account could be covered by long-term capital. Long-term capital is of a more stable nature, and serves to accelerate economic growth. It contributes towards an improvement of the balance of payments by fostering the export- and import-substituting industries, but, on the other hand, payment of interests and dividends and redemption of principal may become a future burden. Moreover, there is a danger that the management of industry might come under the control of foreign capital. So it is not advisable to depend solely upon long-term capital for financing the deficit in the current account. Moreover, since the proposal of the creation of the Interest Equalization Tax¹ by President Kennedy in his special message to the Congress on the balance of payments, in July, 1963, it has become difficult to expect as abundant an inflow of long-term capital as before from the United States to Japan. On the other hand, Japan will be requested to invest more of her long-term capital for the economic development of underdeveloped nations.

Thus the prospect is that the inflow of long-term capital may decrease, while the outflow may increase.

It may, therefore, not be sufficient to maintain the basic balance, but it is necessary to secure the balance on current account.

The third opinion, therefore, should be accepted as the ultimate goal, although the basic balance of payments may be the present aim.

One of the chief causes for the worsening in the current account is the growing deficit of invisible trade items, such as transportation, commissions, and advertising as well as other expenses incidental to trade, and patent royalties. These expenses should be curtailed, but this is very difficult, because expenses incidental to foreign trade will keep in step with the growth of trade, and patent royalties will also increase with the induction of foreign techniques for the modernization of industry.

The only effective way to improve the current account situation is by the promotion of exports.

II

The growth of Japan's exports since 1950 has been remarkable. During the fourteen years between 1950 and 1963, the annual rate of growth reached 15%. This figure is by far the largest of the industrial nations. During the period from 1953 to 1963, the annual rate of growth of exports was almost the same. A comparison of the annual rate of growth of exports of various industrial countries is given in the following table.

With the rapid growth of exports, the share of Japan in world exports has been increasing; it rose from 2.1% in 1954 to 4.3% in 1963, although it is still slightly below the corresponding percentage of prewar years.

¹ The bill on the interest equalization tax passed the Congress and was signed by President Johnson in September, 1964.

Table 4. ANNUAL RATE OF GROWTH OF EXPORTS IN PRINCIPAL INDUSTRIAL COUNTRIES (%)

Country	1950-1963	1953-1963
Japan	14.8	14.7
Germany (F. R.)	14.7	12.5
Italy	11.7	13.4
Netherlands	9.0	8.5
France	7.0	7.7
Belgium-Luxembourg	6.7	7.3
United States	4.9	4.0
Canada	4.6	4.0
United Kingdom	4.3	4.4

Source: MITI, *Tsūshō Hakusho—Sōron*—(Survey of International Trade of Japan—General Introduction—), 1964, p. 117.

In both periods Japan's rate of growth was the highest, almost equal to that of Germany, followed by that of Italy, Netherlands, and France. The exports of the United States and of the United Kingdom increased by about only 4% annually during this period.

Japan's export trade during the period from 1953 to 1963 has been directed mainly towards industrial nations. The annual rate of growth of her exports to industrial countries was 20.1%, while that to non-industrial countries was only 11.1%. Generally speaking, the rate of growth of her exports to underdeveloped nations was very low, and that to Southeast Asia—one of the country's largest markets—was the lowest (see Table 5).

The chief reason why exports to developing countries grow so slowly is found in the declining capacity to import of these countries. Developing

Table 5. ANNUAL RATE OF GROWTH OF JAPAN'S EXPORTS BY REGIONS (%)

	1953-1963
Total Exports	14.7
Industrial Countries	20.1
North America	20.3
United States	20.2
Western Europe	19.6
Non-Industrial Countries	11.1
Oceania	26.0
Underdeveloped Countries	10.4
Southeast Asia	9.0
Latin America	11.0
Africa	10.9
West Asia	13.4
Sino-Soviet Bloc	32.4

Source: MITI, *Tsūshō-Hakusho—Sōron*—(Survey of International Trade of Japan—General Introduction—), 1964, p. 119.

countries are suffering from the shortage of foreign exchange owing to the sluggish export of primary products and the deterioration of their terms of trade.

In order to promote export to these countries, Japan should make greater efforts to co-operate with them in their economic development and should try to buy more from them, although this may not be so simple in practice.

Japan's share in world manufacturing export rose from 3.2% in 1950 to 6.1% in 1960, exceeding the prewar figure, that is, 5.1% in 1938 (see Table 6).

Although the expansion of Japan's export of manufactured goods has been considerable, her share in the world market is still far less than that of the leading industrial countries. Japan should try to overtake these advanced nations.

Table 6. SHARE OF MAJOR INDUSTRIAL COUNTRIES IN WORLD MANUFACTURING EXPORTS (%)

	1938	1950	1960
United States	17.1	21.7	18.7
Germany (F. R.)	19.0	6.1	16.9
United Kingdom	17.7	21.9	14.0
France	5.4	8.3	8.5
Japan	5.1	3.2	6.1
Belgium-Luxembourg	5.1	5.5	5.1
Italy	3.0	3.2	4.6

Source: UN, *World Economic Survey*, New York, 1962, p. 64.

The difference in the growth rate of Japan's exports to industrial and underdeveloped countries changed the geographical distribution of exports. The percentage of exports to Asia and Africa declined, while those to Europe and North America increased (see Table 7).

According to the calculations of the Economic Planning Agency, the elasticity value of Japan's export in relation to world demand was 2.3 during the period from 1953 to 1963. This means that when the world import

Table 7. GEOGRAPHICAL DISTRIBUTION OF JAPAN'S EXPORT (%)

	1934-1936	1953-1955	1961-1963
Asia	52.5	47.4	35.2
Mainland China	(23.8)	(1.1)	(0.8)
Europe	10.7	9.6	16.0
EEC	(4.3)	(4.0)	(5.6)
EFTA		(4.3)	(5.8)
North America	22.7	24.0	29.6
United States	(20.8)	(19.4)	(27.1)
South America	2.8	7.2	7.3
Africa	7.7	9.6	8.2
Oceania	3.7	2.2	3.7
Sino-Soviet Bloc		1.4	3.8

Source: OECD, *Economic Surveys by the OECD, Japan*, Paris, July, 1964, p. 42.

demand increases by 1%, the exports of Japan increase by 2.3%. This elasticity value differs from region to region. It is higher in Canada, Oceania, and the United States and lower in Southeast Asia, Latin America, Africa, and EEC (see Table 8).

It is noteworthy that EEC, which is increasing its demand at an exceedingly rapid pace, should have such a low elasticity. But in the period 1961-1962, this elasticity value improved to 2.5, almost equal to the world average.

It is also to be noted that Southeast Asia, which provides Japan with its largest market, should have a very low elasticity value. It stood at 2.0 during

Table 8. ELASTICITY VALUE OF JAPAN'S EXPORTS IN RELATION TO WORLD DEMAND BY REGIONS, 1953-1963 (%)

	Share of Japan's Exports		Rate of Increase of Import Demand	Elasticity of Demand for Japan's Export
	1953	1963	1953-1963	1953-1963
World	2.3	3.8	6.6	2.3
United States	3.7	8.1	4.4	3.6
Canada	0.9	1.9	3.9	5.1
EEC	0.4	0.8	11.7	1.9
EFTA	0.7	1.1	6.1	3.1
Oceania	1.3	6.1	6.1	4.9
Southeast Asia	8.6	12.0	5.6	2.0
Other Asia and Africa	3.9	5.7	5.4	1.7
Latin America	2.2	3.6	3.2	2.5

Source: Economic Planning Agency, *Keizai-Hakusho* (Economic Survey of Japan), 1964, p. 125.

Table 9. COMMODITY COMPOSITION OF JAPAN'S EXPORTS AND ANNUAL RATE OF GROWTH OF VARIOUS COMMODITIES (%)

	Composition		Annual Rate of Growth
	1953	1963	1953-1963
Total Exports	100.0	100.0	14.7
Foodstuffs	9.4	5.3	11.2
Raw Materials and Fuels	3.5	1.7	6.9
Heavy and Chemical Industrial Products	36.8	52.7	18.9
Chemicals	5.7	5.8	14.4
Metals	15.1	17.3	14.2
Machinery	16.0	29.6	23.9
Light Industrial Products	49.4	39.8	11.9
Textiles	36.1	22.9	8.9
Non-Metallic Mineral Products	4.9	3.9	11.8
Others	8.4	13.0	20.1
Others	0.9	0.6	18.0

Source: MITI, *Tsūshō-Hakusho—Sōron*—(Survey of International Trade of Japan—General Introduction—), 1964, p. 121.

the period from 1953 to 1963, and in the period 1961-1962 it fell to 0.9, climbing up to 1.5 in the period 1962-1963.

The commodity composition of exports has also changed during the period from 1953 to 1963. During this period, the rate of increase of heavy and chemical industrial products was striking, while that of light industrial products—the traditional export items—was not so large. As a result, the share of heavy and chemical industrial products, which was smaller in 1953, rose gradually, exceeding that of light industrial products in 1963 (see Table 9).

Table 10. INTERNATIONAL COMPARISON OF CHANGES IN THE EXPORT COMMODITY STRUCTURE, 1955-1962 (%)

	SITC	Japan	Italy	France	United States	Germany (F. R.)	Bel-Lux.	United Kingdom	Netherlands	Canada
Food	0, 1	0	-6.8	-1.6	3.5	-0.5	1.9	-0.1	-5.9	-0.9
Raw Materials	2, 3, 4	-2.3	-6.5	-4.8	-3.4	-3.5	-3.3	-1.0	0.7	3.8
Metals	67, 68	-4.7	-0.5	-2.9	-1.7	1.9	-4.8	0.9	-2.0	-0.4
Machinery	7-73	9.3	6.8	6.1	4.6	4.7	3.4	6.1	4.2	2.3
Transport Equipment	73	3.8	3.7	4.3	2.1	1.5	1.7	0.4	1.0	1.0
Chemicals	5	1.2	0.8	1.4	1.4	-0.2	-1.0	1.1	1.7	-2.2
Textiles	65	-10.4	-3.9	0.8	-0.7	-1.5	0.1	-4.2	-0.4	0.1
Miscellaneous	6+8- (65, 67, 68)	3.1	6.1	1.1	-1.7	-3.5	0.7	-3.2	0.5	-3.8
Others			0.3	-2.8	0.1	1.1	1.3	0	0.2	0.1
Index of Structural Change*		34.8	35.4	25.8	19.2	18.4	18.2	17.0	16.6	14.6

Source: Economic Planning Agency, *Keizai-Hakusho* (Economic Survey of Japan), 1964, p. 74.

Note: *Index of Structural Change is the sum total of the absolute value of percentage changes.

Table 11. COEFFICIENT OF STRUCTURAL DEVIATION IN EXPORTS AND PRODUCTION

	Share of Heavy and Chemical Industrial Products in the Export of Manufactured Goods (A)	Share of Heavy and Chemical Industrial Products in the Production of Manufactured Goods (B)	Coefficient Structural Deviation (A)/(B)
United States	82.2	55.1	1.49
Germany (F. R.)	85.2	60.7	1.40
United Kingdom	79.7	59.2	1.35
France	70.9	58.8	1.21
Italy	61.4	54.9	1.12
Netherlands	68.4	55.2	1.24
Japan	51.2	61.2	0.84

Source: MITI, *Tsūshō-Hakusho—Sōron*—(Survey of International Trade of Japan—General Introduction—), 1964, p. 241.

Comparison of changes in export commodity structure in various countries during the period from 1955 to 1962 shows that Japan, side by side with Italy, holds the leading position in the world (see Table 10). This indicates the high adaptability of her exports to the world market.

Although Japan has successfully changed her commodity structure of exports in favour of heavy and chemical products, the international competitive strength of her heavy and chemical industries is not so strong. This is made clear by comparing the share of heavy and chemical products in her total manufacturing production with the share of those industrial products in the total export of manufacturing goods.

The coefficient of structural deviation, which is calculated by dividing the share in total exports by the share in total production of those commodities, is lowest for Japan (see Table 11).

Although the heavy and chemical industries have recently been strengthened, their international competitive power is not so strong as that of light industries. This is certified by the comparison of the coefficient of structural deviation in shipments and exports in both industries. The larger the coefficient, the stronger is the competitive power of that industry.

As may be seen in Table 12, this coefficient is higher for light industries than for heavy and chemical industries.

Of the heavy and chemical industries, the machinery industry is the strongest, and the chemical industry the weakest in international competition.

Table 12. COEFFICIENT OF STRUCTURAL DEVIATION IN SHIPMENTS AND EXPORTS

	1950	1955	1959	1961	1962	1963
Total Manufacturing Industry	1.00	1.00	1.00	1.00	1.00	1.00
Heavy and Chemical Industries	0.66	0.81	0.73	0.75	0.76	0.81
Chemicals	0.13	0.36	0.38	0.45	0.55	0.50
Metals	1.05	1.05	0.59	0.61	0.62	0.71
Machinery	0.69	0.83	1.00	0.94	0.91	0.97
Light Industries	1.34	1.21	1.43	1.53	1.48	1.39

Source: Economic Planning Agency, *Keizai-Hakusho* (Economic Survey of Japan), 1964, p. 56.

In the early prewar years, silk was one of the most important Japanese export items, and later came cotton textiles as the export leader. Cotton textiles held their dominant position as the principal exports even in the early postwar years. It was only after 1960 that textiles surrendered their lead to machinery. Today, machinery is the principal export item, and every effort should be made to strengthen this industry as well as other heavy and chemical industries.

Japan's trade expansion owed much to her abundance of efficient labour. The annual rate of increase of productivity of Japan's labour in the period between 1953 and 1962 was 7.2%, while the annual rate of wage increase was 7.1%. This made her labour cost per unit of output stable during this period.

In Western countries, excepting Italy, labour costs increased (see Table 13). This stability in labour costs provided one of the strongest weapons in international competition at that time. But today Japan is changing from a labour-abundant to a labour-scarce country, and wages are tending to rise. Light industries, which are labour-intensive, are suffering from the challenge of the underdeveloped countries. For this reason also, Japan should foster her heavy and chemical industries.

Table 13. ANNUAL RATE OF INCREASE IN PRODUCTIVITY AND WAGES, 1953-1962 (%)

	Labour Productivity	Wages	Labour Cost per Unit of Output
Italy	6.3	5.6	-0.7
Japan	7.2	7.1	-0.1
United States	3.3	3.6	0.3
United Kingdom	2.1	4.2	2.0
France	5.5	7.8	2.2
Germany (F. R.)	4.5	8.2	3.5

Source: Economic Planning Agency, *Keizai-Hakusho* (Economic Survey of Japan), 1964, p. 73.

III

As has been stated, the worsening of the current account is chiefly due to the growing deficit of invisible trade. Invisible trade items may be classified into two main categories, that is, (1) special items, and (2) ordinary ones, which are subdivided into (a) autonomous ones and (b) induced ones.

Special items include receipts from foreign military expenditures (special procurements) and Government transfer payments, such as U.S. aid on the receipt side, and reparations on the payment side.

Receipts from foreign military expenditures, which reached a peak in 1952 and have been declining since then, have been reduced further by the American dollar saving measures which took effect in July, 1962. Although the amount of receipts decreased from \$ 803 million in 1953 to \$ 356 million in 1963, it accounted for 29% of the total invisible receipts in 1963.

Government transfer payments recorded a large surplus in early postwar years due to the receipt of U.S. aid. As U.S. aid ceased in 1952, and reparations payments began to take place in 1955, this account dwindled, and registered a deficit of \$ 30 million in 1962.

Autonomous items include foreign travel, patent royalties, film rentals, copyrights, and other transactions which are made autonomously. These items recorded a deficit of \$ 114 million in 1962.

Induced items include transportation, insurance, investment income, and other items incidental to trade and capital transfer.

The deficits of induced items, amounting to \$ 632 million in 1962, are chiefly responsible for the deficit of ordinary items.

The recent movement of the invisible trade balance tells us that almost all items show a deficit, and that the amount of deficit is increasing (see Table 14).

Table 14. RECENT DEVELOPMENT OF THE INVISIBLE TRADE BALANCE OF JAPAN (Fiscal Year)*

	(In millions of U.S. dollars)			
	1960	1961	1962	1963
Transportation	-224	-239	-214	-244
Insurance	-10	-8	-15	-20
Commission	-29	-50	-74	-108
Open Book Account	-55	-66	-94	-110
"Other" miscellaneous Services	-33	-33	-27	-55
Investment Income	-10	-26	-52	-57
Receipts from Foreign Military Expenditures	403	373	363	339
Foreign Travel	-4	0	-2	-12
Patent Royalties	-92	-108	-108	-129
Donations	23	51	42	39
Other	-41	-43	-44	-52
Total	-72	-139	-225	-409

Source: Economic Planning Agency, *Keizai-Hakusho* (Economic Survey of Japan), 1964, p. 118.

Note: *The fiscal year begins in April and ends in March of the following year.

As is shown in the table above, the deficit in invisible trade is primarily due to the deficit in the transportation account. It is, therefore, necessary to clarify why such a large deficit is recorded under this heading.

"The foreign exchange earnings of the Japanese merchant fleet, and the savings effected by Japan through transporting its imports in its own ships, were also elements of considerable importance in the prewar balance of payments. No reliable figures on these earnings and savings are available, but Japan's fleet immediately before the war was the world's third largest and carried not only well over half of Japan's exports and imports but also a substantial amount of cargo between other countries."¹

If we estimate the transportation account in 1936 with the IMF formula, we get the net surplus of 2 million yen, that is, a surplus of 87 million yen in freight account, and a deficit of 85 million yen in the port disbursement account.² In that year, the cargo-loading ratio under the Japanese flag was 67% for exports and 57% for imports. In 1963, this ratio was 49.6% for exports and 46.9% for imports. As will be shown later, the decline in this ratio is one of the most important factors responsible for the deterioration of the country's transportation account.

The chief causes for the deficit in the transportation account are as

¹ IMF, "Development of Japan's Balance of Payments, 1947-1955."

² Ministry of Transportation, *Kaiun-Hakusho* (Survey of Marine Transportation of Japan), 1964, p. 51.

follows:¹

(1) Rapid increase in the volume of trade

The increase in the volume of the foreign trade of Japan has been so remarkable that the expansion of her merchant fleet tonnage has not been able to keep pace with it. For example, from 1958 to 1962 her tonnage increased by 54%, while her volume of trade increased by 119% (see Table 15).

Table 15. EXPANSION OF TONNAGE AS COMPARED WITH THE INCREASE OF TRADE VOLUME

	1958	1959	1960	1961	1962
Volume of Trade (million M/T)					
Exports	9.3	10.1	11.0	11.1	13.2
Imports	49.1	65.0	87.6	116.3	120.7
Total	58.4	75.1	98.6	127.4	133.9
Index Number (1958=100)	100	129	169	218	229
Tonnage of Ocean-Going Ships (1,000 G/T)	4,548	5,020	5,488	6,055	6,984
Index Number (1958=100)	100	110	121	133	154

Source: Hiroshi Nomura, "Kaiun Shūshi no Dōkō (Trends in Receipts and Payments in Marine Transportation)," *Zaisei-Kinyū Tōkei Geppō* (Monthly Bulletin of Financial and Monetary Statistics) No. 151, Ministry of Finance, 1964, pp. 17-21.

(2) Longer distance of cargo transportation

When the distance of transportation increases, more tonnage is necessary. Since the Second World War, markets for Japanese products and sources of supply of raw materials have greatly changed. Before the war Japan had chiefly been trading with China and other neighbouring nations, but now she is dependent upon the U.S.A. and other distant nations for her raw materials. This lengthens the distance of transportation. For example, the average distance covered by Japan's imports was 3,500 sea miles in 1935, while it reached 5,700 sea miles in 1962.

(3) Wider difference between export and import volumes

As Japan imports raw materials and fuels, and exports manufactured goods, the physical volume of her imports is far larger than that of her exports. Since the War, this difference between export and import volume has been widening owing to the changes in her economic and industrial structure. For example, in 1937, the ratio of export to import volume was 1 : 2.8, while in 1962, the ratio became 1 : 9.2. This ratio is highest for Japan, when compared with those of various other countries (see Table 16).

Such a large imbalance in the volume of exports and imports produces a wide gap in the receipts and payments for freight, because according to the IMF formula the freight of import goods carried by foreign vessels is registered on the payment side, and the freight of export goods carried under the Japanese flag is recorded on the receipt side. Therefore, when the amount of import cargo is far larger than that of export cargo, the payments

¹ H. Nomura, op. cit., pp. 17-21.

Table 16. INTERNATIONAL COMPARISON IN THE VOLUME OF EXPORTS AND IMPORTS

	(In million M/T)					
	Japan	U.S.A.	U.K.	Germany (F. R.)	Italy	France
Export (A)						
1937	12	55	50	17	4	13
1955	8	106	37	15	7	27
1962	13	117	—	18	12	31
Import (B)						
1937	37	43	62	25	20	36
1955	37	139	107	35	38	46
1962	121	181	—	61	68	58
Ratio (B/A)						
1937	2.8	0.8	1.3	1.5	5.0	2.8
1955	4.7	1.3	2.9	2.3	5.4	1.7
1962	9.2	1.5	—	3.4	5.7	1.9

Source: Same as Table 15.

for freight must naturally become much larger than the receipts, although the freight per unit of export cargo (chiefly manufactured goods), is higher than that of import goods (mainly primary products).

(4) Declining ratio of cargo carried by Japanese vessels

The ratio of cargo carried under the Japanese flag has tended to decrease, chiefly owing to the shortage of vessels.

In the prewar days, as is stated above, this ratio was very high owing to the monopolistic position of Japan's shipping in the trade with China and with Japanese colonies.

In the postwar years, as Japan lost this privileged position, the ratio of cargo carried by her own bottoms decreased (see Table 17).

Table 17. THE RATIO OF CARGO CARRIED UNDER THE JAPANESE FLAG (%)

	1956	1957	1958	1959	1960	1961	1962	1963 estimate
Exports	49.7	56.6	58.6	56.1	54.6	53.0	53.1	46.1
Imports	47.0	44.6	58.8	51.5	46.3	40.5	47.7	47.1
General Cargo	47.5	44.9	62.5	51.9	45.7	35.7	48.2	43.6
Petroleum	45.8	43.9	52.1	50.8	47.1	43.4	47.3	52.8

Source: Same as Table 15.

Figures in the above table are the averages for the various items. The percentage in the imports of wheat, soyabeans, sugar, and petroleum products are very low. In 1963, they were respectively, 3.7%, 17.5%, 18.2% and 19.0%.

(5) Growing deficit in port disbursements

As wharfage and other port charges are low in Japanese ports, the amount of receipts of port disbursements is small, while the amount of payments is large owing to the higher port charges in foreign ports which are

estimated to average three times as high as those of Japan (see Table 18).

Table 18. INTERNATIONAL COMPARISON OF PORT DISBURSEMENTS

Japan (Yokohama)	100
Hongkong	47
Singapore	164
Bangkok	170
Bombay	192
Los Angeles	212
Rotterdam	213
New York	267
Sydney	366
Hamburg	430
London	970
Average of Foreign Ports	303

Source: MITI, *Tsūshō-Hakusho—Sōron—*(Survey of International Trade of Japan—General Introduction—), 1964, p. 191.

In the period between 1952 and 1963, about 90% of the freight receipts for export cargoes were offset by payments of port disbursements. The balance of the port disbursement account always shows deficits, and the amount tends to grow larger.

Some argue that port charges and loading expenses should be raised drastically in order to improve the balance of payments. Care should be taken, however, that these charges are not raised too high, because high charges may entail a price rise, thus decreasing the international competitive strength of export commodities.

(6) Financial weakness of the shipping industry

The foundations of Japan's shipping industry were weakened by the Second World War, the vessels destroyed in the war amounting to 2,568 in number and 8.4 million gross tons in tonnage between 1941 and 1945. Shipping companies suffered further losses by the cut of wartime compensation for their losses, and had to build ships with borrowed funds and not with their own owned capital. The failure to increase tonnage in pace with the expansion of trade volume is due to this financial weakness.

Japan's shipping enterprises hold a large number of obsolete and uneconomic vessels, which represent 20% of the total tonnage. Moreover, a cumulative increase of debt, insufficient depreciation, and a growing burden of interest payments are factors which weaken the shipping companies. A far-reaching consolidation of shipping companies took place on April 1, 1964 in order to strengthen their activities. Shipping companies have been integrated into six groups since that date, and the companies joining the group are allowed to defer for five years the payment of interest on shipbuilding money borrowed in the past from the Japan Development Bank.

IV

The fundamental problem of preserving a balance of payments in an open economy, in which import restrictions should be avoided in principle, is one of increasing receipts sufficiently to pay for necessary import of goods and services which are tending to increase. From this point of view, the most important measures are (1) the expansion of exports and (2) the strengthening of the shipping industry. The induction of foreign capital may be necessary, as the country's accumulation of capital is not sufficient at the present time.

(1) As to the expansion of exports, efforts should be made to keep prices stable, to increase the international competitive power of the heavy and chemical industries, and to build up such an industrial structure as is adapted to the growth of world demand.

For this purpose, monetary and taxation policy should be utilized to stimulate exports, and economic diplomacy should be strengthened to secure markets by negotiating with foreign countries for the withdrawal of their discriminatory treatment against Japanese commodities.

On the other hand, orderly marketing should be undertaken to avoid excessive competition.

(2) As to the strengthening of the shipping industry, the cargo loading ratio should be improved to favour the Japanese flag by building more and more ships. The shipping industry should be encouraged to carry cargoes between other countries, as was done vigorously in prewar years.

The tonnage to be built in the next five years is estimated at 7.4 million gross tons. The question is, (1) how to raise the funds necessary for building such a large tonnage of vessels, and (2) how to secure cargoes for the increased number of ships. Referring to the first question, it is suggested that the Government should issue bonds for raising shipbuilding funds, and regarding the second question, it is proposed that a "Ship Japanese" campaign should be carried on with the co-operation of shippers.¹

The pattern of economic growth of Japan has been investment biased. Now that she has entered the stage of the open economy, her pattern of growth should be changed to the export-led type. The rate of growth without external deficit will be decided by (1) the elasticity of exports in relation to world import demand, (2) the elasticity of imports in relation to gross national product, and (3) the rate of growth of world import demand. The higher the elasticity of exports and the rate of growth of world demand, and the lower the elasticity of imports, the higher would be the rate of growth attained. As import elasticity will tend to rise in an open economy, the elasticity of exports must be raised to attain a higher rate of economic growth without a balance of payments deficit. It is estimated that the

¹ Sōgō Seisaku Kenkyū-kai (Research Society for General Policy), *Nihon no Kokusai-shūshi Taisaku* (The Balance of Payments Policy of Japan), Tokyo, Daiyamondo-sha, 1964, pp. 167-172.

elasticity value of exports in relation to world imports was, on an average, 2.3 during past ten years (see Table 8), while it was 1.6 during the past five years. The elasticity value of imports in relation to gross national product is estimated at 1.4, and the yearly growth rate of world imports is at 6%.¹

In this case, when the elasticity value of exports remains 2.3 in future, then the rate of economic growth without external deficit may be 8% or 9%, but when the elasticity value decreases to 1.6, then the rate of growth comes down to 6%. It is, therefore, essential for Japan to maintain high elasticity export values.

Since the elasticity of exports in relation to world import demand is another way of expressing the increases in the share of Japan in the world market, this leads to a simple conclusion that Japan must strengthen her forces of international competition in order to preserve her balance of payments position in an open economy.

¹ Economic Planning Agency, *Keizai Hakusho* (Economic Survey of Japan), pp. 76-77.