Postwar Economy

Reconstruction
Political Reform

- New constitution
  - People (not emperor) are sovereign
  - Women given right to vote
  - Renunciation of war
  - Military forces permanently banned

<table>
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<tr>
<th>Military expenditures as % GNP (1970)</th>
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<tr>
<td>Japan</td>
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<td>0.8</td>
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Political Reform

• Political Parties – spectrum of parties dominated by conservatism

• 1953
  – Democratic and Liberal Party merge → LDP
    • Big business, farmers, and small business

• Left never extends powerbase beyond labor and intellectuals
  – Democratic Socialists, Komeito, Communists control 35-40% of Diet

• LDP controls Diet continuously
  – Except briefly in 1993 and 2009
Banking and Financial Institutions

- Occupation initially wanted to split up large commercial banks
  - Some of these were zaibatsu owned
  - But the occupation goal shifts from reform to recovery
  - So big commercial “city” banks survived and continued to dominate their fields
  - In 1970 the top 15 of 76 commercial banks accounted for 65% of all commercial banks’ assets, loans, advances, and deposits
Banking and Financial Institutions

• Occupation promoted widespread stock ownership by reviving and reforming Japan’s stock market
  – Stocks gained rapidly (from very small base)
  – But remained unimportant relative to other sources of financing
  – Personal savings were high, but flowed into banks (not equity)
  – Firms borrow from banks (rather than raise equity)
Stock Market

• Stock market reopens in 1949
• Ministry of Finance makes it difficult to raise funding through equity issues
  – Existing equity holders had the right to buy new issues at par rate (face value), below the market rate
  – Dividends were required to rise after stock issues until 1996
  – Fixed commission rates deterred the development of a secondary market
  – Set tough criteria on dividend payouts and profitability before the issuance of stock
  – Increased importance of bank financing
Capital Markets

Ownership of Japanese Securities

Year

Percent Ownership

Financial Institutions (excluding Inv. Trusts and Sec. Co.'s)
- Non-financial Enterprises
- All Corporations
- Individuals
- Foreigners
Banking and Financial Institutions

• Temporary Interest Rate Adjustment Law of 1947
  – Regulates interest rates
• Banks are forbidden from underwriting bond issues (similar to US law)
• Ministry of Finance placed regulations on the bond market by permitting a bond cartel (Kisai kai)
Bond Market

• Membership consisted of bureaucrats and bankers
  – Set coupon rates, issue price, and amount of issue until 1955

• Later regulations
  – Only fully secured bonds issues were permitted
  – Yields were set artificially low which reduced demand
  – Minimum firm size levels were set for bond issuers

• Necessary because interest rates were set artificially low
  – Corporate bonds were rationed because government bonds and bonds by public enterprises were given priority (until late 1960s)

• Limited bond market prevented the development of rating agencies

• Also hurt newcomers
Bond and Equity Issues As a Share of External Finance

(Ueda)
Banking and Financial Institutions

• Business use short term loans from banks to finance long term needs
  – Dangerous for everyone
    • Business face fixed finance charges
    • Banks are illiquid
  – But everyone cuts risks elsewhere
    • Big companies diversify and use subcontractors whom they can drop in hard times
    • Big banks share big loans with other banks, place personnel into advisory positions in firms
    • BOJ will bail them out
Administrative Guidance

• Occupation unintentionally bolstered “administrative guidance”

• Government identifies objectives and priorities for Japanese economy and facilitates achieving these goals

• Not a planned economy like old Soviet Union
  – Business and government are in close communication
  – Business has considerable initiative and independence
Administrative Guidance

• Business listens to government goals and priorities because
  – Reluctance on either party (gov or business) to unilaterally adopt policies or make moves in important areas without consulting each other
  – Japanese prefer consensual approach to harmonizing differences which may exist within and between groups
Administrative Guidance

• Occupation made at least 4 decisions which facilitated administrative guidance

1. Did not change Japan’s central banking system (Ministry of Finance controls increasingly important Bank of Japan)

2. Let Japan set up government banks to make public loans to key industries (Reconstruction Finance Bank → Japan Development Bank)
3. Demanded that Japan create a national planning agency to set priorities for postwar reconstruction
   → Economic Planning Agency (EPA) 1946
4. Decided in 1949-50 that Japanese government should control business access to imports of goods, foreign capital, and technology
Economic Planning Agency

• Performed services (wielded little power)
• Drew up 5 years plans
  – More forecasts than plans
• Checked trends in productivity of capital and labor
  – When productivity declined, they encouraged new resources to move into newer areas instead
• Watched production trends abroad to figure out likely growth industries and declining industries
• In 2001 merged with MITI to become METI
Administrative Guidance

- Government influenced which companies would get essential products from abroad
- Government shielded certain industries from foreign competition or expose them to it