

Changes in Intersectoral Terms of Trade and Their Effects on Capital Formation in Agriculture : Comparative Analysis of Japan's and Taiwan's Cases

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Modern economic growth involves the flow of capital and labor between the agricultural and nonagricultural sectors. The terms of trade between the agricultural and nonagricultural sectors affect that flow. To find the role of the terms of trade in economic development, I have analyzed its effect on the transfer of capital between agriculture and nonagriculture and factors affecting changes in the terms of trade, from the perspective of economic development in Japan and Taiwan.

When the terms of trade are favorable to the agriculture sector, it attracts more capital investment, its production shifts upwards, and labor productivity increases. This expansion of production increases the marketable surplus of agricultural products and turns the terms of trade against the sector. Any actual deterioration in the terms of trade induces investors to allocate a larger share of investment to the other sector ; but that in time leads to relative overproduction and consequent deterioration of that sector's terms of trade. Such investment behavior, responsive to changes in market conditions throughout the economy, has therefore caused relatively faster growth of one sector in one period, and of the other in next.

In both Japan and Taiwan the movement in the terms of trade correlates well with the relative growth rates of the two sectors. Agriculture's terms of trade improved when the sector's growth was relatively slow compared to nonagriculture and declined when growth was relatively fast. As the terms of trade turned in favor of the agricultural sector, it attracted more capital investment.