

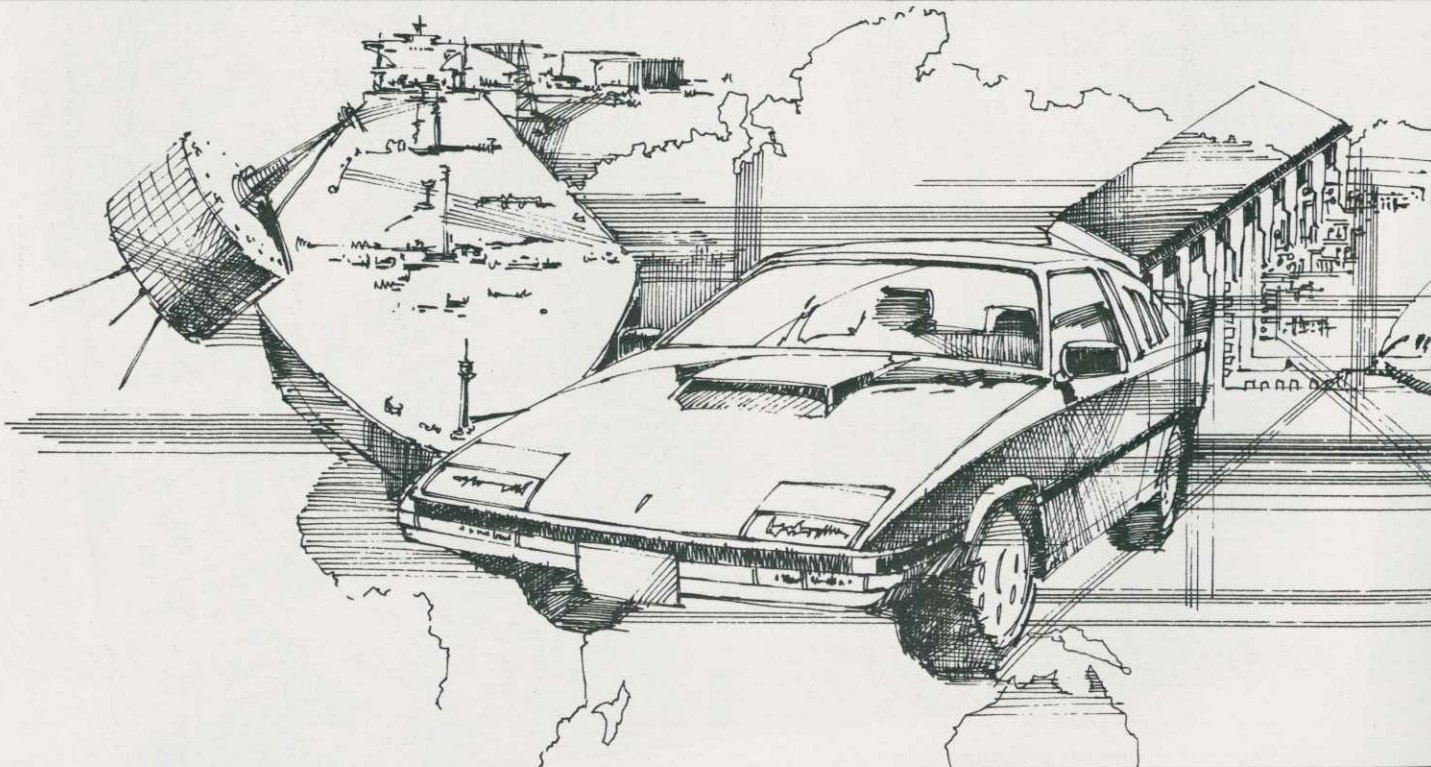
An Outlook for Japan's Industrial Society toward the 21st Century

—In search of Japan's contribution and cooperation in bringing about innovative growth of the international economic system—

Interim report by the Industrial Structure Council

The Planning Subcommittee of the Coordination Committee of the Industrial Structure Council, an advisory council to the Minister of International Trade and Industry, started in July 1985 to draft "The Basic Concept of Industrial Society in the 21st Century." The Planning Subcommittee's task is to probe for the desirable form of industrial structure in the new age from three points of view: (1) "the form of Japan's industrial structure which will be in harmony with the international economic society and which will contribute to the international society;" (2) "changes in domestic economic factors, such as technological innovation and information-orientation, and the form of Japan's industrial structure;" and (3) "the new cultural lifestyle resulting from pluralization of value concepts and aging of society, and the form of Japan's industrial structure."

The report released this time is the interim result of the study focusing on the first point mentioned above. The Planning Subcommittee will continue its study of the desirable form of industrial structure from the viewpoints of (2) and (3). After making overall adjustments, the subcommittee is scheduled to submit a comprehensive report at the end of April.



Redressing the growing external imbalance

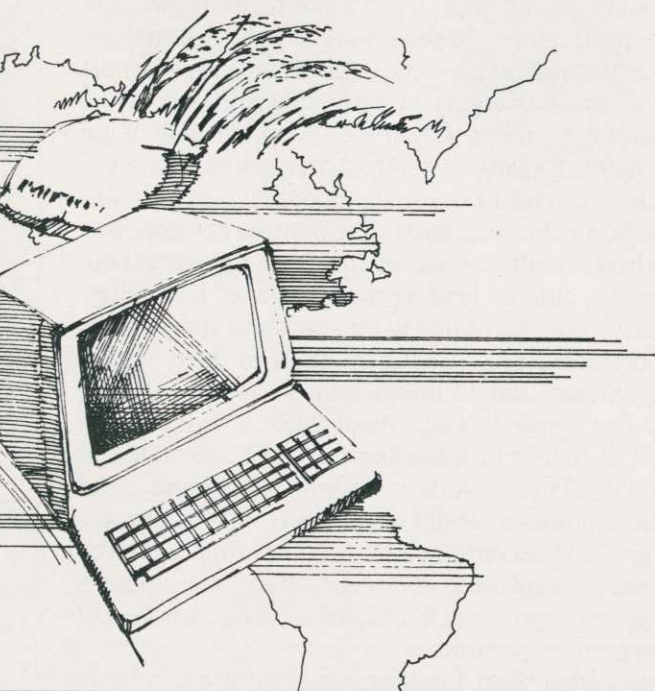
Japan's trade imbalance with other countries has been widening recently. The growing imbalance is attributable to the following background factors:

(1) Goods and capital flows out of Japan to other countries, particularly the United States, as a result of the over-demand and shortage of savings in the U.S. and savings in excess of domestic demand in Japan;

(2) The floating exchange rate system's function of automatically adjusting current account balances has been weakened by the big increase in international capital transactions; and

(3) Income elasticity of export increased as a result of progress in the expansion of industry toward fields in which worldwide growth of demand is expected, while income elasticity of import declined because of the progress made by industry in energy conservation through efforts to overcome the oil crises.

Japan's growing external imbalance is neither desirable for the world economy nor for Japan, taking into consideration the future world economic situation in which international interdependence will increase. The imbalance cannot be rectified by Japan's efforts alone. They can be corrected only through well-directed policy coordination among the principal countries. Notwithstanding, Japan on its part must step up efforts to redress the external imbalance.



Japan has grown into a major economic power which accounts for about 10% of the world's GNP. Now is the time, therefore, for Japan to revise its thinking, throw out national egoism, and from the global standpoint reshape various policies, such as macroeconomic management policies, exchange rate policies with a view to stabilizing the yen rate at a proper level and policies to reorganize the industrial structure. Such changes will put a big burden on various sectors of the domestic economy and involve many sacrifices. Only when these difficulties are surmounted will a new era dawn in the 21st century.

Basic thinking on policy

The following four points are hereby proposed as the basic ideals of future policy:

(1) Innovation: The solution of the disequilibriums existing in the international society (international payments imbalance between developed countries, the North-South gap, uneven distribution of cumulative external debts, etc.) should be achieved through innovative growth of the world economy.

(2) Freedom: Respect for the market mechanism and preservation of the free trade system.

(3) Accommodation: The accommodation of Japan's savings and technological capabilities to contribute to the revitalization of the world economy as well as to progress in academic and basic research.

(4) Rapport: With respect to macroeconomic policy, industrial policy, etc. Japan should strive to establish policy rapport with other countries from the global standpoint.

Basic to the policy for achieving these four points is the paying of consideration to harmonizing Japan's economy and industrial structure with the international economy in the medium and long terms. In this context, special attention must be paid to international cooperation. In the past, whenever Japan faced international trade friction, the need for the "internationalization" of its economic society was repeatedly stressed. Most of Japan's responses in this connection appeared to show insufficient perception of its position in the world economy and a lack of international vision. Japan was able to grow into a major economic power thanks to the free trade system whose benefits it could enjoy to the maximum. In view of this fact, it is necessary for Japan to take measures which foster an environment in which the excellent international economic order known as free trade can be preserved. These measures include relatively high economic growth centering on domestic demand and reform of its economic and industrial structures. And Japan must willingly bear the cost that all this entails.

Direction of policy and its implementation

The policies which must be implemented in line with the above basic thinking are as follows:

(1) International coordination in economic management policy (foreign exchange rate policy to maintain the strong-yen trend and macroeconomic policy)

After the so-called G-5 decision made last September, the high dollar situation was corrected through coordinated intervention and closer policy coordination among the countries concerned. However, taking into account the possibility of increasingly brisk capital movement against the background of worldwide financial deregulation, it is necessary to strive to stabilize the exchange rate at a reasonable level. In order to achieve this, it is essential to strengthen the coordinated intervention system, tighten macro policy coordination, and accelerate the yen's internationalization. Moreover, it is necessary to study extensively the possibility of reforming the monetary system in accordance with changes in the international economic situation.

Major countries also need to cooperate in a macroeconomic policy for revitalizing the world economy. The establishment of a close tripolar cooperation mechanism among Japan, the United States and EC, which together account for about 70% of the free world's economy, merits study. Under such a mechanism, the three poles will mutually agree on their respective policy objectives and conduct a continuous review in implementing this policy package. Considering that the U.S. has enacted the Gramm-Rudman Budget-Balancing Law and will grapple in earnest with the task of reducing its budget deficit, it is desirable that Japan should modify its economic management in the direction of expanding domestic demand and establishing international policy rapport.

(2) Reform of economic and social system aimed at expanding domestic demand (macroeconomic policy for growth led by domestic demand, including expansion of consumption opportunities and creation of domestic investment opportunities)

In the past, the macroeconomic policy tended to depend on external demand. It is necessary now to switch to a policy which emphasizes economic growth led by domestic demand. For this, policy measures that will expand consumption opportunities and create more opportunities for domestic investment should be worked out.

In order to expand personal consumption, it is necessary to secure, through labor-management efforts, wage increases commensurate with the increase in productivity, thus increasing disposable income to a reasonable level. At the same time, it is necessary to reduce, through efforts of labor, management and other

quarters concerned, the total annual real working hours to less than 1,900 hours, a figure which is less than that in the U.S. and Britain. The service industry must be developed to create a life environment in which the additional disposable income and extra free time can be channeled to consumption and recreation.

It is necessary to secure domestic investment opportunities corresponding to the amount of savings which is expected to remain at a high level in terms of international comparison. For instance, it is particularly important to devise ways and means to increase housing investment and to improve the infrastructure (life-related environmental facilities like sewerage systems and parks, and high-speed traffic networks including airports, motor expressways, information communication systems, etc.). For this, a drastic reform of the financial and taxation systems must be carried out, and measures taken to utilize private-sector vitality. Furthermore, for those aspects of the infrastructure whose need for improvement and urgency is particularly high, the increased issue of construction bonds within a set framework should be considered while keeping an eye on the future economic situation, thereby accelerating infrastructure improvement efficiently on a priority basis.

(3) Positive promotion of international division of labor (horizontal division of labor as a means to expand imports of manufactured goods and to promote vigorous investment and technology exchanges)

Efforts must be made to open up the Japanese market further to foreign products, such as by steadily implementing the "Action Program" announced by the government at the end of July last year as well as to positively boost Japan's imports of manufactured goods through such means as promoting horizontal division of labor, so that imported manufactured products will be sufficiently woven into Japan's production and consumption structures. In order to rectify the external imbalance through expanding equilibrium, Japan must step up direct overseas investment vigorously while maintaining harmony with the economic society of the host country. Expansion of direct overseas investment is strongly hoped for from the standpoint of making international contributions, such as helping the development of the host country by way of creating employment opportunities and accelerating the transfer of technology and know-how. According to one estimate, if the cumulative direct overseas investment made by the manufacturing industry should increase by an average 12% annually from now through fiscal 2000, a reduction of about \$53 billion in trade surplus can be expected in fiscal 2000. These efforts to reform Japan's industrial structure, however, would cause pains to the domestic economy, and according to the same estimate referred to above, the expansion of direct overseas investment is expected to deprive about 560,000 Japanese workers of employment opportunities.

On the other hand, foreign direct investment in Japan

would enhance Japan's international economic activities and would have the effects of bringing new technology into the country and of stimulating competition. Moreover, this would contribute greatly to eliminating the perception gap between Japan and other countries. On the other hand, by investing in Japan, the countries of Europe and the United States can expect such effects as the development of the Japanese market, expansion of exports to Japan, and the opportunity to utilize good quality labor and high-level technology. From this standpoint, it is important for Japan to improve and expand the environment for stimulating foreign direct investment in Japan to promote a balanced exchange of investment with other countries.

Recently, requests from developing countries for transfer of technology from Japan have been increasing. From the standpoint of establishing a desirable form of international division of labor, Japan should positively transfer technology to developing countries. At the same time, now that Japan's position has risen in the international economic society, European countries and the United States, too, are demanding that Japan play the role of technology supplier. From this standpoint, it is vital for Japan to promote technical tie-ups with European and American enterprises (as an example the plan of the Japan-EC Industrial Cooperation Center can be useful for this purpose), supply technology to developing countries, and cooperate positively in international research projects.

(4) Positive contribution to international public goods (promotion of the new round of multilateral trade negotiations, promotion of the "Human Frontier Program," drastic expansion of economic cooperation, etc.)

At this time of mounting protectionism, it is necessary for Japan to display leadership, while cooperating with other countries concerned, in launching the new round of multilateral trade negotiations, in order to maintain and strengthen the free trade system.

From the standpoint of expanding the world economy's new frontier through technological development and of contributing to the solution of problems common to all mankind, such as environmental improvement on a global scale, Japan should propose to the world a basic R&D project (Human Frontier Program) for shedding light on the basic principles underlying the various functions possessed by living organisms and applying these principles in engineering. At the same time, Japan must make vigorous efforts to implement this Human Frontier Program by contributing more than 50% of the cost required.

As for official development assistance (ODA), in order to fulfill its international responsibility Japan must make efforts to increase ODA steadily by attaining, first of all, the third medium-term target. In that event, it is important to implement effective economic cooperation aimed at assisting developing countries to achieve economic independence. In addition, in order to broaden

the base of economic cooperation, Japan needs to promote participation in economic cooperation by a wide stratum of its citizens as well as to utilize effectively the vitality, technology and know-how possessed by private enterprise.

Conclusion

As has been stated thus far, even though it may be very difficult for Japan to attain the goal of redressing its external imbalance between now and the year 2000 within the framework of innovative growth of the world economy, it is certainly not impossible to do so, depending on Japan's efforts. In order to attain the goal, while trying to strengthen solidarity with the principal nations, Japan must carry out a macroeconomic policy emphasizing growth led by domestic demand and an exchange rate policy which will help bring about the stabilization of the high-yen trend, based upon which it should implement policies with a view to expanding direct overseas investment, promoting imports and pushing technology transfer. In addition, Japan should increase its contributions to international public goods. At the same time, Japan must strive to sustain and nurture its domestic growth capability by promoting the development of innovative technology, while probing for a way to absorb workers, who will have fewer employment opportunities as a result of progress in the international division of labor than otherwise, by promoting the industries which depend on domestic demand, particularly the service industry which has strong potential to absorb labor.

Needless to say, these reforms will impose on all Japanese people and all sectors of Japanese industry burdens and sacrifices, though the degree of pain may differ from one industrial sector to another and from one stratum of people to another. The government certainly must make the appropriate policy efforts, and it is hoped that all industries, companies and citizens would make efforts to resolve these difficult problems with a new international sense and endeavor to build a Japan which will contribute to the progress of mankind as we move toward the 21st century. ●

FAIR Program

The spirit with which to implement the policy program explained above is FAIR. This is shown clearly in the basic policy ideals proposed on page 35.

