

Part 1: Fiscal and Monetary Policies in the Reconstruction Years

Preface

This book treats the postwar reconstruction period as beginning in the mid-1940s. Differences in terms of the objectives of fiscal and monetary policy, the stability of political and administrative systems, and economic growth rates mandate that this period be distinguished from the “high growth” period that followed it. For our purposes, we will use the year 1955 as a general dividing line. The postwar reconstruction period was marked by the devastation of the wealth and people of Japan by the war, the need to repatriate soldiers and colonists from former territories, and the economic democratization and industrial demilitarization policies of the Supreme Commander for the Allied Powers (SCAP).

We will begin our study by dividing the postwar reconstruction period into three sub-periods: the period from the surrender to the end of 1948; the years from the enactment of the Dodge Plan in 1949 to the San Francisco peace treaty; and the period extending from the peace treaty until the mid-1950s. Political and economic conditions during each of these sub-periods will be considered in light of the general concerns and trends outlined above.

The first sub-period is characterized by policies aimed at rebuilding the economy after the war, while at the same time combating a strong inflationary bias. The Priority Production Plan and lending by the Reconstruction Finance Bank enabled a priority on reconstruction to be maintained, but shortages led to rampant inflation.

The second period begins with the highly deflationary policies of the Dodge Plan and a shift in the objectives of fiscal and monetary policy to a stress on economic stability. During this period, Japan succeeded in quelling inflation, and turned its sights to expanding private-sector trade and rejoining the international economy as soon as a formal peace treaty was in place.

The third period marks the transition to both political independence and high economic growth. It was notable for both strained public finances (in the wake of the Korean War) and sustained economic stability.

In addition to the issues outlined above, the postwar reconstruction period was distinguished by policies designed to democratize and demilitarize the economy, which were given a strong push at the insistence of SCAP. These special postwar policies generally overlap two or more of the sub-periods we have defined.

Before exploring the fiscal and monetary policies during the postwar reconstruction period, let us first survey the economic circumstances in which Japan found itself at the end of the war, its cities devastated and its troops and colonists returning home. Following that, we will look briefly at economic trends in each of the periods under consideration, before moving on to a discussion of fiscal and monetary policies.