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Monetary Foundations for the Era of "Pax Nipponica"

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This paper considers the principle of real currency convertibility which provided the fundamental stability of both the pound sterling and the US dollar during their respective periods of world economic dominance. It then considers a modern version of currency convertibility, namely convertibility based on a range of primary commodities, which has been supported by a number of leading economists, including Fisher, Keynes and Hayek. The potential benefits of implementing this are discussed, as well as the difficulties facing these economists' proposals.

The paper then considers the innovative system of conditional currency convertibility devised by the little-known Australian economist Grondona. This would be much easier to implement than other proposals; would have much greater benefits with much less stress on the economy; and would be suitable for implementation by Japan. In the absence of economic leadership from other countries, and in the face of the economic and social challenges facing Japanese society, the implementation of conditional convertibility of the Yen in this way would appear to be highly desirable, and could provide a valuable example for the rest of the world.

1. Introduction

Following Japan's unique success in developing a world-leading industrial economy outside the European/American cultural tradition, the possibility of Japan succeeding the USA in providing world economic leadership has become a subject of discussion. As part of this discussion, the phrase "Pax Nipponica" has been used to indicate the succession from "Pax Britannica" and "Pax Americana" (Park, 1992).

It is clear that such a "Pax Nipponica" would differ substantially from the two previous eras. In particular, in the currently proposed change of leadership, military power and economic power are not moving together. This raises interesting questions about the meaning of the proposed "Pax Nipponica". Among various possibilities, one meaning is for Japan to become the leading example for other countries wishing to develop economically through sustainable, consumer-led technological development.

A further role for Japan, which would seem necessary if "Pax Nipponica" is to be an appropriate title, is to provide global leadership in maintaining international financial stability, as Britain and the USA provided in their respective heydays.

The growing international role of the Yen, and the need for its further evolution are discussed by Takuwa (1992). This is an important consideration since the use of a nation's currency as an international reserve currency imposes externally generated stresses on its value, requiring appropriate responses from the national monetary authorities. Furthermore, in order to qualify as "Pax Nipponica" it would be necessary for such financial leadership to continue over a timescale of generations. Thus it is interesting to consider what monetary foundations might be created in order to make such leadership possible.

In the change from Pax Britannica to Pax Americana, the end of the former era and the start of the latter were not simultaneous. Pax Britannica is commonly considered to have ended when sterling's fixed convertibility into gold was abandoned after nearly two hundred years. (The sterling "gold standard" that lasted until 1914 was established in 1717 by Sir Isaac Newton. During this period the Bank of England stood ready to exchange gold for sterling on demand at the upper and lower "gold points" of £3.89375 and £3.8875 per ounce of 22 carat gold.)

Pax Americana can perhaps most reasonably be said to have begun at the Bretton Woods conference in 1944, after some thirty years of international turbulence. (It would not seem reasonable to call a period including the two world wars and the great depression "Pax Americana", while the period after 1944 includes what is generally considered the heyday of the USA.)

Likewise, partly because of the USA's continuing military dominance, the dates of the end of "Pax Americana" and the start of "Pax Nipponica" are not clear-cut. Perhaps the earliest date that might be considered the end of "Pax Americana", at least in its economic aspects, is 1971, when the dollar's official convertibility into gold was abandoned. This was the critical step that ushered in the period of rapid world inflation and financial instability that has continued up to the present. For the beginning of "Pax Nipponica" Park has suggested a date of around 1985 based on Japan's economic performance relative to the USA (Park, 1992). However, as far as international financial stability is concerned, that may be considered premature.

Under "Pax Americana" as well as "Pax Britannica", the foundation of the financial system was the policy of maintaining real currency convertibility as a means of stabilizing the value of money. In both cases the government defined the currency in terms of a real commodity, namely gold, and stood ready to exchange it on demand for the specified commodity at specified prices. This system enabled the monetary authorities to maintain the real value of money constant over decades. By comparison with the present era, when monetary authorities expend considerable effort collecting and interpreting various monetary statistics, it is notable that under currency convertibility in the past the real value of money was successfully maintained without controlling or even measuring the "money supply".

However, gold convertibility is only a special case of the general principle of maintaining real currency convertibility, which is the only system that has ever succeeded in preserving the value of money for periods of generations. The monetary economist, Niehans stated in 1978: "...commodity money is the only type of money that can be said to have passed the test of history in market economies." (Niehans)

The classical British economists, notably including Adam Smith, David Ricardo, John Stuart Mill, Stanley Jevons and others, were in unanimous agreement that no other system is equally capable of preventing governments from devaluing the

currency through inflation-which is otherwise irresistible to them. The recent experience of unprecedented global inflation since the end of dollar convertibility in 1971 supports that view. Consequently, viewed from the perspective of the monetary standards maintained for more than two centuries by Britain and the USA, it would seem reasonable to argue that "Pax Nipponica" proper has yet to begin, and that it will not begin until the Yen is stabilised in real terms by implementing a system of real currency convertibility.

However, although some economists favour a return to the gold standard, this author considers that convertibility of the Yen based on gold would not be desirable today due to the serious distortions that would be caused in Japanese monetary policy by changes in the world supply and demand for gold. It is therefore interesting to consider what form the resumption of real convertibility of the Yen might take.

2. A Modern Equivalent of the Gold Standard

Both during the gold standard era and since its abandonment there has been agreement among a number of leading economists that a system of currency convertibility based on a range of primary commodities would be preferable to gold convertibility. Such leading economists as Irving Fisher (1928), Keynes (1938) and Hayek (1943), among others, all proposed or supported others' proposals for the implementation of currency convertibility based on a range of primary commodities.

2.1 Counter-Cyclical Influence

In practice, currency convertibility based on a range of commodities would not only stabilize the real value of the currency, but would also have a stabilising influence on world trade, reducing the severity of both recession and inflation over the trade cycle. This important property of the system of currency convertibility was a major reason for the support that it has received, but unfortunately it is not widely understood today. It has been described by Hayek in the following way:

> "With this system in operation an increase in the demand for liquid assets would lead to the accumulation of stocks of raw commodities of the most general usefulness And as the hoarded currency was returned to circulation and demand for commodities increased, these stocks would be released to satisfy the new demand.
>
> It will be readily seen how the operation of the scheme would go far to stabilise the demand for raw commodities....the secured income of the producers of raw commodities would also go far to stabilise the demand for manufactures." (Hayek, 1943)

This mechanism was described again more recently by Kaldor:

> "When production exceeds consumption, world investment in commodity stocks would automatically rise: this would imply a supplement to income derived from sales to consumers, and thereby stimulate the absorption of primary products through increased production and employment in the industrial regions. A shortage of commodities would cause a depletion of stocks; this would reduce producers' incomes relative to consumers' outlay on such

commodities; it would thereby reduce effective demand for industrial goods until the excess demand for basic commodities was eliminated (Kaldor, 1975)."

Thus, in addition to stabilising the value of money, the implementation of convertibility based on a range of commodities would exert an automatic counter-cyclical influence on the level of economic activity. It would thereby combine the advantages of both "Keynesian" and "monetarist" approaches to economic policy while avoiding their weaknesses; it would avoid both the inflationary tendency and the vulnerability to political interference of Keynesian activism, as well as the inflexibility of monetarism. In view of the bad experience of inflation and unemployment in western countries during the two decades since real dollar convertibility was abandoned, such a policy mechanism is highly desirable .

2.2 Difficulties of Implementation

However, the implementation of real currency convertibility based on a range of commodities faces certain practical problems which are different from the implementation of a gold standard.

First, if the prices of primary commodities were fixed in terms of a major currency, as the price of gold was fixed under the gold standard, this would cause serious economic distortions, both in that country's monetary policy, and in the primary commodity industries concerned. Consequently, in the case of currency convertibility based on a range of primary commodities, a flexible link is required between the currency and commodities.

Second, if the guarantee of convertibility was unconditional, as was the case under the gold standard, this would represent an open-ended financial liability for the government or governments implementing the system. That is, they would be obliged to purchase any quantity of commodities offered at the buying price, and to supply any quantity demanded at the selling price. Such a guarantee would be very unattractive to governments.

Third, if a system of currency convertibility is implemented in a country experiencing inflation, as all countries are today, this could cause a severe shock to the economy, which would be economically risky, and therefore politically unattractive.

Fourth, if the system was as rigid as the gold standard, this would remove much of the power to determine monetary policy from the government, which would also be politically difficult to implement.

2.3 Impractical Proposals

Because of the requirement for flexibility, the proposals for implementing such a system advocated by Fisher (1928), Keynes (1938), Hayek (1943), Graham (1962), and Kaldor (1976) all contain the proposal to define the currency in terms of a weighted "basket" of commodities in order to provide some flexibility. However, despite this change from the concept of the gold standard, when examined carefully from the point of view of actual implantation, none of these economists' proposals would be desirable in practice.

The shortcomings are discussed by Takuwa (1992) and Collins (1985), but in

short, each proposal would impose serious distortions on world commodity markets and government policy, but without achieving corresponding benefits. In particular, they would require complex international agreement to implement, so that individual countries would not be able to obtain the benefits of convertibility. In addition, many details of the system's operations were left to negotiation. This would lose one of the most important features of the gold standard, namely its dependability and freedom from political manipulation.

3. The Grondona System of Conditional Currency Convertibility – a Definitive Solution

A very different proposal for implementing convertibility was published in 1958 by the little-known Australian economist, the late Leo St Clare Grondona (1958). This system differs from the above proposals in a number of critically important aspects (Collins, 1985). The effect of these differences is to strictly limit the financial liability involved in operating the system, thereby eliminating any risk associated with implementation. That is, unlike the gold standard, implementing Grondona's proposal does not require the government to assume an unlimited liability. This has many important implications, the most important of which is that, in contrast to other economists' proposals for commodity convertibility, individual countries are able to implement this system independently in terms of their own currencies, as discussed further below.

3.1 Details of Conditionality

Instead of trying to fix the value of currency in terms of a "basket" of commodities, Grondona's system would partially stabilize the value of the currency separately in terms of each commodity involved. Flexibility is achieved by making the range within which the price of each commodity would be stabilized, adjust automatically according to market conditions, as indicated by the level of reserves held.

Under the original gold standard, a specialized department of the central bank stood ready on demand to exchange currency for gold of specified quality, in specified units, at specified prices, the "gold points". By analogy, under the Grondona system a specialized department of the central bank, the "Commodities Reserve Department" would be established which would stand ready on demand to exchange currency for specified commodities of specified quality and in specified units, individually at specified, but conditional prices. For each commodity involved, the Commodities Reserve Department (CRD) would establish a "price schedule", according to which the prices offered and accepted by the CRD for reserves of each commodity would adjust in proportion to the current level of reserves of the commodity in question (see Table 1).

In addition, the guarantee to provide commodities in exchange for currency on demand at specified prices would not be unconditional but would apply only as long as the CRD was holding reserves, the levels of which would be publicly known at all times. Thus, on occasions, the reserves of one or more commodities might fall to zero, shown at (1) in Figure 1. However, the CRD's lower points would still be

Table 1. Illustrative price-schedule for a single commodity

Units of Commodity in CRD's reserves (Kilotons)	Current CRD buying price (%*)	Units of Commodity in CRD's reserves (Kilotons)	Current CRD selling price (%*)
0 – 49.5	90.0	0.5 – 50	110.0
50 – 99.5	85.5	50.5 – 100	104.5
100 – 149.5	81.0	100.5 – 150	99.0
150 – 199.5	76.5	150.5 – 200	93.5
200 – 249.5	72.0	200.5 – 250	88.0
250 – 299.5	67.5	250.5 – 300	82.5

(*: % of previous medium-term average CIF import price)
(~: minimum unit is 500 tons; "block" of each commodity is 50,000 tons)

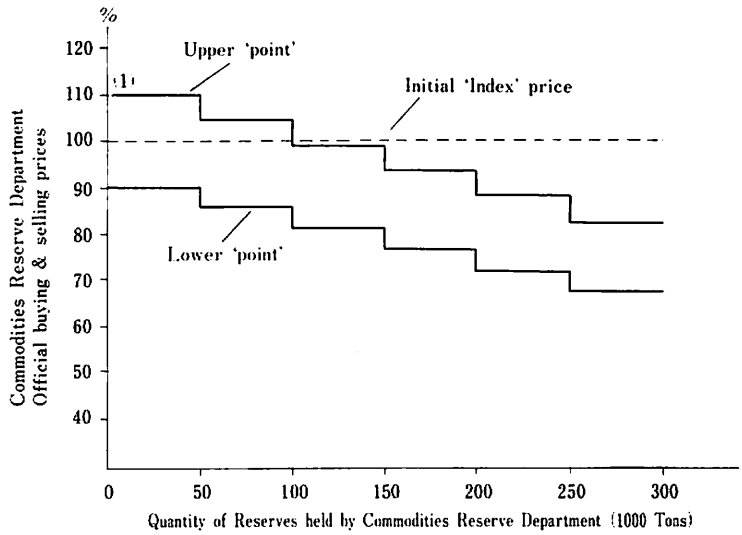

Figure 1. Reserve price schedule based on illustrative figures in Table 1

effective, thereby providing support to the market, and reserves of the commodity would subsequently accumulate again, making the upper points effective once more. This and other important details of Grondona's proposal are described at length in (Grondona, 1958; Grondona, 1975; Collins, 1985).

Thus, with this system in operation, when the value of the currency in terms of a particular commodity was rising (that is, its price in that currency was falling), stocks would be sold to the CRD in exchange for currency. When these stocks reached a prespecified level, the CRD's official buying and selling prices for that commodity would fall by a prespecified amount (as illustrated in figure 1). If the value of the currency in terms of this commodity continued to rise, so that market prices fell to this lower level and reserves continued to accumulate, the process would repeat, and the cycle would continue until the CRD's buying price became unattractive to sellers. Later, when the value of the currency in terms of that

commodity declined and market prices recovered, buyers would repurchase the reserves from the CRD at the successively higher selling prices in its official reserve price schedule as each in turn became attractive relative to the current market price.

3.2 Implications of Conditionality

The change to a conditional system from the more complex proposals referred to above has many important implications which are discussed at length in (Collins, 1985). In particular it definitively solves the problems described in section 2.2 above. First, because the CRD would handle each commodity separately, and the prices at which it would exchange commodities for currency adjust automatically according to the level of reserves, the system would not distort commodity prices. Market forces would continue to raise or lower these, but they would do so more smoothly than at present as large and sudden fluctuations would be partially damped.

Second, the implementation of the system would not involve an open-ended commitment. The scale appropriate to a country's needs, and the maximum outlay that might be required for each commodity, could be decided in advance, while the maximum price for any commodity involved would be guaranteed only as long as reserves were held. Thus the effects that movements in commodity prices could have on the level of national liquidity would also be limited. This has the important consequence that, unlike the proposals for commodity-convertibility mentioned above, individual countries could implement the system independently in terms of their own currencies. Hence, in contrast to all other proposals, the Grondona system would not require international agreement for its implementation or continued operation. In view of the great difficulties that countries even as similar as those of Western Europe have in achieving lasting agreements in the monetary field, this unique feature of Grondona's proposal is of great practical importance.

Third, Grondona fully appreciated that implementation of a "commodity standard" could impose strains on an inflationary economy that would make it politically difficult to implement. Part of his innovativeness was to understand that even a "conditional commodity standard" that had only a limited stabilizing influence would be valuable. Once in operation the influence of his system could subsequently be increased as desired by increasing the scale of operation (after an appropriate period of notice). In this way it would be possible ultimately to eliminate inflation, if this was desired, but without any shock to the economy, making it a politically attractive means of achieving this goal.

Fourth, because the guarantees of convertibility would be conditional, the implementation of Grondona's proposal would not constrain a country's monetary policy as the operation of the gold standard did. As under the gold standard, the operation of the system would lead to counter-cyclical changes in the money supply, but unlike the gold standard these could be over-ruled by the monetary authorities if this was considered desirable. In general, however, this would not be desirable. And as experience of the system grew, public pressure would grow to preserve the value of the currency. In this way the financial discipline of the gold standard era would be relearned in a gradual manner. The implications of implementation for

national monetary policy are discussed in detail in (Collins, 1985).

In addition to these points, Grondona designed his system to be extremely simple and economical to operate. In particular, all costs of transporting commodities to and from the reserves would be borne by the customers of the Commodities Reserve Department, which would require very few staff. Thus the only significant cost of implementation would be the construction of the warehouses needed. In the case of Japan this would amount to several hundred okuen, depending on the scale of implementation. This is a substantial sum. However, it would in practice be spent over several years, and would be dwarfed by the benefits accruing to the country over the following business cycle, and even more over the following 50 years and more.

3.3 Definitive Solution

As seen in section 2 above, there has been considerable agreement among leading economists about the potential benefits for the global economic system of implementing currency convertibility based on primary commodities. Unfortunately they were not able to devise a practical means of implementing it. However, as shown above, Grondona's proposal solves the problems described in section 2.2 above. Consequently it appears to provide a definitive solution to the problem of how to resume currency convertibility, which requires only the political will to be implemented. This was recognized in a number of British publications at the time of Grondona's first publication of his proposal in 1958, as typified by an editorial of the leading business magazine of the time:

> "Epoch-making is a word too often and too lightly used. But to apply it to Mr. Grondona's "Utilising World Abundance" is to restore it to its original, its literal meaning. It can be only a question of time before man's reason and self-interest overcome his inertia and Mr. Grondona's proposals are accepted. When they are they will define the beginning of an era as surely as did the introduction of the gold standard." (The Manager, 1958)

It is tempting to see the elegantly simple solution by the "Pacific Rim" economist, Grondona, of a fundamental problem that has baffled generations of theoretically sophisticated but impractical economists in the older industrialised countries, as symptomatic of the difference in outlook between these regions, and of the reasons for the leadership succession under discussion.

4. Japanese Implementation of Conditional Currency Convertibility

An important aspect of the fact that both Britain and the USA have passed their historic peaks of influence is the apparent inability of their governments to tackle their national economic problems effectively. A common criticism is that they attempt to do many things that should not be the responsibility of government, but they fail to do those things that are government's responsibility, notably defining and preserving the value of the national currency. This is a major change from the time when these countries provided economic leadership for the world, based on real currency convertibility.

In the apparent absence of the required economic leadership coming *from* elsewhere, the prospects for the world's economic future therefore presently depend to a considerable extent on Japan. It will be a true test of Japan's dynamism and continuing national strength whether it can follow these countries' historical example, and succeed in establishing a meaningful Pax Nipponica. It is interesting in this context to consider the implementation of Grondona's proposal by Japan.

Like Britain, Japan depends heavily on imported raw materials, and is therefore particularly well-suited to initiate the system which Grondona designed originally for British implementation. Because the system's guarantee of convertibility would be conditional, the scale of its economic influence would be determined by the scale on which it was established. Grondona suggested that, while the details would need to be tailored to each country's particular conditions, typically some fifteen to twenty commodities should be included (agreeing broadly with other economists' proposals); that these should comprise only major, imported commodities that could be stored economically for up to several years; and that the initial scale of operation in relation to each commodity should be such that in a severe world recession (in which prices fell to their lowest cyclical levels) the maximum level of reserves might be of the order of six months' national imports.

Hence, following Grondona's guidelines, the imported, durable, basic commodities that would be appropriate for initial implementation in the case of Japan include copper, tin, lead, zinc, aluminum, nickel, sugar, coffee, cocoa, cotton, wool, rubber, wheat, barley, maize and soya beans.

Also following Grondona's guidelines, an appropriate scale for initial implementation by Japan might be to set a "block" of each commodity (the maximum quantity which would be accepted or sold at each point in the price schedule) at some 10% of annual imports. The initial lower and upper "points" (the prices at which the CRD would exchange reserves for currency on demand) might be 10% below and above the previous average CIF import prices, allowing a range of some 20% for short-term market price fluctuations. In the case of these 16 commodities, on such a scale of implementation the total outlay on commodity reserves, in the event of a severe world recession in which commodity prices fell about 30% below their previous average, would be of the order of 7000 okuen. However, either a larger or smaller scale of implementation could be chosen in the case of each or all of the commodities involved .

A further important advantage of the Grondona system is that, as under the gold standard, the process of maintaining convertibility is passive. Consequently it is straightforward to simulate the direct effects of the operation of a commodities reserve department using a computer. Such simulation, using past commodity import statistics and market price data, would be useful in planning the establishment of a Japanese CRD in detail.

5. Benefits of Japanese Implementation

Implementation of conditional currency convertibility would have a wide range of effects. In the following, some of the more important implications of Japanese stabilisation of the Yen according to the Grondona system are discussed.

5.1 Direct Benefits

The benefits that would result directly from the implementation of this system include greater stability in both the real value of the Yen, and in Yen-denominated prices of the commodities involved. This would lead to reduced instability over the business cycle, and greater stability in export demand for Japanese products, particularly from countries exporting primary commodities.

The instability of the value of money has long been recognised as a major cause of trade fluctuations (Fisher, 1928), and the serious instability of primary commodity prices is an important factor aggravating the international trade cycle (Collins, 1985). Consequently reducing the cyclical instability of the real value of the Yen, even to a limited extent, would be beneficial, and would also provide useful protection against global recession.

5.2 Domestic Monetary Benefits

From the point of view of Japan's domestic monetary situation also, the establishment of currency convertibility would be valuable. In particular, in view of Japan's serious "baburu keizai" and its aftermath, it would be desirable in helping to prevent the recurrence of such unhealthy financial fluctuations within the Japanese economy.

An important factor contributing to the "baburu keizai" in Japan was the liberalization of international financial markets combined with the continuing rapid evolution of electronic financial systems around the world, which make the control of national money supplies increasingly difficult. Not least is the fundamental difficulty of defining and measuring the quantity of money, due to the continual innovation of new financial instruments.

In this situation, a return to the historical principle of convertibility (albeit in a conditional form) which maintains the value of the currency through market forces rather than through the need to control the quantity of money however defined, is potentially of great value. In particular, if this system had been in operation since the mid-1980s, corrective monetary policies would have been initiated earlier, and the excesses of the "baburu" greatly reduced, saving the economy many thousands of okuen in misallocated resources. Implementing the system today would prevent the recurrence of such a costly policy error, and would help to insulate the Japanese monetary system from destabilising influences transmitted from outside.

5.3 Benefits for Developing Countries

For some decades developing countries have been collectively pressing the governments of the rich nations to stabilize the prices of primary commodities through UNCTAD. Unfortunately the policy which they have advocated has been to stabilise commodity prices between fixed limits. This would require an open-ended financial commitment from the rich countries, and would greatly distort commodity markets. It would also require complex international agreements, and could stabilize no more than a single currency. Consequently the rich countries

have resisted this pressure from developing countries. This in turn has caused ill-feeling as commodity prices continue to fluctuate sharply, causing great diffieulties for these countries, as well as for commodity producers in the economically advanced countries, and aggravating the instability in international trade.

In recent years Japan has made particular efforts to provide aid to developing countries, and is now the largest overseas aid donor. Japan therefore has a natural interest in reducing the instability of primary commodity prices and trade through implementing conditional currency convertibility. The value of the considerable goodwill that it would thereby receive from many developing countries is difficult to estimate, but it is likely to become more valuable in the future as supplies of some raw materials become more uncertain, and as more Japanese citizens travel to other countries .

5.4 Example for Industrialised Countries

The implementation of conditional currency convertibility by Japan would also provide a valuable example for other countries to follow in establishing their own systems. Grondona designed the system specifically to enable countries to establish it independently in terms of their own currencies, and he envisaged that other countries would be likely to follow the example of the leader in this field. Such multi-national implementation (which is distinct from international implementation) would multiply the overall stabilising influence, while giving each country the benefit of national currency convertibility. It would thereby also make exchange rates less volatile, but without requiring chimerical international agreement to achieve this (Collins, 1985).

With the end of the cold war, it is possible that different countries' economic performances will diverge further in future than in recent years. This will make the achievement of detailed international agreement on such complex and sensitive matters as monetary policy even more elusive than it has been since 1971. Furthermore, by the nature of the political process, whereby agreement is reached as a compromise between different countries' political objectives, sometimes in unrelated fields, the result of such international agreement would be less beneficial than the result of market-driven national systems of currency convertibility.

5.5 Societal Benefits

Finally, Japanese society faces a number of major destabilising influences in the coming years. These include its rapid rise to economic wealth, which in most other rich countries has been accompanied by a range of anti-social developments; its rapid internationalisation; the serious economic problems of other advanced countries combined with Japan's vulnerability to "bashing" by their governments; the rapid economic growth of Japan's neighbours; the rapid geo-political changes occurring in the world following the end of the cold war, which makes US leadership less dependable; the increasing pressures for political reform within Japan, the economic effects of which are impossible to predict; and the international pressure for Japan to assume more international responsibilities.

Many of these influences will tend to create inflationary pressures *within Japan*.

The establishment of monetary foundations that would stabilise the value of the Yen in real terms and improve the stability of economic growth would significantly strengthen Japanese society against these dangers. The unique benefits of currency convertibility seen from the classical viewpoint of encouraging financial discipline and protecting citizens against the inflationary interests of politicians, were described clearly in 1848 by J.S. Mill:

> "Everybody can understand convertibility; every one sees that what can be at any moment exchanged for five pounds, is worth five pounds. There is therefore a great preponderance of reasons in favour of a convertible, in preference to even the best regulated inconvertible currency. The temptation to over-issue, in certain financial emergencies, is so strong, that nothing is admissible which can tend in however slight a degree, to weaken the barriers that restrain it" (Mill, 1857).

Despite its advantages, the burden of maintaining a rigid gold standard became too great for both Britain and the USA. The Grondona system is a form of convertibility that does not require a single country to carry an excessive burden. It is therefore an interesting question whether Japan will have the political ability to implement such a fundamental and innovative policy, as Britain and the USA were once able to do in the past. Doing so would represent a further major step in Japan's assuming international responsibilities, as it is frequently urged to do by other countries.

6. Conclusions

Although the concept of "Pax Nipponica" is necessarily different from the preceding eras of "Pax Britannica" and "Pax Americana", there are good grounds for considering the concept in some detail. Clearly a Pax Nipponica will be built on Japan's economic rather than military strength, and will be particularly valuable for other countries in the process of industrial development.

By historical analogy, it would seem a necessary condition for the creation of "Pax Nipponica" that Japan should provide world leadership in maintaining international financial stability. Historically, both Britain and America provided such stability fundamentally through preserving "sound money" through maintaining real convertibility of their national currencies.

Although unfashionable within the economics profession in recent decades, real currency convertibility is the only system that has been successful in providing monetary stability in practice, and it has done so for several centuries. However, rather than using gold as the numeraire, as Britain and the USA did in the past, it would be far preferable today to use a range of primary commodities. This would have a wider range of benefits, provided that a practical means of implementation was available.

Most importantly, in addition to reducing inflation and providing the basis for eliminating it, the resumption of currency convertibility in this way would create a powerful counter-cyclical influence in the world economy, that would tend to reduce the severity of fluctuations in international trade, resisting both inflation and recession over the trade cycle.

A number of leading economists such as Fisher, Keynes and Hayek advocated systems for stabilizing the value of money in terms of primary commodities. However none of these schemes would have been practical to implement. The only practical proposal for resuming real currency convertibility published to date is the long-neglected proposal by the Australian economist Leo St Clare Grondona for a simple system of conditional currency convertibility. Implementation of this proposal by Japan would achieve these benefits without imposing stresses on the economy. As such it would seem worthy of detailed consideration as the monetary foundation for "Pax Nipponica".

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