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"Trade Deficit of the United States from Japan"

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Besides investment and opening of Japanese market, depreciation of dollar to yen is also one of the ways American can do to help reducing trade deficit in long term. However, voices from many sectors are screaming to stop the depreciation of dollars (Holyoke, 1993). Those people found that depreciation is actually increasing the trade deficit. From the year 1990 to 1993, when dollar fell for a third of its value against yen, the trade deficit actually increased consistently with the decrease in value of dollar (Spiers, 1993).

The statement is true at the mean time, but it doesn't addresses the long run effect of the depreciation of dollar. The pattern of increasing trade deficit accompanying with decreasing value of dollar could be answered by the economic theory of the J-curve. The pattern we are facing today is only a portion of the economists' J-curve. It just likes writing a letter `J', you start with a dip and then follow with a sharp upward spike. We are now at the situation of the downward dip, while it is expected that we will surely go on to the upward spike in long term. Why the J-curve works like that?

The pattern of J-curve could be explained with a simple example. When the dollar goes down, the television sets imported from Japan will become more expensive compared with the old price in the U.S., however the consumers in the U.S. will not notice the change in a short time because the price of televisions on the retail markets are still priced with the old price which they were purchased with the old price from Japan. When the retailers in the U.S. ordered new television sets at the current demand of the market, higher price has to be paid. On the other hand, the price of IBM PCs on the Japanese market would not be lowered in the short term because they are purchased with the old high price, and hence the Japanese consumers will not increase their consumption of IBM PCs. Since there are some inertia in consumption in both countries, the volume of trade is carried out in the usual manner, but with a new exchange-rate, the trade deficit will surely increase because of the decrease in real value received by the American and decrease of amount the Japanese have to paid. Nevertheless, in the longer term, the American consumers will realized that the Japanese products are more expensive than before, so rationally they will consume more Japanese products, while the Japanese consumers will find that the American products are cheaper than before, that they will increase their consumption. As a result of these changes in preference, the reduce of trade deficit will offset the adverse consequences of depreciated dollar (Baumol & Blinder, 1994).

Furthermore, J-curve has been already proved in the U.S. history. In 1986, the trade deficit of the United States climbed to a record high of $155 billion (in 1987 dollar), when the dollar started to depreciate in 1985. What amazed the people at that time was that the trade deficit fell from 1987 until 1990 when the dollar were facing another depreciation which was the dip of another J-curve (Baumol & Blinder, 1994). It should not be difficult to realize the relationships between the depreciation of dollar and the swelling trade deficit now. The United

States is now at the same situation as we had in 1985. The trade deficit will soon decline again by following the J-curve pattern. And actually the trade deficit is starting to fall now (Banks, 1993). Therefore, appreciate the dollar will only do the opposite (Baumol & Blinder, 1994) and should never be attempted.

...... The future is optimistic.

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