INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 93/100

10:00 a.m., July 16, 1993

M. Camdessus, Chairman

Executive Directors	Alternate Executive Directors
M. Al-Jasser	A. A. Al-Tuwaijri
T. C. Dawson	J. M. Abbott, Temporary
J. de Groote	
I. Fridriksson	
H. Fukui	N. Tabata
K. P. Geethakrishnan	
J. E. Ismael	K.-T. Hetrakul
	R. Ferrillo, Temporary
	J. C. Jaramillo
	G. Y. Glazkov, Temporary
G. Lanciotti	
J.-P. Landau	
R. Marino	
	O. Kabbaj
	B. S. Dlamini
D. Peretz	
G. A. Posthumus	
	Y.-M. T. Koissy
S. Schoenberg	B. Esdar
	Y. Y. Mohammed
D. E. Smee	
E. L. Waterman	A. M. Tetangco, Jr.
	Wei B.
	A. F. Jiménez de Lucio

L. Van Houtven, Secretary and Counsellor
S. L. Yeager, Assistant

<u>Also Present</u>

Central Asia Department: H. Neiss, Director, B. B. Aghevli, Deputy Director; U. Baumgartner, Y. Horiguchi, J. S. Kahkonen, H. L. Mendis, G. M. Meredith, K. M. Miranda, I. Otani, Y. Yokoyama. European I Department: P. R. Masson, H. Vittas. External Relations Department: G. Hacche, E. Ray. Fiscal Affairs Department: A. T. Mourmouras. Monetary and Exchange Affairs Department: W. E. Alexander. Policy Development and Review Department: J. T. Boorman, Director; M. Allen, N. Kirmani. Research Department: M. Goldstein, Deputy Director; T. A. Bayoumi, R. A. Feldman, S. M. Fries, F. Larsen, G. J. Schinasi. Secretary's Department: A. Leipold, A. Mountford. Treasurer's Department: M. A. Wattleworth. Western Hemisphere Department: S. T. Beza, Counsellor and Director. Office of the Managing Director: P. R. Narvekar, Special Advisor; G. R. Saunders, Personal Assistant. Advisors to Executive Directors: P. Bonzom, Hon C.-W., J. Jonas, S. K. Fayyad, W. Laux, Y.-H. Lee, M. F. Melhem, J. W. van der Kaaij, Yang X. Assistants to Executive Directors: H. M. Al-Atrash, J. H. Brits, Chen M., J. C. Estrella, H. Golriz, S. Ishida, T. Kanada, W. C. Keller, K. J. Langdon, G. J. Matthews, S. C. McDougall, J. K. Orleans-Lindsay, T. Oya, C. F. Pillath, R. K. W. Powell, N. Prasad, E. Quattrociocche, S. K. Regmi, S. Shimizu, A. Sighvatsson, J. B. Wire, Wu H.

1. JAPAN - 1993 ARTICLE IV CONSULTATION

The Executive Directors considered the staff report for the 1993 Article IV consultation with Japan (SM/93/132, 6/22/93; and Sup. 1, 7/12/93). They also had before them a background paper on recent economic developments in Japan (SM/93/142, 7/6/93; and Sup. 1, 7/8/93).

The Deputy Director of the Central Asia Department, updating the staff's assessment of the most recent developments in the Japanese economy, said that the latest data, including those on industrial production in May, and consumer spending in June, were in line with the staff's view of short-term growth prospects. The second quarter was likely to show somewhat weaker growth than the first, followed by mild recovery in the second half of the year.

On the external front, the latest monthly trade data showed a decline in the seasonally adjusted surplus, from a peak of about $11 billion in April to $9 billion in June, the Deputy Director remarked. While it was too early to call that a downward trend, the data belied the impression in some news reports, based on a comparison with previous year's data, that the surplus had continued to soar in recent months. Indeed, the most recent data would cause the staff to revise down moderately the current account surplus projected for 1993, from $147 billion to perhaps a range of $140-145 billion.

Year-on-year inflation, on a consumer price index basis, had fallen below 1 percent in the second quarter, consistent with weak market conditions and the effects of yen appreciation, the Deputy Director of the Central Asia Department stated.

Mr. Fukui made the following statement:

Japan's economy is showing increasing signs of recovery. Toward mid-1991, it entered into an adjustment phase and remained stagnant during the course of FY 1992. The real GNP growth rate in FY 1992 was 0.8 percent, mainly owing to the weakness in business fixed investment and private consumption. Since the beginning of the year, however, some indicators, such as mining and manufacturing production and shipments, started to show an upturn as inventory adjustment made progress. The economic stimulus package of August 1992 and the subsequent implementation of the supplementary budget, which took full effect at the turn of the year, played an important role. Furthermore, there have been positive signs of recovery in private consumption.

It took a relatively long time in this business cycle for the economy to pass through the consolidation process because of the need for a massive adjustment in capital stock, which had built up since 1987 during the course of economic expansion. The situation was aggravated by household and corporate balance sheet adjustments accompanied by a fall in asset prices. A strong adjustment effort by the private sector, along with a series of stimulative policy measures by the Government, have succeeded in putting the economy back on the track to recovery.

Real GNP growth for the third quarter of 1992 was minus 0.6 percent, followed by zero growth for the fourth quarter. But the recently announced estimate for the first quarter of 1993 was 0.6 percent--or 2.3 percent per annum--which shows that the economy has bottomed out. The diffusion index of main economic indicators had been more than 50 percent for three consecutive months beginning in February 1993.

Business fixed investment, which registered a modest increase of 2.7 percent in FY 1991, declined by 5.7 percent in FY 1992 because of a further adjustment in capital stock. Private consumption increased marginally, mainly owing to the lower rate of growth in disposable income and a declining propensity to consume. I would point out, however, that the sizable fall in asset prices did not significantly influence consumption because the liabilities of the household sector were not so large. Reflecting this weak trend in final demand, inventory adjustment was implemented throughout FY 1992.

With regard to the labor market, the unemployment rate remained low at 2.3 percent, in spite of the weak economic activity. This is due to the fact that the demand for employment was maintained by shortening the labor hours as well as to the existence of unfilled labor force positions that persisted from the previous expansionary stage.

The wholesale price index was negative--at minus 1.0 percent--and the consumer price index was as low as 1.6 percent in FY 1992. The main factors contributing to these favorable performances were sluggish domestic demand, a decline in import prices owing to the appreciation of the yen, and a modest increase in wages. This price performance is the best among the major industrial countries.

With regard to the external balance, the current account surplus increased from $90.2 billion in FY 1991 to $126.1 billion in FY 1992. On the export side, the increase is mainly due to price factors--owing to the appreciation of the yen--and a higher proportion of high value-added commodities, while the increase in quantity was only marginal--namely, the increases in export price and quantity were 7.2 percent and 0.1 percent, respectively. On the import side, the continuous economic consolidation and adjustment was a drag on the increase in imports. A substantial increase in the return on foreign investment also added to the expansion of the current account surplus. In contrast, the long-term capital account showed a $47.8 billion net outflow in FY 1992, which is a turnaround from the $39.8 billion net inflow of FY 1991.

The fiscal situation continues to be very severe; the outstanding long-term government debt/GNP ratio is 47 percent, and interest payments on government debt constitute 17 percent of total budget expenditures.

This difficult situation notwithstanding, the FY 1992 budget placed the utmost importance on an increase in public works in the general account, as well as under the Fiscal Investment and Loan Program (FILP), taking into account the sluggish economic activity. In addition, the Comprehensive Economic Measures announced last August, which featured additional public works and measures to stimulate business fixed investment as well as to promote the activities of small and medium-sized enterprises, amounted to ¥ 10.1 trillion--$87 billion--or 2.3 percent of GNP. Last December a supplementary budget was enacted to provide the legislative and budgetary means to implement this economic package. However, these measures resulted in a further increase of outstanding government debt to cover the shortfall in tax revenue, through the additional issuance of government bonds.

The official discount rate was cut by 2.0 percent following three consecutive reductions from April 1992 through February 1993 and now stands at its lowest level ever, at 2.5 percent. Accordingly, short- and long-term market interest rates and the lending rates of banks followed a declining trend, which helped support the recovery of economic activity. However, money supply was sluggish in spite of the decline in interest rates.

It seems that Japan's financial system, affected by the sharp fall in asset prices, had passed through its most difficult stage as of March 1993, and is on the way to regaining stability. Although it will take some time for the banks to clear their nonperforming loans, the stability of the Japanese financial system will no longer be at stake.

In view of the sharp decline in stock and real estate prices, the authorities stood firmly behind the stability of the system and in August 1992 announced the Guidelines on Monetary Administration, which promoted an increase in the capital of banks as well as the liquidation of bad loans and collateralized real estate with the objective of stabilizing the financial system and making it more cost effective. These policies were implemented promptly.

In January 1993, a group of commercial banks established the Cooperative Credit Purchasing Company for the purpose of promoting the liquidation of loans collateralized by real estate. The corporation has purchased ¥ 680 billion of loans as of end-March 1993. This corporation is not intended to buy out the entire stock of nonperforming loans of banks but to provide a guide for real estate transactions in terms of assessment and price, which will be conducive to normalizing and activating the market. This purpose has been successfully met.

It was announced that as of end-March 1993, the total amount of nonperforming loans--namely, loans with interest arrears of more than six months and loans to insolvent clients--was ¥ 12.7 trillion. Compared with the amount at end-September 1992--¥ 12.3 trillion--this shows a slight increase, indicating a leveling off of nonperforming assets of the main banks--City Bank, Long-Term Credit Bank, and Trust Bank. The Bank for International Settlement's (BIS) capital adequacy ratio of 8 percent, which was one of the issues at last year's Board discussion on Japan, was cleared by the banks under the regulation by significant margins--9.2 percent on average--at the end of March 1993.

As to the outlook for FY 1993, the economy is now on a recovery path, as evidenced by the signs of an upturn in private consumption, a steady increase in public investment, and the near completion of inventory adjustment. The policy stance of the FY 1993 budget enacted in early April was stimulative, and soon after its enactment the New Comprehensive Economic Measures, amounting to ¥ 13.2 trillion--$120 billion--were announced, and the necessary legislative and budgetary measures were put in force by the supplementary budget that was passed by the Diet in early June.

There are still some uncertainties, particularly related to the upward trend of the yen. As the consecutive measures of the two sizable policy packages will surely have favorable and continuous effects, it is expected that the economy will be firmly on a sustainable growth path from the latter half of FY 1993, mainly driven by domestic demand. With the expected recovery of the economy, the current account surplus will become smaller. In fact, our imports are increasingly relying on manufactured goods because of the policy orientation of import expansion. As a result, import elasticity against income growth has increased significantly, to 1.6 in 1986-92 from about 0.5 in 1986. The basic trend of a strong yen will also be instrumental in this regard. The wholesale price index will continue to be flat, and the consumer price index will show a marginal increase owing to lax domestic demand and the dampening effect of the appreciation of the yen.

As to fiscal policy, the FY 1993 budget set as its main policy target getting the economy back on a strong recovery path, relying mainly on domestic demand, while managing the ever-difficult fiscal situation. Thus public works expenditure is increasing by 5.8 percent, compared with 4.5 percent in FY 1992, mainly for road and housing construction. The FILP is expanding by 12.4 percent, compared with 10.8 percent in FY 1992, mainly for the construction of highways and houses. Public investment by local governments is expanding by 12.0 percent, compared with 11.5 percent in FY 1992. These rates of increase in the FILP and the public expenditure of local governments are the highest in recent years. Consideration was also given to supporting small and medium-sized enterprises and to securing employment.

Social security expenditure, which constitutes 33 percent of general expenditure and is mainly for assistance to the aged, is another feature of the budget. Expenditure for economic cooperation--for instance, official development assistance (ODA)--increased by 6.5 percent, a proportionally greater increase than for total expenditure, to promote Japan's contribution to the international community.

The New Comprehensive Economic Measures of ¥ 13.2 trillion--or $120 billion--announced this April is the biggest package ever and features the expansion of public expenditure, the promotion of housing and business fixed investment, and support for small and medium-sized businesses. Its stimulative impact is estimated to be about 2.6 percent of GNP in nominal terms, calculated on the basis of the public investment multiplier of "World Economic Model IV," which incorporates various characteristics of the Japanese economy, after deducting land acquisition and working capital from the total amount.

Often the process of decision making and implementation of fiscal policy is delayed because of, for instance, the political situation. It can be said, however, that the series of actions entailed by the two economic policy packages, the two supplementary budgets, and the FY 1993 budget over the relatively short period between August 1992 and June 1993 indicate a relatively smooth and timely enactment of fiscal policy, minimizing unavoidable time lags.

The budgetary situation continues to be extremely difficult in that government long-term debt reached ¥ 184 trillion--$1.7 trillion--or 47.4 percent of GNP, and interest payments constitute 15.9 percent of total budget expenditures. These indicators of the debt burden are the worst among the major industrial countries. The budgetary situation remains under such heavy pressure from structural constraints that the burden of debt-redemption and debt-servicing expenditures is squeezing out other important expenditures.

As is often mentioned, Japanese society is aging rapidly, at a faster pace than ever before. The proportion of the population over 65 will be the highest among the major industrial countries by the year 2,000, whereas in 1991 it was the lowest among them.

Our fiscal policy aims at adapting to the highly aged society while maintaining sustainable growth without inflation. The fulfillment of Japan's increasing responsibilities toward the international community is also an important policy objective. For this purpose, we are firmly committed to reducing as much as possible the government deficit, thus containing the increase in outstanding debt.

Along these lines, we have set a policy target on a medium-term basis to arrest the growth of outstanding debt and to level it off thereafter. This target is certainly a moderate one in view of the huge amount of debt accumulated to date. The additional fiscal burden caused by the two economic stimulus packages mentioned above eventually added to the Government's outstanding debt and made it more difficult to achieve this medium-term policy target, requiring even more severe controls over the budget in the medium term. The economic stimulus packages that were implemented aimed at striking a balance between this difficult fiscal situation and the necessary budgetary stimulus to the economy.

On a "general government" basis, the fiscal account shows a surplus of 3.5 percent of GNP in FY 1992, only because the surplus of social security funds--3.8 percent of GNP--offsets the deficits of the central and local governments--amounting to 0.2 percent of GNP and 0.1 percent of GNP, respectively. The social security fund consists of deposits by participants and is meant to be used for future pension payments to those participants. It cannot be appropriated for financing the government deficit or interest payments. Thus, this fund should be considered a "liability" of the Government. As is clearly stated in the staff report, the financial situation of the social security fund will soon deteriorate as society ages. We take the position, therefore, that the concept of "general government," which aggregates central and local governments and the social security fund, is not appropriate and is a misleading measure of the fiscal situation. We welcome the fact that the staff report now takes account of this point, which our authorities have made repeatedly. Likewise, central government outstanding debt should not be offset by social security fund assets, since this distorts very heavy debt burden of the Central Government. We also have difficulty with the concept of "general government deficit after cyclical adjustment."

I would like to point out that the social security fund is utilized for capital formation through the FILP.

On monetary policy, the official discount rate is now 2.5 percent. Market interest rates responded smoothly, and the lending rate of banks remains at a historically low level. The easing of the monetary situation was beneficial for corporate profits and helped promote inventory adjustment and the restructuring of corporate debt.

The monetary aggregate continues to be stagnant owing to sluggish money demand. The growth of M2 + CD was negative during the period September 1992 through March 1993 for the first time. This is attributable to the sharp decline in asset prices after the bursting of the "bubble." Money supply, however, apparently hit bottom and turned positive--reaching 0.5 percent in April 1993 and 1.5 percent in May 1993; it is expected to show a gradual increase as the economy recovers in the latter half of the fiscal year. In view of the large impact of asset price fluctuations on the real economy, the Bank of Japan will pay close attention to the trend of asset prices.

It will be some time before banks can clear their nonperforming assets. The banks are expected to gradually dispose of these assets through their own efforts in line with their own programs. And, it is not our policy for official funds to be involved. In some cases, smaller banks with bad assets have successfully merged with other banks, thus avoiding adverse effects on the financial system in general. Developments so far indicate that the problem of nonperforming assets will not undermine the stability of the banks' management or the financial system as a whole.

With regard to the banks' nonperforming assets, there may be some question whether the official figure--¥ 12.7 trillion at the end of FY 1993--reflects the actual figure. Since a rough estimate of nonperforming assets using different criteria cannot help but rely on ambiguous assumptions, great care should be taken to avoid provoking an unnecessary reaction by the markets.

At this juncture, the following clarification is in order. A Working Group for the Adequate Disclosure of Banks' Assets was established under the Monetary System Research Council in January 1992. The Group studied intensively for about one year the standards for adequate disclosure of banks' assets compared with those of other major industrial countries, and submitted its report and recommendations for adequate standards to the Government in December 1992. Banks would have to disclose their nonperforming assets according to these standards. It is natural that standards should vary among countries, because the history of financial systems and the concept of systemic stability differ in each country. The nonperforming assets of the major 21 banks and local banks as of end-March 1993 were disclosed in accordance with these new standards.

Local banks are required to disclose only bad loans to insolvent companies, which amounted to ¥ 569 billion, or 0.29 percent of their total assets. This is less than for major banks--namely, 0.33 percent. In addition, their total operational profits in FY 1992 increased by 12.6 percent because of a widening of margins, and current profits moved into surplus for the first time in four years. The burden of nonperforming loans on local banks is possibly less than on major banks because land prices fluctuated less in rural areas than in the large cities.

As to troubled finance companies, banks and insurance companies have worked out supporting plans, and rehabilitation has proceeded according to these plans.

The stock market regained its upward momentum and has averaged around ¥ 20,000 since March 1993--an increase of about 35 percent over last year's low--reflecting signs of economic recovery. Corporate profits are expected to increase, which will further underpin stock prices and push them up further.

With respect to foreign exchange and balance of payments, the yen has appreciated substantially and, as of mid-July, the exchange rate is approximately ¥ 108 per US$1. This represents about a 15 percent appreciation since the beginning of the year. It is cause for concern that this rapid movement of the yen will be an additional burden on the economy in the early stages of recovery.

With regard to the current account surplus, as was noted during the Board's April discussion on the world economic outlook (EBM/93/51 and EBM/93/52, 4/12/93), the quantitative increase in exports is marginal--0.1 percent in FY 1992--and the 7.2 percent price increase in FY 1992 resulting from the shift to high value-added commodities was a major factor behind the 7.4 percent expansion in nominal terms in FY 1992. The decline in imports was mainly due to the sluggish economic situation, which is cyclical; the substantial drop in demand for luxury commodities in the wake of the bursting of the "bubble" was also a contributing factor.

As was pointed out at the world economic outlook discussion, there certainly exist "nonprice" factors in exports. Japanese machinery and parts are used and incorporated in the commodities of trade partners--a vertical production relationship with other countries--and there is a strong demand for them from abroad. Direct investment by Japan, which was significant over the past several years, needs to be accompanied by strong exports of parts, which have a strong comparative advantage.

In our view, the effect of the short-term stimulative economic policy on the trade surplus will be limited in its impact and duration. Although we agree that the fiscal stimulus taken so far is appropriate, and will be effective in reducing the cyclical part of the trade surplus, we doubt the prudence of a policy stance that would put too much emphasis on using fiscal policy to tackle the surplus.

The current account surplus is expected to continue in the medium term, providing valuable savings in the context of the recent worldwide trend of dissaving and contributing to the development of the world economy through the expansion of capital flows, particularly of direct investment. Due note should be taken of the fact that Japan's direct foreign investment is creating new jobs in recipient countries, mainly in the manufacturing sector.

During 1987-92, imports from major trading partners increased by 62 percent, while exports to those countries increased by 49 percent. For example, on a per capita basis, imports from the United States and the European Community exceeded their imports from Japan. This means that Japan has been playing a major role in the expansion of world trade. In this light, the approach of managed trade on a bilateral basis to reduce the trade surplus runs counter to the cause of free trade, which is the fundamental policy stance of the Fund. We agree with the statement in the recent report on the world economic outlook that "the elevation of bilateral trade balances to the status of policy goals is misguided."

As to structural issues, structural reform is being actively pursued as a basis for freer competition. Interest rates on six-month term deposits were liberalized this June. The liberalization of interest rates on liquid deposits, except for checking accounts, is scheduled to be completed in 1994. The schedule of financial liberalization was announced earlier, and its implementation will not be affected by the recent change in the profit structure of financial institutions owing to the sharp fall in asset prices.

A new financial instrument has been introduced in money markets to meet the different needs of market participants. In the capital markets, the criteria for the registration of corporate debentures and the issuance of foreign bonds have been eased.

The Financial System Reform Act, enacted in April 1993, constitutes a major systemic change, permitting the intersection of business between banks and securities companies. Revised legislation controlling finance companies was enacted in November 1992 to upgrade the guidance and supervision of nonbanks. The Committee for the Supervision of Securities Transactions, which aims at securing transparency in securities transactions, has started to function.

External economic cooperation has expanded significantly in the form of official development assistance, subscriptions to the international financial institutions, and, recently, assistance to the former centrally planned economies in transition. Official development assistance in 1992 reached $11.3 billion, which makes Japan the largest donor country in the world for two consecutive years. The target of doubling ODA under the fourth medium-term program was fulfilled, with the provision of a total of $49.7 billion over the period 1988-92.

In the FY 1993 budget, expenditure for economic cooperation has been increased by 6.5 percent, exceeding the rate of increase of general government expenditure. The authorities have embarked on the fifth medium-term plan, increasing the amount of ODA to be provided during the coming five years to $70-75 billion. Also, the "Plan to Increase Financial Cooperation to Developing Countries," launched in June, will incorporate the above-mentioned ODA, untied loans from the Japan Export-Import Bank, and trade insurance. This assistance will facilitate capital flows to developing countries totaling about $120 billion. It should be mentioned that our economic cooperation is based on a policy that takes into consideration the level of military expenditure, the promotion of democratic societies, efforts toward market-oriented economies, and environmental conservation.

Japan has been actively supporting the Fund through various contributions--through the ESAF, parallel lending, the Technical Assistance Fund, and the Arrears Fund. In the 1993 budget, appropriations for the Japanese Technical Assistance Fund were increased by 16 percent, and the Japan-IMF Scholarship Fund for Asia was established so that graduate students from Asian countries and countries undertaking economic transition, including the states of the former Soviet Union, could study at Japanese universities.

Regarding the ESAF successor, Japan will participate actively in its funding on the basis of a renewal of the present Trust Fund arrangement, provided that other countries also contribute to this facility.

Mr. Dawson made the following statement:

Once again this year this chair has fundamental differences of view with respect to key elements of the staff's analysis of economic developments in Japan as well as its specific policy recommendations. We believe that the staff projections for economic recovery in 1993 and 1994 are far too optimistic. We believe that the current account surplus will not adjust as much as the staff projects and that this is a far more serious problem than the staff acknowledges. And, we believe that the misdirected preoccupation with fiscal consolidation, which the staff and the Japanese authorities share, is likely to frustrate the saving and investment adjustments needed to re-establish internal and external balance.

More fundamentally, my authorities have instructed me to convey their basic dissatisfaction with the orientation of these consultations with Japan. Nowhere is there the focus on international economic cooperation that ought to be at the heart of Fund surveillance of major industrial countries.

The recent Tokyo Summit of the Group of Seven (G-7) concluded with a declaration that had the subheading "A Strengthened Commitment to Jobs and Growth." Jobs and growth--these are the goals that G-7 heads of state see as central to their collaboration. In the consultation report on Japan, neither jobs nor growth have any particular priority. The Tokyo Summit Declaration states that "we will consult closely so that our national policies can be mutually reinforcing and compatible with our shared goal of a strengthened and recovering world economy." This is what my authorities believe Fund surveillance of major countries ought to be about. The international ramifications of Japan's economic policies and performance are largely missing from this Article IV review. The Summit communiqué refers to the contribution strong domestic demand-led growth can make "to the important goal of significantly reducing [Japan's] external imbalances." The staff report minimizes the importance of the goal of reducing Japan's current account surplus.

The United States and Japan have recently reached an understanding on a Framework for a New Economic Partnership. In the same spirit of international cooperation as the G-7 communiqué, this understanding is "firmly rooted in the shared interest and responsibility of the United States and Japan to promote global growth, open markets, and a vital world trading system." The framework statement says that:

> Japan will actively pursue the medium-term objectives of promoting strong and sustainable domestic demand-led growth and increasing the market access of competitive

> foreign goods and services, intended to achieve over the medium term a highly significant decrease in its current account surplus, and at promoting a significant increase in global imports of goods and services, including from the United States. In this context, Japan will take measures including fiscal and monetary measures as necessary, to realize these objectives.

These are the goals and policies that my authorities believe ought to be central to the Fund's surveillance of Japan. In this report, they are not. The advice provided does nothing to further the objectives of international cooperation.

In our view, the major contribution that Japan can make to its own economic well-being and to that of the international community is to achieve the strong noninflationary economic growth centered on an expansion of domestic demand and open domestic markets referred to in the Summit communiqué and the Framework Statement. Such a process would not only expand the prosperity of the Japanese, but it would also provide growing market opportunities for the rest of the world. Reduced Japanese current account deficits are absolutely essential, as lopsided trade patterns, where exports are 70 percent larger than imports, frustrate Japan's trading partners, who in a demand-short world, would prefer to earn their own way rather than borrow to buy the goods that Japan has to sell. Weak trade opportunities in Japan not only chill activity in trading partners, they also feed protectionist tendencies. These objectives will not be achieved unless economic activity gets more consistent support from public policy.

The growth scenario spelled out in the staff report would make the Economic Counsellor's old friend from the mid-1980s, "Rosy Scenario," blush with shame. This modern Rosy does not show much today but promises great things to come. For 1993 the staff marches with the consensus, expecting GDP growth and domestic demand to creep forward in step at around 1.0 percent, with the current account racking up a record surplus of $147 billion. But next year domestic demand accelerates to 4.9 percent, carrying GDP up 3.0 percent and cutting the current account surplus by three quarters of a percent of GDP to $127 billion.

We cannot see the basis for expectations of such strong growth in domestic demand. The Organization for Economic Cooperation and Development (OECD) thinks growth next year can recover to 3.1 percent, but it expects domestic demand growth of only 3.4 percent. My Treasury authorities see both growth and domestic demand rising by 2.5 percent next year, while my Federal

Reserve authorities, who arguably view the world with more detachment, cannot see domestic demand next year rising more than 2.1 percent, which only gets growth up to 2.0 percent.

Looked at in detail, the staff forecast appears implausible. Consumption is projected to accelerate from an increase of 1.7 percent this year to 5.3 percent next year. This would raise consumption to the levels achieved during the bubble boom. The income growth needed to support such a consumption bubble is not in evidence. Job growth has slowed, and overtime and bonuses have been curtailed. Productivity has slipped, and unit labor costs have jumped, putting a cloud over job security as well as prospective earnings growth. Wealth effects prompted by a forced rebound in stock prices are supposed to help. This seems like a pretty weak reed to count on to coax out the consumer spending that is built into the staff forecast.

A surge in residential investment of 9.6 percent is also forecast. Housing is improving, but we do not see it developing that much momentum. Plant and equipment investment, which the staff sees springing back at 5.7 percent, is even more dubious. Excess capacity is widespread, profits are poor for the third consecutive year, bank lending is slow, and each revision of business intentions surveys shows successive markdowns in planned business investment.

As the private side is seen to recover so nicely, a sudden deceleration of government expenditure, which seems to be the authorities' current intention, does no harm to the expansion of domestic demand that the staff anticipates. In its forecast, growth in government expenditure drops to 0.9 percent in 1994 from rates of 6.7 percent in 1992 and 8.3 percent in 1993. All this fine, robust, domestic, private sector-led growth allows the economy to gather steam even though the external accounts are adjusting to such an extent they exert a drag on the expansion equivalent to 1.8 percent of GDP. The current account surplus slides back to $127 billion.

As the saying goes: "In your dreams." Yes, this is just the sort of adjustment we would be delighted to see. But what the staff has presented is a scenario, not a plausible expectation of the way the Japanese economy is likely to evolve on the basis of current trends and policies.

The most recent trends do not seem to be going according to the "Rosy Scenario" script. Much of the first quarter advance has been lost in the second quarter. Industrial production, which increased by 1.5 percent in February and 2.5 percent in March, fell by 2.5 percent in April and by 2.4 percent in May. The revival of household expenditure, especially on automobiles and consumer durables, which supported revived activity in the first quarter, has fallen away in the second quarter. New car registrations were down 11.2 percent in April and fell another 10.2 percent in May. Retail sales were down 4.0 percent in April.

The staff says this "correction" has not prompted any significant revision of its forecast, but it does seem to have induced some needed pragmatism into the staff's policy assessment. The July 12 supplementary paper has some entirely sensible comments about the need for fiscal and monetary policy to continue to support activity so that the recovery can gain momentum. There is a hint that budgetary policy should be careful not to withdraw fiscal support prematurely. On monetary policy, the staff now comes as close as it ever does to suggesting that easing may be in order.

The staff makes an issue of the proposition that "Japan's current account behaves in a standard fashion, responding to changes in relative prices and in demand in Japan and partner countries, obviating the need to resort to nonconventional factors to explain its recent developments." We have no trouble with that proposition. The experience of the late-1980s and the 1979-80 period provided good test cases to demonstrate that a sufficient boost to domestic demand coupled with sufficient currency appreciation can turn around a current account surplus. Absorption and expenditure switching work in Japan just as they do in the textbooks. That is why we have advocated policies to boost domestic demand combined with accommodating exchange rate changes to correct Japan's current external surplus.

But the same textbooks teach us that market clearing is not synonymous with an economic optimum. Market distortions and their resultant welfare losses do not go away just because a balance is struck in the current account. In our view, it is no accident that the most recent world economic outlook report shows that, of all the industrial countries, Japan's economic size shrinks the most when calculated on the basis of purchasing power weights rather than market exchange rates. On purchasing power weights, Japan's GDP shrinks by about one half. Market exchange rates overvalue Japanese output precisely because exchange rate adjustments have been used so heavily in the last two decades to help correct recurrent current account surpluses. Current account adjustment would not have required such large adjustments in the value of the yen if the Japanese economy had not been so import resistent.

As Larry Summers put it in his speech to the Keidanren a few weeks ago, Japan presents two enduring problems to the United States and to the rest of the world: an imbalance problem and a penetration problem.

We think the staff largely misses the point, when on page 7, on page 16, and again on page 21 of its report, it lets itself get drawn into tut-tuting about the bogeyman of managed trade, as though sinister forces were menacing this paragon of liberal trade. I think that we could save ourselves a great deal of trouble if we refrained from tilting at this windmill. The U.S.-Japan Framework for a New Economic Partnership, which was agreed on July 10, most emphatically does not impose a managed trade approach. It is designed to introduce more market discipline in trade with Japan. Our negotiations will concentrate on sectors or structural areas where there already is a large presence of the Japanese Government. The objective is not managing trade, but unmanaging trade by opening up markets.

On page 20 of its report, the staff says "the main issue for fiscal policy in FY 1994 is the degree to which the consolidation effort should resume." We totally disagree. Fiscal consolidation in Japan ought to be a fourth order consideration. Staff calculations reported on page 36 of the background paper show that, notwithstanding recent stimulus packages, and notwithstanding expected increases in pensions and medical care, on current trends, between now and the year 2000, the Government will shift from a small net debtor position equivalent to 4.0 percent of GDP in 1992 to a small net creditor position equivalent to 2.0 percent of GDP.

As we stressed at last year's consultation discussion, we see no economic justification whatsoever for the Japanese Government to put itself in the position of becoming a net lender to the rest of the economy. The test of whether Japan will be able to provide well or poorly for its aging population will be whether the economy has the real resources to sustain evolving living standards when there are fewer workers and more dependents. There can be no economic presumption that this long-run objective is advanced by the extra tax effort and spending restraint needed to extract resources from the private sector just to acquire low-yielding financial claims. Bringing Japanese infrastructure levels up to par with those of other major industrial countries would certainly be a more productive use of these resources. Letting Japanese citizens keep a little more of their hard-earned income would also be an option worth considering.

We find the strategy of piling up financial claims in the Trust Fund Bureau even more dubious when it leads to activities like the "price keeping operation." In Kasumigaseki this seems to be thought of as "skillful management." In other countries, it would call into question whether the public trustees are fulfilling their fiduciary responsibilities.

Rather than worrying about a little more or a little less fiscal consolidation, the main issue for fiscal policy for FY 1994 ought to be sustaining the nascent recovery. The projections for 1994 presented in Table 1 of the staff report show the structural deficit being reduced by a full percentage point of GDP and the government sector surplus improving by 0.7 percent of GDP. Given what we see as the likely trend of activity, this looks like an unnecessary and premature withdrawal of fiscal support for economic recovery.

The section of the background paper on external demand and savings-investment balances recounts clearly the sort of rebalancing of savings and investment that took place during the late 1980s and led to the substantial correction of the external surplus. Public sector savings increased considerably. Private sector saving edged down a little. But private investment boomed, so much so that the net savings/investment surplus contracted and, with that, the external surplus also declined. The standard adjustment pattern prevailed.

The unusual feature of this period of current account correction, however, was that gross national saving was rising because of the fiscal consolidation zeal of the Government. To overcome this and still get external adjustment, a boom in investment was required. This boom was achieved through an overly easy monetary policy. The economy responded according to standard textbook expectations, but the highly unbalanced policy that was followed was unsustainable.

As we again look for a rebalancing of savings and investment that would establish noninflationary growth and a shrinking external surplus, the experience of the 1980s should be kept in mind. We should not expect a force-fed private sector investment boom to absorb an artificially stimulated excess supply of savings. A better savings/investment balance is needed in the public sector. With this large economy now saving more than one third of its national income, there is ample room for accommodation on the side of either public saving or public investment. More stress on public sector finances and reduced reliance on monetary policy to achieve the needed rebalancing of savings and investment would have the added advantage of minimizing the impact of adjustment on the exchange rate.

The supplementary paper provides over 50 pages of discussion on the asset price bubble and the role that monetary policy played. The discussion of the asset bubble is detailed and informative. I am not, however, sure what to make of the final chapter on "The Post-Bubble Slowdown in Broad Money Growth in Japan." The burden of this chapter seems to be that the asset bubble, mixed with financial deregulation effects, has shifted the demand for money function in ways that make the monetary aggregates misleading indicators of either the stance of monetary policy or of the direction of the economy. This is disappointing news, as a superficial scan of the data suggests that when the monetary aggregates consistently expanded at low double-digit rates in the late 1980s, asset prices soared and the economy bounded forward. It also appears that when monetary growth melted away to zero after 1989, asset prices collapsed and the economy tanked.

The staff analysis tries to draw us away from any simple-minded conclusion that exaggerated money supply growth caused the recent ups and downs in the Japanese economy. Instead, it stresses the extent to which the causality ran the other way, from asset prices and activity to money demand. I will reserve judgment on this issue until I understand the analysis better. Nevertheless, I suspect that the staff lets monetary policy off the hook too easily. The real side may have been amplifying swings in the demand for money, but the authorities could have done a much better job of resisting rather than accommodating those money demand swings, both on the upside and the downside.

The monetary base usually does not get much attention in discussions of Japanese monetary policy, but this series indicates the authorities have been allowing high-powered money growth to shrivel. Statistics on the base, defined as currency plus bank reserves, have been compiled by Salomon Brothers. They show that the year-on-year growth rate of the base tumbled steadily after the first quarter of 1990, when it had been growing at a 12.2 percent rate. In each of the four quarters from October-December 1991 to July-September 1992 the base declined at annual rates of between 3 percent and 4 percent. Even with lower official interest rates more recently, the base is still only expanding by 1-2 percent.

One aspect of recent monetary experience seems to cry out for closer analysis, namely, the role of deposit transfers to the Post Office. The table on page 43 of the background paper shows M2 + CD growth withering from 11.7 percent in 1990 to 3.6 percent in 1991, to 0.6 percent in 1992, and just into the negative zone in the first quarter of 1993. If M3 is tracked, it shows somewhat steadier growth in the last three years, of 7.1 percent, 5.3 percent, and 3.4 percent, respectively, and 3.9 percent in the first quarter of 1993. The difference is entirely due to postal savings, which are included in M3 but not in M2 + CD. The growth in postal savings rose from 3.4 percent in 1990 to 7.0 percent in 1991, to 12.3 percent in 1992, and has been running at 9.2 percent rate recently.

The numbers look like a low-grade run out of banks and into the Post Office. From the banks' point of view, this was translated into a curtailment of lending. After the boom of the late 1980s, bank lending grew only 5.1 percent in 1990, then slipped to 3.3 percent in 1991, and to 2.5 percent in 1992. While loan growth slowed, the loan/deposit ratio rose from 100 percent in 1990 to 114 percent last year. I would note that this seems to be the opposite of the behavior of banks in the United States during the so-called "credit crunch," when American banks ran down their loans and vastly expanded their securities investments.

While Japanese banks were struggling to maintain lending as deposits slipped, the Post Office had the opposite problem. While it had a surplus of funds, it did not have the same outlets to place these funds as the banks did. As we understand it, the first outlet for excess Post Office deposits are government securities, acquired through the Trust Fund Bureau.

While there is no doubt that broad liquidity was slowing down across the board over the last three years, the shifting of deposits out of banks and into the Post Office introduced an additional distortion into the normal flow of credit. Relatively less was available to bank customers--namely, to the private sector--and relatively more credit was available to the Post Office customers, namely, the public sector.

Looked at in this light, the much-discussed economic stimulus program, which is generally treated as a fiscal package, has a number of monetary dimensions. To get the liquidity bottling up in the Post Office back into the economy, the Government had to generate real projects that the Post Office could fund through the Fiscal Investment Loan Program.

This episode demonstrates the need for the Japanese authorities to finally come to grips with the anachronistic financial practices of the Post Office. It is hard to find any justification for allowing distortions such as those that have emerged in the last few years to persist. Unfortunately, the authorities seem to think market desegmentation is the problem, not the solution. On page 14 of SM/93/132, the staff reports that the authorities indicated financial system liberalization may be slowed down "in order to avoid increasing the current strains." We would encourage the authorities to reconsider this approach.

Mr. Landau made the following statement:

Japan's economic situation remains highly uncertain. Since the beginning of 1993, some indicators have registered positive trends. But other indicators reported in the most recent supplementary paper--such as industrial production, shipments and sales, or unemployment--show somewhat less favorable, or more erratic, trends. Those negative factors point to the substantial downside risks in the forecasts for 1993 and even, as mentioned by Mr. Dawson, in some of the projections for 1994. I thus agree with the staff that Japan's economy has "yet to turn the corner fully" and that the "current momentum has been weak so far." In addition, the international community is increasingly concerned by Japan's persistently high external surpluses.

In such a context, the authorities are confronted with two major issues: how to ensure a strong and sustainable recovery and how best to address the concerns of economic partners about Japan's external accounts. I would like to discuss those two issues in turn, without underestimating their obvious interactions.

As to facilitating a strong and sustainable recovery, there are lessons to draw from the bubble, especially as regards monetary policy. The staff rightly points out that the recent slowdown in activity was mainly due to a series of corrections following the unsustainable boom of the late-1980s. Many factors intervened in the process that led to the tripling of stock prices and the doubling of land prices. Fundamentals--and, most notably, the easy stance of monetary policy--played their role. Speculative behavior, especially but not exclusively in the financial sector, worsened the situation and produced consequences that current economic policies have yet to cope with.

The assessment is not made any easier by the uncertainty that continues to surround the financial sector and that played a key role in past difficulties. Guidelines have now been issued, and steps have been taken by the authorities in this area. I note that the steps taken by the financial industry include, inter alia, enhanced possibilities for the accelerated write-off of bad loans.

In any event, both the experience of the 1980s and the current juncture point to the limits of monetary policy as a way to stimulate growth in Japan. Indeed, and as clearly demonstrated in Chapter 3 of the supplementary paper, nontraditional determinants--such as asset prices and intermediation spreads--have played a major role in the slowdown of monetary aggregates and have thus contributed to reducing the quality of the signals conveyed by monetary data.

Past experience and, especially, the lessons to be drawn from the negative effects of an overly easy stance of monetary policy, certainly justify the authorities' caution regarding a further reduction in interest rates. Those rates are already at all-time lows. Moreover, we cannot concur in this regard with the, at least, implicit recommendation of the staff that Japan try to stimulate external demand through monetary rather than fiscal instruments. In addition, a further reduction could directly contradict the efforts currently being made to tackle the second issue that I have mentioned--the excessive external surplus.

In such circumstances, it was perfectly justified to consider favorably using the relatively large room for maneuver that is available in the fiscal area. The authorities have reached this conclusion progressively. The staff came even more slowly to this view. There is no denying the difficulty of the assessment that both the authorities and the staff had to make in the early 1990s, in view of the idiosyncracies of the post-bubble situation. It remains, however, that we have, as an institution, a record of constantly underestimating the need for fiscal stimulus in Japan.

In its 1990 report, for instance, the staff considered that "fiscal policy should, as a minimum, not impart any additional expansionary impulse to the economy" and that "fiscal policy may well have to be more restrictive." In 1991, the staff, after having found that "the concern should still be more with inflation than with the risks of an excessive slowing of economic growth," mentioned that "continued fiscal consolidation seems appropriate." And, even as late as mid-1992, the staff had a number of reservations about any additional stimulus.

Fortunately, in 1992 and again in 1993, the authorities have taken helpful and--recently--substantial fiscal measures. I note from the staff papers that, if the Nikkei index is any guide, those packages have been especially well received by the markets.

On recent fiscal developments, I have three comments. First, the emphasis now being put on public investments, such as roads and housing, is fully justified. Those are indeed areas in which fiscal policy is relatively reversible. Those are also areas that could contribute to higher-quality growth over the medium term.

Second, past experience regarding delays in implementation points to the need for the authorities to monitor closely the implementation and impact of the most recent stimulus package.

Third, I concur with the staff that in the context of preparing the end-of-year supplementary budget, the authorities should consider favorably allowing automatic stabilizers to work fully. This might even be considered as a minimum. In addition, in view of the downside risks and the 0.7 percent surplus still forecast for 1993 at the relevant level of the general government, including social security, the allusion by the staff to a resumption of the fiscal consolidation effort in FY 1994 might be somewhat premature at this stage. Indeed, the current recovery needs to gain autonomous momentum.

As to the second issue--how best to address the concerns of economic partners about the external accounts--owing in part to relative cyclical positions, inverted J-curve effects, and low commodity prices, in 1992 Japan's trade and current accounts again reached high levels that, since the early 1970s, were surpassed only in the mid-1980s. The staff used to downplay somewhat the problems raised by such trends. As recently as 1991, for instance, it had stated that "the projected surplus [was] not of a magnitude to cause concern." There was, of course, more recent recognition that, as mentioned in this year's appraisal, such excessive surplus could contribute to tensions in international trade.

Here, as in the case of fiscal policy, the staff has been preceded by the Japanese authorities. The recent G-7 Summit communiqué, for instance, indicated that significantly reducing external imbalances is an "important goal." Even more recently, the U.S.-Japanese Framework Agreement stated that Japan's objectives consist in achieving "over the medium term, a highly significant decrease in its current account surplus." I would be interested to hear staff comment on this rather un-Lawsonian objective.

In any event, the question is how best to achieve progress toward the Japanese authorities' objective. In trying to answer this question, I would like to refer to a recent staff working paper entitled "Revisiting Japan's External Adjustment Since 1985" (WP/93/52, June 1993). This study presents the sharp contrast between traditional models, which explain movements in trade flows from changes in demand and relative prices, and so-called revisionist views, which emphasize barriers to entry. The study's conclusion that traditional models explain correctly the behavior of Japan's external balance, leads me to the two following comments:

First, this study fully vindicates the idea that the yen exchange rate does matter and that the appreciation of the currency, together with recovery in the economy, can help achieve the authorities' external objective. In its papers for today's discussion, the staff also concludes that the strengthening of the yen would be consistent with both the cyclical and the structural features of Japan's economy. It should be noted, however, that so far, the degree of appreciation has been smaller than the exchange adjustment that began in 1985. Possible pressures for further appreciation therefore should not be resisted, even though punctual interventions can always signal to the market the need for orderly developments.

Second, I wonder whether the traditional and the revisionist views are as irreconcilable as they seem to be. Indeed, the lags and elasticities mentioned in the working paper might be, respectively, longer and lower in Japan than in other countries. Also, the working paper focuses on changes in trade flows and thus leaves aside the question of why the relative level of Japan's external flows--especially, imports of manufactured goods and inward foreign direct investment--are substantially lower than for other countries.

All these points should lead to consideration not only of comparative advantage but also of the structure of Japanese markets, especially the distribution system. Such topics deserve our attention.

As a final consideration with respect to the external accounts, I would highlight what appears to be the staff's somewhat selective roll-back approach regarding "managed trade agreements." Indeed, after having advised Japan not to accept such agreements, the staff explicitly encourages the authorities to roll-back those agreements that have been signed with the EC. There are, however, other such agreements in effect, and perhaps some others to come. I therefore wonder whether the staff's advice should not be more general in nature.

I remember that, some months ago, the Economic Counsellor jokingly likened a Board discussion on the Japanese economy to "having a bunch of heavy drinkers asking the sober guy, that is, Japan, to indulge a little bit." I wonder whether one could not shed a more positive and constructive light in the comparison. Indeed, Japan's overall and remarkable economic success has given it, at the same time, a direct stake and a major responsibility in the fate of an ever-increasingly integrated world economy. It is thus in Japan's, as well as others', direct interest to have the emerging coordinated strategy for sustainable growth succeed. Besides, both the fiscal stimulus and the opening of the economy could well allow Japan to reach a higher-quality growth path.

Mr. Wei made the following statement:

The year 1992 was an unexpectedly difficult one for the Japanese economy. After more than two years of moderate growth, the economy unfortunately could not achieve a soft landing. Instead, the current recession is probably the deepest since the mid-1970s. The Japanese authorities are once again challenged to take the appropriate policy actions at their disposal to shorten the recession as well as revitalize the economy.

Certainly, the current recession is more cyclical than structural in nature, although the structural element cannot be denied. In retrospect, it seemed unrealistic to expect that the authorities could avoid the current recession simply by adjusting economic policies. It is true that by formulating appropriate macroeconomic policies and by making appropriate adjustments in a timely manner, the authorities can still influence considerably the development of the cycle. However, it is not always easy to correctly manipulate so intricate and sophisticated an economy.

The adjustment process is still far from complete, although the return to positive growth in the first quarter of the year was impressive. The recovery of domestic demand remains mixed, and a number of uncertainties remain that will affect the strength and sustainability of the recovery. It is evident that the seemingly strong recovery was largely attributable to the first stimulus package. In this connection, I am concerned that although the stimulus package could help the economy return to positive growth in a relatively short time by encouraging domestic demand, it cannot entirely substitute for badly needed adjustment, particularly to resolve the fundamental problems mentioned by the staff, which are largely responsible for the current recession. To tackle those problems, especially those structural in nature, stimulus measures may not be helpful but may instead delay their solution or even worsen the problems. For this reason, I remain partially and cautiously optimistic about prospects for a more robust recovery in the remainder of the year. Having said that, I would not rule out the possibility that the likely second-round effect of the first stimulus package and the imminent effect of the second package will continue to play a role in dragging the economy out of recession. Nevertheless, for a more healthy and sustainable recovery, more needs to be done to alter the way in which certain aspects of the economy operate.

As to the key policy issues facing the authorities, looking at the experience with the first stimulus package announced last August, I can go along with the broadly held view that the package came somewhat late because, as the staff points out, initially, the depth and length of the recession were substantially underestimated. As to the appropriateness of the magnitude of the first stimulus package, one could conclude from the adoption of a second package that the first was definitely insufficient. In this context, I would be interested to hear how the magnitude of the two stimulus packages was decided. Was it based primarily on the income-expenditure model? I would also be interested to learn whether the authorities are expected to give renewed consideration to the revenue side of the budget, as mentioned in the staff report.

On monetary policy and exchange rate developments, I note that since the economy started to slow more than two years ago, the authorities have gradually eased monetary policy, as evidenced by the continuous reduction in the official discount rate. At the same time, inflation continued at low levels, and is now lower than when the economy entered into recession. Nevertheless, this monetary easing has not given rise to a parallel growth in monetary aggregates, which seem to be responding mainly to the developments of real factors in the economy. The staff has provided a systematic diagnosis of the phenomenon. In the circumstances, there appears to be some room for further manipulation of monetary policy even though the official discount rate is already at an historically low level. The question is whether it would be worthwhile to do so. As the leeway available may be less than it appears, the authorities are advised not to further reduce the official discount rate at a time when the effects of past easing of monetary policy are far from reflected in the economy. Instead, they are encouraged to take steps to facilitate the growth of money aggregates to be more consistent with, for example, the current level of the official discount rate. The authorities' view on this matter is interesting and deserves more attention and consideration. That being said, I continue to support the pragmatic approach adopted by the authorities in formulating monetary policy, which is based on monitoring a wide range of indicators.

Although the recent marked appreciation of the yen mainly reflects the mixed picture of economic fundamentals in Japan and market reactions to them, there is certainly reason for concern about the rapid pace of appreciation. The appreciation of the yen is justified more by the strength of the external position than by the current fragile general economic situation. I agree that the real concern for the authorities is that such appreciation could weaken or delay the recovery. In this regard, I believe that in contemplating the magnitude of the fiscal stimulus packages, particularly the second package, the authorities must have taken into account the impact of yen appreciation, because the stimulus and yen appreciation are likely to work in opposite directions with respect to helping the economy out of the recession in the short run.

On financial sector issues, the growing volume of nonperforming loans of many Japanese banks is still a matter of grave concern. Although the staff and the authorities continue to disagree on the magnitude of the nonperforming loans, the seriousness of the problem remains. The accumulation of nonperforming loans is reportedly not confined to a small number of banks, and its effects on the health of the financial sector as well as the economy are not yet fully felt and therefore cannot be ignored. On the one hand, the sources of the problem are worrisome. There may be some correlation between this phenomenon and the bubble economy of the past few years. In any event, one cannot underestimate the damage that the accumulation of nonperforming loans can do to the financial system in particular and the economy in general. On the other hand, it will take a long time to repair the damaged image of these banks. It is time to take corrective as well as preventive measures to deal with the problem. In this regard, I welcome the preliminary measures taken by the authorities on a short-term basis. Preventive measures on the part of banks as well as the authorities are much more crucial from a longer-term perspective. Continued reform of the financial sector is needed to address the problem. I would appreciate elaboration by the staff on the effects of the measures taken so far and on additional measures that might be needed in the event that the problem worsens rather than improves in the period ahead.

On structural policies, the issue of the degree of the economy's openness remains the central point of any debate. Although the Japanese economy is very open based on the criteria of formal tariff and nontariff barriers on imports of manufactures, a judgment on openness cannot be confined to the area of manufacturing. For all industrial countries alike, it should be extended to the agricultural sector and to other service areas. Although I understand that the authorities have their particular concerns about further opening these areas, they are encouraged to strengthen efforts on a bilateral as well as a multilateral basis in order to resolve trade disputes mutually and further open their economy to benefit the world economy. The authorities' recent progress in this area is indeed welcome.

On foreign aid, I wish to commend Japan on being the largest provider of foreign assistance in 1992. Nevertheless, I note that Japan's official development assistance during 1988-92 remains below the UN target of 0.7 percent of GDP. The authorities are therefore encouraged to speed up their efforts to achieve the UN target at an early date.

Mr. Ismael made the following statement:

I will focus my intervention on two major issues: the fiscal stimulus and its effects, and the strength of the yen.

Much stress has been placed on the expansionary fiscal stance in Japan as a way of pulling the economy from the rolling recession. However, the focus of the fiscal stimulus has been on public sector spending, which accounts for a relatively small part of GDP and so has little leverage on the corporate sector, where balance sheet retrenchment is well under way. The fiscal stimulus, therefore, has not been sufficient as yet to make the difference between recession and strong recovery.

In the meantime, nominal interest rates have declined sharply, but so has inflation. However, real interest rates are not particularly low, especially at longer maturities, in view of the recent increase in bond yields. In addition, the strengthening of the yen amounts to a de facto monetary tightening, which could adversely affect GDP growth. Moreover, political instability and the approach of the election could delay any additional fiscal stimulus. As I said at the July 9 discussion on world economic and monetary developments, this would shift more of the burden to monetary policy to provide a policy stimulus.

Against this background, interest rates have further to fall. A policy tightening is not warranted at the current stage of the economic cycle.

At the discussion on world economic and monetary developments, Mr. Fukui agreed that the yen should be regarded as being in "overshoot territory" vis-à-vis the U.S. dollar and that the recent appreciation of the yen has not been a product of normal factors: in plain language, it can be said that the appreciation has been brought about by political pressures rather than by easily identifiable economic trends.

In view of the recent retracement of the yen vis-à-vis both the dollar and the deutsche mark, I wonder whether Mr. Fukui, or the staff, believes that this phenomenon is likely to persist because an overvalued yen will not appear attractive on cyclical grounds; the effect of the increasing overvaluation will become more significant; and neither political nor economic influences point to renewed yen strength.

A further strengthening of the yen seems undesirable in view of the evident strains it is placing on the manufacturing sector, which is already under pressure. Moreover, unlike in the mid-1980's, when substantial corporate restructuring allowed the corporate sector to adjust to a stronger yen, the financial pressures relevant at present, and the absence of any strength in either foreign or external demand, suggest that this is not a feasible option in the current period of yen strength. Finally, the U.S. authorities have put greater emphasis more recently on the removal of structural impediments to trade to reduce the Japanese surplus, rather than exchange rate changes, and the success of the trade talks last week in Tokyo has also limited the need for additional appreciation.

In concluding, I would like to say a few words on the importance of the exchange rate of the yen for countries like Indonesia. Between March 31, 1992 and March 23, 1993, the yen appreciated by 15 1/2 percent vis-à-vis the U.S. dollar. In the case of Indonesia, the U.S. dollar value of its yen-denominated debt increased by $2.7 billion without even incurring any additional borrowing. It is therefore important that the parities of the major currencies be kept as stable as possible.

Mr. Schoenberg made the following statement:

Even though the current economic situation in Japan has to be characterized as the most severe recession in almost 20 years, most countries would probably be quite happy if their recession resembled Japan's. Economic activity in Japan may be weak, but the economy is still growing; and an increase in the rate of unemployment from 2.3 percent to 2.5 percent would not be regarded as particularly worrisome anywhere outside Japan. Moreover, if reported indications that the present downturn has already bottomed out prove correct, this recession would be the least severe among those countries experiencing the effects of unsustainable asset price inflation. This comparatively positive assessment remains valid, notwithstanding our expectation that an ongoing balance sheet adjustment and the existing overcapacity in industry will make a quick return to the high growth rates of recent years an unlikely prospect.

Let me say at the outset that I largely agree with the staff's appraisal, except for its recommendations for monetary policy, where I would set a more cautious tone.

An earlier successful policy of fiscal consolidation has allowed Japan to be the only G-7 country to use fiscal policy as an effective instrument for boosting economic activity and to announce two fiscal packages of impressive size. The benefits of a medium-term fiscal policy orientation in terms of increased policy scope are now coming fully to the fore. The rapid recovery of the stock market appears to indicate that these packages had an immediate psychological impact, strengthening the confidence of investors.

The actual impact of the fiscal measures on demand, however, has not yet fully materialized, in view of the usual fairly long time lags in Japan between announcement and implementation. I therefore agree with the staff that the April 1993 package has to be implemented expeditiously, all the more so because recovery will be probably already well under way before all the fiscal measures come fully into effect. I also agree with the staff that a further artificial fiscal demand stimulus might be one step too much and that at present, no further change in policy is required.

In my view, the staff's observation that "past experience would suggest a cautious approach in order to avoid a repeat of the overreaction to previous cyclical weaknesses" particularly holds true for the conduct of monetary policy, which had been too lax for too long in the late-1980s and, accordingly, contributed significantly to the emergence of the bubble economy, which lies at the root of current problems. Japan had to go through a painful process to regain monetary control. Unlike the staff, I cannot see that there is much to be gained by a further reduction of short-term interest rates, which are--like long-term rates--already at record low levels, at a time when the transmission mechanism of monetary policy is still obstructed by the difficulties of the financial sector. Instead, like Mr. Landau, I see an undue emphasis laid by the staff on an active monetary policy as a way to achieve short-term growth objectives--a recent worrisome trend in view of the long history of failed attempts to fine-tune the real economy by monetary measures.

The observation that further interest rate cuts might not lead to inflation at present because of the strengthening of the yen is not a strong argument in a medium-term perspective. I would agree, though, that the dangers of a repetition of past mistakes could be considered somewhat diminished insofar as the private sector may have learned some lessons from the recent experience with asset price inflation. It will take some time for the financial system to resolve the balance sheet problems caused by excessive risk-taking in the past.

Both fiscal packages include a number of measures--according to the staff report, equivalent to 1.1 percent of GDP in each package--designed to limit the extent or the pace of asset price disinflation, in particular, to halt the decline of land prices through government purchases and increased lending by the Housing Loan Corporation, and by providing measures to encourage the acquisition of equities by public corporations. While these measures may help avoid a further downward movement of prices, they may also delay the eventually inevitable full correction, and, accordingly, induce a further downward adjustment at a later stage. I also wonder whether the authorities have shown too much willingness to bail out failing financial institutions, which could lead to moral hazard problems in the future. In this context, I would like to endorse the staff's call for more transparency in the situation of different financial institutions; I also support the staff's view that the current difficulties in the banking system should not lead to a delay in implementing further financial sector reform.

As to the external sector, Japan's current account surpluses have been a focus for discussion for some time. In this context, I would note that it is not the size of the current account surplus in terms of GDP that is, in our view, the most disturbing factor--many countries have experienced or are experiencing current account surpluses of similar or even larger magnitude. It might be even fair to say that Japan's current account surplus is to some extent more a political than an economic problem, related, inter alia, to misguided perceptions and inadequate analysis.

Two aspects, however, indicate that Japan's external position is "suboptimal" from a global welfare point of view. And I am not talking here about the short-term factors on which the staff concentrates when explaining the recent increase in Japan's current account surplus but about the longer-term structural factors. In this context, the data on page 14 of the background paper on the savings/investment balance in Japan are especially interesting. The private saving ratio in Japan is relatively high by international standards, but so is private investment. In fact, private sector investment exceeded private sector saving for the last four years, except in 1992, when the investment ratio dropped precipitously for obvious reasons. Even then, the savings/investment balance was only slightly positive--at about 1 percent of GDP--only because that balance does not reflect the net borrowing of public enterprises, which is included in the public sector figures in the staff report. If data on public enterprises are merged with those of the private sector--and there are many good reasons to do so--the resulting savings/investment balance is negative even for 1992.

It appears, therefore, that the national savings/investment balance, which reflects the current account position, is essentially not the result of private decisions. Instead, the huge gap between general government saving and investment lies at the root of external imbalance phenomenon. The authorities point to the expected changes in the age structure of the Japanese population as the main justification for the huge surplus in the general government account, and "intergenerational equity" as one of the major considerations for their policy of accumulating large surpluses in the social security fund. In view of the relatively low return of additional investment in Japan itself, it also makes sense--so goes the argument--to invest these funds outside Japan.

The argument, however, is not completely persuasive. Not only are a number of countries facing similar demographic developments; in view of Japan's high national saving ratio, it does not appear that the currently active generation is indulging in excessive consumption and overspending, and that, therefore, a shortfall in private sector saving needs to be corrected by government action. Rather, it appears that Japanese workers are sacrificing much more than workers in other countries to increase the living standard of future generations. Seen against the background of the huge capital stock that is being accumulated, the strong emphasis laid by Japanese society on providing an adequate education to the young, and the impact of "normal" technical progress, it is more than likely that the income-earning capacity of the future work force will be much greater than that of the present one. If intergenerational equity considerations are taken into account, I believe that a strong case can be made for less generous transfers from the present generation to future ones. I therefore see a less strong case for a massive general government surplus than does the staff or the Japanese authorities.

Perhaps more important, Japan's current account has to be seen against the background of a comparatively low import ratio. Japan, on a per capita basis among the richest of the OECD countries, has the lowest import ratio of all OECD countries, and that disparity is even more striking if only trade in manufactured goods is taken into account. That trade structure as well as the high differentials in domestic prices for some categories of goods between Japan and other industrial countries corroborate anecdotal evidence that access to Japan's markets is not particularly easy for foreign companies, and that Japan is forsaking the benefits to be gained from a stronger integration into the world economy.

How could this objective be achieved? Managed trade is certainly not the right answer, and I am particularly grateful to the staff for its clear rejection without qualification of that concept. I also welcome Mr. Dawson's statement that the U.S. objective is to "unmanage" trade. Managed trade is particularly dangerous on a bilateral basis, because it runs the risk of leading eventually to a sharing-out of key markets between the suppliers of the countries entering into bilateral trade agreements at the expense of third partners. Also, the experience with managed or planned trade in other parts of the world should be evidence enough of the disadvantages of such a system. For us as protagonists of free trade, there is no alternative to a multilateral open trade system. I am also not convinced of the merits of a forced domestic demand stimulation. That approach not only runs the risk of macroeconomic destabilization--as Japan has recently discovered--but would also, as the footnote on page 7 of the staff report tries to convey, have only limited impact on the rest of the world.

A sudden and substantial revaluation of the yen does not offer an appropriate solution, either. While I share the staff's view that over the medium term, appreciation of the yen looks plausible in view of the strength of Japan's external position, I tend to agree with the authorities that erratic movements in the exchange rate will have not only substantial J-curve effect but also trade-dampening effects by weakening the economic recovery.

Thus, "market access" is the catch word, and I would urge the Japanese authorities to move more vigorously in removing existing barriers to full market access as well as the numerous remaining structural impediments to stronger competition on the domestic markets. The authorities may point to the fact that markets in Japan are legally more open. But that is not the issue. Changes in business culture and practices are required. For instance, Japanese industry is largely vertically structured, and vertically structured economies tend to order internally. I could give many more examples. In addition, the staff offers a number of areas where there is scope for more deregulation.

A strategy for broadening market access would meet the interests of the international community as well as Japan because it would dampen both the upward pressure on the exchange rate and the pressure to inflate the economy.

Mr. Al-Jasser made the following statement:

As Mr. Fukui has indicated, Japan's economy is showing some signs of recovery following two years of weak economic performance. In view of the systemic importance of Japan in the world economy, this is a welcome development, and calls again for further consolidation of this trend. The gradual lowering of the discount rate from 6 percent to 2.5 percent over the past two years, coupled with the fiscal stimulus package adopted at the end of last year, helped strengthen domestic demand, which provided the impetus for the admittedly fledgling economic recovery.

Despite the robust growth in economic activity registered in the first quarter of 1993, the momentum of the upturn remains hesitant, as evidenced by lower industrial production and sales, and a softer labor market in April-May. Appropriately, the policy stance of the 1993 budget was stimulative, and a second fiscal stimulus package was recently enacted. These measures are expected to consolidate the recovery in 1993 with fourth-quarter-to-fourth-quarter GDP growth reaching 2.5 percent.

If the projected improvement in economic activity is realized, a further easing of monetary policy may not be warranted at this time, as it could lead to a depreciation of the exchange rate, thereby aggravating the external surplus.

The improvement in the financial system over the past year is also expected to enhance the economic outlook. The staff notes that while some institutions are still experiencing significant difficulties that could strain the system, the banking sector as a whole seems capable of absorbing a broad range of estimated bad loan losses. In this regard, I welcome the authorities' assertion that the banking system will not need an infusion of public funds. Continued implementation of interest rate liberalization is also a welcome development. However, the authorities need to move forcefully with further reform of the financial system to make it more transparent and efficient. For example, further opening of financial markets to more competition from both domestic and international financial institutions, as well as improving the transparency and disclosure of asset quality in the banking system would be helpful.

The substantial progress that has already been made in certain areas of structural reform is welcome. These reforms will not only play an important role in addressing the external imbalances, but will also enhance the allocative efficiency of the Japanese economy. Nevertheless, much remains to be done in this area if the global economy is to benefit fully from an economic recovery in a systemically important country like Japan. I agree with the staff that priority should be given to reforming the agricultural, distribution, and transportation sectors. Significant liberalization in these sectors will enhance the welfare of the Japanese people through reducing prices and raising productivity and income. Moreover, I welcome the Framework Agreement between the United States and Japan, which is an important step in the right direction for enhancing international trade. More important, the accord should advance the stalled Uruguay trade negotiations.

As to the medium-term outlook, I broadly agree with the staff that the prospective sharp rise in the proportion of the elderly in the Japanese population justifies a medium-term fiscal consolidation, once the recovery is consolidated. However, as I mentioned in my intervention on this issue last year, the pace and degree of this consolidation remains open to question. Indeed, the future path of the savings-investment balance may not prove to be as pessimistic as envisaged by the authorities and the staff. In particular, it is not clear that private sector savings will fall dramatically as the population ages, as many agents are likely to remain economically active after retirement. Moreover, an increase in Japan's foreign investment at the present time would generate an income stream in the future that would reduce the projected strain of an aging population on the external position. In this regard, it would be helpful if next year's background paper included a section on Japanese foreign investment and its positive contribution to growth in other parts of the world, as well as its prospective impact on future flows of income to Japan.

As I mentioned earlier, Japan is a country of great systemic importance in the world economy. Its external surplus remains substantial and is rising. While a number of factors influence the current account surplus, the higher rate of saving in Japan, compared with its trading partners, is a significant factor. While the high saving ratio in Japan has contributed positively to the availability of credit in the world economy, any increase in this ratio will certainly aggravate the trade imbalance. In this context, I am perplexed by the staff's recommendation to put less weight on income taxes and more on consumption taxes, which is likely to lead to even higher savings in Japan. This does not appear to be timely advice when domestic demand needs to be revived through, inter alia, raising domestic consumption.

Japan's record in the provision of official development assistance and parallel financing arrangements for countries undertaking structural adjustment effort is commendable. While I welcome efforts to increase Japan's ODA contributions, I would urge the authorities to take the lead in raising ODA in OECD countries to the modest UN target of 0.7 percent of GNP.

The Japanese authorities have accumulated an enviable track record in domestic economic management. The gradual easing of monetary policy over 1991-93, coupled with the recent fiscal stimulus, is already paving the way for another period of economic growth. That growth can be enhanced through implementing the aforementioned structural reforms, which should also benefit the global economy.

Mr. Smee said that he wished to commend Japan for being the only G-7 country to have elaborated a fiscal consolidation program in the 1980s and to have achieved meaningful results, thereby offering it the opportunity to apply anticyclical fiscal policy as required in the past year and a half. He also wished to commend the staff for the introduction of the monetary conditions index so that Directors might better understand the interaction of monetary policy with interest rates, the exchange rate, and the economy. He was also grateful for the supplementary material included in the background paper, which had helped him better understand the asset price bubble, before, during, and after.

The staff seemed, however, to be caught between two dilemmas, Mr. Smee observed. The first was its concern about the short-term outlook versus the longer-term need for fiscal consolidation. The second dilemma was its concern about financial sector issues--particularly the grey areas of business practices that complicated market access in Japan as well as the need to differentiate between monetary policy and the post-1987 experience, and monetary policy and recent experience--versus the Japanese authorities' contrary views in those areas.

As to the first dilemma, and despite the important policy incentives already taken, it was not yet clear that all elements for a solid recovery in Japan were in place, Mr. Smee continued. To complicate matters further, the international context was not generally supportive of the authorities' efforts. The other major economies were either slowing or were experiencing hesitant recoveries. The strength of the yen in foreign exchange markets was also likely to hinder Japan's economic recovery in its initial stages.

In that uncertain environment, it was especially critical to maintain a medium-term policy focus, Mr. Smee considered. While it was tempting to address lingering current problems with yet more short-term measures, it was essential that the longer-term implications be fully recognized and addressed.

In assessing the stance of monetary policies, he strongly welcomed the staff's use of the monetary conditions index, Mr. Smee stated. Directors would recall that his own authorities had found that index to be a useful indicator for monetary policy in Canada. On a monetary conditions index basis, Japan's monetary policy had tightened significantly as a result of the effective appreciation of the yen, and despite the 75 basis point reduction of official interest rates in February. The authorities had indicated to the staff that they placed a relatively low weight on exchange rate developments compared to other factors affecting policy decisions, although that seemed somewhat at odds with numerous official statements expressing concern over the magnitude and rapidity of the yen's appreciation.

The staff was unambiguous in its view that monetary policy should be eased, and he agreed with the staff on that point, Mr. Smee said. He considered that an additional easing in official interest rates would be appropriate as at least a partial offset to the negative implications for the economy arising from a stronger yen. Moreover, the authorities must stand prepared to tighten monetary conditions if there were indications of renewed inflationary pressures.

On fiscal policy, the staff was somewhat ambiguous, Mr. Smee observed. It seemed to say, "Yes, maybe, but not too much" and "restart fiscal consolidation as soon as you can." That was how he read the staff's recommendations. If he did not know better, he would suspect possible differences of views among various Fund departments regarding fiscal consolidation and what should be done at present compared with the medium term.

Whoever wrote that Japan should "avoid a repeat of the overreaction to previous cyclical weaknesses" had got it right, Mr. Smee considered. That view was supported by expectations with respect to social security--the surplus was forecast to decline over 2 percentage points of GDP from FY 1993 to FY 1998, to only 1 1/2 percent of GDP--and the large amount of unfunded liabilities under the social security system. More broadly, he wondered whether the staff, and the Research Department in particular, had begun looking at the impact that demographic changes in coming years would have for industrial countries and the world economy as a whole. He believed that that issue needed to be confronted sooner rather than later.

As to the second dilemma, he found that the staff report fell into a "they say/we say" format, Mr. Smee commented. While the staff's recommendations came out in the end, they seem muted and required some reading between the lines. There, the first issue was financial fragility. In assessing the state of the Japanese financial system, observers continued to be hampered by a lack of transparency in financial data. The lack of data created suspicions that might not always be fully countered by official assurances and, ultimately, might be harmful to the operation of the system. As the staff pointed out, greater disclosure of the quality of Japanese bank assets would allow market mechanisms to work more effectively, rewarding successful banks and improving overall efficiency. The authorities had noted that concern regarding the financial system had diminished in the past year. The important question, however, was: what had fundamentally changed to reduce concerns in that regard?

Official estimates of problem loans, although increasing by a relatively small amount between September 1992 and March 1993, remained well below unofficial estimates, Mr. Smee observed. While the major commercial banks comfortably met the March 1993 BIS capital standard, that had been facilitated by an easing of domestic regulations and fortuitous circumstances, including stronger equity prices--in themselves aided by government support measures--and the appreciation of the yen, which had reduced the yen valuation of dollar-denominated assets. He also noted that the average discount of 33 percent on nonperforming loans acquired by the banks' cooperative purchasing company could be at odds with anecdotal reports suggesting additional write-downs might be required in the absence of a significant recovery in property values.

As to "managed trade," in addition to the concern about managed trade internationally, he saw a problem in coming to grips with managed trade within Japan--namely, the grey areas of business practices, Mr. Smee stated. The staff noted that there was scope for more deregulation, particularly in the distribution and transportation sectors; that efforts should be made to ensure greater transparency of administrative rules and procedures; and that the case for market opening was particularly strong in the area of agriculture. In sum, the staff report indicated that those grey practices complicated market access and contributed to price differentials. The staff then noted that the change in the current account of the balance of payments could be explained by macroeconomic factors. He wondered about the impact of grey practices on the underlying level of the imbalance; in particular, how important were those grey practices and how much would macroeconomic factors need to overshoot in order to offset them?

The Japanese authorities were legitimately concerned that easier monetary conditions should not initiate another asset price spiral, Mr. Smee remarked. However, the present situation in Japan, and globally, was not the same as that prevailing in the late-1980s. The fact that the official discount rate had never gone below 2 1/2 percent was thus no reason to maintain that the rate should not go below 2 1/2 percent.

In sum, he generally agreed with what he interpreted to be the staff's views on the Japanese economy, Mr. Smee stated. He believed, however, that the staff could have been somewhat more pointed in its remarks and recommendations, particularly with respect to the importance to the economy of the opening up of Japan's markets. He would also re-emphasize that the Japanese authorities should be more forward-looking and view their policy challenges and goals in a medium-term context.

Mr. Peretz, recalling Mr. Smee's comment that Japan had been the only G-7 country to achieve substantial fiscal consolidation in the 1980s, observed that only four years earlier, the United Kingdom had had to find ways to retire government debt ahead of schedule as a way of reducing the current account surplus.

Mr. Peretz then made the following statement:

> You may know that in Britain we have an annual award for the year's best forecaster; it is called the "Golden Guru" award. Some time ago, it was won by the British Treasury. Clearly, in respect of Japan, this year's Golden Guru award goes to Mr. Dawson and not to the staff.
>
> Last year the staff forecast 4 percent growth in 1993, while it now projects an outturn of about 1 percent. The U.K. authorities, while recognizing the uncertainties, continue to forecast growth of 0.5 percent for 1993 and consider the staff's 3 percent growth forecast for next year as optimistic.
>
> Of course, the staff may yet prove to be the winner of next year's award for forecasting: if every year you advocate a fiscal stimulus, you are likely to be right some years at least. My point is that forecasts for Japan have been particularly uncertain, and the experience of both the United States and the United Kingdom in coming out of the recent recession has been that balance sheet adjustment and recovery are taking somewhat longer than was first expected. The Japanese authorities must therefore stay alert to the possibility that they may need to take further action to stimulate a full recovery.
>
> The rise in the yen since the start of this year is broadly consistent with economic fundamentals--namely, the large current account surplus and low inflationary pressure. It gets the real yen rate broadly back onto its long-term trend line. But from a domestic standpoint, appreciation of the yen has meant a significant tightening of overall monetary conditions, representing a threat to the recovery. In this respect, I do not think that a further significant appreciation in the short term would be particularly helpful. It is certainly not the best way to deal with any concern there might be over the extent of the trade imbalance.
>
> Avoiding an excessive appreciation will not be helped if a perception that the authorities see the current historically low interest rates as an effective floor is allowed to gain currency. I would agree with the staff that there may still be room for

further rate reductions at this stage in the cycle, and the authorities would be most unwise to rule these out. Once the recovery is firmly rooted, upward adjustments in interest rates might be needed again.

The high-profile Japanese-U.S. trade discussions may have also played a part in placing upward pressure on the yen. I will not tilt at this windmill; but I will at least mention its existence. I was pleased that the agreement that seems to have emerged has avoided setting specific targets for Japan's current account or levels of manufactured imports. While targets on their own would not have amounted to managed trade, they could easily have led to pressures for managed trade in order to achieve them.

I hope--and indeed expect--that the regular discussions planned between the Japanese and U.S. authorities to monitor trade developments will concentrate on exploring ways of opening up markets further to all trading partners and so strengthen the multilateral approach to trade that the Fund has endorsed. I was glad to hear Mr. Dawson's remarks in this respect. It makes no economic sense at all to concentrate on bilateral trade balances and trade relations. If it did, I might ask questions about the large bilateral U.S. trade surplus with the United Kingdom.

In the case of Japan, the need for more open trade in agriculture, especially rice, is particularly strong. I would also like to see continuing and rapid reform of the distribution system, greater transparency of administrative rules and procedures, especially for public works contracts, as well as nondiscriminatory product quality and design standards.

As to fiscal policy, I agree with the staff that the delay in implementing last August's fiscal stimulus package was most unfortunate. That it was not approved until December makes evaluating its full effect, and the likely effect of the more recent package, even more difficult than usual. Greater urgency seems to have been attached to the April package. But, in view of all this uncertainty, the new Government will need to stand ready to take further action to stimulate domestic demand quickly if the downside risks on the forecast appear to be materializing. The supplementary budget normally prepared toward the end of the calendar year will be an opportunity to make any further adjustments that are required.

The authorities' desire to maintain a fiscal surplus over the medium term can be justified--at least to a degree--by the future pension liabilities associated with an aging population. This is, however, a medium-term issue and should not be used as an excuse for delaying a further fiscal stimulus this year if it appears to be needed.

Having said this, while I accept that provision for the sharp demographic shift is important, it is not clear that it necessarily needs to be carried out through steady public sector saving rather than through the private sector. I wonder whether the staff has any views on this point. For example, could an increase in the dependent population be more efficiently provided for through an expansion of private pension schemes? Perhaps this issue should be looked at in the context of the kind of international study that Mr. Smee has suggested.

In this context, I welcome the recently announced intention of the Ministry of Finance to consider further liberalization of the pension fund market. Investment management companies should be allowed to manage public pension funds, and the artificial distinction between investment management generally and investment trusts could helpfully be eliminated. I agree in general with Mr. Dawson that current strains in the financial system should certainly not be used as an excuse for slowing down deregulation and desegmentation.

With respect to the issue of Japan's current account position, as I said at last year's consultation discussion, the other side of the current account surplus has been a massive contribution to the world's savings. It has, as Mr. Landau mentioned, given the authorities a huge stake in the health of the whole world economy. In the broadest of terms, this should carry some considerable benefits for the future, although I would support Mr. Al-Jasser's suggestion that next year's background paper might have a section on the authorities' overseas investment. For the immediate future, with economic conditions depressed throughout most of the industrial world, there is perhaps no shortage of world savings. Looking beyond that to the medium and longer term, when savings are again in short supply and real interest rates are likely to rise, I still find it entirely plausible that we will eventually be faced with the prospect of declining net savings--only partly offset by lower domestic investment--as a result of the aging population. Thus, there is a downside to the prospect of the likely decline in Japan's trade surplus. This strengthens the case for taking a further look at ways to stimulate private saving in all industrial countries in the longer term, and to redouble our efforts to increase public saving by reducing structural budget deficits.

Mr. Lanciotti made the following statement:

There are encouraging signs that the recession that hit the Japanese economy during the past two years bottomed out in the first part of 1993. However, the most recent indicators do not yet show a true inversion of the economic cycle, while the strong appreciation of the yen feeds the concern that the recovery might begin later than expected. In such circumstances, the need to stimulate and sustain domestic demand--which was addressed by the Japanese authorities with a policy mix that provided for expansionary fiscal policy and easing monetary policy--suggests that the same economic policy mix should be retained.

The authorities' policy mix seeks to balance the need to provide the economy with the stimulus necessary to overcome the slowdown in activity and the need to attain medium-term fiscal consolidation consistent with the future requirements of an aging population. In this respect one may wonder whether this phenomenon is country specific or general, as Mr. Smee has suggested. Therefore, as the countercyclical content of the measures are somewhat reduced by such longer-term considerations, a judgment has to be made on the appropriate balance between the scope for expansionary financial policies aimed at speeding up recovery, and the need to pursue this medium-term fiscal objective. The Economic Stimulus Package approved in August 1992 contained measures equivalent to more than 2 percent of GDP. It is true that the delayed approval of the package by the Diet considerably reduced its impact in terms of demand incentives. However, this was also due to the particular nature of the measures envisaged in the package: some of them did not provide a direct stimulus to final demand. In light of the above considerations, the FY 1993 Budget might perhaps have entailed a somewhat more expansionary stance--for instance, public works outlays were lower than in the final FY 1992 Budget.

In the face of continuing weakness in private demand, it was necessary to adopt a second large fiscal package in April. Indeed, the package was needed not only to provide additional demand support but also to compensate for the prudent stance of the 1993 Budget. The size and composition of the 1993 package seem to be appropriate to provide an adequate fiscal stimulus to domestic demand; the bulk of the measures consist of public infrastructure spending and a front-loading of public works contracts. However, uncertainties still remain about the pace of recovery, and I therefore welcome the authorities' intention to closely monitor the economic situation and to react promptly in the event of a slower than expected recovery. In particular, if it becomes necessary to adopt further measures, due consideration should be given to the possibility of reducing taxes--especially corporate taxes--and, more generally, to overhauling the tax structure. Indeed, tax brackets are the same as they were in 1988, which, owing to the fiscal drag, contributed to reducing households' disposable income and, consequently, consumption expenditure and imports. I can appreciate the authorities' concerns about medium-term fiscal consolidation, but I believe that, at this juncture, such concerns should not lead them to rule out the possibility of tax reductions.

The present stance of monetary policy seems to be correctly oriented toward providing appropriate stimulus to domestic demand. A revival of consumer and private capital expenditure is all the more important in view of the need to strengthen the capital position of the banking system by improving its profitability. As Mr. Fukui has stated, "there may be some question about the official figure" of the banks' nonperforming assets, and "it will be some time before banks can clear" them. More explicitly, the staff estimates that for the whole banking system, nonperforming loans could total more than twice the official estimate for the 21 major banks.

In view of the delicate situation of the financial sector, there is a risk that the active use of monetary policy to stimulate economic recovery could prove ineffective. Indeed, banks have been seeking to improve their profitability and to reduce their riskiest activities through more cautious pricing policies than in the past, so as to make up for the fall in asset values. This, in turn, has resulted in a widening of the differential between loan and deposit interest rates and a dramatic reduction in the rates of growth of private sector credit, thereby partly offsetting the potential expansionary effect of monetary relaxation.

At the same time, monetary policy is to be framed so as to take into account exchange rate developments. I understand the authorities' concern about excessive relaxation of the monetary stance. At the same time, a compelling argument in favor of present monetary policy is the fact that a further appreciation of the yen would be inappropriate at this juncture, because of the disruptive effects it could have on business confidence and on the restructuring process. A strong yen is consistent with a reduction of Japan's current surplus in the long run. However, adjustment of the current account should come not only from yen appreciation but also from recovery of domestic demand.

I would urge the Japanese authorities to continue to play an active role in achieving further progress toward a successful conclusion of the Uruguay Round. Only a comprehensive and far-reaching agreement will promote a durable expansion of international trade, which is key to the promotion of economic growth and job creation throughout the world.

Mr. de Groote made the following statement:

My statement today will address the three following issues: fiscal policy and the recently announced fiscal stimulus package; monetary policy and the situation in the financial sector; and developments in the current account and related trade tensions.

In my statement for the 1992 Article IV consultation, I concluded the discussion of fiscal policy by saying that "the Japanese Government seems to have the ability to adapt further to global demand, and would be well advised to make use of this ability to avert the potential long-term damage of the slowdown, to which the position of its financial intermediaries is especially exposed." To their credit, the authorities have subsequently made good use of the room for maneuver provided by the success of the medium-term fiscal consolidation strategy they had been pursuing since the 1980s. The fiscal stimulus packages approved in December 1992 and April 1993 seem to be large enough to secure the limited benefits that aggregate demand management can provide. The only fly in the ointment was that political constraints prevented the December 1992 package from being implemented earlier, as called for by cyclical conditions.

The two stimulus packages combined are substantially larger than the fiscal stimulus measures introduced during earlier cyclical downturns, which is appropriate in view of the unusual depth of the present recession. Still, two points merit comment. First, the serious concern aroused by the economy's present weakness should not obscure the medium-term goals of Japan's fiscal strategy. Second, the fact that past fiscal stimulus measures have consistently overshot their objectives argues for careful monitoring of fiscal policy in the immediate future. Both the staff and the authorities have stressed the importance of flexibility in the conduct of fiscal policy. I am sure that the authorities are ready to exercise this flexibility by taking additional fiscal measures if economic conditions deteriorate further. I would only add that the principle of symmetry, which is so often honored in this Board, calls for an equal readiness to scale back the fiscal stimulus in the event that Japan's economic situation develops more favorably than was explicitly or implicitly assumed when the packages were being designed. Such an assurance of symmetry would surely have a beneficial effect on the markets as well.

More generally, I am inclined to warn against excessive flexibility in Japan's fiscal policy response to future developments, principally because of the inevitable lag between the time when a measure is decided and the time when it begins to affect the real economy. As the staff explains, the specific conditions of government procurement in Japan could make this lag even longer. It could thus remain uncertain, during the second half of the year, how far the approved measures have already affected the real economy and how much of their effect is still in the pipeline. This lag could also frustrate efforts to time appropriately the effect of the measures taken, since business cycle conditions will probably improve in the not very distant future. Looking at Japan's policy reactions during previous business cycles, it appears that in many cases, the business cycle had already shifted by the time a policy reinforcement began to exert its effects, so that the expected benefits were largely lost. This point deserves to be stressed because Japan is so often accused by the rest of the world, ourselves included, of doing too little to counteract cyclical variations.

Between April 1992 and February 1993, monetary policy was also significantly eased to provide additional support to the fiscal measures. However, with the official discount rate at 2 1/2 percent, short-term interest rates at about 3 percent, and long-term interest rates at 4.3 percent, the staff suggests that "the case for lowering market interest rates has strengthened," pointing to the adverse effect of yen appreciation on the short-term prospects of recovery. On this point I have two remarks. First, even though Japan's recession may be deep by domestic standards, it is not exceptional compared to recessions in other industrial countries. Second, the combined easing of both fiscal and monetary policy has already been substantial, even taking into account the offsetting effect of recent yen appreciation. Thus, present calls for "more flexibility" in the form of additional aggregate demand stimulation appear to be based on the fact that Japan's strong fiscal and external balances permit such flexibility, rather than on any demonstrated need based on developments in the real economy. As there are now signs that the growth of monetary aggregates is beginning to recover, and as long-term interest rates recently fell again, probably as a result of continued low inflation despite some signs of revival, most macroeconomic conditions for a resumption of economic growth are in place. This interest rate decline seems to cast some doubt on the staff's prediction that private business investment will continue to be weak for the remainder of 1993. I also have doubts about the projected negative contribution of inventory investments to 1993 GDP growth. This prediction appears to contradict the staff's own finding that "inventories fell substantially, reaching levels that suggest near completion of the inventory adjustment cycle."

Transmission of the effects of monetary policy is currently obstructed by the difficulties of the financial sector. During our last consultation discussion on Japan, when we spoke about the grave condition of the banking sector, that topic had not yet been fully exposed to glasnost in Japan itself. The current staff report speaks of "concern about the health of the financial system," but there is still some uncertainty about the seriousness of the illness and even about its causes. At that discussion, I quoted some estimates of reserve coverage and their possible impact on the health of the major banks; I would appreciate staff comment on whether these numbers now seem pessimistic. In any event, one indicator of the extent of potential bank losses is the increase in the spread between deposit rates and lending rates.

In fact, this has also decreased the effectiveness of interest rate reduction as a direct stimulus to real investment and growth.

As to the external sector balance, the recent salvos fired westward across the Pacific have once more demonstrated the great political sensitivity of this economic issue. The current account surplus, specifically the trade surplus, is a matter of serious concern to some countries, although not to those who have recently experienced the largest increases in their trade deficits vis-à-vis Japan. The staff's analysis of this problem seems closest to the mark: namely, that the existing current account imbalances between Japan and other industrial countries are mainly the result of diverging macroeconomic development and the J-curve effect of exchange rate movements. Even though some structural rigidities may also have contributed to Japan's surplus, their effect is small: unless the underlying macroeconomic factors are addressed, little will be achieved in terms of more balanced trade results. These findings are also confirmed by the recent IMF Working Paper, "Revisiting Japan's External Adjustment Since 1985." I therefore fully share the Japanese authorities' concern over the growing pressure from abroad in favor of managed trade arrangements, and I understand their rejection of arrangements aimed at fixing market shares. The only viable solution to the so-called problem of bilateral external imbalances is for Japan's trading partners, as well as Japan, to adopt sound macroeconomic policies addressing their own domestic imbalances, and for all participants to seek energetically to advance the cause of multilateral trade liberalization.

Mr. Geethakrishnan made the following statement:

In all recent discussions on the Japanese economy there have been sharp differences of view on the basic question of whether or not the deep recession has bottomed out. The broad agreement in the staff's assessment and Mr. Fukui's statement that the recession has indeed bottomed out and that the recovery process has begun thus provides welcome relief. Signs of recovery have become clearly visible, including the continued rise in the composite index of leading economic indicators and the resumption in the expansion in money supply, reflecting rising confidence.

All this has been possible because of a prudent mix of monetary easing and fiscal stimulus, and the authorities deserve to be commended for the bold policy actions taken to break the back of the deepest recession Japan has faced since the first oil crisis.

There is a perception that despite the depth and severity of the recession, in Japan there has been no undue worsening in the unemployment situation as in many other industrial nations. Instead, Japan has been able to maintain near full employment.

This raises questions. Can the recovery and its expected strengthening lead to excess pressure on the labor market and consequent overheating? Or can the recovery be anchored to potential productivity gains, and if so, what features of past performance, especially in the buildup of capital stock and its modernization, could support such a productivity gain? Indeed, one notes the massive investment by business during the Tokyo stock boom period that ended in 1990. Are there characteristics in this apparent overcapacity that could support higher productivity and higher output growth? In any event, we suspect that concealed behind the statistics on employment there has been considerable slack created through shorter hours of work and other similar features. Staff comment on this point would be welcome.

Another area of concern is the level of corporate profits, which remains depressed. One forecast suggests that after falling by an estimated 3 percent in 1992, private capital investment could decline by twice as much in 1993. This, of course will be a serious setback. What is the extent of this risk to the incipient recovery? On the positive side, companies are getting at least some relief from the recovery in the value of their substantial equity holdings and through accelerated depreciation allowance. I am encouraged by Mr. Fukui's suggestion that the period of massive adjustment in capital stock is over and that companies should start reinvesting once again.

Both Mr. Fukui and the staff have stressed the role of fiscal stimulus in the management of the recession. Both have also underlined the fact that this cannot be a continuing process and that fiscal consolidation should begin soon. I wonder whether, in the staff's view, any further fiscal stimulus is necessary or whether the time is ripe for the fiscal consolidation effort to begin straightaway.

Both the staff and Mr. Fukui have argued against managed trading arrangements as a tool for adjusting the increasing trade surpluses. The concept of managed trade runs counter to the concepts of deregulation and integration of the global economy. This chair firmly believes that the solution lies instead in faster economic growth.

As the staff report has brought out, Japan has emerged as the largest provider of nonmilitary assistance--about $50 billion during 1988-92. Moreover, it has announced its decision to increase official development assistance by 50 percent to $75 billion in the period 1993-97. Japan has also substantially stepped up its direct investment in developing countries, thereby contributing to substantial employment generation in those countries. All this has taken place at a time when Japan has had its own share of political problems and was going through the worst

> recession in its recent past. This not only reflects Japan's confidence in the strength of its recovery but also its abiding commitment to the cause of the developing countries. For this, the Japanese authorities deserve the unreserved appreciation of the developing countries.

The Deputy Director of the Central Asia Department said that clearly the staff's forecasts had been off the mark in 1992. Like most forecasters, the staff had missed the downturn, the severity of the stock adjustment, and the impact of the bursting of the asset bubble on consumer confidence. Nonetheless, in retrospect, he doubted that the substance of the staff's policy recommendations would have changed significantly. If the severity of the recession had been known, for example, the staff would have urged earlier fiscal action. Nonetheless, he doubted that the authorities could be faulted for not having moved more quickly, especially as experience in most countries showed that it was difficult to initiate fiscal adjustment in a short period of time.

As to the staff's scenario for 1993, prospects of 1 percent growth were by no means rosy, the Deputy Director remarked. The recovery would be slow; with the economy operating nearly 4 percent below full capacity, a potential growth rate of over 3 percent meant that the gap between potential and actual output would continue to widen. Stronger domestic demand and a reduced contribution from external demand were forecast owing to the appreciation of the exchange rate, by 20 percent in real terms, which could be expected to have a pronounced impact. In sum, when an economy was at the bottom of a trough, it was difficult to persuasively argue that a recovery was around the corner unless one was willing to accept that the reversal of some of the factors that had been responsible for the downturn would contribute to an automatic adjustment of the economy. In the case of Japan, a sharp increase in capital accumulation in the late 1980s had raised the capital output ratio well above trend, and in the past few years, that ratio had declined closer to normal levels. Moreover, overconsumption in the late 1980s had meant the purchase of large stocks of durable goods. The recession had depleted that stock. Equity prices, which had dropped sharply, had recovered over the past half year or so. Interest rates, which had been raised to tighten monetary policy and stop the growth of the asset bubble, had subsequently been reduced in steps and were currently at an all-time low. Public investment, as a result of the past two fiscal stimulus packages, was currently increasing at an annual rate of 30 percent. The housing cycle had reversed itself. And, the leading indicators supported the conclusion that the adjustment process was effecting a reversal of the downturn.

While it was true that there was not yet evidence of strong recovery, the staff was basing its forecast on the analysis of the abovementioned factors, the Deputy Director continued. The staff did not believe that the Japanese economy was so unusual that there would not be any automaticity in its adjustment and a return to full equilibrium without sustained and continuous fiscal stimulus. There was uncertainty. Exchange rate appreciation had made recovery more difficult. Moreover, the staff might have underestimated the extent of the decline in the capital output ratio. Indeed, the recovery might be weaker. If the economic situation turned out to be weaker than anticipated, the staff's policy prescriptions would be different: it would see more need for another fiscal package and more stimulus. At the current stage, the staff did not see such a need. Moreover, in its analysis, the staff had tried to put Japan in the context of international economy: it had emphasized that the most important contribution Japan could make to the world economy was sustained noninflationary growth and opening its markets. If there was any disagreement with the authorities, it was on specific policies to achieve those objectives.

The issue of the current account surplus had, in the staff's view, been linked too closely to trade issues, making an assessment of its impact more difficult, the Deputy Director observed. In that regard, it was useful to separate the short term from the medium term. Japan's current account surplus had been cited as a major drag on the world economy. That was not true: it was the recession in Japan that had acted as a drag. That was an important distinction. Moreover, it was not correct to characterize the drag as "major." If the Japanese economy were returned--through whatever policies--to full capacity, the impact on growth in the United States and other industrial countries would be 1/10 of 1 percent. Those estimates were, of course, subject to variations, but most studies were in that range.

His statement that the drag was due to the recession was based on the experience of the late-1980s, which confirmed that macroeconomic policies could bring down current account surplus, the Deputy Director explained. The delay in adjusting monetary and, to some extent, fiscal policy had indeed resulted in the bubble years and a reduction in the current account surplus to 1 1/4 percent of GDP. However, the conclusion the staff had drawn from that experience was that its repetition was not desirable. Japan's current problems were directly related to that period. Had more conservative financial policies been followed, the economy might have had a softer landing, and many of the problems that Japan was currently facing, including the increase in the cyclical component of the current account surplus, could have been avoided. The staff therefore considered that the fiscal stimulus in the pipeline was needed and that there was more room for easing monetary policy.

The staff believed that in the short term, financial policies could support the recovery, that the cyclical component of the surplus would be eliminated, and that the current account would gradually decline to 2-2 1/2 percent, the Deputy Director stated. He would emphasize, however, that it was difficult to forecast the level of the current account, and he would not like to put so much emphasis on a specific figure. Japan had an overall savings rate of 30 percent and an investment rate of 33 percent. Small shifts in investment and saving, which were difficult to predict, would mean a large shift in the current account. Consequently, the staff was uncomfortable with the idea of setting a magical target for the longer-term current account surplus.

As to the medium term, the staff could not agree with some of the comments of Mr. Dawson and Mr. Landau on the overall surplus, the Deputy Director remarked. In the staff's view, whatever the merits of stimulating consumption in the short term in a period of recession, over the longer term the best way to generate growth was to increase savings. In view of the established need for global savings over the medium term, it would not be appropriate for Japan to reduce savings through sustained fiscal stimulus. In discussing the link between savings and growth, he would recall the findings of a 1980s study by Lawrence Summers, which were still valid: "A result that the gap in U.S./Japan saving rates is high and increasing is troubling. Unless policy makers urgently address the issue of low American saving, American real economic growth may continue to lag behind Japan's.... Under the lingering influence of Keynes' concern about stagnation due to oversaving has perhaps had more influence on national attitudes towards savings in the U.S. and U.K. than in Japan or continental Europe." The growth gap could, of course, be closed by reducing savings and growth in Japan, but that would not be desirable. Against that background, the best medium-term strategy for Japan would be to maintain a high saving rate by pursuing prudent fiscal policy. As Mr. Summers had concluded,

> ...it is necessary to consider whether increases in public savings to raise national savings might have adverse consequences which would make them infeasible. An obvious risk is the Keynesian fear that increases in public savings will lead to stagnation due to insufficient aggregate demand. Whatever are the merits of this argument in the context of the post-depression period, the fear of excessive savings is not an important one today. Any reductions in demand due to increased government savings can easily be offset by expansionary monetary policies.

In response to Mr. Abbott, the Deputy Director explained that while the citation referred to a specific country, the analysis underlying the statement was of a general nature, and did not rely on the empirical data of a specific country. In that sense, the staff endorsed the general import of that analysis for Japan.

It had been argued that the best way to cope with the problem of an aging population in Japan was to raise public investment and thereby reduce the current account surplus, the Deputy Director recalled. Again, the appropriate level of investment and its composition--public and private--was an important issue that needed to be considered on its own merits and not from the point of view of attaining a given current account target. It should be noted that the private investment/GDP ratio in Japan was about 30 percent, the highest among industrial countries. The public investment/GDP ratio, also at about 30 percent, was likewise the highest among industrial countries. There were recognized deficiencies in many areas of social services that justified a high level of public investment, but there were limits to increasing public investment without incurring inefficiencies and wasting public funds. Over the past two years, public investment had increased by about 30 percent in real terms. Clearly, such a pace could not be sustained.

In meeting the prospective costs of a rapidly aging population, what mattered most was that funds were invested in the highest-yielding alternative available, whether in physical structure or financial assets, whether by the private sector or public sector, or whether in the domestic economy or abroad, the Deputy Director continued. Ultimately, the Government's accumulation of financial assets was only a veil for the accumulation of physical assets. Government savings were in essence injected into the domestic and global pool of savings. Thus, the Government's social security surpluses were used in part to buy back government debt from the public, thereby freeing up financial resources in the private sector, which could then redeploy those funds to their best alternative use. The fact that the private sector had increasingly invested abroad reflected both the enhanced availability of funds and the perception that the marginal return on capital deployed abroad was at least as great as that on investment at home. In the event that the funds being accumulated to meet future costs associated with an aging of population were allocated to their most productive and highest return use, they would ultimately help meet the costs associated with an aging population.

In the staff's view, it would be inappropriate to set an arbitrary target for public investment based on a target of current account surplus, the Deputy Director stated. Good governance dictated that public projects should be based on careful cost/benefit analysis, not on a current account target. There might be some flexibility in accelerating or delaying projects on cyclical considerations in the short term, but such flexibility should be exercised judiciously to avoid the fiscal problem currently being incurred by many industrial countries.

The pattern of aging itself actually could be projected reasonably accurately, but its impact on investment, saving, structural private and public savings and investment was more difficult to assess, the Deputy Director observed. The staff's simulations therefore were intended to provide only a benchmark. As the issue was an important one, it was prudent to keep it under review.

As to Mr. Smee's question of why was Japan different, it should be noted that the problem of aging was more abrupt for Japan than for other industrial countries, the Deputy Director of the Central Asia remarked. At the same time, the Japanese authorities had taken a medium-term view of the issue--an approach the staff would encourage.

Mr. Landau, recalling the staff's observation that during the mid-1980s, macroeconomic policy had contributed to reducing the current account surplus but had also had undesirable effects, including the asset bubble, commented that one should perhaps distinguish two phases in that process. First, fiscal stimulus had by the mid-1980s reduced the current account surplus; and, second, the subsequent relaxation of monetary policy had produced a bubble. Aggregating those two phases yielded a poor picture of what really happened to the Japanese economy, and was relevant to future policy prescriptions in the event that further stimulus appeared necessary. In any event, such stimulus should be provided by fiscal, rather than monetary, action. In his view, attributing the overall difficulties of the bubble economy to the fiscal stimulus of the mid-1980s was somewhat misleading.

Mr. Abbott said that he supported Mr. Landau's view. The sequence of events ought to be examined more carefully. Specifically, the fiscal consolidation in the 1980s took off during the bubble period, when rapid progress was made in bringing down the fiscal deficit. As in other countries, progress in fiscal adjustment was easier in an environment of good growth. Clearly, the fiscal policy approach had not led to subsequent problems and the large increase in the current account surplus in the late-1980s. If there was a problem in policy balance, it was on the monetary side.

He had found several of the staff's remarks disturbing, Mr. Abbott stated. The first was that was that even with a more accurate forecast for 1992, the staff would not have changed its policy advice. It had been his chair's concern for some time that the staff's policy advice was completely independent of Japan's economic performance. It was the same old prescription, and it was unhelpful to Japan as well as to the rest of the world. It was also not what members were looking for in terms of the sort of surveillance function that the Fund should play.

While the staff was experienced and knowledgeable, and entitled to its own view of the relative importance of current account balances, it should be looking at what the heads of government of major shareholders of the organization had said recently in that regard, Mr. Abbott considered. Adjusting current account imbalances was an important objective of the Group of Seven. It was also an important objective of bilateral arrangements between the United States and Japan. For the staff to repeatedly say that Japan's current account surplus was, in its view, a matter of indifference was unacceptable. Moreover, a number of Directors had suggested that there were problems beyond those mentioned in the staff report. It was true that by fiddling around with macroeconomic policy, one could achieve a current account adjustment. In the presence of residual trade problems, however, the usual macroeconomic measures could compound, or leave unchanged, distortions that needed to be addressed.

He considered it inappropriate to quote Mr. Summers's conclusions regarding policies that the United States ought to follow with respect to savings in the context of the consultation discussion on Japan, Mr. Abbott said. While Mr. Summer was precisely right with respect to the policy the United States ought to follow and was trying to follow at the moment, to offer that view as a generalization was simply wrong. Indeed, the staff's economic presentation was slightly bizarre, stressing as it did that maximizing savings was the objective of economic policy. In more standard economics, maximizing the present value of intertemporal consumption was supposed to be the objective. That was not the same as maximizing savings. In his view, the staff ought to refocus its thinking on that issue much more clearly than had been reflected in the current discussion.

Mr. Schoenberg stated that he supported Mr. Abbott insofar as he himself was also somewhat dissatisfied with the staff's one-sided description of the saving investment ratio in Japan. There was no doubt that in the long term, a high investment ratio supported growth, but that was not the issue in Japan's current circumstances. Rather, the question was: why was the investment ratio so high? Moreover, he found it remarkable that the staff had not said anything about the market access problem in Japan.

Although it was true that Japan was facing a severe problem with an aging population, other countries were experiencing a similar problem, perhaps not as severe as in Japan, but serious, nonetheless, Mr. Schoenberg observed. If that justified a high current account surplus for Japan, then other countries would at least need to achieve a modest current account surplus--and that could not work.

Mr. Posthumus remarked that he could not understand why a particular group of members, however large and powerful, should have the right to prescribe to the staff how it should analyze economic policies. That would be a wholly unwelcome way to conduct Fund surveillance. The staff provided similar analysis and advice to all of 175 members of the Fund, many of whom do not agree at all with the staff's conclusions.

The Chairman said that it was the work and the mission of the staff to offer its best judgment and analysis. It was the job of the Executive Board to make a final judgment and to adopt, if needed, a given prescription, as it was doing at present.

Mr. Peretz remarked that he agreed with much of what Mr. Landau had said, but he suspected that the real problem after 1987 was not the loosening of monetary policy in 1987, but the failure to tighten it up again quickly enough once the boom got under way. Indeed, that had been a common mistake among a number of industrial countries, including the United Kingdom, the United States, Japan, and possibly Canada.

He would note, in response to Mr. Schoenberg's observation that all industrial countries had problems with aging populations, the occasional paper issued in September 1986 on "Aging and Social Expenditure in the Major Industrial Countries, 1980-2025." Drawing on the fact that in Japan, the population was aging more sharply than in other countries, the staff had presented some calculations on the projected impact of aging on the current account. The paper appeared to provide an explanation both of Japan's current account surplus and of the underlying current account surplus in recent years, as well as some reasonable prediction that the surplus would disappear in the longer term. Perhaps that analysis, which concluded that the surplus had nothing to do with the current cyclical position but was a medium-term issue, needed to be revisited.

He wished to state that if Japanese investors wished to invest abroad rather than in Japan, he would defend their right to do so, Mr. Peretz concluded.

Mr. Smee said that he wished to clarify that he had not meant to suggest that there should be some target level for the current account. He fully recognized that at any given moment, different countries had different equilibrium levels of their current account balance. As Mr. Peretz had mentioned, the level could be related to demographics; the impact of the aging of the population had current account implications. Rather, he was interested in the staff's observation that there were grey practices--for example, with respect to regulation, market access, and distribution--that had a price impact. He would be interested to know the extent of that price impact, which had implications for assessing the appropriateness of the level of the current account.

Mr. Wei stated that he associated himself with Mr. Posthumus's remarks. The staff should be encouraged to speak out on all issues based on its professionalism and economic knowledge. As to Japan's current account surplus, while the issue was understandably of particular importance in Japan-U.S. trade relations, it should, in his view, be considered in a broader, multilateral context.

Mr. Fukui, commenting on the issue of market access, said that there was no longer any official regulation in terms of tariff or nontariff barriers. The issue was grey areas and how to deal with them. That was an important issue, but one that was difficult to stipulate. He appreciated the staff's efforts in that regard, including its recent study on keiretsu in Japan, and he encouraged the staff to continue its efforts in those gray areas. At the same time, studies conducted in Japan and the United States indicated that clearing up those grey areas could help reduce the trade surplus. Other studies indicated that by clearing up the grey areas, the Japanese economy would become more efficient and the current account surplus would increase.

The Chairman observed that Mr. Fukui's statement that eliminating the grey area would lead to growing surpluses was indeed provocative. He imagined that other Directors might argue that its elimination would certainly lead not only to more efficiency, but also to a higher quality growth and living standards in Japan compatible with reduced current account surpluses. The issue was, of course, open to further discussion.

The Deputy Director of the Central Asia Department, commenting on market access, remarked that the staff had been unequivocal in seeking and supporting all action to remove all identifiable barriers. As to grey areas, their impact was difficult to quantify, as Mr. Fukui had mentioned. It was true that their elimination could result in a higher levels of imports and exports, but as the Chairman had indicated, the impact might not necessarily lead in the direction of a sizable decrease in the current account surplus.

As to the debate on the course of policy in the 1980s, he wished to add two points, the Deputy Director continued. One lesson to be drawn was that the relationship between fiscal policy and the current account surplus was not unidimensional. As Mr. Abbott had observed, during that period there had been a strong fiscal consolidation as well as a sharp decline in the surplus. He would not conclude that by reducing the current account surplus, one could effect a sharp fiscal consolidation. In the short term, to link macroeconomic policies to the current account could give perverse results because of numerous other factors, in Japan as well as in other countries.

The second point was that the sequence of policies was not always easy to trace, but in the earlier part of the bubble, fiscal policy was expansionary ex ante, the Deputy Director remarked. Monetary policy was also excessively relaxed. As the bubble economy evolved, revenue rose much faster than anyone could have expected. Consequently, a period of rapid fiscal consolidation followed. But if one believed that some fiscal stimulus in the short term was necessary to support recovery, it followed that when the economy was already 1-1.5 percent above potential, the fiscal stimulation should be withdrawn. In fact, at that stage, the authorities had not acted quickly enough to tighten monetary policy and withdraw fiscal stimulus. He accepted that most of the responsibility for the bubble economy could be put on monetary policy, rather than on fiscal policy.

The issue of whether to maximize savings or consumption was a difficult one, the Deputy Director observed. The objective in the present instance was to maximize long-term consumption. Excessive saving could reach a point where there was so much capital stock, that what was given up in immediate consumption generated less output and consumption in the future. At that point, there was a need to cut back savings. But Japan was not at that point, and certainly the world was not at that point. Even if Japan were close to that point, its additional savings would be welcomed to push world growth to a higher level by financing investment in other countries.

As to intergenerational issues, in recent history, every generation had been better off than the previous one, the Deputy Director commented. On that basis, one could ask: why should the current generation save more for the coming generation to live better? And, what was the social rate of discount? The staff would not wish to debate such deep issues. The important point was that Japan's fiscal position relative to other countries and the current level of savings was sufficient to justify providing fiscal stimulus in the short term. Over the medium term, the staff saw a gradual decline in savings and therefore did not see the need for any measures to accelerate that process. It would prefer not to interfere in that process through specific measures to reduce the saving rate.

Mr. Al-Jasser said that he wanted to pursue further the staff's observation that experience with fiscal consolidation and external correction in the 1980s showed that there was not, a priori, a relationship between fiscal expansion and rising deficits, and output contraction and the external accounts. He would conclude from that observation that the stance of policy should be based on an assessment of where the economy was headed rather than on any rule of thumb. In his view, based on current trends, a repeat of the investment boom could not be expected. In the 1980s, investment as a share of GNP had reached extremely high levels, whereas in current circumstance, investment was unlikely to achieve such levels in the period ahead. Moreover, the high rate of private savings was expected to be sustained and perhaps even increase.

He had mentioned his perplexity about the staff's advice on consumption, namely, that "in a longer-term perspective a change in the tax structure, putting less weight on income tax and more on consumption tax, would also be desirable," Mr. Al-Jasser recalled. Taken with the staff's indication that it would not recommend implementing policies that affected income distribution, and its statement on the desirability of maximizing long-term consumption, he could not see how that could be achieved by changing the tax structure in a manner that would lower consumption, especially in an economy with a high savings rate. For most developing countries with a high consumption rate, the staff usually advised changing the tax structure so as to induce higher saving and lower consumption. That advice did not appear to be applicable in the case of Japan, especially during a period of recession.

Mr. Posthumus made the following statement:

> I am in broad agreement with the analysis set out in the staff report. The current recession is indeed mainly a reaction to the exceptional period of the "bubble economy," which created some features that make the precise timing and strength of the recovery projected for the second half of 1993 more uncertain than usual. The better than expected growth performance in the first quarter of 1993, following three consecutive quarters of negative growth, suggests that recovery is in the making, although the economy may be crawling along the bottom for the moment. The supplementary paper notes some weakness in macroeconomic indicators in April-May. It is not certain whether the required recovery of private expenditure will soon materialize. In this respect, the first-ever decline of bonuses this summer--by -1.14 percent year-on-year--may keep private consumption depressed. Surveys indicate a further drop in private investment in 1993 to which the recent sharp yen appreciation may add.
>
> According to the staff, at this juncture the macroeconomic policy approach should continue to be directed at averting the

risk of a protracted recession. It seems to me that the Japanese authorities have already gone a long way in doing this. More fine-tuning--which appears not to be ruled out by the staff--prompts questions on the danger of procyclical effects and on the consistency with the medium-term orientation of policy. As the authorities note, in virtually all recessions during the past two decades, the stimulative measures introduced in response to domestic and international concerns have turned out to be excessive. In view of the reduction of potential growth, signaled by the staff, from the 4 percent pace observed during the 1980s to about 3.2 percent, the point of excessive stimulus may be reached even earlier than in the past. Thus, the recovery will of necessity be less forceful than in earlier periods of recovery. As the Economic Counsellor said at our informal session last week, *this is not a negative thing. It would be preferable if* medium-term growth was closer to potential growth than the rate projected by the staff.

The staff suggests that further monetary easing deserves careful consideration, because the sharp yen appreciation adversely affects the short-run outlook for recovery and additionally eases already weak inflationary pressures. I, too, consider the recent rise of the value of the yen to be too rapid. However, real interest rates have dropped well below the levels reached in the 1986-87 downturn, and the supplementary paper shows money growth already recovering somewhat. Therefore, I would prefer a more cautious attitude than the staff suggests, with no further monetary easing barring a real relapse of a broader range of indicators, in conformity with the attitude of the Bank of Japan.

Regarding fiscal policy, I agree with the staff that no further change is required at this point. By strengthening the limited effect of automatic stabilizers through two substantial discretionary budgetary packages within a half year, the authorities have already stretched the role that fiscal policy can play in stabilizing activity. It is only natural that the effects of both stimulus packages are closely monitored before any new actions are considered, especially since approximately one half of the public investment from the first package unintentionally spilled into the early part of FY 1993, and spillover effects are again expected into 1994. The staff keeps the door to a third stimulus package open. The staff's remarks that care should be taken to avoid excessive use of fiscal policy as a countercyclical instrument should have been applied to its own policy advice. Aside from the risk of an undesirable procyclical stimulus, I consider the room for further fiscal stimulus to be limited. The general government deficit, excluding social security, will already rise to 3 percent of GDP in FY 1993, from approximate equilibrium in FY 1990. Gross government debt still amounted to

69 percent of GDP in 1992, a heritage from lax fiscal policies in the 1970s; as Mr. Fukui has pointed out, the assets of the social security system do not reduce the burden of this debt. For this reason, resumption of fiscal consolidation once the recovery is firmly established, as the staff advises, is certainly necessary.

The projected reduction of the current account surplus to 2 percent of GDP in 1998 looks uncertain, especially as it depends on possibly too high medium-term growth figures. Nevertheless, I fully agree with staff that the level of the current account surplus should not be a target that diverts macroeconomic and structural policies away from the objective of sustainable growth with low inflation and free trade. As perfect stabilization policies are impossible, it is inevitable that cyclical factors from time to time add to, or subtract from, the surplus. This should not give rise to an increase in protectionist pressures. If it does, on the basis of wrong perceptions of the nature of the surplus, Fund advice should aim at correcting such perceptions, rather than at pushing countercyclical policies beyond their limits. Setting targets for specific components of the current account, without analyzing and correcting possible underlying market imperfections, is equally undesirable. I fully concur with the staff's and the Japanese authorities' objections to managed trade. Mr. Dawson now calls this unmanaged trade, which is a hopeful sign. In saying this, I would also stress that I agree with the staff that Japan should firmly embark on a program of deregulation of heavily regulated markets. Regardless of the effect on the current account, this would benefit Japanese consumers as well as domestic and foreign producers. I wish the Japanese authorities strength in their international coordination endeavors.

Mr. Glazkov made the following statement:

At this stage of the discussion I will limit myself to brief remarks on the major aspects of Japan's economic performance and policies.

On the primary issue of fiscal support measures, I share the staff's broad agreement with the size and composition of the fiscal packages as well as with the incremental approach that has been adopted by the authorities. The latter provides necessary flexibility, which is crucial in view of the recent mixed fiscal performance of Japan. It is also important to be aware of the fact that a significantly larger increase in public expenditure can be accompanied by waste and inefficiencies.

The multiple task mentioned by Mr. Fukui--"adapting to the rapidly aging society, while maintaining sustainable growth without inflation"--is indeed formidable. In the face of a huge debt burden, successful implementation requires maintaining a delicate balance between the extremely difficult budgetary situation and the necessary fiscal stimulus to the economy.

On monetary policy, it is difficult to add anything to what has already been said. I would only stress, in line with the staff appraisal, that, notwithstanding the room created by the appreciation of the yen for further reducing interest rates, the monetary authorities should stand ready to adjust rates upward "once the recovery is firmly established," especially taking into account lessons of the past, as rightly mentioned by Mr. Peretz.

On financial sector issues, I would urge the authorities to be consistent in their approach to addressing the problems of the financial system, namely, by leaving the sector to earn its way out of its present difficulties without an infusion of public resources. The best way to help the financial institutions is to implement promptly the reform plans designed to create a more efficient, competitive, and transparent financial system.

The authorities' position regarding the dangers of the possibility of excessive risk-taking by the banks seems to be consistent with this approach. As with other problems of the financial sector, the ultimate task is to maintain--difficult although it may be--a balance between state support on the one hand and state regulation and supervision of financial institutions on the other.

Concerning trade balance disputes, I agree with Mr. Fukui that "the effect of the short-term stimulation economic policy on the trade surplus is limited in its impact and duration," and I share his doubt about the prudence of a policy that puts too much emphasis on fiscal measures to tackle the surplus.

I also share the authorities' concern about the growing pressure from abroad for managed trade arrangements. I agree with the staff that such arrangements would undermine free multilateral trade and result in price rises, and that they will by no means be effective in providing a sustainable reduction of current account imbalances.

I was, however, somewhat disappointed with the modest scale of structural measures aimed at addressing the underlying causes of the imbalances, and I share the concerns expressed by Mr. Schoenberg and others in this regard. Leaving aside the sensitive issue of opening up the rice market, the rules and regulations in certain sectors--particularly distribution and transportation--complicate market access and contribute to significant price differentials between Japan and other countries. According to some estimates, regulation and protection in the service industries have allowed Japanese companies to be about one half as productive as their American counterparts. In the area of construction, it is not just that foreign companies virtually get no contracts: restrictive regulations stifle one of the economy's biggest potential areas for consumption and imports. The situation is exacerbated by the complexity and lack of clarity of the rules and regulations. I therefore agree with the staff that, notwithstanding the authorities' efforts to date, substan-tial scope remains for more deregulation. The latter would have the multiple effect of reducing prices, raising productivity and income, and facilitating market access of both domestic and foreign economic agents.

I agree that it is not easy to measure the overall effect of market opening and deregulation on the current account, especially to take into account the rise in efficiency and competitiveness that are expected to result. It is perhaps more difficult to measure their effect in the long term, but for the short term, which is important at present, market opening and deregulation could, in my view, be expected to contribute positively to resolving the problem of the current account.

I concur with the authorities' view, which I believe is shared by the staff, that Japan would be the biggest loser from the failure of the Uruguay Round. The freedom of world trade has been a cornerstone of Japan's economic success. In this light, and notwithstanding the role of other countries in this process, it is in Japan's best interests to proceed, without delay, in making its contribution to the trade liberalization process.

Concerning development assistance, I welcome the authorities' endeavor to substantially increase the volume of foreign aid commensurate with Japan's position in the world economy.

Today, Japan is, as usual, the focus of the world's attention. The reasons for this attention, however, are somewhat different from the traditional ones. Many economists are speculating about whether Japan's economic miracle has ended and the country has entered into the period of maturity, with all its attendant diseases.

I do not believe that there is a simple answer to this question. The previous phase of fast growth is certainly over. The challenges facing Japan now are, to a great extent, different from those it faced earlier and, consequently, the set of measures required to address them is different. While Japan has managed economic renewal, strengthening its economy in response to the shocks of the past, the question is whether a similar response is possible now, when substantially more fundamental changes seem to be called for to address present and--even more--future difficulties. The emergence of new, higher living standard requirements is under way. For a number of reasons, the traditional employment system is likely to disappear forever. Moreover, the sociopolitical consensus that served as the basis of Japan's specific economic model and pace of growth is probably breaking down.

Nevertheless, the outlook for the medium term is, in my view, not bad at all. Perhaps it is too early to say that recovery is already on track, but many factors are now in place that are likely to sustain Japan's strong pace of growth. In the event that the Japanese authorities manage to undertake the necessary set of measures--many of which are presented in the staff report--and if, in particular, structural reforms are more consistent and forward looking, Japan can be expected to continue to outperform most major industrial economies.

Mr. Ferrillo made the following statement:

Japan is going through a downswing whose depth and length were substantially underestimated, not only by the Japanese Government, but also by the staff in last year's Article IV report and in our recent world economic outlook discussion. The sluggishness of macroeconomic indicators in April-May shows clearly that the onset of an upturn was initially overestimated. I am afraid that one blossom on a cherry tree does not make spring.

Having said that, I will not plead for further fiscal expansion at this point. Past experience in Japan and elsewhere points out that discretionary expansionary policies often come too late and have procyclical effects. As the staff has correctly stressed, last year's fiscal stimulus package would have better suited cyclical needs if no considerable political delays had occurred.

The other question relating to the suitability of further fiscal stimulative measures is effectiveness. I believe that fiscal expansion, even on the proposed scale, cannot replace private spending and investment without running into structural fiscal problems. Most worrisome are the still poor prospects for a revival in private sector activity. The upward movement of leading economic indicators is largely due to a fiscally induced rise in housing starts. Retail sales have picked up only slightly as consumer confidence is not yet restored. But the most important element--capital investment--is still slow, and profits are still falling.

In fact, several factors impede a quick recovery of private investment. Excessive credit creation in the banking system in the 1980s led to overinflated asset prices. With the collapse of the "bubble economy," households and firms have been faced with a rapid decline in asset values and have been forced to restructure their balance sheets. The restructuring and consolidation phase, however, is still under way. Despite large corrections, stocks still appear overvalued in the light of economic fundamentals, as the Government has stepped into the market as a major buyer. Another factor adversely influencing the investment environment is the fact that banks will have to impose higher margins on credit in view of their huge bulk of nonperforming assets, their need for higher reserves, and the increase of the risk premium.

Moreover, the staff seems to underestimate the fact that Japanese firms will face growing, rather than falling, capital costs in the next few years, for two reasons. First, the emission of large amounts of bonds to finance investment projects is now subject to the Finance Ministry's approval, which so far has been difficult to obtain. Second, firms today are required to pay interest not only on new bond emissions, but also on old bonds, which were almost interest-free.

In sum, this chair would prefer to see the Japanese authorities pursue a medium-term strategy of fiscal consolidation, while working to eliminate the structural factors that led to the imbalances experienced in the 1980s. The fiscal stimulus packages are not jeopardizing Japan's fiscal position, which is by far the most comfortable among the Group of Seven industrial countries. However, further stimulus would certainly move Japan off its fiscal consolidation path for too long. In this context, the apparent divergence of views between the staff and Mr. Fukui on the fiscal situation is striking. Mr. Fukui notes that "the budgetary situation continues to be extremely difficult"; in contrast, the staff notes "a marked reduction in both gross and net public debt relative to GDP" but does not, in its appraisal, mention any problems concerning the debt burden and recommends further fiscal action. Could the staff comment on this divergence of views, which also determines the possible leeway for additional fiscal action?

As to the current account surplus, I continue to believe that the main instrument to bring down such surpluses is the exchange rate. The considerable appreciation of the yen over the last 12 months could reasonably be expected to lead to a reduction of the huge trade surplus. But economic adjustments caused by exchange rate shifts take a long time--more time, I am afraid, than politicians and government officials are willing to wait. Nevertheless, this should not prevent the Japanese authorities from intensifying their efforts toward market deregulation for the benefit of the world economy as well as for Japan.

Let me, at this point, elaborate on two other issues.

First, the staff report states that short-term economic forecasts are subject to a "greater degree of uncertainty than usual." Among these uncertainties, the ability of the weakened financial system to recover swiftly by tackling adequately nonperforming loans is a key element. According to official reports, nonperforming loans held by 21 major banks total ¥ 12.7 trillion, while the staff estimates that bad loans held by regional banks account for 6-7 percent of total loans. This compares with the average BIS capital adequacy ratio of 9.2 percent for all banks. What are the systemic risks accruing from an insufficient capital adequacy ratio for individual banks or bank categories? Are the stronger banks or the Cooperative Credit Purchasing Company ready to the absorb further bad loans or banks on the verge of bankruptcy?

The second issue concerns corporate alliances among members of keiretsu groupings, which are a major factor on the microeconomic side. Today, recession is putting these links under serious strain as companies are forced to rationalize and adjust to new structural conditions. I would appreciate some additional information about the impact of the recession on cross-shareholdings of keiretsus.

The Executive Directors agreed to continue their discussion in the afternoon.

DECISIONS TAKEN SINCE PREVIOUS BOARD MEETING

The following decisions were adopted by the Executive Board without meeting in the period between EBM/93/99 (7/14/93) and EBM/93/100 (7/16/93).

2. MALAWI - ENHANCED STRUCTURAL ADJUSTMENT FACILITY - EXTENSION OF ADDITIONAL ARRANGEMENT

The commitment period of the additional arrangement for Malawi under the enhanced structural adjustment facility (EBS/91/153, Sup. 1) is extended to March 31, 1994. (EBS/93/109, 7/7/93)

Decision No. 10422-(93/100), adopted
July 14, 1993

3. EXECUTIVE BOARD TRAVEL

Travel by Executive Directors and by an Advisor to Executive Director as set forth in EBAM/93/129 (7/13/93) is approved.

APPROVED: January 12, 1994

LEO VAN HOUTVEN
Secretary