

Mobilising International Surpluses for World Development: A Wider plan for a Japanese initiative

Report of a Study Group of the World Institute for Development Economics Research (WIDER), Helsinki, Finland, of the United Nations University (UNU), Tokyo, Japan

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A Seven-Point Plan

1. The international community should find methods to sustain higher growth in Japan in order to offset the decline in the momentum of the U.S. and counter any tendency towards world deflation.

2. While a part of the required policies would involve stepping up Japanese investment geared to her domestic market, there are real difficulties in absorbing domestically a rate of savings as high as 27 per cent of GNP.

3. For Japan's growth momentum to be sustained, therefore, there is a need for her to continue to rely to a substantial extent on export-led growth and to maintain a significant current account surplus in her balance of payments, in order to enable her to continue to "export" her excess savings abroad.

4. Japan's large current account surplus and her finding a large export market was primarily due to her comparative advantage in her export sectors, but she was also helped by the vast U.S. budget, and consequently, trade deficit.

5. Any reduction in the U.S. budget and trade deficit would tend to shrink, in the absence of offsetting policies, the external market for Japan, and reduce her economic growth and hence in the world economy. One such offsetting policy measure would be to enhance the import capacity of developing countries. This can be accomplished by re-directing the Japanese surplus to finance the deficits of the developing countries. This means that excess Japanese savings which cannot be absorbed domestically or in the U.S. can find a home in financing productive capital formation in the developing countries.

6. There is a need, therefore, for evolving mechanisms for financial intermediation of Japan's surplus towards this end.

7. Once this principle is accepted, the specific financial instruments and

mechanisms can be worked out. They range from the notion of a Japanese Marshall Plan for the developing countries as has been recently proposed, to mechanisms for promoting Japanese investment in developing countries and increased lending by the Japanese international banks. Since the inter-mediation mechanisms have to enable private Japanese savings to find an outlet in developing countries, there may be a need for the Japanese government to promote this process either by subsidising the interest rate on loans to developing countries or by providing some collateral to Japanese private savings institutions to make investment in developing countries attractive.

The considerable reduction in recent years in Japan's fiscal deficit in relation to GNP and in her interest rates should permit this to happen with relative ease in the coming years. In this context the Japanese government could take the initiative of contributing one-tenth of one per cent (0.1 per cent) of her GNP to set up an international fund, while simultaneously inviting other industrial countries to join the fund by making a similar contribution. The fund would permit concessions and incentives of the sort mentioned above which would mobilize private capital flows to developing countries that are a substantial multiple of the resources available from the fund.

Summary

The Study Group arrived at the following conclusions and recommendations:

1. Substantial surpluses on current account are likely to prevail for the next several years among many developed countries, and there is a need for their diversification towards meeting developing country requirements, both on intrinsic grounds, and in the interest of promoting global economic stability.

2. Japan, in particular, should take an initiative to launch a \$ 125 billion five-year plan for resource transfers to developing countries, at an annual rate of \$25 billion. Such an initiative is fully in line with the

three-year programme already begun by Japan for the period 1987-89; if matched by other developed countries, the joint effort would contribute significantly to world development. Depending on the persistence of Japan's current account surplus, the plan might be extended beyond five years.

3. The ideal mechanism for implementing such a Japanese initiative would be to equip a Japanese Government Agency with an explicit government guarantee that will enable it to borrow in the domestic capital market on market terms, with resources for an appropriate level of interest subsidy to be provided to it by a suitable reallocation of Japanese Official Development Assistance.

4. In the Japanese context, the following equivalent mechanisms are also available:

(a) Loans raised under the guarantee of a suitable agency, a Japanese Trust Fund might be covered by private reinsurance arrangements.

(b) Developing countries might borrow from the Japanese commercial banking system against the collateral of zero coupon bonds purchased from the Japanese or international market, or specially issued by the Japanese Government. The amounts borrowed would be a substantial multiple of the investment needed to buy these bonds, whose face value on maturity will be equivalent to the principal borrowed, thereby fully securing the "bullet" repayment of the principal.

The most appropriate mechanism for this form of borrowing would be through a Japanese Trust Fund located in Tokyo and liaising with the World Bank and other regional development banks, for administering the scheme. It could, alternatively, be located within the World Bank, especially if other countries were to join in adding resources to the facility. Its management might be entrusted to a Policy Co-ordination Committee including commercial banks, the Bretton Woods institutions and major developed countries in order to facilitate the evolution of longer-term policy frameworks for lending.

The Trust Fund would purchase the zero coupon bonds from the Japanese Government and from the market, borrow in its own name from the Japanese commercial banking system and from the market, and relend these monies to developing countries at a suitable blended rate.

In order to support a five-year programme of borrowing annually of \$10 billion, with a possible extension to ten years, the Trust Fund would ideally need resources from the Japanese Government for the purchase of the bonds to be used as collateral. This would have no immediate net financial

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impact on the Japanese budget, since the funds would return to the budget when the bonds are purchased. The interest subsidy needed to provide a representative blended rate for lending at below the market rate for borrowing, can be met for the duration of the lending programme, out of the **Increment in Official Development Assistance during the period 1987-1991.**

(c) **Recourse could be had to the Export Import Bank of Japan to step up its co-financing arrangements beyond the recent levels of \$2 billion a year, by drawing more substantially on a pool of resources totalling \$150 billion annually that are available to the Zaisei-Toyushi— the Government's Fiscal Investment and Loan Programme (FILP). Additional amounts in the region of \$10 billion annually for a five-year period, with an extension to ten years if desired, are entirely feasible on this basis.**

(b) **The Export Import Bank of Japan has an unutilized guarantee power of around \$40 billion which could be utilized in a variety of ways for increased transfers to developing countries; the guarantee power itself could be increased either by increasing the Bank's capital or by varying its gearing ratio.**

(e) **The International Monetary Fund should be enabled to borrow in Japan's capital market at the rate of \$5 billion annually for the purpose of programme lending to low-income developing countries, under the IMF's Extended Financing Facility. The Japanese Government should provide an interest subsidy to reduce the cost of these funds to the user.**

(f) **A debt restructuring facility, utilizing market mechanisms, might be established on a Japanese initiative, in order to pave the way for a resumption of lending to debtor countries.**

(g) **Lending under these programmes might focus on infrastructure development, in addition to normal project and programme lending in support of growth-oriented adjustment programmes.**

5. Japan is in a position to aim for a tripling of Official Development Assistance over the period 1985-90. ■