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February 10, 1986

To: Members of the Executive Board

From: The Secretary

Subject: Japan - Staff Report for the 1985 Article IV Consultation

Attached for consideration by the Executive Directors is the staff report for the 1985 Article IV consultation with Japan, which has been tentatively scheduled for discussion on Monday, March 10, 1986.

Mr. B. Smith (ext. 7301) or Mr. Baumgartner (ext. 7307) is available to answer technical or factual questions relating to this paper prior to the Board discussion.

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JAPAN

Staff Report for the 1985 Article IV Consultation

Prepared by the Staff Representatives for the 1985 Consultation with Japan

Approved by P.R. Narvekar and C. David Finch

February 10, 1986

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I. Introduction

The 1985 Article IV consultation discussions were held in Tokyo during November 25-December 7, 1985. The principal Japanese representatives were the Vice Minister of Finance, the Governor of the Bank of Japan, and senior officials of the Ministries of Finance and International Trade and Industry, the Economic Planning Agency, and the Bank of Japan. The staff team consisted of Messrs. Narvekar, Smith, Baumgartner, Ariyoshi (all ASD), Watson (ETR) and Mahler (FAD) and Ms. Boyd (secretary, ETR). Mr. Fujino, Executive Director, was also present.

II. The Economic Upswing, 1983-85

Economic growth in Japan was strong for the third successive year in 1985, even though its momentum slackened over the course of the year. Growth, which had been sustained at over 5 percent at an annual rate between the first quarter of 1983 and the last quarter of 1984, fell to 4.5 percent in the first half of 1985 and further to 2.6 percent in the third quarter. Nevertheless, at 4.7 percent in the first three quarters compared with the previous year, growth was only slightly below that in 1984 (Chart 1). Industrial production, which had expanded at an annual rate of over 10 percent during 1983-84, decelerated sharply in the first half of 1985 and has stagnated in recent months.

The initial impetus to recovery came from a sharp rise in exports, and exports remained a driving force in 1984. In real terms, they rose at an annual rate of about 17 percent during 1983-84, owing to the strength of foreign demand, especially in the United States, and the ability of Japan's industry to respond vigorously to it. Net foreign demand contributed about one half of GNP growth in 1983; it remained important in 1984 but, with a recovery in domestic demand, its contribution fell to one fourth. Slowing domestic and net external demand both contributed to the slackening in growth in 1985.

Beginning in mid-1983 and continuing in 1984, domestic demand strengthened gradually. This was mainly due to a sharp increase in private investment in plant and equipment and a rebuilding of inventories. The rapid growth of exports, the associated strong recovery in profits, and the need to adapt production facilities to changing technology led to an investment boom beginning in mid-1983 and continuing through 1984. Investment remained robust in 1985, although its growth slackened somewhat. Profits weakened in 1985 in response to the slowdown in exports and manufacturing production, but remained favorable in most industries. While investment in the nonmanufacturing sector accelerated in 1985 and that in the transportation equipment and precision machinery industry remained buoyant, depressed market conditions for some electronic products, notably semiconductors, resulted in a sharp curtailment in investment in the electrical machinery industry.

Private consumption has been subdued during the upswing, its growth in fact declining from 4.1 percent in 1982 to 3.2 percent in 1983 and further to 2.9 percent in 1984, reflecting mainly only modest growth in real disposable incomes. Nominal earnings appear to have increased somewhat faster in 1985 than in 1984, but the effect on real disposable incomes has been offset by the re-emergence of fiscal drag, which had been reduced in 1984 because of a tax cut. As a result, growth in real private consumption stabilized in the first three quarters of 1985. Private residential investment turned upward in 1985, ending five years of decline. Government demand has stagnated throughout the period as public finances have been directed toward fiscal consolidation.

Employment has increased by 2.1 percent since early 1983, concentrated in manufacturing, especially in the expanding new and high-technology industries. However, the bias of the recovery toward industries with labor-saving technologies has contributed to the stickiness of unemployment. The unemployment rate, which rose to 2.8 percent in mid-1984, receded to 2.4 percent by early 1985, but rebounded as growth weakened in the second half of 1985, climbing to a historic high of 2.9 percent in November.

Wage developments, while having been a factor in keeping consumption weak, have been generally favorable for employment and investment. Both wage settlements for major corporations and the increases in bonuses recovered somewhat in 1984, but remained moderate in 1985 and bonuses have recently been less buoyant. Unit labor costs in manufacturing declined by 5 percent in 1984 but with the slowing in industrial production, this decline was partly reversed in 1985. Prices have been virtually stable during the upswing; consumer prices rose by about 2 percent in 1985 but wholesale prices fell slightly.

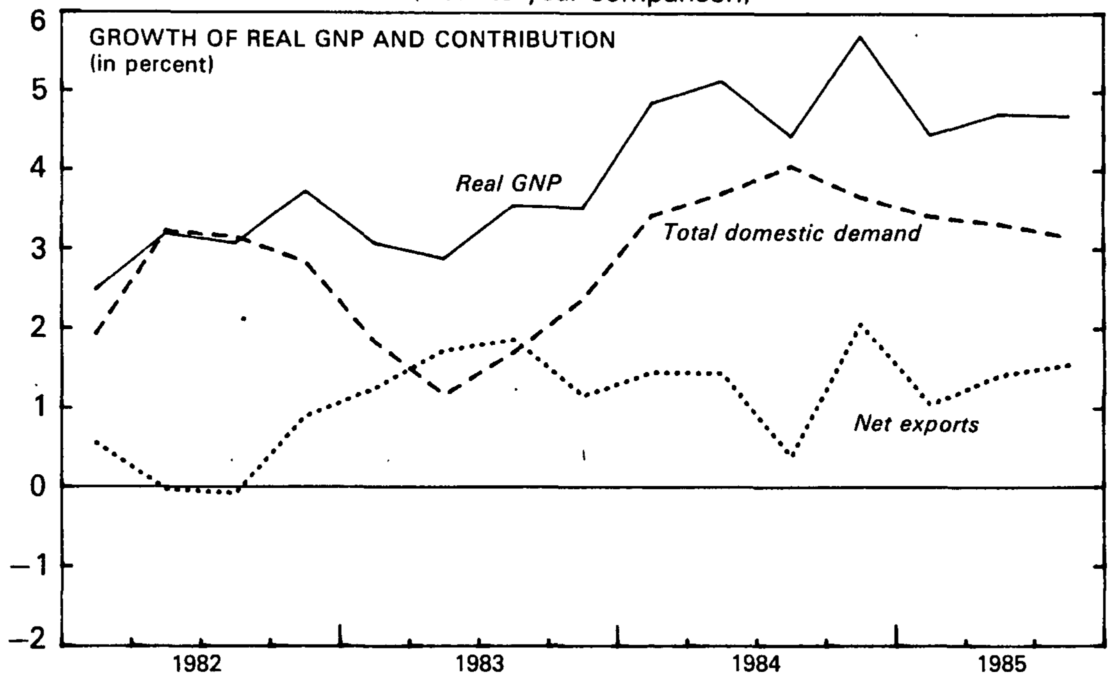
Fiscal deficits were reduced throughout the economic upswing. The deficit in the central government general account declined from 5.2 percent in 1982/83 (fiscal year beginning April 1) to 4.4 percent in 1984/85, as expenditure grew much more slowly than nominal GNP and revenue faster. The expenditure to GNP ratio declined from 17.4 percent in 1982/83 to 17.0 percent in each of the next two years, while the revenue to GNP ratio increased from 12.2 percent in 1982/83 to 12.6 percent in 1984/85. While interest payments, tax-related transfers to local government, defense, and foreign aid expenditure all increased more rapidly than nominal GNP during the 1982/83-1984/85 period, all other major categories of expenditure increased more slowly, with many

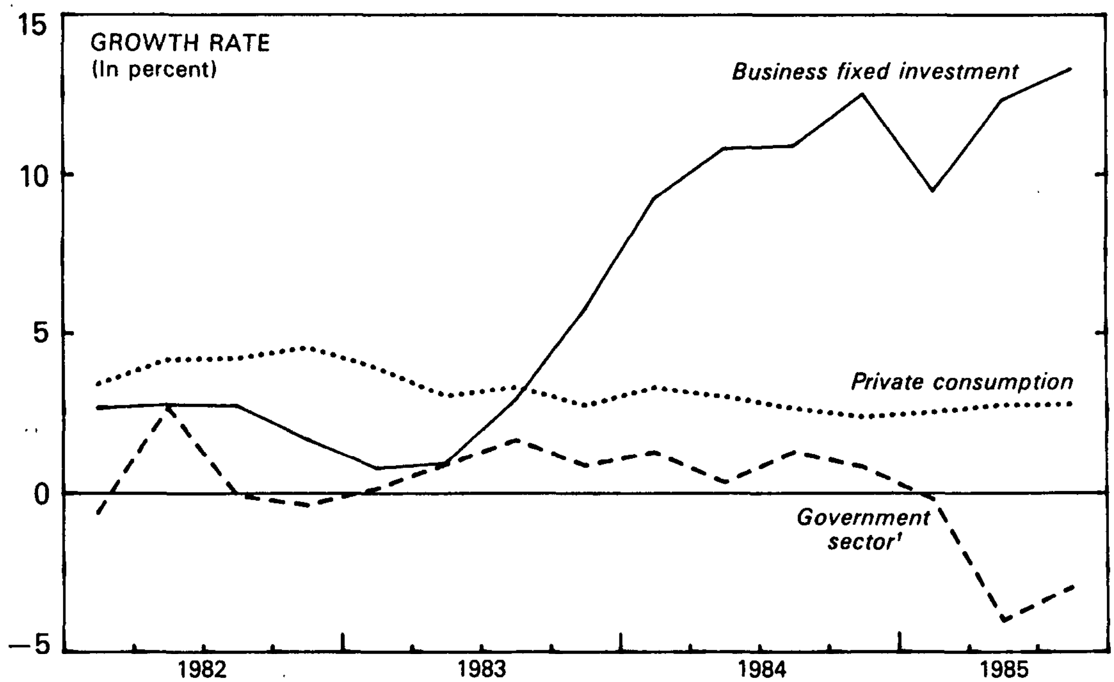
CHART 1

JAPAN

DEVELOPMENTS IN REAL GNP BY MAJOR AGGREGATES, 1982-85

(Year-to-year comparison)





Source: Data provided by the Economic Planning Agency.

[1]Begining in the second quarter of 1985, government sector demand was reduced and business fixed investment increased as a result of the privatization of Nippon Telephone and Telegraph and the Japan Tobacco and Salt Corporation.

not increasing at all. The increase in the revenue ratio was mainly the result of the relatively high income elasticity of the tax system, there being few measures to increase revenue.

Balance of payments developments have been marked by large increases in the current account surplus and the outflow of long-term capital (Chart 2). The current account surplus, which was only $7 billion in 1982 (0.6 percent of GNP), widened to $35 billion (2.8 percent of GNP) in 1984 and $49 billion (3.7 percent of GNP) in 1985. Following rapid export volume growth of 1983 and 1984, export volumes stagnated in 1985, reflecting the slowing pace of world recovery and the weakening of previously buoyant demand for some high-technology products. The lagged effect of the real effective appreciation of the yen in 1983 and early 1984 also contributed. Exports to the United States, which had accounted for most of the earlier rapid export growth, rose at a much reduced pace in 1985. While shipments of cars and consumer electronics to the United States increased, exports of semiconductors and steel fell considerably. Exports to China rose sharply, but exports to most other areas declined. Following an 11 percent increase in 1984, import volume has also stagnated in 1985, reflecting the slowing of industrial production and a number of special factors, such as unusually large imports of oil in 1984, and the expectation of further falls in commodity prices.

Total net outflows of long-term capital, which had increased from $18 billion in 1983 to $50 billion in 1984, rose further to $64 billion in 1985. The increase in 1985 reflected larger purchases of foreign securities, while net long-term bank lending declined and other categories of long-term capital outflows remained broadly unchanged. Interest rates continued to favor long-term U.S. dollar-denominated investments, although interest rate differentials narrowed somewhat over the course of 1985. Other factors contributing to the large purchases of foreign securities were continued portfolio diversification by institutional investors, larger investments by corporations, and the liberalization of foreign bond issues in the Japanese market. The resumption of foreign purchases of Japanese securities--following sizable disinvestment by nonresidents in 1984--and a substantial increase in bond issues by Japanese corporations in overseas markets partly offset the sharp rise in gross long-term capital outflows. Inflows of short-term capital through banks, which had risen sharply in 1984, rose further in 1985.

Following a persistent appreciation in nominal effective terms that reached about 25 percent between late 1982 and April 1984, the yen moved in a relatively narrow band in the second half of 1984 and the first three quarters of 1985 (Chart 3). In real effective terms, the yen appreciated throughout 1983, but turned downwards in the second half of 1984 and by the second quarter of 1985 was as low as the average for any year during the past decade.

III. The September 22 Meeting of the G-5 and Subsequent Developments

The meeting held among the ministers and governors of the five major industrial countries on September 22, 1985 was prompted by a desire to achieve greater convergence in policies and performance among these countries and a more appropriate pattern of exchange rates. In the months prior to the meeting, there had already been some improvement in the alignment in the nominal exchange rates among the major currencies, as the dollar weakened gradually against all other major currencies, including the yen. By September 20, the yen had strengthened against the dollar from the trough of ¥ 263 per $1 in mid-February to ¥ 242, although it had retreated from the historic highs against the major European currencies reached in early 1985--e.g., by 7 percent vis-a-vis the German mark. Nevertheless, the prospect was that external imbalances among the major industrial countries would remain large, with a continuing current account deficit in the United States, and matching external surpluses elsewhere--including in Japan. While these imbalances had the positive effect of supporting economic activity in Japan, there was an opposite effect elsewhere. In the United States in particular, although domestic demand continued to expand at a strong rate, its deceleration from the very rapid expansion experienced earlier in the recovery led to sluggish output growth and heightened pressures for protectionist measures.

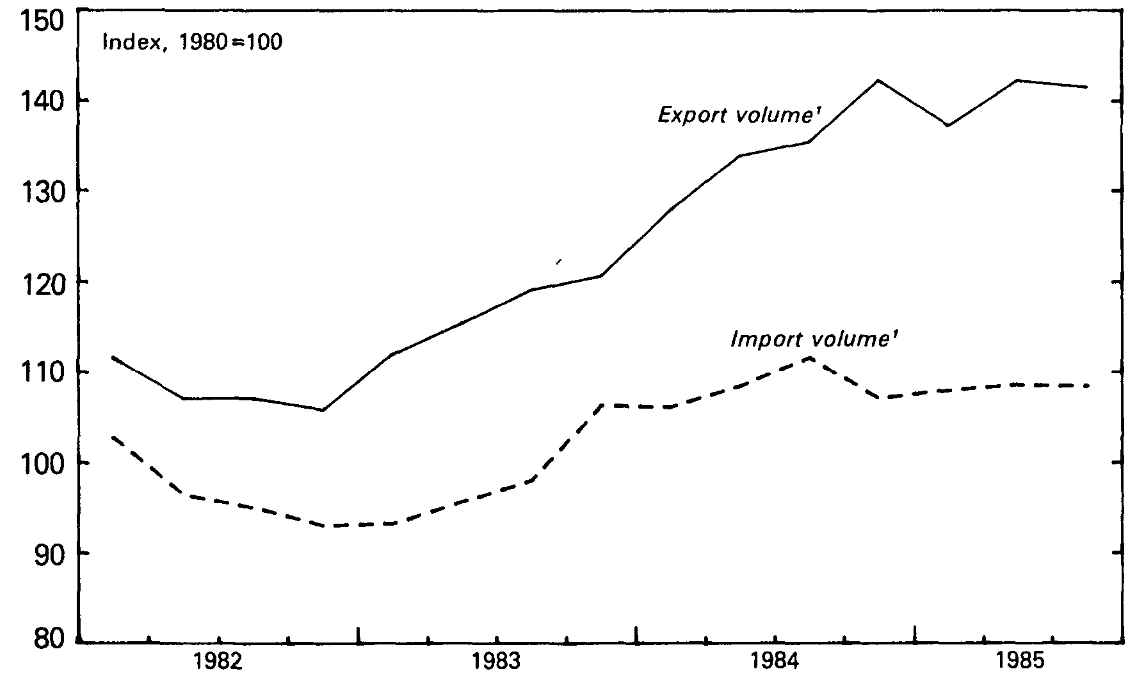
The Japanese authorities view with satisfaction the appreciation of the yen and the realignments among the major currencies that have occurred since September 22. By the end of 1985, the yen had appreciated by a further 21 percent against the dollar to about ¥ 200 per $1, by 3 percent against the German mark and the French franc, and by 13 percent against the pound sterling. In the view of the authorities, the most important factors had been the signal of purpose provided to the market in the Announcement issued following the meeting, and subsequent forceful, coordinated intervention by the major countries in exchange markets.

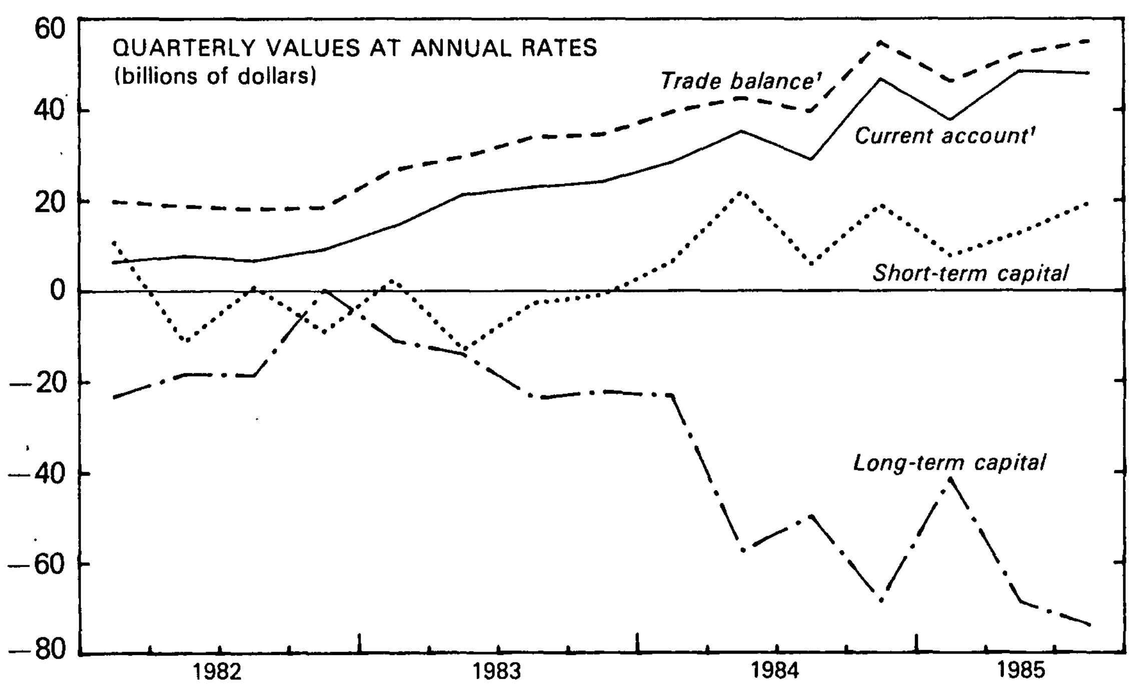
The yen rose sharply to around ¥ 210 per $1 in the two weeks following the G-5 meeting (Chart 4). However, during the middle of October, exchange market sentiment rebounded in favor of the dollar as participants apparently began to question the resolve of the authorities in the major countries and the continuation of large-scale intervention; persistent intervention during this period held the exchange rate at around ¥ 215 per $1. With this market reaction in view, the authorities provided a further signal of their determination when the Bank of Japan allowed interest rates to rise by about 1 1/4 percent in the last week of October by not offsetting a normal market tightening in bank liquidity. Exchange markets reacted strongly, and the yen appreciated to near ¥ 200 per $1. Between early November and the end of the year,

CHART 2

JAPAN

BALANCE OF PAYMENTS, 1982-85

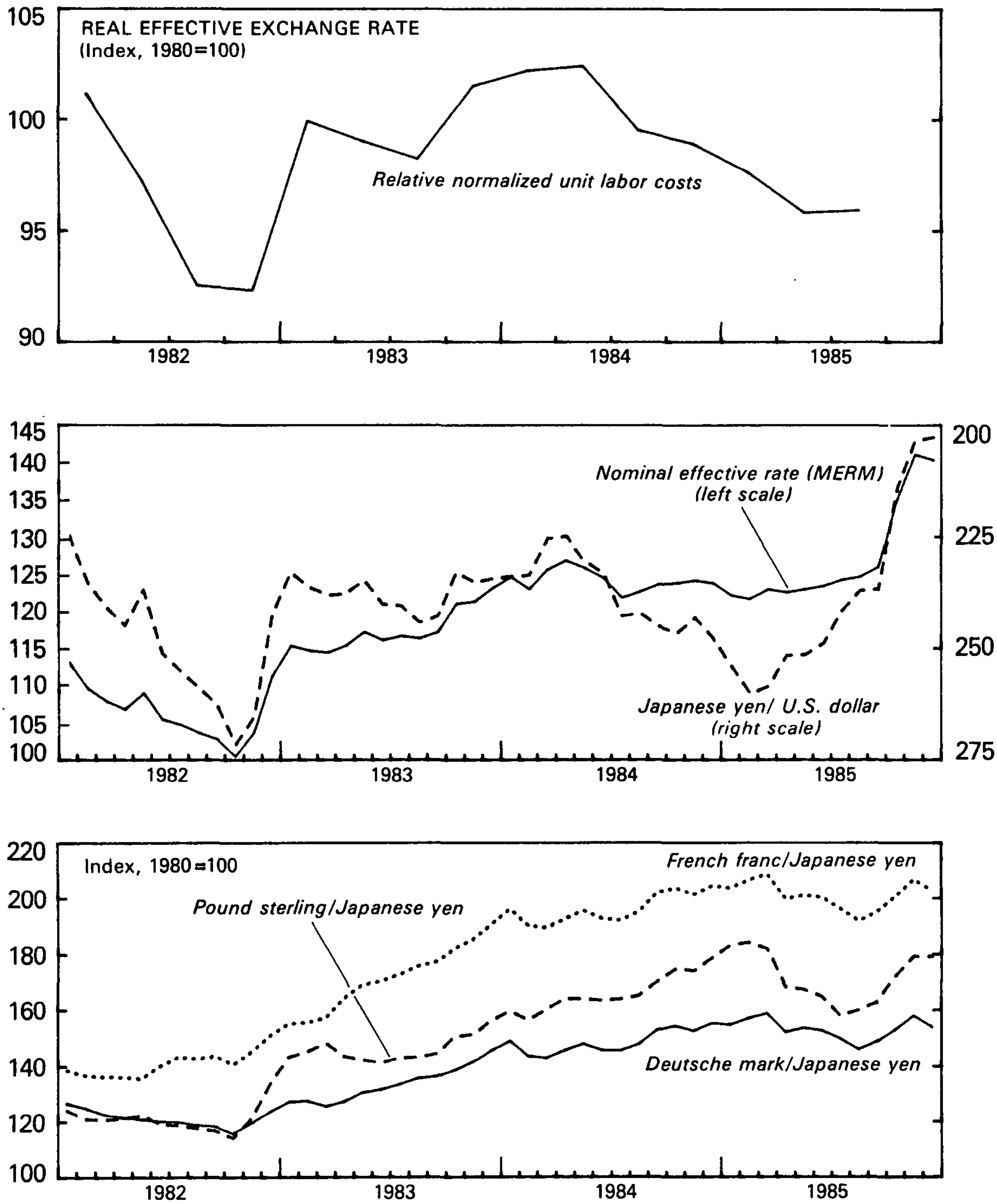




Source: Bank of Japan, Economic Statistics Monthly.

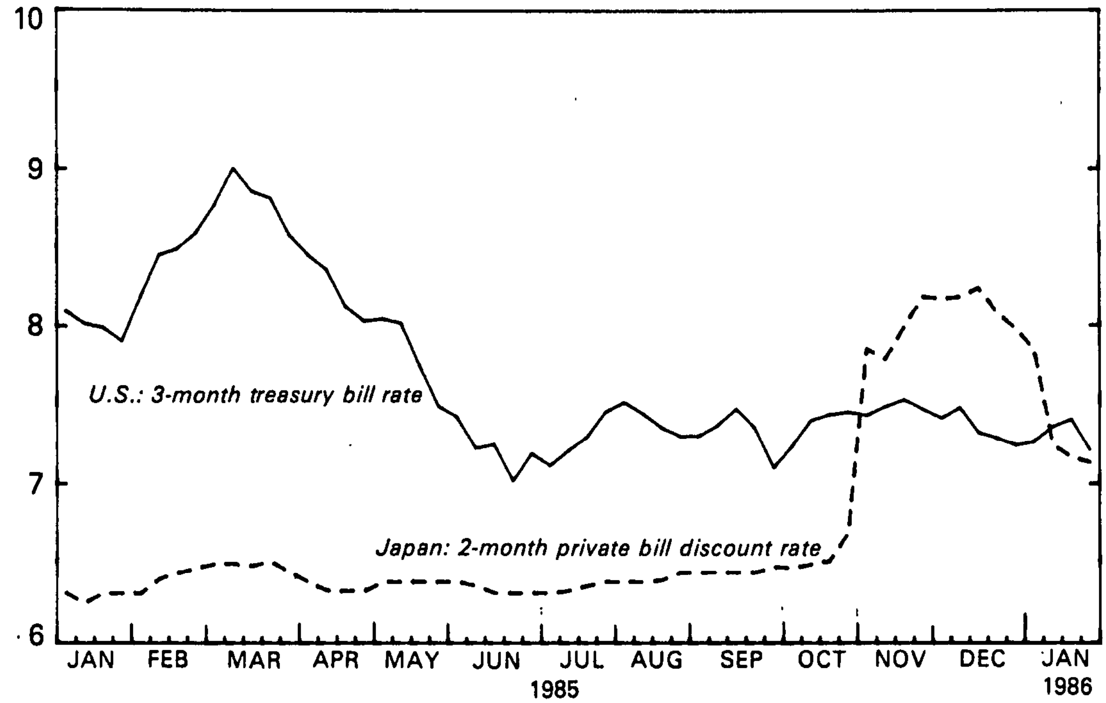
[1]Seasonallly adjusted.

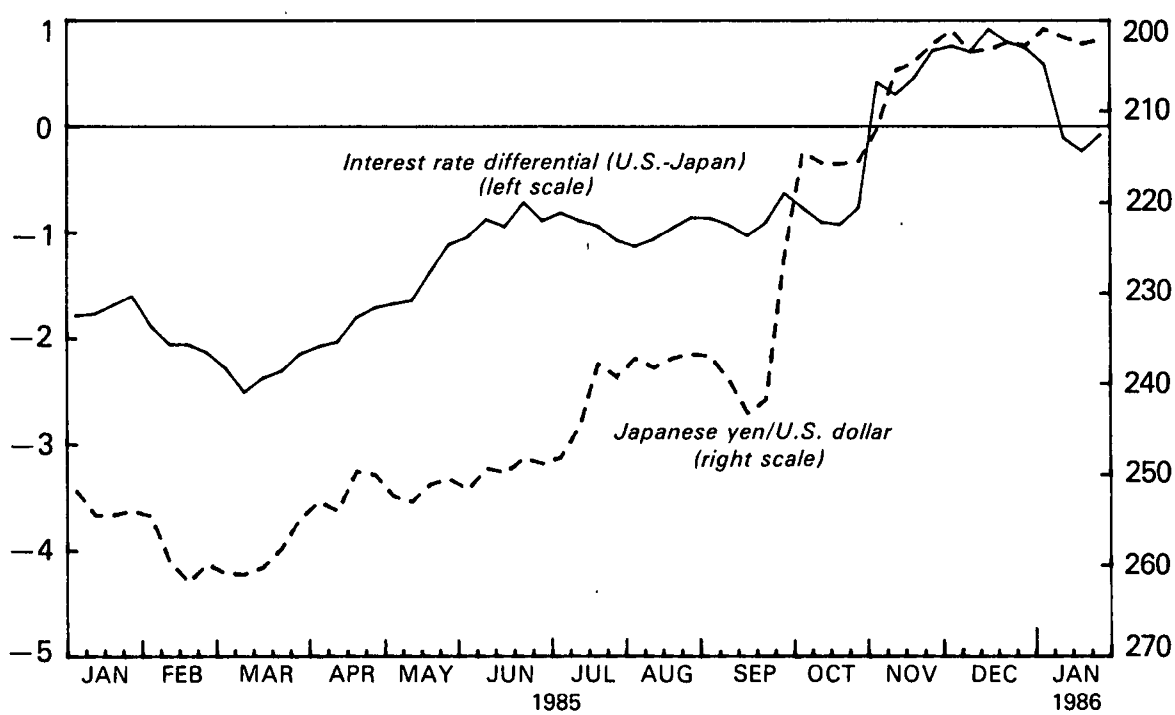
CHART 3
JAPAN
EXCHANGE RATE DEVELOPMENTS, 1982-85



Sources: International Financial Statistics, IMF and staff calculations.

CHART 4
JAPAN
NOMINAL SHORT—TERM INTEREST RATES AND
THE YEN/DOLLAR EXCHANGE RATE, 1985-86





Source: IMF, International Financial Statistics.

the yen remained relatively stable in the ¥ 200-205 per $1 range without support from additional monetary action or sizable intervention.

The authorities believe that the effectiveness of recent exchange market intervention reflects the favorable conditions ruling at the time. As the underlying tone of the dollar had already weakened in the months before the G-5 meeting, coordinated intervention, with the active participation of the United States which had previously been reluctant to be included, had had a powerful impact on exchange market psychology. However, the authorities emphasize that such success is unlikely to endure unless it is supported by broadly compatible policies and performance of the major economies. They note especially the essential contribution of a reduction in the fiscal deficit in the United States, while emphasizing that Japan is willing to play its part by implementing the policies indicated in the Announcement issued at the September 22 meeting.

IV. The Economic Outlook

1. The outlook for 1985/86 and 1986/87

The authorities estimate GNP growth to be 4.2 percent in 1985/86, falling marginally to 4.0 percent in 1986/87 (Table 1). The most striking feature of the forecasts is the projected turnaround in external demand, which is estimated to make a positive contribution to growth equivalent to 0.8 percent of GNP in 1985/86, but is expected to withdraw stimulus, equivalent to 0.2 percent of GNP, in 1986/87. In contrast, the growth of domestic demand is expected to rise from 3.5 percent to 4.3 percent, on account of stronger growth in private consumption and residential investment and further (although smaller) growth in private investment in plant and equipment. Total public sector demand is projected to rise noticeably faster in 1986/87 than in 1985/86, albeit still modestly.

Staff estimates indicate GNP growth of 3.9 percent in 1985/86, a little slower than forecast by the authorities. Consumption growth of 2.7 percent at an annual rate in the first half of 1985/86 would need to increase to almost 4 percent in the second half in order to reach the authorities' forecast. Alternatively, the staff projection implies second half consumption growth of about 3 percent. Recent and prospective developments in nominal disposable incomes do not indicate a significant acceleration in the next few months, while the boost to real consumption stemming from the recent appreciation of the yen could be expected only with a lag. Differences in the projections of the other components of domestic demand for the current year are insignificant. Business surveys indicate that private investment in plant and equipment may weaken in the second half of 1985/86 in response to the slower export growth, while private residential investment is expected to maintain its recovery, helped by recent policy measures. Net external demand is projected to account for less than a fifth of overall growth.

Table 1. Japan: GNP, Price and Balance of Payments Projections, 1985/86-1986/87

	Official Projections		Staff Projections	
	1985/86	1986/87	1985/86	1986/87
Aggregate demand (in real terms, percentage change)				
GNP	4.2	4.0	3.9	2.8
Total domestic demand	3.5	4.3	3.3	3.4
Of which:				
Consumption	3.0	3.6	2.8	3.3
Housing	3.1	4.6	3.3	3.5
Plant and equipment	11.5 1/	7.5	11.2 1/	4.6
Government expenditure 2/	-1.5 3/	2.0	-1.5 3/	2.0
Inventory 4/5/	...	...	-0.2	0.1
Foreign balance 5/	0.8	-0.2	0.7	-0.5
Prices				
Consumer prices	2.1	1.9	2.0	1.3
Wholesale prices	-2.4	-1.8	-2.5	-2.7
GNP deflator	1.5	1.1	1.6	1.1
Balance of payments (US$ bn.)				
Exports	178	184	181	190
Imports (f.o.b.)	-120	-128	-119	-126
Of which: oils	...	...	-42	-39
Trade balance	58	56	62	64
Services and transfers	-7	-5	-7	-5
Current account	51	51	55	59
(Percent of GNP)	3.6	3.1	3.9	3.5

Source: Projections provided by the Japanese authorities and prepared by the staff.

1/ Includes the effect of the privatization of Nippon Telephone and Telegraph (NTT) and the Japan Tobacco Industry. Excluding this effect, real private investment is estimated to rise by about 8 1/2 percent.
2/ Consumption plus investment.
3/ Includes the effect of the privatization of Nippon Telephone and Telegraph (NTT) and the Japan Tobacco Industry. Excluding this effect, real government expenditure is estimated to increase by about 1 percent.
4/ Contribution to GNP growth.
5/ Private plus public.

In the view of the staff, recent developments in the economy, the current stance of policies, and the external outlook point to a substantial slowing of growth in 1986/87. 1/ Staff estimates put GNP growth at 2.8 percent in 1986/87, 1.2 percentage points below the official forecast. Comparing the projections, the main difference arises in the outlook for domestic demand--more particularly in the estimates of private plant and equipment investment. In the staff's view, the prospect of weaker profits and stagnating exports, and the already considerable duration of the investment upswing point to a significant slowdown. High#expected to fall to 1.1 percent.

The staff expects the current account surplus to amount to $55 billion (3.9 percent of GNP) in 1985/86, rising further to $59 billion (3.5 percent of GNP) in 1986/87. However, the increase is due to the falling international value of the numeraire; measured in yen terms, the surplus would, in fact, decline by 5 percent. In contrast, the official forecast is of $51 billion for both years. The increase projected by the staff reflects primarily the "J curve" effect of the recent appreciation of the yen and the assumed decline in oil prices. As a result, the terms of trade are projected to improve by some 7.5 percent in 1985/86 and by a further 5 percent in 1986/87. The stronger yen and lower market growth abroad would lead to a reduction in export volume growth to 3 percent in 1985/86, with no growth likely in 1986/87. In contrast, import volume growth of about 1 percent in 1985/86 would rise to about 5 percent in 1986/87 as a result of the stronger yen. Investment income receipts are expected to rise considerably in both 1985/86 and 1986/87, contributing to the widening of the current account surplus.

In sum, the authorities expect that domestic demand will strengthen sufficiently in 1986/87 to offset the disappearance of the external stimulus, so that output growth will remain more or less unchanged from 1985/86. The staff believes that domestic demand will continue to grow

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1/ Staff projections are based on the working assumption of a decline in crude oil prices from $26.7 per barrel in 1985 to $23.5 per barrel in both 1986 and 1987. The staff estimates that were oil prices to be lower by $5 per barrel, the current account surplus would, in the first instance, be some $8 billion higher. The impact on growth is more difficult to estimate, but it is unlikely that growth in 1986/87 would be substantially higher than currently projected. The staff is currently revising its economic forecasts in the context of the forthcoming World Economic Outlook exercise and these will be made available to Executive Directors prior to the Board meeting.

at about the same rate in 1986/87 as in 1985/86 so that output growth will slacken, fully reflecting the swing in the external position, to a rate distinctly lower than the potential growth rate of the economy.

2. The medium-term outlook

An assessment of the outlook for external adjustment and growth beyond 1986/87 must, of course, be highly tentative. Projections for 1987/88, based on end-1985 exchange rates and only modest increases in demand both in Japan and in external markets, suggest that Japan's current account surplus would stabilize in dollar terms, and decline further to 3.3 percent of GNP. By 1987/88, the "J curve" boost to export values arising from the yen's recent appreciation would wear off. GNP growth, at about 3.5 percent, would remain sluggish.

It is not possible, at this stage, to accurately chart the path of balance of payments developments in the medium term. However, it is instructive to explore, if only in a summary way, some of the forces operating on saving and investment flows, which underlie external prospects.

That Japan has a high saving rate is well known. For the period 1979-84, the private savings rate in Japan (gross private savings were equivalent to 27.7 percent of GNP) was substantially above that in the other major industrial countries (Chart 5). Household savings, which account for over half of total private savings, rose steadily in the 1960s and the early 1970s to about 18 percent of household disposable income. 1/ The rate jumped to almost 24 percent in 1974--when, with high inflation, savers strove to maintain the real value of their financial assets. However, it has since declined persistently, with the exception, again, of the period immediately following the second oil price increase. Abstracting from the sharp increases in 1973-74 and 1979-80, household savings peaked at a level of about 18.5 percent in the early 1970s, with a slow secular decline being evident since then.

A recent international cross-section study carried out in the Fund, 2/ confirms the importance of Japan's population structure in explaining the relatively high saving rate in line with the "life cycle hypothesis" of saving. The relatively low ratio of the aged to the working-age population appears to be the most powerful positive factor

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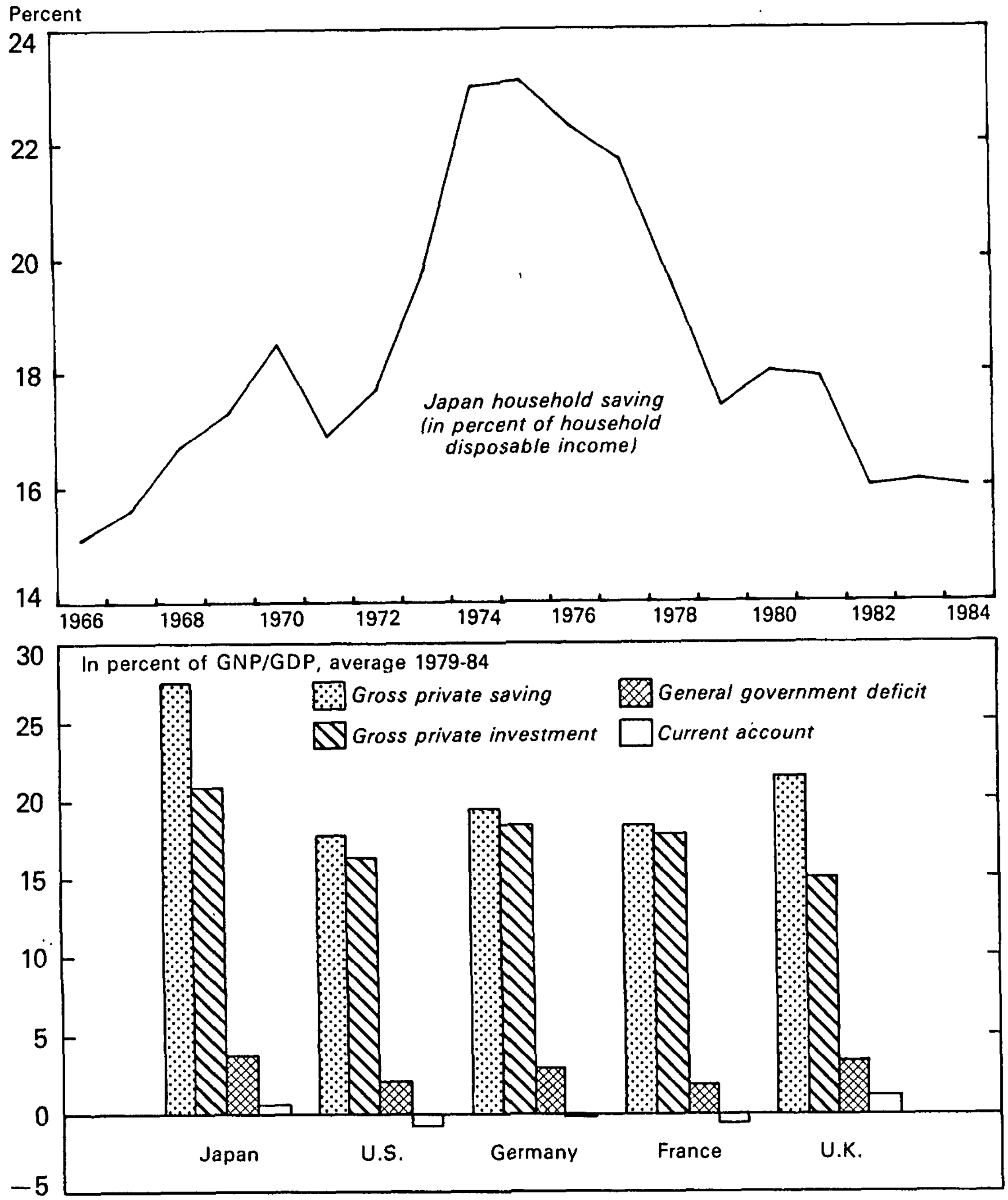
1/ Although corporate savings make up a large part of gross private savings, their contribution in net terms, after allowing for depreciation, and their likely impact on developments in the balance between savings and investment, is much smaller.

2/ "Why is Japan's Private Savings Rate so High" by Charles Yuji Horioka of Kyoto University, who was a consultant in the Asian Department in 1985. It is anticipated that this study will be issued in the DM series, and a summary will be provided in a supplement to the forthcoming paper on recent economic developments in Japan.

CHART 5
JAPAN
SAVINGS AND INVESTMENT IN MAJOR INDUSTRIAL COUNTRIES[1]



Sources: Japan, Economic Planning Agency, and staff calculations.

[1]Data for Japan are on a fiscal year basis.

affecting household savings. However, the relatively high labor force participation rates for the elderly in Japan, which reduces the need for younger workers to save for their old age, appears to have a large offsetting effect. The practice of early retirement in the government and corporate sectors, even though most retirees remain in the workforce, the lower ratio of the young to the working age population, the lower level but more rapid growth of per capita income, and higher land prices also contribute to high savings in Japan. In contrast, the relatively low inflation rate tended to reduce the saving rate.

There is less clear evidence of the importance of financial factors. The Japanese tax system contains numerous tax incentives for saving, more than in other major countries. While the empirical evidence is not conclusive, tentative staff estimates suggest that the impact of these incentives on the level of household saving has been reduced over recent years. There is some evidence that the large lump-sum bonuses paid to workers twice a year, which move broadly in line with firms' profitability and account for about a fifth of total compensation, have tended to increase the saving ratio. The effects of the availability of consumer credit on saving are ambiguous in theory and difficult to ascertain in practice. 1/

The rapid aging of the population is expected to be the predominant factor influencing savings in the future, leading in time to a significant decline in the private saving rate. Other factors are the likely rise in the retirement age and a reduction in the labor force participation rate of the aged in response to increasing social security benefits. These last two developments would have broadly offsetting effects. Tentative staff projections indicate a gradual decline in the household saving rate by perhaps 4 percent of GNP over the course of the next 15 years as a result of these developments. Movements in the short term are more uncertain, being dominated by year-to-year macroeconomic developments, although measures to reduce financial incentives to saving and increase the availability of consumer credit on more attractive terms would be expected to have some immediate effect.

As in the case of savings, private investment has also been high by international standards. Private investment absorbed most of private savings until the early 1970s, and both rose steadily as a proportion of GNP. However, private investment fell sharply following the first oil price hike, from 26.8 percent of GNP in 1973 to 20.6 percent by 1978, as the rate of return on capital fell and future growth prospects were scaled back. Since then, there has been a recovery in private investment on plant and equipment, especially in most recent years as new technologies have become available and growth prospects have improved.

1/ Developments in consumer credit in Japan are reviewed in a supplement to the forthcoming paper on recent economic developments in Japan. Some of the theoretical arguments are discussed in the supplement on private saving referred to earlier.

In contrast, residential investment languished, falling by the equivalent of 2 percent of GNP between 1978 and 1984 as rising land prices outpaced growth in household incomes, and other structural factors depressed housing demand.

There is, perhaps, even more uncertainty surrounding the future course of private investment than for savings. There are bound to be sizable fluctuations in plant and equipment investment in response to developments in economic activity, wages, and capital costs. Trends in such investment will be influenced by perceptions as to the likely future growth path of the economy, in which the pace of technological progress would be an important factor. The authorities' efforts to promote private sector initiative and freedom will also be important in this regard. The latent demand for housing investment would remain strong as housing becomes, more than ever, the area where basic needs are least well satisfied. Whether this will translate into a large enough increase in investment in housing will depend partly on the success of efforts to provide housing financing on attractive terms and deregulate land use, and other developments affecting land and housing costs relative to incomes.

A further important question is the impact of the stance of fiscal policy on private saving and investment behavior. The empirical evidence on this issue is not conclusive, but there is a broad consensus that changes in public sector saving are likely to be partially offset by changes in private sector saving and investment behavior. The Japanese authorities have sought to reinforce such offsetting effects mainly through structural policies to stimulate private sector vitality; these are discussed in Section V.4 below.

V. Policy Issues

1. General considerations

The Japanese economy has grown strongly in recent years without any indication that resource limits were being reached. In 1986, however, growth is expected to fall well below the economy's potential. Moreover, the prospect of further withdrawal of external stimulus beyond 1986 raises the risk that slower growth may persist.

The interests of the international community and Japan coincide in sustained, strong economic growth in Japan, near to its potential rate. The importance of strong noninflationary growth in the major industrial countries was given a central position in the Declaration of the May 1985 Bonn Economic Summit. It was reaffirmed in the Announcement of the G-5 on September 22, 1985 which included a commitment by the Japanese Government to continue policies intended to ensure sustainable noninflationary growth. Strong domestic demand growth in Japan is especially desirable, not only because of Japan's economic size and impact on the world economy, but also because it will tend to alleviate a major international problem--Japan's large and growing external current account surplus.

Japan's widening current account surplus has been a close counterpart of the rising U.S. deficit. During last year's discussion, Executive Directors could agree that during 1983 and 1984, the rise in Japan's external surplus mainly reflected the different cyclical positions of the Japanese and U.S. economies and exchange rate developments which largely reflected developments and policies outside Japan. With Japanese growth at, or in excess of, the sustainable rate, there was little scope for macroeconomic policies in Japan in those years to alleviate the large surpluses. Needless to say, the scope for action on Japan's part to reduce the external imbalance will be greater if external demand falls significantly in 1986.

The large external imbalance among the major countries may be seen positively as a reflection of the transfer of savings from countries such as Japan where they are larger than needed, to countries where savings are deficient relative to the demand for them--such as the United States. Indeed, the responsiveness of Japan's economy to external demand and the willingness of its people to save from the income earned has played a positive role in financing investment worldwide and holding interest rates below levels they would otherwise have reached. At the same time, of course, there are less beneficent aspects to the external imbalances. Most importantly, they are reflected in imbalances in output and employment among countries that bring with them the threat of protectionism. In their Announcement on September 22, 1985, each of the five major industrial countries committed itself to resisting protectionism, while Japan also made a commitment to further open up its markets to foreign suppliers. The realignment of exchange rates among the major currencies that has since occurred is likely to have a positive effect in suppressing protectionism, even though the reduction in current account imbalances it promises will not be immediate. However, the threat of protectionism has not been eliminated and remains one of the greatest problems confronting policymakers.

During most recent years, there have been basic conflicts among the objectives of economic policies in Japan. These conflicts were eased in 1984, at the peak of the recovery, when policies to actively promote economic growth could be put aside. During last year's discussions, Executive Directors generally agreed that the authorities' policy strategy was appropriate to the circumstances ruling at the time. This involved vigorously pursuing fiscal consolidation, which the authorities view as a medium-term objective of the highest priority, and following a cautious monetary policy aimed at encouraging a strong yen in order to reduce the external surplus. More recently, however, the basic policy dilemmas have re-emerged. In particular, the prospect of a considerable slowing of growth in 1986, and the desirability that policies be adapted to counter this, create fundamental conflicts for monetary policy with the objective of establishing a stronger yen, and for fiscal policy with the objective of fiscal consolidation. These dilemmas, and the choices among objectives that must be made, provided the focus for the policy discussions.

2. Monetary policy and the exchange rate

At the time of the last consultation, Executive Directors generally endorsed the authorities' intention not to allow a reduction in interest rates until a stronger yen was established, although some Directors indicated concern regarding high interest rates and the potential impact on economic activity. The authorities indicate that priority in the conduct of monetary policy continues to be accorded to the exchange rate because, in their view, an appropriate exchange rate for the yen is the most powerful instrument available to them to promote external balance over the medium term. During most of 1984, short-term interest rates were kept virtually stable by the Bank of Japan despite downward movement in rates in the United States and in long-term market-related rates in Japan in the middle of the year. The narrowing of interest rate differentials in favor of the dollar supported the strengthening of the yen that began in February 1985. Despite the priority afforded exchange rate considerations, liquidity conditions have become somewhat easier. The 12-monthly growth of M2+CDs, the aggregate most closely monitored by the authorities, rose from below 8 percent in 1984 to 9 percent by the end of 1985; some of the acceleration reflects financial deregulation.

The decision to allow interest rates to rise sharply at the end of October reflected the authorities' desire to consolidate the stronger yen at a time when the foreign exchange market appeared to be questioning the likely continuing impact of large-scale intervention and the durability of the exchange rate realignment achieved to that point. It did not stem from any substantial concern that monetary growth had become too rapid. The authorities note that the existing relatively easy liquidity conditions would mitigate any immediate adverse impact on the economy. At the same time, they do not believe that the rise in interest rates will depress economic activity significantly unless it is perceived to be long lasting. The rise in interest rates resulted from the Bank of Japan's decision not to resist pressures in the interbank market arising from seasonal factors, developments in government finances and exchange market intervention. The authorities had, from the outset, decided not to offset the tightening in bank liquidity as a result of intervention; however, the nonsterilization of intervention accounted for a relatively small part of the shortage of bank liquidity observed in October and November.

During the discussions, the authorities stated that in their conduct of intervention and monetary policy following the September 22 meeting, they were not aiming at any implicit exchange rate target. They considered the strengthening of the yen achieved to date to be substantial, and that it would in time yield positive results. They saw benefit to be obtained from a period of exchange rate stability; adjustment difficulties were already being experienced in small- and mediumsized export industries. However, they stated that they would resist any tendency for the yen to weaken significantly from its present level. The authorities pointed to the recent experience as demonstrating that intervention could, in the right circumstances, play a decisive role in pointing exchange markets in the direction indicated by economic fundamentals.

The authorities would not be unhappy if, in due course, market forces pushed the yen even higher. They indicated that market sentiment in favor of a stronger yen would, in the first instance, allow an unwinding of the tight monetary conditions ruling since late October 1985. Domestic economic conditions would warrant lower nominal interest rates, especially as lower inflation resulting from the exchange rate appreciation would tend to raise real rates. However, the Bank of Japan emphasized that caution is needed in moving to ease monetary conditions, not only to protect the yen, but also to avoid excessive monetary expansion. Although no target for monetary growth in the coming year has been established, the authorities believe that the recent rate of growth in M2+CDs would be a prudent maximum, especially because velocity may not remain low relative to its declining trend as it has for the past three years.

At the time of the discussions, the authorities anticipated a reduction in interest rates in the United States that would allow a corresponding reduction in Japanese short-term rates. Such an expectation was apparently shared by financial markets in Japan which, by mid-December, in anticipation of lower short-term rates, had pushed long-term rates back down to the low rates ruling before the October increase. Since then, long-term rates have varied only slightly and long-term interest differentials in favor of dollar investments have remained virtually unchanged, although about 1 percent lower than at the beginning of 1985. U.S. short-term rates did decline somewhat in the second half of December, and this decline was matched by an easing in short-term rates in Japan. In early January 1986, short-term interest rates were allowed to decline by a further 0.8 percentage point, despite a concurrent firming in rates in the United States. On January 28, following a strengthening of the yen to around ¥ 195 per US$1, the Bank of Japan reduced the discount rate from the rate of 5 percent ruling since October 1983 to 4.5 percent. Following this adjustment, short-term market rates have declined by about 1 percentage point to a level some 0.5 percentage point below that ruling prior to late October, and the shift in short-term interest rate differentials in favor of yen investments has been more than fully reversed.

3. Fiscal policy

Conflicts in the objectives of fiscal policy are especially severe. The need for monetary policy to give priority to exchange rate considerations focuses the burden of demand management on fiscal policy;

however, the central government fiscal deficit remains large and the need for medium-term efforts to reduce it remains clear and, indeed, to the authorities paramount.

Japan's fiscal difficulties arose from the first oil price increase and the efforts of the Government to sustain economic activity. Large deficits were incurred, leading to a rapid growth in the stock of government bonds outstanding and in interest payments. Since the late 1970s, the authorities have viewed fiscal consolidation--which includes reducing the budget deficit and limiting the size of government--as an essential goal of policy. Their main objectives are to substantially reduce the deficit in the general account of the Central Government, and to eliminate by 1990/91 the issue of bonds to cover current spending (so-called deficit financing bonds). The authorities are concerned particularly by a rapid rise in the outstanding debt of the general account, which has risen from 7 percent of GNP to 40 percent over the ten years to 1984/85, and by the increase in the share of expenditures absorbed by interest payments, which has almost doubled over the past five years to 19 percent in 1985/86. A reduction in deficits is needed both to prevent the further erosion of fiscal flexibility by containing the share of interest payments, and to place the Government in a better position to accommodate the increased social welfare expenditure that will inevitably accompany the rapid aging of the population in the next two decades. Efforts have concentrated on expenditure restraint. There has been a reduction in the size of central government employment, a significant restructuring of the social security program and medical benefits and contributions, and some reduction in subsidies provided to the Japan National Railways and for government food operations. The authorities stress that action on the revenue side should only come as a last resort after all reasonable avenues at expenditure cutting have been exhausted.

Despite stringent expenditure controls, progress in reducing deficits has been slow and uneven. The general account deficit fell from 5.6 percent of GNP in 1980/81 to 4.4 percent in 1984/85, while the issue of deficit financing bonds has fallen from ¥ 7.2 billion to ¥ 6.5 trillion (Table 2). General spending has been held virtually unchanged for the past three-and-a-half years, and the authorities recognize that this cannot be sustained for more than one or two more years. Also, slowing nominal income growth, through its effect on budget revenues, has accentuated the difficulties in reducing bond issues as planned. In 1985/86, decelerating economic growth has held revenues somewhat below levels originally projected. In addition, supplementary spending for wage increases and associated with measures taken in October 1985 to stimulate demand has been necessary, and the general account deficit is now expected to amount to 4.0 percent of GNP, compared with 3.7 percent in the original budget. The reduction in deficit financing bond issues will be limited to ¥ 0.3 trillion, less than one half of the cut envisaged in the budget and well short of the reduction of about

Table 2. Japan: Central Government General Account Budget, 1982/83-1986/87

(In trillions of yen)

	1982/83	1983/84	1984/85			1985/86		1986/87
	Settlement	Settlement	Initial	Revised	Settlement	Initial	Revised (Proposed)	Initial (Proposed)
Expenditure	47.25	48.38	50.63	51.51	51.48	52.50	53.22	53.68
General expenditure 2/	32.80	32.90	32.59	33.24	33.21	32.59	33.35	32.58
Interest payments	6.74	7.72	8.94	8.89	8.81	9.97	9.92	10.69
Transfer of local allocation tax to local government	7.54	7.32	8.89	9.04	9.04	9.69	9.69	10.19
Revenue	33.23	35.55	37.73	38.03	38.16	40.51	40.27	42.88
Deficit	14.02	12.84	12.90	13.48	13.32	11.99	12.95	10.80
Financing	14.02	12.84	12.90	13.48	13.32	11.99	12.95	10.80
Bond issues (net)	14.05	13.49	12.68	12.87	12.78	11.68	12.44	10.95
Deficit financing bonds	7.01	6.68	6.46	6.46	6.46	5.73	6.14	5.25
Construction bonds	7.04	6.81	6.23	6.41	6.33	5.95	6.30	5.70
Memorandum items:								
In percent of GNP 3/								
Expenditure	17.4	17.0	16.7	17.0	17.0	16.4	16.6	16.1
Revenue	12.2	12.5	12.4	12.5	12.6	12.7	12.6	12.9
Deficit	5.2	4.5	4.3	4.5	4.4	3.7	4.0	3.2
Bond financing	5.2	4.7	4.2	4.2	4.2	3.7	3.9	3.3
Deficit financing bonds	2.6	2.4	2.1	2.1	2.1	1.8	1.9	1.6

Source: Data provided by the Japanese authorities.

1/ This presentation differs somewhat from that of the authorities, which includes some of the financing items in revenue and expenditure.
2/ This reflects the discretionary component of expenditures, i.e., total expenditures less interest payments, certain contributions to international organizations, and tax transfers to local governments.
3/ On the basis of official revised GNP data up to 1984/85 and staff projections for 1985/86 and 1986/87.

¥ 1.2 trillion per annum that would be required to achieve the authorities' target of eliminating the issue of deficit financing bonds by 1990/91 on a straight line path.

At the time of the discussions, the formulation of the 1986/87 budget was at an early stage. However, the authorities indicated their determination to aim for further fiscal consolidation in the general account in line with their medium-term objective. The authorities remain committed to keeping the medium-term targets despite growing doubts, as years go by, that they can be achieved. They emphasize that the maintenance of the targets provides a clear goal for budgetary efforts which cannot afford to be diminished. While it may not be possible to completely eliminate the issue of deficit financing bonds by 1990/91, the authorities would be reasonably satisfied if they were able to sustain the maximum feasible degree of expenditure restraint in the period up to then. For 1986/87, this would imply a willingness to accept a larger-than-budgeted deficit in the general account if this arose because of slower-than-anticipated revenue growth and as long as expenditure restraint was fully maintained.

The staff expressed the view that, with the likely withdrawal of external stimulus and the consequent weakening of aggregate growth prospects, it would be undesirable that fiscal operations withdraw stimulus from the economy in 1986/87. The case for such a shift in the priorities of fiscal policy in Japan would be even stronger in the event that prospects for action in reducing the budget deficit in the United States are translated into early and substantial measures. Deficits at the general government level, which have been reduced from 3.6 percent of GNP in 1982 to an estimated 1.7 percent in 1985, are much lower than for the general account. 1/ The difference in the level of the deficits is partly due to social security system surpluses, which have been broadly unchanged at 2 1/2-3 percent of GNP in recent years, but are expected to change to deficits with the maturing of the scheme and the aging of the population. Even so, the need for fiscal consolidation is, in the aggregate, clearly much less pressing than for the general account alone. Looking even beyond the general government, public enterprises can also play a useful role in sustaining activity levels. Thus, in the staff's view, there did appear to be scope for stimulatory action by the public sector outside the general account so that fiscal policy, taken as a whole, need not hamper economic growth in 1986/87.

1/ The general government includes the central government general account, the social security system, and local governments. While the central government general account is viewed by the authorities as the principal budget for fiscal policy purposes, central government budget operations include, in addition, lending by the Fiscal Investment and Loans Program (FILP) other than to financial agencies, 38 special accounts and budgets for 12 government affiliated agencies.

The authorities agree that there is more room at other levels of the public sector for fiscal policy to sustain growth. At the local government level, for example, where more progress in reducing deficits has been achieved, there is also more room for fiscal stimulus. There is no formal objective to reduce local government deficits, and their areas of expenditure responsibility provide greater scope for flexibility. Advantage of this flexibility was already taken in the October 1985 demand stimulus package which provided for additional local government public works spending of up to ¥ 800 billion, financed by additional bond issues. Nevertheless, it is recognized that there is further room for local governments to provide stimulus to the economy in 1986/87. In addition, the authorities see scope for sizable increases in loans from the Fiscal Investment and Loans Program (FILP) to fund larger investments by nonfinancial public enterprises, particularly for highway construction and public housing. Funds available to FILP from the Post Office savings system are expected to increase substantially in 1986/87. Moreover, FILP investments in projects involving private sector participation would be expected to play a useful role in increasing private investment.

Since the mission's return, details of the proposed 1986/87 general account budget have become available. As expected, the budget continues to place emphasis on expenditure restraint, with total discretionary expenditure being unchanged from the initial 1985/86 budget. Public works expenditure is to decline by 2.3 percent and substantial cuts are planned in food subsidies and the subsidy provided to the railways; in contrast, priority expenditure for defense and foreign aid are to rise by more than 6 percent. Total revenues are projected to increase by 5.8 percent. Proposed changes in the tax structure are small and are expected to yield additional revenue equivalent to 0.1 percent of GNP. As a result, the general account deficit would decline to 3.2 percent of GNP. The amount of deficit financing bonds to be issued is budgeted to decline by ¥ 0.9 trillion from the revised estimate for 1985/86.

With the slowing of growth as projected by the staff, the proposed central government (general account) budget would, if implemented without change, result in a withdrawal of stimulus from the economy equivalent to over 1.0 percent of GNP, up from a revised estimate of 0.4 percent in 1985/86. However, in line with the indications provided to the mission, the authorities have made efforts to mitigate the impact of their fiscal consolidation efforts in the general account by adopting measures at other levels of government designed to support economic activity. There is only limited information available at this stage on local government budgets, but it appears these are likely to provide a net addition of stimulus equivalent to about 0.1 percent of GNP. Also, for the first time since 1982/83, FILP lending for investment by public enterprises is to increase substantially (11 percent) in 1986/87, which would have an overall stimulatory impact equivalent to about 0.2 percent of GNP.

Overall, the present budget proposals, were they to be implemented without change, would result in a withdrawal of fiscal stimulus by the broad public sector equivalent to 0.7 percent of GNP. The withdrawal would, however, be lower were revenues to fall short of the budget estimates (which seems likely if growth falls as forecast by the staff) and expenditures not reducëd correspondingly. The same would apply if additional expenditures are incurred, as would appear necessary to cover probable increases in government wages which are not provided for in the budget. The possible effect of these factors would be to reduce the projected withdrawal of fiscal stimulus by the broad public sector, perhaps to about 0.5 percent of GNP. In addition, based on past experience additional public works spending may well be forthcoming in the second half of the year to fill the gap left by the bringing forward of expenditures from this period in the October 1985 stimulus measures.

Options for a major tax reform are now under study by the Tax Systems Council. This will be the first comprehensive overhaul of the tax system that was put in place in 1950 and has been adjusted in a piecemeal fashion since then. The objective is to establish a system of taxation appropriate to the times and the needs of the economy, especially by promoting equity, efficiency, and simplicity. The political leadership has decided that the reform should be revenue neutral. However, in establishing the new tax framework the authorities would take into account the need to provide room to augment revenues in due course when this is warranted. Recommendations for the reform are expected to be completed in the second half of 1986, and are likely to be implemented in the 1987/88 budget. In view of the pending major reform, the authorities did not consider it to be appropriate to make significant tax changes in the 1986/87 budget.

Details on the likely shape of tax reform are incomplete at this stage. The authorities indicate their intention to consolidate and reorganize tax incentives presently provided, to close loopholes, and to widen the tax base. The present heavy reliance on the personal income tax is believed to involve an inequitable burden on wage and salary earners while many small businesses and farmers are lightly taxed. It is expected that personal income tax rates (especially at the middle and upper ranges) will be reduced and that a broadly based indirect tax, such as a value-added tax, will be introduced. There is increasing support for reducing the generous and often-abused tax exemptions for income from small savings. Pending a basic change in small savings taxation, stricter monitoring of eligibility for tax exemption is to be introduced in 1986.

Tax reform would also consider the appropriate level of corporate taxes. Reliance on corporate taxes (which account for 30 percent of tax revenue) is unusually high in Japan, due in part to the large share of corporate income in total GNP and the low overall tax take. At the same time, Japan has not introduced extensive deductions and allowances for corporate investment as have some other industrial countries. While recognizing that developments in corporate tax practices in other major countries must be taken into account in the corporate tax system in Japan, the authorities do not support the introduction of generalized investment allowances.

4. Policies to encourage private sector activity

Administrative reform has become a major focus of policies to promote economic growth. It encompasses privatization of public enterprises, private sector participation in public works, deregulation, and other policies aimed at promoting administrative efficiency, scaling back the size and role of government, and encouraging private sector activity. The role seen for these programs by the Government has increased significantly in recent years with the growing perception that domestic private sector vitality must be the foundation of Japan's future economic growth. Reliance on them has also been increased in a macroeconomic context as exchange rate and fiscal consolidation objectives have diminished the scope for monetary and fiscal policies to be used actively to stimulate growth.

The "privatization" of public works is an important new initiative. The concept fits well with present needs, as it would allow additional investment to support growth and supplement the stock of social infrastructure (which remains clearly deficient in comparison with the other major industrial countries) without placing large demands on public finances. So far, only limited progress has been made in giving substance to the concept. A new private body has been established to construct and operate the new Kansai International Airport, and provision has been made in the FILP plan for 1986/87 for a bridge/tunnel spanning Tokyo Bay to be constructed with private sector participation. These projects are estimated to cost ¥ 1 trillion each, but expenditure in 1986/87 is likely to be very small.

The mechanisms for defining how the private sector is to participate in constructing and operating public works have still to be developed. Potential private sector parties in large projects are requesting incentives and guarantees to protect them from the greater risk involved in large and long-gestation projects, but the Government is wary of the potential costs. Privatization also encompasses the sale of public enterprises. During the past year, the Nippon Telephone and Telegraph and the former Japan Tobacco and Salt Corporation have been reorganized as joint stock companies, and it is intended that the Government will sell shares to the public. The Government is also pushing ahead with plans to privatize Japan National Railways.

Wide-ranging deregulation steps are currently being considered by the Government and some have been implemented. It is estimated that industries accounting for about 25 percent of GDP are subject to substantial controls, including transport, communications, finance, and agriculture; manufacturing is not strongly affected. In addition, extensive regulations on land use constitute major impediments to urban and housing development; the Government took steps in 1985 to ease restrictions on land use.

The September 22 Announcement of the G-5 included an undertaking by the Japanese authorities to enlarge consumer and mortgage credit markets. The October 15, 1985 stimulus measures included liberalization of the conditions attached to loans provided by the Housing Loan Corporation, expected to result in additional loans of about ¥ 500 billion, equivalent to 3 percent of private residential investment. The 1986/87 budget also provides new three-year tax credits for interest on housing loans of up to ¥ 20 million, equivalent to 1 percent for private loans, or 1/2 percent for loans from public agencies. The authorities have also requested the banks to positively consider increasing consumer loans. The authorities point out, however, that these markets are now well developed. The ratio of consumer credit to private disposable income (12.4 percent in 1983) was broadly in line with the average ratio in major European countries, all of which have ratios well below that in the United States. Outstanding housing loans total about ¥ 60-65 trillion, equivalent to about one fourth of the U.S. mortgage market. As a further measure aimed at increasing consumption, the authorities are encouraging a reduction in working hours toward the adoption of a general five-day work week, although it mostly remains to individual businesses to determine working hours.

5. Trade policy

During 1985, Japan took several initiatives to further open its markets to foreign products. 1/ These included the introduction in April 1985 of the seventh package of market opening measures since late 1981; the endorsement of the report of the Advisory Committee on External Economic Issues, the so-called "Okita Report," which includes wide-ranging recommendations on the internationalization of the Japanese economy; and the announcement in June 1985 of tariff cuts on a large number of products. Furthermore, in July 1985 an Action Program was adopted to guide liberalization efforts over the coming three years in the areas of tariffs, import quotas, standards and certification requirements and import procedures, government procurement, trade in services, import promotion, and financial markets. Moreover, bilateral negotiations on market-opening measures were conducted with the United States covering four sectors: telecommunications, forest products, pharmaceuticals and medical equipment, and electronics.

Tariff cuts were announced for 1,853 items and tariffs on some electronic products eliminated in 1985. In addition, Japan has announced its readiness to eliminate tariffs on industrial products in

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1/ The paper "Japan, Recent Trade Measures," SM/85/256, prepared for the information of the Executive Board, gives details of most of these initiatives.

concert with other advanced industrialized countries in a new round of multilateral trade negotiations. As a first step, Japan has suggested talks on the elimination of tariffs on high-technology products prior to a new round. Japan has also proposed efforts to make fundamental improvements in the Generalized System of Preferences.

Measures have been announced to relax and streamline standards, certification requirements and import procedures-- the pervasiveness and complexity of which have been widely regarded as important obstacles to imports--and further changes to be implemented in the course of the next three years are currently under discussion. Of 88 areas where simplified procedures were promised, steps have been taken so far in 25. The objectives are to enhance transparency, align Japanese requirements to international standards where possible, simplify and speed up procedures, accept foreign inspection data, and widen the scope of self-certification. Similarly, revisions in Government procurement procedures are being considered to ensure fair competition among domestic and foreign bidders. In the Action Program, Japan has also expressed its readiness to discuss the relaxation and dismantling of existing restrictions on trade in services in the new round of multilateral trade negotiations.

The authorities hope that the recent exchange rate changes will contribute to a durable abatement of protectionist forces abroad, although they believe this will need to be supported by efforts in all countries. As to their own efforts, the authorities emphasize the comprehensiveness and medium-term perspective of the Action Program, and the prominence and publicity given to promoting imports and enhancing economic cooperation. They reiterate their belief that in many areas foreign suppliers have yet to exploit the opportunities available to them; they emphasize that quantitative import targets suggested by some trade partners would be inconsistent with Japan's market-oriented economic system. While acknowledging that protection remains significant in some areas, especially for agriculture, they point out that industrial tariffs are among the lowest in the industrial countries and there are no quotas on imports of manufactures, with the principal exception of leather and leather products. The authorities consider that political considerations would not permit significant liberalization measures in the heavily protected agricultural sector in the near future.

With respect to market access for developing countries, the authorities acknowledge domestic pressure for restraint on textile imports from several Asian countries. While the Japanese Government has not requested voluntary export restraints, discussions between the domestic and foreign industries have resulted in ad hoc trade inhibiting arrangements, such as quantitative limits, "check prices", and undertakings not to disrupt the Japanese market. Also, quotas on silk imports have been lowered over recent years in light of declining domestic demand; as a parallel measure, the number of domestic looms is being reduced by one fourth. The authorities stated that, these developments notwithstanding, efforts would be made to facilitate imports from developing countries by encouraging shifts from traditional sectors of Japanese industry toward higher value-added products. A recently announced program to provide loans to small companies in sectors affected by the yen's appreciation is intended only to provide temporary support to facilitate adjustment.

There were two major developments in the area of export restraint in 1985. First, exports of steel to the United States became subject to quantitative limits established in bilateral negotiations. Second, the ceiling on exports of automobiles to the United States was increased by 24 percent for the period April 1985-March 1986. While the United States did not seek a further extension of voluntary export restrictions on Japanese automobiles to the United States, the Japanese authorities believed that an immediate and complete end to restraint would cause disruption and be harmful to U.S.-Japanese trade relations. No decision has been announced on policies to apply after March 1986, but the authorities expressed their wish to terminate this and other restraint arrangements when conditions permit. In this respect, the recent appreciation of the yen is regarded as a positive factor.

6. Liberalization of financial markets

The liberalization of financial markets has been designed both to strengthen the role of market forces in the domestic financial system and to promote greater international use of the yen. In reforming the financial system, the authorities have adopted a step-by-step approach in order to avoid market disruptions and problems for the orientation and implementation of monetary policy. Measures fall into four broad categories: the deregulation of domestic interest rates and money and capital markets; the removal of remaining barriers to capital flows, following the elimination of virtually all formal restrictions to capital flows in December 1980; the promotion of Euro-yen markets; and the widening of the scope for foreign institutions to participate in Japan's financial markets.

Measures introduced in 1985 largely aimed at implementing the plans announced in the report of the joint Japan-U.S. Working Group on Yen/-Dollar Exchange Rate Issues in May 1984. 1/ In the area of the domestic financial markets, measures were taken to increase the availability of certificates of deposit (CDs), money market certificates (MMCs) were introduced, interest rates on very large bank deposits were freed, and a bankers' acceptance market for yen-denominated trade bills and a bond futures market were established. In the area of the Euro-yen market, the withholding tax on interest paid to nonresidents on bond issues by Japanese borrowers was repealed. With regard to foreign access to

1/ This report was reviewed in detail in "Japan--Recent Economic Developments," SM/85/56, Supplement 1.

Japanese financial markets, nine foreign banks were permitted to participate in trust banking, and membership of the Tokyo Stock Exchange has been expanded, thus permitting nonresident securities firms to join.

The bankers' acceptance market--the establishment of which has been regarded as a potentially important step in the internationalization of the yen--has not developed strongly. Use of the bankers' acceptance market by large firms has been limited because of lower costs in existing financing channels; the reluctance of banks to enlarge the scope of "spread banking" and the incidence of stamp duties have also been cited as factors. Measures currently planned to further develop short-term markets focus on the creation of a market for short-term government debt, which will also facilitate the conduct of monetary policy. The authorities obtained authorization in May 1985 to issue short-term government refinancing bonds, and are now finalizing details to allow short-term bonds to be issued beginning in 1986. Current plans are for the issue by public auction of bonds of maturity of up to six months and in large denominations for acquisition only by institutional and corporate investors; these bonds would be subject to withholding and capital gains taxes.

The authorities intend to reduce the present minimum denomination of deposits with market interest rates from ¥ 1 billion ($5 million) by the spring of 1987. At the same time, the minimum denominations for CDs and MMCs, at present ¥ 100 million ($500,000) and ¥ 50 million ($250,000), will be reduced; other limitations on the issue of these instruments are to be eased gradually. However, further progress in this direction would not appear to be feasible in the absence of reform of the postal saving system. In this regard, a number of critical issues in integrating postal savings into a market-oriented system are yet to be addressed, and are unlikely to be resolved in the near future. These include the various advantages granted to the postal savings system in attracting deposits under current regulations and restrictions on its asset management.

There has been increasing use of the Euro-yen bond market, mainly by nonresident issuers. Many nonresident issuers of Euro-yen bonds have swapped the proceeds into other currencies, while Japanese issuers have been able to obtain alternative yen financing on favorable terms through foreign currency bond issues with swap arrangements. Consideration is being given to further easing the qualification standards for Euro-yen bond issues by residents and nonresidents, and the regulations on the issuance of Euro-yen CDs. The authorities are also studying the establishment of an offshore market in Tokyo. They note that, beyond the development of a suitable institutional framework, the pace of development of the Euro-yen markets will depend on the emergence of strong demand for yen-denominated assets.

The authorities emphasize the importance of improvements in the supervision of financial institutions and other aspects of the regulatory framework to ensure stability of the system in a liberalized environment. Capital/asset and liquidity ratios and other prudential parameters are under review and legislation to strengthen and broaden the deposit insurance system is being prepared.

7. Capital flows to developing countries

During recent years, there has been a substantial increase in flows of capital from Japan to developing countries. The total flow of financial resources rose from $6 billion in 1980 to $16 billion in 1984. Official Development Assistance (ODA) reached $4.3 billion (0.35 percent of GDP) in 1984, up by 15 percent from 1983. ODA flows kept pace in yen terms with the authorities' target of doubling ODA in the five years to 1985, although, in U.S. dollar terms, they have fallen short of the target, reflecting principally the weakness of the yen against the dollar and lower internationally agreed funding for some multilateral agencies. In 1985, the Government announced a new target of doubling ODA in dollar terms over the next seven years; the authorities are confident that this target can be achieved.

Flows of private capital to developing countries have also increased sharply, rising from $2.0 billion (net) in 1980 to $11.0 billion in 1984. While there has been a net repayment of private export credits in recent years, and direct investment has shown large year-to-year fluctuations, private flows to multilateral agencies have grown substantially. Other bilateral credits, including bonds, have risen sharply--from $0.7 billion in 1980 to $7.8 billion in 1984. A notable feature of long-term flows has been the continuing access to the Japanese bond market of developing countries and of development finance institutions. In the first nine months of 1985, these categories of borrowers accounted for over two thirds of foreign issues and placements on the Japanese bond market, totaling approximately ¥ 900 billion ($3.8 billion) at an annual rate.

With regard to the international debt situation, the Japanese authorities welcomed the initiative taken at the 1985 Fund/Bank Annual Meetings by the Secretary of the U.S. Treasury. They expressed support for a strengthening of the debt strategy, emphasizing that this should be implemented strictly on a case-by-case basis, and that additional financing would need to be associated with effectively designed and monitored economic policies. They signaled also the importance of appropriate burden-sharing among commercial banks and among countries. Subsequently, in December 1985, leading Japanese banks addressed a message of support to the Managing Director of the Fund and the President of the World Bank. The banks welcomed the U.S. debt initiative as a positive and constructive approach, and indicated their willingness to participate, together with all other parties, on a case-by-case basis.

VI. Staff Appraisal

Japan's economic performance over the past three years has continued to be impressive: during these years, growth was in excess of 4 percent per annum, and it was accompanied by price stability, the creation of a large number of jobs and a decline in fiscal deficits. Japan's industry demonstrated its leadership, especially in areas such as consumer durables and high technology goods, the result of successful restructuring in the past, the rapid absorption of new technologies, and strong competitiveness. Certainly, this success has not been seen equally in all areas. The unemployment rate has remained high by past standards--although far below that experienced in virtually all other industrial countries--social overhead capital remains deficient in some areas, and private residential investment has been weak despite a lower standard of housing than in most other industrial countries. In all, however, the achievements provide eloquent witness that Japan's basic policy stance has been well-conceived.

The large external imbalances among the major industrial countries, of which Japan's current account surplus is a dramatic manifestation, and the deterioration in the international trade climate, have led to renewed efforts at international policy coordination among the major industrial countries. As part of these efforts, Japan intervened heavily in foreign exchange markets in conjunction with other countries, and tightened monetary conditions in late October. These policy initiatives have been successful in supporting a substantial appreciation of the yen vis-a-vis the U.S. dollar. The appreciation of the yen has clearly improved the prospects for external adjustment, though the current account surplus will probably continue to widen in dollar terms in the short run, reflecting the initial "J curve" effect of the stronger yen. Forecasts beyond 1986/87 must, of course, remain highly tentative, but the staff projects that the current account surplus may well stabilize in dollar terms in 1987/88, and decline further as a share of GNP.

External adjustment, as represented by this current account path, may be regarded as slow, but would, nevertheless, imply a substantial withdrawal of stimulus from the economy. At the same time, the staff does not foresee a marked acceleration of domestic demand in 1986/87, which, with the exception of investment in plant and equipment, has remained subdued throughout the upswing. While terms of trade gains--reflecting the appreciation of the yen and falling oil prices--should strengthen private consumption, private investment in plant and equipment is, in fact, likely to lose vigor. On the whole, based on present policies, the staff projects real growth of somewhat less than 3 percent in 1986/87, falling well short of the economy's potential.

This outlook--against the background of a pressing need for strong growth around the world--poses difficult policy challenges. The dilemmas for monetary and fiscal policy sharpen once again. In recent years, monetary policy has been aimed primarily at the exchange rate objective of preventing a weakness in the yen. In times of weak aggregate demand, such a policy would have, of course, a cost in terms of domestic economic objectives. Toward the end of 1985, monetary policy was used aggressively to support an appreciation of the yen while more recently, the opportunity provided by a further rise in the yen has been taken to cautiously reverse the earlier tightening, and the discount rate has been reduced. In the staff's view, the primacy given to exchange rate considerations in the conduct of monetary policy has been broadly appropriate. At the same time, any further opportunity afforded by a strengthening of the yen and/or a decline in foreign interest rates must be seized.

On the side of fiscal policy, the conflict--particularly sharp, again, in times of weak aggregate demand--is between the need to pursue the objective of fiscal consolidation and that to support demand. On occasions in the past when the conflict became particularly acute, the authorities demonstrated flexibility, by making allowance for conjunctural considerations in deciding on the progress to be made toward the former objective. The staff sees merit in the authorities' medium-term fiscal consolidation objective but has in the past also very much welcomed this flexibility, an approach broadly endorsed by Executive Directors. With the prospect that growth will be well below its potential, together with continuing low inflation and a large external surplus, the occasion for the demonstration of such a flexible attitude is at hand again. Moreover, it is to be noted that the objective of fiscal consolidation relates primarily to the central government's general account operations and scope still exists for action at other levels of government to support demand. To a degree, this is a reconciliation that the authorities have sought in their fiscal policy for the coming year. While the general account budget as recently presented reflects the precedence given to reducing the deficit by expenditure restraint, the authorities have, at the same time, made provision for increased expenditure by local governments and public enterprises.

The proposed general account budget for 1986/87, which provides for a reduction of the deficit to 3.2 percent of GNP from 4.0 percent in the previous year, would result in a sizable withdrawal of demand stimulus from the economy. This withdrawal would be mitigated to some extent by the expansionary impulse expected to emanate from the planned activities of other levels of the Government. In the staff's view, any withdrawal of demand stimulus would be inappropriate at a time when the economy is likely to be otherwise weak. The staff would, therefore, recommend that at least the automatic stabilizer be allowed to operate in the budgetary transactions of the general account. The budget is based on an estimated real income growth of 4 percent; to the extent that actual growth falls short of this estimate, creating a revenue shortfall, this should not be offset by raising taxes or cutting back expenditures even further. In addition, public works expenditures should be increased, at least to the extent necessary to compensate for the expenditure brought forward in the October 1985 measures to stimulate demand.

Even with these steps, there may still be some unwelcome withdrawal of demand from the economy by the public sector. Fiscal drag is likely to continue to hinder consumption growth in 1986/87, and an income tax cut in anticipation of a complete overhaul of the tax system to be introduced in 1987/88--an option firmly rejected by the authorities during the discussions--would serve a useful purpose and must be kept in mind. The staff fully supports the principal objectives guiding tax reform, and the broad dimensions of the reform, as they have been drawn so far, would indeed seem appropriate. The authorities' endeavor to provide better balance by reducing tax incentives which currently strongly favor savings would be part of this.

There is concern that a rapid decline in the public sector deficit would inhibit a reduction in the external imbalance. The authorities believe that a reduction in the size of government resulting from fiscal consolidation would bring about larger private investment. It is also possible that the expectation of lower future tax liabilities will reduce private saving. In any event, the increase in the ratio of retired to working-age persons and other changes in the population structure are likely to lead to a significant decline in the private saving rate in time. These factors may well be sufficient to promote an improvement in the saving/investment balance in a long-run perspective, but are unlikely to be effective in the coming few years. In this context, the Government's plans to strengthen the private sector and widen its scope through deregulation, privatization of public enterprises, and private sector participation in public works gain a special importance. However, these policies have yet to be fully specified and, on the basis of the general proposals made so far, it is not possible to assess that they will have a major macroeconomic impact in the near future.

In recent years, the role of market forces in the financial system has been strengthened and the foundations laid for the further development of Euro-yen markets and a larger international role for the yen. Long-term capital markets have emerged as an efficient conduit for channeling surplus savings to both domestic and foreign users, and there has been a closer integration of domestic and foreign markets and the various segments of the domestic money markets. However, liberalization of long-term capital markets has proceeded farther than that of short-term markets, and further steps to liberalize short-term markets are needed and should not be delayed. First, interest rates on smaller deposits need to be liberalized, and to do so will require reform of the postal saving system. The issues to be resolved are difficult ones, but they need to be addressed as a matter of priority. Second, the issuance of short-term government bonds and the evolution of a strong secondary market in such bonds would serve to facilitate monetary policy and provide investors, including foreign investors, with attractive assets. The staff hopes that short-term government bond issues in sizable amounts and with a suitably wide range of maturities and denominations can begin soon. Third, the remaining barriers between domestic and Euro-yen markets need to be dismantled, and the establishment of an offshore financial market deserves active consideration. The authorities' efforts to strengthen the regulatory framework to ensure the stability of the financial system in a liberalized environment are well conceived.

Japan has embarked on a systematic policy of opening its markets to imports. This is, indeed, commendable. As one of the largest trading nations, it is in Japan's vital interest to counter protectionist forces and the contribution Japan can make on a global scale to reducing trade friction and rolling back protectionism is large. Market opening and import promotion measures are unlikely to have a major impact on Japan's current account surplus, but their effect is far greater than the additional imports they elicit, for they influence the international trade climate in a substantial way. The measures so far introduced are wide ranging and the Action Program promises further liberalization in the course of the next two-and-a-half years. However, significant barriers remain.

Acting from a position of strength and with a record of successful structural adjustment in the past, Japan should take bold action to further open its markets. Such action would include reducing and eliminating tariffs on manufactured goods, reducing the level of protection of the agricultural sector, and addressing forcefully the barriers deriving from the regulatory framework. It is of particular importance that, as Japan moves up the technological ladder, markets become available to developing countries. Financial and other support to specific sectors that could impede structural change in the economy, including that encouraged by the appreciation of the yen, should be eliminated as soon as possible. Equally, other actions that serve to constrain free trade, on however informal a basis, should be avoided. Export restraint in various forms has been an important feature of the recent trend toward protectionism, and the staff hopes that the international situation will permit Japan soon to discontinue these trade practices. The staff welcomes Japan's leadership in the initiation of a new round of multilateral trade talks.

Japan has played an important role in channeling finance to developing countries. It will be important that official policies be oriented toward facilitating a return to prudent, spontaneous financing to countries rebuilding their creditworthiness and seeking to regain more normal access to commercial flows. Furthermore, Japan's participation in shaping and carrying out current plans to strengthen the debt strategy will be crucial to their success. There is also a need to ensure larger flows of official aid to developing countries. The staff welcomes the plan of doubling official assistance over the next seven years, but believes that aid should be increased even further.

The staff's message as contained in these pages is not one that promises, from possible actions on Japan's part, an easy or quick resolution of some of the major problems confronting the world economy. Payments disequilibria are, if anything, likely to be aggravated in the short run, notwithstanding the significant exchange rate realignment that has taken place; little immediate relief from protectionist pressures can, therefore, be expected from this source. Domestic demand in Japan, too, is unlikely to strengthen autonomously in the foreseeable future. Interest rates have come back down and the staff hopes that before long circumstances will make it possible to provide some further positive stimulus from this side. On the fiscal policy side, the authorities are firmly committed to achieving a better balance in the central government's general account and to reducing the size of the government, but the staff believes that there is, nonetheless, scope for action in support of demand. Fiscal consolidation, together with deregulation of the private sector, will probably help stimulate private investment, but one cannot be confident of the strength of this response. Larger wage increases, if these could be engineered, could stimulate private consumption but what is gained here may be lost, especially over the longer run, through a weakened incentive to invest. Japan can--and should--open its domestic markets further to the inflow of goods and services, but the contribution of this to reducing its current account surplus would not be large. Japan can--and should--take steps to further internationalize the yen but again the impact on the exchange rate is likely to be small in the short run.

In the longer run, some of the forces that are already in train in Japan--demographic and other--appear likely to work toward a reduction of the country's savings rate and thus of its current account surplus. The latter process will be helped to the extent that private investment picks up in response to government withdrawal or deregulation, an expectation that can clearly be entertained principally for the longer run. An unknown is the likely pace of technological progress and of its industrial application through new investment; it is not impossible that this will be a force making for increased absorption in Japan as the country responds to the new international challenge that it faces.

It is evident that dealing with the present tensions in the world economy--as reflected in the increasing disruption of trade flows--will require appropriate actions in the rest of the world as well as in Japan. International cooperation has recently received renewed impetus and Japan's contribution, in both formulating and implementing the international consensus, has been important. During the discussions in Tokyo, the staff team was impressed by the willingness of the Japanese authorities to take account of views expressed in international fora, and it can fairly be said that, in formulating their policies, they have demonstrated their preparedness to cooperate internationally. It is crucial that this approach be maintained and built upon by appropriate policy actions both in Japan and elsewhere.

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

JAPAN

Basic Data

Population
Total population (June 1985) 120,700,000
GNP per capita (1985) 1/2/ US$10,950

	1983 (Percent share)	1982	1983	1984	1985 2/
		(In trillions of yen)			
GDP 3/		269.6	280.1		
Agriculture	3.3	9.1	9.4		
Mining and manufacturing	29.4	79.5	82.4		
Services	63.3	166.6	177.1		
Other 5/	4.0	14.5	11.1		
GNP					
At constant 1980 prices		256.4	264.5	278.1	289.7
At current prices		269.7	280.4	298.6	316.2
		(Percentage changes over previous year in constant prices)			
Private consumption	52.5	4.1	3.2	2.9	2.7
Private residential investment	4.8	-0.7	-6.2	-2.2	3.0
Private equipment investment	17.2	2.5	2.9	10.7	11.0
Government consumption	9.4	1.9	2.8	2.6	2.5
Government investment	8.7	-1.0	-1.6	-2.9	-7.4
Stockbuilding 6/7/	0.3	-0.1	-0.4	0.5	--
Total domestic demand	92.8	2.8	1.7	3.9	3.3
Foreign balance 6/	7.2	0.3	1.5	1.3	0.9
Real GNP	100.0	3.1	3.2	5.1	4.2
Nominal GNP	...	5.0	4.0	6.5	5.9
Prices, income, and employment		(Percentage changes over previous year except where indicated)			
Wholesale prices		1.8	-2.2	-0.3	-0.9
Consumer prices		2.6	1.8	2.3	2.1
GNP deflator		1.9	0.8	1.3	1.7
Hourly compensation 8/		5.5	3.3	3.6	4.6
Real hourly compensation 8/9/		2.8	1.5	1.3	2.4
Real disposable income 9/10/		3.1	0.8	2.1	2.1
Average propensity to consume (in percent) 10/		79.3	79.1	78.7	78.1
Unemployment (in percent, period average)		2.4	2.6	2.7	2.6
Manufacturing					
Employment of regular workers		0.7	-0.1	1.4	1.2
Output		0.4	3.5	11.2	5.0
Productivity		0.1	3.0	8.1	3.6
Unit labor cost		5.1	0.3	-4.7	1.0
Inventory ratio (in percent) 11/		105.3	98.9	94.8	98.6

Basic Data (concluded)

	1982	1983	1984	1985 2/
Financial aggregates	(Percentage changes over previous year)			
M2 + CDs 12/	9.2	7.4	7.8	8.4
Domestic credit 13/	8.2	7.5	8.9	10.0
Public sector	5.2	2.3	6.6	2.5
Private sector	9.0	8.7	9.4	11.6
Fiscal aggregates	(Fiscal year basis, in trillions of yen)			
Central Government				
Revenues	33.2	35.6	38.2	40.3 14/
Expenditures	47.3	48.4	51.5	53.2 14/
Deficit (-)	-14.0	-12.8	-13.3	-12.9 14/
Deficit/GNP (in percent)	5.2	4.5	4.4	4.0 14/
Fiscal investment and loan program	20.6	20.7	19.6 15/	20.9 15/
General government				
Deficit/GNP (in percent)	-3.4	-3.0	...	...
Balance of payments	(In billions of U.S. dollars)			
Exports	137.7	145.5	168.3	174.0
Imports	-119.6	-114.0	-124.0	-118.0
Trade balance	18.1	31.5	44.3	56.0
Services and transfers	-11.2	-10.7	-9.3	-7.0
Current balance	6.9	20.8	35.0	49.0
Net long-term capital 16/	-15.0	-17.7	-49.7	-64.0
Japanese	-27.4	-32.5	-56.8	-80.0
Foreign	12.4	14.8	7.1	16.0
Basic balance	-8.1	3.1	-14.6	-15.0
Net short-term capital	3.2	-1.5	17.0	14.8
Nonbank 17/	3.2	2.1	-0.6	4.3
Bank	--	-3.6	17.6	10.5
Overall balance	-4.9	1.6	2.4	-0.2
Export volume	-2.4	8.6	15.7	4.7
Import volume	-0.5	1.2	10.8	--
Gross official reserves 18/	(At end of period, in billions of U.S. dollars)			
Total reserves	24.3	25.5	27.3	27.5
Exchange rates (period average)				
Effective exchange rate (MERM; 1980=100	106.6	117.3	124.1	127.1 19/
Real effective exchange rate (relative normalized unit labor costs; 1980=100)	95.8	99.7	100.8	96.4 20/
¥ per U.S. dollar	249.1	237.5	237.5	238.5 19/

1/ At an exchange rate of US$1 = ¥ 238.5
2/ Staff estimates.
3/ At market prices.
4/ 1982 percent share.
5/ Includes construction, statistical discrepancy, imputed interest, and import taxes.
6/ Contribution to real GNP.
7/ Includes public and private.
8/ Regular employees in the manufacturing sector.
9/ Deflated by CPI.
10/ Workers' households.
11/ Index of the ratio of producers' inventory to shipment.
12/ Period average.
13/ End of period.
14/ Revised budget.
15/ Initial budget.
16/ Excluding Gensaki transactions.
17/ Including Gensaki transactions and errors and omissions.
18/ Including gold (national valuation).
19/ Actual.
20/ Actual average of first three quarters.

Japan--Fund Relations

(As of December 31, 1985; in millions of SDRs)

I. Membership Status

(a) Japan became a member of the Fund on August 13, 1952.
(b) Japan has accepted the obligations of Article VIII, Sections 2, 3, and 4 of the Fund agreement.

A. Financial Relations

II. General Department (General Resources Account)

(a) Quota: SDR 4,223.3 million.
(b) Total Fund holdings of Japanese yen: SDR 2,815.1 million (66.7 percent of quota).
(c) Fund credit: None.
(d) Reserve tranche position: SDR 1,408.3 million.
(e) Current Operational Budget (maximum use of currency):

Purchases:	SDR 69.9 million
Repurchases:	SDR 73.7 million

(f) Lending to the Fund (amounts):

	Limits	Outstanding	Uncalled
GAB	2,125.0	--	2,125.0
SFF	900.0	662.8	--
Enlarged Access	525.0	...	...
Total	1,637.5	...	...

III. Current Stand-By or Extended Arrangement and Special Facilities

No use of Fund credit during the last ten years.

IV. SDR Department

(a) Net cumulative allocation: SDR 891.7 million.
(b) Holdings: SDR 1,926.2 million (216.0 percent of net cumulative allocation).
(c) Current Designation Plan (amount of maximum designation): None.

V. Administered Accounts

Not applicable.

VI. Overdue Obligations to the Fund (actual amounts and dates due)

None.

B. Nonfinancial Relations

VII. Exchange Rate Arrangements

The authorities in Japan do not maintain margins in respect of exchange transactions, and exchange rates are determined on the basis of demand and supply conditions in the exchange market. However, the authorities intervene from time to time to maintain orderly conditions in the exchange market. There are not taxes or subsidies on purchases or sales of foreign exchange. On December 31, the exchange rate of the yen, as determined by the Fund under Rule O-2(a), was SDR 0.00454064 per Japanese yen.

VIII. Last Article IV Consultation

The Staff Report for the 1984 Article IV consultation with Japan (SM/85/33) was considered by the Executive Board at EBM/84/34 (March 4, 1985). Japan is on a 12-month consultation cycle.

IX. Technical Assistance

Not applicable.

X. Resident Representative

Not applicable.

Japan--Statistical Issues

1. Outstanding statistical issues

Government finance

Due to the differing underlying methodologies and the resulting discrepancies between *IFS* data on government finance and the corresponding data reported for publication in the *Government Finance Statistics Yearbook*, the authorities have ceased providing data beyond 1979 for inclusion in *IFS*.

With regard to the *Yearbook*, data are lacking on the operations of social security funds and on the functional classification of expenditure and lending minus repayment. In addition, since the reported data on tax revenue are not adjusted for taxes not collected during the current fiscal year, it is not possible to compile realistic measures of government deficit/surplus and the associated financing. For this reason, reported data on these aggregates are not published in the *Yearbook*. The 1985 *Yearbook* will include incomplete data through 1974 for local governments.

2. Coverage, currentness, and reporting of data in IFS

The table below shows the currentness and coverage of data published in the country page for Japan in the February 1986 issue of *IFS*. The data are based on reports sent to the Fund's Bureau of Statistics by the Bank of Japan and the Ministry of Finance (government finance and balance of payments statistics), which during the past year have been provided on a timely basis.

Status of IFS Data

		Latest Data in February 1986 IFS
Real Sector	- National accounts	Q3 1985
	- Prices: consumer	October 1985
	wholesale	November 1985
	- Production: industrial	October 1985
	- Employment: manufacturing	October 1985
	- Earnings	October 1985
Government Finance	- Deficit/surplus	1979
	- Financing	1979
	- Debt	1979
Monetary Accounts	- Monetary authorities	November 1985
	- Deposit money banks	November 1985
	- Other financial institutions	Q2 1985
External Sector	- Merchandise trade: values	November 1985
	prices	November 1985
	- Balance of payments	August 1985
	- International reserves	December 1985
	- Exchange rates	December 1985