

Letter from Japan

The Turning Point?

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ONE is tempted to question the reliability of statistics when one is told that the Japanese economy grew, in terms of real gross national product, at an annual rate in excess of 13 per cent for three successive years. The year 1958* was a recession year, and yet the rate of growth of real GNP was 3.2 per cent over 1957. The latest boom began in 1958; and since then the annual growth rate has been, successively, 17.9, 13.2 and 15.5 per cent. At this rate national income can be doubled in less than five years!

Such a performance belied the expectation of practically all the academic economists; and they are now being hard pressed to explain how this was possible and to foretell what is in store after this. What, for example, becomes of that reputed stability of capital-output ratio in the neighbourhood of 3? A growth rate of 15 per cent year after year would imply a rate of net saving of 45 per cent; and this is clearly fantastic. Should we then assume the estimated value of the saving ratio to be accurate and divide it by the growth rate to obtain the implied magnitude of marginal capital-output ratio? If we do so a capital-output ratio of less than 2 is indicated for the three successive years. This is too good to be true. Something seems to be wrong somewhere.

'Catching-up' Hypothesis

In a longer perspective, however, one could say that Japan is still in the process of catching up with her own potential productive strength. War years (1937-1945) necessitated the diversion of resources from productive investment and war damages almost halved the accumulated capital structure of the economy. But if we could assume that Japan's historical trend of 2.5 per cent rise, annually, of per man produc-

tivity was bound to assert itself sooner or later, making up for the temporary loss by a greater rise later, such a potential trend line would stand above the actual achievement at least up to the end of 1961, suggesting the plausibility of the catching-up hypothesis. The practical content of this hypothesis has two facets, namely: (1) the flowering of an unusual cluster of innovations from which Japan had been isolated because, of the war and yet which Japan was technically ready to make; and (2) the converging of both the consumer durables of prewar vintage (refrigerators, vacuum cleaners, automobiles, etc) and those of postwar (television, room-coolers, etc) at the same time. In both respects, verification is easy to make.

How Was Investment Financed?

Usually a boom of this magnitude tends to create bottle-necks and to invite price rises discouraging exports in favour of domestic sales. It is recorded, however, that domestic wholesale prices have been generally on the decline since 1957, the general index standing at 92.3 in March 1962 compared with the average of 1955-57. How was this possible? The basic factor in the situation was clearly a continued rise in productivity of unusual speed, which offered the opportunity of satisfying simultaneously all the three desiderata of (a) lowering prices, (b) maintaining high profit rate, and (c) raising the wage level. Fortunately, too, the unit value index of Japan's imports has been on the decline continually since 1957. The supply of labour force also has been ample. Thus with the satisfactory expansion of exports from year to year (20 per cent from 1958 to 1959, 17 per cent from 1959 to 1960, and 5 per cent from 1960 to 1961), the cold and foreign exchange reserves, while fluctuating somewhat, still stood at the end of 1961 at a level twice that of the 1955-end and 70 per cent above that of the 1958-end.

Indeed, it seems difficult to find fault with the health of the fast-

growing Japanese economy of the past three years until we begin to scrutinize the monetary and financial situation in greater detail. To do so leads us 'naturally' to the prognostication of coming months also.

A high rate of growth requires a fast-growing supply capacity and hence a high rate of investment; but it is also important to note that a high rate of growth is supported by increasing volume of investment expenditures. Thus gross domestic capital formation attained an unprecedented level of 40.1 per cent of GXP in 1960 after setting a record in the previous year at 36.1 per cent. It is estimated that the 1961 ratio was comparable to that of 1960. Merely, two problems suggest themselves: (1) how was such a high level of investment financed after all? (2) Is not the increase in supply capacity outrunning the consumption needs? We shall concern ourselves with the first of these two problems in the balance of this article.

In terms of national economic accounting, what is most striking in the case of Japan is an extremely high propensity of personal saving. Whereas in the United States saving usually accounts for 7 to 8 per cent of disposable personal income, this ratio in Japan has been as high as 15 to 20 per cent in recent years. True, Japan's personal saving includes business saving by individual proprietors — a category which covers a Yio mean proportion of business activities of the country. But a more direct study is available to support the claim of high saving propensity. Income and expenditure survey of urban wage and salary workers shows that the average ratio of saving to disposable income has stood around the level of 15 per cent in the recent years, probably the highest in the world.

Another characteristic discernible in national economic accounting figures is a substantial contribution made by the public sector towards enlarging the sources of gross

* We shall speak throughout in terms of fiscal year whenever we use national income statistics, i.e. a 12-month period from April 1 in the year indicated to March 31 of the following year.

saving. In 1960, for example, Government saving occupied 22 per cent of the total gross saving of the economy. By implication, therefore, we can see that gross business saving in Japan is a much smaller part of total saving than in a country like the United States. The U.S. statistics for 1960 shows this ratio to have been 70 per cent whereas in Japan it stood at 46 per cent in 1960. Inevitably, Japan's private business world depends for its plant and equipment outlays upon external sources to a degree much higher than in the United States. While in the latter the sum of retained profits and depreciation allowances is usually equal to or only slightly below the total of plant and equipment outlays, the same source in Japan seldom accounts for more than 50 per cent of such outlays. In 1961 the ratio stood at 42 per cent in a survey of 333 large corporations by the Industrial Bank of Japan. Thus bank loans constitute a major proportion of funds for fixed capital investment: and for this reason the monetary situation has a direct bearing on investment.

Credit Over-Stretched

We must look at the monetary picture of the fiscal year, that has just passed, against this background. During the year the net balance of Government against public was 407 billion yen in the former's favour. Of this sum about one-half was accounted for by the absorption of yen funds due to a sizable deficit in international accounts. 107 billion yen is almost one-half of the total current in circulation at the beginning of 1961 fiscal year: and the absorption of funds from public, to the extent it was bound to have a deflationary effect, other things remaining equal. In fact, such an effect would have been salutary in terms of the logic of the classical gold standard mechanism. Excess of imports over exports should cause a deflation in the domestic economy to induce the necessary adjustment.

What actually happened in Japan during the fiscal year 1961 was most remarkable. The central bank either chose, or was importuned, to acquiesce in the offsetting operation against the absorption

of more than the amount the Government absorbed during the year. Thus, by the end of the fiscal year, i.e. the end of March 1962, the Bank of Japan loans outstanding stood above the total of bank notes in circulation for the first time in the history of Japan. Usually such loans stay at approximately 40 per cent of the latter.

This fact alone suggests amply that Japan's internal credit structure has been stretched to the maximum during the course of 1961 in order to enable private business to continue its course of high-level investment in defiance of usual automatic adjustment mechanism. We are bound to reap the fruits of this excess in the coming year.

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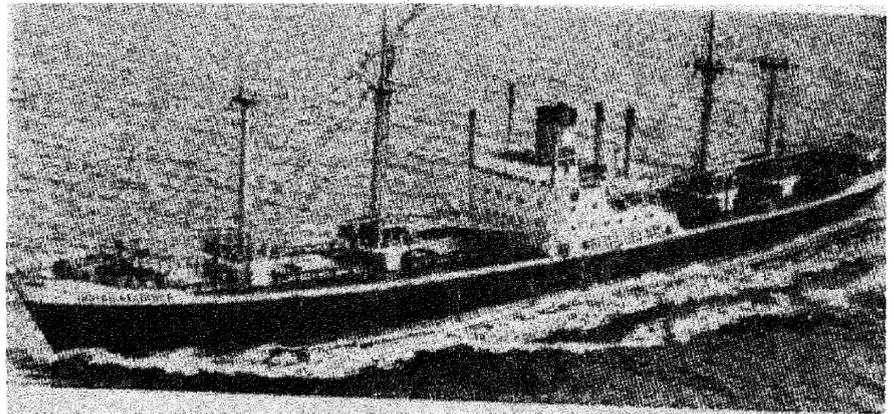
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