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Australia’s Role in
Japan’s Postwar Trade Strategy:
Development of Japanese Trade
under the Sterling Trade and Payments
Agreements, 1947-1954

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A thesis submitted for the degree of
Doctor of Philosophy
at The Australian National University
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Except where otherwise indicated, the work contained in this thesis is entirely my own.

Teruhiko Fukushima

April 1995
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This thesis is a product of patience and encouragement. It took me many years to finish due
to medical problems which compelled me to leave Canberra for Tokyo to have surgery in
the middle of my PhD course. At times things looked so hopeless that I once seriously
considered withdrawing from the course. Even after assuming my present position as
lecturer of Australian Studies at Obirin University, medical considerations prevented me
from concentrating on research and writing.

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ABSTRACT

This thesis analyses Australia’s role in the re-establishment of postwar Japanese trade networks from 1947 to the mid 1950s. The Sterling Trade and Payments Agreements which stipulated settlement in pounds sterling of Japan’s trade with the sterling area was an important determinant of Australia–Japan trade during this period. Under this Agreement, Australia played a significant role in sustaining Japan’s postwar strategy of economic self-reliance through trade promotion on a more multilateral basis.

Firstly, Australia assumed a pivotal role in shifting Japan’s postwar trade strategy, under a worldwide dollar shortage, from dollar-based trade to expansion of more multilateral trade networks. The Supreme Commander for Allied Powers in Occupied Japan (SCAP) did not initially show much interest in stimulating trade with the sterling area, placing higher priority on maximisation of Japan’s export sales to dollar markets. From late 1949 onwards, however, SCAP came to emphasise promotion of trade with the sterling and other non-dollar areas as a central strategy for increasing Japan’s economic self-reliance and reducing its dependence on US aid. The Sterling Trade and Payments Agreements provided for multilateral settlement in soft currency of Japan’s sterling trade, allowing Japan to use its sterling surplus to finance the procurement of wool and other important commodities from Australia. Australia’s bilateral trade surplus provided the other sterling area countries with purchasing power to buy Japanese industrial goods. Australia emerged not only as an alternative supplier to the United States but also as the lubricant for Japan’s overall sterling trade.

Secondly, among the sterling area countries, Australia took the initiative in normalising trade relations with Japan. In August 1951, the Japanese government concluded a revised Sterling Payments Agreement that deprived Japan of the right to convert its sterling surplus into dollars. Japanese government and business had been inclined towards a dollar-based trade strategy, in anticipation of extra dollar income through the US strategic aid program. When the US administration showed that it was not prepared to provide expanded economic assistance, Japan had no alternative but to achieve economic self-reliance through more multilateral trade on an unsubsidised
commercial basis. With the new Sterling Payments Agreement, which further facilitated financial settlement of Japan's overall sterling trade, Japan confirmed its commitment to this trade strategy. In these circumstances, it became imperative for the Japanese government to regulate the reduction of trade barriers within the sterling area through diplomatic approaches. Australia responded positively to the Japanese request that it relax its discriminatory import licensing when Japan's serious sterling shortage of 1953-54 severely affected Australia's export sales to Japan. This paved the way for the 1957 Commerce Agreement, which made Australia the first country to conclude a formal trade agreement with Japan among the fourteen contracting parties (including several sterling area countries) maintaining discriminatory treatment of Japan even after its accession to the GATT in 1955. Success in concluding the Commerce Agreement with Australia impressed the Japanese with the feasibility of pursuing a multilateral trade strategy. The common interest in multilateral trading arrangements has hence been a consistent function of the Australia-Japan relationship in the postwar period.
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ABBREVIATIONS

AM: Australian Mission in Tokyo
CCC: Commodity Credit Corporation, United States
Crosec: Secretary of State for Commonwealth Relations, British Government
DA: Department of the Army, US Administration
DCA: Department of Commerce and Agriculture, Australian Government
DS: Diplomatic Section, SCAP
EROA: Economic Rehabilitation in Occupied Area, US aid
ESB: Economic Stabilisation Board (Keizai Antei Hombu)
ESS: Economic and Scientific Section, SCAP
FECB: Foreign Exchange Control Board (Gaikoku Kawase Kanri Iinkai)
FO: Foreign Office, British Government
GARIOA: Government Appropriation for Relief in Occupied Areas, US aid
IEFC: International Emergency Food Committee
IMF: International Monetary Fund
IWA: International Wheat Agreement
MAF: Ministry of Agriculture and Forestry (Norinsho)
MFA: Ministry of Foreign Affairs (Gaimusho)
MITI: Ministry of International Trade and Industry (Tsushosangyosho)
MOF: Ministry of Finance (Okurasho)
MSA: Mutual Security Act, United States
OJEIRF: Occupied Japan Export-Import Revolving Fund
SCAP: Supreme Commander for Allied Powers in Occupied Japan
UKLM: United Kingdom Liaison Mission in Tokyo
The Significance of the Sterling Trade and Payments Agreements in Japan’s Postwar Trade Policy towards Australia

The Commerce Agreement of 1957 was a significant breakthrough in postwar Australia-Japan trade relations. By stipulating the exchange of most-favoured-nation treatment and the application of non-discriminatory treatment in trade, it established an institutional framework for the development of bilateral trade under which Japan became Australia’s largest export market especially for mineral resources from the mid 1960s onwards. It secured the development of this significant trade relationship within the framework of the multilateral trading system established under the GATT. One of the architects of the Agreement as Secretary of the Department of Trade in the Australian government, Sir John Crawford, wrote that, ‘without the agreement of 1957 the course of mutual trade expansion would have been both vastly more difficult and a good deal slower’.¹ The Japanese chief negotiator, Nobuhiko Ushiba, described the Agreement as ‘epoch-making’ in that Australia agreed to place Japanese trade on an equal basis.²

THE POLITICAL SIGNIFICANCE OF THE 1957 COMMERCE AGREEMENT

The Commerce Agreement had considerable political significance. The Australian government moved to open its domestic market for Japanese industrial goods in exchange for improved access to the Japanese market for primary commodities. In an attempt to give more favourable treatment to the former enemy, the Australian government ran the risk of bitter domestic opposition. There remained widespread wartime antipathy and thereby strong hesitation to resume normal economic or political relations with Japan among the

Australian public. The prewar experience reminded Australian consumers of the influx of cheap, low-quality Japanese textile goods which aroused among the Australian manufacturers and trade unions enormous anxiety about exposing the Australian domestic market to Japanese industries which were rapidly restoring their strong competitiveness centred on labour-intensive light industries despite heavy damage incurred during the Pacific War. In pursuit of a promising outlet for agricultural products, however, Canberra’s ‘political’ decision to conclude a formal trade agreement with Japan promoted the establishment of closer trade relations between the two mutually complementary economies.\(^3\)

Australia’s move was in line with the trade strategy which it developed after the end of World War II. Although Australia was an original contracting party to the General Agreements on Tariffs and Trade (GATT), the government found that the new international trade organisation did not favour primary producers such as Australia because the GATT principles of non-discriminatory treatment and elimination of trade barriers excepted agricultural trade. The Australian government, therefore, tried to pursue its commercial interests in bilateral negotiations by obtaining improved market access for its agricultural exports in exchange for reduction of its domestic industrial protection. In 1956 Australia concluded a Trade Agreement with the United Kingdom which allowed Australia to reduce the margins of preferential tariffs as stipulated in the 1932 Ottawa Agreement, to make Australia a more attractive trading nation for the countries outside the British Commonwealth such as Japan. From a commercial viewpoint, it was in Australia’s interest to approach Japan also to liberalise bilateral trade in order to maintain and develop the Japanese domestic market which seemed to have the potential to become a huge outlet for Australian primary products, as long as Australia could retain the right to check excessive inflows of Japanese goods whenever its less competitive domestic industry was threatened. These Australian policy considerations which constituted the background to the 1957 Commerce Agreement with Japan have already been well documented in Crawford’s work. Rix has explained in detail the political process whereby the Australian policy makers took

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\(^3\) Crawford, 1968, p.356.
the initiative towards expansion of Japanese trade without antagonising potentially hostile domestic interests.4

The Agreement also had political significance for Japan. It drove an important wedge into the system of international trade discrimination against Japan. Ushiba emphasised the political importance of Australia’s commitment to most-favoured-nation treatment for Japanese trade, as Australia became the first country to agree to give concessions among the GATT contracting parties which retained the right to discriminate against Japan under Article XXXV after Japan joined the GATT in 1955.5 Moreover, the Commerce Agreement with Australia was the fourth formal trade agreement concluded by the postwar Japanese government, following those with the United States, Canada and Norway.

One of the most important issues in Japan’s postwar diplomacy was the restoration of international status through membership of international economic organisations such as the International Monetary Fund (IMF) and the GATT. In particular, accession to the GATT allowed Japan non-discriminatory most-favoured-nation treatment which could help to promote its export trade. Japan had to face enormous difficulties in achieving these objectives.6 Four months after the restoration of independence in April 1952, Japan was admitted to the IMF. In 1955, Japan achieved the long-awaited goal of membership in the GATT. In granting accession to Japan, however, the fourteen GATT contracting parties including the United Kingdom, Australia, New Zealand, South Africa, France and the Benelux Countries, refused to enter into normal GATT relations with Japan by retaining the right to discriminate specifically against Japan under GATT Article XXXV. Despite Japan’s formal membership in the GATT, these parties were allowed to maintain discriminatory import restrictions selectively against Japanese goods.

Retention of GATT Article XXXV by a dozen of the contracting parties had an adverse effect on the promotion of Japan’s exports of competitive light industrial goods into advanced markets and thus caused balance of payments problems. Furthermore, the other

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4 Alan Rix, *Coming to Terms: The Politics of Australia’s Trade with Japan, 1945-57*, Sydney, Allen & Unwin, 1986. Especially his Chapter 6 discusses the problems of the Australian government in accommodating Japan in the postwar international trading system, while retaining its right to impose selective restrictions on imports from Japan to maintain domestic protection.
5 Ushiba and Hara, 1979, p.241.
6 For an outline of the problem of Japan’s accession to the GATT, see Tatsuo Akaneya, *Nihon no Gatto Kanyu Mondai* [Japan’s membership into the GATT], Tokyo Daigaku Shuppankai, 1992.
war-defeated nations, West Germany and Italy, had been admitted to the GATT much earlier and there were only a few cases in which Article XXXV was retained. Italy became a GATT contracting party in 1949 and West Germany in 1951. In 1948, India and Pakistan retained Article XXXV against South Africa in protest against its racial discrimination policy. Cuba adopted a policy of applying Article XXXV against any new contracting party. It was evident that some Western countries were still concerned that Japan would exploit its competitive edge in the marketing of its light industrial goods and might repeat its prewar export drive and unfair trade practices. If Japan was to seek economic development through trade promotion and restoration of its international status by participating in the international trade forum, the government had to focus on removal of retention of rights under Article XXXV.

In September 1957, soon after the signing of the Commerce Agreement, the Japanese Ministry of Foreign Affairs published the first issue of Waga Gaiko no Kinkyo, the so-called, Gaiko Seisho [Diplomatic Blue Paper]. Gaiko Seisho indicated three important objectives in Japanese foreign relations, including economic diplomacy which aimed at the ‘peaceful advance of Japanese economic power overseas’. While the 1957 issue of the Blue Paper did not give a clear definition of economic diplomacy, the 1958 issue was more explicit pointing out that the international trade barriers for the purposes of exchange controls and domestic industrial protection and trade discrimination against Japan were the targets of economic diplomacy. The 1962 issue went so far as to describe the removal of trade discrimination against Japan as the ‘most important point in economic diplomacy of our country whose mission is export promotion’.

Yamamoto argues that economic diplomacy was an inevitable priority in Japan’s postwar foreign relations:

The emphasis on economic diplomacy has a long history which goes back to the restoration of Japan’s independence by the San Francisco Peace treaty and the resumption of diplomacy. The most imminent problem was how an

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8 Gaimusho [Ministry of Foreign Affairs (MFA)], Waga Gaiko no Kinkyo, vol.1, 1957, p.9. The other two issues were promotion of good relations with Japan’s Asian neighbours and maintenance of the mutually cooperative relations with the United States.
independent Japan could find an opportunity for its survival in the world. Moreover, despite independence, there was no room at all for Japan to take its own diplomatic initiative. Under these conditions Japan had no alternative but to centre its diplomatic activities on restoration of its status in international economic society through conclusion of treaties of commerce and navigation and entry into the international economic organisations within the political framework established by the San Francisco Treaty.\textsuperscript{11}

Thus the removal of the systematic trade discrimination against Japan was the most challenging task in postwar Japanese diplomacy.

In view of this situation, the Commerce Agreement with Australia had significant political meaning for the Japanese government. The exchange of most-favoured-nation treatment in trade virtually put Australia-Japan trade on a normal GATT basis except in the case of an emergency. Australia’s commitment in the Agreement to review retention of Article XXXV within three years put considerable pressure on the other parties which continued to discriminate against Japan, particularly those of the British Commonwealth of Nations. The significance of the political effect of the Agreement was such that the Japanese negotiators showed preparedness to make compromises in the settlement of specific bilateral trade issues raised by Australia. For example, Japan had hesitated to provide assurance on maintaining the existing duty-free entry for wool for three years until Australia revealed its readiness for eventual removal of retention of Article XXXV by promising its review within three years.\textsuperscript{12}

Apart from its political significance, the meaning of the Commerce Agreement in the evolution of the postwar Japanese trade strategy has not been fully examined. In fact, little research has so far been undertaken on the specific trade policy considerations which drove the Japanese government into negotiations for liberalisation of bilateral trade with Australia.\textsuperscript{13} The significance of the diplomatic issue of trade discrimination under the GATT suggests that Japanese trade policy had focused on export promotion through the


\textsuperscript{12} Toshimichi Kajiki, ‘Nichi-Go Tsusho Kosho wo Kaerimite’ [Japan-Australia trade negotiations], \textit{Boeki to Kanzei}, vol.5, no.8, August 1957, pp.36-37; Kan’ichiro Akiyama, ‘Nichi-Go Tsusho Kyotei no Sciritsu to Nichi-Go Boeki’ [The conclusion of the Japan-Australia Commerce Agreement and Japan-Australia trade], \textit{Kaigai Keizai Jijo}, no.272, vol.7, no.13, First half of July 1957, p.398.

\textsuperscript{13} For Japan's accession to GATT, see Akaneya, 1992. For a descriptive history of Japan-Australia trade, see Katsuhiro Narita, \textit{Nichi-Go Tsusho Gaikoshi} [The history of Japan-Australia trade and diplomacy], Shin Hyoron, 1971.
elimination of trade barriers in a desperate attempt to achieve economic recovery and growth. In this context, the Commerce Agreement with Australia would appear to be one of the positive outcomes of this approach.\textsuperscript{14} However, this observation does not begin to explain Australia’s special position in postwar Japanese trade strategy. By the mid 1950s, Australia had become one of the largest suppliers to Japan, second only to the United States. Although less significant as an export market, Australia recorded the fourth largest intake of Japanese goods in 1951. Despite relatively large bilateral commercial exchanges which had developed since the early postwar period, Australia’s position in Japanese commercial affairs has not been fully explained nor appreciated by the Japanese. In order to understand the real significance of the Commerce Agreement, it is necessary to clarify the role of the large volume of two-way trade with Australia in the context of the evolution of the postwar Japanese strategy for economic recovery and growth.

\begin{center}
JAPAN’S FINANCING OF THE BILATERAL TRADE DEFICIT WITH AUSTRALIA
\end{center}

A key to the Japanese policy on Australian trade was Japan’s huge trade deficit with Australia. As Table 1 shows, Japan’s imports from Australia were usually larger than its exports during the first decade of the postwar period with the exception of 1946–47. While Japan tended to record deficits in trade with Australia in the prewar days, the margin of these deficits widened in the postwar period. In 1953, the trade imbalance even reached a ratio of nineteen to one in Australia’s favour. While Australia’s tight import restrictions aggravated Japan’s unfavourable balance, a significant factor was the increased dependence of the postwar Japanese economy on imports from Australia.\textsuperscript{15} The loss of Manchuria meant that Japan had no choice but to purchase wool from Australia in order to resume

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\item \textsuperscript{14} In fact, Kawanami, former Japanese official of the Ministry of Foreign Affairs, recalls that in explaining the content of the draft Commerce Agreement for obtaining approval from the other ministries he had insisted that at any rate the Agreement would contribute towards an increase in Japan’s exports to Australia. (Interview with Masayoshi Kawanami, 30 August 1983) Kawanami was Deputy Chief of the Fourth Division, the Economic Bureau, the Ministry of Foreign Affairs during the negotiations for the Commerce Agreement with Australia. He was in charge of drafting the Agreement and sending instructions for the Japanese negotiators in Canberra led by Nobuhiko Ushiba.
\item \textsuperscript{15} In comparison with the prewar period, Japan’s dependence on foreign trade decreased as a whole in the postwar period due to the decline in purchases of raw materials and foodstuffs from its former colonies and traditional suppliers such as China, Korea and Taiwan. G.C. Allen, \textit{Japan as a Market and Source of Supply}, Oxford, Pergamon Press, 1967, Chapter 3.
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<tr>
<td>1967</td>
<td>285,266</td>
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The postwar food shortage also made it imperative for Japan to increase dependence on overseas wheat suppliers such as the United States and Australia.16

In the 1950s, improvement of the balance of payments position through export promotion became an important issue in the management of the Japanese economy. In general, Japan enjoyed favourable balances on current account in the first decade of the

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postwar period with the exception of 1946, 1953 and 1954.\footnote{Ibid., p.80.} This was due to US aid and special procurement during the Korean War which offset the perennial deficits in the trade account.\footnote{The US aid through the Government Appropriation for Relief in Occupied Area (GARIOA) funds was calculated as government donation in current account for statistical reasons. Akira Inuta, \textit{Kokusai Kin’yu, Boeki} [International finance and trade], Okurasho Zaiseishishitsu, ed., \textit{Showa Zaiseishi: Shusen kara Kowa made} [The history of finance during the Showa period: From the end of the Pacific War to the peace settlement], vol.15, Toyo Keizai Shimposha, 1976, p.607.} As US aid was withdrawn and the Korean War Boom waned, Japan was faced with the serious problem of ‘how to lift the ceiling of the balance of payments’. After buoyant domestic investment brought about high economic growth during the early 1950s and in 1956, the rapid increase in imports soon resulted in serious deficits in the trade account. In order to achieve the ‘national objective’ of maintaining a high level of investment and economic growth, it became imperative for the Japanese economy to finance increasing overseas purchases by the promotion of exports. Thus economic diplomacy had a significant role to play in the expansion of Japanese export markets.\footnote{Yamamoto, 1973, pp.31-32.} In view of the huge bilateral trade deficits and Australia’s tight import controls on Japanese goods during the early 1950s, it was no wonder that the Japanese officials emphasised the need to increase exports through reduction of trade barriers in Australian markets in the bilateral trade negotiations. Even after the conclusion of the Commerce Agreement, Japanese industrial circles continued to point out the problem of lopsided trade until Australia finally and formally abrogated its right to invoke GATT Article XXXV in the revised Commerce Agreement of 1963.\footnote{Allen, 1967, p.98. Japanese business leaders voiced their concern about the serious problem of Japan’s unfavourable trade imbalance with Australia in the inaugural meeting of the Japan-Australia Business Cooperation Committee held in May 1963. Hajime Takaki, ‘Dai-1-kai Nichi-Go Keizai Godo Iinkai nitsuite’ [On the inaugural Japan-Australia Business Cooperation Committee], \textit{Keizai to Gaiko}, no. 413, Second half of May 1963, p.15; Yasutaro Nizizeki, ‘Nichih-Go Keizai Godo Iinkai ni Sanka shite’ [Participating in the Japan-Australia Business Cooperation Committee], \textit{Keidanren Geppo}, vol.11, no.7, July 1963, pp.8-9. For analysis of the Japan-Australia Business Cooperation Committee, see Mayumi Kamada, ‘Private Economic Diplomacy in Australia-Japan Relations: The Role of Business Cooperation Committees’, Ph.D. thesis, Australian National University, 1989.} If improvement of the bilateral trade imbalance was one of the most significant objectives in postwar Japan’s diplomatic approach towards Australia, then the question arises as to why Japan let the bilateral trade deficit grow as it did. Before the early 1960s, when Japan accepted its international obligations under the GATT and the IMF to liberalise
import trade and renounce import restrictions for the purpose of safeguarding the balance of payments, the Japanese government had a wide range of measures at its disposal to check the inflow of Australian products. If it was seriously concerned about deterioration of the balance of payments, Tokyo could have corrected its huge bilateral trade deficit by imposing strong restraints on purchases from Australia, which were not indispensable. Food purchases from Australia could have been minimised if Japan had concentrated its domestic resources on increased rice production. As a supplier of raw materials for industrial production, Australia was less significant than the United States. While Japan also accumulated a huge trade deficit with the US in the postwar period, the main import commodity from the US was raw cotton which played a far more important role in the Japanese economy than Australian wool since Japan could not expect to earn significant income from the export of woollen manufactures.

After the retreat from the Chinese continent and the subsequent embargo on trade with the Communist countries, Japan had lost its traditional export markets for woollen products such as China, Manchuria and Korea so that woollen goods were manufactured mainly for domestic consumption. The future demand for woollen textiles also looked gloomy due to rapid technological advances in the production of artificial fibre. There developed an argument within Japanese domestic circles that in the light of the need to improve the balance of payments, purchases of raw wool should be curtailed to encourage the production of artificial fibre which was less dependent on the overseas supply of raw materials. Cotton textiles made from US raw cotton were one of Japan’s largest export items before the 1960s. There was every reason, therefore, for Japan to maintain purchases of US raw cotton, while reducing purchases of Australian wool.

While the huge deficit in US trade could be offset through US aid and the Korean War special procurement up until the early 1950s, if Japan wanted to pursue economic self-reliance without dependence on this extra dollar income, it needed to concentrate its

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21 The ratio of exports in the total production of Japanese woollen piece goods was 13.3% on average over the period 1934-36, while the highest figure recorded between 1946 and 1955 was 9.0% in 1955 with an annual average of 4.9%. Tsushosangyōshō Tsushōkyoku Tsushō Chosaka, 1956, pp.148-149.


23 In this thesis, the term 'economic self-reliance' will be used to correspond with the Japanese term keizai jiritsu, which can be defined as the situation where Japan is able to sustain economic growth without incurring the deterioration of the balance of payments position. While the SCAP and Japanese officials often used 'economic self-support' for keizai jiritsu in English documents, I believe the term 'self-
domestic resources on production of exportable goods. This could have earned dollars to pay for essential imports from the US. Although Japan could have financed its imports from the US by its export income from other areas such as Southeast Asia during the prewar period, suspension of dollar convertibility throughout the world during the postwar period annulled this method of settlement.²⁴ Hence, it would have been in Japan’s interest to make optimum use of its limited foreign currency reserves by giving first priority to importing raw materials for manufactured goods which were competitive in the tough dollar markets while confining other import trade to suppliers which were prepared to buy an adequate volume of Japanese goods. There seems to have been little room for Japan to maintain an unfavourable trade balance through the importation of products which would not generate export income. Despite this, Japan still continued to buy from Australia and accumulate unfavourable bilateral trade deficits. Why did Japan continue to run these deficits with Australia and how were they financed?

AUSTRALIA'S ROLE UNDER THE STERLING TRADE AND PAYMENTS AGREEMENTS

After the conclusion of the Interim Sterling Payments Agreement in November 1947 and the subsequent Overall Sterling Payments Agreement in May 1948 between the Supreme Commander for Allied Powers in Occupied Japan (SCAP) and the representatives of the United Kingdom Mission in Tokyo, postwar Japanese trade with the sterling area countries was mainly settled by sterling cash. Australia and New Zealand became parties to the Interim Agreement, and the Overall Agreement was applied to trade between Japan and all the sterling area countries except Hong Kong. In August 1951 the new Sterling Payments Agreement was concluded by the Japanese government and the United Kingdom delegates to include Hong Kong and to further facilitate Japan’s sterling trade. Under these Sterling Payments Agreements, Japan’s overall sterling balance was a significant determinant of trade with Australia up until the mid 1950s.²⁵

²⁵ Both the Interim and the Overall Payments Agreements were concluded through exchange of memoranda. The memorandum for the Interim Agreement was entitled ‘Interim Agreement for Financing Private Trade with Japan’, which hereafter will be described as the ‘Interim Payments Agreement’. The memorandum for the Overall Agreement was entitled ‘Payments Arrangements for
The Overall Payments Agreement was expected to play a role in expanding Japanese sterling trade. The worldwide dollar shortage in the early postwar period encouraged each country to balance its trade on a country-by-country basis to conserve extremely limited dollar balances. The need to settle dollar transactions in cash on the spot hampered trade expansion. Sterling area countries had been good export markets for Japanese light industrial goods since the 1930s, and the inability of the United Kingdom to supply to these markets in the postwar period offered opportunities for Japan to export manufactured goods to the sterling area. Since the Overall Payments Agreement provided for sterling settlement, the foreign exchange control authorities of these countries felt freer in granting import licences for Japanese goods with less concern about the need to use the dollar. This resulted in the accumulation of a certain amount of sterling by Japan. Under circumstances where free convertibility of sterling into dollars had been suspended, accumulated sterling could only be used in the sterling area. Since the Agreement stipulated a so-called dollar convertibility clause which gave SCAP the right to convert sterling funds in its account into dollars every six months, the sterling countries restrained purchases from Japan for fear of a dollar drain should SCAP exercise this right rigidly. In order to balance Japan's overall sterling trade at a maximum level, it was necessary for Japan to spend the surplus accrued from sales to each sterling area country on purchases from suppliers in the same area.

Australia had the largest capacity to supply Japan with imports among the sterling area countries and was the main absorber of Japanese sterling funds. Japan's deficits in bilateral transactions with Australia played a significant role in providing the other sterling countries with purchasing power for Japanese goods and expanding Japan's trade with the whole sterling area. In addition, Australia's capacity to supply foodstuffs contributed towards saving dollar expenditure as a substitute source for US wheat.26 If Japanese

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26 Cohen, 1958, p.142
purchases from Australia had dwindled, Japan would have accumulated excessive amounts of sterling which might eventually have had to be converted into dollars, and the sterling area countries would have been forced to restrain imports from Japan to avoid the risk of losing their dollars. Then overall Japanese sterling trade would have struck a balance at a low level. This would have resulted in the shrinkage of the overall level of Japanese trade and industrial production for export.

Australia also played an important part in raising the level of Japanese sterling trade when stagnation of British purchases of Japanese goods affected Japan's procurement from the sterling area. As the main supplier to Japan among the sterling countries, Australia was most sensitive to curtailment of Japanese sterling trade. It was in Australia's interest to let Japan accumulate an adequate amount of sterling by giving Japanese goods the opportunity to compete more freely in sterling area markets. Thus, among the sterling area countries which tended to impose tight controls on Japanese imports in defence of the value of the pound sterling as well as for reasons of domestic industrial protection, Australia became most responsive to Japanese diplomatic approaches in pursuit of relaxation of import restrictions in the sterling area where tight import controls severely affected Japan's export earnings. Apart from the political objectives of economic diplomacy to normalise Japan's status within international trade organisations, the successful conclusion of the 1957 Commerce Agreement should therefore be examined in the context of the expansion of Japan's overall sterling trade in the postwar period.

This thesis analyses Japan's trade policy interests leading up to the Commerce Agreement with Australia by focusing on Australia's significance in the overall expansion of Japanese sterling trade. In order to clarify Australia's position in the Japanese trade strategy, it is necessary to begin with a discussion of the significance of sterling trade in the process whereby the Japanese consolidated their postwar strategy for economic recovery and self-reliance through trade promotion on a more multilateral basis, overcoming the inclination towards restoration of the traditional Chinese commercial links, or development of domestic resources, or dependence on dollar-based trade through US economic assistance.

27 India was more positive in leaving their market open for Japanese capital goods for their own economic development. Sakito Sato, 'Kyotei Boeki kara Mita Pondo Boeki' [Sterling trade through bilateral arrangements], Yushutsu Menshifu Geppo, vol.3, no.9, September 1953, p.2.
DEBATE OVER POSTWAR JAPANESE TRADE STRATEGY FOR ECONOMIC RECOVERY AND SELF-RELIANCE

Chapter 2 examines the policy debate over the restoration of Japanese trade networks destroyed during the Pacific War. In the early postwar period, Japanese government officials aimed at the recovery of Japanese trade centred on industrial exports to Asia. However, Japan was forced to change these plans when the deterioration of the Cold War in Asia made it clear that Japan could no longer count on the restoration of traditional import and export trade with the Chinese continent at the end of the 1940s.

The breakdown of the original trade strategy based on the traditional Chinese networks deprived the Japanese of their confidence in achieving economic recovery and self-reliance centred on trade promotion on a commercial basis. As international circumstances in the Cold War prevented Japan from restoring its traditional commercial links, the worldwide dollar shortage forced many trading nations to maintain tight exchange controls on overseas trade, and US aid for Japanese recovery was curtailed, there emerged two types of strategy to overcome Japan’s predicament.

The first proposal advocated that Japan should concentrate on development of its domestic resources to achieve economic recovery, since it could not count on benefits from trade expansion, given the difficult international circumstances. This view was mainly advocated by the intellectuals, but it was also in line with the economic recovery programs for government-led domestic development centred on the heavy and chemical industries, as visualised by the Economic Stabilisation Board during the early postwar period. This strategy was rejected by the government under the leadership of Prime Minister Shigeru Yoshida who preferred market-oriented economic management to government intervention and also by Joseph Dodge who as SCAP’s advisor instructed the Japanese government to implement austere economic policies to achieve economic self-reliance.

The second proposal focused on making full use of extra dollar supply through the US strategic aid program for economic development of Southeast Asia. Although the Korean War Boom provided Japan with extra dollar income through special procurements, it was evident that Japan could not count on such ‘windfall profits’ in the medium to long term. Nor could it rely on US appropriated funds which were to be curtailed with the Peace Settlement in sight. With Chinese links broken, Japan increased its dependence on supply of
commodities from the dollar area. Although it did need to earn dollars through export promotion on a normal commercial basis, its heavy industrial sectors had not been strong enough to compete with the producers of the other advanced countries. This situation led the Japanese to seek every possible source of dollar income and depend heavily on the United States.

Hence, when there emerged a proposal for a US-Japan Economic Cooperation Program in late 1950, Japanese government and business circles developed a strong interest in the prospect of integrating Southeast Asian markets with Japanese industrial production. The Cooperation Program aimed to utilise the US strategic aid to provide the non-Communist Southeast Asian countries with purchasing power for Japanese capital goods for their economic development. If the Program had materialised, Japan could have expected to obtain the double advantage of a source of a stable dollar income and special commercial networks which would substitute for the traditional Chinese continental markets, subsidised by the US aid for strategic reasons. These benefits seemed so attractive that the Japanese had excessive expectations for implementation of the Program, which proved fruitless, as the US administration was not in the event prepared to provide additional aid for Japan. The Japanese over-reaction to the proposal for handy dollar income reflected a lack of confidence in achievement of economic self-reliance under tough international trading circumstances.

Deprived of this handy source of dollar income, Japan had no alternative but to make its own self-help efforts for industrial rationalisation and export promotion on an unsubsidised commercial basis, as prescribed by the Dodge Line. Since Japan's industrial sectors were yet to strengthen their competitive edge, it had to develop its exports to any market where demand for industrial goods was active, without excessive stress on dollar earnings. This situation also compelled Japan to divert its procurement of raw materials and foodstuffs away from the dollar area, in order to save its scarce funds. Under the worldwide dollar shortage, the key to trade expansion had to be sought in bilateral trade and payments agreements. In fact, William Logan, who visited Japan as SCAP's advisor following the introduction of the Dodge Line, proposed expansion of networks of trade and payments agreements with non-dollar area countries, as a strategy for trade promotion under austere policies for economic self-reliance which forced Japanese industrial sectors to
abandon their reliance on government subsidies and to compete in overseas markets on a commercial basis. Logan also emphasised promotion of raw materials and foodstuffs imports rather than strict balancing of bilateral trade in the operation of these bilateral trade and payments agreements, in order to mitigate the restrictive effects of bilateral agreements under which both parties tended to restrict imports to maintain a strict trade balance for fear of a dollar drain.

The core of this idea was for economic self-reliance through trade promotion on a more multilateral basis, in that it aimed to expand Japan’s trade networks without undue emphasis on dollar earnings or the establishment of special commercial links with any specific region. If Japan was to finance its overseas purchases of raw materials and foodstuffs, it would have to make its own self-help effort for export promotion, as illustrated in the implementation of the Dodge Line. If Japan was to maintain active export performance to sustain its industrial operation, it would have to promote sales not only to the dollar area but also to the non-dollar area, and in turn it would have to diversify its sources of commodity supply from the dollar area to provide the purchasing power to non-dollar customers. This strategy was gradually consolidated within the Japanese government during the postwar period and became firmly established, as Japan confirmed its commitment to participation in the liberal international trade institution under the GATT. Although the Japanese occasionally showed an inclination to be enticed by the prospect of Chinese trade, domestic development and extra dollar income through US aid, it was this strategy that laid the foundation for Japan’s rapid economic growth during the 1960s.

The sterling area played the most important role in the evolution of this strategy for postwar trade promotion on a more multilateral basis, particularly under the worldwide dollar shortage. Firstly, despite the provision for dollar convertibility of Japan’s sterling surplus, the Overall Payments Agreement stipulated trade settlement through soft-currency in sterling, to minimise the rigidity of the normal dollar based open account transactions. Secondly, the Sterling Trade Arrangements were devices to promote multilateral transactions in that they aimed at balancing trade at the highest possible level by seeking balance with several sterling area countries together including Australia as one trading party with Japan. Thus each sterling participant in the Trade Arrangements did not have to worry about strict balancing of its own bilateral transactions with Japan. Thirdly, the sterling area
was important as Japan’s ‘natural’ export market because of strong demand for Japanese imports despite its restrictive policies deriving from concern about a dollar drain. Furthermore, the sterling area countries in Asia such as India, Pakistan and the British Malay Straits Colonies proved good customers of Japan’s heavy chemical goods.

It was Australia that played a pivotal role as the main non-dollar commodity supplier and, more significantly, as the circulator of purchasing power between Japan and the other sterling area countries, in absorbing Japan’s sterling surplus through its huge capacity to supply raw materials and foodstuffs. The important role of the Sterling Payments Agreements and Australia in sustaining a trade strategy on a more multilateral basis was not fully appreciated by the occupation authority nor by the Japanese government at the outset. They gradually came to recognise its significance, as Japan’s sterling trade increased its weight under the Sterling Trade and Payments Agreements, and on the other hand, the feasibility of the other strategies became doubtful. Hence, the remaining chapters of this thesis will trace the process whereby SCAP, and later the Japanese government, strengthened their commitment to expansion of sterling trade, focusing on the operations of the Sterling Payments Agreements up until 1954 when Australia made an important decision to open its market substantially for Japanese goods. The intention is to clarify Australia’s important role in sustaining Japan’s postwar strategy for trade promotion on a more multilateral basis. In this context, the real implication of the 1957 Commerce Agreement can be understood as central to the evolution of the postwar Japanese trade strategy.

**SCAP AND THE SIGNIFICANCE OF STERLING TRADE FOR POSTWAR JAPAN**

Chapter 3 discusses Australia-Japan trade in the early postwar period, before the expansion of Japanese sterling trade, focusing on Japan’s procurement of Australian wool. Since Japan had tended to have an unfavourable balance in Australian trade since the prewar days, resumption of imports from Australia rested on payments arrangements. Before the Overall Payments Agreement, Japan had few ways of financing purchases from Australia. Enjoying the benefits of a postwar sellers’ market, Australian did not have any particular need to grant special credit to its former enemy. It was also out of the question for the Japanese occupation authority to allocate to purchases from Australia its extremely limited dollar
funds appropriated from US aid for urgent relief in a war damaged nation. Imports of Australian wool virtually ceased and the shortage of raw wool seriously hampered the activities of the Japanese woollen mills in mid 1947.

In order to overcome these difficulties, SCAP adopted an anomalous system of wool procurement. It commissioned an American commercial firm to purchase raw wool in the most economical way it could from all over the world. Since the firm was experienced in dealing in South American wool, postwar Japanese wool imports were diverted to South America and South Africa, and Australian wool could not regain its prewar dominance in the Japanese market despite the fact that the Japanese woollen interests were extremely eager to use the Australian product. This case illustrates the fact that Australia-Japan trade could not flourish as long as Japan lacked a means of financing its purchases from Australia centred on wool during the early occupation period.

Chapter 4 reveals SCAP's conservative management of sterling funds and the stagnation of Japan's sterling trade until mid 1949. The Overall Payments Agreement unleashed active demand for Japanese goods such as cotton textiles among the sterling area countries. Concerned about the heavy dependence of the Japanese industrial production on raw materials from the dollar area, such as raw cotton, SCAP gave only low priority to purchases from the sterling area in the issuance of import licences, because capacity to supply strategic materials such as Indian raw cotton was extremely limited. Given Japan's dependence on US appropriated funds, SCAP was reluctant to run the risk of a dollar drain, allowing the sterling area to import in sterling transactions Japanese goods produced from raw materials from the dollar area. Hence, emphasising the urgent need for dollar earnings, SCAP tried to give higher priority for procurement of raw materials for industrial goods which could earn dollars through export and from sources which were prepared to purchase these Japanese goods. SCAP even showed interest in diverting imports not only of raw wool but also of wheat away from the sterling area to South America which seemed to have considerable demand for Japanese manufactured goods. SCAP officials in charge of the sterling funds also adopted a conservative approach to sterling trade, reluctant to give approval to the allocation of these funds for imports unless they had an adequate amount of sterling balance in hand. Thus SCAP tended to underbuy from the sterling area. When SCAP officials denied the possibility of converting accumulated sterling surplus into dollars,
the sterling area countries, in turn, tightened their import licensing against Japanese goods. Australia’s sales to Japan were badly affected by SCAP’s approach, which was biased against sterling trade out of its concern about dollar savings. It tried to link Japanese trade firmly with the dollar area, even at the cost of more multilateral expansion of commercial networks.

Chapter 5 reveals that SCAP began to recognise the significance of sterling trade for Japanese economic recovery from late 1949. SCAP did not convert its sterling funds into dollars even on the occasion of the devaluation of the pound sterling in September 1949 lest the sterling area should cease purchases from Japan for fear of a dollar drain. From the end of that year, SCAP authorised vigorous purchasing in the sterling area, particularly in Australia. Australia not only emerged as an important supplier of raw wool and wheat but also sustained Japanese exports to the sterling area countries which enjoyed extra purchasing power in the shape of sterling funds earned by Australia from Japan. The change in SCAP’s approach reflected the shift in the US occupation goals from suppressing Japan’s military strength to promoting its economic recovery and self-reliance, as illustrated in the so-called ‘reverse course’ of the occupation goals. However, due to the nature of Japan’s purchases from the sterling area, which tended to have a heavy seasonal concentration, and as a result of the deliberate delay in the relaxation of Britain’s tight import licensing, SCAP often fell short of sterling funds on a short term basis. When the British financial authority hesitated to extend special credit facilities to meet SCAP’s seasonal sterling shortage, the conservative SCAP fund controllers tried to improve the situation by a suspension in granting sterling import licences, to the detriment of Australia’s commercial sales. Although SCAP officials began to show interest in trade promotion on a more multilateral basis without giving top priority to dollar saving, they were yet to appreciate fully the importance of sterling trade.

Chapter 6 examines how SCAP came to integrate sterling trade with Japan’s economic recovery and self-reliance through the expansion of industrial production and trading activities. In the negotiations for a Sterling Trade Arrangement for the year 1950/51, SCAP officials went so far as to propose the establishment of freer non-discriminatory trade rules between Japan and the sterling area. SCAP’s approach was no longer biased towards dollar trade, for it agreed to ‘swap’ dollars for sterling to cope with
the seasonal shortages. SCAP also came to regard removal of the dollar convertibility clause in the Overall Payments Agreement as acceptable if the range of Japan’s sterling trade was widened through freer transferability of Japan’s sterling balances. In fact, the existence of the dollar convertibility clause had become meaningless, for SCAP showed little hesitation in increasing the amount of its ‘sterling working balance’ for which it had agreed to waive the right to convert into dollars. Purchases from Australia were also substantially liberalised as the automatic approval system was applied to a large part of wool import in 1950. Freed from financial restraints, Japan’s sterling purchases expanded considerably to sustain expanded production activities during the Korean War Boom. At this stage, SCAP eventually confirmed its commitment to the strategy to pursue Japan’s economic self-reliance through trade promotion on a more multilateral basis.

Chapter 7 covers the stage where policy discretion on sterling trade and the negotiating power for a new Sterling Payments Agreement to replace the Overall Agreement was handed over to the Japanese government, in preparation for the San Francisco Peace Treaty in 1951. While Japanese officials made an attempt to introduce the GATT principle of non-discriminatory freer trade in the negotiations, their initial stance towards sterling trade was not as positive as their SCAP predecessors. They opposed the British request to remove the dollar convertibility clause because this might invite excessive accumulation of unusable sterling surplus in Japan’s accounts. But their real intention was to keep the Japanese currency as hard as possible and to link Japanese trade once again more closely with the dollar area. The Japanese government even considered the possibility of proposing Japan’s treatment as a dollar area country in the British import licensing system, should the United Kingdom refuse to retain the clause. This was an extraordinary option which might have jeopardised the commercial networks with the sterling area established under the Overall Payments Agreement.

In the background was the fact that Japanese government and business circles had too high an expectation of the US-Japan Economic Cooperation Program for strategic economic aid to Southeast Asia. The enticement of a stable source of extra dollar supply was such that the Japanese could not appreciate the significance of the sterling trade network already established by SCAP. However, the Cooperation Program did not bear fruit. In the end, Japan was forced to concede to the British request on political grounds in
order to finalise the sterling negotiations in time for the opening of the San Francisco Peace Conference. Japan’s approval of the removal of the dollar convertibility clause indicated that Japan had to make commitment to a trade strategy directed at developing its trade network on a more multilateral basis. In other words, the Japanese were forced to shake away their feeling of dependency on the United States, on the eve of the restoration of independence.

Chapter 8 discusses Japanese responses to the expansion of sterling trade following the 1951 Sterling Payments Agreement. After the removal of the dollar convertibility clause, the sterling area increased its purchases from Japan remarkably from the latter half of 1951 to early 1952. As a result, Japan accumulated a huge amount of sterling surplus. There arose a controversy within the Japanese government over measures to tackle these sterling accumulations. As the Japanese exchange control authority, the Foreign Exchange Control Board (FECB) took the view that it was unsound to accumulate unusable sterling surpluses, as it would weaken Japan’s dollar position. The FECB advocated the introduction of drastic financial restraints on export sales to the sterling area. The Ministry of International Trade and Industry (MITI) and the Ministry of Foreign Affairs (MFA) argued that such export restraint measures would do damage to the commercial networks with the sterling area and that the introduction of such arbitrary restrictive measures might infringe the principle of freer multilateral trade under the Bretton-Woods system in which Japan had already pledged to participate. The solution to the sterling accumulation should be sought in expansion of procurement of sterling commodities, they argued.

In the event, export restraint measures were introduced in a much more moderated form than originally proposed by the FECB in March 1952, due to the intervention by MITI and the MFA. This meant that Japan reconfirmed its intention to pursue expansion of sterling trade under the Sterling Payments Agreement and its commitment to the strategy for trade promotion on a more multilateral basis. In fact, the Japanese government unveiled extensive procurement programs from the sterling area in which Australia consolidated its position as the main commodity supplier for Japan. As illustrated by the conclusion of the long-term barley purchase contract with Australia in November 1952, Japan came to emphasis securing stable supplies of Australian products on a commercial basis.
The sudden increases in Japanese imports after the new Sterling Payments Agreement resulted in the deterioration of the balance of payments position of the sterling area countries. Under guidance from London, the sterling area adopted collective action to tighten sharply import licensing in March 1952. This caused a rapid drain of Japan's sterling funds, and a serious sterling shortage resulted. In 1953, Japan's trade balance continued to deteriorate not only with the sterling area but also with the dollar area and other countries with which Japan settled trade through open accounts. It became imperative for Japan to overcome this crisis in the overall balance of payments position in 1953–54.

AUSTRALIA'S ROLE IN JAPANESE STRATEGY FOR ECONOMIC SELF-RELIANCE

Chapter 9 looks at the measures adopted by the Japanese government which tried to tackle the crisis through export promotion rather than arbitrary import restrictions. The Yoshida government attributed the balance of payments crisis to the overheated economic conditions that developed in anticipation of the continuation of the Korean War Boom. Yoshida considered it imperative to strengthen Japan's industrial competitiveness by restraining inflationary pressure and at the same time rationalising industrial structure, in order to overcome the fundamental bottlenecks affecting Japan's economic self-reliance. Hence, the Yoshida government opted for an austere economic policy to restrain domestic demand rather than introduce selective import controls as had occurred in the sterling area. Such import restrictions were considered unhelpful since they might have aggravated inflationary pressure. An immediate solution to the crisis in the balance of payments could only be found in the promotion of exports. Industrial rationalisation programs aimed at strengthening the competitiveness of the heavy and chemical industries. When heavy industry products became competitive enough to match those of the other Western industrialised countries, Japan could expect to increase its heavy industrial exports to Southeast Asia where it enjoyed a geographical comparative advantage. But it would still take some time before this rationalisation process was fully completed and the region enjoyed the political stability necessary to initiate economic development.
Under these circumstances, the Japanese government again showed an inclination towards dependence on extra dollar supplies. In the negotiations for the Mutual Security Act (MSA) Agreement with the United States in 1953–54, the Yoshida government tried to obtain not only purely military assistance but also aid for economic development, in return for its commitment to increasing self-defence efforts. Business circles welcomed this aid program proposal, as they had the fruitless US-Japan Economic Cooperation Program in the previous years. However, the US administration not only flatly rejected the Japanese request, but also urged the Japanese to make efforts for economic self-reliance through sound trade promotion.

If Japan was to address the crisis through trade promotion without counting on extra dollar supplies, it had to pursue export promotion through minimising overseas trade barriers against Japanese goods. While North American markets had been liberalised in the first half of the 1950s through the conclusion of the formal bilateral trade treaty and agreement with the United States and Canada, the sterling area had imposed tight import restrictions against Japan since 1952. It became imperative for the Japanese government to initiate economic diplomacy to persuade sterling area countries to relax their selective and tight import licensing against Japanese goods, in an attempt to improve the serious sterling shortage.

Australia was the main target in this economic diplomacy, as Japan recorded the largest bilateral deficit with Australia among the sterling area countries during the balance of payments crisis. Between 1952 and 1954, Tokyo requested that Canberra should relax its import controls on several occasions, insisting that with the risk of a dollar drain eliminated, Australia should cease its discriminatory treatment and categorise Japan as a soft currency source in its import licensing system. At first, Australia conceded only minor relaxations. In 1954, however, Japan’s tight monetary policy severely affected Australia’s sales of wool and other commodities, and the Japanese government attempted to divert imports away from Australia, as it concluded barter trade arrangements with Argentina for the purchase of wool and the exports of machinery. Alarmed at these developments, the Australian government made a significant decision to relax its import restrictions substantially by giving most imports from Japan soft currency treatment in November 1954. This measure virtually put Japan’s export trade to Australia on a normal non-discriminatory
basis in that most Japanese goods were to be given equal treatment in import licensing with other soft currency countries in the Australian market. Although Australia still retained the right to invoke selective import restrictions targeting Japan, import licensing to safeguard the balance of payments played a far more significant role in Australia's domestic protection at that time. Thereafter, the focus in Australia-Japan trade relations shifted towards political issues such as Japan's accession to the GATT and negotiations toward a formal trade agreement between the two nations.

The significance of the diplomatic approach to ameliorate sterling shortages was that Japan further deepened its commitment to a multilateral based trade strategy, in that it opted for minimisation of overseas trade barriers to promote export competition on a commercial basis. The government had little alternative but to rule out arbitrary import restrictions and dependence on extra dollar supply, if it was to aim seriously at achieving economic self-reliance. Under this strategy, the Japanese recognised the need not only to secure stable commodity supplies from Australia but also to promote exports to the Australian market.

Chapter 10 concludes that sterling trade played a central part in the Japanese strategy for economic recovery and self-reliance through trade promotion on a more multilateral basis in the postwar period. Australia contributed strongly towards sustaining the expansion of Japan's sterling trade in that it provided the sterling area countries with purchasing power for Japanese goods through its bilateral surplus earned from export sales to Japan. Although SCAP and the Japanese government were once inclined to develop a postwar Japanese trade network with a preference for dollar earnings and with Southeast Asia as a substitute for the Chinese continent, against sterling trade, such a strategy did not bear fruit. Japan had no alternative but to aim at expanding its trade in any direction without bias toward any specific currency area or region. In the implementation of this strategy, the sterling area made a significant contribution to sustaining Japanese industrial recovery through active import demand for Japanese industrial goods. Australia's role was important as a lubricator of postwar Japanese trade growth under the Sterling Payments Agreements. Australia's supply capacity was significant in maintaining the overall trade balance between Japan and the sterling area. By providing adequate purchasing power with other sterling countries through its bilateral trade surplus with Japan, Australia helped Japan
to expand commercial opportunities in sterling markets. Without Australia, Japan would surely have been forced to restrain expansion of sterling trade, because of concern about a dollar drain through excessive accumulation of unusable sterling surplus, or the sterling area would have kept imports from Japan under tighter control to prevent Japan from converting its sterling balance into dollars. As Japan's dependence on industrial exports to multilateral channels increased, minimisation of trade barriers in the sterling markets through trade negotiations became a more pressing issue in the Japanese economic diplomacy. Realising the significance of securing a profitable export market in Japan, Australia took the initiative to consolidate freer bilateral trade relations with Japan, through the relaxation of its import licensing against Japanese goods in November 1954.

Chapter 10 further examines the importance of the 1957 Commerce Agreement in the context of Australia's role in the evolution of the postwar Japanese strategy for trade promotion on a more multilateral basis. As one of the biggest beneficiaries of the Japanese strategy for trade in multilateral directions, it was in Australia's interest to respond positively to the Japanese aspirations for participation in the liberal international trade forum under the GATT, lest Japan should move away from this strategy and divert import trade towards other suppliers. At the same time as the announcement of the relaxation of import licensing in November 1954, Australia also submitted the proposal for opening trade talks with Japan. Canberra revealed a preparedness to negotiate a formal trade agreement containing exchange of most-favoured-nation treatment. Discouraged by strong anti-Japanese sentiment in Australia and its restrictive trade approach as revealed in its retention of Article XXXV on the occasion of Japan's accession to membership of the GATT, however, Japanese officials were remarkably passive towards the offer to negotiate. As the Japanese realised the genuineness of Australia's intentions for bilateral trade liberalisation, they became confident about the prospect of breaking through the international chains of trade discrimination under the GATT and the feasibility of the multilateral trade strategy.

Acceptance of the Australian request for non-discriminatory treatment of wheat imports meant that the Japanese government also had to make an important decision to abandon the surplus disposal agreement with the United States. The surplus disposal program symbolised Japan's lingering attachment to dependence on US trade channels and inclination towards domestic agricultural development. The relinquishment of the program
which gave preference to US agricultural products meant that Japan reconfirmed its commitment to trade expansion on a multilateral basis guided by commercial factors. From this perspective, the 1957 Commerce Agreement can be seen as Australia's significant role in consolidating the Japanese commitment to the strategy for trade promotion on a more multilateral basis. This thesis explores the role of the Sterling Payments Agreements in laying the foundations of this strategy.
2 Japan’s Postwar Trade Strategy and the Role of the Sterling Trade and Payments Agreements

When Japan was defeated in the Pacific War, the reconstruction of the war-shattered economy became the most pressing task for the Japanese nation. The enormous reduction of production capacity and the loss of overseas colonies forced Japan to rethink its trade strategy for economic recovery. This chapter examines the four different policy issues in Japanese trade strategy in the immediate postwar period: the re-establishment of commercial links with East Asia; the policy debates over promotion of foreign trade and/or domestic development; the reliance on US-Japan economic cooperation; and the engagement in establishment of more multilateral commercial networks through bilateral trade and payments agreements.

It will be shown that the fourth element in the trade strategy involving trade and payments agreements with the sterling area set Japan on a path towards trade expansion on a more multilateral basis. Australia played a significant role as the lubricator of Japan’s overall sterling trade. Indeed, it was Australian export earnings which provided the whole sterling area with purchasing power for essential Japanese manufactured goods.

RE-ESTABLISHING COMMERCIAL LINKS WITH EAST ASIA

Just a day after the end of the Pacific War on 15 August 1945, the inaugural meeting of the Senso Mondai Kenkyukai [Workshop on the postwar problems] was held, attended by a dozen young Japanese bureaucrats and academics. Its organiser, Saburo Okita, recalls that they started talking about postwar Japan’s participation in the liberal international economic organisations under the Bretton-Woods system from the outset.¹ After the forty odd


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meetings, the workshop issued its report entitled *Nihon Keizai Saiken no Kihon Mondai* [Basic problems in reconstruction of the Japanese economy] in March 1946. A revised version of this report was published by the Ministry of Foreign Affairs in September. The report proposed a strategy for the restoration of the war-devastated Japanese economy through participation in the international division of labour. It presented arguments about the direction of Japan’s trade. The report categorically rejected seeking autarchy derived from ‘narrow-minded nationalism’ on the grounds that it would result in the deterioration of Japanese economic activities as the prewar economic management for autarchy had invited the devastation of the country by the Pacific War. Instead, it emphasised an alternative strategy to promote trade through participation in the international division of labour.\(^2\) Despite its strong interest in international trade, the report did not deny the necessity to attain self-sufficiency in foodstuffs and raw materials during the early postwar period when low production levels, unfavourable terms of export and lack of finance made it extremely difficult to initiate trade.\(^3\)

With regard to the specific features of postwar Japanese trade networks, the government planners, as exemplified in an official memorandum of mid 1946 from the MFA, proposed to promote the exports of heavy and chemical industrial goods towards ‘Toa’. While the Chinese characters for ‘Toa’ stand for East Asia, the concept of ‘Toa’ developed here referred not only to the Far East but also to Southeast and South Asia including India.\(^4\)

The Japanese idea for re-establishing commercial links with ‘East Asia’ was based on the following three considerations. Firstly, the Japanese planners did not see a bright future for light industrial exports. Although they did not deny their significance, it was expected

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4 It was stated, ‘If Burma and India are included in the East Asian areas, trade with East Asia will form a great part of Japan’s trade with Asia’. Gaimusho, ‘Nihon no Tai-Toa Boeki no Shorai’ [The future of Japanese trade with East Asia], 20/9/46, Gaimusho Gaiko Shiryoukan [Diplomatic Archives Office, MFA; hereafter abbreviated as DAO], E’2.0. 0.9. An English memorandum on Japanese trade appears in the same DAO documents. MFA, ‘Japan’s Trade with the East Asian Countries’, Undated (August 1946?), DAO, *ibid.*
that Japan’s labour-intensive sectors would face tough competition from Asian countries such as China and India which were expected to achieve rapid industrialisation centred on these sectors. Moreover, it would become difficult to secure procurement of an adequate volume of raw materials such as raw cotton from these countries as they would try to utilise the commodities for their own industrial production. Nor did the Japanese strategy refer to the possibility of light industrial exports to the Western markets as there had been in the 1930s. The option of an export drive through ‘social dumping’ was categorically rejected on the grounds that the Bretton-Woods system would not permit that, and cheap labour would hamper development of Japanese domestic markets.

Secondly, the strategy laid special emphasis on heavy and chemical industrial exports to East Asia. The planners were conscious of the ‘intermediate status’ of the Japanese industrial structure and observed that, ‘as much cannot be expected of the exports of industrial goods to the United States and highly industrialized European countries, Japan is obliged to seek markets for them in East Asia’. While they pointed out that the export of machinery and chemical products to East Asia had flourished from 1937 on, their idea depended on the calculation that, in an attempt to procure capital goods for industrialisation with their lower national incomes, East Asian countries might look to the importation of Japanese manufactures which were cheaper, even if of lesser quality, than those from Western sources. This calculation was based on the expectation that it was most favourable for Japan to develop industrialisation, for example in machinery, where large values could be added to the input of labour, Japan’s sole abundant resource. In addition, the similarity of living standards, labour efficiency and physical conditions in East Asia would allow Japanese manufactures to adapt better to the needs of Asian consumers than could Western manufacturers. The Japanese aspiration to heavy industrial production was such that it foreshadowed the later development of the other strategies for domestic development and reliance on US economic cooperation, when the East Asian commercial links evaporated.

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6 Ibid., p.198.
7 ‘Nihon no Tai-Toa Boeki no Shorai’, p.5.
8 Ibid., p.2
9 Ibid., p.15.
Thirdly, the aim of the strategy was the establishment of an East Asian trading sphere under the heading of ‘industrial division of labour on an equal footing between China and Japan’.\textsuperscript{10} The idea derived from the awareness of the absolute necessity of export earnings from East Asia to finance the importation of materials required for Japan’s economic recovery, as Japan was expected to become more dependent on the US for these supplies.\textsuperscript{11}

Although the planners had the clear intention of committing Japan to the freer and multilateral international trade system, they were conscious of the difficulties in developing trade under this system in the light of the shortage of products and tight exchange controls. Hence, they saw the need to re-establish traditional commercial links with China.

These considerations led Japanese officials to concentrate on development of regional trade with East Asia. Their bias towards East Asian trade can be traced in the proposal to maintain purchases, regardless of the economic rationale, of rice and sugar from Taiwan and Korea which were dearer than other suppliers, in order to give these countries purchasing power for Japanese manufactures.\textsuperscript{12} Emphasis on integration of postwar Japanese trade with East Asia might be perceived as a vestige of Japan’s wartime ambition for the Great East Asian Co-Prosperity Sphere. To allay these fears, the planners argued:

\textit{Of course, Japan has no intention of monopolizing East Asian trade but expects such countries as British India, Australia, and China will take part in it. On the contrary, Japan is most anxious to go into rational international division of labour or international economic cooperation, instead of competition, with them [\textit{my emphasis}].}\textsuperscript{13}

In view of the strong focus on Asia’s rapid industrialisation, participation in a ‘rational international division of labour’ by the three countries nominated in the document may have meant participation as industrial manufacturers rather than commodity producers. If so, it is interesting that the two big trading nations in the sterling area, namely India and Australia, were regarded here as rivals in industrial exports rather than potential export markets and raw material suppliers. If these countries were to develop as industrial rivals, Japan might face tough competition not only from the Western advanced producers but also from these

\textsuperscript{10} \textit{Ibid.}, p.7.
\textsuperscript{11} \textit{Ibid.}, p.5; ‘Kaitei Nihon Keizai Saiken no Kihon Mondai’, p.200.
\textsuperscript{12} The Foreign Affairs memorandum expected that ‘the dilemma will be solved in the world trade structure which aims at multilateral trade relations’; ‘Nihon no Tai-Toa Boeki no Shorai’, p.13
\textsuperscript{13} ‘Japan’s Trade with the East Asian Countries’, pp.2-3.
neighbouring countries. Such a lack of confidence in Japanese industry’s competitive ability and overestimation of the prospects of industrial development of these Asia Pacific countries may partly explain the reason for inclination which emerged later towards domestic development and reliance on the US over an option to promote sterling trade on a commercial basis.

There were serious difficulties in the early postwar strategy with the promotion of heavy industrial exports to East Asia as a solution to increasing dependence on US supplies. Firstly, the Japanese plan neglected the possibility that Japanese exports would face tough competition from Western countries in East Asian markets. To be sure, at the initial stage of the recovery of postwar industrial production, exportation of Japanese heavy industrial goods to East Asia was considered feasible on the grounds of their price competitiveness, due to the geographical proximity to the East Asian markets and government subsidies.

The extremely tough reparations program in the initial stages of the occupation was moderated in late 1947, and Japanese industries were relieved from concern that the Allied Powers might confiscate their production facilities and equipment as reparation for East Asian countries. The shift in US occupation policy vitalised Japanese aspirations for the formulation of a program for economic recovery. In May 1948, the Japanese Economic Stabilisation Board started discussing a Five-Year Plan for Economic Restoration which aimed at overcoming inflation through the expansion of industrial production. Expansion of industrial activities was in line with the concept of Keisha Seisan Hoshiki [First priorities for production of coal and steel], which aimed at the recovery of production levels by concentrating domestic resources on coal and steel production through interventionist measures such as loans by the Reconstruction Finance Bank and price subsidies. The policy played a role in preventing the disruption of the process of heavy and chemical industrialisation after the war; the cost was hyper-inflation. Japanese steel products thus

16 Yutaka Kosai, ‘Fukkoki’ [Period of economic recovery], Ryutarō Komiya, Masahiro Okuno and Kotaro Suzumura, eds., Nihon no Sango Sou Seisaku [Japan’s industrial policy], University of Tokyo Press, 1984, pp.30-34.
became competitive with those of other advanced countries because of government subsidies.\textsuperscript{17}

US occupation policy shifted towards giving first priority to Japan’s economic stabilisation rather than the restoration of production levels, through a policy for restraining inflation at any cost. In December 1948, the Supreme Commander for Allied Powers, General Douglas MacArthur, ordered the Japanese government led by Shigeru Yoshida to implement a ‘Nine Point Economic Stabilisation Directive’ introducing extremely tough fiscal restraint aimed at balancing the government budget. In order to promote the economic stabilisation program, Joseph Dodge, president of the Detroit Bank, visited Japan as financial advisor to SCAP in February 1949.

The austere domestic economic policies recommended by Dodge discouraged Japanese aspirations for the expansion of heavy and chemical industrial exports. Based on the idea that expansion of production was not a panacea to increase exports, the Dodge Line curtailed government subsidies drastically in order to achieve a ‘genuine’ balance of the budget.\textsuperscript{18} Although the Dodge Line aimed at Japan’s trade recovery through strengthening its industrial competitiveness by means of austere measures in the mid to long term, in the short term it exposed Japanese industries to tough international competition, and the abolition of price subsidies revealed the uncompetitiveness of the Japanese steel industry.\textsuperscript{19} Cohen explains the difficulties facing the Japanese industries and their effect on export trade:

Naturally, in the absence of subsidies, higher steel prices reflect themselves in higher costs in the steel-using industries such as machinery and equipment, metal products, rolling stock, etc. Paradoxically, therefore, it is just those Japanese industries which have the best hope of expanding exports that are high-cost producers when compared with international competitors, while the older, lighter consumer goods industries, more of whose products it may be difficult in the future to sell abroad because of the growth of indigenous industry in underdeveloped countries, are lower-cost producers.\textsuperscript{20}

\textsuperscript{17} Cohen, 1958, p.70.
\textsuperscript{18} Shiraiishi, 1983, pp.54-55.
\textsuperscript{20} Cohen, 1958, pp.75-76.
Thus, in order to sustain heavy and chemical industrial exports, even to the adjacent East Asian markets, Japan had to spend some time on the drastic rationalisation of these sectors. Since industrial rationalisation would require launching new investment to modernise production facilities, a sharp contradiction was evident between the concept of the Dodge Line and the reality of industrial rationalisation; in fact, the Japanese economy had to wait until the Korean War Boom provided extra revenue for both the government budget and the balance of payments to enable governmental and industrial circles to implement rationalisation programs.21 Before then, Japan had no alternative but to earn export income through the competitive light industrial sector, if she was to pursue opportunities in the freer multilateral international trading system without developing preferential commercial links with the adjacent East Asian region.

The second difficulty in the Japanese trade strategy was that its credibility was totally dependent on the premise that trade with China would be fully open to postwar Japan, and that China would soon become politically stable enough to implement rapid industrialisation. It is evident that the strategy put Japan’s traditional partners such as China, Korea and Taiwan at the centre of its East Asian trade strategy. Behind the emphasis on traditional Chinese trade lay a pessimistic view about the development of commercial links outside the Far Eastern region. The MFA report of September 1946 on problems in the recovery of the Japanese economy pointed out that there was uncertainty about whether Japan would be allowed to join the free multilateral international trade system.22 While many Asian nations were obtaining independence during the 1940s, there was anxiety among the planners that Western countries would still exert influence in keeping Japanese goods away from their former colonial markets as they had done against the Japanese export drive during the 1930s. One of the documents revealed this suspicion about possible barriers to be imposed on Japanese goods in these markets. It stated that when Japan had to face competition from Western countries in East Asian markets, it would be convenient if Japan was advised in advance as to how much she would be ‘permitted’ to export to these outlets.23

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23 ‘Nihon no Tai Toa Boeki no Shorai’, p.15.
If Japanese industry was to compete with European products in Southeast Asian markets under such conditions, the supply of cheaper raw materials from China was crucial. Okita, the central figure in the formulation of the strategy, envisaged enormous difficulties in the future of Southeast Asian trade and tough competition with European manufacturers in these markets, because of the uncompetitive nature of Japan’s steel products resulting from the breakdown in the supply of raw materials from cheap Chinese sources.24

When the recession under the Dodge Line hit the Japanese economy, there was increased optimism about the restoration of Chinese trade. In fact, a survey undertaken by the Federation of Economic Organizations [Keidanren] from late 1949 to early 1950 found that, among its member companies, there was overwhelming support for resumption of Chinese trade as a solution to the economic crisis. Following the shift to completely private trade at the beginning of 1950, SCAP also began to encourage exports to Communist China.25 The US Department of State made a decision to permit Japan to trade with China in March 1950, and the Japanese commercial firms entered several contracts for purchases of Chinese commodities such as soya bean, coal and salt. At the end of April, the House of Councilors passed a resolution for the promotion of China-Japan trade.26

The rising tide of interest in Chinese trade was completely shattered when Communist China joined the Korean War against the United Nations Forces led by the United States in October 1950. In response to the US embargo on trade with China, the Japanese government introduced a ban on exports to China in December 1950. Retaliation by China halted plans to import coal, iron ore, soya bean, and other minerals and made procurement of these commodities from dearer alternative suppliers inevitable.27 Since Japan’s embargo against Chinese trade under the US occupation covered a far wider range of goods than

24 Saburo Okita, ‘Ajia Keizai to Nihon Keizai’ [Japan and Asian economies], Sekai, no.52, April 1950, pp.48-49.
those introduced by the West European countries under the Coordinating Committee for Export to Communist Area (COCOM), Japan’s trade with China ceased except for indirect trade via Hong Kong channels.  

When the special procurement boom began to subside in 1952, there was renewed optimism about Chinese trade among Japanese domestic business circles. On their return from the International Economic Conference in Moscow, the three Japanese Diet Members visited Beijing to conclude a Japan-China Trade Arrangement in June 1952. Although the Japanese government had made application to participate in COCOM a month before — soon after the power to regulate of Chinese trade was handed over by SCAP — it expected that, having joined COCOM, Japan’s trade with China would be favoured by more moderate regulation. In fact, hardline US policy against China forced the Japanese government to accept stricter regulation of Chinese trade.  

Japan’s trade regulations against China remained stricter than those against other communist countries until 1957. Hence, in the early 1950s the Japanese had to face the problem of making up for the loss of Chinese trade by establishing alternative commercial networks.

**FOREIGN TRADE OR DOMESTIC DEVELOPMENT?**

The recession induced by the deflationary policy of the Dodge Line and the closure of Chinese trade resulted in an important policy debate over the future direction of the Japanese economy. Economists such as Hiromi Arisawa and Shigeto Tsuru, both of whom had been involved in the formulation of the MFA economic recovery strategy in the early postwar period, advocated maximisation of the development of Japan’s domestic resources, warning of the danger of excessive dependence on foreign trade. Their idea, which was called *kaihatsu shugi* (the domestic development school), was based on pessimism about the international trade environment at the height of the Cold War. Arisawa wrote, showing his anxiety about the Dodge Line:

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30 *Ibid.*, p.127. Ishii’s article points out the inter-departmental conflicts over the problem of the embargo on Chinese trade and its effect on Japan’s economic self-support within the US administration under President Dwight Eisenhower.
In these days the process for economic stability is the process for decontrol as well as return to free trade ... However, if we turn our eyes to the serious problems facing the Japanese economy under the international circumstances in which postwar Japanese economy is placed, there is no guarantee that return to free trade will offer a self-evident answer for their solution.\textsuperscript{31}

He pointed out three factors which made the postwar international circumstances 'disadvantageous' to the expansion of trade. Firstly, the closure of East-West trade because of the Cold War had reduced export markets for capitalist countries. Secondly, rapid technological innovation such as the introduction of synthetic fibres would reduce world demand for Southeast Asian raw materials. This would result in a shrinkage of Southeast Asian purchasing power. Furthermore, development of the cotton textile industries in India would curtail India's exports of raw cotton and imports of cotton piece goods. Thirdly, the concentration of the wealth and capital of the world on the United States had resulted in a worldwide shortage of purchasing power. It would still take some years before US dollar aid led to expansion of other countries' exports.\textsuperscript{32}

Tsuru did not hide his scepticism about the possibility of a return to an international free trade system, in view of the rising significance of 'political' influence in trade. His arguments centred on the increase in trade within the communist bloc and within the British Commonwealth of Nations, financial settlement of trade through dollar aid and the increasing significance of quantitative import restrictions, instead of tariffs, as an instrument for trade control. Thus he asserted, 'lower prices may not sell as much as in the past' and 'Japan will surely lose if it becomes the only country seeking free trade'.\textsuperscript{33}

According to Tsuruta, the ideas of Arisawa and Tsuru are in line with Nihon Keizai Saiken no Kihon Mondai in that they were united in their emphasis on the significance of government intervention and in their doubt about the market mechanism of automatic adjustment.\textsuperscript{34} As discussed earlier, Nihon Keizai no Kihon Mondai revealed a strong

\textsuperscript{31} Hiromi Arisawa, 'Nihon Shihon Shugi no Unmei: Nakayama Kyoju no 'Nihon Keizai no Kao' ni Yosete' [The fate of the Japanese capitalism: Comments on Professor Nakayama's article], \textit{Hyoron}, February 1950, p.8.

\textsuperscript{32} \textit{Ibid.}, pp 8-14.


preference for trade with China centred on heavy and chemical industrial exports. The emphasis on the development of domestic resources through economic planning was a reaction, in desperation, to the stern realities of international politics under the Cold War which deprived postwar Japan of its traditional trade partners on the Chinese continent.

Opposing the domestic development school, there emerged ideas stressing the significance of foreign trade for the Japanese economy. Ichiro Nakayama, Professor of Economics at the Hitotsubashi University in Tokyo, represented the foreign trade school (boeki shugi). In his book entitled Nihon Keizai no Kao [The face of the Japanese Economy], Nakayama was optimistic about the international trade environment and the future of Japanese trade. He praised the Bretton-Woods system because it made clear its intention to construct a peaceful world through the recovery of world trade and creation of an international key currency. Nakayama appreciated the Breton-Woods system's stress on the principle of international cooperation in management of the world economy. On the future direction of Japanese trade, Nakayama revealed a strong hope for Southeast Asian trade growth fostered by programs for Asian reconstruction and development under the US Point Four Plan and the British Colombo Plan.

This emphasis on Southeast Asian trade was the antithesis of the domestic development argument. Nakayama warned against expecting too much from Chinese trade, insisting that there was little possibility of an increase in Chinese purchases of Japan's competitive consumer goods such as textiles, as China would confine its imports to capital goods in an attempt to construct a foundation for economic development at any cost. Nakayama claimed that there was no need to fear Asia's industrialisation because there would remain ample room for the horizontal division of industrial production. There should also not be an overestimation of the effects of technological innovation in diminishing international import demand for Asian raw materials such as natural rubber, raw silk, raw cotton and raw wool. This argument ignored the economic cost in the production

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35 Ichiro Nakayama, Nihon Keizai no Kao [The face of the Japanese economy], Nihon Hyoron Shinsha, 1953, pp.144-145. This book is an omnibus of his articles which mainly appeared in the monthly journal Hyoron during the late 1940s to the early 1950s. The debate originated from Nakayama's article of the same title as his book which appeared in the December 1949 issue of the Hyoron. In the subsequent issues, Arisawa and Tsuru raised their criticism to Nakayama's arguments for foreign trade.

36 Ibid., pp.96-102.
of substitute goods made from domestic resources. While Nakayama’s arguments were based on the theory of the international division of labour in accordance with comparative advantage, he did not present specific policy options for the expansion of trade. But his arguments suggest that Nakayama had in mind export promotion centred on light industrial goods, making full use of their strong competitiveness.

In view of his emphasis on the unfavourable effect of import restrictions in the sterling area and the restrictive nature of bilateral trade and payment agreements, Nakayama seems to have been conscious of the need to minimise restrictive measures imposed on Japanese exports. He took an optimistic view of the prospect for reducing trade barriers, when he suggested that a solution for overcoming the stagnation of trading activities should be sought through strengthening international cooperation. Further, he warned against overemphasising the politicisation of postwar trade. Taking as an example the import restrictions adopted by the sterling area countries in 1951–52, he argued that the United Kingdom would not be able to keep the other British Commonwealth nations from opening their doors to Japanese goods as long as these nations saw mutual interest in Japanese trade. This view was in line with that of the Japanese government approach during the 1950s and the early 1960s when the economic diplomacy to open export markets through bilateral negotiations played a significant role in the promotion of Japan’s trade policy, as discussed in Chapter 9.

Okita presented his own unique idea which in a sense encompassed the arguments of both Arisawa and Nakayama. As one of the authors of *Nihon Keizai Saiken no Kihon Mondai*, he was well aware of the bleak international circumstances in which the existing political situation prevented full realisation of the benefits of the international division of production. Hence, Okita argued for the need to maintain the domestic steel industry through ‘artificial measures’ such as protective tariffs and subsidies, even at the cost of economic efficiency, in view of the significance of maintaining employment, saving foreign exchange, maintaining strategic industries and minimising the unfavourable effect of fluctuations in the world economy. On the other hand, he shared Nakayama’s optimism about international cooperation under the Bretton-Woods system, insisting that, ‘if

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37 Ibid., p.138.
38 Tsuruta, 1982, p.29.
judgements and considerations based on long-term interests for the world economy come forth, overcoming the specific interests of private capital, there is no reason to assert that international trade will result in unilateral losses for smaller nations.\textsuperscript{40}

According to Tsuruta, postwar Japanese industrial policy was developed in line with Okita's views, as shown in the implementation of the heavy industrial modernisation and rationalisation programs along with promotion of overseas export centred on competitive light industrial goods during the early to mid 1950s. He observes the tension over the preference in economic policy between trade promotion on a market-oriented commercial basis and heavy and chemical industrialisation through government intervention. There was no necessary consensus within Japanese domestic policy circles about the feasibility of expanding heavy industrial production during the 1950s. For example, Hisato Ichimata, President of the Bank of Japan, took a critical attitude against the establishment of a large-scale steel production plant in Chiba by the Kawasaki Steel Company since he was concerned about its commercial feasibility. Raising doubts about Japan's capacity to develop the automobile industry efficiently, the Ministry of Transportation supported an increase in imports as a solution to the rising demand for automobiles.\textsuperscript{41}

Kono provides an explanation for postwar Japanese economic policy which contained the dual elements of both trade promotion based on comparative advantage and heavy and chemical industrial development through government intervention. Under the coalition between the Socialist Party and the Democratic Party led by Prime Ministers Tetsu Katayama and Hitoshi Ashida in 1947–48, the Japanese government worked out economic restoration programs drafted by the Economic Stabilisation Board. The programs gave priority to restoration of production levels centred on the heavy and chemical industries with less dependence on overseas trade, as illustrated in Keisha Seisan Hoshiki. This direction was in line with the ideas of Tsuru, Arisawa and Okita, who all participated in the workshop for Nihon Keizai Saiken no Kihon Mondai. When Yoshida formed his second cabinet after the demise of the coalition government in November 1948, however, he showed strong leadership in turning the direction of economic policy from restoration of production to the promotion of exports. The introduction of the Dodge Line emphasising

\textsuperscript{40} Saburo Okita, 'Kokusai Kaihatsu ka, Boeki Izon ka' [Domestic development or foreign trade?], Kokumin Keizai, vol.4, no.6, June 1949, pp.9-14.

\textsuperscript{41} Tsuruta, 1982, pp.33-39.
economic stability in 1949 further strengthened Yoshida’s position on trade promotion based on a competitive light industrial sector. But there still remained strong voices advocating heavy and chemical industrialisation through government intervention in anticipation of its effects in the creation of employment opportunities, among government and political circles centred on the domestic industrial sections of MITI. While Kono’s observation suggests that postwar Japanese economic policy was formulated with the background of tension between market-oriented trade promotion and government-led industrial development, there is no denying that Yoshida shifted the weight of government policy away from domestic development to foreign trade.

A document presented by MITI acknowledges this point. In launching the Law for Promotion of Industrial Rationalisation in July 1952, MITI warned that the apparently remarkable restoration of domestic production levels was mainly due to the instability caused by the Korean War Boom. Japan’s overall level of trade still remained extremely low. In order to maintain the minimum daily food supply of 2,160 calories per capita, as prescribed by SCAP, it was estimated that Japan still had to depend on imports for one-fifth of its total food supply, as well as other raw materials. It followed that these import demands needed to be offset by active promotion of exports if Japan was to maintain a sound balance of its external payments. Furthermore, in the light of the increasing liabilities for settlement of overseas debt, the cessation of US aid and reparation payment responsibilities, incurred with the restoration of independence, Japan needed to depend more on the promotion of trade. MITI concluded that it should adopt a stance based on the foreign trade school as a means for achieving economic self-reliance.

If Japan was to pursue expansion of foreign trade, it was imperative to find a means to finance its imports of essential foodstuffs and raw materials. In the circumstance of the worldwide dollar shortage, two options were open. The first option was to rely on US goodwill to continue dollar aid, directly or indirectly for Japan. The second was to create

purchasing power for Japanese goods among its trade partners through Japan's own effort to expand two-way balanced trade. It is no wonder that the Japanese were tempted to adopt the first and easier option.

**EXCESSIVE EXPECTATION CONCERNING THE US-JAPAN ECONOMIC COOPERATION PROGRAM**

At the beginning of the 1950s, dissatisfaction increased within the Japanese policy circles over the austere recessionary policy of the Dodge Line and the tight regulation of Chinese trade. The stagnation of trade was such that there seemed to be no alternative but to rely on US aid unless Japan was to reverse its anti-Chinese policy and pursue the resumption of active trade with Communist China against the will of the US administration. But the outbreak of the Korean War in June 1950 and subsequent dollar earnings which accrued to Japan through special procurement provided timely relief to the Japanese economy. Special procurement provided Japan with extra dollar earnings of $150 million in 1950, $624 million in 1951, $791 million in 1952 and $803 million in 1953.\(^{44}\)

Before the Korean War Boom, the Japanese government was preoccupied with securing dollar earnings through the US aid program for reconstruction and development of Southeast Asia. The Economic Stabilisation Board (ESB) worked on a program for Japan's economic self-reliance in response to the introduction of the Dodge Line. Given that economic self-reliance was defined as 'sustaining sound balance of payments as well as achieving an improvement of living standards', Japan had to find measures to overcome the dollar shortage which was expected to emerge as US aid was withdrawn.\(^{45}\) The report titled *Jiritsu Keizai Tassei no Shojoken* [Conditions for achieving economic self-reliance]

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\(^{44}\) Akira Inuta, *Kokusai Kin'yū Boeki*, [International finance and trade], Okurasho Zaiseishis-shitsu [Finance History Unit, Ministry of Finance(MOF)], ed., *Shōwa Zaiseishi: Shusen kara Kowa made* [The history of finance during the Showa period: From the end of the Pacific War to the peace settlement], vol.15, Tokyo Keizai Shimposha, 1976, p.606. The cited figures are the aggregated sum of the goods and services which the Allied Forces procured in Japan (special procurement in a narrow sense) and the receipts for the goods and services which the military personnel, staff and their families consumed in Japan special procurement in a broad sense).

which was submitted by the ESB on 3 June 1950 just before the outbreak of the Korean War, argued that it would be impossible to overcome the dollar shortage by 1953 given the shrinkage of raw silk exports to the US and the loss of the Chinese market, because free convertibility of sterling into dollars was yet to be restored and Japan had to depend on restrictive bilateral arrangements for the expansion of trade. The ESB report saw one option in larger demand for Japanese capital goods under an Asian version of the Marshall Plan which had been discussed within the US administration.  

The idea for an Asian version of the Marshall Plan came from the US Undersecretary of the Army, Tracy Voorhees in January 1950. Voorhees proposed that Japan’s trade recovery be promoted through ‘coordinated aid’, that is, ‘US dollar aid to South East Asia which was tied to purchases in Japan’. Voorhees’ assistant, Robert West, and Stanley Andrews of the Department of Agriculture were accordingly given a mission to study the feasibility of linking Japanese industrial production with Southeast Asia. Their report highlighted Japan’s capacity to contribute towards increased food production in Southeast Asia through supply of fertilisers, farm machinery, agricultural technicians and other capital goods to sustain agricultural and industrial development programs which were getting under way in the region. Purchases of Japanese industrial products were to be financed through increased export of Southeast Asian foodstuffs and raw materials. In fact, the Andrew-West report was optimistic that successful development programs would enable Japan to purchase two-thirds of its total food requirement from Southeast Asia and Australia by 1952. On the difficulties in financing trade between Japan and the Southeast Asian countries, the report underlined the unfavourable effect of tight import licensing policies by the sterling countries led by the United Kingdom in the latter half of 1949 and the resultant shortage of Japan’s sterling holdings. It also referred to the restrictive aspects of the existing Sterling Trade Arrangement which did not allow the sterling countries which were

46 Ibid., pp.90-98.
47 Borden, 1984, p.126.
48 Stanley Andrews and Robert West, ‘Report of Southeast and South Asia Food and Trade Mission’, March 1950, pp.8-11. SCAP, 6365(3), ESS(A)02450. SCAP records are available at the Archives on Contemporary Political History of the National Diet Library, Tokyo. These records are copied from the original documents of the National Archives, Washington D.C. into microfiches. In this thesis, the sources of the SCAP documents are described under the heading ‘SCAP’, followed by the four digits numbers with parenthesised numbers, which correspond to the box numbers of the original documents, then followed by SCAP sections’ abbreviations such as ESS with parenthesised alphabetical letters and five digit numbers, which denote the microfiche numbers of the National Diet Library Archives.
not participating in the Arrangement (such as Burma and Pakistan) to increase their purchases of Japanese goods by paying sterling beyond the sum of their respective export earnings in their bilateral trade with Japan. The Andrews-West Report saw bright prospects for the expansion of Japan’s trade with Southeast Asia through the relaxation of existing trade arrangements.

SCAP had also begun to consider the possibility of mobilising Japan’s industrial capacity for economic development in Southeast Asia. In April 1950, a document entitled, ‘Japan’s Export Potential With Specific Reference to the Economic Development of the Countries of South and South East Asia’ was formulated by the Economic and Scientific Section (ESS).49 Mentioning the stable growth of Japanese exports to South and Southeast Asia in the postwar period, the document pointed out the importance for Japan of the import of foodstuffs and raw materials from the region. In view of the projects under consideration for domestic development in these countries such as agricultural mechanisation, improvement of transportation, communication and electric power facilities and expansion of textile manufacture, the document stressed that Japan had the capacity to meet the rising demand for machinery and transportation equipment. It was estimated that Japan’s exports to the region would increase from $232 million in 1949 to $259 million in 1950, $410 million in 1951 and $710 million in 1955.

Significantly, the document referred to the prospect for the settlement of trade through normal commercial channels, ‘in a large measure, payment for such goods [Japan’s capital goods] can be made through Japan’s imports from these [Southeast Asian] countries under existing and proposed trade agreements ... The needs of the South and Southeast Asian countries have been explored by SCAP from time to time with a view to expanding Japan’s export trade and at the same time contributing to the rehabilitation and development of those countries’.50 This seems to have reflected the complicated reaction of the ESS Chief, William F. Marquat, to Washington in working out a plan for the integration of Japanese trade with Southeast Asia. According to Borden:

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49 Economic Studies Unit, Trade Arrangements Branch, Foreign Trade and Commerce Division, ESS, ‘Japan’s Export Potential With Specific Reference to the Economic Development of the Countries of South and South East Asia’, 15 April 1950, SCAP, 6686(17), ESS(A)04799.

50 Ibid.
General Marquat, head of ESS, reacted somewhat bitterly to the Andrews-West report in March, since it implied that SCAP had overlooked such obvious and beneficial remedies for the Japanese trade dilemma. He said that in the postwar climate of intense Asian nationalism, the theme of the report would provoke anti-Japanese sentiments because it was "economically similar" to the former Japanese "Co-prosperity Sphere." On the other hand, he boasted that the ESS had so successfully promoted Japanese-Southeast Asian trade that it had aroused the "bitter reactions of the British."  

What SCAP had in mind at this stage was expansion of Japan’s trade with South and Southeast Asia through 'existing and proposed trade agreements' on an unsubsidised commercial basis, without dependence on the injection of extra dollars through the proposed US 'coordinated aid'. In this sense, SCAP's idea was quite in line with the Dodge Line. If Japan was to pursue this course, it would have to develop its commercial networks on a more multilateral basis without excessive inclination towards dollar-based trade. Since the Overall Payments Agreement and the Sterling Trade Arrangement covered the largest volume of trade among the other bilateral agreements, it was evident that the sterling area would play a significant role in expanding Japanese trade in this direction. 

In fact, the provisions of the Overall Payments Agreement contained a mechanism which could lead Japan's sterling trade towards balance at an increased level. The settlement of trade in such a soft currency as sterling mitigated the unfavourable effect of the worldwide dollar shortage. Since the Sterling Trade Arrangement treated the sterling area countries such as the United Kingdom and its colonies, Australia, New Zealand and India, and later South Africa and Ceylon as a single party in trading with Japan, it minimised the demerits of bilateral trade arrangements which tended to reduce the level of trade. If Japan's trade with Australia had been regulated by a bilateral trade arrangement, Japan would not have been able to increase its purchases of Australian wool from the depressed level that had existed before the introduction of the Sterling Trade Arrangement, as pointed out in Chapter 3. By late 1949, as discussed in Chapter 5, SCAP had agreed virtually to suspend its right under the Overall Payment Agreement to convert its sterling funds into dollars in order to relieve the sterling countries from anxiety about losing dollars through active purchases of Japanese goods. Moreover, if Japan was allowed to transfer its sterling funds more freely to payments of imports from sterling countries not participating in the

51 Borden, 1984, p.128.
Sterling Trade Arrangement such as Burma and Pakistan, it could expect procurement of a wider range of commodities on a sterling basis. In fact, reflecting these considerations, SCAP persisted in the increased transferability of its sterling balance for facilitating purchases from Burma and Pakistan in the 1950 sterling trade negotiations, as shown in Chapter 6. Hence, the sterling area had significant weight in SCAP’s trade strategy for Japan’s economic self-reliance at this period. The ESS document of April 1950 estimated the share of the sterling countries in Japan’s export to South and Southeast Asia at 45 per cent in 1950, 37 per cent in 1951 and 31 per cent in 1955. The decreasing trend was due to the diminishing share of India which was expected to become more self-sufficient in textile production.52

As the US dollar aid program to Southeast Asia took shape in October 1950, at the height of the Korean War special procurement, the Japanese government moved away from the Dodge Line strategy for economic self-reliance without dependence on US aid and showed increasing interest in the possibility of securing a stable source of extra dollar income through participation in the US-Japan Economic Cooperation Program which aimed to mobilise the Japanese industrial capacity in the US strategy for containment of Communism in Asia.

An English document by the MFA in December 1950, entitled ‘Position of National Economy of Japan in Asia’ revealed government recognition of the importance of Southeast Asian trade for the Japanese economy.53 Behind this document lay the prospect of ‘drastic retrogression of our Chinese trade’. In justifying the priority which it attached to Southeast Asian trade, the document pointed out factors such as the ‘complementary’ and ‘mutually advantageous’ nature of Japanese capital goods and technology and Southeast Asian raw materials, geographical proximity and lower freight cost, and industrialisation and agricultural modernisation programs in the region. While the tone was supportive of SCAP’s strategy for trade expansion guided by comparative advantage on a commercial basis, the document emphasised ‘capital aid’ from the US, Britain and other interested parties as an essential factor for successful economic development. This was the start of

52 ‘Japan’s Export Potential With Specific Reference to the Economic Development of the Countries of South and South East Asia’.
Japan's shift towards reliance on US dollar aid to Southeast Asia, and it represented a deviation from the self-reliant trade strategy under the Dodge Line.

In 1951, the US aid program to Southeast Asia was named the US-Japan Economic Cooperation Program. Borden explains its objectives as envisaged by the SCAP and Washington policy makers:

Morrow, Marquat, Dulles, Dodge, the Army, and the State Department all viewed procurement as a way to continue to subsidize Japan's economy without aid. Until Southeast Asia developed sufficient raw materials supplies and until world currency convertibility was restored, dollar subsidies for Japan were necessary to preserve American markets and ensure that the strong forces in Japan which supported extensive trade with China did not prevail.\(^{54}\)

In May, Marquat officially endorsed Japanese participation in the Economic Cooperation Program with the United States, reporting that Japan was in a good position to export to Southeast Asia capital and consumer goods which America or European manufacturers could not supply, as they were involved in military production. Marquat also suggested that Japan should make an effort to obtain US economic and technological aid. In quick response to the Marquat statement, the Yoshida government endorsed its commitment to cooperation with the United States.\(^{55}\) Japanese government officials still recognised the significance of commercial purchases from the sterling area as well as dollar subsidies, but gave top priority to securing essential raw materials rather than export promotion in sterling trade during the height of the Korean War Boom. In February 1951 the ESB submitted to SCAP Japanese interests in the Economic Cooperation Program, including extension of sterling credit facilities such as pound usance and dollar swap.\(^{56}\)

As the Korean War Boom subsided, when the armistice talks started in Korea in July 1951, it became evident that Japan would sooner or later lose extra dollar earnings under special procurement arrangements. At this point, strong Japanese preference for extra

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\(^{54}\) Borden, 1984, p.151.


dollar earnings through US aid to the region emerged. The ‘B Document’ which was taken by Japanese delegates to the San Francisco Peace Conference estimated development of Japanese trade up to 1954. It predicted the inevitability of dollar deficits as a result of dollar loans to improve electric power generation facilities which had been the most serious bottleneck in improving Japan’s production capacity. The document recommended two measures to reimburse the dollar deficit, namely, diversion of dollar imports to the sterling or open account areas and allocation of a part of US military and economic aid to Southeast Asia for purchases of Japanese goods. According to Nakamura, the objective of the ‘B Document’ lay in confirming that the Japanese economy could not achieve self-reliance without US loans and the aid program for economic development of Southeast Asia as well as special procurement. It was at this stage that the Japanese government made an attempt to shift its central strategy from self-reliant trade expansion through payments and trade arrangements to the dependence on easy dollar earnings through US aid, as discussed in Chapter 7.

Although Japanese government and business circles developed an attitude favouring increased dependence on the US aid program for Southeast Asia in the pursuit of Japan’s economic ‘self-reliance’, the US-Japan Economic Cooperation Program did not, in the event, come to fruition. When the possibility of the US supply of dollars for the region became bleak, Japan had no option but to provide Southeast Asian countries with purchasing power through normal commercial channels with increased Japanese import of commodities, from these countries in order to promote export markets for Japan’s heavy and chemical industrial goods. Around November 1951, the Japanese government changed its stance towards the Economic Cooperation with the United States. In its memorandum to SCAP in February 1952, entitled ‘Establishment of Viable Economy and Promotion of Economic Cooperation’, the Japanese government revealed its intention to seek dollar earnings through the ‘new special procurement’, by committing itself to cooperation with the United States in military production. As will be pointed out in Chapter 9, Japan expected to earn dollars through the US Mutual Security Program encompassing the

Southeast Asian region. However, the Mutual Security Program concentrated on defence assistance in military terms, excluding dollar aid for Japan’s economic self-reliance. Thus, emphasis was placed on Japan’s cooperation to further economic development of Southeast Asian countries through the supply of Japanese industrial goods via normal trade channels rather than US aid. The memorandum stated that Japan was prepared to make a positive contribution towards the economic development of the Southeast Asian countries through the increased import of goods and raw materials from the region. This was also expected to improve Japan’s enormous surplus in sterling trade.²⁵

Since these countries were primarily underdeveloped due to social and political instability, they were seriously limited in their ability to finance trade through the supply of commodities for Japan. For example, Japan’s trade with Indonesia, a promising trade partner for Japan, resulted in such a huge Japanese surplus after the conclusion of the dollar-based open account trade and payments arrangements in July 1952, that the Japanese government had to resort to tight regulation of textile exports to Indonesia in August 1954.²⁶ It was found that Indonesia’s domestic regulations and the monopoly by the Dutch commercial firms and domestic shipping services caused the prices of its export commodities such as rubber and copra to rise.²⁷

In contrast, the sterling area countries in Southeast and South Asia could utilise purchasing power earned by the large supply capacity of Australia under the Overall Payments Agreement. More significantly, the dollar convertibility clause was removed in the new Sterling Payments Agreement of August 1951. Freed from concern about the loss of dollars, the sterling area countries in Southeast and South Asia could feel more relaxed about increasing their purchases from Japan. The range of uses of Japan’s sterling surplus was also widened as sterling became transferable to purchases from all the sterling area countries such as Burma and Pakistan which had not been covered by the Sterling Trade

²⁵ Quoted in Nakamura, 1982, pp.298-300.
²⁶ Anonymous, ‘Tai-Indonesia Keizai Danko no Kiki: Kajo Yushutsu Mondai to Baisho Mikaietsu no Karamiai’ [Deterioration of economic relations with Indonesia: Excessive trade surplus and reparations problems], *Ekonomisto*, vol.32, no.32, 7 August 1954, pp.34-39. There was suspicion in Japan that the Indonesian government intended to settle its accumulated trade deficits through Japanese reparation.
²⁷ Heitaro Inagaki, Member of the House of Councilors and Chairman of the Yokoham Rubber, ‘Tonan-a Shokoku ni taisuru Nihon no Boeki Taisaku ni tsuite’ [On Japanese trade policy towards Southeast Asia], *Keizai Jidai*, vol.18, no.1, January 1953, pp.47-50. The article is the record of Inagaki’s address on his return home as a leader of the Japanese government goodwill mission sent to Southeast Asian countries.
Arrangements but by individual bilateral arrangements. In fact, contrary to the SCAP prediction of April 1950 that the share of the sterling countries in South and Southeast Asia in Japan’s total export to the region would decline from 45 per cent in 1950 to 31 per cent in 1955, the share was maintained well above 40 per cent in 1955.

On the other hand, the exports to the non-dollar, non-sterling countries such as Indonesia, the Philippines and Thailand did not show as great an increase as expected. Since the trading activities with these countries still remained unimpressive in the early 1960s, the MFA did not hide its pessimism about the future of trade with these Southeast Asian countries in the early 1960s. Pointing out the diminishing Japanese imports from Southeast Asia, the MFA asserted in the 1960 issue of its Diplomatic Blue Paper:

As this tendency of imbalanced trade ... will not be solved unless economic development of the less developed countries makes progress, our trade with the Southeast Asian region will be forced to decline under the present situation. Hence we have no way to increase trade with the region but to develop Southeast Asian commodities which Japan can import or to provide these countries with purchasing power through some measures.62

In order to develop trade relations with the non-sterling countries in Southeast Asia, Japan had to wait until the establishment of special commercial ties such as the reparation agreements in the late 1950s.63

THE SIGNIFICANCE OF BILATERAL TRADE AND PAYMENTS AGREEMENTS

The failure to generate dollar earnings from the US-Japan Economic Cooperation Program meant that Japan had to depend on bilateral trade and payments agreements for the expansion of trade in the period of worldwide dollar shortage. Japan had to return to a trade strategy based on a more multilateral basis under the Dodge Line. In fact, the idea to


63 For Japan’s reparation agreements with the Southeast Asian countries, see Hagiwara, 1972, chapter 2 and Hideo Kobayashi, Sengo Nihon Shihonshugi to ‘Higashi Ajia Keizaiken’ [Postwar Japanese capitalism and ‘East Asia economic sphere’], Ochanomizu Shobo, 1983, chapter 1.
expand Japan’s trade through a network of trade arrangements derived from the days of the Dodge Line. Soon after the Dodge Line was implemented, SCAP invited several advisors to make recommendations for measures to be introduced for the recovery of Japanese trade. In September 1949, SCAP received a visit by the US Foreign Trade Advisory Commission led by Ormond Freile from the office of the Assistant Secretary of the Army. Freile supported export promotion on a unsubsidised commercial basis, by recommending full restoration of private import and export trade and abolition of export floor prices.64 Fearful of a recurrence of Japan’s social dumping of the 1930s with the removal of controls on export prices, Britain suggested the promotion of Chinese trade ‘as the logical outlet for Japan’s export’.65 In fact, Britain had lost its eagerness to expand the overall level of Japan’s sterling trade by early 1950 although the other sterling countries desired the growth of Japanese trade, as will be explained in Chapter 6.

Soon after Freile made his recommendation, the Director General of the Joint Export-Import Agency for Germany, William Logan, visited Japan to advise on trade expansion through decontrol. The Logan Mission made significant recommendations on trade policy which should ‘work as a permanent “lever” for the implementation of Japan’s economic stabilisation plan’.66 His recommendations included, simplification of import and export procedures, transfer of exchange controls to private banks, expansion of bilateral trade and payments agreements, and export promotion through increased import.67 In order to achieve an expansion of trade under the Dodge Line, Logan proposed to increase Japanese exports to the non-dollar areas where Japanese industrial goods could compete well on a commercial basis. Lack of purchasing power in these areas would be solved by expansion of Japan’s imports of their commodities, the so-called ‘import first method’. For this purpose, Logan recommended development of a network of bilateral trade and payments agreements. In order to minimise the tendency of bilateral agreements to balance trade at a lower level, he proposed provisions in the arrangements to allow the parties to ‘swing’ a

64 Ormond Freile, ‘Recommendations and Findings of the Advisory Mission for International Trade’, October 1949, SCAP, 5978(1), ESS(C)00078.
65 Borden, 1984, p.96.
certain amount of imbalance left at the end of the stipulated period into the following period without requiring settlement of the whole balance in cash.\textsuperscript{68}

The Logan concept would culminate in diversion of Japan’s import trade from the dollar area to the non-dollar area. By thus saving its dollar expenditure, Japan could expect to increase dollar purchases of raw materials for export goods such as raw cotton. This was a significant change from previous SCAP trade policy which gave top priority to earning dollars through export to the dollar area, as discussed in Chapter 4.\textsuperscript{69} SCAP immediately put Logan’s recommendations into practice. Soon after his mission, it finalised the negotiations for the Sterling Trade Arrangement for the year 1949/50. The Arrangement was revised to allow expansion of sterling trade, as discussed in Chapter 5.

Both the Freile mission and the Logan Plan did ultimately contribute to the Sterling Trade Arrangement, although the Freile mission was not receptive to development of bilateral trade and payments agreements pointing out their discriminatory effects on the dollar area countries such as the United States and Canada. However, the mission recommended the abolition of the trade plans attached to most of SCAP’s bilateral agreements and the establishment of provisions in the arrangements for consultation between SCAP and its counterparts ‘with the view to transferring credits to third countries’ in order to remove the necessity of balancing trade.\textsuperscript{70} This proposal was based on the same stance as Logan’s. While the Trade Plan was greatly simplified in the Sterling Trade Arrangements from 1949 in late 1949, the SCAP officials came to emphasise transferability of sterling funds to purchases from the sterling countries not participating in the Sterling Trade Arrangements such as rice from Burma and raw cotton from Pakistan and Egypt. Although the sterling side strongly resisted the introduction of full transferability, it agreed to permit diversion of a certain amount of Japan’s sterling funds towards trade with the non-participants, as discussed in Chapters 5 and 6. In this sense, the Sterling Arrangements also reflected Freile’s recommendations.

\textsuperscript{68} Ibid., p.412.
\textsuperscript{69} Kato, 1949, p.21.
\textsuperscript{70} John F. Shaw, Department of State, ‘Commercial Arrangements for Conducting the Foreign Trade of Occupied Japan’, October 1949, SCAP, 5978(1), ESS(C)00078. Shaw’s document was attached to Freile’s report.
The Logan plan was based on the assumption that Japan’s importation of raw materials for export goods should be financed by US dollar aid. Since the Economic Cooperation Program for extra dollar income through ‘coordinated aid’ to Southeast Asia had not materialised, Japan had a more pressing need to divert its supply to sterling and other non-dollar sources, in order to save dollars in imports. In this respect, Australia’s supply capacity played a significant role as an alternative source of foodstuffs such as wheat and barley. The conclusion of the long-term purchase agreement for barley from Australia in November 1952 illustrated the Japanese attempt to shift the purchase of foodstuffs to non-dollar sources of supply, as discussed in Chapter 8.

Although the Logan plan gave hope to the Japanese government and business circles which had been concerned about stagnation of exports caused by the devaluation of the pound sterling in September 1949, it also created scepticism about whether Logan’s success in bringing recovery to West German trade could be repeated in Japan as well. Compared with West Germany, Japan would have to face four handicaps. Firstly, West Germany enjoyed generous US aid under the Government Appropriation for Relief in Occupied Areas (GARIOA) as well as the Marshall Plan. Secondly, German machinery had strong international competitiveness due to its superior quality. Thirdly, West Germany could count on buoyant market conditions in Western Europe even though it had lost its traditional East European markets. Fourthly, West German commercial firms could maintain their strength while the dissolution of corporate oligopoly, namely zaibatsu kaitai, left hundreds of small less powerful firms in Japan in place of the prewar giant commercial firms. Of these handicaps, Japan could only expect to overcome through its own efforts the second and the fourth. Accordingly, industrial rationalisation and export promotion through revitalisation of commercial firms became important issues in Japanese trade and industrial policy during the 1950s.

Further pessimism prevailed over the Logan plan. The editorial of the economic journal Daiyamondo argued:

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72 Taxation measures such as tax rebates for opening overseas branches of commercial firms became one of the most important measures for export promotion from around 1953. Shiraishi, 1983, pp.123-124.
Thus unless a drastic measure is adopted to liberalise international conversion of currencies, the world-wide crisis will never be overcome merely by introduction of barter systems. The trade arrangement with the sterling area which has recently been concluded reveals this situation vividly. That is, under the current trade arrangement, the imports from the sterling area doubled last year’s, but exports remained the same. Because of that, Japan recorded a ten million pound deficit, which has worked to offset last year’s surplus. In view of this, it seems premature to assume that a barter system will immediately lead to export promotion.  

This argument shares the pessimism of the advocates of domestic development. It reflects strong doubt about the feasibility of a free multilateral trade system under the worldwide dollar shortage. The editorial was right in suggesting that export promotion through increased imports rested on the goodwill of Japan’s trade partners to relax import licensing. Hence, the diplomatic approaches for minimisation of trade barriers became another significant element in Japanese trade strategy during the 1950s which was initiated by the Logan plan. In this sense, Japan’s economic diplomacy in the 1950s was a logical development, as Japanese export goods were often subject to discriminatory treatment in import licensing and later under the GATT rules, especially among the sterling area countries.

While Logan recommended expansion of trade on a commercial basis and removal of domestic controls on trade, it does not follow that Japanese trade was drastically decontrolled. On the contrary, tight exchange controls remained a significant determinant of Japanese trade in the 1950s. Soon after Logan left Japan in October 1949, Jan A. Mladek and Ernest A. Wichin of the IMF visited Japan to give advice on a proposed system for Japan’s foreign exchange control. Following their recommendations, the Foreign Exchange and Foreign Exchange Control Law was enacted in December 1949. The law was designed to impose control on the whole range of activities related to foreign exchange and trade to maintain a sound balance in the payments position. Taking Logan’s advice, the foreign exchange budget allocation system was also established to support management of foreign exchanges under the law. Thus Logan’s idea was incorporated within the

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74 Inuta, 1976, p.54.
framework of the tight exchange control system proposed by Mладек and Вичин. In fact, Japan’s sterling trade after the peace settlement developed in an environment in which there was tension between considerations emphasising expansion of trade volumes on the one hand and sound exchange controls on the other, as revealed in Chapter 8.

The foreign exchange allocation system tended to give preference to sterling and other non-dollar trade to save dollar expenditure, so sterling trade became less constrained under normal conditions. However, in the case of a recurrent deterioration of the balance of payments, sterling trade became subject to foreign exchange restrictions under the system. Such circumstances affected the commercial interests of the main sterling suppliers, namely Australia, as shown in Chapter 9. It worked to strengthen Japan’s negotiating position in its diplomatic approaches to open Australian markets: Canberra drastically relaxed its tight discriminatory import licensing after November 1954.

In the early postwar period, Japan set out a strategy to re-establish the traditional trade network with East Asia centred on export of Japanese capital goods and imports of raw materials and foodstuffs from the Chinese continent. However, the austere policy prescribed by the Dodge Line exposed the uncompetitive nature of the Japanese heavy and chemical industries. The embargo introduced at the height of the Korean War completely shattered the Japanese aspiration for resumption of Chinese trade. Although Japan had to expect export earnings from the competitive light industrial sector, the tight exchange controls under the worldwide dollar shortage placed severe fetters on Japan’s attempts to promote exports. These bleak international circumstances created pessimism over the future of Japanese trade, which led to ideas stressing the development of Japan’s domestic resources rather than reliance on foreign trade. At the same time, Japanese government and business circles put excessive expectation on US ‘coordinated aid’ for the development of Southeast Asian trade, as a stopgap for the reduced US aid for Japan and the decline in the Korean War special procurement.

As the US-Japan Economic Cooperation Program proved fruitless, Japan had no alternative but to pursue a strategy of economic self-reliance through trade expansion on a normal commercial basis through more multilateral channels, as prescribed by the Dodge Line. Under this strategy the sterling area played a leading role, because the sterling trade

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75 Inoya, 1950, p.17.
and payments agreements provided a flexible mechanism to balance Japan’s overall sterling trade at a maximum level. Because it had the largest supply capacity in the sterling area, Australia assumed the role not only of helping divert Japan’s procurement from the dollar area but also of providing the other sterling countries with purchasing power for Japanese goods.

As sterling trade increased its significance, Japan faced a pressing need to liberalise trade barriers in the sterling area countries which tended to introduce tight import restrictions against Japanese goods in order to safeguard their balance of payments and sustain the value of the pound sterling. Hence, the sterling area also emerged as an important target for Japan’s economic diplomacy to open the sterling markets for Japanese exports. Since Canberra perceived the increasing significance of Japan as an outlet of primary commodities, Australia also took initiatives to respond positively to Japanese diplomatic approaches to relax Australia’s tight exchange controls.

The following chapters explore the management of trade under the sterling payments and trade agreements in detail and reveal the increasing priority which SCAP and the Japanese government came to give to trade with the sterling area countries, especially with Australia. It starts with the early postwar period when top priority was given to saving dollars, at the expense of expansion of Japan’s sterling trade and purchases of Australian wool.
3 Japan’s Wool Procurement System during the Occupation Period

Wool had been the central commodity in Australia-Japan trade during the prewar period. Australia had always been the largest supplier of wool to Japan. Before the mid 1930s, Australia’s share of the wool market amounted to approximately ninety per cent on average. The dependence of the Japanese woollen mills on Australian wool was based on the fact that Australian merino types were suitable for production of worsted fabrics used for the *kimono*, so the Japanese spindles, cards and looms were manufactured to fit Australian wool. As a result, Japan had become the second largest buyer of Australian wool by 1935 when Japan’s share reached almost one-third of total Australian wool exports. The Trade Diversion dispute of 1936 and Japan’s shift to a wartime economy reduced its demand for Australian wool, and the outbreak of the Pacific War terminated any exchange of commodities between the two nations.

**DIVERSION OF WOOL IMPORTS IN POSTWAR JAPAN**

Wool regained its position as the most important commodity when Australia-Japan trade was resumed in 1947, and wool remained on top until the mid 1960s when trade in minerals and resources took over. In the postwar period, the Japanese wool manufacturing industry resumed production utilising the prewar facilities and equipment, and Australian merino types were favoured for the production of worsted fabrics used for Western style apparel. Despite this, Australia’s share in Japan’s wool imports never reached its prewar level,

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1 Ito, 1957, p.97.
3 Ito, 1957, p.97.
staying around 70 per cent on average. Instead, other suppliers, especially South America, recorded a remarkable increase in their shares. Japan’s postwar wool procurement became relatively diversified compared with the prewar period.

The trade statistics show that the diversification of wool supply was evident from the beginning of the postwar period when wool procurement was controlled by the Japanese occupation authority. This chapter examines SCAP’s wool procurement policy before the introduction of a private wool import system in January 1950, in an attempt to show how Japan’s lack of a means for financing trade affected its wool purchases from the most coveted source, Australia. The predicament forced SCAP to seek anomalous trading methods for wool procurement and diversify the purchase of wool to non-Australian suppliers.

REHABILITATION PLAN FOR THE JAPANESE WOOL TEXTILE INDUSTRY

The production capacity of the wool manufacturing industry was considerably reduced as a result of wartime damage and the forcible scrapping of equipment and facilities for military production by the government. The percentage of total available capacity in 1945 against the figures of 1939 were 24 per cent in worsted spindles, 57 per cent in woollen cards and 33 per cent in textile looms respectively.\(^4\) Since wool manufacturing matched the occupation goals of demilitarising Japan, SCAP encouraged the resumption of production from the outset.\(^5\) In ‘A Program for the Japanese Woolen Industry’ of August 1947, SCAP set up an interim target to more than double the production capacity of 1945.\(^6\) Together with the objective of supplying the minimum amount of clothing for the Japanese people to prevent ‘disease and unrest’ and to provide a solution to the massive unemployment problem, SCAP emphasised the potential of the industry to become an excellent source of foreign exchange in view of the huge demand for wool manufactured goods in the Far East which had traditionally been a good market for Japanese wool fabrics in the prewar period.\(^7\)

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\(^{6}\) Textile Division, Economic and Scientific Section (ESS), SCAP, ‘A Program for the Japanese Woolen Industry’, 25 August 1947, SCAP, 6090(4), ESS(D)00807.

\(^{7}\) F.E. Pickelle, Deputy Chief, Foreign Trade Division, ESS, to W.F. Marquat, Chief, ESS, ‘Importation of Raw Wool’, 6 January 1947, SCAP, 6090(3), ESS(D)00806.
SCAP's emphasis on the rehabilitation of the Japanese wool manufacturing industry indicates that there was a growing demand for imported raw wool in Japan. Financial constraints, however, made it difficult to implement wool procurement.

Since Japan still had some wool stocks at the beginning of the occupation, SCAP initially directed the Japanese industry to use up these stocks for the moment. However, due to the relatively high operation rate approved by SCAP, these stocks declined so quickly that the Japanese government had to make an urgent plea to SCAP to import raw wool in early 1946. While emphasising the urgent need for raw wool, however, the Japanese government admitted the necessity to give a higher priority to the import of foodstuffs than wool. Thus with limited funds available, there was no alternative but to finance the importation of wool through the export of finished goods. Because exports of the Japanese wool manufacturing industry had earned only about 12 per cent of the cost of imported raw wool in the prewar period, the Exports and Imports Division of the ESS, which was responsible for supervising trading activities, rejected the Japanese application for wool to be imported and suggested manufacturing fabrics of a lower wool content.

At the beginning of 1947, it seemed imminent that raw wool stocks would soon run out. In this event, there would be no way but to shutdown the Japanese mills. Concerned about the ill effects of such a shutdown on the whole Japanese economy, the Foreign Trade and Commerce Division which was reorganised from the Exports and Imports Division, came to advocate strongly the resumption of wool imports, either by asking the British Commonwealth of Nations to extend credit to Japan or by making use of sterling or even dollars in the SCAP Trust Fund Account.

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8 Kanematsu Yomo Nempo, 1949, pp.73-74.
10 Import-Export Division, ESS, 'I.J.G. Application for the Importation of Wool', 12 March 1946, SCAP, 6782(7), ESS(A)05903. While the writer of this document describe the Division's name as the 'Import-Export Division', SCAP's official record describes it as the 'Exports and Imports Division'. SCAP, History of the Nonmilitary Activities of the Occupation of Japan, vol.2, Administration of the Occupation, p.60. In order to avoid confusion, I will use the 'Exports and Imports Division' in the main arguments, while leaving the title attached to the original document in showing the sources in the footnotes.
11 Pickelle to Marquat, 6 January 1947, ibid. The SCAP Trust Fund Account was originally opened to save the proceeds of Japanese exports to US which was dealt exclusively by the United States Commercial Corporation. Hiroshi Nishikawa, 'Boeki no Jittai to Tsusho Seisaku' [Realities of international trade and policy], Tshushosangyo sho Tsusho Sangyo Seisakushi Hensan linkai [Committee for the history of international trade policy, MITI], ed., Tsusho Sangyo Seisakushi, Dai-4-kan: Dai-I-ki,
JAPAN'S FIRST APPROACH TO AUSTRALIA FOR WOOL PROCUREMENT

In 1947, the Foreign Trade and Commerce Division began to examine various methods of financing the procurement of raw wool. In January, Frank Pickelle, then Deputy Chief (later Chief) of the Division presented to the Chief of the ESS, William F. Marquat, a proposal to purchase 30,000 bales of raw wool before March, and a further 90,000 bales before December making a total of 120,000 bales altogether for the 1947 calendar year. At first, it was planned to finance the purchase of the wool mainly from the credit expected to accrue from export sales of existing stocks of wool fabrics and prospective future products and, if this was insufficient, from the SCAP Trust Fund Account. However, financing through the small credit balance in the SCAP Trust Fund Account was ruled out since the Fund had to be spent on the procurement of essential raw materials of higher priority than wool such as cotton which was only available from the United States in dollars. Moreover, the British Commonwealth of Nations was least interested in the SCAP proposal of credit extension to Japan, though SCAP argued that this would benefit the British countries such as Hong Kong, Malaya and India which seemed to have a large demand for Japanese wool manufactured goods.

With no other feasible means of financing wool procurements, SCAP directly approached Japan's traditional wool supplier, Australia, with the Pickelle plan which proposed to finance wool imports by Japan's standing credits of approximately $500,000 from the export of raw silk to Australia in the previous year. In fact, SCAP had previously approached Australia with a similar proposal in 1946. It is necessary at this stage to examine the discussions between Australia and Japan in the second half of 1946, in order to comprehend fully the significance of this silk-wool barter proposal.

When S.F. Lynch of the Australian Department of External Affairs visited Japan to investigate the prospects for trade, in July 1946, SCAP asked him to finance a shipment of wool to Japan by sending Australia back some of the finished goods in return. This proposal was rejected because this system totally deprived Australia of control over how its

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Sengo Fukkoki(3) [The history of international trade and industry policy, volume 4: First period for postwar restoration no.3], Tsusho Sangyo Chosakai, 1990, p.142.
12 Pickelle to Marquat, 'Importation of Raw Wool', 14 January 1947, SCAP, 6787(7), ESS(A)05903.
13 Radiogram from SCAP to Washington, C-68950, 10 January 1947, SCAP, 6090(3), ESS(D)00806.
facing the forthcoming election in September, to be seen to be lending a hand to its former enemy. After the Labor government was reelected, Australia made an offer for wool sales to show its conciliatory stance towards SCAP's aim to rehabilitate the Japanese economy centred on the textile industry, which would have less potential to stimulate Japan's remilitarisation.\textsuperscript{14}

In December 1946, E.E. Ward, representing W. MacMahon Ball, the British Commonwealth Representative in Tokyo, presented Australia's reply to Peter McDermott, then chief of the Foreign Trade and Commerce Division. Australia rejected the proposed wool processing system as well as the extension of credit on the grounds that it had also refused raw wool sales on a credit basis to France and China. Instead, Ward insisted that Japanese purchases of raw wool from Australia should be made on a cash basis either in dollars or sterling.\textsuperscript{15} In view of the lower priority given to the procurement of raw wool, Australia's proposal for cash payments was quite unacceptable to SCAP. Furthermore, Ward's attitude seems to have offended the SCAP officials. According to the story told by one of the ESS officials to Hugh Wrigley, the Australian Commercial Counsellor in Tokyo in December 1947, in submitting the Australian proposal, Ward demanded dollars for wool and in return McDermott equally definitely demanded dollars for all Australian purchases from Japan.\textsuperscript{16} The rumour about the claims by Ward and McDermott seems to have been without foundation. McDermott did show a strong attachment to dollar earnings through the conversion of SCAP's sterling funds, and by so doing made the sterling area sceptical about SCAP's intention to expand Japan's sterling trade in the forthcoming 1948/49 trade negotiations between SCAP and the sterling area countries, as discussed in the following chapter. Moreover, the US Department of State tried to insert a provision to enable SCAP to convert its sterling funds at any time when dollars were required to repay debts incurred.

\textsuperscript{14} Rix, 1986, pp.58-60.
\textsuperscript{15} Foreign Trade Division, 'Memorandum for Record', 2 January 1947, SCAP, 6090(3), ESS(D)00806. SCAP's official record states that the Exports and Imports Division was reorganised into the 'Foreign Trade and Commerce Division' sometime in late 1946, and does not refer to the naming of the 'Foreign Trade Division', as above. SCAP, History of the Nonmilitary Activities of the Occupation of Japan, vol.2, p.60. The officials used the 'Foreign Trade Division' throughout 1947 until mid 1948. when they began to use both 'Foreign Trade' and 'Foreign Trade and Commerce' mixedly. Again, I will use the 'Foreign Trade and Commerce Division' in my main arguments, while the leaving the title used in the original documents as it is in showing sources in the footnotes.
\textsuperscript{16} Hugh Wrigley, Australian Commercial Counsellor in Tokyo, to J.A. Tonkin, Department of Commerce and Agriculture (DCA), Canberra, 7 December 1947, AA, A606, R40/1/42. 'AA' denotes that the cited documents are located in the Australian Archives Office in Canberra.
within the sterling area, in the Interim Sterling Payments Agreement of November 1947, which is to be discussed later. The provision was proposed in the light of a previous condition that Japan was required to make payment in dollars for the purchases of raw wool from Australia.\(^{17}\)

Thus, in reply to Australia’s cash payment proposal, SCAP adopted a firmer attitude in January 1947. It submitted its wool barter plan: that 30,000 bales of Australian wool be financed by the standing credit from raw silk exports and from the SCAP Trust Fund Account. This time SCAP attached the warning that if the plan was not accepted, Japan’s source of raw wool would be diverted from Australia to the United States causing ‘the loss to Australia of one of her best prewar customers’. At the same time, SCAP claimed the right of the Japanese government to select the type and quality of wool to be purchased from Australia.\(^{18}\) SCAP’s readiness to spend cash from the Trust Fund showed its determination to secure the supply of the types of Australian wool demanded by the Japanese consumers.

In reply, Australia insisted on selecting raw wool for Japan ‘from stocks not in demand by other perspective buyers’.\(^{19}\) The Australian wool industry persisted in the argument that the finer types of wool should only be sold at auction. Since these finer types were sold at higher prices in the Australian auctions reflecting keen competition under the postwar sellers’ market conditions, it was virtually impossible for Japan to procure finer qualities from Australia in the light of the limited funds available to SCAP.\(^{20}\)

The coarse types of wool offered by Australia would never have been suitable for the production of exportable wool fabrics. After all SCAP could only issue an order for 7,350 bales of disposable Australian wool in return for Japan’s standing credit. SCAP did not hide its frustration to Washington:

\(^{17}\) Foreign Trade Division, ‘Memorandum for Record’, 16 January 1948, SCAP, 6092(10), ESS(B)00938.
\(^{18}\) Marquat to W. Macmahon Ball, British Commonwealth Member, Allied Council for Japan, ‘Importation of Wool from Australia’, 17 January 1947, SCAP, 6090(3), ESS(D)00806.
\(^{19}\) Ball to Marquat, ‘Importation of Wool from Australia’, 8 February 1947, ibid.
\(^{20}\) Rix explains that the Australian Prime Minister, Ben Chifley and his cabinet had basically accepted the SCAP proposal. However, the External Affairs Minister, H.V. Evatt, who was in Tokyo at that time, turned down the proposal, giving as his reasons, ‘further piecemeal settlement of Japan issues before a Peace Treaty, strengthening of Japan’s economy without regard to Australia’s security, possible pressure for entry of Japanese nationals to Australia, and public outcry over supply of raw materials to Japan so soon after the end of the war’. Rix, 1986, p.60.
Australia's policy not understood here. Our position is that if purchase is made on sight draft terms, Japan, under control and supervision of SCAP, is entitled to same consideration and privileges accorded other buyers, particularly in view of Japanese prewar wool purchases from Australia.\(^{21}\)

When the 7,481 bales of wool ordered were shipped to Yokkaichi in Mie Prefecture on 8 June 1948, the whole content was made up of extremely coarse types. One Japanese wool manufacturer remembered his impression at the inspection of the content:

> We remember the occasion when the first postwar shipment of 7,400 bales arrived. We felt genuine indignation against the Australian government. Almost all of them were of extremely low quality. No worsted types which we had requested were included. I had a feeling that they pushed on us only the types which almost looked like the rubbish of their wartime stocks.\(^{22}\)

Thus the chance to develop an extensive wool purchase programme between Australia and SCAP was lost. Although SCAP's request might have been extravagant in view of the postwar sellers' market, Australia's flat refusal led SCAP to an alternative means to finance wool procurement, to maintain the productive operation of the Japanese wool manufacturing industry.

**SEARCH FOR A MEANS OF WOOL PROCUREMENT**

Faced with Australia's firm policy to sell wool only at auction, SCAP became attracted to the proposals for processing raw wool received from US firms.\(^{23}\) In April 1947, a number of US firms approached the occupation authority to present offers.\(^{24}\) However, it proved quite difficult to reach any agreement over the provisions of processing contracts. While various methods of payment for processing were raised, SCAP preferred contracts on a credit basis under which private traders would supply raw wool against future deliveries of wool textiles, in order to minimise SCAP's control and supervision of the Japanese

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\(^{21}\) Telecom, 'Wool', 13 March 1947, SCAP, 6787(7), ESS(A)05903.

\(^{22}\) Yuzo Usami, et.al., 'Yomo Kogyo no Fukko wo meguru Omoide' [Memory of the restoration of the wool industry], Nihon Yomo Sangyo Kyogikai [Japan Council of Wool Industries], *Yomo Sangyo Senso 20-nen no Ayumi* [20 years history of the wool industry], 1967, p.43.

\(^{23}\) Pickelle to Marquat, 'Proposed SCAP Wool Import Policy', 28(?) May 1947, SCAP, 6709(38), ESS(C)05439.

\(^{24}\) Foreign Trade Division, 'Memorandum for Record', 12 April 1947, SCAP, 6030(3), ESS(D)00805.
industry. On the other hand, many US firms wanted contracts on commission whereby the firms would pay predetermined spinning fees for processing. They were familiar with this system which had been used in similar types of processing contracts with European manufacturers.

SCAP even started to consider seriously the possibility of accepting dearer US wool to a value of $1,000,000 held by the Commodity Credit Corporation (CCC). Later, however, Tokyo found that the US Department of Agriculture would retain the finer types of wool for the US domestic manufacturers, and the types of wool offered by the CCC were available from other suppliers at lower prices. This plan was deferred pending the development of processing programs.

SCAP’s response to the CCC offer illustrates its stance on wool procurement. The continued or increased operation of the Japanese wool manufacturing industry was desirable because it was consistent with the occupation aim of economic recovery to maintain Japan’s social stability. But SCAP could not afford to spare its limited funds for raw wool because this would affect the import of far more critical foodstuffs and raw materials such as cotton. Hence purchases of raw wool had to be financed by export proceeds. However, Japan needed fine quality wool to manufacture exportable fabrics. This was why SCAP insisted on reserving Japan’s right to select the types of wool to be purchased. The problem was that these types of wool were most desired by other consumer countries which could offer better deals to wool suppliers than Japan. The best way to ensure immediate procurement of raw wool of Japan’s own choice was to make cash payments.

In July 1947, it became evident that existing stocks of greasy wool held by the Japanese mills had been ‘virtually exhausted’. SCAP sent Washington a firm request for wool worth $1,000,000 which was equivalent to 6,000 to 9,000 bales. Payments would be made from the SCAP Trust Fund Account. A month later Tokyo received five bids from US commercial firms, two bids for Australian wool and three for South American.

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25 Radiogram from SCAP to Washington, C-53210, 8 June 1947, SCAP, 6090(4), ESS(D)00808.
26 ‘Teleconference’ [between SCAP officials and Washington officials], 16 August 1947, SCAP, 6709(38), ESS(C)05439.
27 Radiogram from SCAP to Washington, C-54018, 14 July 1947, SCAP, 6090(4), ESS(D)00808.
28 Foreign Trade Division, ‘Memorandum for Record’, 19 August 1947, SCAP, ibid.
29 Radiogram from SCAP to Washington, C-54018, 14 July 1947, ibid.
30 Radiogram from Washington to SCAP, WAR 84873, 24 August 1947, ibid.