"INCLUSIVE GROWTH: A NEW DEVELOPMENT CHALLENGE AND A NEW GROUND FOR REGIONAL COOPERATION"

--- a case of Japan ---

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1. What are the key features of your country's basic development strategy?

Japan's postwar economy may be divided into four periods. In the first, postwar economic reconstruction got under way, followed by the promotion of a self-sustaining economy under the Dodge Line policy of 1949, and Japan's return to the international economy with the establishment of a fixed exchange rate of Y360 to the dollar.

The Dodge Line, named after Joseph Dodge, the economic adviser to the General Headquarters of the Allied Occupation Forces, was a set of drastic anti-inflation measures based on the belief that a prerequisite for economic independence was stability of currency values, which was necessary to obtain economic aid. Under the plan, the government carried out such a strict policy of austerity that its budget for fiscal 1949 registered a surplus of revenues.

The second period from the latter half of the 1950's to the first half of the 1960's was marked by full-scale technological progress and rapid growth of the economy, a period which started with the Jinmu Boom of 1956, followed by a recession in 1958, then the Iwato Boom of 1959-1961, and an adjustment phase from 1962 to 1965.

The longest postwar period of prosperity was the third, which followed the recovery from a recession in 1965 and witnessed the clearing of the ceiling on the balance of payments that had until then been a major obstruction to economic expansion.

The fourth period began in 1970, after which the Japanese Economy underwent a major crisis amid the turbulent world economic situation and coped with a series of knotty problems, including the upward revaluation of the yen and worldwide spiraling prices for primary products, the petroleum in particular.

What factors enabled Japan to accomplish a rapid recovery ?

First, industrial facilities and technology had been accumulating since the war. Even at the end of the war, Japan had enough steel and machinery production facilities to meet domestic needs for some time.

Second, Japan renounced arms after the war, and this enabled the nation to concentrate its resources on the manufacture of civilian goods, which aided production activities. Moreover, low military expenditures rendered it possible to keep the scale of fiscal spending small. Consequently, Japan was able to reduce the tax burdens, which in turn facilitated the accumulation of private capital.

Third, the government lent assistance to private enterprises. Strong ties were formed between Japan's industry and the government, leading to the establishment of a mechanism whereby the business community's wishes were directly reflected in government policies.

2. What are the successes and challenges of this strategy?

For four years and nine months from the end of the 1965 recession through the summer of 1970, Japan enjoyed the longest economic upsurge in the postwar years. The average annual growth rate during this period (fiscal 1965-1970) was a high 11.8%. This record-breaking book substantially boosted the country's economic strength, moving Japan into the number two spot in the developed world, behind only the United States in terms of GDP up until 2010.

The problems were, however, also engendered in the domestic economy, such as the spread of pollution, delays in the improvement of infrastructure, and consumer price inflation, casting a shadow over the prosperity. External problems were also caused by the very fast pace of growth in Japan's exports and payments surplus, as instanced by the rise of protectionism and moves toward curbing Japanese imports in other developed countries, notably in Western Europe and the United States.

Economic friction between Japan and the industrial nations of the Western democracies became prominent in the 1970's. Four factors were behind this trend.

First, increased exports of certain Japanese products such as textiles and steel in the 1960's and colour television sets and automobiles in the 1970's resulted in economic friction because they caused Japan's trading partners to have higher unemployment rates.

Second, Japan's trade surplus vis-à-vis the West caused some countries to react by placing trade restrictions on specific product categories. The import restrictions that France imposed on videocassette recorders in 1982 are a case in point.

Third, the structure of the Japanese economy itself drew criticism because of such common perceptions as that the Japanese market was closed.

Fourth, competition was growing increasingly fierce, especially in high technology.

Even when other Western democracies complained about individual problems, the underlying issue was usually the macroeconomic factor of an accumulated current account surplus. Economic friction has tended to increase in severity whenever Japan's current account surplus exceeded 2 % of nominal GDP. It was 2.7% in fiscal 1972 and 2.9% in the April-June quarter of 1978.

3. Has this strategy been adjusted or changed over the years? If so, how has it been adjusted or changed? In particular, what has your government done to promote inclusive growth? (Please highlight key initiatives or programs).

On two occasions, in September and December of 1972, Japan took measures to improve its external economic relations. Implemented in the first half of the 1970's, these included such import promotion steps as increasing oil reserves and stepping up stockpiling of such nonferrous metals as copper and zinc. In addition, import duties were reduced before the Tokyo Round of multilateral trade negotiations under the auspices of the General Agreement of Tariffs and Trade (GATT) was concluded; import quotas on items with residual import restrictions, such as beef, oranges, and fruit juice, were extended.

In January 1983, before Prime Minister Yasuhiro Nakasone's visit to the United States, Japan lowered tariffs on the disputed items such as tobacco products, chocolate, and cookies, and took steps to promote the

distribution of foreign tobacco products. In March of the same year, improvements in the standards and certification system were decided upon in accordance with requests received from a number of countries and to bring Japan's system in line with the GATT's Standards Code. And in October 1983, in addition to the conventional measures of stimulating domestic demand through public works investment and lowering tariffs, Japan announced steps to raise the value of the yen by such means as floating Japanese Government guaranteed bond in the United States.

A major change in the course of the post-world war II economic development of Japan was brought in by a significant exchange rate realignment known as "the Plaza Accord" of September 1985. It was a meeting of the finance ministers and the central bankers of the Group of Five industrial nations at the Plaza Hotel in New York, agreement was reached on closer coordination of macroeconomic policies among the G-5 countries to (1)intervene in currency markets to achieve realignment, devaluing the dollar and bolstering the yen and Deutsch mark; (2)reduce the U.S. budget deficit; and (3)boost domestic demand both in Japan and West Germany.

The effect of this agreement was dramatic. The value of the dollar, which stood at Y243 shortly before the meeting, soon broke through the Y200 mark, dropping to around Y180 by April 1986 and to Y120 by the end of 1987. This rapid appreciation of the yen fueled fears of a recession, with domestic manufacturers losing large shares of both the domestic and overseas markets to lower priced products of foreign rivals. Some were also worried about deindustrialization, as companies shifted to offshore production, especially in Southeast Asia, and workers in uncompetitive industries, such as coal, lost their jobs. There was even the anxiety that technology development, which had been the mainstay of growth in manufacturing, would also be increasingly undertake abroad.

It was, nonetheless, a beginning of the new phase of development of Japanese industries in the form of production networking linking the domestic factories with the local production sites of parts and components abroad. Japanese manufactures of electric appliances and electronics started to set up a region-wide optimal supply system of

parts and components across the South-east Asia as well as in the East Asia, and it lead gradually to a de-facto integration in the region.

In the context of far-reaching changes in the world economy, calls intensified for a structural transformation of the Japanese economy as well. Among the most prominent of these calls were the two "Maekawa Reports", issued in 1986 and 1987 by a blue-ribbon panel headed by the late Bank of Japan Governor Haruo Maekawa.

The reports contended that the economy had to be restructured to reduce Japan's ballooning external surpluses and improve the people's quality of life so that it more accurately reflected the country's leading place in the world economy. These should be accomplished, the reports contended, largely through market forces and by making economic growth more reliant of domestic demand rather than exports. More than a quarter of century has passed since the two Maekawa Reports, but this objective seems yet unrealized. The Japanese economy seems still very much dependent on the external demand rather than the domestic demand.

4. What are the elements of your country's experience on inclusive growth that in your view can be shared at the regional level to promote regional economic cooperation as well as the building of a people-centered East Asian Community?

Japanese employment practices might have significant effects on inclusive growth in the past. The one is so-called "life-long employment" and the other is the seniority system.

The Japanese practice of guaranteeing employment until workers reach mandatory retirement age enables employers, who can monitor the abilities of workers over many years, to make intelligent decisions about job assignments. Long-term employment, on the other hand, gives employees the opportunity to develop company-specific skills, including knowledge about the character of the people they work with, and the content as well as functioning of the company's organization and operations, which usually differ from one firm to another. For workers, a job guarantee provides a sense of security and makes it easy to design a plan for their lives.

Companies that adopt long-term employment develop a habit of relying on the "in-house labour market" to fill vacant posts. Instead of recruiting from the external labour market to meet needs, they look for suitable people already working for them. On seeing that they have opportunities for promotion into higher posts, workers become inclined to stay with the company, and long-term employment grows longer.

The seniority system is a system whereby wages and promotions are being linked to the age of the worker and the number of years of continuous employment.

Theoretically, workers at one company who, at the employer's expense, are provided with marketable skills could be lured away to other companies by the promise of higher starting wages. To prevent this from happening, the employer needs to hold wages down over the years of training and lift them when the skills have been acquired. For this reason as well, wage scales have come to describe an ascending curve linked to age and years of loyal services. With these wage scales in place, moreover, workers have no incentive to switch jobs after training, because their pay would go down in their new company. This strengthens loyalty to the company and bolsters the practice of long-term employment.

The battle against poverty and exclusion begins with creating and maintaining high-productivity jobs, that is a central goal of Asian regionalism. In this regard, Japan's experience in the past could be an interesting reference.