

The Effects of the Recent Deflation Policy upon the Economy of Japan

The Economy of Japan in 1953 had shown a striking expansion, accompanied with notorious level-up of industrial production, national income, wage and consumption rates, without giving rise to remarkable upwards trend in commodity price movements. However, such an increase of activity inside this country naturally led to a decline in her foreign investment. The balance of payments in this year accounted \$ 194 million deficit, which led the international balance of Japan to a critical point. Hence, in 1954, the government had decided to adopt deflation policy, which was mainly realized by tight money policy and government fiscal retrenchment, in order to attain the consolidation and reconstruction of Japanese economy. As the result of this policy change, the Japanese economy which had walked one-sided expansion way since the Korean boom turned for the first time to the process of recession. In key statistics, there were seen the downwards movement of prices, the drop in mining and manufacturing production, rapid level-off of wage and national consumption, and the other general deflationary phenomena had gradually permeated; such as the increase of smaller firms falling into bankruptcy, the increase of unemployment, the monetary stringency in business circles, etc., However, since the middle of the year, with the turning of export to the upward trends and that of balance of payments from deficit to surplus, the progress of recession reached its bottom, and

towards the later part of the year there appeared some tendency of business recovery, seen in the upward turn of prices and re-increase of production. In addition to this, the uneasy political status led at last to the collapse of the Yoshida Cabinet and the birth of Hatoyama Cabinet, and with this political change there appeared in business circles some expectation of policy change from deflation to expanding economy. In some circles there were, however, the opinions warning such groundless expectative interests, but the economic circles in general greeted the new year anyway with somewhat bright feeling.

Now we follow the yearly movements of Japanese economy in 1954, referring with the key statistics available now.

1. *Prices.* It is the movements of prices which reflected the deflation policy mostly. We can divide 1954 roughly into three periods as to the wholesale price movements. First, the succeeding rising period from the beginning of the year to the middle of February, second, the time of sharp drop up to August, and third the period of reactionary rise from August to the year end.

The first step of deflation policy was started in October 1953 with the strengthening of higher rate application system by the Bank of Japan. But at that time the inflationary tendency was still strong, and moreover the continuation of speculative demand for fear of import cut still raised the wholesale prices by

1.5 per cent from the beginning of the year till the middle of February.

Hence, the tight money policy of the Bank of Japan was more strengthened in January and in March successively, and these policies cut down heavily the well-treated import finance, which had been considered as the source of credit expansion. In consequence, accompanied with the aggravation of short age of money, the wholesale price index turned at last to downwards trend, marking its peak of 162.1 (June 1950=100) in the middle of February. The index continued to fall with 1-3% of average monthly stride until 147.1 in August, and the rate of decline within this half year reached significantly 9.2%. Viewing the rate of decline by major commodity groups respectively, they were 13% in foods, 12% each in textiles and metals, 7% each in construction materials and miscellaneous goods, 6% in chemicals, 5% in fuels and 3% in machinery. But since about August the price movements ceased falling by the effect of upward turn in export and of some increase in inventory finance. Moreover, since September the general index showed upward trend reflecting especially the rise of prices of steel and steel products on account of the favorable export conditions, and registered 150.5 in December which was 2% higher compared with the bottom in August. Entering in this year, steel prices has been more strong reflecting the strong tone in world markets, and recently non-ferrous metals, especially copper, also follows the oversea high prices. But prices of textiles and lumber have always been weak on account of inactive domestic demand, and the prices of other commodities also remained almost unchanged in general.

Thus the average wholesale prices in 1954 was 1.5% lower than that of the previous year.

But taking into consideration 5.4% rise of food-stuffs which was the effect of the poor crops in 1953, the general prices excluding food were 3.2% lower than those of the previous year. Such a drop in domestic wholesale prices brought also naturally the fall of export commodity prices, and the high level of Japanese prices compared with international prices seen in 1953 was almost disappeared recently.

Contrary to the striking drop in wholesale prices stated above, the consumer price index (all urban) had shown rather strong trend from 188 (1951=100) in January to 121 in October. The reason is generally considered to be the time-lag of propagation from wholesale to consumer stages, but in this case this rather depends upon the fact that the consumer demands were held relatively strong notwithstanding the deflationary situation, which will be referred after. Further it was another reason that house rent and other charges and fees kept upward movements during this period inasmuch as they had been still in low level heretofore. However entering in November the consumer prices also fell to 118 on account of the drop of food prices, and stood still on the same level in December. Though the consumer prices kept the high level through the year, the upward trend can be said remarkably levelled off compared with the situation of the previous year, when the index showed 8% rise from 107 in January to 116 in December.

2. *Production and Stock.* Next to prices, production and stock suffered from strong effects of the deflation policy. The annual average of monthly production index of mining and manufacturing combined in 1954 was 165.2 (1934-36=100), which showed 6.5% increase from 155.1 of the previous year. Compared with the 23% increase in previous year, the rate of

increase was strikingly blunted. Viewing the trend through the year, in somewhat detail, it succeeded the increasing trend of the previous year, the index reaching the peak of 172 in March. But since about April, the deflation effect had gradually decreased the effective demand and brought the increase of producer's stock, turning from the heretofore decreasing trend of stock in dealers' circles on the beginning step. Then the production index began to fall on account of the short-time running of many firms and this tendency continued and the index showed 156 in August which was as much as 9% lower than the peak in March. The short-time operation was conspicuous in those industries, the products prices of which fell largely, that is steel, machinery, rubber and leather products, wool and wool fabrics and dyestuffs, etc., and it was generally heavier in durable goods than in consumer goods industry.

As to the trend of producer's stock position, though it increased gradually since January, when the stock index was 127 (1950=100), it turned into aggressive increase from April as stated above, and reached 190 in July, recording as much as 50% increase from January. However, here too, as the recovery of export began to exert its effect, the stock position turned to decrease from August and showed 154 in December. In response to such stock movement the production index also began to rise again, and restored up to 169 in December. But, compared these year-end levels to those of the previous year, the stock position is still 28% higher, and the production level is 2% lower.

3. *Wages and Employments.* The monthly average of employees wage of all industries in 1954 was ¥ 17,898, which showed 7% higher than that of the previous year. But,

compared with the increasing trend all through the year in 1953, the wage movements in 1954 did not show almost any significant change from ¥ 16,402 in January to ¥ 16,160 in November. In the other hand, as consumer prices rose 5% compared with the previous year's level, the real wage (after tax) of workers in manufacturing industries rose slightly by 2%, recording the index 106 as 1934-36=100.

Speaking about the employment, the index of all industries was 100.6 (1951=100) in 1954, showing almost no change compared with 100.4 in 1953.

However, though wages as well as employment have markedly levelled off the increasing rate in 1954, it was the fact to be noticed that in spite of being under deflationary situation they hold the highest level after the war and have not yet indicated any particular tendency to fall. This fact is considered as due to the following circumstances: first, the deflation pressure did not extend to labour circles, confined mainly to the cut-down of profit, and second, the existence of strong labor unions checked the cut-down of wages and employment. The deflation pressure in labor section appeared rather partially. The figures of wages and employments mentioned above do not include smaller firms under 30 employees. In these smaller firms bankruptcy, discharge and delay of wage payment occurred successively as these firms stand on poor foundations, both employers and employees together. Thus the number of perfect unemployment persons showed 580 thousand in yearly average, exceeding 130 thousand the previous year averages of 450 thousand, and in August it reached the peak of 710 thousand. Furthermore, the total amount of delayed wage payments in all Japan cumulated to ¥ 2,022 million in October from

¥ 516 million in January. Though this figure decreased to some extent since October, it still showed ¥ 1,476 million at the end of the year, and the employees concerned are accounted 147 thousand.

4. *Family Expenditure.* Monthly average of living expenditure of Tokyo workers' families in 1954 was ¥ 27,980, 13% increase compared with ¥ 24,787 in 1953. But considering the rise in consumer prices, the increase is only 6% in real terms. Thus the real consumption level reached just 100 as the prewar base (1934-36). But the consumption level of all families in all urban areas was exactly the same as the level of the previous year, showing no increase. The difference between this and that of Tokyo families is understood as due to the decrease of income in particular areas which consisted of specific depressed industries, such as coal minings and shipbuildings, etc., and at the same time as due to the more severe effect of deflation policy on small proprietors' families such as merchants and artisans. Nevertheless, though the increase rate was markedly slowed down in the sphere of family budget as well as in labour section, the deflation pressure was very slight and the highest level of per head consumption and wage after the war was maintained. If we were forced to say the effect of deflation in consumer's economy, we can only point out the decrease in propensity to consume or increase in propensity to save as the result of psychological reaction by consumers. In the case of Tokyo workers' families, living expenditures decreased from 83.7% in 1953 to 80.3% in 1954 as total actual income (before tax) taken 100, and the contrary savings ratio increased from 4.3% to 6.5%.

5. *Foreign Trade.* The direct aim of turning economic policy to the deflation taken from

the end of 1953 was to recover the balance of payments which run into very unfavourable situation on account of the abnormally expanded import at that time. But at the beginning, there remained urgent import demand of food on account of the poor crops on farm in 1953 and happened to continue some speculative import demand arising for fear of direct import-cut policy. Hence the amount of import did not turn to decrease even after entering in 1954, and the deficit balance of payments succeeded until May, cumulating as much as \$ 188 million deficit since the beginning of the year. But since March, as export came to turn to increase somewhat and import also turn to decrease, the balance of payments accounted barely \$ 11 million surplus in June. Since then, export kept up increasing trend and at the same time import showed sharp decrease. Hence the surplus increased month by month and cumulated \$ 288 million by the end of December. Thus the balance of foreign exchange payments recorded just \$ 100 million surplus in spite of the sharp decrease by \$ 209 million from the amount of previous year in receipts from special procurements. The value of trade was as follows: the export in 1954 was \$ 1,533 million increasing from \$ 1,156 million in 1953, and the import was \$ 1,962 million decreasing from \$ 2,101 million. This \$ 100 million of surplus is really \$ 294 million improvement compared with \$ 194 million deficit in 1953.

However, it should be noticed that such a favourable change in export owed rather more to the other reasons than to the direct effect of deflation policy. The export increase was focussed to the textile goods about the middle of the year, and later to the metals (mainly steel and copper), and to the mass contract of steel ships in the latter half of the year.

The main cause of these increases was the release of import limitation in sterling area in case of textiles, and the expanded demand for steel in European countries and the artificial enforcement of export owing to the poor domestic demand in case of metals, and the special link trade system as compensation export, etc. in case of vessels and other machinery or plants. On the other hand, the import decrease also owed much to the squandering away of stocks of materials imported in the previous year. Such circumstances will be anyway apt to bring the reincrease of import demand. Therefore we can not necessarily enjoy the unexpected favourable change of balance of payments in 1954 unconditionally.

6. *Summary.* The true aim of the recent deflation policy was to consolidate the economy of Japan in stronger foundation, in order to get into the stage of expansion without inflation in near future. This aim is not yet reached. The balance of payments has been recovered, but is still at an unstable situation. The promotion of export on the more stable condition through increasing the labour productivi-

ty and cutting down the production costs should strongly be requested hereafter. The commodity price level has come down near to the level of international prices. But the rising price factors in export industries are not yet remarkably eliminated. Moreover, wage costs are considered not to have been cut down.

But Japanese Government cannot adopt stronger deflation policy because of the serious unemployment problem. Unemployment statistics of Japan mentioned above only reveals a part of the number of unemployed. Japan has so many disguised unemployments of cyclical nature as well as of structural nature. The yearly rate of increasing labor force is as high as 1.4 per cent. Japanese economy must have a growth rate of more than 1.4 per cent in order to give jobs to these new labor force and at the same time, to raise the national income and consumption level perhead to some extent. Here mainly lies the limit of adopting the strong deflationary consolidation policy in this country.

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