

Price Busting and the Current Business Trend

By Hamano Takayoshi

Japan is ending the year 1997 with its economy mired in stagnation, far from a robust recovery. The current slowdown is characterized by shrinking consumer spending, which, along with the impact of deregulation, has prompted a downward spiral in commodity prices. Most notably in provincial cities, moves are gaining momentum to break the price-maintenance system, a phenomena known as "price busting." What is behind such a trend, and how will it affect the economy in the months ahead?

The current financial crunch

Government statistics released in September showed that Japan's gross domestic product in the April-June quarter plunged 11.2% in annual terms, the largest drop since the first oil crisis 23 years ago. Most economists predict Japan will find it extremely difficult to achieve 1.9% growth in real terms in the current fiscal year ending March 31, 1998, as originally forecast by the

government. A revised projection by a private research institute put fiscal 1997 growth well below the 1% level, bordering on recession. Dragged lower by the downtrend, share prices sagged to the year's nadir on the Tokyo Stock Exchange in October and November.

Economists point out the prevailing bearish sentiment resulted from reaction to the last-minute buying rush prior to a near-doubling of the sales tax in April, the abolition of special reductions in the income and residential taxes and an increase in individual medical costs in September. These financial factors will combine to raise individual burdens by as much as ¥9 trillion, according to some projections. Japanese consumer spending now totals ¥300 trillion, but even so, ¥9 trillion is not a negligible amount, and it is not surprising that the siphoning of such a vast sum from consumers by the government has led to fiscal recession.

The reaction to the buying rush prior to the rise in the consumption tax was originally forecast to end in three months, that is by the end of June. But

consumer spending, measured by sales at department stores and supermarkets as well as sales of new cars, has remained sluggish, due partly to some unfavorable weather since July, but more to simple consumer restraint in the face of higher taxes. Bankruptcies of general contractors and large supermarket operators added to the woes, which hampered a business recovery.

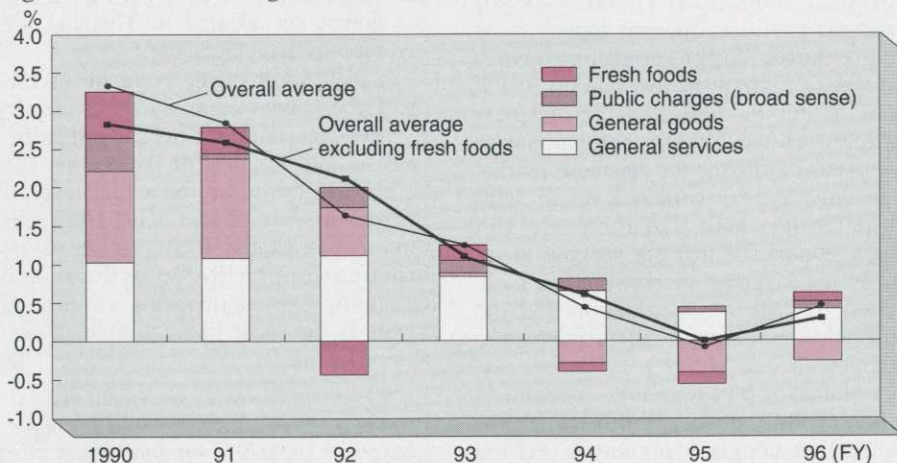
Development of price busting

The delay in business recovery has impelled some distributors to break the price-maintenance system—"price busting"—especially in provincial cities. The term "price busting" originated from the title of a novel by economic writer Shiroyama Saburo, and became a buzzword in Japan in 1994. At that time, large supermarkets were selling low-priced own-brand products equaling national-brand commodities in quality, which caught on with consumers. This period was also characterized by the emergence of discount stores, which drastically reduced commodity prices through mass procurement.

A report on fiscal 1997 price movements released by the Economic Planning Agency in early October showed the ratio of increase in commodity prices has been sagging steadily year on year since fiscal 1990.

General commodities (excluding service charges and public utility rates) had been the main factors boosting prices in Japan up to fiscal 1993. In a reverse trend, however, general commodity prices have been dropping since fiscal 1994 and dragging down prices as a whole, underlining a continuation of the impact of price busting. Fiscal 1996 saw a slight business recovery, which helped shrink the rate of decline in commodity prices, and slightly raised the rate of increase in all prices. Since the start of fiscal 1997, prices

Figure: Factors Affecting Rise in Consumer Prices



Note: 1. Based on the Consumer Price Index by the Statistics Bureau of the Management and Coordination Agency.

2. The classification of goods and services is that used by the Economic Planning Agency.

Source: Price Bureau, Economic Planning Agency "Price Report '97"

rose some 1.5% in April from the previous month, due to the 67% increase in the sales tax, from 3% to 5%, but they have remained flat since, according to national statistics.

As part of efforts to curtail the financial deficit, the government has outlined policies for curbing public works, which, combined with other factors, have helped aggravate the business slowdown and prompt price collapses, particularly in provincial cities. The extent of price-cutting differs from city to city, and so accurate statistics are not available.

Generally speaking, however, gasoline, cellular phones, clothes, sundry goods, whiskey, stationery and rice are among the items for which prices have dipped conspicuously. Gasoline prices have hit a 10-year low and cellular phones, clothes and sundry goods have become typical targets of price busting. Whiskey prices were lowered after reductions in the liquor tax. Entry into the Japanese market by foreign stationery retailers is blamed for reductions in stationery prices. Weak prices of free-market rice, which hit rice farmers, resulted from a bumper crop for the fourth consecutive year, which boosted rice stocks, as did rice trade deregulation under a new food law. Besides commodity prices, service charges at golf courses and other leisure facilities have also dropped significantly.

How is price busting affecting businesses?

It is often the case in provincial cities with limited trade areas that once a "bargain shop" opens, "bargain sales" spread to other shops and trigger bitter price-cutting competition. The slow business recovery is largely blamed for giving rise to price cutting. However, deregulation is also cited as a factor, as in the case of gasoline and rice. The gasoline price collapse is a typical case of the impact of deregulation. Petroleum imports, previously licensed only to refiners, were liberalized in 1996, and restrictions on the opening of new service stations in highly competi-

tive areas were lifted. At the same time, the expansion of bargain-price gasoline retailers into provincial cities accelerated the momentum of the downward trend. Retail gasoline prices have now come down to the ¥100 per-liter level, from the ¥110 level prevalent until several years ago. In some regions, gasoline is traded even below ¥90. Industrial analysts predict that if the trend continues, a third of the service stations across Japan will go out of business. But looked at another way, the long-awaited deregulation has at last partially changed Japan's high-cost structure.

In the market economy, where a certain level of income is maintained and elements of competition work, demand ordinarily expands when the prices of consumer goods come down.

However, people in the distribution sector note there is an increasing tendency among consumers lately to refrain from buying goods on impulse or by chance, and instead to buy goods for a specific purpose. Consumers have tightened their purse strings and are no longer increasing the ratio of consumption in their household income even though prices have come down. So, when something sells, other things do not sell, a phenomena known as zero-sum. This trend may reflect consumer resistance to the package of government policies which have sacrificed consumers, including the higher sales tax, in the form of a cautious shopping trend. It may also result in the government finding it difficult to raise the sales tax to supplement revenue sources even if the financial crunch deepens further. It can be said the government has belittled consumers.

To pull the country out of the current doldrums, the government, on Nov. 18, announced stimulative measures based on an economic package proposed by the ruling Liberal Democratic Party in late October. However, the package has been criticized, both domestically and internationally, as an ineffective remedy. The *Financial Times*, in its Oct. 22 editorial titled "Empty Package," regarded the initiative as "much more than just a disappointment." Such criti-

cism makes sense because the LDP approach failed to envisage any concrete fiscal measures. Although the package included measures to boost the property market by land use deregulation and help business by trying to cut corporate taxes, it was devoid of specifics, including how and when the measures will be implemented.



Price battle on the shelves: Rice market competition can be seen daily in the supermarket

What should the government do then?

As not a few economists point out, the Japanese economy is now at a great turning point. It seems that the Japanese, in large part, have become bearish because they are left in the dark as to where Japan will go after passing the turning point. If so, it will be important for the government to tell the people in clear terms how the administrative structure will slim down and how the economy will become more manageable in the 21st century through the proposed six-point reform program including administrative, fiscal and financial reforms. The government is required to convince people that every cloud does have a silver lining. It may be difficult to implement economic stimulus measures and structural reform at the same time. Yet, it will be sad to see the emergence in Japan of a pessimistic "new economy" theory that is a reversal of the U.S. "new economy" theory.

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