Japan's trade profile determined by IMF austerity, U.S. collapse

by David Goldman

U.S. Commerce Secretary Malcolm Baldrige's July 26 arrival in Tokyo provided the occasion for a new low point not only for the dollar/yen exchange rate, but for the coherence of American official statements as well. Baldrige told Prime Minister Yasuhiro Nakasone that the Reagan administration was "losing credibility" because the U.S. trade deficit with Japan had grown into the $60 billion per annum range, and demanded that Japan adopt a target for increased imports.

With some patience, Nakasone told Baldrige he shared the U.S. administration's concerns about protectionist measures in the United States and pointed out that Tokyo was already following an open-market policy. Baldrige responded that Japanese imports of U.S. goods had not increased, even though Tokyo had reduced its trade barriers. "It's not just a question of lowering barriers," Baldrige said. "It's a question of the will of the Japanese people to accept imports."

The U.S. commerce secretary could not deny the obvious, namely, that 1) Japan's currency has appreciated by almost 40% against the dollar since September 1985, drastically increasing the cost of Japanese goods in the United States; 2) Japan has had the lowest tariff barriers of any industrial nation since 1980; 3) Japan has bent over backwards to simplify procedures for American exporters to its home market. In the absence of any Japanese policy which might be construed to undermine cooperation with Washington, Baldrige came up with the strange suggestion that the Japanese people, by some silent conspiracy, boycott American goods.

The implication could not be more ridiculous, nor at greater variance with the facts. McKinsey and Co.'s Tokyo office chief Kenichi Ohmae has presented data before the National Press Club, and in various print media, showing that the Japanese buy far more American brand-name goods than Americans buy Japanese brand-name goods. As of 1984, Ohmae calculates, the average Japanese bought $215 of imported U.S. goods, while the average American bought $243 of Japanese goods. However, each Japanese bought an additional $368 of American goods produced in Japan; the average American bought only $44 of Japanese goods produced in the United States.

The Japanese total purchases of American-brand goods amounted to $583 per person, or 6% of Japan's national income, while the American total amounted to only $287, roughly half as much, and only 2% of U.S. national income.

Clearly, Baldrige is talking rubbish, and the enormous Japanese trade surplus with the United States is of entirely different origin. Unfortunately, Nakasone's administration has contributed little clarity to the discussion. Japan's own policy, formulated in the "Report of the Advisory Group on Economic Structural Adjustment" of April 7, 1986, propitiates the extravagant misconceptions of the United States, and thus perpetuates them. The report, drafted under the leadership of Haruo Maekawa, calls for "balanced economic growth and resultant import expansion," "striving for economic growth led by domestic demand," "liberalization and internationalization of the nation's financial and capital markets," and so forth. The mechanism would involve "domestic demand expansion policies that have large multiplier effects and will lead to increased private consumption," such as housing subsidies, social infrastructure spending, and tax cuts to increase disposable income.

The Maekawa Report provides a set of recommendations which correspond to the U.S. administration's demand, presented at the May Summit of top OECD nations in Tokyo and elsewhere, that Japan undertake domestic reflation in order to stimulate economic activity, and, presumably, increase imports from the United States, lowering its huge trade surplus. As a conciliatory gesture, the Maekawa recommendations have already failed, through no fault of the Japanese; as Federal Reserve chairman Paul Volcker has made painfully clear, the talk of stimulating economic activity merely packaged a more urgent demand: that Japan (along with Germany) join the Federal Reserve in a rapid monetary inflation, in order to prop up the crumbling world financial structure, without collapsing the U.S. dollar. This the Japanese have refused to do, with good reason. Why should Japan mortgage its currency to the endangered U.S. banking system?

Japan's trade profile

Japan has, in fact, had little choice concerning where the fruits of its diligent and productive industry would be channeled in the world market. We will show in the following analysis of Japanese trade, that two overriding developments in the world economy produced the Japanese trade surplus in its present, contested form. The first is the destruction of developing-sector trade at the hands of the International Monetary Fund; the second is the collapse of American industry, especially capital-goods capacity.

The assumption underlying the absurdities in Commerce Secretary Baldrige's position is that the world economy has been in recovery for the past several years, but that the Japanese have, somehow, captured an excessive portion of the recovering world market. On the contrary: The most readily available data concerning international trade show that Japan's trade profile is dictated by a global depression, rather than recovery, in world trade.

World trade has fallen, not risen, since the first full year of the present world depression, namely 1980. In 1980, all the world's nations exported a grand total of $1.9 trillion in physical goods. By 1983, the volume had fallen to $1.67 trillion, or about 12% less. At the height of the supposed "recovery," in 1985, world exports were only $1.72 trillion, still 10% lower than the 1980 level. During the 1975-80 period, world trade had *grown* by 5% a year.

TABLE 1

Geographical distribution of Japanese trade

All figures in percent; negative numbers denoted by (-)

	1965	1968	1972	1976	1980	1984
OECD						
Exports	49.3	50.9	55.0	46.3	46.1	56.0
Imports	49.8	50.3	50.9	39.1	33.7	39.0
Balance	35.3	45.3	73.7	240	106	124.7
Non-OECD						
Exports	50.7	49.1	45.0	54.7	53.9	44.0
Imports	50.2	49.0	49.1	60.9	66.3	61.0
Balance	63.8	—	6.1	140	206	24.7
U.S.A.						
Exports	29.7	31.9	31.4	23.7	24.5	35.6
Imports	29.0	24.7	25.0	18.3	17.4	19.8
Balance	51.1	59.0	60.8	167.1	62.6	99.5
OPEC						
Exports	6.5	5.0	6.5	13.8	14.3	9.3
Imports	14.8	15.3	19.5	33.7	40.2	30.4
Balance	(-2.35)	—	(-8.1)	(-519)	(-332)	(-75.9)
Africa						
Exports	9.6	7.1	7.1	8.6	5.9	3.7
Imports	4.3	6.4	5.0	3.2	3.2	2.3
Balance	1.6	—	17.2	15.1	28.0	9.3
Ibero-America						
Exports	5.4	5.4	6.5	7.1	6.5	4.7
Imports	8.7	7.4	6.0	3.7	4.0	5.2
Balance	(-8.6)	—	2.0	1.0	24.5	2.5
Asia						
Exports	26.9	28.3	23.9	23.7	28.1	26.1
Imports	19.2	16.6	19.7	23.0	25.8	27.9
Balance	2.5	—	43.0	42.3	1.0	18.9

Source: Organization for Economic Cooperation and Development (OECD)

The true position of world trade is even worse than the numbers show. To start with, American imports rose from $256 billion in 1980, to $361 billion in 1985. These imports, bought at 40% to 70% below American producer prices, merely replaced production capacity we lost at home. In other words, the increase in U.S. imports reflects, not economic growth, but decay. Total world trade in 1985 *minus* the $104 billion increase in U.S. imports was only $1.663 trillion, lower than the supposed nadir of international trade in 1983, when exports fell to $1.667 trillion.

Developing-sector collapse

Table 1 shows the percentage of Japan's exports and imports to and from the world's major trading areas, during the past 20 years. One fact jumps out of the data: Between 1980 and 1984, a net swing occurred of about 20% in total Japanese exports, favoring the OECD nations (the world's top 20 non-communist industrial nations) at the expense of the developing sector. That swing reversed a historical pattern over the 15 years 1965-80, which showed a slow shift toward the developing world.

That this should have happened is no surprise whatever; the collapse of the financial position of the developing world began in 1980, after the "second oil shock" in 1979, leading to the global debt crisis of 1982, and the imposition of International Monetary Fund conditionalities upon virtually the entire developing world. Previously, Japan's exports to non-OECD countries, i.e., developing-sector economies, had risen from 50.7% to 54.7% of total exports, between 1965 and 1976, and maintained approximately that level through 1980.

Clearly, the largest component of the increased exports to non-OECD countries went to the newly rich OPEC nations, which absorbed 14.3% of Japanese shipments in 1980, against only 6.5% in 1965. However, the other major developing-sector markets, Asia and Ibero-America, also showed significant increases over the earlier period.

Uniformly, Japan's exports to the developing sector collapsed after 1980, as a proportion of total exports. With the exception of the Asian market, Japanese exports fell in absolute terms as well. Exports to Ibero-America fell from $8.48 billion to $7.95 billion, a fall of 6.3%; exports to Africa fell from $7.70 billion to $6.23 billion, a fall of 21.2%. Exports to Asian developing nations, however, rose from $36.38 billion to $44.316 billion, an increase of 22% in absolute terms.

American industrial decay

Japan's orientation to the OECD market, and to the American market in particular, is evident from Table 1. Exports to the United States rose from 29.7% of the total in 1965, to 35.6% of the total in 1984, and have no doubt risen further since. As the table shows, Japan's trade surplus with the United States is equal to its entire global trade balance (in fact, Japan's oil imports still produce a deficit in its trade with non-OECD nations, equal to about a fifth of its surplus with respect to the OECD as a whole).

None of these results should be the subject of any surprise. Remarkable, however, is the change in the *composition* of Japan's exports, shown in **Table 2**.

Between 1972 and 1984, capital equipment rose from 26.1% of Japanese exports, to 46.8%. Consumer durable goods also rose, but by much less, i.e., from 20% to 28.3%. However, consumer durables barely rose during the 1980-84 period, from 27.4% to 28.3%, as a portion of the total. During the same four years, capital-goods exports rose from 40.1% to 46.8%.

TABLE 2

Composition of Japanese exports by industrial category

(All figures in percent)

	1972	1976	1980	1984
Industrial supplies	31.0	32.9	28.6	21.7
Capital equipment	26.1	40.3	40.1	46.8
Consumer non-durables	3.1	1.3	1.1	1.1
Consumer durables	20.0	22.6	27.4	28.3

That result runs at variance with the popular image of a Japan flooding the American domestic market with automobiles, television sets, tape recorders, and microwave ovens. In fact, an enormous net swing toward capital-equipment exports coincided with the increase of exports to the United States. Capital equipment outweighs consumer durables by a full two-thirds in Japan's export profile.

Because Japan has maintained such a high volume of capital-equipment exports, it has uniquely succeeded in maintaining the capital-intensivity of home industrial production. **Table 3** reviews the last five years' industrial-output results, showing that Japanese capital-goods production in 1985 had risen 34% above the 1980 level, and much faster than the overall industrial production index. Consumer-durables production rose even faster than capital-goods production, although capital-goods exports rose faster than consumer-goods exports. This provokes a conclusion, once again, opposite to the usual prejudice. Rather than dumping consumer goods on the West to re-tool industry at home, the Japanese are exporting more capital goods, and consuming comparatively more industrial goods at home.

According to an *EIR* survey of American capital-goods purchasers, U.S. manufacturers prefer Japanese capital equipment over American in the following principal areas: pharmaceuticals, machine tools, forging, flexible manufac-

TABLE 3
Japanese industrial production index by sector

	1980	1981	1982	1983	1984	1985
Industrial supplies	100.0	97.3	96.4	100.5	111.5	114.6
Capital equipment	100.0	106.0	106.4	106.2	123.3	134.0
Consumer non-durable	100.0	103.3	106.5	110.0	113.0	116.2
Consumer durables	100.0	107.8	110.1	117.5	136.9	147.7
Total	100.0	101.0	101.4	105.0	116.5	121.7

turing, cement, materials-handling, steel-making, electronic components, and electrical distribution equipment.

In numerous interviews with U.S. industry specialists, *EIR* was told that American manufacturers prefer Japanese equipment regardless of cost, because it is superior. In some cases, e.g., pharmaceutical equipment, steel-making technology, cement-making equipment, and electronic component production, American manufacturers cannot find an American product that meets their standards, and have no choice but to import equipment from Japan.

A December 1985 publication of the Japan Institute for Economic and Social Affairs, entitled, *Trading with Japan,* seeks to defend Japan's capital-goods exports in this light. Answering the question, "Aren't Japanese exports destroying America's industrial base?" the Institute argues:

"The idea that Japanese exports are destroying America's industrial base disregards two facts. One is that Japan is supplying American businesses with a large and growing volume of capital goods—goods that are enhancing the production capacity of the purchasing corporations. The other is that a global integration of corporate activities is underway, and exports in categories reflecting this integration—roughly 30% of Japan's exports to the United States—in many cases are indispensable to the U.S. companies that purchase them.

"For example, Japan supplies many parts for use in U.S. manufacturing, and it offers finished goods through original equipment manufacturing (OEM) arrangements, in which the purchaser's brand name is put on the product; these supplies of parts and OEM products allow U.S. corporations to respond to needs of their customers that they cannot meet with their own production facilities. Two other export categories of this sort are goods not produced in significant numbers in the United States and goods produced in Japan by affiliates of U.S. companies."

The Institute's report includes **Table 4,** breaking down the origin of the 30% of Japan's exports to the United States arising from "economic integration."

According to data prepared for a *White Paper on International Trade* published by Japan's Ministry of International Trade and Industry (MITI) in 1985, the United States imported 23% of its total capital-goods purchases in 1984, against only 10% in 1975. Japan was the most important, but not the only source, of these capital goods. In 1984, America bought slightly over $20 billion of capital equipment from Japan, along with about $15 billion from the European Economic Community, and about $12 billion from Asia excluding Japan.

The view from MITI

In summary, the collapse of American productive capacity, most of all in the capital-goods sector, created America's trade deficit with Japan. Hiroshi Ushida, head of the MITI, reviewed the problem with unusual bluntness at a March 13 symposium in Tokyo:

"The major problem currently faced by the United States is the reduction of budgetary and trade deficits. However, even if these deficits were successfully reduced for the time being through strong U.S. government action or the large-scale cooperation of other governments, the result would still be only the treatment of the symptoms of the emergency patient, and not the basic rebuilding of the patient's physical makeup. . . . the [U.S.] rate of increase of industrial productivity has been falling off from year to year. If the growth rate of productivity continues to be low for a long time, a great drop in American competitive strength could not be avoided.

"The problem of American productivity is widely recognized as being rooted in such basic factors as capital, labor, managerial strength, and labor-management relations. If the

TABLE 4

Type of production	Exports to U.S. ($ billions)
U.S. companies' exports to the U.S.	$2
Original equipment manufacturing	$5
Parts	$8
Assembly in U.S.	$4
Total	$19

United States wishes to reduce its trade deficit, it ought to devote special efforts to the improvement of these factors at the same time that it requests other nations to cooperate. . . .

"Another cause of the trade imbalance is the creation of cavities, or 'hollowing,' in American industry; that is, American manufacturers have moved major portions of their production to locations abroad instead of investing within their own country to improve productivity."

Japan's financial power

During the five years from 1981 through the end of 1986, Japan will have accumulated current-account surpluses in excess of $170 billion. (By contrast, the United States owes $170 billion net to foreigners, and the total is rising by $150 billion per annum.) That is almost equal to the $189 billion collective surplus of the oil-exporting nations during the 1979-81 peak of their financial power. The shift in the world's center of financial power from OPEC to Japan is evident in **Table 5.**

TABLE 5
Current account surplus (deficit)

	Oil exporting nations	Japan
1979	54.0	(7.9)
1980	100.1	(9.5)
1981	34.7	6.2
1982	(23.4)	8.1
1983	(17.0)	22.2
1984	(5.7)	36.4
1985	(8.9)	40.9
1986	(30)*	60*
Cumulative	$103.8	156.4

Japan has invested virtually all of its accumulated wealth in the United States, "which has kept interest rates from rising even further than they have and has financed investment beyond that level that domestic saving alone would have allowed," as the Japan Institute for Social and Economic Research notes in the cited report. Japan will put about $60 billion into U.S. markets this year.

How decisive the Japanese surplus has become for U.S. markets was made clear last May, when fears of a pullout, or even of a reduction of new inflows, provoked the worst week in U.S. bond market history. Wall Street bond traders reprogrammed their trading computers to show the yen-dollar exchange rate at all times. Of course, no such flight of Japanese funds occurred; the last thing the Japanese want at this point is to undermine the American market.

Apart from the Japanese surplus, the $150 billion per year capital inflow into the United States almost is entirely in anonymous funds, largely of criminal or dubious origin. In the December 1985 *EIR Quarterly Report,* we demonstrated that $80 billion per year of the $150 billion in annual capital imports to the United States derive from untraceable sources. Approximately $50 billion per year of capital inflows is reported as "errors and omissions" on the balance-of-payments tables, and an additional $30 billion reflects sales of securities to the equivalent of numbered Swiss bank accounts. This category consists mainly of sales of Eurobonds by American corporations, to anonymous investors. Narcotics revenues—the so-called narco-dollars—account for the majority of such untraceable capital inflows.

Japan's alternatives

EIR has reported the likelihood of a near-term breakdown in the offshore "Eurodollar market," endangering America's capacity to finance its payments deficit. Under circumstances of general financial crisis, the mechanisms which have mediated $80 billion a year of anonymous money into the United States cannot function. Japan may emerge, by the end of this year, as the only major source of financing for America's balance-of-payments deficit.

This circumstance identifies a special sort of leverage which Japan will enjoy in world economic affairs. As the only functioning industrial economy in the world, Japan has replaced production and trade forfeited by other sectors. Apart from the global gray market in loose funds, it is the world's only significant financial power. Japanese officials frequently make reference to their nation's need to play a role in world affairs commensurate with its economic strength. As the financial crisis unfolds, Japan will have no other choice. The above data demonstrate that Japan has become massively dependent upon the American market, although through no fault of its own. A financial crisis which undermined the American market would provoke a devastating economic crisis in Japan, unless the Japanese themselves lead the introduction of policies to resolve it.

As MITI director Ushida emphasizes, nothing short of rebuilding the shattered import-absorption capacity of the developing world can solve the crisis. Japan has an opportunity ready-made to redeploy its financial su lus on behalf of this goal, in the form of the "Marshall Plan" initiatives proposed for the Middle East, South Africa, Ibero-America, and ASEAN. Israel Prime Minister Shimon Peres's proposal for a Middle East "Marshall Plan" is consistent, both in economic and political terms, with the African "Marshall Plan" under consideration by Britain's House of Commons, and the ASEAN development proposal offered by Japanese Foreign Minister Shintaro Abe earlier this year.

These initiatives require a fund based on contributions from participating governments. As the wealthiest industrial nation, Japan has a great deal to offer such initiatives, and thus a decisive role to play in the reconstruction of the world economy.