

# The Japanese Economy Faces Independence\*

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## Three Fundamental Errors.

1. Since this paper has no unified thesis worthy of the name, let me make the most of what it has — an antithesis, with three heads. Discussion of current Japanese economic problems, particularly in countries or in economic circles competing with Japan, usually features at least one of these three types of statement:

a. Japan is a dangerous competitor largely because she has recovered more quickly and easily from the war than have her commercial rivals.

b. Japanese recovery is in fact practically complete and on a stable footing, thanks largely to American aid during the period of Occupation, and the world's humanitarian concern can be directed almost entirely elsewhere.

c. If the workers and farmers of Japan had a higher standard of living, they would furnish sufficient markets for Japanese production and reduce Japan's need to export her surpluses.

2. All three of these views are practically one hundred per cent wrong. Japan is dangerous not as an over-fed bully, but as an under-fed desperado. She is still, as one author has put it, "The Hungry Guest." Japan's

recovery is far from complete, her building and stock-market booms facades of surface prosperity, her basic problems unsolved, her future gloomy. And any rise in the standard of living of her workers and farmers would only increase Japan's need to import both food and raw materials, and therefore also her need for exports to pay for them.

## Basic Economic Problems.

3. Within a month after V-J Day (August 15, 1945), Japan found herself faced with a number of basic and inter-related economic problems. She had hoped to solve them through hegemony in a Greater East Asia Co-Prosperity Sphere, but had lost the war instead. The succeeding years have developed no postwar substitute for Co-Prosperity. There has been a measure of recovery, and a larger measure of stop-gap assistance, but the basic problems are as far from solution as they were in August 1945. The shift from military occupation to a measure of political independence contributes to their solution only in a manner most circuitous and indirect.

4. The Japanese living standard is itself a problem. Low by European or American standards before the war, it is still lower today. As of early 1952, Japanese national income per capita was estimated at 181 yen (\$46) of 1934-36 purchasing power, as against 209 yen (\$58) in the period 1934-36 itself.<sup>1) 2)</sup> This is a decline of over 13 per cent. The fall in real consumption per capita,

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which is probably preferable as a measure of the standard of living, is of the same order of magnitude. It is easy to be misled by aggregate statistics of industrial production (which reached 109 per cent of prewar in 1951) or foodgrain production (which reached 113 per cent of prewar in the same year). These figures are impressive and probably accurate, but they make allowance for neither fifteen years of population growth nor for the lagging of the imports required to supplement Japanese consumption.

At the same time, however, Japan's standard remains second or third in Asia. It is well above, for example, the standards of India and China. It is below that of Malaya, however, and may also be below that of Asiatic Russia. (We need not dwell on the political implications of the last-named inequality, should it indeed prove correct.)

5. Japan's national capital has also failed to recover from the war. Comprehensive and pertinent statistics are lacking, but we estimate that Japan's total wealth was reduced by wartime destruction and neglect by an extent approximating 35 per cent of its 1935 census value. (The loss in industrial capacity was 30 per cent, in shipping 80 per cent, etc.) The process of deterioration of fixed capital continued after the war, but new construction more than compensated for this, particularly

in such industries as textiles, iron and steel, shipbuilding, and electric power. There has undoubtedly been substantial recovery since the Surrender, but equally undoubtedly Japan's capital stock has not reached its prewar real value. Adjustment to a per capita basis makes the picture still more unfavorable. As for working capital, an inflation comparable with that of France has produced an acute shortage, and continuing pressure to relieve it by methods which only increase the degree of inflation.

6. We have referred several times to Japan's population in passing. Let us now consider the Japanese population problem directly. For a generation or more it has been commonplace to summarize Japan's problem in a catch-phrase, "too many people on too little land." Japan's population had risen from somewhat less than 30 million when Commodore Perry first visited Japan in 1853 to nearly 70 million in 1935. Urbanization and industrialization has been slow to check this upward rush; militaristic propaganda may have been one important explanation. After the war, however, militaristic propaganda vanished, but the increase was resumed faster than ever. A normal excess of births over deaths was augmented by the equally normal rise in the marriage and birth rate which ensues when troops return from overseas. In addition, five million overseas Japanese from China, Korea, and elsewhere were absorbed into the homeland economy, while Occupation sanitary and medical measures reduced death rates. The present Japanese population is approximately 85 million, and may reach 100 million as early as 1965. Japan's population density is over 560 per square mile, and approximately 3,600 per square mile of arable land.<sup>3)</sup> The excess of births over deaths, however,

1) Statistics in this essay are derived from Jerome B. Cohen, *Economic Problems of Free Japan* (Princeton: Center of International Studies, Princeton University, 1952) which contains an excellent up-to-date selection. (I do not, however, agree with the major policy conclusions of this volume.)

2) The period 1934—36 comprises the three (depression) years which immediately preceded the "China Incident" of 1937, after which Japan was engaged in large-scale military operations until 1945.

has fallen from 25.7 per thousand of population in 1948 to 15.6 per thousand in 1951, and the annual increase per year from 1.5 million to 0.8 million during the same period. Stability of population, however, may not be restored in the present century.

7. The war has also disrupted quite completely Japan's international trade adjustment, both on its import and on its export side. The direct loss of territory — 52 per cent of the land area previously incorporated into the Empire, including Formosa, Korea, and Southern Sakhalin — is less important than the loss of raw materials and markets both in these territories and elsewhere in the former Co-Prosperity Sphere.

8. Taking the import side first, Japan's food deficiencies were supplied at bargain prices by the Japanese Empire before World War II; there was even a small surplus for re-export. Korea and Formosa no longer export rice in large quantities. If they did, Japan could buy only at high world prices. Similarly, Japan's prewar imports of soybeans, coking coal, and iron ore came from North China and Manchuria, nominally independent but within the Co-Prosperity Sphere; terms were again exploitative. Any future imports from this area must be at or even above world prices. The exploiting power has changed hands, for reasons to be considered be-

3) Comparisons between Japan and some other leading countries are tabulated below:

Country and Year	Population Density	
	Per Square Mile of Total Area	Per Square Mile of Cultivated Area
United States (1950)	41.9	213.3
United Kingdom (1950)	536.9	1763.5
France (1949)	195.4	509.3
Germany (Western) (1950)	493.4	1424.7
China (1948)	203.4	1639.3
Japan (1950)	563.3	3596.1

low.

9. At the same time Japan has lost the markets for her major exports. China, including Formosa and Manchuria, absorbed over 40 per cent of Japan's total exports in the pre-war decade. That market is now largely closed by a combination of political considerations, Chinese industrialization, and the development of Sino-Soviet trade. As for Japanese exports to Europe and America, they were dominated by raw silk and silk fabrics for the 70 years ending in 1940. With the world silk market cut drastically by the development of nylon,<sup>4)</sup> Japan has no replacement as a source of foreign exchange.

10. Difficulties in balancing Japan's international accounts follow naturally from the combination of increased need for outside imports, higher import prices, and loss of export markets. Indeed, there is pressure from both sides simultaneously; Japan's trade and payments position has been gripped since 1945 in a vise or nut-cracker. As though this were not enough, the Japanese position is further imperilled by the inconvertibility of the pound sterling. Japan's sales are concentrated in the sterling area and her purchases in the dollar area, so that hardship is imposed when her accumulating sterling balances are limited in convertibility to dollars.

Japan's international accounts — the attainment of national self-support through a viable international balance — form the crux of the entire Japanese economic problem. The peculiar importance of Japan's international accounts to her economy parallels the importance of the British accounts to the United Kingdom; the reasons are likewise parallel.

4) As a result of competition from nylon, Japan's annual raw silk output fell from 650,000 bales in 1935-39 to 180,000 bales in 1951.

Japan must import simultaneously a crucial 15 to 20 per cent of her basic food requirements and considerably larger percentages of the raw materials for all but one of her major commodity exports.<sup>5)</sup> If Japan imports too much food, she will lack raw materials for the exports which pay for the food. If she imports too much raw material, her workers will have nothing to eat while the material is being processed.

11. Japan's real problem as a nation, it cannot be overstressed, is not disposal of surplus *exports* but payment for surplus *imports*. In this respect again, it resembles the problem of Britain. Each rise in Japan's relative living standards makes Japan more difficult rather than more easy. It increases the demand for food, which must be imported at the margin.<sup>6)</sup> At the same time, it retains for home consumption part of the products which must be exported to pay for the imported food.

12. Of Japan's commodity exports, we have said, only one is really "made in Japan" with-

5) Japan must import 100 per cent of her cotton, wool, phosphates, rubber, nickel, tin, and bauxite, 82 per cent of her iron ore, 88 per cent of her oil, 80 per cent of her salt, and 70 per cent of her coking coal.

The United Kingdom is more dependent than Japan upon outside sources of foodstuffs, but less dependent upon outside sources of raw materials, particularly coal and iron. The similarity is still obvious enough, particularly since both are island nations, for Japan to be referred to constantly as the "Britain of the Orient."

6) Net calories consumed per day in 1950-51 are estimated by the UN Food and Agriculture Organization at 2142 in Japan, as against 3233 in the United States, 3080 in Great Britain, 2700 in France, and 1600 in India. From this comparison one can deduce the likelihood of increased demand for food following any increase in the Japanese standard of living. (The corresponding 1934-38 averages for the four countries are 2180, 3150, 3100, 2830, and 1970.)

out requiring imported raw materials. This exception is silk. This is another reason, quite apart from the quantitative importance of silk in Japan's prewar trade, why the worldwide decline of silk has caused such a stock to Japan's international economic position. It was a stroke of ill-fortune that the invention of nylon coincided so closely with the collapse of the Japanese Empire and the Co-Prosperity Sphere.

13. Apart from current trade transactions, a heavy weight of potential foreign indebtedness hangs over Japan's international accounts. Japan owes the rest of the world only \$454 million in prewar foreign exchange bonds. However, war reparation claims amounting to slightly over \$20 billion have been presented by several East Asian countries; when and if China and Korea present their bills, the total will be much higher. In addition, Japan owes the United States \$2 billion for postwar aid, although this claim seems likely to be waived. The final amount of Japanese reparations liabilities is still under negotiation, but service on any substantial portion of the claims appears completely fantastic under present conditions.

14. A final key problem facing Japan is uncertainty regarding the nature of her future economic and political system. The prewar pattern of monopolies and cartels may be re-established. A free-enterprise capitalism like that of Canada or the United States may come to dominate. There may be nationalization or socialization on either British or Russian or Chinese patterns. If war should break out, there is danger of invasion or occupation from Siberia, from China, or from Korea. Aerial attack from one or both sides is practically certain, however sincere Japan's attempts to maintain neutrality in such a con-

flict. There is danger also of internal revolution from the Marxian Left, and somewhat less danger of internal revolution from the Nationalist Right.

These political and economic dangers and uncertainties naturally reduce the attractiveness of any but short-term private commercial lending to Japan, almost regardless of such offsets as tax concessions. As a matter of fact, in the first two years following legalization of private foreign investment (1950—52), only \$ 50 million gross (perhaps \$ 30 million net) of foreign private capital actually entered Japan. The same dangers and uncertainties also reduce the attractiveness of any but short-term domestic investment by Japanese capitalists themselves. As in many another country less developed economically, potential savings are squandered in luxury consumption, while a high level of statistical “capital formation” represents bank loan expansion of a questionable character. Investments concentrate in short-term projects — speculation in inventories, securities, and real estate. Downtown Tokyo, with its building boom, night clubs, and milk baths, gives visitors from abroad inflated ideas of Japan's recovery and capacity to pay war reparations. Economists should view these phenomena as they should have viewed the American stock-market boom of 1928—29, rather as evidence of the unattractiveness of more productive investment. At any rate, this is not the way Japan was originally modernized during the great days of the Meiji Emperor (1867—1912).

#### Short-Run Solutions.

15. Although bringing about a substantial degree of recovery from post-war paralysis, the Allied Occupation solved none of these basic problems during its seven years of authority. It began by renunciation of all res-

ponsibility for Japan's economy. This blindness was cured in a few months by exposure to the facts of Japanese life, and replaced by short-term aid coupled by intensive study of the problems involved — by personnel whose turnover was usually too rapid for maximum efficiency.

During the five-year period 1945—50, the Japanese economy was supported by approximately \$ 2 billion of direct United States aid in goods, mainly distributed by an agency called GARIOA (Government Administered Relief in Occupied Areas). A secondary source of short-term aid arising from the Occupation was the sale of foreign currency for yen by members of the Occupation Forces.

Since 1950, direct aid has been replaced by another windfall in the form of “special procurement” of military supplies for United Nations forces in Korea. These in turn may be replaced by special procurement of defense goods for the United States domestic rearmament program and of civilian supplies for Korean reconstruction. The Korean crisis also brought on for 18 months or so an international “gray market” in which Japan was able to sell a wide variety of goods, especially metals and machinery, despite prices higher than prevailed in the United States, the United Kingdom, and other normal competitors. These developments, combined with private purchases in Japan by members of the United Nations forces themselves, caused Japan's dollar cash holdings to rise from \$ 278 million at the opening of the Korean War to \$ 660 million in May 1952.

An unfortunate aspect of the picture of a succession of temporary and artificial supports has been its effect upon Japanese business and financial circles. These have been able to evade or avoid serious attempts to adjust

to Japan's long-run dollar-shortage position. Their outlook alternates with the headlines between complacency and desperation; the former attitude has been predominant.

16. Americans have asked in increasing numbers, "Has aid to Japan been a complete waste? Has America been pouring water down a rat-hole in Japan?" The answer is in the negative. The aid has not been a waste. It has done good in Japan; in fact, the Japanese economy would have collapsed without it. It has been not a waste but a stop-gap. Unlike the Marshall Plan in Western Europe, it was devoted almost entirely to relief and hardly at all to recovery. It afforded a kind of breathing spell, of which full advantage was taken neither by the Americans nor by the Japanese.

American relief has undoubtedly done good and been appreciated in Japan. Equally undoubtedly, it has been resented elsewhere in Asia, particularly in China and the Philippines. The Chinese and Filipinos see America support the Japanese living standard at a level higher than their own, after they had been America's allies in the war against Japan. From an ethical viewpoint, their resentment is only natural, particularly since they had hoped to receive for themselves some part of the assistance which went in reality to the Japanese.

17. Is continued aid a long-run solution? No more so in Japan than in Europe. It is not looked on as such by the Americans, particularly the American taxpayers. Neither is it expected by the Japanese. Dependence on American aid weakens them with respect to elements in America who seek to attach humiliating conditions to the continuance of such aid. The Japanese are proud of never having fallen to "colonial" status.

18. Does formal political independence (recovered April 28, 1952) change the situation in any fundamental way? Is independence itself any kind of solution? The answer must again be in the negative. Independence gives the Japanese more freedom to exercise their own ingenuity to solve their own problems, without the need to secure SCAP agreement, which was a paralyzing element at times during the Occupation. But freedom is no guarantee of success. Ambitious Japanese plans for self-sufficiency in food for Japan proper through land reclamation, or through settlement on the northern island of Hokkaido, have been failing steadily for over half a century, due to the increase of Japan's population. More recently, an ambitious five-year plan to achieve a balanced international payments position by 1953 collapsed before the realities of Communist control in China and fighting elsewhere in East Asia. In general, too, Japanese political and economic groups — business, agriculture, and labor alike — have devoted since the Surrender more insight and ingenuity to protecting themselves against a coming deluge than in preventing or even postponing the deluge itself.

#### **Longer-Run Solutions.**

19. In considering Japan's long-run economic position, it is easy to reach conclusions of utter despair. Indeed, it is difficult to avoid them. They may be summarized as a choice between three unhappy alternatives, singly or in combination: a sharply reduced population, a drastically lower standard of living, and international beggary on a grand scale. Barring some technological miracle, does Japan have any escape over the longer period?

20. Of all the long-run solutions which I

have seen suggested, no single one is large enough to meet the massive problems involved. If there is to be a solution, or even a significant alleviation, it will have to be a multiple one. It will have to be brought about through some combination of several small items, no one of which would make much impression by itself. In the remainder of this discussion, I should like to note the attractive and the unattractive aspects of several such small items.

21. Contrary to popular opinion, we have seen that raising Japan's relative standard of living would make her trade position worse instead of better. The converse proposition seems to hold. Some lowering of Japan's standard of living (closer so the level of Continental Asia) would improve Japan's chances of international self-sufficiency. It would reduce the production costs of Japan's exports, and also the volume of Japan's necessary imports. It could be brought about, for example, by a further devaluation of the Japanese yen, if the devaluation were followed by refusal to raise wages when the prices of imported consumer goods rose, and if the strikes that would surely follow were broken by police and militia action. This is all true, but as we have also seen, the Japanese standard of living is still 10 or 15 per cent below pre-war. The Japanese people, like the Europeans, are impatient for the cut to be restored, and indeed for something better. Any further cut, even a small one, is possible only under a dictatorial or Fascist Government, in the political realities of present-day Japan (which are no different in this respect from those of France or any other Western European country). Any Japanese government strong enough to "sit on bayonets," to retain power while lowering the living standards

of the Japanese people, would probably also be strong enough to threaten the peace of Asia. It would be feared and hated not only by China and the Soviet Union, but also by Australia, Korea, New Zealand, India, and the Philippines. It might face external attack before being permitted even to consolidate its domestic power.

22. Confiscation by the State of most or all of the rent, interest, and dividend income now received by the Japanese capitalists is a solution which has wide appeal in the Japanese cities. It would furnish resources for raising the living standards of the remainder of the population without foreign aid. At the same time it would permit financing of capital improvements (again without foreign aid) which would lower production costs and increase output in the longer run. This is the Marxist solution. It has been applied in Eastern Europe and in China within the past decade, and is advocated by the Japanese Left Wing. The Occupation has indeed applied it partially in Japan itself, however unintentionally, in its celebrated program of land reform.<sup>7)</sup> The preference of Japanese capitalists for consumption and short-term speculation over long-term investment in productive facilities adds to the force of this position.

23. Less drastic than either the Fascist solution of lowered living standards for the masses, or than the Marxist solution of expropriation for the capitalists, is the Japanese

7) Japan's large holders of agricultural land were compensated by national bonds, whose purchasing power fell to negligible proportions during the postwar inflation. (The result of the reform has been a peasantry relatively satisfied and stable by comparison with the urban workers who form the mass base of the Socialist and Communist Parties.)

industrialists' own hope for lower costs, particularly lower export costs, through increased labor productivity. Labor productivity in Japanese industry could be increased readily by wholesale dismissals of manual workers and office employees who are surplus by American standards, but Japanese capitalists shrink from such "beheadings." Their motives are partly feudal, partly humanitarian, partly nepotistic, and partly fear of trade-union reprisals. To increase productivity without mass unemployment requires heavy capital investment in plant and equipment, both to supplement what the Japanese have and to replace some of the depreciated and obsolete relics in their present factories. This capital must come largely from abroad (meaning the United States), although the Japanese capitalists could doubtless reduce their dependence on foreign sources by venturing a larger part of their own incomes. There is particular hope of attracting foreign capital (but not foreign control)<sup>8)</sup> to such industries as chemicals, electric power, iron and steel, shipbuilding, and textiles. Within the last-named field, new synthetics like orlon and vinylon are receiving special attention. For here are fibers which, like silk, can be made in Japan from Japanese raw materials such as limestone and water-power, without imports of cotton, wool, or wood pulp. Their development might provide Japan with a replacement for her vital silk export industry.

Once a solution or solutions for Japan's economic malaise is in sight for other rea-

8) Foreign investment in Japan must be approved by the Foreign Investment Commission, which is extremely reluctant to approve investment contracts involving more than 50 per cent foreign control of a Japanese enterprise. It is expected that approvals will become extremely rare, although some have been granted.

sons or from other sources, it requires no rash optimism to expect progress to be hastened by an influx of foreign private capital. But in view of the risks involved in Japan and the alternative opportunities available elsewhere, it is surely futile to expect the exclusive, or even the initial, contributions to Japanese recovery to spring from so cool, calculating, and hard-headed a group as private international investors. For the present at least, more humanitarian and altruistic investors such as the International Bank for Reconstruction and Development are probably more promising sources for capital assistance. These would doubtless be concentrated in what have come to be called "social overhead capital" projects such as highway improvements, reforestation, flood control, electric power, and perhaps plant and equipment for education and social services. All of these are sadly needed in Japan, but are not primarily in the minds of Japanese industrialists when they list the projects which they would like to finance with foreign funds.

24. Japan's share of world trade — which has itself been declining as a total — is still far below its pre-war value. Whereas in 1937 Japanese exports and imports were each 5.0 per cent of the global aggregate, the 1951 percentages are 1.8 and 2.5 respectively. Professor Cohen has estimated, on the basis of reasonable extrapolations of the Japanese population, that Japanese exports in 1955 must rise by \$1,543 million and Japanese imports by \$1,236 million if the real per capita levels of 1934—38 are to be regained.<sup>9)</sup> One might expect therefore to see, in view of the vital

9) Cohen, *op. cit.*, Table 28, p. 66. The "dollars" are of 1951 purchasing power, and the "exports" do not include possible military procurement items.



importance of international trade to Japanese economic life, diversified interest in expanding Japanese trade with all countries, all regions, all power blocs alike. But such is in fact not the case. One group of Japanese business men and publicists, by no means exclusively of Marxist persuasion, sees Japan's salvation entirely through increased trade with Communist China, the Soviet Union, and the remainder of the Soviet bloc, to the exclusion of opportunities in Southeast Asia and the Western countries. Another group finds Japan's major hope in expanded trade with Southeast Asia, a secondary hope in trade with the United States and Western Europe, but is willing to eschew economic relations with China and Russia. It is no exaggeration to refer to a "China" versus "Southeast Asia" controversy as being in constant progress within Japan itself.

The best source of rice imports for Japan is Southeast Asia — particularly Thailand, although both Burma and Indo-China will also have large exportable surpluses if peace is restored. China and Russia have no significant amounts of rice for export. The best source of soybeans, coal, and iron for Japan is Manchuria, now known as the Northeast Province of the Chinese People's Republic. No Southeast Asian country can furnish these goods in adequate amounts, although iron production is being expanded (with Japanese technical assistance) in India, Malaya, and the Philippines. With all respect for potential miracles from revived multilateral trade, it is clearly ridiculous and almost suicidal for an over-populated trading and industrial nation like Japan to cut herself off from either area for the sake of trade with the other.

25. Expanded trade with China and Russia, particularly with China, is probably the catch-

word most widely favored in Japan today as a solution to all her economic problems.

(The Japanese have a weakness for such slogans or catchwords; the Peace Treaty was expected likewise to solve all Japan's problems, until it was ratified and solved none of them.) And indeed some expansion in this direction is inevitable, even at the cost of reduced aid or capital imports from the United States. Manchuria and North China remain, as has been said, Japan's best sources of coal, iron and soy-beans; she will not continue indefinitely imports from the United States at inflated prices. Furthermore, such areas as West China and Siberia provide the only large-scale immigration opportunities open to Japan's surplus population, although as yet little enthusiasm has developed for immigration to these cold or barren regions. If, as the Japanese claim, their trade with China is subjected to greater restrictions than is America's or Western Europe, it is difficult to see how the movement for liberalization can be resisted, either by the Japanese or the American Government. (British opinion favors expanded Sino-Japanese trade, which would reduce Anglo-Japanese competition in other world markets.)

But it would be highly dangerous to Japan to place total or major reliance upon expanded trade with either China, or Russia, or an economic bloc headed by these two countries. Both China and the Soviet Union are sub-continent, potentially almost self-sufficient at any standard of living, and even now relatively autarchic at their present low levels. In addition, the control over their foreign trade is centralized in State agencies; there is no competition among Russian or Chinese traders, of which Japanese might gain advantage. Japan, on the other hand,

needs trade in order to survive, and much of Japan's negotiation is carried on by relatively small and highly competitive brokers and traders. Under these circumstances, one does not need the ingenuity of a Hitler or a Schacht to seize the chance for exploiting Japan. Japanese goods would probably be falling constantly in money or barter value relative to Chinese or Russian goods — that is, Japan's terms of trade would probably be deteriorating constantly.<sup>10)</sup> A subsidiary problem is the possible financing of revolutionary activities in Japan with the yen proceeds from Chinese and Soviet exports. (Rumors in Osaka and Kobe in the summer of 1952 had the Japanese Communist Party supported largely by the illegal sale of Chinese opium smuggled into these two ports by Communist agents.)

26. Until she became dependent upon Thailand for part of her rice imports, Japan had never considered trade with Southeast Asia as particularly vital to her economy. Today there is some feeling that, with China cut off by political differences, a substitute salvation may be found on the remainder of the Asian Continent. Japanese trade with the "ECAFE Region," particularly her export trade, has grown rapidly since 1949. Certainly, if Southeast Asia were to develop economically, this area could serve simultaneously as a source for not only rice but likewise, rubber, tin, petroleum, cotton, and iron ore, and

10) I have met Japanese Marxists who believe that the labor theory of value can fix the relative values of Japanese and Chinese goods and thereby prevent exploitation of either party by the other. Even if we suppose that Japanese goods can be reduced to hours of Japanese labor, and Chinese goods likewise to hours of Chinese labor, does the labor theory of value tell us how many hours of Chinese labor is equivalent to one hour of Japanese?

as a market for a wide range of Japan's manufactured products, from textiles to textile machinery and from bicycles to locomotives. Japanese technical assistance is also assisting to develop Asian supplies of coal, iron, bauxite, etc., to replace politically expensive Chinese and economically expensive Western sources.

One key question, however, is whether the economic development of Southeast Asia will materialize soon enough and on a large enough scale to assist Japan in its present plight. On its pre-1950 level, Southeast Asia is still too small and unimportant an economic region for trading partnership with a relative giant like Japan. And as yet, the development of Southeast Asia has been lagging far behind schedule, partly because of the diversion of funds to the Korean War and partly because of delays in the restoration of peace to Burma, Indo-China, Indonesia, Malaya, and the Philippines.

Another question is whether the Western Powers — the United States, the United Kingdom, and France — will permit Japan access to the Southeast Asian market on equitable terms when development begins to take hold. (The Japanese resent, for example, Britain's refusal to sanction Japanese participation in the so-called Colombo plan for the development of Southeast Asia.) Actually Japan has little discrimination to fear if development is on a large enough scale to provide opportunities for all. If the development program is petty and niggardly, however, there will naturally be great temptation to restrict the limited benefits to countries which were first in the field.

In countries economically independent of Western influence, it will be Asian nationalism and Asian resentment of Japanese Oc-

cupation during World War II which may prevent Japan from full participation in the benefits of any but the largest-scale development program. In light industries like textiles, especially, Japan's export possibilities will be subordinated to the development of both factory and cottage industries in the Southeast Asian countries themselves, both for nationalism and for diversification. Japan's long-term export prospects look much better in heavy industries like machine tools and transportation equipment. For the shorter period, Korean reconstruction is the most promising single all-around market. Imports for Japanese factories will probably become more abundant as Southeast Asia develops, in spite of proposals for processing plants and refineries in the producing countries themselves.

27. It is difficult for a realist to anticipate any great increase in Japanese access to Western markets within the next decade. Her exports are either luxuries, like silk, or highly competitive with Western products, like fish and textiles. In the United States, Japanese fish, crockery, toys, etc., rouse demands for increased tariff protection every time they become large enough in volume to promise assistance to Japan. (Since, by the same token, they become large enough to disturb the competing domestic industry.) In Great Britain and the Commonwealth countries, dollar shortages have been more real and less potential than Japan's, and the Sterling Area as a whole has had an unfavorable balance with Japan. Here, sharpened Imperial preference and agreed cuts in imports have made life difficult for the Japanese exporter. Until this time (Spring, 1953) British influence has also denied to the Japanese access to the reciprocal tariff reductions of the GA-

TT agreement (General Agreement on Tariffs and Trade).

There is a measure of truth in the rationalizations by which Japan has been excluded from GATT — Japanese wages are lower than the wages paid by their British competitors, and may be held down by monopsonistic exploitation; occasional desperate Japanese exporters "dump" in world markets by selling below their Japanese asking prices, while others have been known to forge foreign trademarks and otherwise disguise the origin of their goods. Yet it is difficult for the neutral observer to avoid the feeling that, under the guise of commercial morality, Japanese export trade as a whole is being assessed penalties appropriate to felony because of the international misdemeanors of a minority, and that by a judge whose impartiality is open to question. It may be too strong to say, as has been said, that increased tariffs and rigid quotas on Japanese exports in Western countries will drive Japan into the Communist camp, but their effect is manifestly in no opposite direction.

28. Exchange rate adjustment is an important phase of the Japanese economy in which political independence may mean a substantial grant of freedom and power, although Japan has somewhat limited this new freedom by adherence to the International Monetary Fund and International Bank for Reconstruction and Development. The present exchange rate of 360 yen to the dollar was imposed by the Occupation (on the advice of Mr. Joseph M. Dodge, presently Budget Director of the Eisenhower Administration) in April 1949. Majority opinion in Japanese business circles criticized this rate as over-valuing the yen at that time. This opinion was strengthened when Japan was not permitted

to meet the British and other devaluations in the Autumn of 1949, and again when the rate has been maintained through the Korean War inflation. The 360—to—1 ratio overvalues the yen somewhat in terms of purchasing power, and it may be surprising that it has not been revised in the first year of Japanese independence.

An economist, however, may doubt whether any simple alteration in the dollar-yen rate will assist materially in Japan's struggle for a viable economy. The interests quietly urging devaluation to 400, 450, or 500 to the dollar are export interests. They see such action as improving world markets for Japanese exports — primarily at British expense — and they are probably correct. (Retaliatory devaluation on Britain's part would be difficult to justify, since Japan was not permitted to meet the British devaluation of 1949.) on the other hand, devaluation would also raise the prices of Japan's essential imports of food and raw materials from dollar countries. Increased food prices in particular would probably set off another wave of domestic inflation unless, as suggested in paragraph 21 above, they become a mechanism for lowering the people's standard of living another notch.

From the viewpoint of avoiding domestic inflation, upward revaluation of the yen (to 300 or 250 to the dollar) would cheapen Japan's food and raw material imports in terms of yen, and would therefore be a step forward. But no such move is favored in Japan, since it would either price Japanese exports out of world markets or at the very least force contraction of profit margins throughout Japan's manufacturing and export trades. (These profit margins appear exorbitant to foreigners, 20 and 25 per cent per year on

invested capital being not uncommonly reported in company accounts. These high profits, however, must be viewed in the light of the high risk of loss involved, and likewise in the light of the inadequate depreciation allowances which have been computed with insufficient regard for the rising replacement cost of capital.)

29. To secure simultaneously the benefits of devaluation (lower export prices in foreign currencies) and appreciation (lower import prices in domestic currency), a number of countries throughout the world have turned to multiple-rate systems of foreign exchange, despite the disapproval of the International Bank and Monetary Fund. Among Far Eastern nations, Indonesia and Thailand have taken the lead in this development. Its purpose is to make essential imports cheap at home and those exports cheap abroad where foreign competition is important, while making non-essential imports expensive at home and extracting maximum monopoly profit from those exports where competition is lacking.

In the Philippine Republic, the peso is markedly overvalued as a result of fixation of an unrealistic rate in a philippine-American treaty, but a tax on purchases of foreign exchange (except for essential imports) serves some of the purposes of a multiple-rate system. The Philippine example may be more useful for Japan than the open and complex multiple-rate systems of Indonesia and Thailand. Japan may find it helpful, at least temporarily, to devalue the yen on the export side, and apply the export rate to discourage luxury imports. At the same time, however, she may be able to hold the price-stability line at home by keeping the import rate for essential food, raw materials, and capital for

development at the present rate or even at a lower one. Some such system, I believe, is worth considerable study, although it conceals at least two inflationary features which may be serious. One is the pressure it would put on the Japanese budget, already strained by "internal security" expenditures. If every dollar of exports requires the Foreign Exchange Control Board to pay exporters 400 yen, and every dollar of essential imports brings in from importers only 360 yen, the Control Board would run a 40-yen deficit on every dollar of balanced trade. A second source of inflationary pressure might be increased foreign demand for Japanese export products themselves, which in the case of textiles, iron and steel, building materials, etc., is reflected almost at once on the internal market.

#### **Toward Foreign Understanding.**

30. Some observers see the Japanese economic scene as completely black. Most observers see it only as gray, but a dark shade of gray. Bright spots there are, in the form of hopeful possibilities. We have listed some which look most promising; needless to say, there are a number of others. Under present conditions, no one of them is large enough quantitatively to provide a remedy, or indeed anything more than a palliative. Some combination of two or three or more may cumulate into a cure before it is too late. But despite the celebrated industry and endurance of the Japanese people, cumulation cannot be guaranteed, much less early cumulation.

Meanwhile greater understanding by foreign countries is in order. Few, apart from the United States, will be able to make positive contributions to the Japanese economy; <sup>11)</sup> most are too completely occupied with

their own domestic and regional problems. They can, however, refrain from interfering with Japan's recovery, and resist temptation to discriminate against Japanese trade and shipping.

Among "foreign countries" must be included an America which has sunk more capital than it had intended into Japanese aid, and has received a smaller return than it had expected. Western Europe and the British commonwealth must likewise be included, as having suffered most from the desperation and "unfairness" of Japanese economic competition. Understanding by all foreign countries can assist Japan to keep her head above water until the Cold War decreases in intensity, until Southeast Asia develops, until Japan's population stabilizes, or until some other fundamental solution is worked out. Active assistance of Europe and America may,

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11) Professor Cohen (*op. cit.*, p. 88) has formulated a 12-point program of possible American assistance to Japan, of which the following eight provisions are of special interest to third countries:

"1. Cancel the \$ 2 billion aid debt which Japan owes the United States.

"2. Give Japan sizable defense contracts each year for five years after special procurement for Korea and possible Korean rehabilitation ends.

"3. Revise tariffs downward on those products which Japan can sell in the United States.

"4. Undertake a campaign to educate the U. S. public to the current need to buy Japanese goods.

"7. Expand development aid to South and Southeast Asia and require that external costs be met by procurement in Japan.

"10. Develop Alaskan wood pulp and lumber products from government lands to be sold to Japan on a cost basis.

"11. Insist that Japan be admitted to GATT and accorded most-favored-nation treatment.

"12. Condition aid to other countries on the requirement that they not discriminate in trade against Japan."

in the case of Southeast Asia especially, benefit the Southeast Asian countries and the developed countries and the developed countries as well as Japan.

Sunrise is a long way off in the Land of the Rising Sun. Such moonshine as we have outlined may substitute for sunshine until the dawn, or it may not. This much, however,

can be said with some confidence. Restriction against Japanese trade is a mistake, however righteous and humanitarian may be its motivation. And any call to Japan to soften her economic competition and raise her export costs in return for favors past, present, or future is bad economics, regardless of any ethical plausibility.

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## Résumé of Articles

### SHIONOYA, Tsugumo, "Classical Theory of Technical Progress"

The theory of technical progress has been taken up for discussion anew parallel with an advance in the theory of economic development based on the Keynesian school of economics. On this particular issue, however, there are not a few questions requiring clarification. To make good in this issue, it is necessary to study again the theory of technical progress as embodied in the classical school of economics. The reason is that the theory of economic development which is to include in itself the new theory of technical progress is by nature to take the place of the similar ideas developed in the classical school.

"The Wealth of Nations" by Adam Smith which laid a firm foundation for the classical school of economics as a system governing the theory of economic development deals with technical progress as a development of division of labor. According to Smith, division of labor develops hand in hand with capital formation which constitutes the propelling force of economic development. His theory on a decline in the rate of profit and

his conception of steady society appear as if each of them indicated the conditions limiting capital formation or a development of division of labor and the latter's consequences. But the relationship between his way of thinking on this specific point and his theory that a development of division of labor rests on the scope of the market is not clear. The reason is that the basic principle governing effective demand that is necessary to understand all these uniformly is lacking.

Adjusting the theories developed by Smith, David Ricardo completed the classical theory of economic development. His economics is divided into two systems. One is the system on the theories of long-term equilibrium which, on the assumption that technics is unchangeable, analyzes the process by which an economic system is converged into a stationary state without development because of a decline in the rate of profit resulting from the law of diminishing returns. The other is a system of the theories on long-term movement which analyzes the process by which technical progress suspends its process of convergence into a stationary state under an economic system and works out its