FOR AGENDA

SM/84/32

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January 30, 1984

To: Members of the Executive Board

From: The Secretary

Subject: Japan - Staff Report for the 1983 Article IV Consultation

Attached for consideration by the Executive Directors is the staff report for the 1983 Article IV consultation with Japan, which has been tentatively scheduled for discussion on Wednesday, February 29, 1984.

If Executive Directors have technical or factual questions relating to this paper prior to the Board discussion, they should contact Ms. Schadler, ext. (5)7317.

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INTERNATIONAL MONETARY FUND

JAPAN

Staff Report for the 1983 Article IV Consultation

Prepared by the Staff Representatives for the 1983 Consultation with Japan 1/

Approved by P. R. Narvekar and Subimal Mookerjee

January 27, 1984

I. Introduction 2/

The adjustment of the Japanese economy to the economic disturbances of the 1970s has been remarkably successful and has resulted in better fundamental conditions in Japan than in other major industrial countries. Inflation has remained below 3 percent for more than two years and expectations of any significant acceleration of prices are widely believed to be absent. Although the terms of trade loss resulting from the first oil price increase was accompanied by a sharp increase in wages, that resulting from the second oil price increase was absorbed to a far greater extent by labor; consequently, the share of capital in manufactured value added was held constant and cost conditions remain relatively favorable (Chart 1). The sizable current account deficits that emerged in the wake of both episodes were quickly reversed owing to the competitiveness of Japanese exports and successful energy conservation efforts. The large central government budget deficit remains a problem, but since 1981 there has been progress in reversing the growth of both expenditure and the deficit as a proportion of GNP. More generally, growth and employment have been substantially better in recent years in Japan than in other industrial countries.

Nevertheless, economic growth was weak during 1980-83. The annual growth rate of real GNP slowed from 5.2 percent in 1979 to an estimated

1/ Consultation discussions were held in Tokyo from November 22-December 2, 1983 with officials of the Ministries of Finance and International Trade and Industry, the Economic Planning Agency, and the Bank of Japan. The staff team comprised Messrs. Narvekar, Boorman, and Hides, Ms. Schadler, Mr. Kashiwagi (all of ASD), Ms. Eken (ETRD), and Mrs. Tighe (TRE). Mr. Hirao, Executive Director, attended the meetings as observer.

2/ This report was prepared before the 1984/85 budget (fiscal year ending March 31, 1985) and the official forecasts for 1984/85 were released publicly. A supplement containing an assessment of the budget and forecasts will be presented after their release.

3.1 percent in 1983 and that of total domestic demand from 6.4 percent to an estimated 2.0 percent; the rate of unemployment increased from 2.0 percent to 2.7 percent; and the annual growth of real private fixed investment declined from over 11 percent to an estimated 1.6 percent. These trends were rooted in both domestic and international developments. The rapid restoration of credible price stability has not yet had the generally expected beneficial effects on growth. Low wage increases were an important factor behind the strong cost position of industry, but also tended to dampen the growth of incomes. The resulting slow growth of private expenditure weakened profits during most of the period. Despite the sluggishness of private sector growth, the Government's commitment to reducing the large fiscal deficit translated into a considerable withdrawal of fiscal stimulus. Net foreign demand, which accounted for over 60 percent of growth during the first two years after the second oil price increases, fell in late 1981 and continued weak throughout 1982, though there has been a substantial pickup more recently.

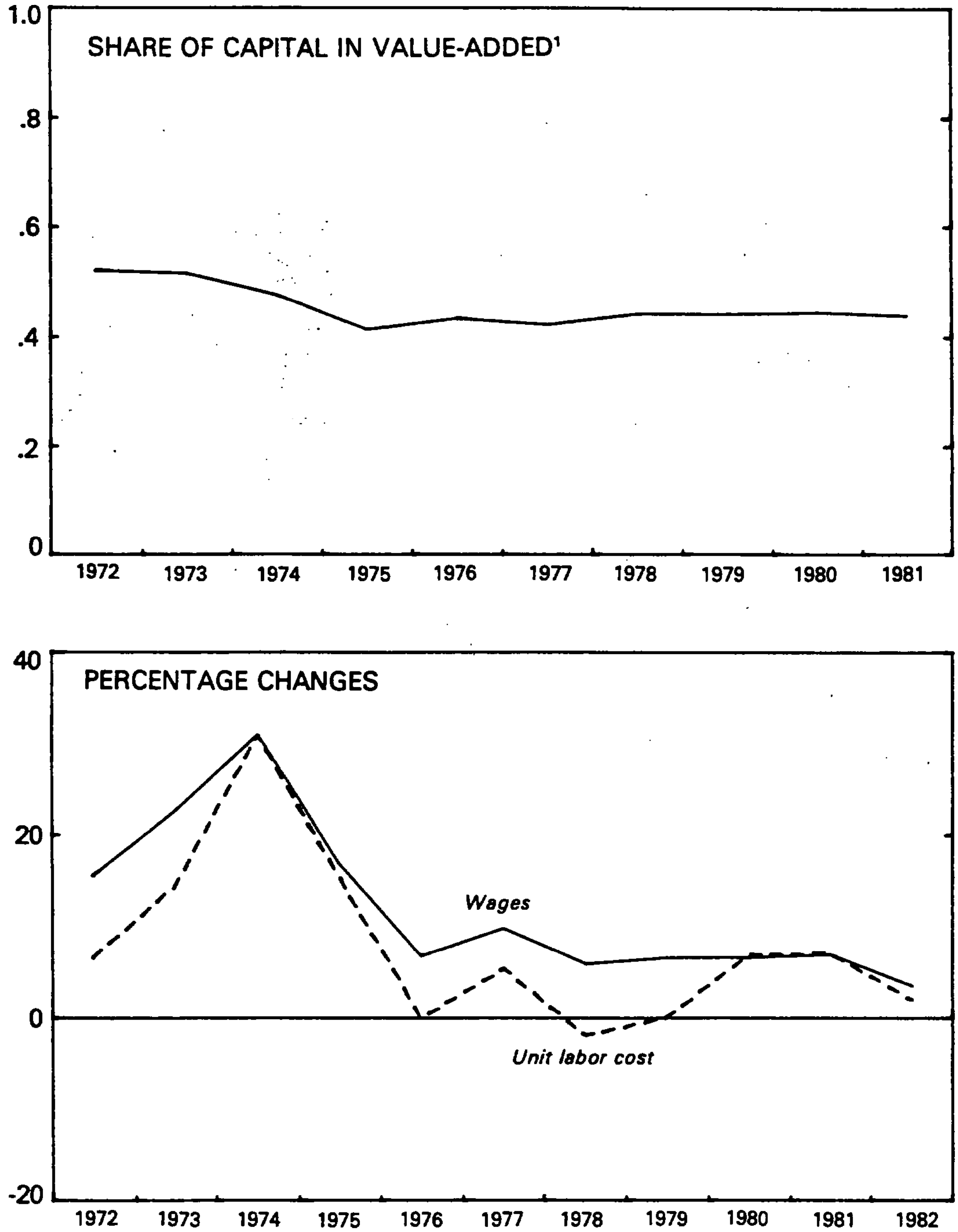
In an effort to bolster domestic demand, monetary policy was eased between mid-1980 and late 1981. The persistence of high interest rates overseas and the associated weakness of the yen, however, led the authorities to tighten monetary policy somewhat during 1982 and have since limited the scope for increasing support for domestic demand through an easing of monetary conditions. Real interest rates in Japan remain very high.

II. Background to the Discussions

After more than three years of erratic but generally declining growth, the first signs of a pickup in activity have appeared in recent months. Thus far, this pickup has reflected primarily an improvement in external factors. In real terms, net foreign demand (GNP basis) accounted for about 60 percent of the 3.8 percent growth of GNP (annual rate) during the first three quarters of 1983 (Chart 2). The staff estimates that the current account surplus increased from $7 billion in 1982 to $21 billion (1.9 percent of estimated GNP) in 1983 (Table 1). After a severe deterioration during 1982, the value of exports rebounded in early 1983, despite an extension and broadening of voluntary export restraints. Volume growth was robust owing to a strong recovery in North American and Southeast Asian export markets, considerable excess capacity in industry in the face of weak domestic demand, and the lagged effects of the depreciation of the yen through October 1982. However, while export performance has been strong, only a little more than half the improvement in the current account balance in 1983 derives from higher export receipts. Of the estimated $14 billion improvement in 1983, $7 billion stems from a decline in fuel import payments, owing to reductions in both price and volume. Weak domestic demand contributed to stagnant non-fuel imports during the first half of the year,

CHART 1
JAPAN

COST CONDITIONS IN MANUFACTURING, 1972-82



Sources: Economic Planning Agency, *Annual Report on National Accounts;* and Bank of Japan, *Economic Statistics Annual.*
[1]Based on national accounts data which currently extend only through 1981.

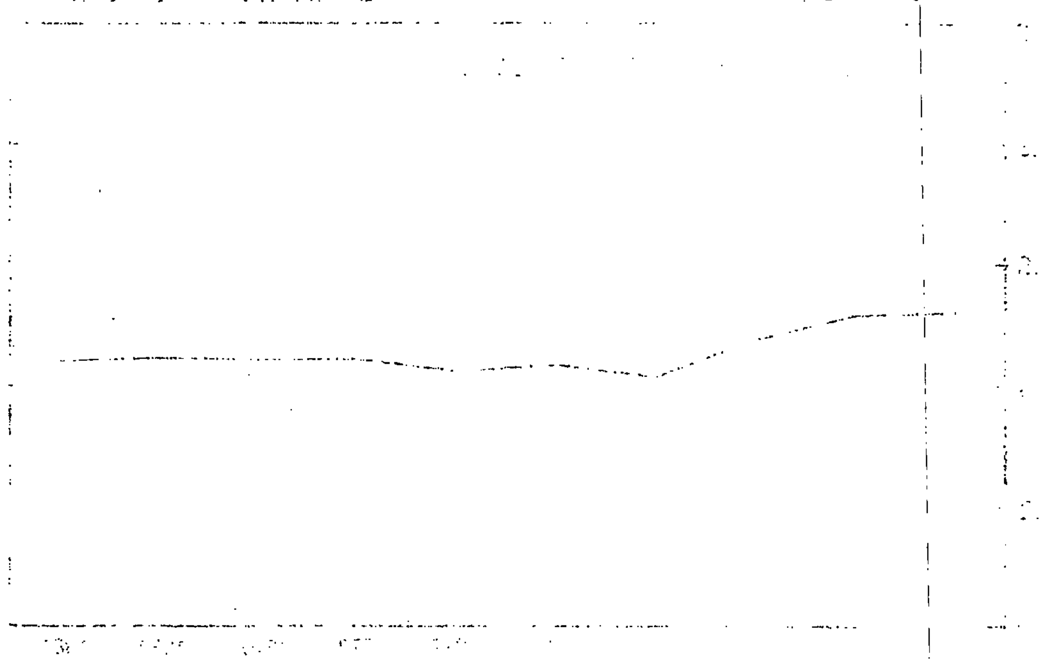
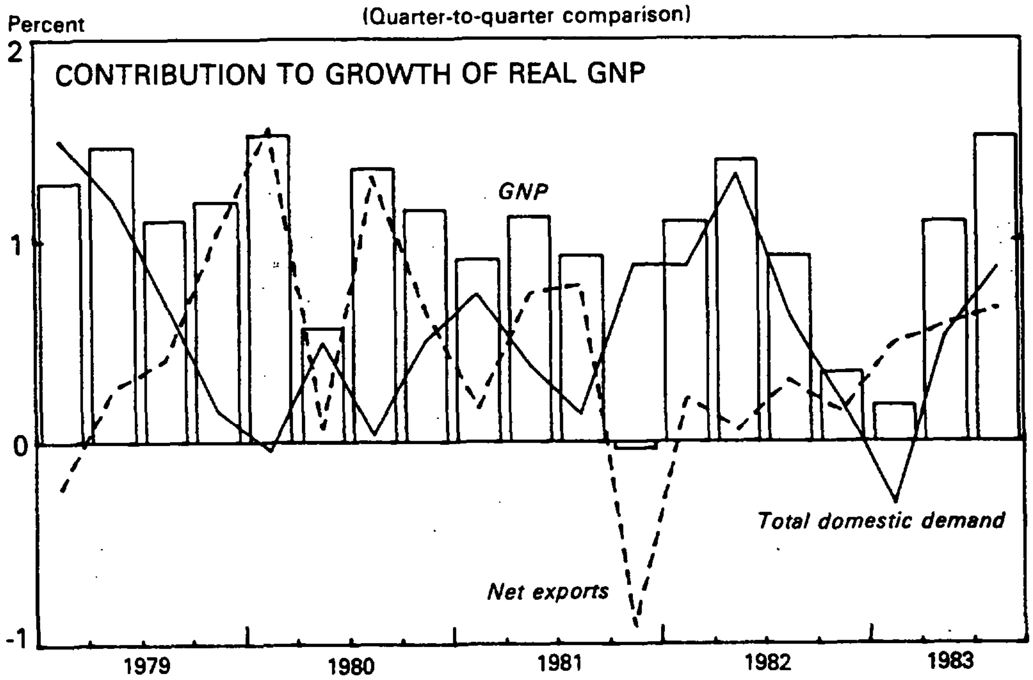


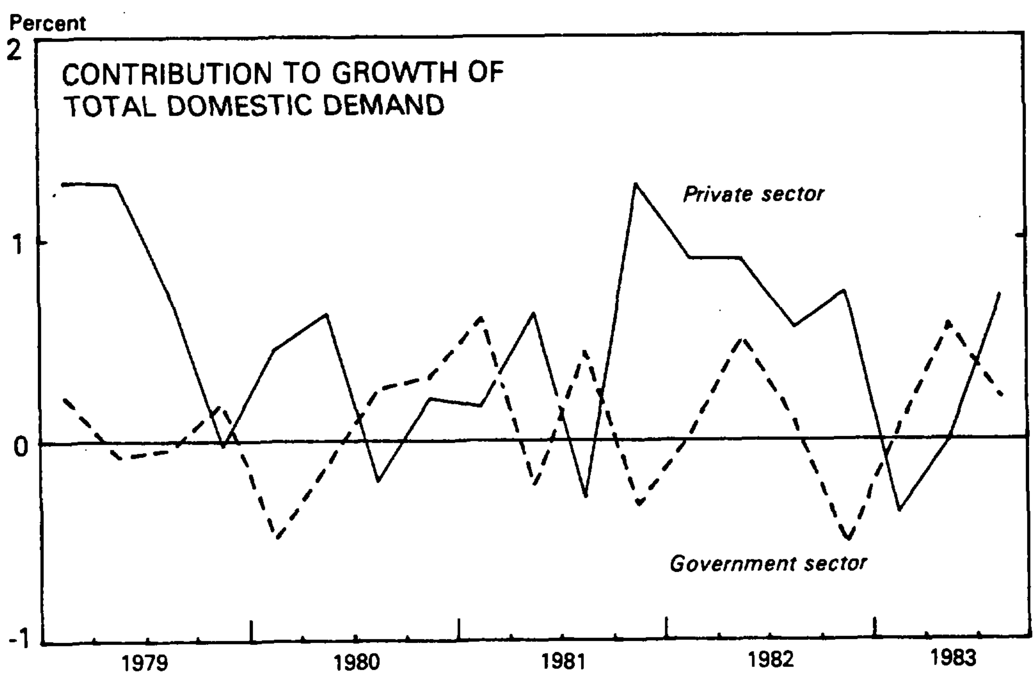
CHART 2

JAPAN

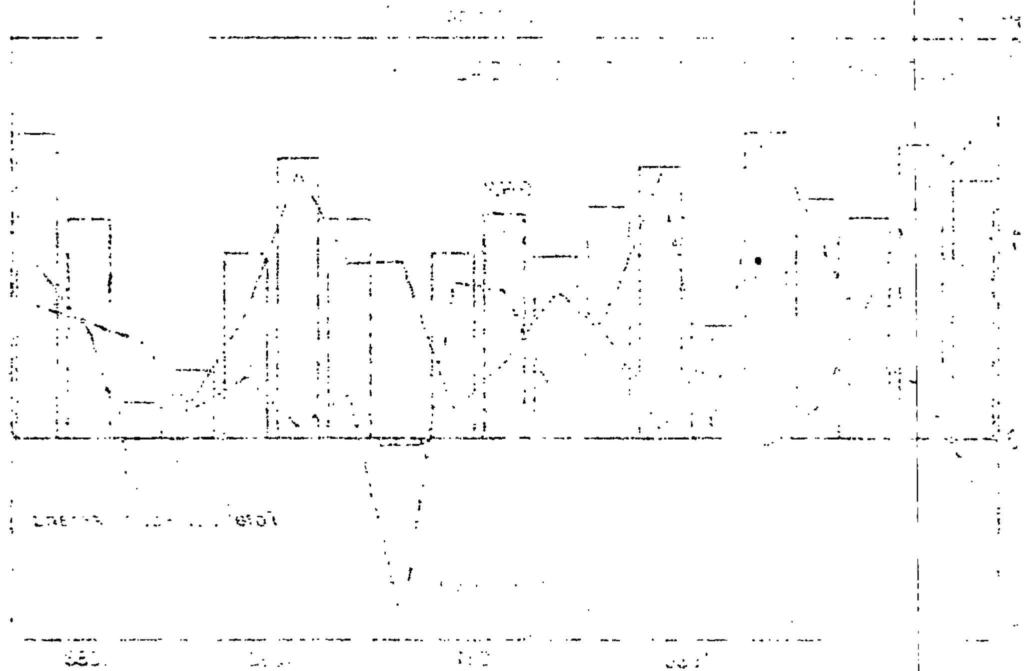
DEVELOPMENTS IN REAL GNP BY MAJOR AGGREGATES, 1979-83

(Quarter-to-quarter comparison)





Source: Economic Planning Agency, *Annual Report on National Accounts*.



although during the third quarter these imports picked up with the growth of industrial activity.

Table 1. Japan: Current Account Developments, 1982-83

	1982	1983 1/
	(In billions of U.S. dollars)	
Current account	6.9	21.1
Exports	137.7	145.7
Imports	-119.6	-114.0
Of which: fuels	-65.6	-58.5
Services and transfers	-11.2	-10.6
	(Percentage change)	
Export volume	-2.3	7.9
Import volume	-0.5	0.2
Of which: fuels	-3.5	-1.8
Export dollar unit value	-6.8	-1.4
Import dollar unit value	-7.7	-4.3
Terms of trade	1.0	3.0

1/ Staff estimates.

Given the favorable cost/price structure of industry, the recovery of export demand elicited a strong rebound in industrial production early in 1983, ending a year of stagnation. This, in turn, translated into an increase in overtime work and an improvement in capacity utilization with an accompanying increase in business fixed investment. Nevertheless, as exports account for about one half of manufactured output and manufacturing comprises only about 30 percent of GNP, the effect of exports on domestic incomes and growth has thus far been limited.

The growth of private domestic demand, which was maintained rather steadily at an annual rate of just under 4 percent throughout 1982, fell sharply in early 1983 as a result of weakness in all sectors, but then recovered to an annual rate of about 3.5 percent in the third quarter. The slowdown in growth of private consumption reflected the effects on disposable income of the low wage settlement for employees of major corporations in 1983/84, a decline in corporate profits during the second half of 1982/83 and the first half of 1983/84, and unusually low semi-annual bonus payments to employees. The savings ratio, which had been declining since the mid-1970s, appears to have stabilized, at least temporarily, in 1983. Consumption growth increased in the third quarter largely as a result of the removal of temporary factors that had depressed growth earlier in the year. After a brief, but strong spurt during the second half of 1982, residential investment declined sharply during the first half of 1983 owing to the termination of temporary, favorable factors and continuing structural imbalances in the housing market. A moderate rebound in housing investment occurred in the third quarter. Plant and equipment investment declined during late 1982 and early 1983 but has since picked up considerably. Developments in inventory accumulation have been mixed but generally weak during 1983.

The rate of unemployment, though considerably lower than in other industrial countries, reached a post-war record of 2.8 percent in September 1983 but subsequently fell to 2.6 percent (Chart 3). The rise during 1983 reflected an acceleration of labor force growth and a somewhat slower rise in employment. Nevertheless, the recorded rate of unemployment appears to understate the degree of labor market slack since there exists considerable hidden unemployment in the form of labor hoarding by firms. In the face of deteriorating labor market conditions, weak profits and lower inflation, wage behavior has been moderate. The 4.4 percent increase in average wage rates agreed to in the 1983 wage negotiations for employees of major corporations is the lowest in the 27-year history of the negotiations. Consequently, with the resumption of output and productivity growth in manufacturing, unit labor costs have fallen considerably in recent months and profits appear to be recovering.

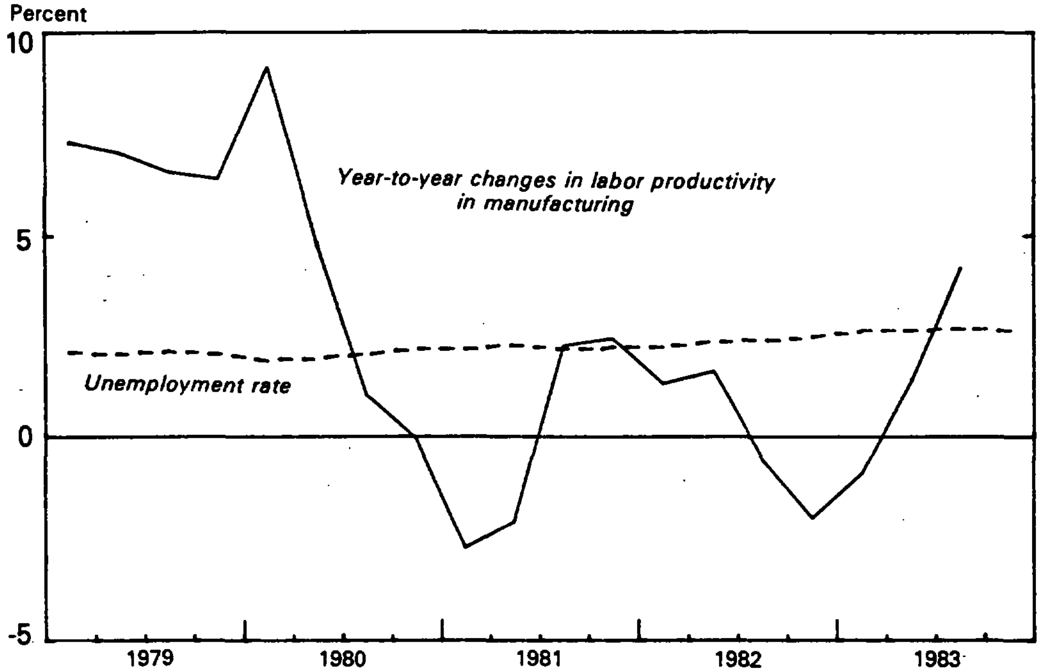
Prices have changed little during 1982 and 1983 reflecting the decline in energy prices as well as the weakness of domestic demand. Wholesale prices, which increased by 0.9 percent during 1982, fell by more than 1 percent during the year to October 1983 (Chart 4). Consumer price increases slowed from 1.8 percent during 1982 to 1.4 percent during the year to October 1983.

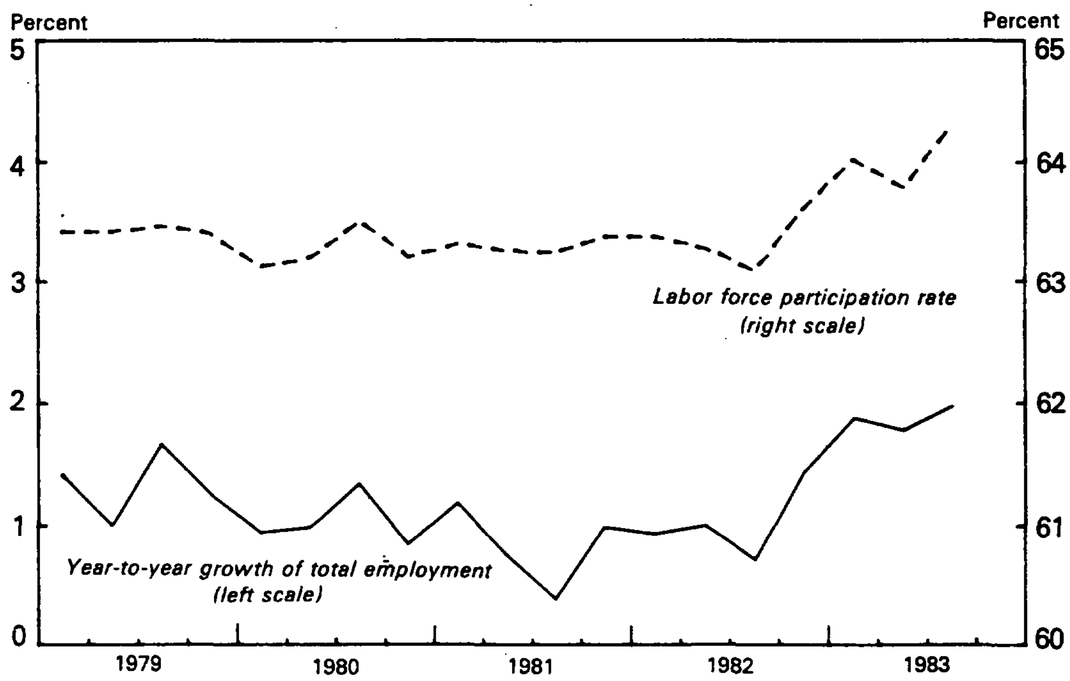
On the basis of these developments, the staff concurs with the authorities' estimates that GNP growth will be about 3.5 percent in 1983/84 as compared to 3.3 percent in 1982/83. However, the staff estimates that half of this growth will be accounted for by net foreign demand, while the authorities expect that this sector will account for no more than a third. The staff expects export growth to remain strong throughout the fiscal year and imports to pick up moderately during the second half; the current account surplus therefore is projected to reach $24 billion in 1983/84. The pickup in domestic demand that occurred in the September quarter should continue, though at a moderate pace, through the remainder of this fiscal year. The increase in industrial

CHART 3

JAPAN

LABOR MARKET CONDITIONS, 1979-83





Sources: IMF , Data Fund and Ministry of Labor, *Monthly Labor Statistics and Research Bulletin*.

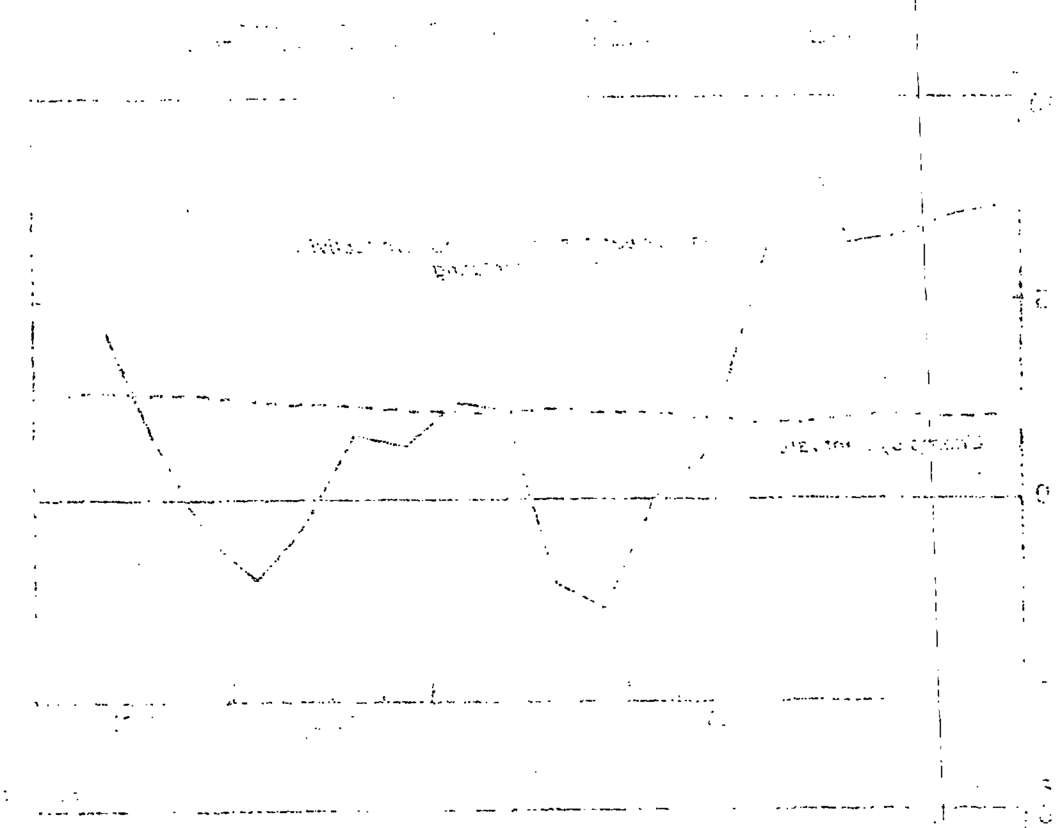
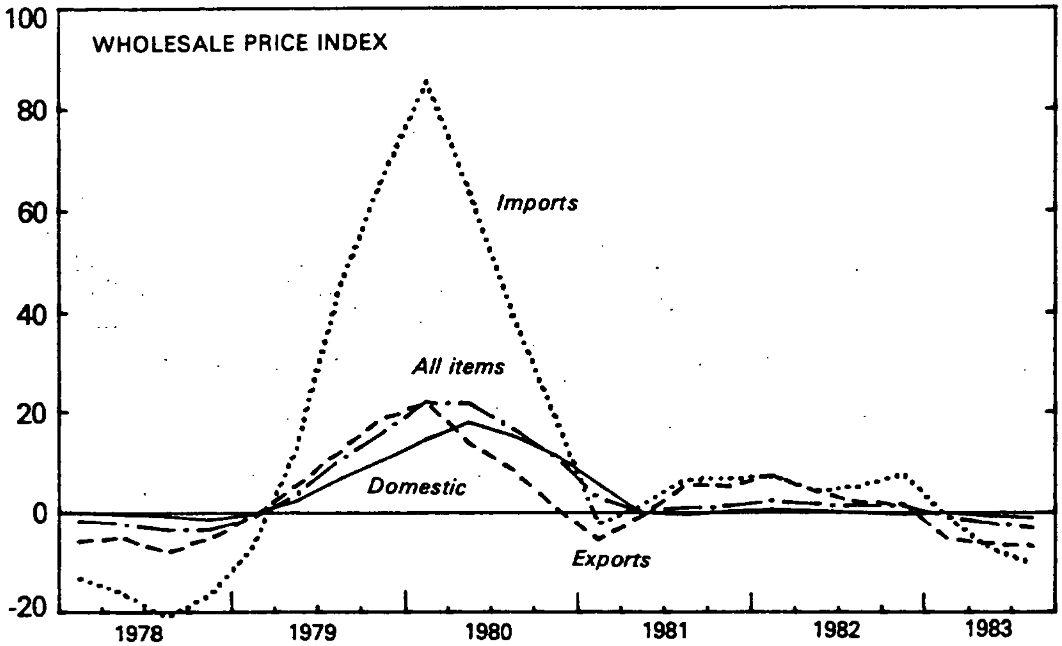


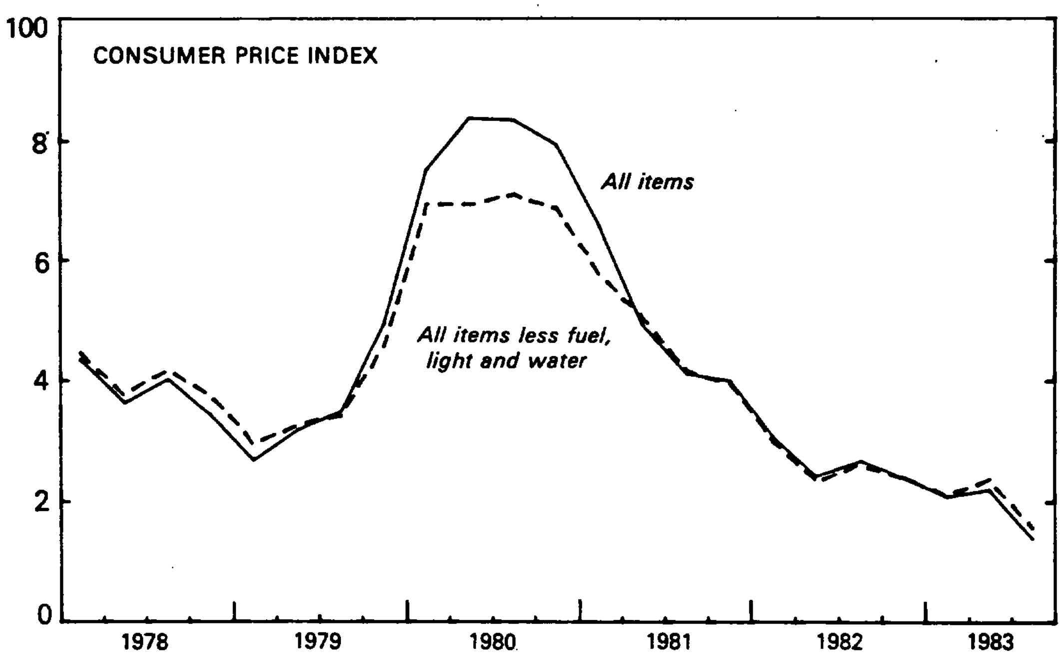
CHART 4

JAPAN

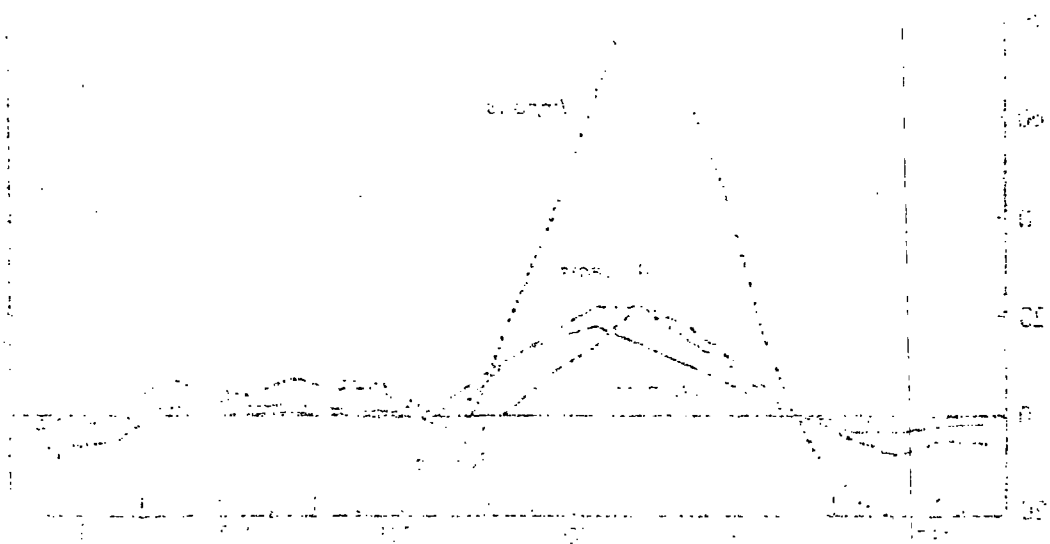
WHOLESALE AND CONSUMER PRICES, 1978-83

(Year-to-year percentage changes)





Source: Bank of Japan, *Economic Statistics Monthly*.



activity and the moderation of costs should result in a considerable increase in profits. Initially, the effects of this have been concentrated in stronger plant and equipment investment; the effects on incomes and consumption are likely to materialize only with a considerable lag.

After increasing by 18 percent between early November 1982 and mid-January 1983, the nominal effective value of the yen remained fairly stable through September, but increased by some 3.5 percent between early October and mid-January 1984 (Table 2). 1/ These developments reflected the pervasive strengthening of the yen during the last two months of 1982, but divergent trends in its behavior vis-a-vis other major currencies during 1983. Following an appreciation of almost 20 percent against the dollar between early November 1982 and mid-January 1983, the dollar value of the yen was generally stable during 1983. The modest movements during the year--most notably a depreciation between early June and end-August and a subsequent offsetting appreciation through end-September--closely paralleled changes in the interest rate differential between Japan and the United States (Chart 5). Against major European currencies, the yen strengthened by somewhat less than against the dollar between November 1982 and January 1983, but then appreciated substantially between late March 1983 and mid-January 1984. These movements appear to have resulted from the relatively favorable prospects for factors affecting Japanese competitiveness in both goods and capital markets. The real value of the yen increased substantially against the major European currencies, but only slightly vis-a-vis the U.S. dollar between the third quarter of 1982 and the third quarter of 1983 (Chart 6).

Net capital outflows remained brisk during the first three quarters of 1983 owing to continued large net outflows of long-term capital. After a sharp rebound in foreign purchases of Japanese securities at the end of 1982, such purchases remained high during the first half of 1983 but slackened considerably during the third quarter. Direct investment outflows and trade credits slowed somewhat in 1983, but Japanese lending abroad and purchases of foreign securities were unusually large during this period. The latter appears to have resulted from slack domestic corporate demand for funds, an ongoing diversification of Japanese portfolios, and, during part of the period, a widening of interest differentials against Japan reflecting primarily an increase in U.S. interest rates. Foreign lending by Japanese banks, excluding changes in interbank deposits, appears to have increased considerably more rapidly than global bank lending during the first half of 1983.

1/ Exchange rate changes described in the text are point-to-point changes calculated to capture the full extent of major adjustments and are not comparable to changes presented in Table 2 which are based on period averages.

Table 2. Japan: Exchange Rates of the Yen, 1/ 1982-83

(Period averages)

	MERM 1975=100	¥/$	¥/DM	¥/FF	¥/£	¥/SwFr	Relative Normalized Unit Labor Costs
1982							
January	143.02	224.59	97.99	38.56	423.68	121.80	108.5 2/
October	127.06	271.40	107.27	37.97	460.66	125.05	101.5 3/
November	131.23	265.13	103.76	36.75	432.64	120.68	
December	140.76	242.52	100.28	35.37	392.69	118.07	
1983							
January	145.86	232.94	97.53	34.41	366.48	118.38	111.4 4/
May	148.17	234.80	95.13	31.60	369.56	114.00	109.6 5/
August	147.06	244.33	91.41	30.39	367.02	112.95	
September	148.09	242.77	90.99	30.12	363.89	112.22	
October	153.03	233.01	89.56	29.31	348.96	110.43	
December	155.65	234.43	85.27	27.94	336.01	106.69	
Percentage change between ((-) = depreciation) 6/							
January and October 1982	-11.16	-17.25	-8.65	1.55	-8.03	-2.60	
October 1982 and January 1983	14.80	16.51	9.99	10.35	25.70	5.63	
January and May 1983	1.58	-0.79	2.52	8.89	-0.83	3.84	
May and August 1983	-0.75	-3.90	4.07	3.98	0.69	0.93	
August and October 1983	4.06	4.86	2.07	3.68	5.18	2.28	
October and December 1983	1.71	-0.61	5.03	4.90	3.85	3.51	

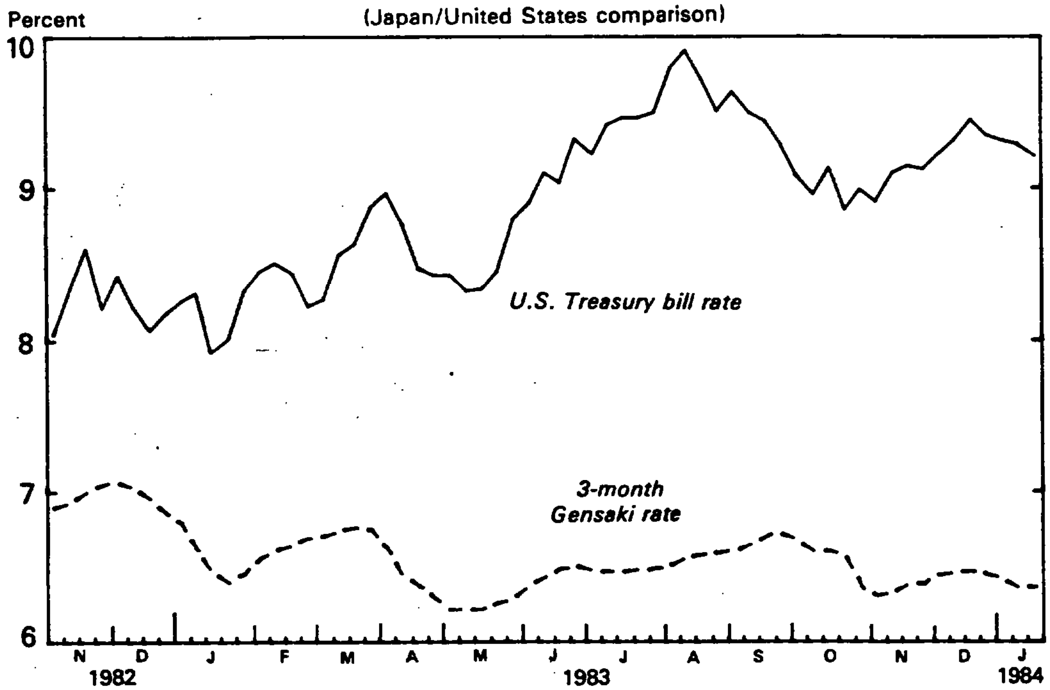
1/ Calculated from representative rates.
2/ QI 1982.
3/ QIV 1982.
4/ QI 1983.
5/ QII 1983.
6/ The periods for these calculations were chosen to highlight the major short- to medium-term swings of exchange rates.

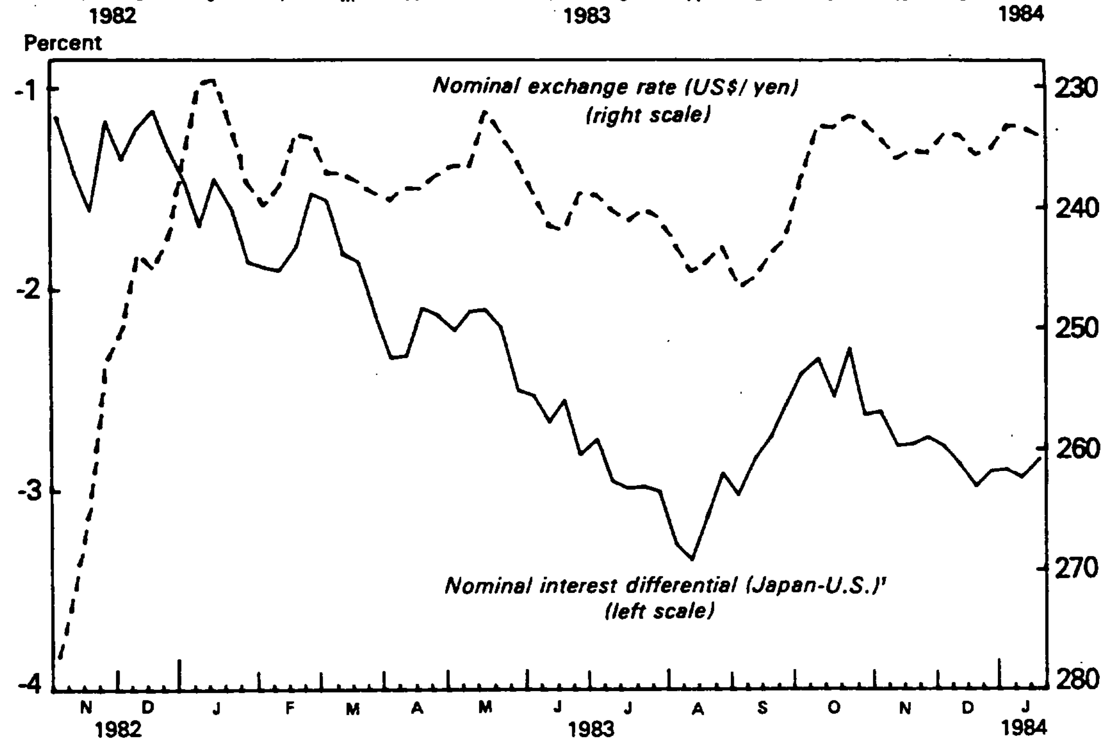
CHART 5

JAPAN

NOMINAL INTEREST RATES AND THE NOMINAL EXCHANGE RATE, 1982-84

(Japan/United States comparison)





Sources: IMF data fund and data provided by the Japanese authorities.

[1]Gensaki rate less the U.S. Treasury bill rate.

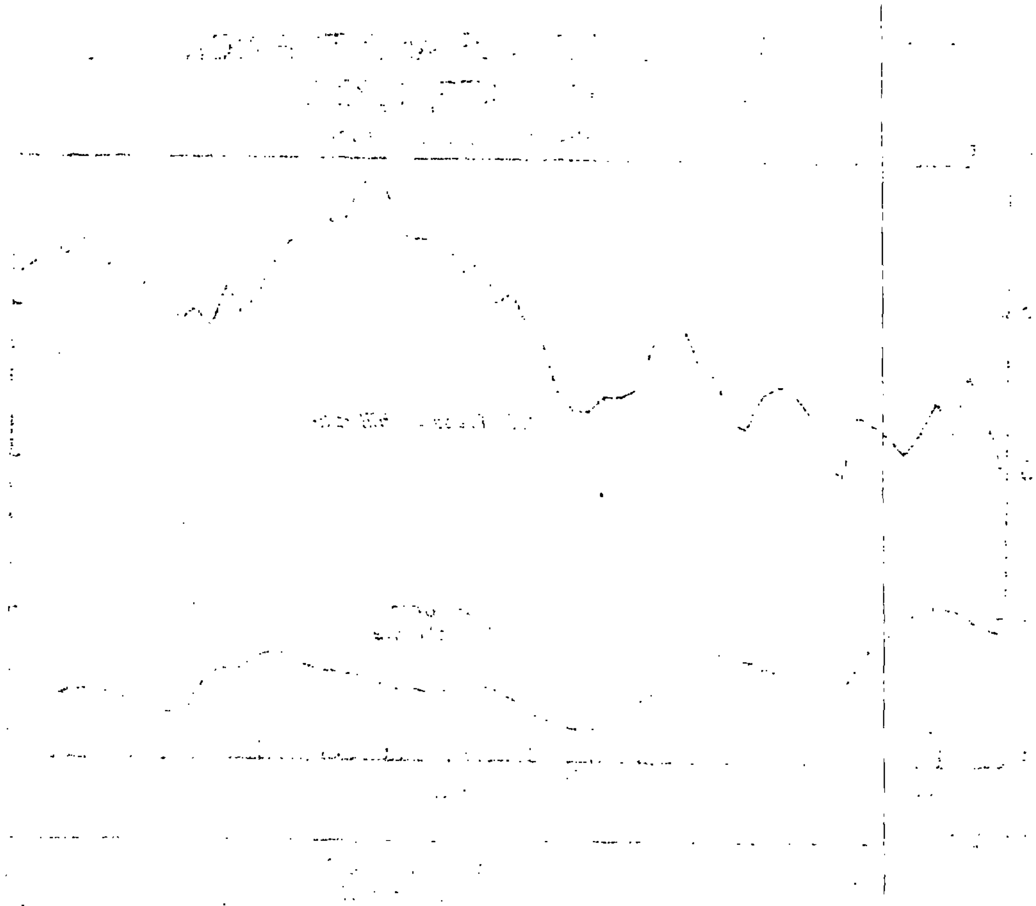
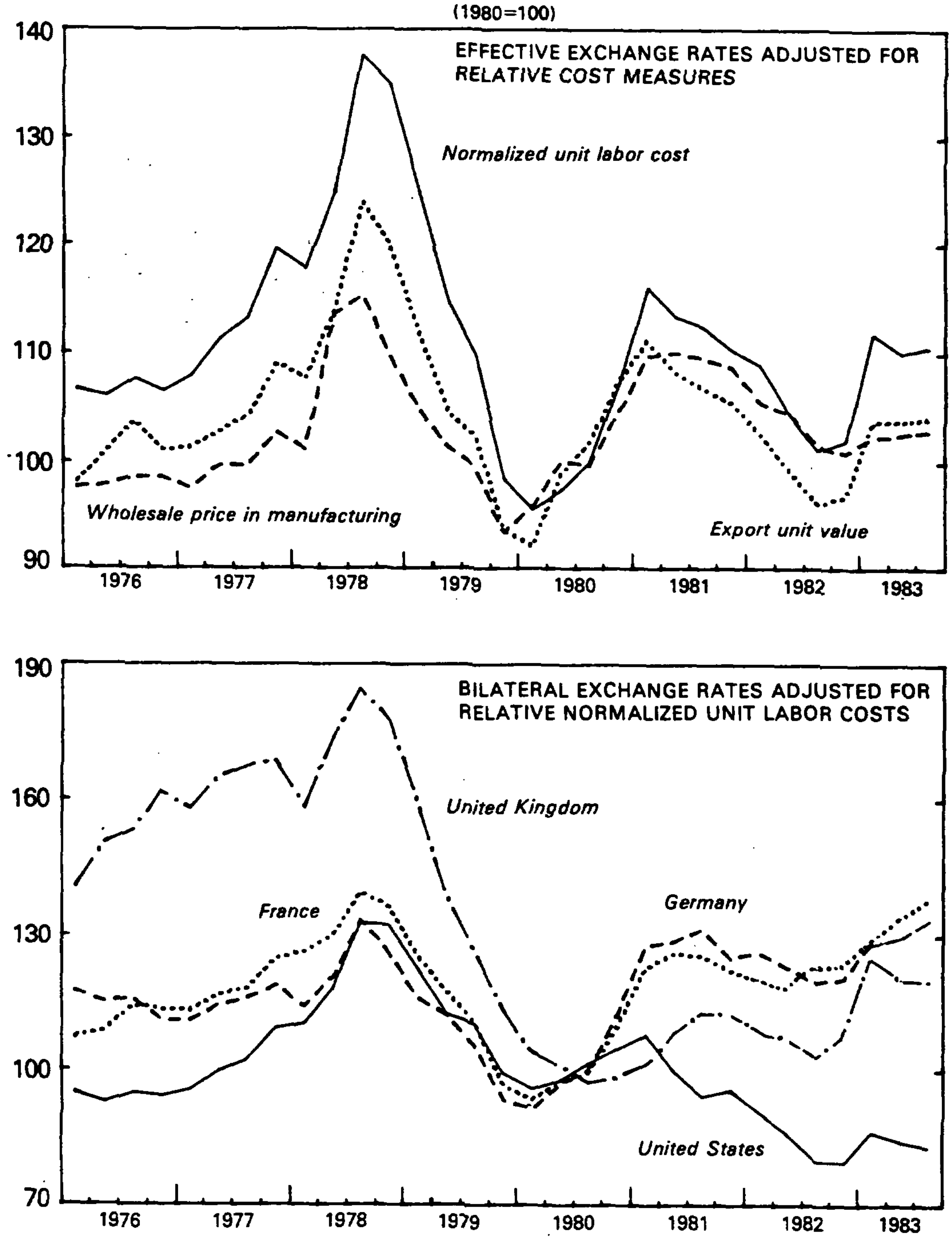


CHART 6

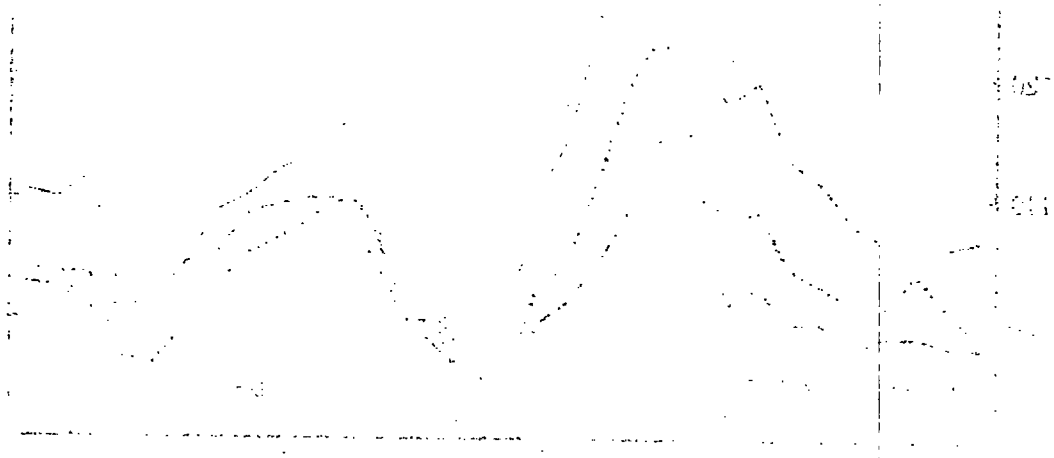
JAPAN

INDICATORS OF THE REAL VALUE OF THE YEN, 1976-83[1]

(1980=100)



Source: IMF, *International Financial Statistics* and Data Fund.
[1] Rising indices denote falling competitiveness.



In 1981 the Japanese authorities announced their intention to double the dollar value of official development assistance for the period 1981-85 relative to that during the previous five-year period. Despite declines in the dollar value of actual disbursements in 1981 and 1982, the authorities remain committed to their announced target. This will require average annual increases in disbursements of ODA of about 28 percent between 1983 and 1985.

III. Policy Discussions

The formulation of macroeconomic policies continues to be dominated by the Government's commitment to reducing large central government budget deficits through slower growth of expenditures, the desire to achieve a sustained recovery led by private domestic demand, and a concern to avoid any weakening of the yen. In addition, the authorities have addressed policies to international complaints about the implications of Japan's rising current account surplus and the degree of openness of Japan's goods markets and financial system. These considerations have continued to present obvious conflicts in the conduct of policy. The active use of monetary policy to help stimulate demand has been constrained by its potentially adverse effect on the value of the yen. Despite the belief of the authorities that a reduction in the fiscal deficit is a prerequisite for sustained recovery in the medium term, they have had to confront the more immediate trade-off between progress in reducing the budget deficit and minimizing the withdrawal of support to domestic demand.

The authorities believe that many of the factors underlying the recent performance of the domestic economy--particularly high interest rates and the weakness of the yen--are largely attributable to foreign influences. Lower energy prices and the strength of the foreign recovery have also contributed substantially to the growth of the current account surplus. For their part, the authorities announced in October a set of measures designed to help stimulate domestic demand and further open Japan's trade and financial markets to the rest of the world. The measures included additional public works expenditure for the current fiscal year, a cut in personal income and local taxes, some tariff reductions and other import promotion measures, and steps to enhance the international attractiveness of yen-denominated assets. At the same time, the official discount rate was reduced by half a percentage point. The authorities said that under current circumstances, these measures represent their utmost effort to help support a recovery of domestic growth and to respond to international concern over developments in the Japanese economy.

1. Fiscal policy

During the last two fiscal years, the overall stance of fiscal policy was restrictive; it remains so in 1983/84. Budgetary policy during this period has reflected the flexibility demonstrated by the authorities in their efforts to reconcile the objectives of reducing the large fiscal deficit and avoiding the weakening of domestic demand growth. However, the authorities remain convinced that the arguments for immediate progress in reducing the large central government deficit are compelling. First, with central government interest payments equivalent to 17 percent of expenditure in 1983/84 and increasing, they fear that the flexibility of fiscal policy to respond to future disturbances has been seriously impaired. Second, a smaller deficit and lower level of public expenditure would better place the Government to respond to demands arising in later years from the projected rapid aging of the population. On a more general level, the authorities view the increasing dependence on the public sector as debilitating to the private sector which provided the dynamism in the Japanese economy up to the early 1970s. Credible efforts to reduce the deficit, therefore, should enhance the private sector's confidence in economic prospects and help sustain growth in the medium term despite possible depressing effects in the short term. The authorities do not believe that Japan's high savings rate or the fact that the deficit of the general government is substantially smaller than that of the Central Government should lessen concern about the central government deficit.

Beyond these motivations for reducing the fiscal deficit, the authorities also doubt the effectiveness of fiscal policy as a mechanism for supporting domestic demand. They believe that, over time, certain public and private sector activities have a high degree of substitutability. They fear that government demands on credit markets could eventually crowd out a recovery of private investment even though the large-scale issue of government bonds to date is not believed to have been an immediate cause of recent high interest rates or sluggish private investment. Shorter-term considerations are also of concern. The authorities argued that increases in public debt tend to produce expectations of a larger future tax burden that dampen current private spending. Moreover, the authorities believe that the effectiveness of fiscal policy has diminished owing to a decline in the fiscal multiplier.

The Government's strategy for reducing the deficit is included in the medium-term guidelines for growth through 1990/91 adopted in August 1983. These guidelines replaced a medium-term plan that aimed at reducing the issuance of bonds to finance current expenditure (that is, a deficit in excess of public investment spending) from 2.1 percent of GNP in 1981/82 to zero in 1984/85. The original plan was to be executed in parallel with the authorities' efforts to reduce the overall central government deficit and contain the growth of expenditures. However, in both 1981/82 and 1982/83, the unexpected weakness of the economy produced substantial revenue shortfalls, and persistently high interest rates aggravated the large debt service burden. Consequently, the planned degree of fiscal restraint was not realized. Despite these setbacks, the overall deficit as a proportion of GNP was reduced from 5.7 percent in 1980/81 to 5.2 percent in 1982/83 (Table 3). The share of expenditure in GNP, which had increased from about 13 percent in 1973/74 to about 18 percent in 1981/82, was reduced slightly in 1982/83. Nevertheless, the persistent weakness of the economy foreclosed the possibility of adhering to the medium-term plan, which was formally abandoned in late 1982.

The new medium-term guidelines call for eliminating the issuance of bonds to finance current expenditure by 1990/91, restraining the growth of government expenditure, and improving the efficiency of such expenditure through administrative reform. These guidelines are based on a projected average annual growth rate of 4 percent through 1990/91. While there has been some debate over this estimate, the authorities felt that this was all that could be achieved given the possible adverse short-term effects of fiscal reconstruction on growth and the need to avoid excessive reliance on foreign demand. Moreover, higher growth could not be relied on to reduce the deficit. Although there are no official estimates of the "structural" component of the deficit, the authorities thought that a large portion of the deficit is "structural" in the sense that the growth of some expenditures is virtually fixed owing to legal and institutional arrangements and structural changes in the economy are reducing the elasticity of the tax system.

The difficulties in eliminating deficit financing of current expenditure by 1990/91 are underscored by projected budgetary trends. On average, the deficit would have to be reduced by ¥ 1 trillion (2 percent of 1983/84 expenditure) per annum; with no change in the tax system, revenue is projected to grow by about ¥ 2 trillion per annum, of which ¥ 0.6 trillion would be automatically transferred to local governments under present legal arrangements and ¥ 1 trillion would go to increased debt service. Therefore, insofar as the authorities do not believe that there is a public consensus in favor of an increase in taxes to meet the medium-term goal, severe expenditure restraint would be needed. As the effects of such expenditure restraint are felt, however, the public attitude toward tax increases could change, and allow such increases to contribute toward meeting the medium-term goal. The authorities also indicated that there could be some flexibility in year-to-year progress in meeting the goal.

The initial 1983/84 budget, which provided for a reduction in the deficit from 5.2 percent of GNP to 4.5 percent, reflected a redoubling of efforts to contain expenditure with no tax measures to augment revenue. Expenditure as a proportion of GNP was budgeted to decline by 0.8 percent--slightly more than the decline in 1982/83. However, in response to the persistence of weak economic growth, public works expenditures were frontloaded. As was the case in 1981/82, this left open the possibility of reducing the planned withdrawal of fiscal

Table 3. Japan: Central Government General Account Budget, 1981/82-1983/84

(In billions of yen)

	1981/82			1982/83			1983/84
	Initial	Revised	Settle-ment	Initial	Revised	Settle-ment	Initial
Adjusted expenditures 1/	45,756	46,093	45,889	48,368	47,394	47,077	47,907
Adjusted revenue 1/	34,511	34,170	31,413	39,000	32,976	33,234	35,211
Adjusted deficit 1/	11,245	11,923	14,476	9,368	14,418	13,843	12,696
In percent of GNP 2/							
Bond issues	4.6	5.0	5.1	3.8	5.4	5.3	4.7
Adjusted deficit	4.2	4.7	5.7	3.4	5.4	5.2	4.5
Memorandum items: official accounts							
Expenditures	46,788	47,125	46,921	49,681	47,562	47,245	50,380
Revenue	34,511	34,170	33,907	39,200	33,176	33,434	37,033
Deficit	-12,277	-12,955	-13,014	-10,481	-14,386	-13,811	-13,347
Bond issues	12,270	12,900	12,900	10,440	14,345	14,045	13,345

Sources: Staff calculation based on data provided by the Japanese authorities.

1/ These accounts reflect adjustments for financing items made by the staff which are explained fully in the forthcoming "Japan: Recent Economic Developments."

2/ On the basis of the official forecast for or estimate of nominal GNP prevailing at that time.

stimulus for the year as a whole by augmenting budgeted expenditures for the second half of the year so as to maintain the pace of expenditures established during the first half. Actual tax revenues during the first 8 months of the year were somewhat less than planned, but a projected improvement in profits during the second half is expected to bring tax receipts for the year closer to the budgeted amount.

Budgetary changes included in the October measures increased public works contracts by the Central Government by about 7 percent relative to the amount planned in the initial budget. 1/ The October measures also included tax reductions in the form of an increase in the minimum taxable income, a reduction in tax rates, primarily for middle-income taxpayers, and a decline in local taxes. About ¥ 150 billion of the tax reduction was for 1983/84 and, subject to Diet approval, an additional ¥ 1.06 trillion is scheduled for 1984/85. The latter may be offset by increases in indirect, corporate and other taxes. The authorities thought that in the current economic environment of growing consumer confidence and stable prices, the income tax reductions would help stimulate demand whether or not offsetting increases in other taxes were implemented. Taken together, the fiscal measures included in the October package are estimated to increase the 1983/84 central government deficit from 4.5 percent to 4.8 percent of GNP. Even after these measures are taken into account, however, staff calculations indicate that, on a cyclically-adjusted basis, the withdrawal of stimulus by the Central Government in 1983/84 will be about one half of a percent of GNP--somewhat smaller than that in the previous fiscal year.

2. Monetary policy

The authorities indicated that the liberalization of domestic financial markets in recent years has significantly affected the conduct of monetary policy. Open market operations have become more important as an instrument for implementing policy changes and the transmission mechanism from changes in interbank rates to domestic activity has been strengthened by the development of free short-term money markets. Quantitative credit controls had not been used actively for some time and their importance as a monetary instrument would continue to diminish. However, such controls would probably still be used if an abrupt change in monetary policy were needed. Insofar as the official discount rate is generally kept below market interest rates and credit through the discount window is rationed, changes in the official discount rate are mainly symbolic. Generally, these are accompanied by open market operations to adjust free market interest rates and by changes in other administered rates. Financial market liberalization is also affecting the demand for money as a result of disintermediation arising

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1/ Details of these measures are reported in the forthcoming "Japan: Recent Economic Developments."

from differences between administered interest rates on bank deposits and those on a wider variety of new assets with free rates. Because these changes are occurring slowly, however, instability in the demand for money is not believed to be an immediate problem.

While domestic considerations alone--the absence of inflationary expectations and high real interest rates--would warrant an easing of monetary conditions, exchange rate considerations have been central to the formulation of monetary policy throughout most of 1982 and 1983. The growth of broad money declined from a year-to-year rate of 11 percent in the fourth quarter of 1981 to about 7 percent in the third quarter of 1983--a deceleration somewhat less than the combined effects of the slowdown in the growth of nominal GNP and trend movements in velocity. Both short- and long-term nominal interest rates have moved within narrow margins throughout 1982 and 1983 while the inflation rate has declined by about 1 percentage point.

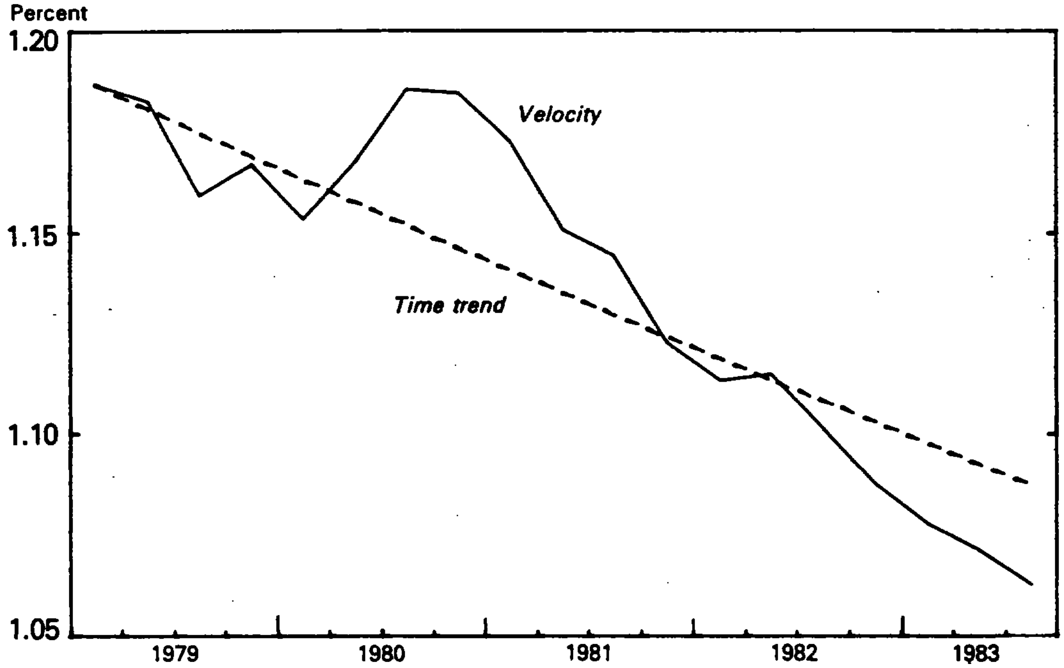
In contrast to 1982, when the weakening of the yen had prompted a tightening of monetary policy, the generally stable behavior of the yen against the dollar and some strengthening against major European currencies during 1983 relieved the pressure from exchange markets for further changes in monetary policy. The authorities explained that after a slight easing of policy with the appreciation of the yen in late 1982, the degree of monetary restraint was unchanged until October 1983. Money had been allowed to grow only as fast as was possible without producing conditions that would weaken the yen. A reduction in the discount rate had been considered early in the year, but had been rejected because the risk of inducing a renewed depreciation of the yen had seemed too great. Nevertheless, broad money continued to increase somewhat faster than nominal income growth adjusted for trend changes in velocity and, between January and May, short-term nominal interest rates declined by up to one half of one percentage point (Chart 7).

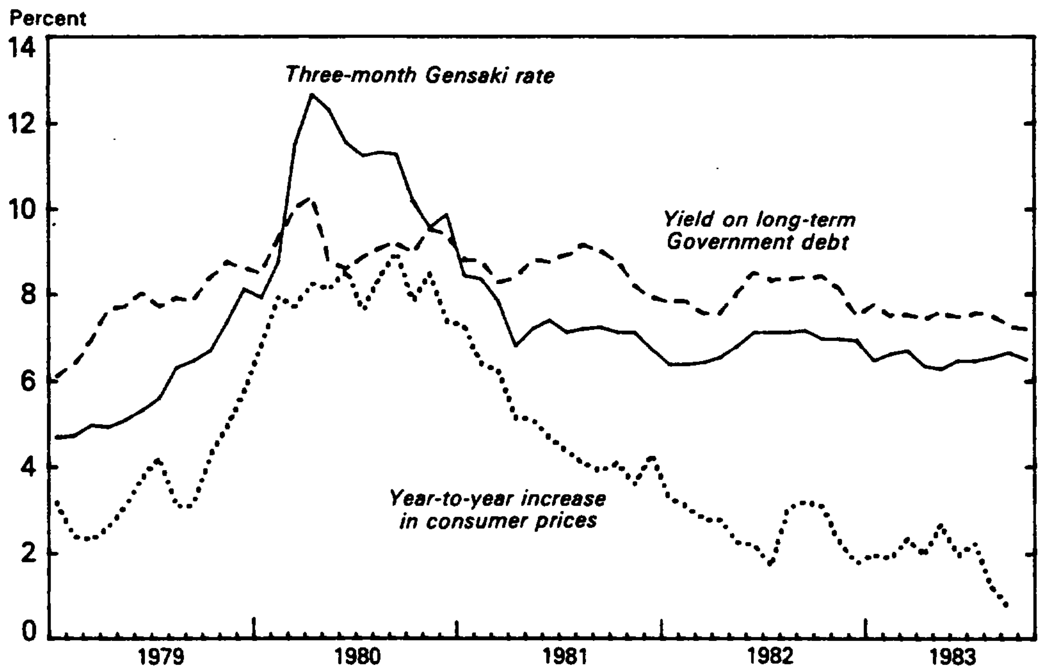
The authorities said that the developments just mentioned were not indicative of an easing of monetary policy. In their view, the faster-than-trend decline in velocity had probably resulted from lags in the adjustment of savings behavior to the decline in income growth or the tendency for savings behavior to respond to permanent rather than transitory changes in income. The decline in interest rates during the first half of the year, as well as a subsequent firming on the order of one half of one percentage point between June and September, was attributable to normal seasonal fluctuations. While no positive monetary action had been taken to stem the weakening of the yen during the summer months, the normal seasonal increase in interest rates during this period might have been offset through policy actions had the yen been stronger. The authorities had stood ready to take more aggressive action on interest rates, but the decline in foreign interest rates and strengthening of the yen during September made this unnecessary.

CHART 7

JAPAN

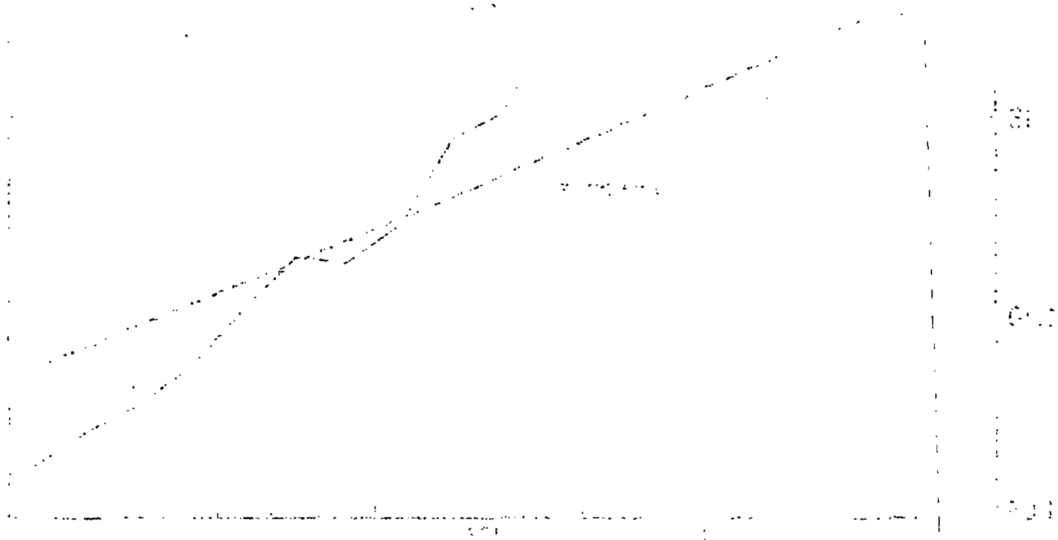
INDICATORS OF THE STANCE OF MONETARY POLICY, 1979-83





Sources: Bank of Japan, *Economic Statistics Monthly* and IMF, *International Financial Statistics*.

[1]The time trend is calculated from a regression of M2/GNP on a time trend from 1975-83.



On October 21, the official discount rate was reduced, for the first time since December 1981, from 5.5 percent to 5.0 percent. This was intended to signal a significant easing of monetary policy and, along with other changes in interest rates, expected to improve business profits and encourage investment. Following the reduction of the discount rate, other administered interest rates were also reduced (long-term administered rates by 0.2 percentage points, the short-term prime rate by 0.5 percentage points and administered deposit rates by 0.25 percentage points). Supporting open market operations reduced inter-bank and other short-term market rates by some 0.2 to 0.5 percentage points. Nevertheless, the projection for year-to-year growth of broad money for the fourth quarter (which was announced prior to the discount rate action) remained at about 7 percent--similar to the growth rate observed in the previous two quarters.

Political pressure for a discount rate cut had been strong throughout the past year but had been resisted until the risks of adversely affecting the value of the yen were judged to be small. The authorities said that two factors had been taken into account in deciding on the discount rate cut in October. First, since August, U.S. interest rates had declined slightly and the growth of M1 in the United States had returned to within its target range, dampening expectations of further increases in U.S. interest rates. Second, the strengthening of the yen during September had been interpreted, at least in part, as as an indication that Japan's strong foreign balance was beginning to influence the exchange rate. The basic balance had moved into surplus between April and September, and this was expected to have a stronger effect on the exchange rate than an increase in the current account surplus alone. The authorities were encouraged that the reduction in the discount rate had not weakened the yen. Foreign exchange market intervention by the United States following the action and market perception that the Japanese authorities would intervene should the yen weaken significantly were believed to have had a stabilizing effect.

3. Exchange rates

Although the authorities remain of the view that the current level of the yen does not reflect fully the relatively strong competitive position of the Japanese economy, their views on the degree to which the yen should be considered unduly weak appeared to have changed slightly during the past year. This seemed to reflect both the fact that the yen had already strengthened substantially against currencies other than the dollar and a judgment that the fundamentals of the U.S. economy had improved. Nevertheless, the authorities were anxious to see a further strengthening of the yen, particularly against the dollar. Not only would an appreciation be the most effective means of reducing the current account surplus, but it would enhance price stability, help the recovery of domestic demand through a favorable terms of trade effect, and eventually allow an easing of monetary policy which would lower interest costs for private investors and the Government's debt servicing burden. It was noted that the business community, in particular, had appreciated the substantial reduction in the volatility of the yen during the last year which was attributed to the convergence of economic conditions in the major industrial countries.

These hopes notwithstanding, there seemed to be somewhat less optimism on the prospects for a significant strengthening of the yen vis-a-vis the dollar than on previous occasions. The authorities continued to believe that the fundamentals of the Japanese economy--particularly the large current account surplus and relatively favorable cost and price conditions--should tend to strengthen the yen, but feared that foreign interest rates could remain high for some time and dominate the influence of these forces. In fact, in private forecasts for 1984/85, it was generally assumed that the yen would be in the range of ¥ 220-230/US$1, while a year ago an exchange rate of ¥ 200-210/US$1 was being projected. It was hoped that a period of stability in foreign interest rates, even if at a high level, would allow Japan's favorable fundamentals to have a larger effect on the exchange rate.

The authorities generally thought that the possibility for policy action to influence the value of the yen was limited, both because the problem is more one of a strong dollar than of a weak yen and because the forces responsible for the current alignment of exchange rates were largely beyond their control. The authorities saw a positive, though limited, role for coordinated intervention during periods when a currency was clearly undervalued. The coordinated intervention in early August had been useful, but its effect had been small. Not only was it hastily formulated in the face of disorderly market conditions, but it had also not been accompanied by supporting changes in macroeconomic policies in other countries.

4. Financial market policies

During the last decade there has been a dramatic evolution of the Japanese financial system from one dependent mainly on bank lending largely funded by deposits with officially controlled interest rates, to one with a variety of assets and considerable scope for the interplay of market forces. This evolution has been the result of a number of factors, the most important of which are the large-scale issue of government debt since 1975 and a higher degree of integration of the Japanese financial system with the rest of the world. Remaining issues related to financial market liberalization--control over administered bank deposit rates, restrictions on the range and characteristics of assets, and regulations that compartmentalize the functions of financial institutions--are the subject of considerable debate both within and outside Japan. The authorities recognize that market forces will continue to exert strong pressure for further decontrol and, therefore, that the process is inevitable. Nevertheless, representatives of both the Government and private sector believe that there should be official guidance of the path and pace of change so that problems can be recognized and attended to as they arise.

The large-scale maturing of long-term government debt due to begin in 1985 is widely expected to intensify the pressure for liberalization. A large volume of short-term assets with free interest rates will become available and could result in substantial disintermediation given the current regulated structure of bank deposit rates. The financing needs of the Government are also likely to require further changes in the traditional roles of financial institutions. Already, during the last year, several restrictions on commercial bank activities in government bond markets were removed and further changes are scheduled. The authorities also acknowledged that a wider array of government debt instruments would probably be necessary to meet refinancing needs. However, in this connection, the authorities questioned the desirability of expanding and enhancing the competitiveness of the presently very limited Treasury bill market: large-scale disintermediation could result while deposit rates remain controlled and the required increase in yields on Treasury bills, which are now absorbed primarily by the Central Bank, would raise government funding costs. The authorities also stressed that Treasury bills in Japan are used only for temporary financing within a year, rather than for general revenue raising, and therefore the market is not well-suited to expansion.

Other domestic factors may dampen the pace and limit the scope of liberalization, particularly the deregulation of deposit rates, which is an important prerequisite for more general liberalization measures. Among these is the perceived need to protect the postal savings system which currently absorbs about 30 percent of personal savings in relatively short-term deposits at regulated interest rates and is an important means of financing the Government's net lending operation. Beyond this institutional constraint, is the perception that small savers are best protected by a stable even if lower-than-market structure of interest rates. The authorities indicated that, for the time being, deregulation would proceed with a further freeing of interest rates on large deposits with short maturities.

Regulatory changes in recent years have virtually freed Japan's money and capital markets of formal restrictions on the international movement of funds. In addition, during the last two years certain guidelines on international borrowing and lending were removed or eased. Recently, however, there has been growing foreign criticism of the limited array of available assets and certain regulatory practices and taxes which are believed to limit the attractiveness of Japanese markets and inhibit capital inflows. The authorities noted that nonresident and resident investors receive identical treatment in Japanese markets. Insofar as foreign demands are for reciprocal treatment of investors--that is, for non-Japanese institutions to have the same privileges in Japanese markets as Japanese institutions have in foreign markets--the authorities said that this would imply that all financial markets have identical structures, which is not and cannot be the case. The authorities also believed that international capital flows and exchange rates are based on investors' views of fundamental economic and political conditions rather than the particular characteristics of countries' capital markets.

Nevertheless, in response to some of these criticisms, a number of changes were announced in the October measures and in conjunction with the U.S.-Japanese summit in November. Among these steps, the authorities undertook to reduce restrictions on forward foreign exchange transactions, to consider the establishment of a bankers' acceptance market, to reform legislation that currently limits foreign investment in certain companies, to lower the denomination of, and enlarge the ceiling on, each bank's issue of certificates of deposit, and to ease guidelines on the issue of Euro-yen bonds by residents. The authorities, as well as many private market participants, thought that the short-term effects of these measures on the value of the yen were likely to be small. In the long run, they could help improve the efficiency of capital markets and maintain an appropriate structure of exchange rates. In any event, it was noted that the measures were consistent with official intentions to liberalize domestic financial markets.

On a more general level, the authorities seemed to have adopted a significantly more positive attitude than in the past toward promoting the internationalization of the yen. They expect, however, that the international use of the yen as a transaction, investment and reserve currency will increase only gradually. Measures such as those recently adopted could facilitate internationalization, but the process could not be forced artificially. The authorities remain opposed to the imposition of controls on capital outflows as a yen defense measure as this was not believed to be consistent with the long-term objective of fostering the international attractiveness of the Tokyo capital market.

As part of the October measures, the Government announced its intention to seek enabling legislation for the issuance of foreign-currency-denominated government bonds abroad. The authorities indicated, however, that such issues would be unlikely under present conditions--in particular, the high level of interest rates in some foreign markets and the risk of crowding out in markets with lower interest rates. Nevertheless, during the past year the Government has encouraged the issue of foreign-currency-denominated government-guaranteed bonds abroad.

5. Commercial policy

Two sets of market opening measures, announced in May 1982 and January 1983, were implemented in April 1983. Together, these reduced the average tariff on dutiable imports from 7.7 percent to 4.5 percent, relaxed import quotas on a wide range of agricultural products, simplified import testing procedures and liberalized government procurement policies and trade in services. Further tariff reductions and steps to promote imports through concessional import financing were announced in October. These measures were expected to have some impact, particularly on imports of manufactured goods, but, because nearly two thirds of imports are energy products and raw materials with relatively inelastic demand, the effect on total imports was expected to be small.

The Japanese Government has met international crticism of the growing exports by acceding to an increasing number of requests for voluntary export restraints. It is estimated that about 40 percent of Japan's exports to the United States and the European Community are in categories subject to some sort of restraint. The authorities viewed these arrangements as the best means of supporting the free trade system when industries in trading partner countries suffer from structural problems. In such situations, import restrictions imposed by importing countries would tend to be more severe and to remain in effect for longer periods than voluntary restraints by exporting countries. It was important, however, in the view of the authorities, that export restraints be coupled with adjustment measures in the importing countries. The restraint agreements were not seen as permanent, and some had already been eliminated. The authorities were concerned about the recent increase in pressure for protection to nurture high-technology industries. Whereas protectionist measures in industrial countries have traditionally been based on the need to facilitate structural adjustments, the extension of protection to high-technology infant industries was believed to pose a serious threat to the future expansion of world trade which was expected to be concentrated in this area.

The authorities said that voluntary export arrangements had probably dampened domestic investment growth somewhat and increased direct investment abroad. There were no quantitative estimates of the impact of the agreements on export volume growth but there had probably been some depressing effect, particularly on exports of automobiles and video tape recorders. To some extent, especially for automobiles, these effects had been offset by the export of higher value-added items. The effects of the arrangements on the value of the yen were uncertain, though it was thought that the yen might have been somewhat stronger had the arrangements not been in effect.

The authorities believed that with the world recovery trade volume growth would pick up and tend to lessen protectionist pressures during the coming year. Nevertheless, in countries with weak recoveries and where structural adjustment has been slow, such pressures could remain strong. The Japanese Government has recently proposed a new round of multilateral trade negotiations.

IV. Staff Appraisal

Since the mid-1970s, Japan has proved highly capable of adjusting to disruptions in the world economy. External price increases have not been permitted to distort the domestic price and wage structure and the adaptation of industry to structural changes has proceeded rapidly. This performance reflects the timely and efficient response of policy to changing circumstances and the ability of the society to effect an acceptable apportionment of the adverse impact of external shocks among its various groups.

These fundamental strengths of the Japanese economy have contributed to higher growth and lower unemployment during recent years than in other industrial countries. The containment of domestic costs and prices and the ability of industry to respond to changes in the structure of demand have sustained and enhanced the strength of the Japanese economy in international trade, but the positive influence of these developments on domestic demand has been weaker than expected. As a result, there have been periods of weak domestic demand--such as in 1980, mid-1981 and again during early 1983--when growth has been sustained largely by trade performance.

Final private domestic demand declined in the first half of 1983 although the support provided by the public sector and an upturn in inventory accumulation led to a slight expansion of total domestic demand. Some of the weakness in the economy was due to temporary factors and their removal, along with the beneficial impact of the recent export expansion, produced a rebound in the growth of private domestic demand in the third quarter. While this rebound was broad-based, developments in some of the factors underlying the performance of private consumption and residential investment--in particular disposable income growth, the savings ratio and structural aspects of the housing market--remain uncertain. It is also disquieting that inventory accumulation has been rather slow. Nevertheless, industrial activity and the growth of exports remain strong, and a pickup in profits and business fixed investment has already commenced. If these trends persist, they should eventually translate into higher disposable income and consumption. Given these mixed signals, the staff is optimistic--but cautiously so--on the strength of the recovery of domestic demand expected during the next year.

The surge in the current account surplus during the last year is a result of a number of forces: lower energy prices; the strength of the recovery in foreign markets; weak conditions in the domestic economy which both slowed import growth and increased the incentive to export; and the weakening of the yen during much of 1982. More fundamentally, the underlying strength of the current account reflects an unusually high propensity to save as well as some enhancement in the attractiveness of foreign relative to domestic investment during the last decade. The current account surplus can be viewed as a ready source of savings for other countries; however, at this particular juncture, some of the factors behind the sharp increase in the surplus—the rapid increase in exports and, until recently, the slow increase in non-oil imports--pose problems for the rest of the world.

In light of these developments, and the authorities' own concern about their international repercussions, the major policy problem in the staff's view is how the authorities should set policies within the admittedly limited room for maneuver available so as to support the recovery of private domestic demand which seems to be emerging. This objective is desirable not only from a domestic perspective, but also from the standpoint of maximizing Japan's contribution to the world economy.

Nowhere is the nexus between conditions in the world economy and the stance of Japanese policies more clear than in the conduct of monetary policy. The authorities' desire to use monetary policy to help stimulate the domestic economy is understandable given the absence of inflationary expectations and high real interest rates. However, high interest rates abroad limit the scope for easing monetary policy without risking an unwanted depreciation of the yen. In view of this constraint, the authorities should continue to use monetary policy to support domestic activity only to the extent that this can be done without unduly weakening the yen.

The authorities' caution in this regard is reflected in their response to domestic pressures for a reduction in the official discount rate. This step was taken only when the risk of weakening the yen was considered to be minimal. It is reassuring, however, that despite this easing of monetary conditions, the yen has remained generally steady against the U.S. dollar and even appreciated against European currencies. This suggests that there may have been some strengthening of the influence of fundamental conditions on the value of the yen which, if sustained, could lessen the external constraint on monetary policy. In the more immediate context, however, the staff welcomes the authorities' commitment to take offsetting action, including on interest rates, should the yen again show persistent signs of weakening.

During 1983, the nominal effective value of the yen increased by almost 7 percent. The real effective value of the yen is also estimated to have increased though by somewhat less. Underlying these developments were quite different movements in the yen's value vis-a-vis other major currencies; in nominal terms, it strengthened substantially against major European currencies and maintained its value against the dollar. The persistently high level of the dollar against all currencies suggests that factors affecting the longer term position of the dollar itself may have strengthened. These conditions tend to reduce somewhat the extent to which the present level of the yen should be viewed as excessively weak. However, they do not contradict the position--shared by the authorities and the staff--that a strengthening of the yen, especially against the dollar, would be desirable to adjust trade flows and to support domestic growth through improved terms of trade.

With respect to fiscal policy, the staff understands the authorities' views on the problems posed by a continued high level of deficit spending. The inflexibility of fiscal policy induced by growing interest payments, the expected burden on the public sector arising from the projected aging of the population, and the public consensus in favor of a restoration of fiscal balance are indications of the need to reduce the deficit in the medium term. It also seems clear that there is strong political support for doing this through reductions in public spending. To the extent that scope exists for such reductions, the staff supports this aim, but the magnitude of the proposed adjustment would seem to suggest some role for tax policy as well in this effort once the recovery of domestic demand seems secure.

At the same time, the staff continues to welcome the flexibility demonstrated by the authorities in recent years in adapting fiscal policy to the situation of weaker-than-expected domestic demand. These adaptations have been particularly appropriate in view of the constraint imposed on monetary policy by the policy mix in other countries, the absence of inflationary expectations and general agreement that crowding out of private sector activity is not at present a problem. Under present circumstances, continued flexibility in fiscal policy would seem to be appropriate. In particular, in framing and initially implementing next year's budget, the options of again frontloading public works expenditures and delaying possible implementation of indirect or other tax increases to offset a personal income tax reduction should be kept open. This would give the authorities the option of moderating the withdrawal of fiscal support while the strength of the emerging recovery remains uncertain. Should the recovery eventually prove as robust as hoped, the planned withdrawal of stimulus would occur virtually automatically during the latter part of the year. In the staff's view, the risks of slowing somewhat the progress toward meeting the authorities' medium-term fiscal objectives are considerably less than those attached to a possible faltering of the recovery of the Japanese economy, especially given the importance of Japan in the world economy. Ensuring a strong and sustained recovery is also essential to eventual progress in reducing the deficit and to preventing a widening of the gap between domestic savings and investment--with attendant implications for trade flows--as such progress is realized.

There has been an increasing reliance on trade policy measures to mitigate international concerns about some of the forces behind Japan's growing current account surplus. Japan's steps during the last two years to further open its markets to foreign producers are commendable, especially in view of the intensification of protectionist measures in many of its trading partners. Further efforts to reduce impediments to trade would be welcome. The case for such progress is particularly compelling in the area of agriculture where, for some products, subsidies have produced large gaps between prices on the domestic and world markets. While the immediate effects of market opening measures may not appear to be large, the potential effects in terms of increasing imports and forestalling protectionist pressures abroad are important. The foreign pressures that have led to the extension and broadening of voluntary export restraint measures during the last year are disconcerting. These measures can be condoned only insofar as they provide an opportunity for undertaking structural adjustments in importing countries, and this opportunity is used quickly and efficiently. However, in many cases these measures will be difficult to dismantle and may well delay technological advance and structural adjustment in importing countries. It behoves Japan, as a major trading nation to adopt an active leadership role in encouraging multilateral discussions through GATT and other forums on rolling back protectionist measures and increasing trade flows. Its recent initiative in this connection is most welcome.

During the last several years, the virtually complete dismantling of formal restrictions in Japan's money and capital markets on the international movement of funds has contributed toward making Tokyo the second largest financial market in the world. Nevertheless, the authorities intend to examine ways in which an even more attractive array of assets can be made available to both foreign and domestic investors, to review tax laws and other regulations which may impede the inflow of capital and to encourage the internationalization of the yen. Together with efforts to keep financial regulations transparent and constancy in the direction of liberalization, such actions should help assure that the exchange rate fully reflects market forces. In most cases, however, the exchange rate effects of specific measures to broaden financial markets are unpredictable, at least in the short run. Therefore, such measures should be implemented as soon as other conditions permit, as part of the effort to improve the overall efficiency of Japan's financial markets, rather than with the specific intention of influencing the exchange rate.

It must be reiterated that the Japanese authorities have been confronted with difficult policy choices during the last year. Broadly speaking, the choices made have enhanced the performance of the Japanese economy and its role in the international economic system. Inflation remains low and although the recovery of domestic demand faltered during the first half of 1983, positive signs of a rebound in domestic growth have recently emerged. The growth of the current account surplus has aggravated protectionist pressures, but it has also been the source of Japan's substantial contribution of savings to the global economy. Finally, the authorities must be commended for their continued commitment to meeting their medium-term goal on financial assistance to developing countries, even though this implies a sharp acceleration of assistance over the next two years.

It is recommended that the next Article IV consultation with Japan be held on the standard 12-month cycle.

JAPAN

Basic Data

Population

Total population (June 1983) 119,190,000
GNP per capita (1983) 1/2/ US$9,811

	1981 (Percent Share)	1980	1981	1982	1983 2/
GNP		(In trillions of yen)			
At constant 1975 prices		189.8	197.3	202.9	210.3
At current prices		235.8	251.8	264.8	274.9
		(Percentage changes over previous year in constant prices)			
Private consumption	52.0	1.3	0.7	4.2	3.4
Private residential investment	5.5	-9.4	-2.5	-0.7	-5.2
Private equipment investment	17.2	8.0	5.6	3.5	1.7
Government consumption	9.5	2.9	5.2	2.3	2.3
Government investment	9.5	-3.2	3.9	-0.2	0.3
Stockbuilding 3/4/	0.6	-0.1	-0.2	0.1	-0.5
Total domestic demand	94.3	1.2	2.0	3.2	1.6
Foreign balance 3/	5.7	3.5	2.1	0.3	1.6
Real GNP	100.0	4.8	4.0	3.4	3.1
Nominal GNP	...	7.7	6.8	5.2	3.8

Prices, income and employment	(Percentage changes over previous year except where indicated)			
Wholesale prices	17.8	1.4	0.5	-0.7
Consumer prices	8.0	4.9	2.6	1.8
GNP deflator	2.8	2.7	1.7	0.7
Hourly compensation 5/	7.4	5.5	5.6	3.0
Real hourly compensation 5/6/	-0.5	0.5	2.8	1.4
Real disposable income 6/7/	-1.4	-1.0	3.0	1.0
Average propensity to consume (in percent) 7/	77.9	79.2	78.3	79.1
Unemployment (in percent)	2.0	2.2	2.4	2.7

Manufacturing				
Employment of regular workers	1.1	1.1	0.7	-0.1
Output	4.7	1.0	0.3	3.4
Productivity	3.7	--	0.1	3.0
Unit labor cost	3.6	5.5	5.5	--
Inventory ratio (in percent) 8/	100.0	104.9	105.3	98.9

Basic Data (concluded)

	1980	1981	1982	1983 2/
Financial aggregates	(Percentage changes over previous year)			
M2 9/	9.2	8.9	9.2	7.4
Domestic credit 10/	8.4	10.0	8.2	7.1
Public sector	9.1	13.0	5.2	3.0
Private sector	8.3	9.3	9.0	8.0
Fiscal Aggregates	(Fiscal year basis, in trillions of yen)			
Central Government				
Revenues 11/	28.9	31.4	33.2	35.2 11/
Expenditures	42.4	45.9	47.1	47.9 11/
Deficit (-)	-13.5	-14.5	-13.8	-12.7 11/
Deficit/GNP (in percent)	5.6	5.7	5.2	4.5 11/
Fiscal investment and loan program	18.1	19.4	20.6	20.7
General government				
Deficit/GNP (in percent)	-4.0	-3.7	...	...
Balance of payments	(In billions of U.S. dollars)			
Exports	126.7	149.5	137.7	145.7
Imports	-124.6	-129.5	-119.6	-114.0
Trade balance	2.1	20.0	18.1	31.7
Services and transfers	-12.9	-15.2	-11.2	-10.6
Current balance	-10.7	4.8	6.9	21.1
Net long-term capital 12/	2.3	-9.7	-15.0	-17.6
Japanese	-10.8	-22.8	-27.4	-30.9
Foreign	13.1	13.1	12.4	13.3
Basic balance	-8.4	-4.9	-8.1	3.5
Net short-term capital	13.2	9.1	3.2	-2.3
Nonbank 13/	--	2.7	3.2	2.2
Bank	13.1	6.4	--	-4.5
Overall balance	4.8	4.2	-4.9	1.2
Gross official reserves 14/	(At end of period, in billions of U.S. dollars)			
Total reserves	25.7	29.2	24.3	26.0
In months of imports of goods and services	1.8	1.9	1.7	2.7

1/ At an exchange rate of US$1 = ¥ 235.
2/ Staff estimates.
3/ Contribution to real GNP.
4/ Includes public and private.
5/ Regular employees in the manufacturing sector.
6/ Deflated by CPI.
7/ Workers' households.
8/ Index of the ratio of producers' inventory to shipment.
9/ Period average.
10/ End of period.
11/ Initial budget.
12/ Excluding Gensaki transactions.
13/ Including Gensaki transactions and errors and omissions.
14/ Including gold (national valuation).

Fund Relations with Japan
(As of December 31, 1983)

Quota:	SDR 4,223.3 million.
Fund holdings of Japanese yen:	SDR 2,863.4 million or 67.8 percent of quota.
SDR position:	Holdings are SDR 1,848.2 million or 207.3 percent of net cumulative allocation of SDR 891.7 million.
Gold distribution:	1,026,995.292 fine ounces.
Lending to the Fund:	
SFF:	The maximum commitment of Japan is SDR 900 million; net borrowing by the Fund as of December 31, 1983 was SDR 862.7 million.
GAB:	The maximum commitment of Japan is SDR 2,125 million. The Fund's indebtedness to the GAB presently is nil.
Exchange system:	Since February 12, 1973, the yen has been allowed to float. The exchange rate as of January 19, 1984 was ¥ 233.85 = US$1.
Last Article IV consultation:	March 18, 1983.