Lecture: Contemporary Economic History of Japan

No. 26

Closing Chapter: Shift to Stable Growth

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1. Shift to Stable Growth

- It took about 5 years for Japanese economy, over which a recessionary mood after the first oil crisis loomed, to be considered belatedly to have gotten on “the new track of growth.”
- During this time span, the private capital investment lacked the enthusiasm due to a substantial decline in capacity operating rates and a delayed rebound in company profits, and a growth pattern in the high growth period, purported as “an investment leads another investment,” concealed itself; thus, the recovery was drawn down under the initiative of exports as indicated in significant trade surplus from ’76 to ’77.
- But the process of this revival invited critiques on Japan from foreign countries, causing an appreciation of the yen rate, which put the break on the rehabilitation.

- To deal with these overseas criticisms, a recovery of domestic demand was necessary, but a fiscal expansion for that purpose had to be evaluated against a severe tradeoff with price hikes: In view of the ratio of bond issue to the government finance standing nearly at 30% , a hesitation on increasing public spending could not be avoided.
- It was still fresh in people’s memory that, at the turning point of the economic trend after the Nixon shock, the expansive fiscal policies ingenerated an excessive liquidity paving the way for wild price spirals. If a further pressure was placed on daily lives of people with an increase in consumer prices, there was a possibility that a government’s political footing of the conservative administration per se could be dug away.
- It was on this reason that, as stated in the above, Fukuda Cabinet, being cautious about a fiscal economic expansion measure in consideration of such restrictions, failed to respond to the expectations of economic circles.

Major Economic Indicators 1976--1980

Year	Real Gross National Product	Y/Y Growth Rate	Export	Import	Trade Balance	Foreign Re-serves	Rate of Depen-dence on Public Bond	Rate of In-crease in Con-sumer Price
	Billion Yen		Million Dollars					
1976	199,630	4.6 %	70,577	67,284	3,293	16,997	29,9%	9.5
1977	210,234	5.3	84,625	71,668	12,956	29,208	29.7	6.9
1978	221,243	5.2	98,696	84,635	14,333	28,813	32.0	3.8
1979	232,878	5.3	107,020	120,471	-13,451	18,543	39.6	4.8
1980	242,131	4.0	138,058	143,976	- 5,919	27,020	33.5	7.6

GNP is in the 1980 price.
Source: Research Bureau, Economic Planning Agency, ed., Economic Directory, 1990 edition

- Nevertheless, in view of the growth rates around 5% during this time and the relative macroscopic indexes, this period rather presented aspects which deserved an evaluation to be the years when the economy had shifted to a stage of the stable growth. But the economic circles, unable to thoroughly accommodate themselves to the drop from high growth rates in the years of steep economic growth, were enfolded in a strong recessionary mood. Additionally, the government could not be quite sure how to convert its economic policy to the newly-emerged state of affairs.
- At the same time, it was a problem that, as mentioned earlier, a structure of the growth under the exports' initiative was considered not to last long in the face of criticisms from overseas. The expansion in Japan's exports was regarded to bring a trouble on the overall world economy, rather than emanating a partial friction as in the old days. That much, the position Japan occupied in the world economy was significant, and to such an extent, its role as a major economic power came to be expected.
- A fiscal stimulus laggardly adopted by the government, in hindsight, achieved a certain degree of effect on the turnaround of the economy, but it rapidly heightened the level of dependence on public bonds, and resulted in positioning a financial reconstruction as the paramount challenge in the 80s.

- Amid the insufficiently conclusive government policies, what served as the backbone of the recovery was voluntary management efforts of corporations, purported as a "weight reduction management," corresponding to the substantial environmental variations in the early 70s (the shift to floating system and sharp rise in energy prices).
- Energy-saving measures, as requested once again in the period of the 2nd oil shock in '79, became one of the critical items symbolizing the times for management of corporations, and as a result, endeavors of industrial circles steadily proved fruitful, exemplified in a case where the demand for electric power for the industrial use underran that for consumer.
- In addition, employment adjustments were implemented in order to recover an external competitiveness compatible with the higher yen, while increases in labor productivity were sought out at production sites through automations and others, which materialized the cost reduction.

- According to a survey by MITI, in 1975-77, corporations making efforts to reduce their weights by conducting personnel relocations for the employment adjustment, ran at ratio of 1 out three companies, and leases of employees to allied enterprises at 1 out of four.
- Resulted from these corporate endeavors was the “account settlement in decrease in income and increase in profit” in Sep. ’78 for the first time in the postwar times. Simultaneously, in the face of a lagging turnaround of the economy, an overemployment mood intensified further.
- The burden of employment problems was increasing on Japanese corporations who had positioned the securement of lifelong employment as a principal objective of the corporate management, as symbolized in Nippon Steel’s plan to conduct a broad range of facilities’ cessation and job cutbacks so as to transform its company quality to one that could be profitable even at a capacity utilization ratio of 70%.

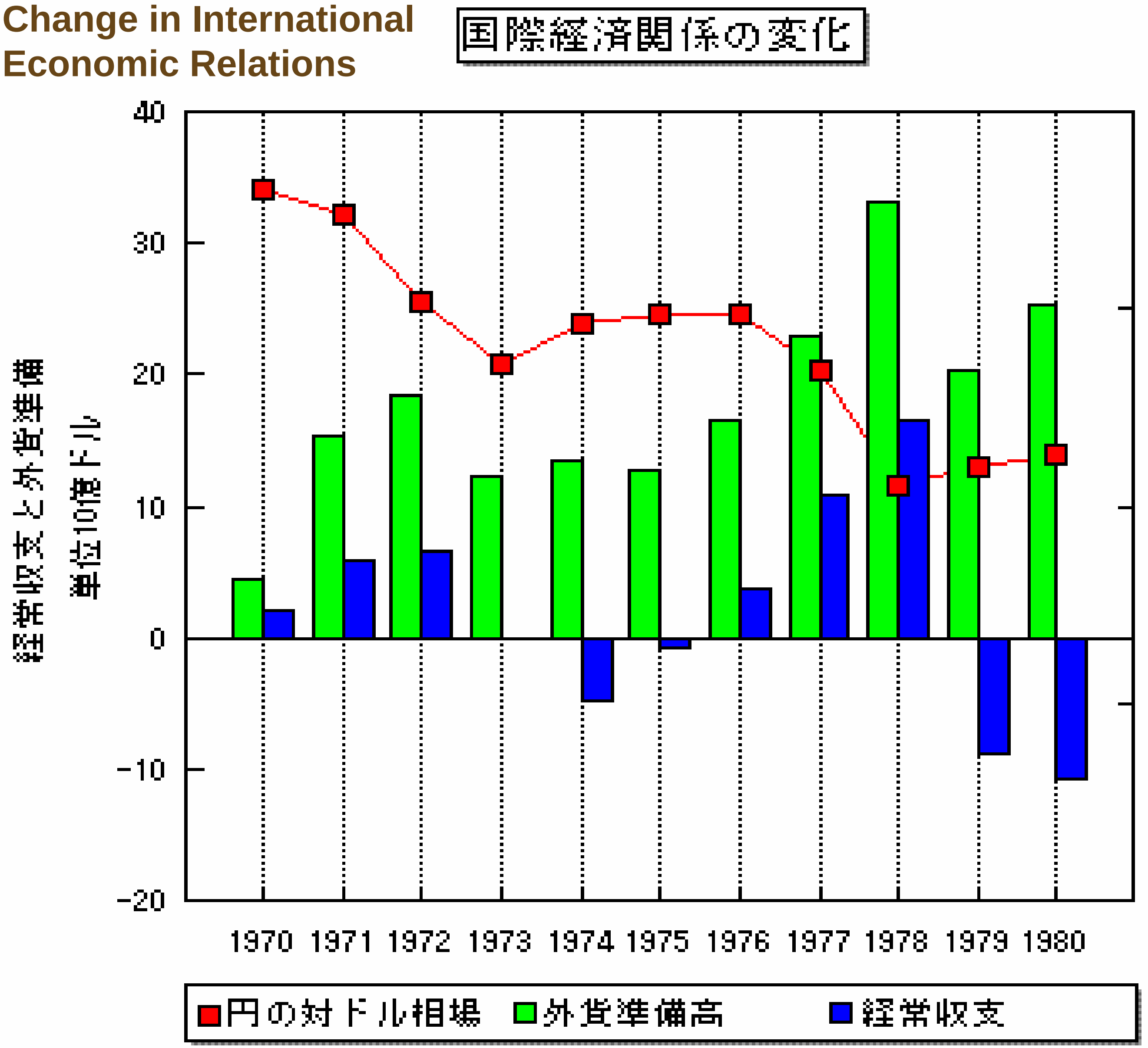
- This kind of effort by individual corporation faced some limits depending on an industrial category.
- Excessive equipments, having become obvious since the oil crisis, left grave problems not to be resolved over a short period in major industry sectors that took on the high growth such as shipbuilding, steel, vinyl chloride, chemical fertilizer, textiles, and aluminum smelting, which called for measures for structurally-depressed industries.
- Damages by the appreciating yen were particularly serious to such industrial categories that lost an international competitiveness on account of steep hikes in costs of raw materials and energy, and to ones undergoing catch-ups of developing countries. This indicated that the industrial structure was coming under pressure to be transformed in a medium term.

2 Progression of Yen Appreciation

- To take a look at an international economic relationship, there was an economic summit held in London in May ’77 which agreed upon; the promotion of the cooperation among developed nations including the attainment of each country’s growth objective based on the Japan-U.S.-Germany locomotive theory, the inauguration of IMF new lending mechanism, the reduction of tariffs, and the alleviation of nontariff barriers.
- But the footfall of Japanese economy thereafter was that not only did its 6.7% growth target for ’77 become impossible to be attained, but also little headway was made in reducing the level of trade surplus.
- Accordingly, in an IMF World Bank general assembly held in Sep., adverse criticisms on Japan’s trade surplus became intensified, and the country was hard pressed for surplus reduction measures focusing on the promotion of imports, firstly from the U.S., and then from EC. Against this background, the yen rate rapidly went up from ¥293 per dollar in the early 77 to ¥222 in Mar. ’78, an upvalue of 31%.

- **Consequently, the government adopted a variety of measures: the compilation of a supplementary budget and comprehensive economic measures including the reduction of the discount rate in Sep. '77, the eight articles of external economic measures in Dec., and in '78, the liberalization of foreign exchange controls, being the target of strong accusations by foreign countries, and another round of chopping the discount rate. These, however, did not get far enough to cast aside disapprovals on Japan's currency/trade measures.**
- **In '78, attributed to the effect of the higher yen, the disequilibrium in balance of payments started improving, and exchange rates of yen against dollar gradually retrieved a stability. But the petroleum supply disruption, on account of the political turmoil in Iran in the year-end of '78, coupled with the outbreak of China-Vietnam War, quickened the pace of price hikes of crude oil/international commodity market trend, which, in reversal, brought about a record of a large deficit of 14 billion dollars in '79. During this period, the yen rate that was turning cheaper from Nov. '78 went down further as the current-account deficit expanded at a rapid tempo from the second half of '79, to around ¥250 that was close to the level at the end of '77.**

Change in International Economic Relations



Current-Account Balance
Unit: Billion Dollars

Yen Exchange Rates to Dollar

Yen Exchange Rates to Dollar

Foreign Currency Reserves

Current-Account Balance

3 Administrative/Fiscal Reform and Fiscal Reconstruction

- As time advanced into the 1980s, it was an administrative and fiscal reform that constituted the policy task for the conservative government of Zenko Suzuki Cabinet followed by Nakasone Cabinet.
- The temporary council of research on public administration system was installed whereby the deliberations on an administrative reform progressed, while the government adopted at the Cabinet meeting the " zero ceiling in principle" (zero-based budgeting in principle) to fundamentally restrict guidelines for the estimate budget request for '82 at 0% growth from the previous year, and also for '83 budget, "to cut back 5% from '82 budget amount in principle", a minus-based budget for the first time ever. On another front, on Jul. 30, '83 the temporary council submitted its third report (the basic report) encompassing such pending issues as the breakup and privatization of the three public corporations of national railway, telephone/telegraph, state monopoly, and further, the abolishment or merger of government agencies, and recommend guidelines for overcoming the fiscal crisis through the course of "reconstruction of the public finance without a tax increase."

- The succeeding Nakasone Cabinet, proclaiming in its policy speech in Sep. ’83, “The most important challenge in serene reforms is to resolutely carry out the administrative and fiscal reform,” positioned the administrative/fiscal reform as the uppermost issue of domestic politics of Nakasone regime.
- Accordingly, Management and Coordination Agency was established by integrating Office of the Prime Minister and Administrative Management Agency (July 1, ’84), the law was formed to privatize the public corporations of both telephone/ telegraph and state monopoly, and the minus-based budget for the general expenditure in the ’85 budget was carries forward.
- Furthermore on Sep. 4, ’84, Prime Minister Nakasone inaugurated “the economic policy study group” (chaired by Mitsubishi Research Institute’s chairman Noboru Makino) as his private study session in order to explore economic planks regarding the adoption of private-sector initiatives, the way of being for public-works investment, the manner of utilization of advanced technologies, etc. The report submitted on Oct. 30 by the group, entitled “Economic policies and the incubation of private-sector initiatives in coming years,” enumerated big projects of expense scales of a few trillion yen to be operated jointly by the government and private sectors, and propounded a proactive promotion of “utilization of underground, sea-level, and aerial regions.”

- And as specific measures to achieve its recommendations, the report called for making legislative/institutional adjustments to revise preferential treatments for participating corporations, which included an alleviation of developmental restrictions, an unhitch of national/public lands, an issuance of the license to private businesses on the reclamation of publicly-owned water body, a restriction alleviation on air right utilization, and a revision of Leased Land Law.

- Corresponding to such government policies, on July 22, ’85, Provisional Council on Administrative and Fiscal Reform (chaired by the Keidanren honorary chairman Toshio Doko) submitted its report on the relaxation of regulations including governmental approvals and licenses extended over 254 items, and the delegation of authorities to local autonomies, so as to draw forth the private-sector initiatives. The report was characterized by hammering out a functional enhancement of the cabinet, as well as addressing an appeal on the utilization of private-sector initiatives, hence recommending that a making of the “simple and strong government” go hand-in-hand with a power of the private sector.

- On the other, Prime Minister Nakasone in Jan. '85, having returned from the summit with U.S. President Reagan, gave his instructions in the cabinet meeting to put together market-opening measures designed for the U.S. , and to venture to simplify import formalities and improve the standard certification system in areas of communication devices, electronics, lumber, medical equipments, and pharmaceuticals.
- Further on Apr. 9, the minister, through an unusual "address to the nation" in live telecast, emphasized, "in order to sustain the free trade framework, Japanese market needs to be opened up on the principle of 'freedom as a rule, restriction for exceptional cases' as much as possible," solicited the understanding on reducing the government regulations on imports to their utmost and entrusting to the choice and responsibility of consumers, and urged his people to "make an additional purchase of imported products for 100 dollars per person" for the sake of an import expansion.

- On top of this, in Oct. Nakasone established another personal advisory panel, “the study group regarding economic structural adjustments for the international collaboration” (chaired by former president of Bank of Japan Haruo Maekawa), to discuss measures for transforming Japanese industrial structure from an export-dependent format to an external-collaboration model.
- Its specific agenda were three:
  - ①Schemes regarding an adjustment of the mid-term economic structure to properly consort with requests from the international economy
  - ②Schemes to maintain a pertinent balance of trade
  - ③Schemes regarding the international collaboration to stabilize and maintain the appropriate value of currencies
- It was the reporting of this study group, “Maekawa report”, that exerted a significant influence on what economic policies should be thereafter.

4 Big Exporter Under Stable Growth

- Background for Maekawa report to have been put together ---Japan's international position in the 1980s
- Japanese economy overcame the second oil crisis smoothly compared to Western countries. On the other, these countries, having carried on monetary restraint policies over a long period to control inflation triggered by the steep rise in petroleum prices, were tormented by no growths and minus growths, high rates of unemployment and commodity price hikes.
- Among them U.S. interest rate recorded the highest level in the post-WWII years with the official rate at 14%, and including an additional rate for higher-interest-rates application for large banks, it reached 18%. Such high interest rates across the world exerted an adverse impact on the world economy by exercising strong deflationary pressures over countries' economies, standing in the way of business upswings, and increasing interest-payment burdens of nonoil developing countries causing accumulating debts problems.

- **The high interest rates of the U.S. had a substantial impact on Japanese economy as well, bringing about a cheaper-yen trend, making a low interest rate policy to boost the economy difficult, hence constituting a factor to stand in the way to the recovery of domestic demand.**
- **Nonetheless, Japanese economy shifted to a moderate recovery process in ’81. In this business upturn process, the propensity for inequality was conspicuous among business categories, sizes of companies, and areas. Among business categories, processing-format industries with a relatively light influence of the runup in petroleum prices increased their output consistently, whereas recoveries were slow with industries in formats to consumer a large quantity of petroleum/energy that were strongly affected by oil-price hikes.**
- **Growth rates of the economy ranged from 3% to a little more than 5%: they turned up being pulled by the expansion of exports from around ’83, and all in all throughout the first half of the 80s the continuous growth at the stable tempo was observed from a macroscopic standpoint.**
- **Consumer prices after ’82 were forced down and low in their increase rates, and in the fiscal phase, though appearing to be back to the status in ’83 when Nakasone Cabinet come onstage, the degree on dependence on public bonds steadily declined. The problem was, pursuant to the export expansion from ’83, the trade surplus rose sharply, only to stumble across harsh critiques from overseas.**

Major Economic Indicators 1980--1985

Year	Real Gross National Product	Y/Y Growth Rate	Export	Import	Trade Balance	Foreign Re-serves	Rate of Depen-dence on Public Bond	Rate of In-crease in Con-sumer Price
	Billion Yen		Million Dollars					
1980	242,131	4.0%	138,058	143,976	5,919	27,020	33.5%	7.6
1981	250,159	3.3	151,938	142,734	9,204	27,231	26.2	4.0
1982	258,241	3.2	136.640	127,313	9,328	24,015	21.0	2.6
1983	267,700	3.7	152,697	129,351	23,328	25,109	26.5	1.9
1984	281,399	5.1	169,612	134,545	35,066	26,538	25.0	2.2
1985	293,982	4.5	182,634	130,031	52,603	27,917	22.2	1.9

- Aiming at securing the free trade framework, the government went ahead and executed the voluntary restraint on the export of automobiles to the U.S. in May ’81. Also, the economic mission dispatched to Europe in Oct. that year faced a barrage of attacks of criticisms against Japan and strong demands for its voluntary export restriction.
- In a meeting with Prime Minister Zenko Suzuki back in Japan, the mission offered counsel for him to take actions, reporting, “Economic problems have become political issues to such an extent that the alignment with Free World countries could be impaired.”

  →Measures were adopted to expand imports including the reduction of tariff and the lending of foreign currencies for emergency imports.
- A voluntary export restriction demanded by the Western countries was the means to be evaded as much as possible.
- In spite of a stagnation in domestic demand, Japanese corporations, in addition to the low yen rates just then, were equipped with an international competitiveness strengthened by their investment in the labor-energy savings realized through the first and second oil shocks, which lent itself to the recovery on the initiative of the foreign demand. In terms of corporate performances, mired in a slump were such domestic demand-based material industries as petroleum, aluminum, chemicals, paper pulp, and housing, whereas processing industries of export-orientation, like automobile, electricity, shipbuilding, and metal products, racked up profits: A bipolar movement was being observed.

- In the face of the dappling of recovery process, Suzuki Cabinet that positioned the administrative/fiscal reform as the uppermost issue was unable to take the bold course of a fiscal measure.
- While exports maintained a boom chiefly bound for the U.S., the capital investment by private corporations gradually gathered steam , and the economy transformed from an export-led recovery to a business expansion process centered on domestic demand in the mid-80s.
- But this recovery process accentuated problems like high interest rates and the cheap yen, and a rigidification of public finance, and the expansion at the initiative of exports provoked an aggravation of external trade frictions.
- At the five countries' financial ministers' meeting (G5) hurriedly-summoned on Set. 22, '85 at Plaza Hotel in New York, U.S. government largely changed its stance of no-intervention to exchange rate until then.
- Based on this, the countries participating in G5 decided on the concerted intervention toward a correction of the high-value dollar.
- Through the joint intervention on the basis of G5 agreement (Plaza Accord), on Nov. 25 the yen's exchange rate against dollar rose above ¥200, an yen's ascent of 20%, and kept on appreciating thereafter. Thus, Japanese economy came to be preoccupied with responses to an abrupt rise of the yen.

5 Strong Yen and Heisei Economic Boom

- **1986 was the year when the term “Zaitech” (financial technology) obtained citizenship. Corporations, retaining vast amounts of excess funds, were extremely reluctant to make capital investment due to a progress in the yen appreciation depression, slanted to an efficient operation of funds being unutilized in their primary corporate activities so as to supplement the stagnated performance in main line of their businesses.**
- **At the same time, another factor lying in the background of Zaitech boom was that concerns for operating methods further enhanced in the private sector including general depositors and investors who harbored reservation about the decrease in value of deposits and savings with the cuts in official rates over four times.**
- **Magazines specialized in money caught on, newspaper and weekly magazines made features of money.**
  - **According to Wako economic research institute’s survey against 964 companies listed on the first section of the Tokyo Stock Exchange (excluding banking, insurance, securities), firms in the black in the nonoperating expenditure and receipt during the first half of 1986 increased by 95 from the year before to 470, occupying 48.8% of the total.**
- **It was not the case that a speculative “bubble” phenomenon transpired in ’86, but the ground for the later years was already formed.**

- But as many corporations worsened their performances attributed to the rapid appreciation of yen upheld after Plaza Accord of ’85, it did not necessarily mean that Japanese economy under Zaitech boom came to good business conditions immediately.
- Amid worldwide surroundings of low interest rates and money glut, the stock markets of ’87 enjoyed securities rising steeply in prices and indicated a situation which was termed as “the phenomenon of the spontaneous worldwide upturn in stock values.” These markets, however, triggered by the nosedive purported as “Black Monday” that raided New York Stock Market on Monday, Oct. 19, brought about the worldwide chain-tumble phenomenon.

- Due partially to this disturbing factor, Japanese economy remained at 4-percent-line growths during 1986-87 as seen in the following chart.
- It was in ’88 or later that growth rates turned up, and into ’89 particularly, against the background of exports growing at a sluggish pace and the trade surplus heading for scaling down, that the economy attained a growth in excess of 7%, which was regarded as a proof that Japanese economy was delivering on its transformation to an economic structure under the initiative of domestic demand.
- The degree of dependence on public bonds settled down at about 10%, and an expansion of business was being achieved without excessively relying on fiscal administrative policies.
- Though the rate of increase in consumer price became higher showing some factor for concern about future of the economy, to sum it up, a few years of the latter part of the ’80s represented a strong economy for a long period since the second half of the 1960s.

Major Economic Indicators　1986--1990

Year	Nominal Gross National Product	Y/Y Growth Rate	Export	Import	Trade Balance	Foreign Re-serves	Rate of Depen-dence on Public Bond	Rate of In-crease in Con-sumer Price
	Billion Yen		Million Dollars					
1986	339,363	4.6	215,116	125,380	89,736	58,389	21.0	0.0
1987	355,522	4.8	238,036	162,034	75,993	84,857	16.3	0.5
1988	379,657	6.8	272,865	193,991	78,874	99,353	11.6	0.8
1989	406,477	7.1	273.652	214,087	59,565	73,496	10.1	2.9
1990	438,687	8.0	296,581	242,285	54,296	69,894	10.6	3.3

- To follow such foot steps of Japanese economy in more detail, amid “Zaitech” boom from around ’86, a listing of the stock of Nippon Telegraph and Telephone Corp. (NTT) in Feb. ’87 brought a stock boom.
- In the same month of Feb., the seven countries’ financial ministers’ meeting (G7, except for Italy being absent) held in Paris put together a joint communique, known as “Louvre Accord.” The agreement , for one, requested surplus countries to expand domestic demand and cut back surplus, and deficit countries to reduce fiscal deficit and improve external balance, and for another, indicated a judgment to state, “the ongoing standard of exchange rates generally accord with fundamental economic terms and conditions of each country.”
- This Louvre Accord signified for Japan to accept that the strong yen since Plaza Accord was the irreversible change. But exchange rates of yen did not stabilize at the level agreed upon then: In late Apr. that year, influenced by the remark of U.S.Trade Representative Clayton Yeutter, “If nothing is done, ¥100 to a dollar is not improbable,” weakening of the dollar gained speed, and on Apr. 24, Tokyo foreign exchange market plunged into ¥130 line to a dollar.

- Despite such a fluctuation in exchange rates, Japanese economy of 1987 bent its steps toward a steady recovery supported by the robust domestic private demand such as personal consumption and housing investment, as well as the emergency economic package in excess of 6 trillion yen decided on in May.
- While ’86 experienced a climate known as “the high-yen recession” caused by the sharp appreciation of the yen against the dollar, the economy hitting bottom in Oct.-Dec. ’86 registered tones of recovery attributed to the effectiveness of corporate countermeasures against the high yen, and the positive effect of the high yen that lowered imported raw-material prices.
- Meanwhile, there was a noteworthy transition unfolding on the trading front:
  - **That is, Japan’s imports of final goods occupied 45.6% of the gross import value in ’87. The ratio of the imports of final goods steadily advanced compared to 31.0% of ’85 and 41.7% of ’86.**
  - **Although Japan’s was still low by comparison with the ratios of U.S. and Canada in excess of 80%, and ones of West Germany and France at about 70%, Japanese trade structure came to have a horizontal relationship of the division of labor having gotten away from a vertical relationship of the division of labor in a conventional processing-trade format. The reasons were, for one, the progress in opening up of the market, and for another, a deteriorating competitiveness of Japanese industries due to the high yen and an expansion in the overseas production.**

- This trend continued in succeeding years, Japan's imports of final goods in value during the first half of '88 recorded a substantial increase of 49.4% from a year before, which exceeded the growth rates of 31.4% of '86 and 25.0% of '87.
- In the meantime, '88 edition of *Economic White Paper* was released with a subtitle of "the sustainment of a domestic demand-based growth and the contribution to the international society", which proclaimed that:
  - **"Japanese economy overcame a yen appreciation depression that started in the fall of '85 ;"**
  - **The economic growth led by domestic demand was achieved;**
  - **In the process of business recovery, a balance of the economy took a turn for the better as seen in a reduction in the current account surplus by the increase in imports of final goods, an improvement in the employment situation, and a stabilization in commodity prices;**
  - **The economic climate was moving into a steady growth attributable to the development of the personal consumption and capital investment**.
- Thus, the time frame of the business uptrend reached 43 months, exceeding the duration of "Iwato Boom," to have become one large-scale economic boom next to "Izanagi Boom."

- Amid the “domestic demand-led ” big boom, two problems rose to the surface.
- One was an economic friction with the U.S., and another was commodity prices.
- In the wake of coming close the deadline of the agreement regarding the import liberalization of beef and orange in ’88, economic disputes between Japan and the U.S. intensified even further. In the negotiation of agricultural commodity, the U.S. strongly demanded the elimination of the quota, which resulted in the decision on Jun.20 to abolish the quantitative restriction for beef and orange in Apr. ’92. Further, U.S. President Reagan signed the Omnibus bill in Aug. that year. This Omnibus Trade and Competitiveness Act is made up of 10 cantos covering a broad range of contents not only concerning trades but also the protection, reinforcement, and fosterage of domestic industries: trade and customs and tariff, export enhancement, international financial policy, agricultural trade, Foreign Corrupt Practices Act (prohibiting U.S. firms from bribing foreign government officials), education/training and American competitiveness, Buy American Act, protection/fosterage of small businesses, patent system, foreign shipping and air transportation.

- Japan had to keep up efforts to liberalize its market and protect a free trade framework while indirectly holding U.S. movements in check that further strengthened a propensity toward protectionism.
- 3 years into talks since its onset already, the ministerial summit of GATT Uruguay Round (the new round of multilateral trade negotiations) couldn't clinch the decision on account of issues like the dispute in agricultural sector between the U.S. and EC, thus difficult challenge lay in a heap against maintaining a free trade structure.
- In ’89, the U.S. intensified its offensive even further. On Apr. 28, U.S. Trade Representative (USTR) announced the by-country report with respect to barriers to foreign trade that was to serve as the baseline for the application of the article Super 301 (identification and negotiation regarding unfair trade nations/practices, retaliation) included in the Omnibus Trade Act of ’88, and pointed out to Japan regarding barriers to trade in 7 fields and 3 items including semiconductors and supercomputers. In addition, USTR on May 25 concluded that unfair trade practices existed in 3 fields of supercomputer, space satellite, wood processed goods, and that the article Super 301 was to be applied.

- **In the face of aggravating issues between Japan and the U.S., what made the matter even more complicated were the two announcements: Sony's buyout of a U.S. large movie company, Columbia Pictures Entertainment, in Sep. '89, and Mitsubishi Estate's buyout of Rockefeller Group in Oct. As the news on Sony was disclosed, *Newsweek* carried a negative article to say, "They bought a part of American soul," and U.S. lawmakers started preparing a bill to limit Japan's investment in the U.S., the press reported.**

- In this period, Japan-U.S. conference on Structural Impediments Initiative commenced on Sep. 4 to resolve trade imbalance between the two countries. The SII meeting was proposed by the U.S. based on a thought that the reason for the trade imbalance not to diminish, despite the yen appreciation against the US dollar, might be rooted in the structure of Japanese economy per se featured in an inefficient distribution system and an imbalance between savings and investments. This redefined Japan to relax various regulations and systems/customs for the sake of a further market opening.

- On the other, in ’89, the price runup became obvious, particularly the land price issue, and disparities between domestic and foreign prices of products and services, generated a considerable debate.
- For that matter, Bank of Japan raised the central bank rate by 0.75% to 3.25% per annum from May 31, 1989, which was the first move in 9 years and 2 months since Mar. ’80 corresponding to the price hike following the second oil crisis.
- This year’s *Economic White Paper* pointed out that, along with the expansion of GNP, the stock (outstanding balance of asset) of Japanese economy increased, enhancing its influence to the total economy year after year, and positioned this as a progress in Japanese economy’s propensity to stock.
- Since then pull-ups of interest rates continued due to concerns on prices of commodity and land, and 1990’s Japanese economy entered in a high-interest-rate epoch having completely concluded the monetary relaxation since Plaza Accord. BOJ raised the central bank rate by 0.5% to 4.25% on Dec. 25, ’89, then by 1.0% on Mar.20, ’90, and on Aug. 30 by 0.75% up to 6.0% a year.

- The tightening of money directly hit the securities market and real estate market, and even golf/resort membership markets, that enjoyed the full benefit of money glut taking on a “bubble” phenomenon.
- The average stock price of the first section of Tokyo Stock Exchange of ’90 that started at ¥38,712 slithered down since then, and on Apr. 2, recorded a big crash of ¥1,978 in a day, and registered a dropping below the mark of ¥20,000 on Oct. 1.
- Moreover, since the summer of that year, a downward trend of land prices of inner-city districts in places like Tokyo became evident, which was accelerated by the policy of landholding tax (land-value tax) originated from the land-tax reform instituted by the government. The epoch of an asset inflation under monetary relaxation was about to end.

6 Bubble Burst and Protracted Recession

- In Dec. 1991, Economic Planning Agency made an announcement of “Retrospect and Issues of ’91 Economy” which stated that Japanese economy entered a moderately decelerating process.
- With respect to Japanese economy of ’91, this report summed up that, due to the decrease in housing investment and the slacking off of the increase in capital investment, the expansion tempo of domestic demand moderately decelerated, and that the economy was in a process of making the transition from the past high growth to a growing path that would enable a sustained expansion without inflation.
- The reasons for the slowing down were the efficacy of monetary tightening, the stock adjustment, and the decline in securities’ prices. But thanks to a positive effect of monetary easing and an underlying trend of price stability from the second half of ’91, coupled with an anticipated recovery of the world business climate , the probability for a downturn in economy to lead to a deep decline is not great, the report forecasted optimistically.

- But Japanese economy in the ’90s came to betray this kind of optimistic outlook and suffer a long recession. The economic growth rates fell off to 1.9% in ’92, and below 1% from the next year.
- The real growth rate dropped to a minus in ’93, and a zero growth in ’94. During this time span, as exports expanded favorably and the trade surplus reached levels exceeding 100 billion dollars, the problem was a striking slump in domestic demand. Because of the tax revenue shortfalls, the progress in fiscal rehabilitation was aborted and the dependence on public bonds enhanced.
- After the burst of the bubble, under the burden of defaulted credits to be purported as the aftermath, an extremely low-interest state of things prevailed. On the financial front, nevertheless, amid developing liberalization of finance, the management turmoil of and treatment of bankruptcies by financial institutions became important issues. Instead the low interest made a possibility for additional measures from the financial angle extremely smaller, and narrowed room for anticyclical measures. Thus continued the state of economy with no way out.

- With respect to the financial instability, Itoman-Sumitomo Bank affair from ’90 had a lasting effect bringing about the allegation over lands and paintings in ’91, and other scandalous cases were made known, like, compensations for clients' losses by securities firms, the illegal loan incident by influential banks, and the financial and securities’ circles were preoccupied with responses to those.
- Partially affected by these affairs, the domestic economy that deaccelerated from the first half of ’91 further aggravated signs of decline in ’92, and with no clue to recovery, the recessionary mood became stronger across corporations and household budgets.
- In mid-Aug. ’92, the average stock price of the first section of Tokyo Stock Exchange dipped from ¥15,000 at one point, marking the range of drop at 60% as compared to the highest price of ¥38,915.87 at the peak in the year-end of ’89., which manifested the consummation of the bubble economy.

Major Economic Indicators 1990－1996

Year	Nominal Gross National Product	Y/Y Growth Rate	Export	Import	Trade Balance	Foreign Re-serves	Rate of Depen-dence on Public Bond	Rate of In-crease in Con-sumer Price
	Billion Yen		Million Dollars					
1990	438,816	7.9	296,581	242,285	54,296	69,894	10.6	3.3
1991	463.174	5.5	320,610	232,376	88,234	68,230	9.5	2.8
1992	471.926	1.8	344,000	233,107	110,894	70,045	13.5	1.6
1993	476,746	1.0	366,227	244,207	121,882	101,737	20.9	1.2
1994	477,026	0.4	408,465	290,521	117,945	141,523	21.6	0.4
1995	488,523	1.9	439,699	343,512	96,187	203,951	26.4	－ 0.2
1996			408,703	351,966	56,737	219,357		0.4

- The consumer psychology cooled off with the drop in stock prices provoked a slump in sales of durable consumer goods starting with automobiles, audio-video equipments, and home electric appliances. Consequently, corporations, used to easily raise low-interest capitals from the market to conduct aggressive capital investments of a double-digit growth per annum during the bubble times, suffered from excess inventories, and coupled with an increase in the fixed cost burden like depreciation, substantially deteriorated their business performances.
- On the other hand, the export alone was going strong as noted earlier, and owing to the recession-led decline in imports, the current-account surplus in ’92 topped 100 billion dollars, recording the highest ever.
- This level of significant trade surplus could not be eased by the export expansion plan which was schemed upon request from top managements of U.S. auto industry and auto parts industry who visited Japan accompanying U.S. President Bush in Jan. ’92. The ground swell of pressures on Japan was also observed in the accord regarding Japan-U.S. semiconductor agreement, whereby Japan, as a compensation for the lifting of sanctions by the U.S., had to come to terms with specifying a share position of foreign-made semiconductors in Japanese market.

- It was in the financial and securities' industries that the bubble's aftermath was most grave, and particularly the treatment of defaulted credits of land-collateral loans became a serious issue in fear of triggering a credit insecurity. But due to the political turmoil in the wake of Sagawa Express affair, the '92 supplementary budget was not approved until Dec. making anticyclical measures fall behind the curve.
- In addition, the exchange rate, having been leveling off somewhat in a cheap-yen trend throughout the past 5 years, fell into a rapid appreciating-yen phasis once again starting in Feb. '93 against the background of Japan's substantial trade surplus, and recorded ¥100.40 to the dollar on Aug. 17. The yen, then, went back to sort of cheaper level toward the year-end.
- This higher yen worsened corporate profits centering in export industries, and they embarked on employment adjustments, which cooled off consumer minds only to add momentum to the consumptive stagnation.
- With restructuring like factory closedowns and cuts in personnel, the employment problem assumed serious proportions, where large corporations mapped out a plan one after another for cutting back on personnel by the unit of 1,000.

- Thence the government came out with “New Package of Economic Measures” in Apr. and “Emergency Economic Package” in Sep. after Hosokawa regime took over, and implemented counter-measures such as the investment scale-up in public sector, the tax incentive for promoting acquisition of a dwelling house, and the enhancement of lending. Additionally, on the financial front, the central bank rate was abated to 1.75% which was lower than at any time in history.

- But these policies, albeit offsetting the drops of business conditions, exerted a week pervasive effect for their scale. Japanese economy of ’93, although there was an expectation of reaching bottom in the first half of the year, turned back to low water due to the sudden appreciation of yen, thus came to see the old year out without presenting a vision for a rehabilitation from the deflationary spiral where daily activities dwindled on account of a demand deficiency in the magnitude unprecedented in the post war era.

- With respect to foreign relations during this time, Prime Minister Kiichi Miyazawa had a talk with U.S. President Clinton in Tokyo in Jul. ’93, whereat agreed on a framework of a new conference to comprehensively take up economic issues between the two nations that the both leaders had decided on at their meeting in Apr.: New Japan-U.S. Economic Council made a start.
- The framework was comprised of the following three pillars:

  ① Reduction of Japan’s current-account surplus and cutback in U.S. fiscal deficit

  ②Commencement of negotiation/discussion by sector and structure

  ③Corporation in environment and technology
- The final draft agreement of Uruguay Round was adopted, which was followed up by the consensus document signed by 125 countries/regions in Marrakech, Morocco on Apr. 15, ’94, whereby World Trade Organization (WTO) was set out for the establishment on Jan. 1, ’95 in succession to GATT.
- Amid this movement to aspire for maintaining/promoting the world’s free trade structure, U.S. strategy to place an importance on bilateral talks stayed unchanged as seen in the new economic council as in the above, reinforcing movements to form a block economy that could have led to a discrimination of extra-area trades.

- World economy from ’95 to ’96, while growths slowed down in developed countries like the U.S, was on an expansionary course as a whole, developing countries centering in Asia maintained high growths.
- Particularly, at the moment Japan appeared to be turning its steps toward a recovery process, though moderate, in the beginning of ’95, Great Hanshin Earthquake occurred, and coupled with a steep appreciation of yen to ¥80 mark in the same year, Japanese economy quickly lost its momentum once again. Imports of products and raw materials from overseas surged, price tumbles known as the “price slashing” accelerated on the basis of the high yen, and an employment instability continued.
- Furthermore, the defaulted credit which financial institutions faced, and the decline of land prices which ingenerated that credit issue, stood in the way of an economic rejuvenation. The financial instability brought about the management crash even into banking facilities which had been said “never to go broke”; in the wake of collapses of two credit unions of Tokyo Kyowa and Anzen that surfaced in ’94, the management bust of Cosmo credit union, the largest inside Tokyo, hitched to the fore in Jul. ’95, and one month later in Aug. Bank of Japan made an announcement on the processing of Hyogo Bank, the largest of the second-tier regional banks, and Kisarazu Shinkin bank of the largest scale.

- And then, the yen exchange rate returned back to ¥100 mark in Aug. ’95, the central bank rate was slashed to a historical low of 0.5% in Sep., and reflationary packages like “the economic measures” of the largest scale were implemented, which succeeded in averting a bottom deepening of economic conditions.
- But in Sep. that year, the loss on off-the-book trading at an overseas branch of a Japanese bank came into the open, making confidence in Japanese financial system turn shaky, which engendered “Japan premium.”
- Japanese economy into 1996, under a long period of business stagnation since the burst of the bubble economy, underwent a transition being unable to seize an opportunity for a full-fledged recovery. And this situation led to de facto collapses of Sanyo Securities, Hokkaido Development Bank, and Yamaichi Securities in the fall of ’97.