'7-year plan': how to wreck an economy

Last week, Premier Masayoshi Ohira repudiated Japan's entire postwar economic miracle by adopting a seven-year economic plan which capitulates to Washington's demands that Japan "restructure its economy." The crux of the plan is a mammoth $1.1 trillion ($160 billion per year) public works program aimed at replacing exports and private capital investment with public spending. The $1.1 trillion figure is equal to Japan's entire GNP for 1978! At the same time, the plan aims to reduce Japan's dependence on oil for energy from the current 75 percent to only 48 percent in order to meet the Tokyo summit pledge to limit oil imports to 6.3 million barrels per day by 1985.

"The plan was drawn up under pressure from the international circles which are attacking Japan ... and it is ridiculous," exclaimed one angry Japanese banker.

Only last year an international scandal arose when Richard Rivers of the U.S. Special Trade Office bluntly relayed the U.S. Treasury's demand that Japan restructure its economy away from an industry and exports orientation to a services economy. Rivers was even forced to deny he ever made such demands. Now the Ohira administration has adopted that very program. After expressing astonishment at the huge size of the public works program, Philip Tresize of the Brookings Institution—which designed Carter's economic policy toward Japan—labeled the plan "a healthy move in the right direction" and said it would be welcomed in Washington.

Abandon EMF

Complementing the seven-year plan, the Finance Ministry in early August announced new restrictions on Japanese banks' international dollar lending which comply exactly with the demands made by former Treasury Secretary Michael Blumenthal during his February trip to Tokyo. The restrictions limit Japanese participation in international dollar syndication to no more than 25 percent or occasionally 33 percent of a given loan, and prohibit them from undercutting high Euromarket interest rates.

Under the policy of Ohira's predecessor Takeo Fukuda, Japan's banks had acted in alliance with Germany and France in implementing the European Monetary Fund (EMF) policy of issuing large volumes of low-interest dollar-denominated loans to developing countries for manufacturing projects, not just resource extraction. Thus, Japan's international dollar loans rose from a cumulative total of $7 billion at the end of 1977 to over $25 billion by this June. In February, Blumenthal told Tokyo that overseas yen loans were fine, but he would not tolerate Japan becoming such a powerhouse in dollar lending, particularly for manufacturing projects at rates lower than the exhorbitant Euromarket rates, and particularly in alliance with the EMF. While West Germany is continuing such loans to the benefit of its economy, the Japanese Finance Ministry has now ordered Japanese banks to cut back, under a clear threat: "The banks may encounter trouble in obtaining the necessary funds on the Eurodollar market. If the Japanese banks continue tapping the Eurodollar market to keep up their high pace of overseas loans, monetary officials worry, they might be hurt badly in an international monetary turmoil," according to the July 24 business daily *Nihon Keizai Shimbun.*

Under prime ministers Kakuei Tanaka, Takeo Miki and Takeo Fukuda, Japan's policymakers recognized that economic recovery at home depended upon restoring healthy world trade and capital formation, in contrast to the IMF's austerity policy. Fukuda in particular fashioned an alliance with Helmut Schmidt and Giscard d'Estaing, under which the combined financial resources of Europe, Japan and certain OPEC countries would be channeled to finance a recovery of world trade led by industrial development projects in the developing countries. This was also seen as the way to restore the value of the dollar, since the loans would be financed in dollars. Japan's own recovery would be led by exports of plant and equipment to the developing countries, not just television sets to the U.S. (See Figure I.)

Ohira is now forcing Japan to abandon any role in restoring healthy world growth, and is turning Japan inward toward a semi-autarkic economic model that can only be described as Schachtian. This is not simply a case of compromising under pressure from London and Washington, as certainly occurred under previous administrations, but an unprecedented adoption of the policy that Britain and the U.S. have tried to force on Japan since August 15, 1971.

The restructuring

The banks, who resisted a token effort by the finance ministry to curtail them last December, are furious at this more serious effort now: "We are bound to lose business and this will put a heavy squeeze on Japan's merchant banking in the future," commented one banker to *Nihon Keizai Shimbun.*

The seven-year plan's major features make clear the drastic change in Japan's economic structure which Ohira is trying to enforce:

1) Replace exports with public spending as the major stimulus to the economy;

2) Fulfill the Tokyo summit pledge to restrict Japan's oil imports—Japan has no domestic production—to 6.3 million barrels per day. (See energy box)

3) Double the stock of "social capital"—sewers, parks, public-financed housing, bridges, etc.—by 1985 at a cost of $1.1 trillion, more than 1978's GNP.

4) Finance the public works by raising taxes from current 20 percent of GNP to 26.5 percent by 1985. This does not preclude the need for additional massive public borrowing;

5) Achieve 5.7 percent real GNP growth per year on the average during the plan

6) Reduce consumer inflation to 5 percent per year

7) Reduce balance of payments to an "internationally acceptable standard."

"Mission impossible" was how the plan was described in a secret memo by Japan's Institute for Energy Economics. The memo pointed out that the plan is a contradictory hodgepodge; for example, it is not possible simultaneously to restrict oil consumption so drastically and maintain anything above 3 percent yearly growth.

The plan is, indeed, "mission impossible," but for even more fundamental reasons. The plan is an attempt to "restructure Japan to longterm low-growth in the era of limited resources." The political economy of Japan makes this impossible outside of an outright fascist government, which the Ohira administration is not—even considering Ohira's ties to the British-sponsored "strike north" fascists of the 1930s and the Schachtian economic content of his seven-year plan. Other Prime Ministers, including Fukuda, have given lip service to the codephrase "low-growth," but all have realized that it is impossible in practice. Ohira is the first to try to implement it.

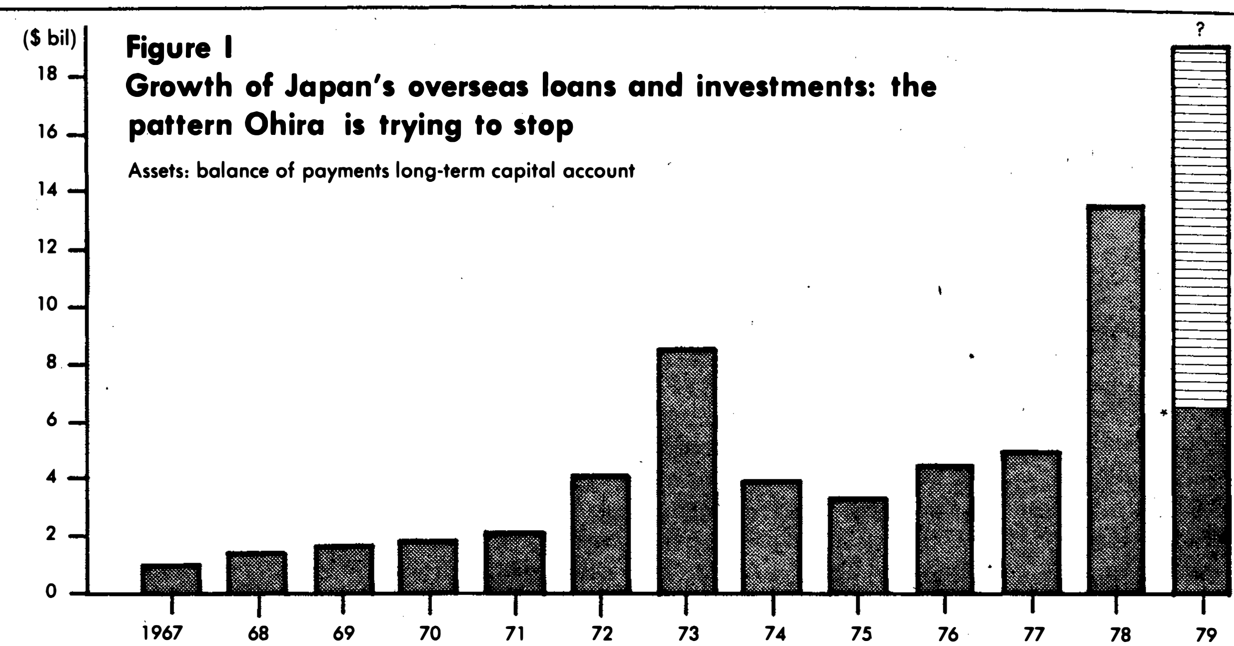
The plan proposes to replace private capital investment in industry which raises productivity, with public investment in social infrastructure which does not. Under such a program, the population will simply trade off private consumption for public consumption. Living standards cannot rise, while the inflation resulting from such a program will in fact lead to a cutback in living standards. As part of a program of industrial growth, balanced social investment is both useful and necessary. As a substitute for industrial growth, it can only create financial and economic chaos. Hope for a stable 5.7 percent real growth under such a policy is an opium dream.

How Japan's economy works

Japan is already in a financial crisis, the direct result of years of stagnation of world trade. For April through June, wholesale prices rose at the annual rate of 19

Figure I
Growth of Japan's overseas loans and investments: the pattern Ohira is trying to stop

Assets: balance of payments long-term capital account



Source: Ministry of Finance

*For 1979, full column is the investment that will occur if the pace-setting rate of Jan.-April (*) is continued for the rest of 1979. New Ministry of Finance rules are aimed at preventing this. In 1979, in contrast to earlier years, much of Japan's international lending was yen-denominated.

percent, the worst since the "crazy prices" of era of 1973. In June, the largest banks—who have been running on virtual negative interest margins for a year and a half—refused to buy any more government bonds until the bond yields and the discount rate were raised. The government, running a 40 percent budget deficit, had no choice but to comply: It raised the discount rate from 4.25 percent to 5.25 percent.

Ohira's response to this crisis in the short term is severe austerity and financial retrenchment. The finance ministry quota for total new domestic lending by the largest banks means an 8 percent reduction from last year, the worst cutback since postwar recovery took off in 1955. In the longterm, Ohira's answer is the seven-year plan.

A look at the basic structure of the economy makes clear why the Ohira program can only exacerbate this crisis. During the postwar "miracle" years of 1955-1971, Japan's
velopment that any economy, whether "mature" or not, can follow. Japan experienced not only high rates of growth, but more importantly, accelerating rates of growth. The key to this was that capital formation continuously rose as a percent of GNP, reaching 30 percent at the high point of 1970 (not including government investment). As a result, labor productivity also rose tremendously, as much as 12-14 percent per year. This meant living standards could triple during the same period while consumption declined as a percent of GNP! (See Figure II.)

Exports—while not so high a proportion of GNP (only 12 percent)—were the engine of this process. Japan was a "future-oriented" economy, geared to the growth of world trade. Its plans for the 1970s were to shift to exports of plant and machinery, not just autos and TVs.

August 15, 1971 and the oil crisis of 1973 sent Japan into an economic crisis from which it has never recovered. Not so much because of their direct effects on Japan, as because of their effects on world trade as a whole. The 1955-71 growth
corporate debt-loads, which remained perfectly manageable as long as high productivity increased and high growth remained. Without that buffer, the debt loads become unmanageable. The crisis of 1971 immediately caused spiralling inflation, reaching 30 percent by 1973 in a country where inflation had been virtually nonexistent during the 1955-71 period. This was followed

Ohira slashes Japan's nuclear goals

Perhaps no other issue better expresses Premier Masayoshi Ohira's attack on the entire thrust of postwar Japanese economics than his downgrading of Japan's nuclear and fusion power programs. His administration proposes to spend $25 billion over the next 11 years on such "alternate energy sources" as coal, coal liquefaction, solar energy, etc. while reducing the previous 1985 target for nuclear power by 15 percent and that for 1990 by 10 percent. Meanwhile the plan "includes a removal of nuclear fusion on which a considerable amount of money has been invested," according to the *Mainichi* of July 17.

Much more than Japan's energy resources is at stake here. The course of the entire economy is altered by this energy proposal. In 1971, Japan's Industrial Structure Council—a business advisory body to the Ministry of International Trade and Industry (MITI)—developed a long-term economic plan whose core was making Japan a fusion-power economy by the 1990s or 2000. All investments in other industries, development of computers, transfer of technology to the newly industrializing nations and other key decisions were organized around the key target of bringing Japan into the high-technology "knowledge intensive" era of fusion power. Nuclear power was viewed as a transition to that era. One MITI official predicted, "By the year 2000 Japan will supply half the world's energy by mass production and export of fusion power machines." Not unimportantly, possession of substantial nuclear and fusion power resources would free resourceless Japan from energy blackmail by Britain and the United States through Anglo-American control of the seven oil multinationals.

To this end, under programs launched by Prime Ministers Takeo Miki and Takeo Fukuda, Japan raised its research spending on fusion tenfold, from only $40 million as its share of joint research with the U.S. proposed by Fukuda. Ohira is now relegating fusion power production to some time in the next century, and cutting out further increases.

Planners in the early 1970s envisioned Japan getting 20 percent of its electricity from nuclear power by 1980 and 30 percent by 1990, at the least. Instead, due to "environmentalist" pressure, nuclear is only 10-12 percent of electricity now, and Ohira has reduced still further the already bleak target of 20 percent by 1990.

For the dubious purpose of lowering oil as a source of energy from 75 percent to 48 percent by 1985, Ohira proposes that Japan mimic Jimmy Carter's energy program.

by the 1974-75 depression when industrial production fell 11 percent. Previously, the word recession in Japan meant growth of only 3 percent.

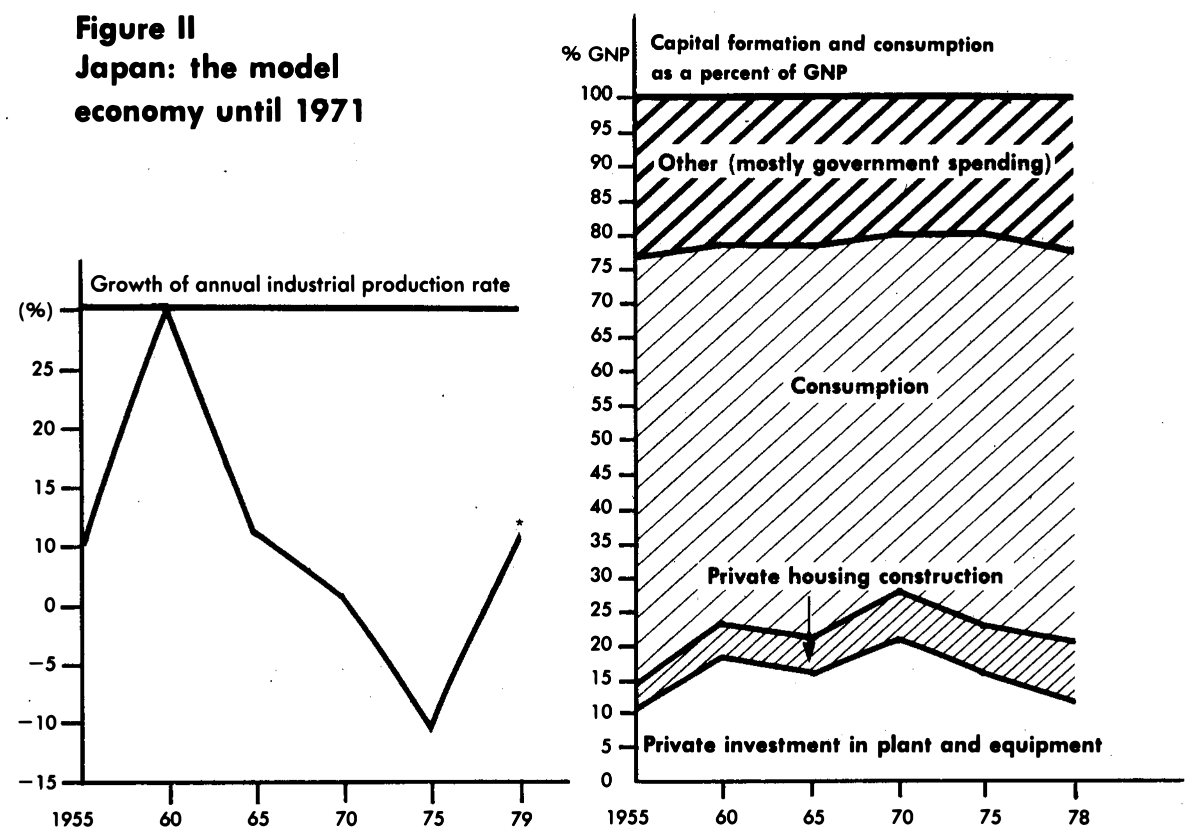
Japan "recovered" from that recession only by an unsustainable export boom. The boom was based on vastly increasing Japan's market shares, not on overall growth of world trade. The boom had to end as long as IMF austerity policies and Euromarket speculation prevailed. U.S. protectionism simply hurried the end.

This news service has always maintained that in the absence of genuine world trade recovery, Japan has a latent inflation rate of 25-30 percent. The inflation can be suppressed or hidden but not eliminated. Once the export boom ended (as it did with 1978's real export decline of 0.8 percent, a further 3-4 percent decline in Jan.-June of this year), then Japan immediately faced either raging inflation or deep recession or some combination of the two. (See figure III.)

Fukuda's 1978 policy was to hold the economy together domestically while working for a genuine international recovery through his cooperation with Germany, France, and sections of OPEC.

What would have been simply an extended period of financial strain until international trade recovered, has now become a financial crisis precisely because Ohira abandoned Fukuda's international economic policy. Corporate, banking and government finances are all stretched incredibly taut. Corporate managers throughout the last two years channeled all their efforts into reducing the debt load that now threatened them with bankruptcy. In fact, in 1978, for the first time in postwar history, the manufacturing corporations actually reduced their overall total cumulative debt by 3 percent—an unheard of phenomenon anywhere in the advanced industrial world. At the same time they limited capital investment to rationalizing or patching up

Figure II
Japan: the model economy until 1971



*1979=Jan.-June 1979/Jan.-June 1978 Source: Ministry of International Trade & Industry

Except for the hiatus of the 1958 recession, the secular tendency of the growth of Japan's annual industrial production rate was up between 1955 and 1971, with private capital investment reaching a high point of 28% of GNP in 1970. In that same period, the rising ratio of capital output to consumption (the latter fell from 64% to 53% in the same period) produced increases in labor productivity which allowed personal income to *triple* in that period, while overall GNP multiplied by a factor of 4.5. After 1971, when the growth in industrial production fell to near zero, investment has fallen, and consumption risen as percentages of GNP, while real wages rose no more than 2% between 1975 and 1979. The Ohira program will reinforce the tendency to stagnation in productivity and capital formation; restoration of Japan's pre-1971 economic dynamo appears to depend on a general upturn in the world trade picture.

their existing base, not to expansion.

Very many corporations survived only because the banks gave them under-the-table debt moratoria and because the interest rate banks charged went below the rate the banks had to pay on deposits. Half of the 13 largest banks—who do virtually all of the lending to the big "zaibatsu" companies that dominate the economy—ran negative interest margins, also unheard of elsewhere. Meanwhile, the government ran a 40 percent budget deficit!

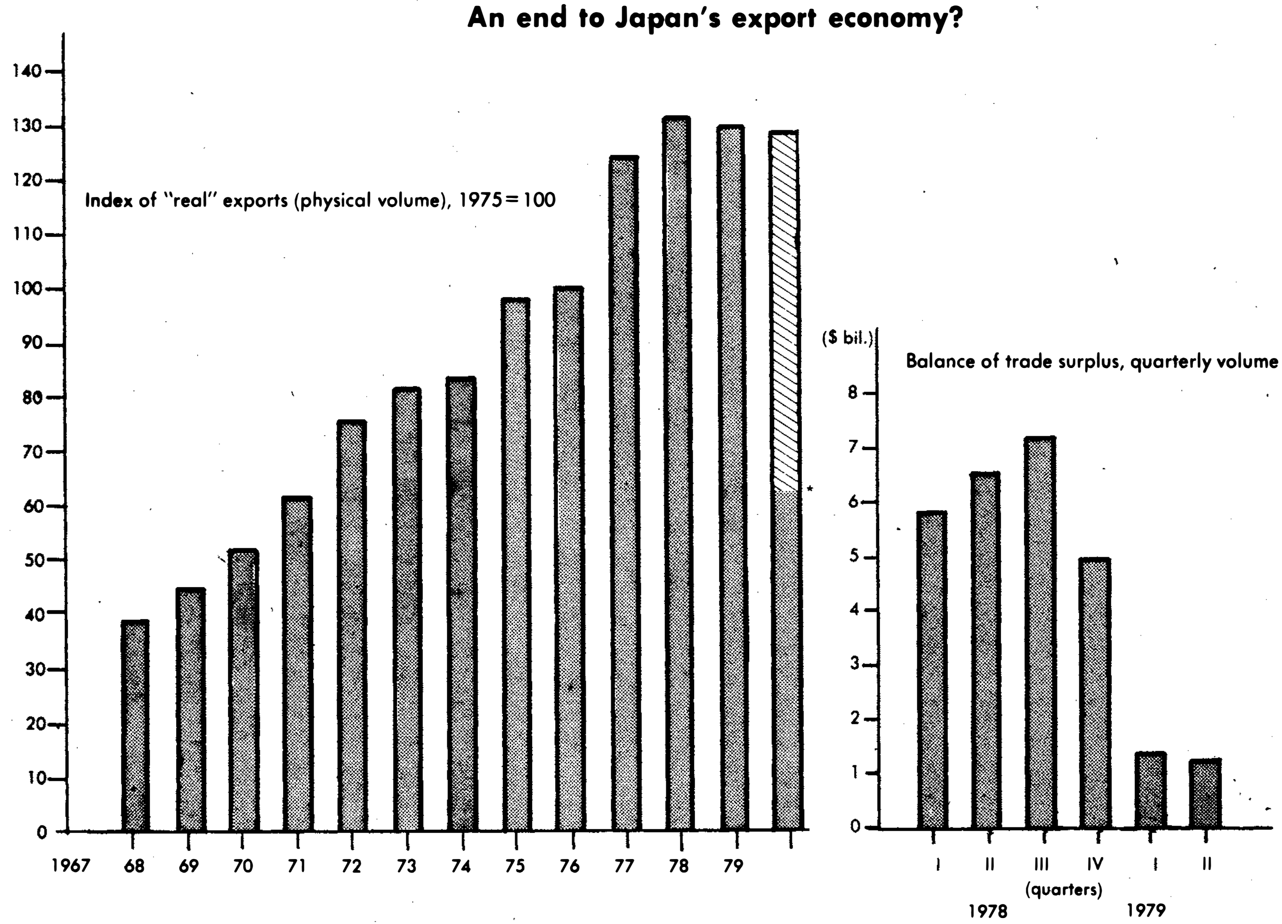
In fact, in no other advanced economy could the economy survive while half the leading banks were running virtually negative profits under conditions of large government deficit. Japan's economy has surprising resilience because of the long years of capital investment, and secondly, because politically the Japanese are willing to say, "*Let's ignore the numbers and keep production going.*" The Bank of Japan made sure the banks were sufficiently supplied with funds to maintain this bailout policy.

This policy was only possible, however, when the yen, the Japanese currency, was stable or rising, as it was last year. Then inflation was suppressed—wholesale prices in fact fell 4 percent in 1978. But once the yen came under attack, as it has been since oil prices rose, then the central bank could not continue funding the banks to enable them to bail out the corporations. Previously latent inflation then raged into the open. In Japan, by April-June, prices were rising at a 19 percent annual rate.

Ohira's only answer is austerity—the worst credit crunch since 1955, a proposed 1980 budget with the lowest rise in spending since 1961, and immense taxation to sponsor a public works-based economy. Not even the Japanese miracle economy can survive such a policy.

—***Richard Katz***

Figure III
An end to Japan's export economy?



*EIR estimate, Jan.-June 1979; full column is extrapolation based on Jan.-June rate.

Source: Ministry of International Trade and Industry