Japan not be ‘enticed’ into soft-currency treatment, however much sterling exports might increase. This ‘ideology’ was quite in line with Japan’s initiative to seek American Account status in sterling trade. The attachment to hard currency status meant closer affiliation of Japanese trade with the dollar area. Menzies was aware of the preference for dollar earnings within Japanese domestic policy circles and identified one of the reasons for Japanese opposition to deletion of the dollar convertibility clause.

Mr. Menzies then observed that in his various talks with both Americans and Japanese industrialists, it was obvious that their ideas on the payments negotiations still seemed to be based on certain misconceptions. Their argument had been that it was useless for Japan to accumulate sterling if she was unable to buy sterling goods in return; the retention of the convertibility clause was accordingly desirable in order to ensure a flow of dollars into Japan for the purchase of necessary raw materials. Mr. Roberts (British Minister, Commercial) confirmed that this view was also held by Japanese industrialists in the Kansai [Osaka area] who thought that a retention of the dollar clause would enable them to utilise sterling balances to buy American cotton for dollars.

As mentioned previously, SCAP had one time adopted a more liberal approach to the question of dollar convertibility of Japan’s sterling funds, as it shifted from dollar earnings to finance Japan’s standing liabilities to expansion of trade networks with non-dollar areas as a central strategies for achieving self-reliance of the Japanese economy without US appropriated funds. On the other hand, the Japanese still held a strong sense of dependency on the United States, especially for imports of strategic raw materials and foodstuffs, and therefore saw a pressing need to earn dollars by any means. From the viewpoint of the Japanese foreign exchange control authority as well, it was also sound to prevent excessive accumulation of unusable soft currencies. These factors culminated in the Japanese government’s attachment to the dollar convertibility clause and the proposal for American Account status. In this sense, there is no denying that the sterling area was given lower priority than the dollar area as a post-independence trade partner for Japan.

Nevertheless, the political necessity to settle the sterling payments negotiations prior to the San Francisco Peace Conference forced the Japanese to accept most of the British proposals, including the deletion of the dollar convertibility clause, an ambiguous assurance

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87 Kiuchi, 15 August 1954, p.4.
against excessive sterling accumulation and Hong Kong’s inclusion in the Payments Agreement. Their acceptance, no matter how reluctantly, carried with it the implication that Japan’s economic self-reliance would inevitably be subject to the influence of the development of sterling trade, as the new Agreement would direct a large portion of Japanese exports to sterling markets. If Japan could have abandoned the sterling payments negotiations and obtained American Account status, the shape of post-Peace Treaty Japanese trade relations would have been quite different. Japan might have been more closely connected with the dollar area, but at the cost of a substantial reduction in the overall level of trade, a decrease in production levels, and possibly, a delay in achieving economic self-reliance.

In this respect, the Sterling Payments Agreement of 1951 was an important turning point in Japan’s postwar trade relations. Without an additional dollar supply, Japan had no alternative but to pursue economic self-reliance through a strategy of promoting trade on a commercial basis in multilateral directions without excessive dependence on the dollar area. The new Payments Agreement forced Japan to focus on developing commercial networks with the sterling area, by drastically moderating Japan’s exchange controls on sterling trade. This could be expected to stimulate active purchases of Japanese goods by the sterling area. The Japanese government was then faced with an important question: how far should it allow sterling surpluses to accumulate. So the next chapter will examine the handling by the Japanese government of the excessive accumulation of sterling surpluses after the 1951 Sterling Payments Agreement. The answer would be significant in determining the Japanese commitment to trade on a more multilateral basis.
8 The Japanese Handling of the Sterling Surplus, 1951–52

The new Sterling Payments Agreement minimised Japanese exchange controls on trade with the sterling area countries by the removal of the dollar convertibility clause. The Japanese government was seriously concerned about the effects of eliminating the clause, as described in the previous chapter, and in fact, Japan accumulated a huge sterling surplus from the second half of 1951 to 1952. Conversely, from 1953 to 1954 Japan faced a serious shortage of sterling, as sterling area countries tightened import licensing in order to safeguard their balance of payments. Thus, Japanese trade during the first half of the 1950s was severely affected by the volatility of Japan’s sterling balances.

These developments had profound implications for postwar Japanese trade strategy. The new Sterling Payments Agreement provided Japan with an opportunity to develop its trade in the post Peace Settlement period on a more multilateral basis. Japan’s balance of payments had been dependent on the extra dollar supply from US appropriated funds and, subsequently, special procurement during the Korean War. Although the Korean War Boom boosted Japan’s supply of dollars, it was obvious that this situation could not last for long. It was apparent that Japan needed to divert its trade from the dollar area into more multilateral channels centred on the sterling area, if it was to trade without extra dollars in circumstances of a worldwide dollar shortage.

The Sterling Payments Agreement allowed multilateral settlement of trade between Japan and the whole sterling area through the removal of the dollar convertibility clause. Freed from the risk of a dollar drain, the sterling area countries were able to import Japanese goods extensively. Japan in turn could utilise resultant sterling surpluses to increase its purchases of foodstuffs and raw materials from the sterling area. The problem was that a large portion of Japan’s exports to the sterling area, principally cotton textiles, were produced from raw materials purchased in dollars. Japan would incur the risk of a dollar loss unless it was able to curtail its dollar expenditure by purchasing a large volume of
commodities from the sterling area. But the capacity of the whole sterling area to supply commodities remained very limited.

This situation posed a dilemma for Japanese policy makers. If Japan continued to accumulate a sterling surplus without being able to obtain raw materials and foodstuffs from the sterling area, its foreign currency position would be seriously distorted. On the other hand, if Japan was to seek a rigid balance in sterling trade in order to safeguard its dollar balance, it would be forced to restrain exports to the sterling area. This might lower Japan's overall export and production levels, since the sterling area was rapidly regaining its prewar status as an important export market for Japanese goods. Restricting trade in this way was contrary to the principle of freer trade under the Bretton-Woods system, in which Japan was seeking to participate. The Sterling Payments Agreement forced Japan to choose one of two options: expansion of non-dollar trade to sustain its economic activities, or tight exchange control to maintain a sound foreign currency position. Which it chose was critical to Japan's future trade strategy.

This chapter looks at the implications of the new Sterling Payments Agreement for Japan's trade strategy after the signing of the Peace Treaty in September 1951, highlighting the Japanese handling of the sterling surplus in 1951–52. Over this problem there developed intra-governmental policy debate between those who advocated trade expansion and those who favoured currency restraint. The process whereby the former school claimed victory illustrates Japan's increasing commitment to a strategy of promoting trade through non-dollar channels. In this strategy, Australia came to be recognised as a major alternative supplier of raw materials and foodstuffs.

**THE IMPLICATIONS OF THE 1951 STERLING PAYMENTS AGREEMENT**

As mentioned in Chapter 7, the Japanese government rushed to conclude the new Sterling Payments Agreement on 31 August 1951 for reasons of political expediency. The Agreement was settled just prior to the departure of the Japanese delegates for the San Francisco Peace Conference. Although policy makers were concerned about the possible excessive accumulation of sterling surpluses, they seem to have conceded to the removal of the dollar convertibility clause without fully comprehending the implications for Japanese
trade in the post occupation period. Nobutane Kiuchi, then Chairman of the FECB, who vehemently criticised the new Payments Agreement, said:

... in short, it [the new Sterling Payments Agreement] meant that Japan yielded to the enticement of soft-currency status. In the negotiations, the British representative, although in a most friendly manner, stated, 'if the dollar clause is removed, Britain will treat Japan as a soft-currency source, and since soft-currency treatment means relaxation of import licensing, Japanese exports will increase'. This statement attracted some of our delegates more than anything else. To confess honestly, since I myself did not know that high prices in the sterling area were as remarkable as to be revealed later on, I could not understand the real meaning of this enticement of soft-currency.¹

This suggests that the Japanese government did not grasp the full implications of the elimination of the dollar convertibility clause on Japan's overall trade relations. It merely expected an increase in exports to the sterling area through soft-currency treatment.

At the end of 1951, when the Japanese began to realise how serious the problem of sterling accumulation was, Bunrokō Yoshino, an official of the Fourth Division of the MFA's Economic Affairs Bureau directing trade with the sterling area, succinctly outlined the significance of the 1951 Agreement for Japan's overall trade in an article in the *Monthly of Cotton Yarn and Textile Exports*.² Yoshino's article observed that prewar Japanese trade deficits with the dollar area had been offset by surpluses with the sterling area. Since the 1951 Sterling Payments Agreement completely suspended convertibility of sterling into dollars, Japan would incur large dollar liabilities because exports to the sterling area were produced from raw materials purchased from the dollar area. If this situation continued, and special procurements decreased too, the Japanese economy would be in serious trouble unless sterling surpluses were exchanged for strategic raw materials which could then be used to produce export goods for the dollar area. Yoshino was realistic enough to admit that the possibility of increasing dollar earnings was extremely low. The prospects for substantially expanding purchases from the sterling area were also bleak, except in the case

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¹ Nobutane Kiuchi, ‘Sogo Keizai Seisaku to Kawase Boeki Kanri Seisaku (2)’ [Overall economic policy and foreign exchange trade control policy], *Gaikoku Kawase*, no.54, 1 August 1952, p.4.

² Bunrokō Yoshino, ‘Sutaringu Boeki no Shin Dankai’ [The new stage of sterling trade], *Yushutsu Menshifu Geppo*, vol.1, no.8, December 1951, pp.1-7. As Chief of the Fourth Division Yoshino was later to be responsible for drafting the 1957 Commerce Agreement with Australia.
of raw wool, rubber and bauxite. Moreover, the United Kingdom was reluctant to grant Japanese imports the benefit of soft-currency treatment or to purchase non-essential items.

Yoshino’s pragmatism led him to argue that the Japanese government should enter into extensive negotiations with the independent British Commonwealth countries, including Australia, India, New Zealand, Ceylon, Burma and Pakistan. These trade negotiations would aim at obtaining soft-currency status, which India had already conceded to Japan in October 1951. They would also focus on working out investment and development programs for Indian iron ore and coal, and long-term supply contracts for Australian wheat, barley and sugar. Yoshino’s proposal was to be reflected in actual government policy, as discussed later. Yoshino concluded his article with an assessment of implications of the 1951 Sterling Payments Agreement for Japanese trade.

Our country crossed the ‘Rubicon’ in the evolution of the postwar trade policy, when we agreed to shelving the dollar clause in the new Payments Agreement. In short, before then, we had requested every country in the world to make settlement of trade, at least formally, through payment of dollar-linked currencies. Therefore, this fundamental principle was abolished in trade with the sterling area. The effect, in either a good or a bad sense, has already been exemplified in transactions with the sterling area...

However, as far as sterling trade is concerned, the die is already cast, and so the sole problem is how far we can proceed with the established policies. In short, established policies are to expand exports to the sterling area as much as possible to the extent that they will not hamper dollar earnings; to secure imports of raw materials by utilising thus obtained sterling funds in a most efficient way; and to prevent dollar loss by saving dollar imports. We must admit that these policies still fail to address the issue of how to implement an export drive for active dollar earning. But no doubt, these are the most effective ways for Japan at present to improve, even partially, our chronic dollar drain ...³

Yoshino’s conclusion indicates that there was little alternative for Japan but to promote trade with the sterling area as a key to dollar saving, having accepted the removal of the dollar convertibility clause.

There was another force inside the Japanese government which did not support an expansion of sterling trade. When the tight import restrictions by the United Kingdom and other sterling area countries started to affect Japan’s sterling balances in mid 1952, Kiuchi defended Britain’s intensification of import licensing:

³ Ibid.
There will be many people who will answer that increased trade was better, when asked which is better for Japan, the past increase or the present reduction. But this is wrong. If the increase in trade is a normal one, the answer may be yes. But the problem is that the past increase in trade was based on subsidised exports sustained by unrealistic exchange rates [between yen and pound sterling]. This will entice business circles to easier trade with the sterling area, discourage their determination for rationalisation, decrease dollar exports, increase inflationary pressure and eventually make it impossible to maintain the 360 yen rate. If that is so, we should feel happy about the fact that the subsidised exports have now ceased. Another point which should be noted is that the excessive sterling accumulation would not have emerged if we had retained the dollar clause.

Kiuchi’s position represents that of the controllers of foreign exchange funds. The Japanese acceptance of the new Sterling Payments Agreement was the first setback for the foreign exchange controllers. They made several attempts to bring Japanese policy back into line by stressing the significance of maintaining a sound foreign currency position even at the cost of expansion of sterling trade. Japan’s huge accumulation of sterling surplus from late 1951 to early 1952 prompted another battle between the trade promoters and the exchange controllers within the Japanese government over the measures to be adopted to cope with growing sterling reserves.

MITI AND MFA URGE AN EXPANSION OF STERLING TRADE

After conclusion of the 1951 Sterling Payments Agreement, a strong force emerged within the Japanese government to pursue active expansion of sterling trade. In mid September 1951, Nobuhiko Ushiba, then Director of MITI’s International Trade Bureau, approached N.S. Roberts, the UKLM Commercial Minister. Ushiba revealed the Japanese decision to relax import licensing on sterling commodities ‘in accordance with the basic principles embodied in the new Payments Agreement’, submitting that Japanese purchases from the sterling area in the September–December quarter in 1951 were estimated to increase by about three times over the same quarter in the previous year. In talks with Roberts in late September, Ushiba outlined MITI’s intention to balance Japan’s trade with the whole

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4 Nobutane Kiuchi, ‘Sogo Keizai Seisaku to Kawase Bocki Kanri Seisaku (1)’, Gaikoku Kawase, no.53, 15 July 1952, p.3.

5 Nobuhiko Ushiba, Director, International Trade Bureau, MITI, to Roberts, 13 September 1951, AA, CP553/1, 194/B/10/103. Ushiba was originally affiliated with the Ministry of Foreign Affairs. It was common for the MFA officials to have responsibility for international trade in MITI soon after its establishment in 1949.

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sterling area at around £310 million for the period from July 1951 to June 1952. While this figure was larger than that of the previous year by £100 million, Ushiba was confident of Japan's capability to supply such a large volume of exports.  

Ushiba's attitude did not reflect the concern about excessive accumulation of sterling surpluses that had been repeatedly expressed by Japanese financial officials during the payments negotiations. All he proposed was to authorise the trade target through an exchange of letters and to review the figures in six months. The MITI estimates of Japanese imports from the sterling area in 1951/52 clearly indicated increasing Japanese interest in diverting purchases of foodstuffs and raw materials away from dollar sources. Takio Oda, Director General of International Trade, MITI, revealed that his Ministry's policy was to maintain sterling trade 'on as high a level as possible'. It thus seemed that Japan was prepared to tackle the problem of sterling accumulation through corresponding increases in sterling commodity procurement rather than through foreign exchange controls. The Australian Commercial Counsellor in Tokyo, H.C. Menzies, was impressed with Ushiba's approach and wrote back to Canberra, the 'Japanese apparently are going ahead with the implementation of the [new Payments] Arrangement and considerable freeing of trade between the Sterling Area and Japan'.  

This did not stop Japanese financial officials from attempting to forestall excessive sterling accumulation. The FECB and the Ministry of Finance (MOF) took the position that Japan's exports to the sterling area should be drastically curtailed until the surplus sterling balance was reduced. They pointed out that a large portion of sterling exports were produced from raw materials from the dollar area, thus causing a dollar drain. They were also reluctant to increase procurement from the sterling area because dearer prices for sterling commodities could increase inflationary pressure in Japan, thus weakening the competitiveness of Japanese industrial goods and counteracting the effects of rationalisation programs. From this viewpoint, the most effective measure to check sterling

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6 Sterling Area Working Party, 'Minutes of the Seventy-Seventh Meeting', 26 September 1951, AA, CP553/1, 194/B/10/50/6.
7 Telegram from UKLM to FO, no.1342, 25 September 1951, AA, A1838, 479/2/10 Part 2.
8 C.C. Campbell, Director of Trade and Services, 'JG Policy re Exports to Sterling Area', 19 February 1952, SCAP, 6417(22), ESS(E)00968.
9 Menzies to DCA, 21 September 1951, AA, CP553/1, 194/B/10/103.
10 Campbell to Adjutant General, 'Export of Japanese Steel to the United Kingdom', 7 March 1952, SCAP, 6417(22), ESS(E)00968.
accumulation would be the reintroduction of dollar convertibility through cancellation of the Sterling Payments Agreement.

The United Kingdom was able to capitalise on the eagerness of the FECB and MOF officials to take drastic action to restrain excessive accumulation of sterling reserves. London said that it was not prepared to give Japan soft currency treatment in its foreign exchange controls, because Japanese financial officials might request restoration of the dollar convertibility clause if active purchasing by the sterling area led to excessive sterling accumulation in Japan.\textsuperscript{11} Nor did Britain intend to relax import restrictions on non-essential Japanese goods for the same reason.\textsuperscript{12} When the FECB Chairman Kiuchi visited London in October, the British Treasury proposed an exchange of letters to the effect that both sides were to confine imports from the other party to essential goods, with the importing party to decide which items were essential.\textsuperscript{13}

In October, Kiuchi signed a letter to the Treasury in which he accepted the British proposal.\textsuperscript{14} There is no document which throws light on Kiuchi's motives. But, judging from his known resistance to the removal of the dollar convertibility clause and his approach to foreign exchange control, it is easy to imagine that his main concern was to prevent excessive accumulation of sterling surpluses. If the sterling area countries were prepared to extend their purchases even to non-essential items, the possibility of sterling accumulation would rise. If accumulation occurred, Japan might be pressed to increase procurement from the sterling area to offset the trade imbalance, regardless of prices or the essentiality of commodities. If Japan confined its purchases to essential items, the only alternative would be for it to curtail exports to the sterling area or for the sterling area to tighten import licensing. No wonder, then, that Kiuchi preferred reduced and balanced trade to achieve sound exchange controls over a 'subsidised' expansion of exports fuelled by inflation within the sterling area and the removal of the dollar convertibility clause.

\textsuperscript{11} Twenty-third meeting of the Commonwealth Liaison Committee, London, 'Minutes of Meeting Held on 5th September 1951', AA, A606, R40/1/111.
\textsuperscript{12} Cable from Crosec to Canberra, no.194, 29 September 1951, CP553/1, 194/B/10/103.
\textsuperscript{13} Modified draft letter to Kiuchi from Bank of England, 'Our Talks in London between 12--22 October regarding Draft Memorandum, UKLM (Dated 2 October) and Kiuchi (Dated 4 October)', 19 November 1951, DAO, B'0.0.2.0.
\textsuperscript{14} Cable from Crosec to Canberra, no.215, 21 November 1951, AA, CP553/1, 194/B/10/103.
When Tokyo was informed of Kiuchi’s letter at the end of October, the Japanese government was determined to modify its content. Led by the Ministry of Foreign Affairs (MFA) and MITI, the Japanese government sought to clarify its position, stating that its main concern was acquisition of soft-currency treatment in import licensing from the British foreign exchange control authority, and not the prevention of excessive sterling accumulation. In a memorandum to Roberts blaming Britain for restrictions on non-essential Japanese goods, Ushiba asserted that it was difficult to understand why Japan could not be treated as a soft-currency source despite shelving the dollar convertibility clause. Ushiba further complained about the low availability of essential commodities such as wheat, barley, rice, oil and sugar from the sterling area.  

The ever-increasing sterling surplus did not deter the Japanese officials. In mid November, Kiuchi in London conveyed to the British his concern that Japan’s sterling surplus had already reached £40 million and that it might reach £70 million by the end of the year. Despite this, a MFA official told the UKLM that excessive accumulation could be tolerated if the surplus was created by sales of merchandise made from raw materials imported from non-dollar sources. He urged an increase in non-essential imports, explaining the Japanese intra-governmental conflict of views as follows.

As you know, there is a faction which argues that sterling should be convertible and another faction which does not care. The new Payments Agreement was duly concluded because the latter faction claimed victory. But as we are not given soft-currency treatment as expected and the trend for sterling accumulation is being intensified, this faction nowadays faces considerable difficulties. If you wish to advance the prestige of the new Payments Agreement, I want you to give due consideration to this point ...  

In fact, late November marked an important turning point in the Japanese approach to sterling trade, triggered by an intra-government debate over Kiuchi’s letter. In an inter-Ministerial meeting of the officials of the MFA, MOF, MITI, the FECB and the ESB, Ushiba proposed that Kiuchi’s letter be endorsed by the Japanese government, with the

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15 Ushiba to Roberts, 21 November 1951, DAO, B’0.0.2.0.
16 Cable from the Australian High Commissioner’s Office in London to Canberra, no.6063, 15 November 1951, AA, CP553/1, 194/B/10/103.
17 Kokusai Keizaikyoku Dai 4 Kacho [Chief, Fourth Division, International Trade Bureau, MFA], ‘Tomasu-shi tono Kondan no Ken’ [On the meeting with Mr Thomas], 1 November 1951, DAO, B’0.0.2.0.
exception of the paragraph on confining purchases to essential items. The Director of MOF’s Financial Bureau complained that Kiuchi’s letter included a paragraph stating that Anglo-Japanese consultations should be held to discuss appropriate measures to be adopted if it seemed likely that the Japanese surplus would exceed £30 million at the end of Japan’s purchasing season. As this figure had already been surpassed, the paragraph might give the sterling area countries the impression that the Japanese government was not concerned about sterling accumulation. Eventually MOF agreed to Ushiba’s proposal on condition that Britain be informed of Japan’s intention to ask for consultations in due course to discuss measures to prevent sterling accumulation.\(^{18}\)

This was a victory for MITI and the MFA which had advocated expansion of sterling trade and soft-currency treatment for Japan over Kiuchi, the FECB and MOF, which had been eager to impose restraints on sterling accumulation. The paragraph on the essentiality of imports was dropped. While MOF wished to include some paragraphs clarifying procedures to check further accumulation, no major modification was to be made. It is interesting that the FECB officials at the meeting stood with Ushiba in supporting endorsement of Kiuchi’s letter with only minor modifications on essentiality. In view of the role of the FECB as Japan’s foreign exchange control authority, they might well have sided with MOF and called for major modifications. It is suspected that FECB officials considered the matter to be one of bureaucratic prestige for the Board. They may have wished to avoid modifications which would have contradicted the content of a letter written by their own Chairman.

Kiuchi himself may have regretted the contents of his letter. Still in London, he asked to withdraw his letter in December, but his request was refused by the British Treasury.\(^{19}\) After his return to Tokyo, Kiuchi declined to comment on the matter to UKLM officials, saying that he had not been informed of the endorsement of his letter with minor modifications.\(^{20}\)

\(^{18}\) Kei 4 [Fourth Division, International Trade Bureau], ‘Kiuchi-shi Retta ni kansuru 11-gatsu 22-nichi Kaigi Gijiroku’ [Minutes of the meeting on Mr Kiuchi’s letter on 22 November], 22 November 1951, DAO, B’0.0.2.0.
\(^{19}\) Commonwealth Liaison Committee, ‘Minutes of the Twenty-Ninth Meeting’, 12 December 1951, AA, CP553/1, 194/B/10/103.
The handling of Kiuchi’s letter gave MITI and the MFA the opportunity to push their case strongly for an expansion of sterling trade and soft-currency treatment for Japan. It allowed them to grasp the initiative on Japan’s sterling policy from the FECB and MOF, which were more inclined to impose restraints on excessive accumulation of sterling surplus. In fact, Menzies observed that domestic opinion had turned favourably towards promotion of sterling trade, because of the constant pressure on MITI for an increase in sterling procurement to offset the accumulated surplus. He also acknowledged the role of Sir Esler Dening, who was to be appointed the first postwar British Ambassador to Japan in May 1952, in guiding Japanese public opinion in this direction, especially in the Osaka region.21 Menzies’ observation was not without foundation, because the textile industry — the frontrunner in Japan’s export drive to the sterling area — was concentrated in the Osaka region. In a panel discussion for the journal Keizai Rengo on the shape of Japan’s trade relations after the Peace Settlement, Takeshi Sakurada, President of the Nisshin Spinning Company and later President of the Japan Chamber of Commerce and Industry, pointed out that Tokyo business circles had not understood the significance of sterling trade, which he considered would contribute towards Japan’s economic self-reliance and reduce dependence on extra dollar supply through special procurement.22 In fact, cotton exporters presented a petition to the government as early as November, opposing the introduction of export controls to restrain sterling accumulation.23

THE REJECTION OF THE FECB PROPOSAL FOR EXPORT FINANCE RESTRAINT MEASURES

Japan’s exports to the sterling area continued to increase from late 1951 to early 1952. Table 8.1 clearly indicates the effect of the new Sterling Payments Agreement in unleashing import demand for Japanese goods among the sterling area countries; Japan’s sterling remained at quite a high level from September 1951 to April 1952.

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23 Kyushichi Toyoshima, President, Nihon Menshifu Yushutsu Kyokai [Japan Cotton Yarn and Textile Exporters’ Association] to MOF, the ESB, MITI and the FECB, ‘Pondo Chiikiimu ke Yushutsu Seigenan ni taisuru Hantai Chinjo no Ken’ [Petition opposing proposed export restrictions against the sterling area], Yushutsu Menshifu Geppo, vol.1, no.8, December 1951, p.29.
Table 8.1  Japan’s Export-Import Trade with the Sterling Area: January–March 1951 to April–June 1952 ($ million)

<table>
<thead>
<tr>
<th></th>
<th>Exports to Sterling Area</th>
<th>Imports from Sterling Area</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>1951</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Jan-Mar</td>
<td>96</td>
<td>139</td>
<td>-43</td>
</tr>
<tr>
<td>Apr-Jun</td>
<td>154</td>
<td>160</td>
<td>-6</td>
</tr>
<tr>
<td>Jul-Sep</td>
<td>144</td>
<td>130</td>
<td>14</td>
</tr>
<tr>
<td>Oct-Dec</td>
<td>192</td>
<td>85</td>
<td>107</td>
</tr>
<tr>
<td>1952</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Jan-Mar</td>
<td>182</td>
<td>130</td>
<td>52</td>
</tr>
<tr>
<td>Apr-Jun</td>
<td>158</td>
<td>121</td>
<td>37</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>926</strong></td>
<td><strong>765</strong></td>
<td><strong>161</strong></td>
</tr>
</tbody>
</table>


Australia contributed substantially to the increase in Japan’s sterling exports to become Japan’s fourth largest export market in 1951, after the United States, Indonesia and Pakistan. Japan’s main export item to Australia in this year was not the traditional cotton piece goods but steel. Australia’s housing boom had caused a quadrupling in purchases of Japanese steel over the previous year, making Australia Japan’s largest steel customer in terms of sales value during this year.  

Japan’s purchases from the sterling area did not catch up with exports, because of limited supplies and higher prices in sterling countries. Moreover, the administrative transfer of sterling balances for settlement in sterling of Japan’s imports from non-dollar, non-sterling area countries, as approved in the new Payments Agreement, did not utilise as much of Japan’s sterling surplus as expected. On the contrary, it was suspected that non-dollar non-sterling countries in Southeast Asia like Thailand and Indonesia purchased

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24 The Japanese steel industry appreciated the significance of Australian market in 1951 in a reserved manner. The steel mills were more impressed with the sudden rise of their exports to Argentina which also more than quadrupled from the previous year and recorded the largest quantity in 1951. Nihon Tekko Renmei [Japan Steel League], Sengo Tekkoshi [The postwar history of steel], 1959, pp.631-633. Argentina was to grow to be Japan’s most important steel market during the 1950s and emerged as Australia’s rival in wool sales to Japan, using the value of its steel market as bargaining leverage, in 1953–54 when Japan’s balance of payments position deteriorated, as discussed in Chapter 9.
Japanese goods via Hong Kong, paying with their abundant sterling funds, while exporting their commodities to Japan for dollars.\textsuperscript{25} Table 8.2 indicates that Japan’s sterling balance tripled from £41 million at the end of September 1951 to £127 million at the end of June 1952. In early 1952, a policy debate emerged within the Japanese government over measures to tackle the rapid accumulation of sterling surpluses.

**Table 8.2  Japan’s Foreign Currency Balances, June 1950–June 1952**

<table>
<thead>
<tr>
<th>Year/Months</th>
<th>Dollar Account ($ million)</th>
<th>Pound Account (£ million)</th>
<th>Open Account ($ million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1950</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>June</td>
<td></td>
<td>17</td>
<td>–28</td>
</tr>
<tr>
<td>September</td>
<td>353</td>
<td>21</td>
<td>–10</td>
</tr>
<tr>
<td>December</td>
<td>462</td>
<td>19</td>
<td>27</td>
</tr>
<tr>
<td>1951</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>March</td>
<td>401</td>
<td>15</td>
<td>43</td>
</tr>
<tr>
<td>June</td>
<td>322</td>
<td>44</td>
<td>37</td>
</tr>
<tr>
<td>September</td>
<td>484</td>
<td>41</td>
<td>73</td>
</tr>
<tr>
<td>December</td>
<td>583</td>
<td>75</td>
<td>120</td>
</tr>
<tr>
<td>1952</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>March</td>
<td>643</td>
<td>97</td>
<td>137</td>
</tr>
<tr>
<td>June</td>
<td>678</td>
<td>127</td>
<td>135</td>
</tr>
</tbody>
</table>

*Note:* Each figure indicates balance at the end of the corresponding month.


The FECB opened the debate with Kiuchi proposing drastic measures to cope with the sterling accumulation. The Chairman of the FECB called for the diversion of Japanese exports from the sterling area to the dollar area, including particularly those items which were produced from raw materials obtained from the dollar area, such as steel. It was reported that Kiuchi suggested that Japan be treated as an American Account country, that is, within the dollar area, and that it restore the dollar convertibility clause in the Sterling Payments Agreement in the forthcoming Anglo-Japanese Trade Review Conference, as one

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measure to implement this policy. Despite past setbacks, the FECB had not given up its aspiration for drastic measures to overcome the sterling accumulation, even at the risk of Japan’s losing a considerable portion of its exports to the sterling area.

The FECB did not waste time in implementing restraint measures. On 16 February, it announced the introduction of emergency measures to tighten export finance for sterling. Kiuchi admitted that these measures would not solve the fundamental problem of Japan’s sterling accumulation, saying that they were introduced ‘only as a part of the process’ towards revision of the Sterling Payments Agreement. He suggested to introduce a realistic exchange rate of around 850 to 900 yen to one pound sterling, instead of the existing 1008 yen. If fully implemented, the FECB’s proposal would severely restrain Japanese exports to the sterling area.

Japanese business was opposed to the measures, pointing out that the sterling area was a good customer, particularly for the cotton textile industry. MITI officials shared this anxiety about a possible reduction in Japan’s sterling trade, while conceding the need to rectify the problem of excessive sterling accumulation. Hence, the Ministry issued a counter-proposal for quantitative export adjustment measures for steel and textiles soon after the implementation of the FECB’s new financial restraints, which had already led to

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27 ‘Pondo Taisaku wo Sekkyokukai’ [Towards active measures against the sterling accumulation], Nihon Keizai Shimbun, 17 February 1952. The FECB’s emergency measures included the lowering of the yen-denominated sterling forward market exchange rate and the shortening of the ‘export booking period’ during which the Japanese government guaranteed Japanese exporters to compensate for any loss resulting from possible devaluation of the pound sterling before they received export proceeds. In particular, the new regulations provided that the ‘export booking’ could only be made after the arrival of export letters of credit instead of after the conclusion of export contracts. Thus Japanese exporters had to take considerable risks, knowing that the pound might be devalued, as had been persistently rumoured.
28 ‘Pondo Mondai no Bapponsaku’ [Drastic measures for the sterling problem], Nihon Keizai Shimbun, 22 February 1952.
30 The statement of Tatichiro Matsuo, Deputy Director, International Trade Bureau, MITI, 26 February 1952, in the panel discussion for a journal of the Tokyo Chamber of Commerce and Industry. ‘Pondo Taisaku wo megutto’ [On the measures against the sterling accumulation], Tosho, no.59, March 1952, p.9.
virtual suspension of new export contracts for the sterling area. While the FECB doubted the efficacy of the MITI proposal, Hayato Ikeda, Minister for Finance and a close aide to Prime Minister Yoshida, adopted the MITI line. Ikeda accepted the principle that it was unfavourable to try to overcome the sterling accumulation through drastic financial restraints, which might have an adverse effect on Japanese exports. Although he had been considering other financial measures, he found them no longer necessary now that MITI had initiated its own export adjustment program.

Ikeda’s intervention turned the tide. On 26 February, officials of MITI, MOF, the FECB and the Bank of Japan agreed to a considerable relaxation of the financial export restraints of 16 February and to the adoption of the MITI proposal for quantitative export adjustments for steel and textiles. Under these measures, the government would issue approval for exports of these items up to a ceiling, set according to the export levels of the previous year. With regard to exports to entrepot markets such as Hong Kong and Singapore, the ceiling would be based on 1950 rather than 1951 levels, as the latter were regarded as being abnormally high.

This was a serious blow to the FECB, and especially to its Chairman, who seems to have been shocked. Kiuchi later wrote that February 1952 marked an important turning point for Japan’s postwar trade policy, with public opinion driving the Yoshida cabinet to deny the Board’s sound logic that the national currency should be kept ‘as hard as possible’. Kiuchi’s indignation was such that he denounced the government decision as an outcome of the policy to ‘consider it wise not to uphold any principle and pursue tiny marginal profits arbitrarily’. The FECB policy to enforce tight exchange controls had been rejected in favour of an expansion of overall trade volumes, as proposed by MITI. This

31 ‘Tetsu nado Yushutsu Chosei’ [Export restraint on steel], Nihon Keizai Shimbun, 21 February 1952.
32 ‘Pondo Taisaku Tsusansho-An ni Kirika: Zosho, Gensokuteki ni Ryokai’ [Finance Minister accepts the MITI proposal against the sterling accumulation], Nihon Keizai Shimbun, 26 February 1952.
33 ‘Shikinmen no Kisei Kanwa’ [Relaxation of financial restraints], Nihon Keizai Shimbun, 27 February 1952. Under relaxation, the ‘export booking period’ was extended from the original FECB plan and Japanese exporters could make ‘export booking’ at the time of conclusion of export contracts. Thus they did not have to wait for arrival of export letter of credits.
34 Gaimu Daijin [Minister for Foreign Affairs], ‘Pondo Chikimuke Yushutsu Chosei ni kansuru Ken’ [On the export adjustments for the sterling area], no.Kei-4-Go 170, 12 March 1952, DAO, B’0.0.2.1.
35 Nobutane Kiuchi, ‘Boeki Seisaku no Kaiko to Hansei (Sono 1)’ [Retrospect and review of trade policy, part 1], Gaikoku Kawase, no.100, 1 August 1954, p.5.
36 Kiuchi, ‘Boeki Seisaku no Kaiko to Hansei (Sono 2)’, Gaikoku Kawase, no.101, 15 August 1954, p.4.
ensured that Japan’s trade policy in the post Peace Settlement period would focus on expansion of trade volumes with non-dollar areas, especially the sterling area, rather than on a strict balancing of trade with each currency area.

EXTERNAL OPPOSITION TO RESTRICTIVE MEASURES ON STERLING EXPORTS

The setback for the FECB did not mean that Japanese officials advocated expansion of sterling trade unconditionally or that they accepted Japan’s sterling accumulation. Rather, they emphasised increasing the supply of strategic raw materials and foodstuffs from the sterling area in order to make the most efficient use of Japan’s abundant sterling surplus. A good example was the treatment of Japanese steel exports to the United Kingdom in early 1952.

In early February, Japanese steel mills entered into a contract with a visiting British steel purchasing mission to export 110,000 tons of steel at £490 million. The Japanese government did not approve this export contract on the grounds that London had declined in return to offer Japan 70,000 tons of wheat and 20,000 tons of sugar which Britain had planned to purchase from Australia. Tokyo insisted that London’s refusal revealed its unwillingness to supply Japan with essential goods and help it lessen its accumulated sterling surplus. This indicates Japan’s preparedness to tolerate a high level of sterling surplus as long as it could be used to purchase essential commodities from the sterling area. The British delegates in Tokyo objected to Japan’s refusal to ratify the steel export contract on the grounds that the proposed barter deal of Japanese steel for Australian wheat and sugar contradicted the spirit of less restrictive trade, as embodied in the Sterling Payments Agreement. If Britain accepted the proposed barter deal, delegates claimed that she might be forced to purchase these foodstuffs from somewhere else, making dollar payments.

Unexpected pressure from Washington broke the impasse. SCAP had consistently adopted a ‘hands off’ policy on Japan’s sterling trade problems since the negotiation of the

38 Gaimusho, ‘DS tono Teirei Kaiken’ [Regular meeting with DS (Diplomatic Section, SCAP)], 9 February 1952, DAO, E’0.0.0.5.
1951 Sterling Payments Agreement. Washington maintained this approach in mid February, even though the US administration did consider it desirable for Japan to reach some agreement with the sterling area to overcome the excessive sterling accumulation without introducing restrictive measures.\textsuperscript{40} On receiving the news of the Japanese government's refusal to ratify the steel export contract to Britain, however, Washington sent a strong message to SCAP.

Washington instructed SCAP to inform the Japanese government that Britain was making an effort to rearm in the interest of the free world and that its defence program would be seriously hampered if Japanese steel was unavailable.\textsuperscript{41} Washington's aim was to promote Japan's sterling trade, thus encouraging Japan to utilise its sterling surplus to maximise procurement of commodities that would contribute to its economic development, to save dollars, and also to develop sources of raw materials in Southeast Asia either through import trade or overseas investment.\textsuperscript{42} This was similar to the idea behind the US-Japan Economic Cooperation Program in that Washington tried to link Japan's production capacity with development in Southeast Asia. What was different, however, was that the US administration was not prepared to provide any financial aid.\textsuperscript{43} Japan was asked not to impose restrictions on trade with the sterling area. Marquat conveyed Washington's position to the MFA, although reluctantly, perhaps due to his sympathy with Japan's difficulty in handling the sterling accumulation.\textsuperscript{44} SCAP's intervention compelled the Japanese government to approve steel exports to Britain on condition that a portion of the consignment be deferred until the latter part of the year.\textsuperscript{45}

Apart from US pressure, there was another reason for Japan's adopting a less restrictive approach to sterling trade. In discussions over the desirability of renewing the Sterling Payments Agreement in mid 1952, the MFA examined several policy options to

\textsuperscript{40} Campbell, 'Sterling Problem', 23 February 1952, SCP, 6417(22), ESS(E)00968; Gordon A. Millar, Signal Corps, Executive Officer, SCAP to Sherwood F. Fine and W.W. Diehl, Diplomatic Section (DS), SCAP and Campbell, 19 February 1952, \textit{ibid}.

\textsuperscript{41} Radiogram from DA to SCAP, no.DA902290, 29 February 1952, \textit{ibid}.

\textsuperscript{42} Radiogram from DA to Fine, Diehl and Campbell, 1 March 1952, \textit{ibid}.

\textsuperscript{43} In fact, Washington instructed SCAP to make sure that the US intervention in Japan's refusal of steel export approval for Britain should not be interpreted as a sign of US readiness to assist Japan in financial difficulties arising from the sterling accumulation. Radiogram from US Department of the State to SCAP, no.031530Z, 4 March 1952, \textit{ibid}.

\textsuperscript{44} Gaimusho, 'DS tōn Teirei Kaiken', 12 March 1952, DAO, E'0.0.0.5.

\textsuperscript{45} Campbell to Marquat, 'Steel for UK', 13 March 1952, SCP, \textit{op.cit}.

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tackle the excessive sterling surplus. The option to terminate the Agreement had to be ‘avoided by any means’ as this could have had an adverse effect on Anglo-Japanese relations and caused considerable damage to Japanese export industries.\textsuperscript{46} The option to revise the Agreement so as to exempt Japan from its obligation to abide by the official cross rate between the US dollar and the pound and then to apply a more realistic exchange rate to Japanese exports to the sterling area was also ruled out. This was because it might infringe the IMF obligation to abide by the official cross rate except for a spread of 1 per cent off parity, creating problems for Japan’s membership in the IMF, which was due in August. The option to establish an export-import price adjustment fund by imposing a levy on sterling export proceeds and to subsidiise imports from the sterling area might infringe the principle of most-favoured-nation treatment stipulated in the GATT provisions. It might also affect discussions on Japan’s accession among the GATT contracting parties.\textsuperscript{47}

Considerations of Japan’s membership in the IMF and the GATT prevented the Japanese government from introducing selective regulatory measures to cope with sterling accumulation, with government leaders giving priority to participation in the Bretton-Woods system. In heated discussions over the control measures in February, Ikeda ruled out adjusting the yen-sterling exchange rate because of the unfavourable impact this might have on Japan’s membership in the IMF.\textsuperscript{48} In short, the long-term objective of participation in a freer international trade regime prevented the government from acting to curb fluctuations in sterling trade. The only alternative left was two-way expansion of trade in order to balance Japan’s overall sterling trade.

\textbf{JAPAN INCLINES TOWARDS EXPANDING STERLING TRADE}

In view of this situation, the Japanese pushed for increased availability of commodities from the sterling area in the Sterling Trade and Payments Review Conference, which was held in March 1952 in Tokyo to discuss the imbalance in trade between Japan and the sterling area. It was inevitable that Japan would take up the issue of excessive accumulation of sterling

\textsuperscript{46} Gaimusho, Keizaikyoku, Dai 4-ka, ‘Nichi-Ei Shiharai Kyotei Manki Taisho Hoshin (An)’ [Policy for the expiry of the Anglo-Japanese Payments Agreement], 16 July 1952, DAO, B’0.0.2.1.


\textsuperscript{48} ‘Pondo Mondai de Iken Kokan: Keizai Kyoryoku Saiko Kaigi’ [Exchange of opinions over the sterling problem in the ministerial conference on economic cooperation], Nihon Keizai Shimbun, 29 February 1952.

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surplus in the Review. London instructed H.H. Thomas, Financial Minister for the UKLM, to deter the Japanese from renouncing the Sterling Payments Agreement or asking for a revision. The British government also objected to Japan’s introduction of selective export controls to the sterling area without consultation, prefiring a tightening of import restrictions by the sterling area as a remedy to the problem. London was obviously concerned about Japan’s desire to revert to the previous arrangement by, for example, restoring the dollar convertibility clause, as advocated by the FECB.

In fact, though, London’s anxiety did not materialise in the Review. Although MITI’s Oda complained about the lack of availability and high prices of commodities from the sterling area, he did not call for a revision of the Sterling Payments Agreement. The British delegates were so impressed by Oda’s approach that they later reported to London that the Japanese stance was ‘remarkably sensible.’ While the two sides did not reach agreement on specific measures to cope with the accumulation, London acknowledged the Japanese claim that the trade imbalance was caused by the limited availability and high prices of sterling commodities.

While the Japanese were prepared to try to overcome the sterling accumulation through increased purchases of sterling commodities, they also emphasised the need to lower trade barriers against Japanese exports to the sterling area. They requested, for example, most-favoured-nation treatment for Japanese exports in the sterling area. They also contended that the export adjustment measures introduced in early March were only of a temporary nature, emphasising Japan’s commitment to expansion of two-way trade with the sterling area. The Japanese stance was based on very real concern about the introduction of drastic import restrictions by the sterling area countries to safeguard the balance of payments. These restrictions were to be implemented soon after the Review, and in fact, the MFA registered an official protest about Britain’s unilateral suspension of import licensing for cotton from Japan without due consultation in April. London rejected the Japanese case, saying that Japan was displaying the same hasty reaction which had led to the

51 Cable from Crosec to Canberra, no.46, 20 March 1952, AA, A1838, 479/2/10 Part 2.
imposition of export adjustment measures in March.\textsuperscript{53} The Japanese emphasis on relaxation of import controls gave the British delegates the impression that the Japanese officials were ‘obviously very frightened’ at the forthcoming introduction of drastic import restrictions.\textsuperscript{54}

Japan’s emphasis on two-way expansion of sterling trade at the Review reflected the victory of MITI and the MFA over the FECB and MOF over the handling of the sterling accumulation. At the conference, Oda went so far as to assert to the British delegates that the tightening of export finance measures introduced by the FECB in February was a ‘dead issue’, a point the MFA officials agreed on. In front of the British delegates, Kiuchi contradicted Oda, emphasising that these financial measures were still in effect. He added, though, that they were intended to discourage speculation and not to curtail Japan’s exports to the sterling area.\textsuperscript{55} Kiuchi did not conceal his concern about the sterling accumulation, protesting that the existing surplus level was ‘shocking and alarming’ and contrary to British assurances given repeatedly in the payments negotiations in the previous year.\textsuperscript{56} With the tightening of import licensing imminent, Japanese financial officials had to restrain themselves from taking action to curb Japan’s sterling accumulation because such an approach might justify the strengthening of import restrictions by the sterling area. This could result in a decline in Japan’s exports even to a level below that before the conclusion of the 1951 Sterling Payments Agreement, as was actually to happen later. Hence, while agreeing to Kiuchi’s claim about the effectiveness of financial measures in tackling sterling accumulation, MOF officials stressed their intention to encourage relaxation of import finance for sterling commodities. In this way, they hoped to impress the British delegates with their willingness to cooperate and achieve two-way expansion of Japan’s sterling trade.\textsuperscript{57}

Japan’s commitment to expansion of sterling trade gave Japanese officials an appreciation of Australia’s role as an engine to maintain Japan’s trade with the whole sterling area at a high level. In the Sterling Trade Review Conference, the Japanese attributed the sterling accumulation to the unexpectedly low procurement of Australian


\textsuperscript{54} Sterling Area Working Party, ‘Minutes of the Eighty Sixth Meeting’, \textit{op.cit.}

\textsuperscript{55} Telegram from Dening to FO, no.496 DRIVE, 25 March 1952, AA, CP553/1, 194/B/10/50/6.

\textsuperscript{56} Telegram from Dening to FO, no.471 DRIVE, 21 March 1952, \textit{ibid.}

\textsuperscript{57} Telegram from Dening to FO, no.496 DRIVE, 25 March 1952, \textit{op.cit.}
wheat due to bad crops. This was the only item singled out by the Japanese, illustrating Australia’s significance as the main supplier in the sterling area. In fact, Japan’s expectations concerning Australia were such that Oda approached Menzies with a proposal to purchase 350,000 tons of wheat, 150,000 tons of barley, 50,000 tons of sugar and 50,000 tons of iron ore. Although these figures were beyond Australia’s realistic supply capacity, Oda’s proposal indicated that Japan regarded Australia as a promising alternative supplier to the United States. It seemed that Australia-Japan trade relations would flourish as long as Japan had abundant foreign currency to finance purchases from Australia.

Japan’s huge bilateral deficit because of active procurement from Australia meant that other sterling area countries had greater purchasing power to direct towards Japanese industrial goods. Perkins points out that Australia had the trade structure to offset its deficit in dollars with a huge surplus in non-dollar, non-sterling balances. The resultant surplus in Australia’s overall non-sterling balance had been absorbed by the deficit in its sterling balance during the 1950s, except in 1952-53, when it introduced tight import licensing because of the deterioration in its balance of payments position. This observation suggests that in the postwar period the sterling surplus earned by Australia in bilateral trade with Japan had been transferred to other sterling area countries so that they could finance their purchases from Japan. Despite the worldwide trend towards tight exchange controls in a period of dollar shortage, Japan and the sterling area countries benefited from a multilateral settlement system provided by the Sterling Payments Agreements. Under this system Japan could continue to increase its production level to meet active demand for Japanese goods within the sterling area. It, in turn, could also utilise its overall sterling surplus to maintain procurement of important raw materials such as raw wool.

58 Sterling Area Working party, 'Minutes of the Eighty Fifth Meeting', 20 March 1952, op.cit.
59 Menzies to DCA, 12 January 1952, AA, A609, 552/137/15. Australia introduced the embargo on iron ore exports for the purpose of conservation of scarce domestic resources in 1938. This decision was made in reaction to the Japanese move to develop a Western Australian iron ore mine through a British dummy company. The embargo was lifted in 1960 following the discovery of abundant deposits in the Kimberley district in Western Australia. For Australia’s decision for the iron ore embargo, see Akio Watanabe, ‘Tekkoseki Kin’yu Mondai wo meguru Nichi-Go Funso (1938-39 nen)’ [The Japan-Australia dispute over the iron ore embargo (1938-39)], Chihiro Hosoya, ed., Taiheiyo-Ajia-Ken no Kokusai Keizai Funsoshi: 1922-1945 [The history of international economic disputes in the Pacific-Asia sphere: 1922-1945], Tokyo Daigaku Shuppankai, 1983, chapter 8.
From this viewpoint, Australia was the lynchpin in the postwar multilateral transaction system between Japan and the sterling area. Without Australia’s huge capacity to supply commodities, Japan could not have used the enormous sterling surplus it earned from exports produced from dollar financed raw materials. Such a situation would have weakened the positions of MITI and the MFA and might have strengthened the call for restoration of the dollar convertibility clause or the introduction of dollar cash settlement in sterling trade. If the possibility of a dollar drain in trade with Japan had reemerged, the exchange control authorities within the sterling area would have had no hesitation in restricting imports from Japan. Japan would then have lost both export markets to sustain its production level as well as handy sterling cash to finance its procurement of commodities from the sterling area. In other words, Australia’s presence increased Japan’s commitment to expansion of trade with the sterling area.

Once the Japanese government decided to promote imports from the sterling area as a solution to the problem of sterling accumulation, it began to pursue long-term purchase contracts to secure the stable supply of important commodities from the sterling area.61 In his talks with Menzies in August, Ushiba proposed a three-year contract to purchase 150,000-200,000 tons of barley annually.62 This was a period when Japan still faced a shortfall of foodstuffs for domestic consumption. The Japanese government entered into various trade arrangements to secure a supply of foodstuffs, as well as launching a five-year program to expand domestic food production in 1952.63 The Japanese government also made a sudden decision to purchase 700,000 tons of Canadian barley in October, when the Australian contract was still under negotiation. Menzies warned the MFA that this sort of speculative action would make the Australian government doubt Japan’s desire for a long-term contract.64 His protest seems to have influenced the Japanese officials, and the Japanese Food Agency duly entered into a contract in mid November with the Australian Barley Board, which promised to make 50 per cent of Australia’s exportable surplus barley

63 Norinsho [Ministry of Agriculture and Forestry (MAF)], Norinsho Nempo [The annual of the Ministry of Agriculture and Forestry], 1954, pp.413-414.
available for shipment to Japan. Such Japanese initiatives as the barley contract show that Japan's trade strategy was shifting in emphasis from exchange controls to achieve dollar savings to the securing of a stable supply of strategic commodities from non-dollar sources.

Menzies believed that the impetus for the government's decision on the barley contract was provided by MITI and the MFA. By late 1952, the Japanese government had become concerned about the rapid fall in the sterling balance, caused by an intensification of import licensing by the sterling area countries from March. The two Ministries had to persuade MOF, which took over control of foreign exchange on the abolition of the FECB in April, to allocate these declining funds to barley purchases. Domestic supply conditions were so poor that the Japanese Ministry of Agriculture and Forestry (MAF) was forced to purchase overseas foodstuffs, including those from the sterling area, even in 1953 when Japan's sterling shortage deteriorated further.

Another explanation for the enthusiasm of MITI and the MFA for the barley contract is found in the Ministries' desire to increase Japan's diplomatic leverage to a point where it could ask Australia to relax its import restrictions on Japanese goods. The MFA issued a Note Verbale to the Australian Embassy in Tokyo on 17 November, only three days after the conclusion of the barley contract. In it, the Japanese government drew Australia's attention to Japan's running deficit in sterling trade and called for a relaxation of import controls. The Note mentioned the barley contract and conveyed the MFA's willingness to conclude similar arrangements for other commodities, to 'bring about an orderly expansion' of Australia-Japan trade, the 'common objective for both countries'. MITI and the MFA were, it seems, trying to utilise the atmosphere of goodwill created by the barley contract to gain Australia's cooperation in alleviating Japan's sterling shortage. The Ministries were already aware that the solution to the problem lay in the relaxation of import restrictions by the sterling area including Australia, and that this could only be achieved through diplomatic channels. From this perspective, the conclusion of the barley contract indicates the

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67 Norinsho, 1954, pp.405-408.
68 MFA to Australian Embassy in Tokyo, 'Note Verbale', 17 November 1952, Gaimusho Keizaikyoku Dai 4-ka, Nichi-Go Tsusho Kosho no Kei oyobi Mondaiten [The development of the Japan-Australia trade negotiations], January 1957, pp.2-4.
consolidation of a more liberal trade strategy under which Japan aimed to expand both import and export trade with the non-dollar area as the key to achieving the national objective of economic self-reliance.

Thus Japan consolidated its commitment to the trade strategy of expansion of non-dollar trade through the new Sterling Payments Agreement. The removal of the dollar convertibility clause unleashed strong demand in the sterling area for Japanese goods. This gave the Japanese government the task of coping with an excessive accumulation of sterling surplus in 1951–52. Although the Japanese foreign exchange control authority, led by FECB Chairman Kiuchi, attempted to introduce export regulations to prevent distortion of the Japanese foreign currency position, the government, led by MITI and the MFA, eventually opted to promote commodity procurement from the sterling area to offset its huge sterling surplus. It was not in Japan’s interest to adopt tight controls and run the risk of suppressing exports to the sterling area, which had grown to be a good market not only for competitive Japanese textiles and other light industrial goods but also for uncompetitive heavy and chemical goods. Behind the government decision lay US pressure for cooperation with the British defence effort and the need to avoid selective measures which might infringe the principles of the freer postwar international trade system under the IMF and the GATT.

In the event, the move to refrain from tight export restraints forced the Japanese government to pursue diversion of import trade from North American sources to avoid dollar expenditure. This drew Japan’s attention to the significance of developing commercial links with Australia, which had the largest supply capacity of the non-dollar countries, through the introduction of long-term purchase contracts. Furthermore, Australia played an important role in sustaining Japan’s trade with the whole sterling area, since its bilateral trade surplus with Japan indirectly supplied the other sterling area countries with purchasing power to obtain Japanese goods.

As long as Japan sought to expand sterling trade, it needed to hold a certain amount of sterling cash on hand to finance its commodity purchases. When tight import licensing caused its sterling position to deteriorate, Japan again faced a decision that would have an important impact on the consolidation of its postwar trade strategy.
Economic Diplomacy: The Japanese Response to the Sterling Shortage, 1953–54

By the time Japan had clarified its commitment to expansion of sterling trade to divert commodity purchases from dollar sources, as discussed in Chapter 8, it was facing a new problem: a serious sterling shortage caused by the sterling area’s tight import controls and a subsequent crisis in the balance of payments in 1953. Measures adopted by the Japanese government to improve its sterling balances entrenched the direction of the Japanese trade strategy in the post Peace Settlement period. The crisis in the balance of payments made the Japanese government and business leaders recognise the need to accelerate the rationalisation program to strengthen the competitiveness of the heavy and chemical industries. This meant that Japan could not introduce drastic import restrictions to counter those of the sterling area, since such restrictions might intensify inflationary pressure and hence hamper the rationalisation program. Furthermore, Japan could not count on extra dollar supply because special procurement was declining and the United States was not prepared to launch a new aid program that would assist Japan.

With no immediate solution at hand, the Japanese government was to adopt a strategy of self-help through industrial rationalisation and other measures. At the same time, it was aware of the need to develop commercial links on a more multilateral basis in order to secure purchases of commodities from non-dollar sources and save dollars. This highlighted the significance of achieving a reduction in import restrictions against Japanese goods in the sterling area. As long as Japan did not countervail import restrictions, the solution had to be sought in diplomatic approaches to the individual sterling area countries. Since Japan’s bilateral trade deficit with Australia was larger than that with the other sterling area countries, Australia became the main target of Japanese economic diplomacy in seeking relaxation of import licensing.
This chapter examines the factors leading to Australia's relaxation of the discriminatory import licensing system against Japan in November 1954. This was a landmark in the history of the postwar Australia-Japan trade relations in that Japan was granted soft currency treatment in Australia's import licensing system. This normalisation of bilateral trade relations was the product of a remarkable expansion of Australia-Japan two-way trade under the multilateral settlement system provided by the Sterling Payments Agreement. The enormous benefits of this system brought the two countries to the next stage in commitment to expand trade on a more multilateral basis.

JAPAN'S SLOW RESPONSE TO THE STERLING SHORTAGE PROBLEM

The intensification of import licensing which the sterling area countries collectively implemented from March 1952 began to affect Japan's sterling account from mid 1952. Table 9.1 shows that Japan's sterling trade was in deficit in the October quarter of 1952. The sterling balance at the end of June 1953 had fallen so drastically that it was only one-quarter of the balance for the corresponding period in the previous year, as indicated in Table 9.2.

The problem of the sterling trade deficit drew the attention of the Japanese government in mid 1952, despite the still high level of sterling accumulation. Japanese officials approached the British to try to improve the situation. While requesting increased availability of sterling commodities, the Japanese government expressed strong concern about the tightening of import licensing.\(^1\) In October, Japan decided to remove the export adjustment measures for steel and textile exports to the sterling area.\(^2\) The rapidly dwindling sterling surplus also drove Japan to accept further extension of the Sterling Payments Agreement at the end of the year.\(^3\) At this stage, it was in Japan's interest to

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\(^1\) 'Reply by Her Majesty's Government to Japanese Observations of 1 August, 1952', undated (August 1952?), AA, A609, 552/137/15

\(^2\) MFA, Tokyo, 'Note Verba', no.1345, 22 October 1952, *ibid.*

maintain sterling trade through soft-currency settlement in order to avoid deterioration of its sterling trade deficit.

Table 9.1  Japan’s Export-Import Trade with the Sterling Area, July–September 1952 to October–December 1954

<table>
<thead>
<tr>
<th></th>
<th>Exports to Sterling Area</th>
<th>Imports from Sterling Area</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>1952</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Jul–Sep</td>
<td>108</td>
<td>117</td>
<td>−9</td>
</tr>
<tr>
<td>Oct–Dec</td>
<td>92</td>
<td>135</td>
<td>−43</td>
</tr>
<tr>
<td>1953</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Jan–Mar</td>
<td>74</td>
<td>167</td>
<td>−93</td>
</tr>
<tr>
<td>Apr–Jun</td>
<td>75</td>
<td>174</td>
<td>−99</td>
</tr>
<tr>
<td>Jul–Sep</td>
<td>82</td>
<td>143</td>
<td>−61</td>
</tr>
<tr>
<td>Oct–Dec</td>
<td>87</td>
<td>118</td>
<td>−31</td>
</tr>
<tr>
<td>1954</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Jan–Mar</td>
<td>86</td>
<td>122</td>
<td>−36</td>
</tr>
<tr>
<td>Apr–Jun</td>
<td>109</td>
<td>139</td>
<td>−30</td>
</tr>
<tr>
<td>Jul–Sep</td>
<td>131</td>
<td>85</td>
<td>−46</td>
</tr>
<tr>
<td>Oct–Dec</td>
<td>166</td>
<td>87</td>
<td>−79</td>
</tr>
</tbody>
</table>


Table 9.2  Japan’s Foreign Currency Balance, September 1951–December 1953

<table>
<thead>
<tr>
<th>Year/Month</th>
<th>Dollar Account ($ million)</th>
<th>Pound Account (£ million)</th>
<th>Clearing Account ($ million)</th>
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<tbody>
<tr>
<td>1952</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>September</td>
<td>719</td>
<td>120</td>
<td>127</td>
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<tr>
<td>December</td>
<td>760</td>
<td>89</td>
<td>128</td>
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<tr>
<td>1953</td>
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<tr>
<td>March</td>
<td>836</td>
<td>52</td>
<td>84</td>
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<tr>
<td>June</td>
<td>834</td>
<td>33</td>
<td>57</td>
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<tr>
<td>September</td>
<td>883</td>
<td>33</td>
<td>45</td>
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<tr>
<td>December</td>
<td>789</td>
<td>43</td>
<td>70</td>
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Note: Each figure indicates the amount of balances at the end of the corresponding month.

Source: Keizai Kikakucho, 1962, p.185.
At the beginning of 1953, however, there was no sign of any improvement in the situation, and Japan's sterling balance had fallen to around £50 million, the lowest figure since September 1951. Alarmed at the ongoing problem of sterling shortage, Tokyo officially called for an opening of trade talks, to which Britain agreed, but only for explanatory purposes. The Anglo-Japanese trade talks were held in March in Tokyo and in April in London. The Japanese issued a strong warning that Japan would be forced to curtail purchases of sterling commodities, unless the sterling area relaxed its tight import restrictions. The British government, however, considered it unlikely that the trade surplus with Japan of the past several months would continue, as Japan would not be increasing its purchases of wool and cotton. In fact, the general policy of the British Commonwealth for 1953 was to keep import licensing tight until Japan's sterling balance fell to around £55 million, and so Britain was not prepared to increase substantially its purchases from Japan. All that the two sides agreed upon was that the sterling area would relax its import licensing to maintain Japan's annual sterling revenue at £197 million, almost the same amount as the 1952 annual figure, that a joint review conference would be held in four or five months time, and that the United Kingdom would offer Japan dollar swap facilities.

Despite the feeling of alarm at the sterling shortage problem, revealed in Japan's diplomatic approach to the sterling area countries, the Japanese government was slow to introduce drastic measures to improve its trade balance with the sterling area. In government talks on the level of the April–September 1953 foreign currency budget, held in March 1953, MITI proposed to avoid curtailing purchases of sterling commodities through active use of dollar swaps; as the dollar balance still stood at a high level, as shown in Table 9.2. MOF intervened, stating that MITI estimates of Japan's sterling balance for the next six months were overly optimistic. The foreign currency budget for the first half

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4 Cable from Crosec to Canberra, no.6, 20 January 1953, AA, CP553/1, 194/B/10/118.
5 Cable from Crosec to Canberra, no.31, 14 March 1953, AA, A609, 552/137/15.
6 Cable from Australian High Commissioner's Office in London to Canberra, no.81, 8 January 1953, AA, CP553/1, 194/B/10/118.
7 'Extract of the Commonwealth Liaison Committee', 18 April 1953, AA, A609, 552/137/16.
9 'Doru Utte Oginau: Tsusansho Pondo Fusoku ni Teian' [Dollar sales: MITI proposal against the sterling shortage], Nihon Keizai Shim bun, 4 March 1953.
10 'Pondo Mitooshi Kuichigau: Gaika Yosan Ketsuron Mochikoshi' [Pound estimates differ: Conclusion on
of the financial year (FY) 1953 was settled at ministerial level, where it was agreed to allocate $540 million of the overall foreign currency budget of $1,100 million to the dollar area, $300 million to the sterling area and $240 million to the open account area, in line with the MITI proposal.\(^{11}\) Compared with total imports from the sterling area of $538 million in FY1952, the allocation of $300 million for the April–September quarters meant that purchases from the sterling area would be maintained at the existing level, without being affected by the rapidly decreasing sterling balance.

The only measure which the government adopted to cope with the sterling shortage was to suspend the Automatic Approval process for imports from the sterling area on 13 February. This was adopted because applications for Automatic Approval imports from the sterling area were increasing rapidly, due to speculation that the government would introduce import controls. The prices of sterling commodities had fallen considerably compared with the previous year, thus further attracting Japanese demand. As a result, the total sum of such applications surpassed the amount allocated in FY1952 foreign currency budget. However, only five days later, MITI announced the resumption of Automatic Approval of imports from the sterling area, though on a more restricted basis to exclude the commodities such as rubber and pig iron which were subject to speculative purchasing.\(^{12}\)

Behind the government decision to avoid drastic curtailment of allocation of the foreign currency budget to sterling purchases lay the consideration to strengthen the price competitiveness of Japanese industrial goods by ensuring a stable supply of cheaper raw materials. MOF advocated reducing the sterling foreign currency budget on the grounds that import-export trade should be balanced in each currency as long as international trade was subject to tight exchange controls and there was a serious dollar shortage. MITI, on the other hand, argued against tightening import restrictions on the grounds that they might: (1) promote speculative sterling imports; (2) result in loss of sterling sources of strategic raw materials of good quality at competitive prices; (3) result in increased domestic prices, which would weaken the export competitiveness of the Japanese manufacturing industry.

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\(^{11}\) ‘Ei no Taido ni Kakaru: Pondo Yunyu Jissai niwa Shukusho Yoso’ [Dependent on British approach: Sterling imports to be reduced], *Nihon Keizai Shimbun*, 14 March 1953.

\(^{12}\) ‘Pondo Boeki Kiki no Jittai: Pondo AA Yunyu wa Naze Teishi Sareta ka’ [The crisis in sterling trade: Why the sterling AA imports were suspended?], *Ekonomisuto*, vol.31, no.9, 28 February 1953, pp.38-39.
currently undergoing rationalisation. In other words, Japanese government policy was based on a desire to improve the sterling trade imbalance by securing an abundant supply of cheaper raw materials from the sterling area and utilising them to strengthen the price competitiveness of Japanese export goods. This was similar to the ‘import-first’ policy of the Logan Plan, discussed in Chapter 2. The Logan Plan was designed to promote Japanese trade under the austere economic policy motivated by the Dodge Line. This time the Japanese government was also forced to introduce austere financial and fiscal measures to overcome the ongoing sterling shortage and the subsequent crisis in the balance of payments position.

FINANCIAL RESTRAINTS TO OVERCOME THE CRISIS IN THE BALANCE OF PAYMENTS

While the Japanese government refrained from introducing drastic controls on imports from the sterling area, Japan’s balance of payments position continued to deteriorate. As indicated in Table 9.2, Japan’s foreign currency balance in the clearing account began to decline from the beginning of 1953; Japan’s dollar position also deteriorated from the second half of the year. This was caused by a rapid increase in overall imports, which reached $1,135 million during the 1953 calendar year (CY) against $755 million during 1952. Compared with this strong import demand, the increase in exports was unimpressive, with total exports during CY1953 amounting to $1,275 million against $1,273 million during CY1952.

The crisis in the balance of payments alarmed Japanese officials. The Japanese government attributed the adverse trade imbalance to the inflationary effect of the increase in national income during the Korean War Boom. The 1953 issue of Economic White Paper put out by the Economic Deliberation Agency identified the domestic factors hampering export promotion. The prices of Japan’s heavy and chemical industrial goods were higher than those of other industrialised countries, due to high raw material costs, low labour productivity and the use of obsolete production equipment and facilities. The

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remarkable economic recovery of the occupation period had provided the Japanese nation with high purchasing power and created an income effect, expanding domestic consumption of industrial products, at the expense of export promotion. The 1954 Economic White Paper also pointed to the increased purchasing power of the Japanese nation to explain the substantial increase in imports during 1953. Other factors mentioned were the poor food crop of 1952, traders' speculative reaction to low imports in the previous year, high domestic prices and the relaxation of import finance.

The remedy was to restrain domestic demand through austere financial and fiscal policies in the short term, and to strengthen the price competitiveness of the heavy and chemical industries through the implementation of rationalisation programs in the longer term. The option to improve the balance of payments position by devaluation of the yen was categorically rejected, since it would lift the import prices of strategic raw materials and foodstuffs. The price elasticity of exports was extremely low, because of tight exchange controls prevailing all over the world under the dollar shortage, and the IMF provisions imposed strict restrictions on margins of devaluation. The Japanese government thus introduced a series of restraint measures on import finance from October 1953 and strengthened them in the first half of 1954. Prime Minister Yoshida also showed strong leadership in keeping the government budget expenditure for FY1954 below ¥1,000 billion in January 1954.

The government's austere approach to the balance of payments crisis was justified in the 1954 Economic White Paper, which asserted that it was time to 'retreat a step backwards and consolidate'. Stressing the need for domestic demand to cool down so that

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17 Sadao Takahashi, Okurasho Daijin Kanbo Chosaka [Research Division, Minister's Secretariat, Ministry of Finance (MOF)], 'Nihon Keizai no Kiki wa Dokoni Aruka: An'ina Kotosaku dewa Sukuiwarenai' [Where is the cause of the crisis of the Japanese economy?: No solution through an easy patch-up measure], Gaikoku Kawase, no.92, 1 April 1954, p.4.
18 These restraint measures included suspension of the handling of import settlement bills for non-essential items, shortening of the settlement period of import bills, and abolition of financial measures to promote import expansion to tackle the excessive sterling accumulation from 1952. 'Kokusai Shushi no Kiki wa Sattaka' [Has the balance of payments crisis gone?], Ekonomisuto, vol.32, no.50, 11 December 1954, p.26.
capital could be accumulated and mobilised for increased productivity of the heavy and chemical industry, the 1954 issue asserted in conclusion:

There is no short cut in capital accumulation. There is no alternative but to wait for saving of consumption by the nation unless we are to depend on foreign aid (my emphasis). 20

This observation has two implications for the trade strategy. Firstly, 'no short cut' means that it would take time for the heavy and chemical industrial sectors to become competitive enough to rival their counterparts in industrialised countries and become Japan's central export earners. How could Japan sustain its balance of payments in the meantime, faced with the stern reality of the diminishing US special procurement now that the Korean War was over? Secondly, the alternative to 'depend on foreign aid' was still open to the Japanese. This encouraged Japanese government and business circles to look forward to the re-emergence of the US-Japan Economic Cooperation Program, which had once held so much promise, as discussed in Chapter 7.

In July 1953, the Japanese government entered into negotiations to receive US aid under the Mutual Security Act (MSA). The MSA enabled the US administration to offer non-Communist countries military aid to prevent Communist infiltration, on the condition that recipient countries cooperated with US-led collective security programs and strengthened their own defence capability. The ceasefire in Korea was being negotiated, and it was obvious that special procurement would dwindle. Hence, Japanese business circles welcomed MSA aid as an alternative source of extra dollar supply.

In mid July, the Federation of Economic Organisations (Keidanren), the association of Japan's large business corporations, issued an official request for the MSA aid. What Keidanren wanted was to obtain not only purely military assistance but also economic aid for national development. In other words, Japanese business aimed to secure a source of extra dollar supply on a more permanent basis to substitute for special procurement. Keidanren's official request ran as follows.

Our balance of payments has kept just in balance thanks to special procurement worth in the order of more than $800 million, so we have not reached a level of complete self-reliance. Therefore, if we could receive special procurement on a regular basis through MSA programs as a temporary measure until we can fulfill

the long-term plans for economic self-reliance centred on normal trade, MSA aid will contribute towards establishing the foundation for our industrial production and strengthening our international competitiveness in the future ... In this sense, we strongly expect that MSA aid should not be limited to military assistance, including offshore procurement for the US Army, but that, at the same time, it should take the form of defence support aid, contributing towards securing essential materials, technological improvement and modernisation of production facilities.\(^{21}\)

In particular, *Keidanren* requested that US aid and offshore procurement be provided 'on a planned regular basis' to contribute towards modernisation not only of the military industry but also of the heavy and chemical industries, 'which should be the axis of our industry in the future'. Japanese business circles also hoped that the United States would explore the possibility of active procurement of Japanese industrial goods when granting MSA aid to non-Communist countries in Asia.\(^{22}\) These requests reflected the hopes held for the earlier US-Japan Economic Cooperation Program in 1950–51.

Japanese government and business circles had targeted the heavy and chemical industries as Japan's main future export earners. These sectors were still in the process of rationalisation and had yet to strengthen their competitive edge. Moreover, the Asian non-Communist countries which were expected to substitute for Japan's traditional Chinese export market lacked adequate purchasing power. The easiest way to overcome this predicament was to secure extra dollar supplies through MSA aid. While arguing that Japan would meet the suggested guidelines of the MSA program, in view of its 'international stand as one of the members of the free world', Japanese business circles tried to capitalise on the US military aid program for their own purpose: facilitating the tough task of achieving economic self-reliance.\(^{23}\)

The Japanese government shared business expectations for overall economic aid. Yasuhara points out that without fully understanding the MSA provisions, the Japanese government held the naive belief that it would be able to obtain US economic aid while evading pressure to strengthen the Japanese military capability to which the public was...

\(^{21}\) Keizai Dantai Rengokai [Japan Employers' Federation], 'MSA Ukeire ni kansuru Ippanteki Yobo Iken' [General requests on the MSA], *Keidanren Geppo*, vol.1, no.8, August 1953, p.42.

\(^{22}\) *Ibid.*

\(^{23}\) *Ibid.*
vehemently opposed. The US administration under President Dwight Eisenhower was not prepared to concede such economic aid and flatly rejected the Japanese proposal, thus shattering Japan’s naive hopes. Even when the prospects for economic aid looked extremely bleak, the Japanese Foreign Minister, Katsuo Okazaki, revealed the strength of the government’s attachment, by stating that it was too early to give up hope and that there was no change in the government policy to pursue US economic aid in the negotiations.

In the October talks led by Walter Robertson, head of the Far East Division of the US State Department, and Hayato Ikeda, former Japanese Minister for Finance, however, it became clear that all Japan could expect to gain was surplus disposal of US agricultural products equivalent to $50 million based on Section 550 of the MSA. Under the surplus disposal program, Japan could obtain US surplus wheat with payment to be made in yen. This yen remittance was to be pooled in Japan as a fund, only a part of which would be granted to Japan, and a large part of which was to be used for the military procurement by the US forces in Japan. This was far from the kind of aid which the Japanese had in mind. On the contrary, there was concern that Japan’s dollar position would deteriorate if a large part of the US military procurement in Japan was not paid in dollars but financed from the yen fund for surplus disposal. Although the United States pledged offshore procurement orders worth $100 million in the Mutual Defense Assistance Agreements concluded in March 1954, this figure included financing from the surplus disposal yen fund in the order of $40 million. In fact the US procurement record amounted to only $70 million in USFY1954, to the great disappointment of the Japanese government.

Japan’s naive hopes for extra dollar supply through the MSA program were thus completely shattered. This confirmed yet again that there was no way left for Japan but to achieve economic self-reliance through promotion of exports on a normal commercial basis.

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25 ‘Keizai Enjo wo Akiramezu’ [We will not give up economic aid], Nihon Keizai Shimbun, 3 August 1953.
27 Yasuhara, 1988, p.165.
while maintaining its rationalisation efforts, by making the most of the gradually dwindling US offshore procurement. It is noteworthy that the MSA negotiations obliged Japan to commit itself to tightening inflationary policy and concentrating on export promotion.

Sakamoto emphasises that in the Ikeda-Robertson talks the US administration put strong pressure on Japan’s former Minister for Finance to adjust Japan’s economic policy so as to stabilise inflation and tackle the crisis in the balance of payments position. In Washington, Ikeda was blamed by Joseph Dodge for Japan’s failure to utilise the ‘windfall’ profits’ obtained from special procurements effectively, and Dodge strongly urged Japan to shift its economic policy towards curtailment of imports and promotion of exports through austere fiscal restraints and self-help efforts. Sakamoto argues that Dodge’s advice strengthened Prime Minister Shigeru Yoshida’s determination to introduce austere fiscal and monetary policies from late 1953. Yoshida himself later revealed that when he made the decision to cut budget expenditure in late 1953, he had felt the same way as he had on the occasion of the implementation of the Dodge Line in 1949. In 1949, SCAP had adopted a trade policy of diverting trade into non-dollar sources, expanding the networks of bilateral trade and payments agreements, and restoring normal private trade, in response to the Logan Plan. The Japanese government now adopted a similar policy of promoting trade on a normal commercial basis without counting on special procurement.

THE SIGNIFICANCE OF ECONOMIC DIPLOMACY IN PLACING TRADE ON A MORE MULTILATERAL BASIS

The volatile fluctuations in the sterling balance made it imperative for the Japanese government to shift the weight of its trade policy from dependence on extra dollar supply to promotion of trade on a normal commercial basis in the first half of the 1950s. The excessive sterling accumulation in 1951–52 highlighted the importance of expanding imports from the sterling area. Declining special procurement along with the unsatisfactory outcome of the MSA negotiations forced Japan to recognise the increasing need to divert purchases into non-dollar channels to save dollars. In order to secure adequate financing of

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29 Ibid., pp.42-45.
purchases from these sources when the balance of payments deteriorated in 1953–54, Japan had to rely on economic diplomacy to achieve a relaxation of the tight import controls, especially in the sterling area.

In May 1952, the Policy Coordination Division of MITI’s Minister’s Secretariat emphasised trade promotion in Southeast Asia as a central trade strategy for Japan after the Peace Settlement. This proposal was based on the optimistic premise that the existing decline in trade caused by the tightening of import licensing by the sterling area and the decrease in special procurement was just a temporary setback. This premise derived from the observation that the worldwide trend to increase military production would continue as a result of the Cold War, regardless of the outcome of the Korean War, so that the sterling area countries would be forced to relax their import licensing to secure supplies of essential Japanese goods.31 This thinking lay behind MITI’s opposition to restraints on export finance, proposed by the FECB in February.

In a document in August, however, MITI outlined its belief that world trade might follow a declining trend. The tightening of import licensing by the sterling area countries from March, together with the active exports to Southeast Asia by West European countries and the decline in special procurement, began to affect Japanese exports badly and foreshadowed the deterioration of the balance of payments position. MITI also admitted that it was necessary to develop a ‘comprehensive policy encompassing diplomatic and cultural aspects’ to resolve the highly political problems of reparation before Japan would be able to promote trade with Southeast Asia. Hence, the Ministry advocated implementation of the US-Japan Economic Cooperation Program centred on the ‘special procurement in a broader sense’ in that it would not be confined to military procurement.32 The emergence of a call for ‘broader’ special procurement was also in line with Japan’s

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31 Tshushosangyosho Daijin Kambo Somuka [Policy Coordination Division, Minister’s Secretariat, MITI], ‘Kowago no Tsusho Sangyo Taisaku no Hoko’ [The direction of international trade and industry policy after the peace settlement], 29 May 1952, cited in Haruhiito Takeda, ‘Jiritsu kara Seicho he’ [From self-reliance to economic growth], Tsushosangyosho Tsusho Sangyo Seisakushi Hensan Linkai [Committee for the history of international trade policy, MITI], ed., 1989, Tsusho Sangyo Seisakushi, Dai-5-kan: Dai-2-ki, Jiritsu Kiban Kakuritsuuki(1) [The history of international trade policy, volume 5: Second period for economic self-reliance, no.1], Tsusho Sangyo Chosakai, 1989, chapter 1, p.74. This book is part of a series of an official history of the MITI. Takeda’s chapter intensively cites internal documents of the Ministry.


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quest for overall economic aid in the MSA negotiations with the United States, as mentioned previously.

When the sterling shortage worsened and it became obvious that special procurement was dwindling rapidly, MITI started to emphasise economic diplomacy to secure every possible export market for Japanese goods. It also advocated diverting imports to non-dollar suppliers. The November document specifically pointed out the need to promote the early conclusion of the Treaties of Commerce and Navigation, Trade Agreements, a revised Anglo-Japanese Payments Agreement, and Japan’s membership to the GATT. The government’s interest in these initiatives as a means of promoting exports reflects a shift from its earlier position to give higher priority to the prevention of sterling accumulation than to the establishment of an institutional framework of trade relations, as discussed in Chapter 7.

In 1953, when the government and business circles hoped to secure a new source of dollar supply through the MSA program, plans emerged within the MITI to lay more stress on export promotion than on special procurement. In the document of April 1953, when a ceasefire in Korea appeared imminent following the death of Josef Stalin in March, MITI dropped further promotion of special procurement from its nine main trade policy objectives while nominating export promotion as the first objective. Special procurement was excluded from the list in view of the past tendency to attribute difficulties in export promotion to the decline in special procurement. This again indicates that Japan realised it had little alternative but to expand trade on a normal commercial basis, and for this purpose to adopt a strategy to facilitate trade on a more multilateral basis. Although Japan’s future trade was to centre on heavy and chemical industry exports to developing countries in Asia, MITI categorically rejected such drastic interventionist measures as export subsidies and devaluation of the yen, on the grounds that while they would only provide temporary relief, they could affect external relations and hamper the industrial

33 Tsushosangyosho, ‘Tsusho Sangyo Seisaku no Kihon Hoshin’ [Basic strategy of the international trade and industry policy], 8 November 1952, cited in Takeda, 1989, p.82.

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rationalisation process. Hence, all that was recommended to promote exports was such measures as strengthening commercial firms and expanding the import-export link system. This was to be introduced to overcome the shortage of sterling balance and affected Australia’s wool sales to Japan.\footnote{Tsushosangyoshō, ‘Showa 28-nen Shinseisaku Shiryo’ [Documents on new policies for 1953], Undated, cited in Takeda, 1989, pp.97-98.}

These policy considerations implied the increasing significance to Japan of economic diplomacy. Although the Japanese government worked out a long-term strategy to promote heavy and chemical industrial exports to Asian developing countries, it would be some time before Japan’s heavy and chemical industries were able to compete with their the Western rivals. As well, until the reparation negotiations were settled, Asian countries did not have purchasing power to obtain Japanese goods. With the interventionist approach rejected, the most effective measure to achieve export promotion and overcome the crisis in the balance of payments within a short period was to persuade trading partners to relax import restrictions imposed on Japan’s competitive industrial goods in overseas markets. These were the background factors which highlighted the significance of the economic diplomacy during the first half of the 1950s.

As the MSA negotiations proved, Japan could not count on US aid to overcome the crisis in the balance of payments, and economic diplomacy became more salient in Japan’s trade strategy. In December 1953, Kiyohide Okano, who held the dual portfolios of Minister for International Trade and Industry and Director-General of the Economic Deliberation Agency, presented his program for achieving economic self-reliance. This so-called Okano Plan envisaged three goals: to improve the balance of payments position ‘through normal trade as much as possible’; to accomplish this goal while Japan could still count on a high level of extra dollar supply; and to increase the levels of exports and domestic self-sufficiency. The measures to be adopted to achieve these goals were increased exports through promotion of economic diplomacy and the strengthening of economic cooperation with Southeast Asian countries through reparation agreements. The Okano Plan was distinct from previous plans for economic self-reliance in stressing not only the rationalisation of the heavy and chemical industries but also diplomatic approaches to open Japan’s export markets. Miyazaki says that the main significance of the Okano Plan was
that it confirmed that, in view of the diminishing special procurement, the Japanese had no other alternative but to pursue export promotion independently.\textsuperscript{37}

In fact, the 1954 issue of Trade White Paper asserted that there was considerable room for economic diplomacy in attempts to overcome existing bottlenecks. These included the international network of trade discrimination against Japan, the limited convertibility of currencies, uncompetitive basic industries, weak commercial firms and lack of marketing effort.\textsuperscript{38} MOF also expressed its strong commitment to economic diplomacy, arguing that Japan had no alternative but to sustain production levels through export promotion if it was to achieve the national objective of attaining economic growth without inviting inflation, and that ‘for this purpose it was a must to push economic diplomacy forward in a vigorous manner to achieve removal of tariff barriers and to relax import restrictions’.\textsuperscript{39} Thus, the crisis in the balance of payments in 1953–53 urged the Japanese government to concentrate on an ‘export first’ trade strategy in which economic diplomacy had a significant role.

The Japanese diplomatic effort during the first half of the 1950s was significant. Japan succeeded in opening North American markets through an exchange of most-favoured-nation treatment when it concluded the Treaty of Friendship, Commerce and Navigation with the United States in April 1953 and the Commerce Agreement with Canada in March 1954. Japan also secured membership in the IMF in May 1952 and provisional membership in the GATT in October 1953, and became a formal contracting party in September 1955. Further promotion of the liberal institutional framework for trade relations remained the ultimate objective of Japan’s economic diplomacy in the second half of the 1950s and the early 1960s. In particular, since the fourteen contracting parties refused to enter normal GATT relations with Japan by retaining GATT Article XXXV in 1955, the onus of Japan’s economic diplomacy was to remove trade discrimination by negotiating bilateral treaties or agreements of commerce and navigation with these countries.

\textsuperscript{37} Miyazaki, 1957, pp.179-180.
\textsuperscript{38} Tsushosangyosho, Nihon Boeki no Genjo [Current situations of Japanese trade (Trade White Paper)], Tsusho Sangyo Chosakai, 1954, p.29.
\textsuperscript{39} Okurasho, ‘Kongo no Keizai Seisaku no Kihonteki Kangaekata’ [Basic considerations on economic policy], 16 August 1954, Arisawa and Inaba, 1966, p.254.
Apart from the goal of establishing an institutional framework for freer trade relations, economic diplomacy in the first half of the 1950s had another important objective. In order to bring about immediate improvement of the crisis in the balance of payments in 1953–54, Japan had to concentrate on export promotion. With the convertibility of currencies yet to be restored, import licensing for exchange control had far more restrictive effects than tariff barriers in the non-dollar area countries. If Japan was to improve its adverse trade imbalance with these countries, it had to aim to increase its exports within the framework of the existing bilateral payments and trade agreements. In fact, the official history of postwar Japanese diplomacy by the Ministry of Foreign Affairs defines the period from 1952 to 1956 as one of consolidation of trade relations through bilateral trade and payments agreements.40

This perspective gives weight to the significance of promoting economic diplomacy in the sterling area. The 1951 Sterling Payments Agreement was the most important payments agreement for Japan, because it provided the institutional framework for a flourishing non-dollar trade by introducing the principle of multilateral settlement with the whole sterling area through the removal of the dollar convertibility clause. In fact, Japan’s sterling trade showed remarkable growth from late 1951 to 1952. The tightening of import licensing by the sterling area countries from March 1952 then brought about a huge sterling shortage for Japan and triggered the crisis in the balance of payments in 1953–54. Here it became imperative for the Japanese authorities to negotiate a relaxation of import restrictions. The president of one Japanese firm observed that Japan’s exports to the sterling area countries would increase considerably if import licensing was relaxed.41 In particular, attributing the substantial fall in exports of competitive textiles to the sterling area to import restrictions, Keidanren urged the relaxation of import licensing through diplomatic approaches.42 MITI officials also advocated economic diplomacy and improvement of the price competitiveness of the heavy and chemical industries as the most effective remedies to overcome the crisis in the balance of payments.43

41 ‘Pondo no Kokansei Kaifuku to Nihon no Boeki’ [Restoration of the convertibility of the pound and Japan’s trade], Keidanren Geppo, vol.1, no.5, May 1953, p.19.
43 Yoshie Imai (Chief, International Trade Policy Division, International Trade Bureau), ‘Kongo no Nichi-
Such diplomatic approaches had to be made multilaterally, in that Japan's sterling trade was already being conducted on a more multilateral basis. Although the United Kingdom took sole responsibility for the 1951 Payments Agreement negotiations with Japan, the new Agreement deprived London of its control over trade between the whole sterling area and Japan. Since the need for strict balancing of trade was dissipated, independent British Commonwealth countries, such as Australia, India and New Zealand, controlled their own bilateral trade with Japan. Japan thus had to develop diplomatic channels not only with the United Kingdom but also with these individual sterling area countries in order to correct the sterling shortage. It was in this context that Australia emerged as an important target for Japan's economic diplomacy.

JAPANESE ECONOMIC DIPLOMACY TOWARDS AUSTRALIA

Along with the establishment of a strategy to promote trade with non-dollar area countries, the Japanese government used economic diplomacy to overcome the crisis in the balance of payments in 1953–54. The Anglo-Japanese trade and payments talks were held in London from December 1953 to find a solution to Japan's serious sterling shortage and to discuss renewal of the Sterling Payments Agreement, which was due to expire at the end of the year. The negotiations were finalised on 29 January 1954 with the Payments Agreement being extended for one year. A Trade Plan was set out to secure expansion of Japan's sterling exports, which had dropped considerably since the previous year. The Trade Plan estimated Japanese annual exports to the United Kingdom at £14.5 million, to its colonies at £91.5 million, and to individual independent sterling area countries such as the dominions at £92.5 million. Imports from the respective parties were estimated at £16 million, £32.5 million and £135 million. The Plan was expected to contribute towards offsetting Japan's sterling deficit of £109 million during 1953.  

It was doubtful, however, whether the Anglo-Japanese Trade Plan would be effective in improving Japan's serious sterling shortage. Although the United Kingdom and its

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Ei Boeki nitsuite' [The next stage of Anglo-Japanese trade], *Tosho*, no.72, May 1953, pp.9-15; Kyoichiro Matsuo (Deputy Director, International Trade Bureau), 'Yushutsu Fushin no Gen'in to Sono Taisaku' [Causes of stagnant exports and its remedies], *Tsusho Sangyo Kenkyu*, July 1953, pp.11-15.


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colonies agreed to issue import licences for Japanese goods up to the amounts prescribed in
the Plan, the figures for independent sterling area countries were merely estimates. Thus,
no guarantee was given that these countries, which accounted for almost half of total
estimated Japanese exports in the Trade Plan, would also relax import licensing.
Furthermore, exports to these destinations seemed to be overestimated, with the figures
inflated from the 1953 record by 70 per cent.\footnote{Ibid., pp.4-5.} Unless the independent sterling area
countries, including Australia, were prepared to open their markets to Japanese goods,
Japan could not hope for much improvement in the sterling balance. The president of one
firm in the textile industry, which had suffered a sharp drop in sterling exports, strongly
advocated further negotiations with the independent sterling area countries.\footnote{Kojiro Abe (President, Toyo Spinning Company), ‘Nichi-Ei Boeki Shiharai Kyotei to Pondo Boeki
Tenkai ni tsuite’ [On the Anglo-Japanese Payments and Trade Agreement and the development of
sterling trade], Keizaijin, vol.8, no.4, April 1954, p.10.}

While Japan entered into trade talks with several sterling area countries, Australia was
by far the most important target of its diplomatic efforts.\footnote{The Trade Arrangements were concluded with Pakistan in April and with Burma in December 1953.} Table 9.3 clearly shows the
salience of Australia’s tight import restrictions against Japanese goods. Australia was by far
Japan’s largest supplier within the sterling area in 1953, when Japan was slow in regulating
its imports for the reasons already explained. On the other hand, Japan’s exports to
Australia had fallen by two-thirds over the 1952 figure. As a result, Australia’s share in
total imports of Japanese goods by the whole sterling area in 1953 shrank to only 2.8 per
cent. These figures indicate how tightly Australia imposed import controls on the inflow of
Japanese goods. The resultant Japanese bilateral trade deficit of $163 million (£58 million)
accounted for more than half of Japan’s total deficit in sterling trade in that year.

Japan’s first diplomatic approach to Australia was made in November 1952. On this
occasion the Japanese Ministry of Foreign Affairs simply tried to draw Canberra’s attention
to Japan’s concern about Australia’s tight import restrictions, taking the opportunity to
express Japan’s appreciation for the long-term barley purchase contract, as already
explained in Chapter 8. In 1953, Japanese diplomatic approaches shifted in tone, to reflect
the growing seriousness of the sterling shortage problem.
Table 9.3  Japan's Trade with the Sterling Area Countries, 1953

(Unit: £ million)

<table>
<thead>
<tr>
<th></th>
<th>Exports</th>
<th>Imports</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>United Kingdom</td>
<td>33.1</td>
<td>49.1</td>
<td>−16.0</td>
</tr>
<tr>
<td>Aden</td>
<td>3.9</td>
<td>2.0</td>
<td>1.9</td>
</tr>
<tr>
<td>Hongkong</td>
<td>62.2</td>
<td>7.9</td>
<td>54.3</td>
</tr>
<tr>
<td>Malaya</td>
<td>7.4</td>
<td>50.4</td>
<td>−43.0</td>
</tr>
<tr>
<td>Singapore</td>
<td>32.1</td>
<td>13.0</td>
<td>19.1</td>
</tr>
<tr>
<td>Nigeria</td>
<td>11.6</td>
<td>0.2</td>
<td>11.4</td>
</tr>
<tr>
<td>East Africa</td>
<td>0.9</td>
<td>4.7</td>
<td>−3.8</td>
</tr>
<tr>
<td>Australia</td>
<td>9.0</td>
<td>172.3</td>
<td>−163.3</td>
</tr>
<tr>
<td>Ceylon</td>
<td>13.9</td>
<td>2.2</td>
<td>12.7</td>
</tr>
<tr>
<td>Burma</td>
<td>33.1</td>
<td>50.2</td>
<td>−17.1</td>
</tr>
<tr>
<td>India</td>
<td>27.4</td>
<td>75.1</td>
<td>−47.7</td>
</tr>
<tr>
<td>Pakistan</td>
<td>14.9</td>
<td>108.0</td>
<td>−93.1</td>
</tr>
<tr>
<td>New Zealand</td>
<td>1.4</td>
<td>9.8</td>
<td>−8.4</td>
</tr>
<tr>
<td>South Africa</td>
<td>28.2</td>
<td>19.6</td>
<td>8.6</td>
</tr>
<tr>
<td>Others</td>
<td>38.3</td>
<td>38.1</td>
<td>0.2</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>317.4</td>
<td>602.6</td>
<td>−284.8</td>
</tr>
</tbody>
</table>


In a Note Verbale dated 12 May, the Japanese government requested relaxation of Australia's import restrictions, pointing out that Japanese exports to Australia during the second half of 1952 amounted to only one-tenth of its imports from Australia. Despite the soft currency settlement agreed to in the Sterling Payments Agreement and the rapid improvement in its balance of payments, Canberra had imposed tight import restrictions against Japanese goods since March 1952, maintaining Japan's treatment as a hard currency source. Hence, Japan issued a warning that it might be forced to 'taper off her imports from the Sterling Area', unless the downward trend of Japanese exports improved dramatically.48 This document indicates that Australia's hard currency treatment of Japanese imports was singled out as a target of the Japanese diplomatic approach to Canberra.

Australia's initial response to Japan's harsher request was a gradual and small scale relaxation of import licensing. In July 1953, Canberra replied that it had implemented

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partial moderation of import licensing on Japanese goods in January–March and in April–June quarters and that it was prepared to issue licensing on 24 items including cotton piece goods. However, the Australian government asserted that this relaxation was the maximum possible concession and found no necessity to agree to informal trade talks as the Japanese had proposed.49

Canberra's approach was based on the assumption that Japan was bluffing in threatening to curtail purchases from Australia. At the end of August, MITI issued an official statement setting out the Japanese intention to reduce purchases of Australian wool during the period from October to March and to increase imports of Argentinian wool. This was the first time that the Japanese government specifically referred to a diversion of wool imports from Australia to Argentina. Canberra regarded the statement as giving 'only a preliminary indication' of the Japanese intention, in view of MITI's previous policy of not imposing restrictions on imports from the sterling area as a measure to improve the trade imbalance.50 However, the MITI statement was timely, and Canberra soon decided to increase the total amount of import licences issued for Japanese goods from £12 million to £18 million annually, and to widen the range of items to be licensed.51 Australian government officials were clearly concerned that Japan's sterling shortage could affect Australia's wool sales.52

Since these corrective measures included neither Japan's soft currency treatment nor an increase in exports, the Japanese government again requested a relaxation of import licensing in stronger terms in November. Tokyo argued that Japan's bilateral deficit with Australia from January to August was almost equivalent to the decrease in its sterling balance during the same period. Now that Australia's import restrictions had proved to be the largest single factor affecting Japan's serious sterling shortage, the Japanese government did not hesitate to warn Australia:

... the Japanese Government fear that unless measures be expeditiously taken on the part of the Australian Government of arresting the deteriorating tendency, the

49 Australian Embassy in Tokyo to MFA, 'Note Verbale', no.131, 22 July 1953, *ibid.*, pp.5-10.
51 Cabinet Minute, Australia, 'Trade with Japan', Decision no.833, Submission no.542, 2 September 1953, *ibid.*
52 Cable from Canberra to the Australian Embassy in Tokyo, no.368, 14 September 1953, *ibid.*
Japanese Government might find itself unable to continue imports from Australia on the pace and scale as in the past periods.53

Although the May warning had referred to the possibility of decreasing purchases from the entire sterling area, this time Japan did not conceal its intention to specifically target Australia.

CURTAILMENT OF JAPANESE PURCHASES OF AUSTRALIAN WOOL

The Japanese meant what they said. From 1953 to 1954, Japan introduced measures to divert imports from the sterling area to other non-dollar areas. Combined with the effects of Japan’s financial restraints, these measures caused Australian sales to Japan to fall. Wool, which was the main trading item not only in Australia-Japan bilateral trade but also in Japan’s entire sterling trade, was worst affected.

After the Japanese import trade system was handed over to private channels in January 1950, Japan’s wool purchases were regulated by the foreign currency allocation system. From September 1951, the sterling accumulation had raised the allocation of the foreign currency budget to imports of wool from the sterling area, and Japanese wool importers rushed into the Australian market. As a result, Japanese wool purchases in 1952 not only almost doubled those in 1950, but the Australian share reached its prewar level of 85 per cent. Active Japanese purchases led Australian officials to observe that the Japanese presence at wool auctions sustained market prices and that Japanese bidding had become an important factor in wool price setting for the first time in the postwar period.54

Although the downward trend in Japan’s sterling balance from late 1952 did not affect its total wool imports in 1953, Japan gradually began to squeeze out Australian wool. Table 9.4 shows that total wool purchases in 1953 actually increased by 23 per cent over the previous year. At this stage Japan’s foreign currency allocation had not been affected by the sterling shortage, reflecting its trade policy of securing an adequate supply of raw materials. Yet purchases from Australia were kept at almost the same level as in 1952. Most of the increase in total wool imports came from Argentina. In 1954, Japan’s

54 J.G. Crawford, Secretary, DCA to Commercial Counsellor, AM, 3 April 1952, AA, A609, 317/20/6.
deflationary policy and the reduction in its foreign currency budget, together with the abundant wool stock acquired in the previous year, lowered its total purchases by 13 per cent. Australia was hardest hit, with wool sales falling by nearly 30 per cent. Its share in Japanese wool imports plunged to 62 per cent, the lowest since 1948 when the Draper coordination system was introduced. Argentinian wool was also cut, but by the average ratio of 13 per cent.

<table>
<thead>
<tr>
<th>Year</th>
<th>Aust</th>
<th>%</th>
<th>NZ</th>
<th>SA</th>
<th>Arg</th>
<th>Urg</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>34–36</td>
<td>56,156</td>
<td>84.4</td>
<td>3,703</td>
<td>3,009</td>
<td>1,692</td>
<td>984</td>
<td>66,540</td>
</tr>
<tr>
<td>1947</td>
<td>728</td>
<td>96.6</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>754</td>
</tr>
<tr>
<td>1948</td>
<td>7,276</td>
<td>42.1</td>
<td>41</td>
<td>1,948</td>
<td>7,115</td>
<td>423</td>
<td>17,268</td>
</tr>
<tr>
<td>1949</td>
<td>18,840</td>
<td>74.9</td>
<td>2,845</td>
<td>3,151</td>
<td>0</td>
<td>0</td>
<td>25,140</td>
</tr>
<tr>
<td>1950</td>
<td>49,491</td>
<td>83.4</td>
<td>2,015</td>
<td>1,459</td>
<td>1,743</td>
<td>3,387</td>
<td>59,339</td>
</tr>
<tr>
<td>1951</td>
<td>121,042</td>
<td>61.7</td>
<td>9,758</td>
<td>1,832</td>
<td>16,505</td>
<td>4,237</td>
<td>196,121</td>
</tr>
<tr>
<td>1952</td>
<td>118,034</td>
<td>85.1</td>
<td>2,891</td>
<td>9,302</td>
<td>1,933</td>
<td>1,620</td>
<td>138,664</td>
</tr>
<tr>
<td>1953</td>
<td>128,229</td>
<td>75.6</td>
<td>3,733</td>
<td>14,487</td>
<td>24,079</td>
<td>10,119</td>
<td>169,597</td>
</tr>
<tr>
<td>1954</td>
<td>92,058</td>
<td>62.6</td>
<td>1,842</td>
<td>6,073</td>
<td>20,736</td>
<td>5,850</td>
<td>147,065</td>
</tr>
<tr>
<td>1955</td>
<td>122,351</td>
<td>80.1</td>
<td>3,624</td>
<td>8,547</td>
<td>10,326</td>
<td>3,814</td>
<td>152,671</td>
</tr>
</tbody>
</table>

**Notes**: a: Australia; b: Australia’s share in the total Japanese imports; c: New Zealand; d: South Africa; e: Argentina; f: Uruguay; g: Annual averages, 1934–36.

**Source**: Tsushosangyosho Tsushokyoku Tsushochosaka, 1956, pp.262-263.

The increase in imports of Argentinian wool was a purposeful act by the Japanese government. Interventionist measures had been ruled out in view of the unfavourable effects these might have on the industrial rationalisation program. Import restrictions could cause a shortage of raw materials, thus strengthening inflationary pressure and contradicting the principles of freer trade under the Bretton-Woods system. With options limited, Japan

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55 Australia’s low share in 1951 did not reflect the actual shape of Japanese wool imports. Australia’s share in quantity amounted to 73.5 per cent from September 1950 to August 1951, and 86.9 per cent from September 1951 to August 1952. Thus Australia’s 61.7 per cent share in terms of value seems to have been caused by higher prices from other sources, particularly Argentina. The poor crop due to the drought in 1951 and the introduction of sales tax and floor prices on wool exports by the Argentinian government tended to push Argentinian wool prices above international market prices by 25 per cent. *Kanematsu Yomo Nempo*, no.21, 1951-52, pp.334-337.
was, in fact, not averse to diverting purchases from the sterling area to other sources which were prepared to import more Japanese goods. In fact, one MITI official — and MITI had been the strongest advocate for maintaining the overall import level — supported diversion of purchases from the sterling area into the open account countries as the handiest and most appropriate remedy for the sterling shortage. This, it was argued, might strengthen Japan’s bargaining position in trade talks with the individual sterling area countries, particularly suppliers of commodities such as Australia.  

In order to promote diversion of wool purchases into the open account sources, Japan concluded a new Trade Arrangement with Argentina in April 1953. This included a Trade Plan outlining a $20 million Japanese wool purchase for that year. Although purchases of Argentinian wool did not increase as expected due to price hikes, Japan and Argentina entered into a barter arrangement in September, the so-called ‘combination deal’ contract, in which the two countries were to exchange $40 million worth of wheat and wool for the equivalent amount of steel. Argentina also agreed to apply a preferential exchange rate, which would have the effect of lowering the purchase price of dearer Argentinian wool. The merit of increased wool purchases from Argentina did not lie in the quality and price of its wool but in the export opportunities for Japanese steel. With the deteriorating balance of payments position, Japan desperately needed export contracts. In fact, from August, MITI intensified the link system whereby a certain export achievement in woollen products was required when a producer applied for foreign currency to finance purchases of raw wool. In this context, Argentina remained the ‘sole promising market which was left for Japan under the bleak reality of stagnant exports’. As a result, Argentina emerged as the largest customer of Japanese steel in terms of quantity in 1953. With another ‘combination

57 Toshio Nakamura, Tsunsansho Tsushokyoku Dai 2-ka [Second Division], ‘Nichi-A Shintosho Kyotei ni tsuite’ [On the new Japan-Argentina Trade Arrangement], Gaikoku Kawase, no.73, 1 June 1953, pp.39-40.
59 Kanematsu Yomo Nempo, no.23, 1953-54, pp.267-269. The link system was not welcomed by the woollen industry, since it tended to promote exports at discounted prices, which squeezed the financial conditions of the mills.
60 Nakamura, 1953, p.41.
deal' concluded in May 1954, Argentina consolidated its position as Japan's largest steel export market in 1954–55.  

The Japanese wool textile industry had mixed feelings about the diversion of wool imports to Argentina. Despite the application of the preferential exchange rate, Argentinian wool was expensive and its quality poor. However, the wool textile industry was in a position where it could not justify increased allocation of the foreign currency budget. Japanese wool textiles were traditionally produced for domestic consumption, although the industry depended on overseas supply for most raw materials. Moreover, Manchuria and Korea, the largest export markets in the prewar period, had been virtually closed. Although the wool industry expressed its strong dissatisfaction, it had no alternative but to accept the curtailment of wool purchases from Australia. To maintain their operation level, the wool mills were forced to utilise available raw wool, however coarse its quality. The mills concentrated their efforts on research into Argentinian wool, which they found was fit for production of yarn for hand-knitting. Ultimately, the leaders of the industry acknowledged the benefits of the 'combination deals' with Argentina.  

The Japanese diversion of wool imports alarmed Australian government officials. C.J. Carne, Australian Commercial Counsellor in Tokyo, reported the Japanese move to Canberra:

> The Japanese seem prepared to adopt almost any device which will gain trade–barter, triangular deals, incentive schemes, link systems, permission to traffic in licences, etc ... Whatever the reasons, Australia has made little effort to redress the imbalanced trade between herself and Japan and the latter cannot be expected to be patient for ever.

J.G. Crawford, Secretary of the Department of Commerce and Agriculture and one of the architects of the 1957 Commerce Agreement, shared Carne's alarm at the further curtailment of wool sales to Japan. He was particularly concerned about the effect of falling prices, which might cause a reversal in Australia's balance of payments. Crawford outlined

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62 Miyoji Ueno, ‘Gemmo Yunyu Seigen to Keseihin no Kyoko Yushutsu nitsuite’ [The import restrictions on raw wool and the forced exports of woollen products], *Yomo*, September 1953, pp.8-10; Renzo Ito, ‘Gemmo no Yunyu Yokuatsu wa Gusaku’ [The import regulation of raw wool is folly], *Yomo*, November 1953, pp.7-8.
his determination to press the government for remedial action. Crawford was also mindful of the total Japanese embargo placed on Australian wool in 1936 in retaliation for its Trade Diversion Policy, which had adopted higher tariffs on Japanese cotton and artificial silk piece goods. He advised his Minister, ‘[O]n our pre-war experience Japan might be expected to react against discriminatory trade measures, if she had opportunities of doing so, by turning to other sources of supply’.

In the event, Australia made a decision important in the history of the postwar Australia-Japan trade relations in November 1954. On 17 November, the Australian government conveyed its readiness to enter into trade talks with Japan. More significantly, two days later, Canberra announced the relaxation of import licensing. Japan was given soft currency treatment with the exception of 36 items, including cotton and artificial silk piece goods and toys. This was an important breakthrough in postwar trade between Australia and Japan. From March 1952 to February 1960, Australia’s control of import trade had been implemented mainly by import licensing under the discretion of the Department of Trade and Customs, in order to safeguard the balance of payments. Although the government said that import licensing was a temporary measure, its effect on domestic industrial protection was more profound than that of tariffs. The granting of soft currency status heralded a near normalisation of Australia-Japan trade relations, with Japanese goods enjoying virtually the same treatment as those from the United Kingdom and other sterling area countries in Australia’s import controls.

The success of the Sterling Payments Agreement in expanding sterling trade under the multilateral settlement system further committed Japan to a strategy to promote trade on a normal commercial basis, more multilaterally, without dependence on extra dollar supply. Even in the event of the serious sterling shortage caused by the tightening of import licensing by the sterling area countries in 1953, Japan was slow to restrain its imports from the sterling area, since commodities from this source were cheap enough to sustain

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65 Crawford to Carne, 8 April 1954, ibid.

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production of Japanese goods at competitive prices. The government strategy was to strengthen the competitiveness of Japanese industries, especially by rationalising the heavy and chemical sectors. This left the government little alternative but to introduce deflationary policies and measures for export promotion through the export-import link system, when faced with the crisis in the balance of payments of late 1953.

This situation highlighted the significance of economic diplomacy for Japan, which had to persuade the sterling area to relax import restrictions immediately. The huge bilateral trade deficit with Australia and Australia's discriminatory treatment of Japan in import licensing became the most significant target of Japan's diplomatic efforts. As the financial measures introduced to reduce Japan's overall imports took effect, MITI made several attempts to divert wool purchases away from Australia, as illustrated in the 'combination deals' with Argentina. Australia's concern motivated Canberra's decision to remove the discriminatory treatment against Japanese goods in import licensing in November 1954. This decision released Australia and Japan from the tight exchange controls which had constituted the main barriers to trade under the postwar worldwide dollar shortage. It was in Australia's own best interest to secure Japanese export markets by showing a positive response towards consolidation of Australia-Japan trade relations developed under the Sterling Payments Agreement. The scene was set for bilateral trade relations to flourish between the two countries. These developments paved the way for the conclusion of the Commerce Agreement between the two countries in 1957.
10 The Role of Australia in the Evolution of the Postwar Japanese Trade Strategy and the Commerce Agreement of 1957

At the outset of the postwar period, the US occupation authority and the Japanese government faced the enormous task of bringing the war-devastated Japanese economy back on a path towards economic recovery and self-reliance. Policy options were considerably circumscribed by the international circumstances. The Cold War severed Japan’s commercial links with its traditional export markets and sources of raw materials and foodstuffs on the Chinese continent. A serious dollar shortage prevailed all over the world. As a result, many countries maintained tight import controls to safeguard their foreign currency positions, despite the establishment of an institutional framework for freer international trade and payments under the Bretton-Woods system. Although the Korean War Boom provided Japan with enormous revenue in the shape of special procurement, US aid was curtailed in the early 1950s and Japan could not count on extra dollar supply through the US strategic aid to Southeast Asia.

The Sterling Payments Agreements gave Japan the opportunity to pursue economic self-reliance through a trade strategy based on promoting trade with non-dollar countries on a commercial basis. The sterling area countries actively demanded Japanese manufactured goods, especially those in short supply due to insufficient production in the United Kingdom. The mechanism for multilateral settlement of Japan’s sterling trade minimised the restrictive effects of exchange controls, since the sterling area countries were allowed to purchase Japanese goods through payment in sterling. The resultant sterling surplus enabled Japan to finance its procurement of important raw materials and foodstuffs from Australia. At the same time, Australia’s huge bilateral trade surplus with Japan was transferred to the other sterling area countries, giving them extra purchasing power to buy Japanese goods. In this sense, Australia played a pivotal role in sustaining and expanding Japan’s sterling trade under the worldwide dollar shortage of the postwar period.
The Japanese, however, did not at first fully appreciate the importance of sterling trade and Australia in the re-establishment of postwar commercial networks. As pointed out in Chapter 2, the Japanese wanted to restore traditional trade relations with the Chinese continent and saw this as the key to the recovery of the Japanese economy. The intensification of the Cold War in Asia along with the birth of Communist China and the outbreak of the Korean War virtually closed Japan's traditional commercial networks with East Asia. The Japanese response to the loss of Chinese trade was two-fold. Some academics thought that the international environment was so problematic that they advocated concentrating on the development of domestic resources. Government and business circles wished to promote dollar based trade, with US assistance. US strategic aid would, they hoped, link Japan's production capacity with the economic development of non-Communist Southeast Asian countries, consolidating these countries as alternatives to traditional East Asian export markets.

US policy in the Japanese occupation prevented Japan from carrying out either of these plans. Although its goal shifted from Japan's democratisation and de-militarisation to economic recovery after 1948, the US administration also began to emphasise the necessity for Japan to become economically self-reliant. In 1949, austere financial and fiscal measures were introduced, as advocated by the Dodge Line. This meant that Japanese industry could no longer rely on government subsidies, without which the strategy for domestic economic development was not feasible. Although the US-Japan Economic Cooperation Program raised Japanese expectations of US strategic aid in 1950–51, the US administration was not prepared to inject extra dollars into the Japanese economy. US appropriated funds for the Japanese occupation were reduced. Under US pressure, Japan was forced to abandon its attachment to the renewal of traditional Chinese trade and to the strategy for domestic economic development. US determination to withhold economic aid shattered the strategy to develop Japanese trade networks based on extra dollar supply of a non-commercial nature, such as US strategic aid to Southeast Asia. Japan had no alternative but to promote trade on a more multilateral basis. It dealt not only with the dollar area but also with non-dollar area countries that had the capacity to supply foodstuffs and raw materials essential to economic recovery and that were in return prepared to
purchase unsubsidised Japanese goods on a commercial basis, through expansion of the network of bilateral trade and payments agreements.

Since international trade had stagnated as a result of the dollar shortage, the promotion of trade on a more multilateral basis provided a solution in moderating the restrictive effects of bilateral trade and payments agreements. As Chapter 3 illustrated, the purely bilateral trade arrangement was least effective in the case of Australia-Japan trade, since Japan was constantly short of foreign currencies to finance its procurement of Australian wool. This predicament resulted in the diversion of Japanese wool purchases to non-Australian sources under the Draper coordination system during the occupation period. Although the Overall Sterling Payments Agreement was concluded in May 1948 to facilitate trade through the introduction of a multilateral settlement system in soft currency between Japan and the whole sterling area, growth of Japan’s sterling trade was seriously hampered, as pointed out in Chapter 4. SCAP officials adopted a restrictive approach to financing purchases from the sterling area, in order to minimise a dollar drain through active purchases by the sterling area of essential Japanese goods which were produced from dollar-imported raw materials. The Overall Payments Agreement almost broke down when some SCAP officials wanted to convert sterling funds into dollars on the eve of the devaluation of the pound sterling in September 1949. It was General MacArthur’s highly political decision to maintain Japan’s commercial links with the sterling area that prevented the conversion from taking place.

The Logan Plan was introduced to expand trade by broadening the networks of bilateral arrangements. It was in this context that the Sterling Payments Agreement increased in significance. Chapter 5 indicated SCAP’s increasing interest in diverting of Japanese purchases of foodstuffs and raw materials from the dollar area into the non-dollar area, in the face of the downward trend in US appropriated funds for Japan. SCAP looked to the sterling area for increased procurement of commodities in the negotiations for the Sterling Trade Arrangement of 1949/50. Australia was expected to become the main supplier of raw wool, wheat and barley within the sterling area, since other sterling area countries still lacked sufficient quantities of commodities. Without Australia’s supply capacity, Japan’s sterling trade would have resulted in an excessive accumulation of sterling,
which might have justified dollar conversion by SCAP. In this case the overall level of Japanese sterling trade would have been drastically curtailed.

As the significance of the sterling area for Japan's economic recovery was recognised, SCAP's focus in sterling trade shifted from rigid exchange controls to avoid a dollar drain to the liberalisation of trade relations. As mentioned in Chapter 6, SCAP attempted to revise the Sterling Trade Arrangement of 1950/51 in line with GATT principles of most-favoured-nation treatment and non-discrimination. Due to Japan's healthy dollar position after special procurement during the Korean War, SCAP did not object to swapping dollars to cope with seasonal sterling shortages. SCAP also insisted on freer transfer of its sterling funds in the 1950/51 sterling trade negotiations. Its intention was to promote Japan's sterling trade further on a more multilateral basis, utilising sterling funds earned from the participants in the Sterling Trade Arrangement for extensive procurement of commodities from such non-participants as Burma and Pakistan. Once SCAP made a commitment to promote Japan's sterling trade on a freer, multilateral basis, it no longer persisted in maintaining tight exchange controls on sterling funds, and it became receptive to the British proposal for removal of the dollar convertibility clause from the Overall Payments Agreement.

In sharp contrast with SCAP's liberal approach to sterling trade, the Japanese government showed a strong desire to retain the dollar convertibility clause, when they took over negotiating power from SCAP for a new Sterling Payments Agreement in 1951. As shown in Chapter 7, Japanese officials were seriously concerned about excessive accumulation of unusable sterling. The Japanese approach indicates that the government attached importance to maintaining a sound dollar position so that Japan could impose controls on outflows to the sterling area of essential export goods, most of which had been produced from raw materials obtained through dollar payment. The Japanese hoped to integrate Japan with the dollar area, and they considered the possibility of classifying Japan as an American Account country in Britain's import licensing system. This idea was contemplated on the assumption that Japan could still count on extra dollar supply from US strategic aid to Southeast Asia under the US-Japan Economic Cooperation Program. However, the strategy broke down when the US administration did not proceed with the aid program. The Japanese government was further compelled to agree to the removal of the
dollar convertibility clause for political reasons; it needed to conclude the new Sterling Payments Agreement by the end of August 1951, in time for the opening of the San Francisco Peace Conference in September.

The 1951 Sterling Payments Agreement was an important landmark in the evolution of the Japanese trade strategy in the post Peace Treaty period, in that the Japanese government, which strongly preferred dollar based trade, had nevertheless to pursue expansion of trade networks on a more multilateral basis as a result of the removal of the dollar convertibility clause. Within the Japanese government, the Ministry of International Trade and Industry and the Ministry of Foreign Affairs accepted the need to follow this trade strategy: they favoured further diversion of commodity procurement to sterling suppliers as a remedy to the excessive accumulation of sterling, as pointed out in Chapter 8. Although the Japanese Foreign Exchange Control Board tried to push the case for maintaining tight exchange controls to ensure a sound foreign currency position, its proposal for drastic restraints on exports to the sterling area was turned down in February 1952, when MITI and the MFA intervened. Government leaders were concerned about the effects of arbitrary adoption of restrictive trade and exchange control measures, in view of Japan’s commitment to a freer international trade system as provided for by the IMF and the GATT.

Under the strategy for trading on a more multilateral basis, Australia’s capacity as the most important commodity supplier within the non-dollar area was again highlighted. The Japanese proposal for extensive procurement of such strategic commodities as wheat, sugar and iron ore indicated that Japan began to look seriously to Australia as an alternative supplier to North America. In fact, Japan entered into a long-term contract to purchase Australian barley in November 1952, in order to secure a stable commodity supply from this source. Trade with Australia also helped Japan consume its huge sterling surplus, persuading government officials of the feasibility of a policy of not adopting drastic export control measures, as advocated by the FECB.

Once the government was committed to promotion of trade on a more multilateral basis, it became imperative for Japan to achieve economic self-reliance through self-help initiatives in the industrial sector. Although the government focused on promotion of heavy and chemical industrial exports to non-Communist Asian markets as a long-term objective
of Japan’s trade policy, those sectors which had flourished on windfall profits achieved through US special procurement had to undergo rationalisation before they could compete on a commercial basis with their counterparts in other industrialised countries. The need to proceed with further industrial rationalisation was recognised when Japan faced a balance of payments crisis in 1953–54; inflationary pressure since the Korean War Boom had weakened the competitive edge of Japanese industry. The government could not resort to arbitrary import restrictions to safeguard the balance of payments, because interventionist measures would affect Japan’s industrial competitiveness and would be contradictory to the principles of freer international trade. The government thus had no alternative but to introduce austere financial and budgetary restraints in late 1953.

As discussed in Chapter 9, it was in this context that economic diplomacy came to play a significant role in the liberalisation of Japan’s trade relations. Once interventionist measures were ruled out, Japan could expect an immediate increase in its exports only if trade barriers against Japanese exports were minimised through diplomatic approaches. While the Japanese government succeeded in concluding treaties and/or agreements of commerce and navigation with several countries, including the United States and Canada during the first half of the 1950s, it was economic diplomacy towards the sterling area countries that was significant in overcoming the crisis in the balance of payments in 1953/54. The sterling area countries intensified their import licensing against Japanese goods in March 1952, to safeguard their balance of payments. These measures resulted in a serious sterling shortage, which in turn triggered a crisis in Japan’s foreign currency position. With the dollar shortage, import licensing had far more restrictive effects than tariffs as a trade barrier. Since the 1951 Sterling Payments Agreement made it unnecessary to set up a forum for collective adjustment of the annual trade volumes between Japan and the sterling area countries as in the previous Sterling Trade Arrangements, Japan had to make diplomatic approaches in order to ameliorate its sterling trade deficit with the United Kingdom and with other British Commonwealth countries.

Australia was selected as the most important target of Japanese economic diplomacy to improve its sterling shortage, since it recorded the largest bilateral trade surplus with Japan among the sterling area countries. In particular, Canberra maintained discriminatory classification of Japan as a hard currency source in its import licensing system, despite the
removal of the dollar convertibility clause from the Sterling Payments Agreement. As a result, Japan recorded a huge bilateral trade deficit with Australia, aggravating its sterling shortage. In its diplomatic approach to Canberra, Tokyo called for a relaxation of import restrictions against Japanese goods, and threatened to cut its purchases from Australia. Shortly afterwards, the Japanese government attempted to divert procurement of raw wool away from Australia to South America. In November 1954, Canberra announced its decision to give Japan soft currency treatment in import licensing, virtually eliminating discriminatory trade barriers against Japanese goods for exchange control purposes. Japan’s active diplomatic approaches towards Canberra and the ensuing positive outcomes from the November 1954 decision indicate the significance of liberalisation of bilateral trade relations with Australia, as Australia proved important not only as a commodity supplier but also as an export market.

In fact, Australia’s November 1954 decision was the landmark in opening the Australian market for Japanese industrial exports and acted as a harbinger of the Commerce Agreement. While Canberra responded positively to the Japanese diplomatic approach for relaxation of tight import licensing, at the same time the Australian government wished further to consolidate the freer bilateral trade relations developed under the Sterling Payments Agreement. On 17 November, two days before the announcement of the relaxation of import licensing against Japanese goods, Australia’s Minister for External Affairs expressed willingness to enter into talks ‘to examine mutual trade problems’. While the Australian government made it clear that it wanted to ‘reserve its position’ on Japan’s membership of the GATT, it admitted that ‘the proposed trade talks with Japan would bear the G.A.T.T. position in mind’. This signified that Australia was prepared to discuss overall trade relations with Japan, including the GATT problem. In fact, after the November 1954 decision, Australia took the initiative in developing freer bilateral trade relations with Japan, eventually by the conclusion of the 1957 Commerce Agreement.

The Japanese were reserved in their response to Australia’s offer. As pointed out in Chapters 8 and 9, the Japanese government had raised the GATT issue in the negotiations for the 1951 Sterling Payments Agreement and the subsequent review conference in 1952.

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The sterling area countries, including Australia, had tried to evade the issue by saying that they would discuss it in the formal GATT forum rather than in the payments negotiations with Japan. But when Japan's sterling balance deteriorated in 1953, Japan began to focus on the problem of tight import licensing by the sterling area countries. In diplomatic approaches towards Australia during 1953, the Japanese specifically targeted Australia's discriminatory import licensing and Japan's soft-currency treatment, while proposing informal trade talks with Australia. They were so much concerned about the sterling shortage that they no longer referred to the GATT and other trade issues. This lack of reference to overall trade problems with Australia may be interpreted as a diplomatic tactic to allow both parties to concentrate on the urgent issue and avoid the broader, more complicated GATT issues.

As Rix points out, Japan's response to Australia's November 1954 offer to hold the long-awaited trade talks was 'deliberately understated'. In fact, in an official reply to Canberra which pointed out 'the lack of any concrete references' to Australia's proposal for trade talks, the Japanese government stated that it was difficult to determine Japanese attitudes towards the talks at that moment. With regard to the GATT question, Japan asked Australia only to give 'prompt and full support' to Japan's accession to the GATT. There was no sign of euphoria on the Japanese side about Australia's offer for trade talks to develop freer bilateral trade relations. One of the reasons for Japan's attitude may be that the Australian offer was made before Japan was formally admitted as a member of the GATT in September 1955. The Japanese government was concerned that Australia might make some additional requests in the proposed trade talks in return for its acceptance of Japan's accession. Any bilateral deal, prior to formal membership, to partly exempt Australia from its obligation to apply GATT rules to Japanese trade or to give some special treatment to Australia might have prejudiced Japan's status in the GATT. In fact, in its instructions to the Japanese Embassy in Canberra in August 1955, the Ministry of Foreign Affairs emphasised the need to avoid being forced to accept any extra requests from

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2 Rix, 1986, p.201.
Australia, reconfirming that the forthcoming trade talks should be of an ‘informal and noncommittal’ nature.\(^5\)

This cautious diplomatic approach continued until the opening of the negotiations for the Commerce Agreement. Even after Australia revealed its intention to retain GATT Article XXXV in the event of Japan’s formal membership of the GATT, Japan adopted a wait and see attitude. Japan did not dare to push the issue of Australia’s refusal to apply most-favoured-nation treatment to Japanese trade, even though an agreement between the two sides over opening the trade talks should have given Japan a good opportunity request the removal of Australia’s trade discrimination. It was Canberra that first expressed readiness to enter into negotiations for a formal trade agreement, in May 1956. Although Japan accepted the Australian offer, its response was not very enthusiastic. It proposed deferring the start of the negotiations until August on the grounds of ‘the pending talks with the United Kingdom and other governments on payments and trade matters’.\(^6\) My interpretation is that the Japanese government gave first priority to the ongoing payments negotiations with the United Kingdom as the key to Japanese trade with the overall sterling area, and therefore tried to avoid giving the British the impression that it was also making a backdoor deal with Australia. In fact, Japan did not hesitate to request elimination of the discriminatory treatment of Japanese goods under the Sterling Payments Agreement in its negotiations with Britain.\(^7\) As on the occasion of the 1936 Trade Diversion Dispute, Japanese officials may still have regarded Australia as just one member of the British Empire and therefore under British control, particularly in trade matters.

Only after Australia informally revealed in July 1956 its negotiation proposals, including the possibility of exchange of most-favoured-nation treatment with Japan, did the negotiations start moving. Both governments exchanged their respective requests in August and their respective initial reactions in October. At this stage, the Japanese government eventually raised its official request for Australia’s application of normal GATT provisions

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\(^7\) Tsushosangyo Shijo 1-ka [First Marketing Division], ‘Nichi-Ei Shihara Kyotei oyobi Boeki Torikime nituite’ [On the Anglo-Japanese Payments Agreement and the Trade Arrangement], Tshusho Chosa Geppo, no.70, April 1957, p.3.
to trade with Japan. In November, the formal negotiations for the Commerce Agreement were opened in Canberra between Australian officials led by Dr W.A. Westerman of the Department of Trade, and the Japanese delegates headed by Nobuhiko Ushiba who had returned to the Ministry of Foreign Affairs as Counsellor of the Minister’s Secretariat. Thus Australia’s strong initiatives encouraged the Japanese government to pursue liberalisation of Australia-Japan trade relations within the framework of bilateral negotiations for the Commerce Agreement.

Japan’s passive approach in the initial stages of the negotiations can be explained by the pessimism within government and business circles over the prospect of a trade deal with Australia. In his memoirs, Ushiba reveals that every other MFA official predicted possible breakdown of the Commerce Agreement negotiations. They hesitated to take on the hard task of negotiating with the Australians, and were concerned about strong anti-Japanese sentiment. But when he arrived in Canberra, Ushiba was much impressed with the ‘reasonable’ attitude of the Australian negotiators. Haruhiko Nishi, who served as Japan’s first postwar ambassador to Australia in 1952–55, confirms Ushiba’s observation about Tokyo’s feelings. With regard to Tokyo’s slow response to Australia’s positive offer for trade talks in 1954, Nishi explains that his Ministry was so concerned about anti-Japanese sentiment in Australia that its officials saw little prospect for the exchange of most-favoured-nation treatment with Australia, even on a conditional basis. Japanese businessmen shared the pessimism about marketing prospects in Australia, pointing out that Japanese sundry goods were sold in Australia without made-in-Japan labels because Australian retailers were concerned about the effect of anti-Japanese feeling. On the other hand, staff of the Japanese diplomatic mission in Australia recognised that Japanese commercial firms needed to make a more sustained sales effort, overcoming their pessimism about trade barriers in Australia.

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Given Japanese pessimism about the prospects of trade negotiations and export marketing, Australia’s generous offer to exchange most-favoured-nation treatment should have given the Japanese negotiators enormous confidence over future trade relations with Australia under the framework set out in the Commerce Agreement. Ushiba believes that this Agreement was an important turning point in developing friendly commercial relations with countries which had had a strong antipathy towards Japan.\textsuperscript{12} In fact, the Commerce Agreement with Australia set the precedent for Japanese economic diplomacy. It provided the pattern for normalisation of Japan’s relations with those GATT parties which discriminated against Japan based on Article XXXV, with Japan negotiating bilateral agreements which provided for selective import controls in the case of a sudden surge of Japanese goods threatening domestic industries.\textsuperscript{13} In this sense, Australia’s offer raised Japanese expectations when negotiating trade on a more multilateral basis with the remaining 12 GATT signatories still applying Article XXXV. In March 1958, the Japan Spinners’ Association noted that the Commerce Agreement had led to a remarkable increase in textile exports to Australia, and called for the cultivation of this important promising market with discretion and in a gradual manner without causing unnecessary alarm among the Australian people.\textsuperscript{14} Apart from its practical effects on export activities, the Commerce Agreement played an important role in boosting the confidence of Japanese government and business circles in Australian trade.

Australia’s initiative on the Commerce Agreement had another significant effect on the multilateralisation of Japan’s postwar trade with international trade networks. One of the aims of the Australian government in its proposal for exchange of most-favoured-nation treatment and non-discriminatory treatment was to facilitate access to the Japanese wheat market. Australia was concerned about Japan’s wheat import trade, which had largely been distorted by non-commercial factors, and wished to obtain the share of the Japanese market which Australia could expect if Japan’s purchases were ‘based purely on price and

\textsuperscript{12} Ushiba, 1984, p.96.

\textsuperscript{13} Article V of the Commerce Agreement provided waiver of each parties’ obligations such as the most-favoured-nation treatment as stipulated in Article I and non-discriminatory treatment in Article II, in case ‘unforeseen developments’ threatened to cause serious injury to domestic industries. The Commerce Agreement between Japan and Canada in 1954 also contains a similar emergency action clause, though, in more restricted terms.

quality.\textsuperscript{15} It was Japan’s purchases of surplus wheat from the United States that Australia regarded as an important target, since American surplus disposals prejudiced Australia’s commercial interest in Japanese trade. Any solution to this problem would force the Japanese government to make a choice between dollar-based trade with North America through the preferential surplus disposal agreement and trade on a non-discriminatory multilateral basis under the GATT.

The purchases of US surplus wheat started when the Japanese government concluded the Mutual Defence Assistance Agreement (MSA Agreement) in March 1954. As discussed in Chapter 8, the Yoshida government expected that the MSA Agreement would provide Japan with extra dollar supply to overcome the crisis in the balance of payments. Japan gave priority to US surplus wheat over normal wheat purchases on a commercial basis, bearing in mind the benefits of US defence support that would be obtained in return. The US surplus disposal arrangements were a product of Japan’s strong attachment to a dollar-based trade strategy arising from pessimism over the future of Japanese trade without the traditional Chinese commercial links and a sense of dependency on the generosity of the United States. The Japanese were not confident enough to commit themselves to more multilateral trade on a commercial basis through their own self-help efforts at export promotion.

In May 1955, Japan concluded another surplus disposal agreement based on the Agricultural Trade and Development and Assistance Act 1954 (US Public Law 480), under which it was to purchase US surplus wheat, barley and other commodities in the order of $85 million. In February 1956, Japan revised the agreement to purchase $66 million of US surplus commodities, including wheat. By the time formal negotiations for the Commerce Agreement started in Canberra in November, there had developed serious intra-governmental disputes over renewal of the surplus disposal agreement with the United States. If Japan was to open its market to Australian wheat to assist Canberra, it would have to abandon the surplus disposal program because domestic demand for wheat had fallen considerably due to the good rice crop in the previous year. There was strong opposition to the surplus disposal scheme from those who believed in the need to develop

\textsuperscript{15} Australia-Japan Trade Negotiations, ‘First Plenary Meeting Thursday 1st November, 1956’, Gaimusho Keizaikyoku Dai 4-ka, 1957, p.64. 

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more independent economic diplomacy and to achieve economic self-reliance without excessive dependence on the US surplus disposal program which forced dearer commodities on Japanese consumers. However, the Ministry of Agriculture and Forestry (MAF), led by its Minister, Ichiro Kono, lobbied strongly for the surplus disposal agreement, in order to promote its own program for strengthening domestic food production. The MAF tried to capitalise on the yen fund which was used to fund Japanese payments for US surplus commodities, to provide finance at low interest rates for domestic economic development projects such as the augmentation of power generation capacity through construction of dams. Kono succeeded in persuading the US administration into increased use of the fund for agricultural purposes in the February 1956 agreement. In the end, however, the Japanese government opted for the establishment of freer trade links with Australia, deciding not to renew the surplus disposal agreement in December.

From this perspective, the Commerce Agreement can be seen as a landmark through which Japan reconfirmed its commitment to trade on a more multilateral basis, setting aside other options. Akaneya argues that it represented the triumph of the international trade school over the domestic development school. As discussed in Chapter 2, with the Peace Settlement in sight, the domestic development school advocated the development of domestic resources financed by the introduction of foreign capital as the key strategy for the post-independence self-reliance of the Japanese economy. The MAF idea for increased food production through the use of the surplus disposal fund fitted with the argument of this school. In the early 1950s, Japan opted for the promotion of international trade through networks of bilateral payments and trade agreements, as it could not count on the US-Japan Economic Cooperation Program. As this thesis has argued, the Sterling Payments Agreement was the largest and the most important agreement which made this trade strategy feasible. Under the Agreement Australia's capacity to supply commodities played a pivotal role, by circulating purchasing power from Japan to other sterling area countries. The fact that the MAF proposal was set aside in preference to developing more liberal trade

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relations with Australia meant that once again the Japanese government had not favoured domestic development. By offering Japan an attractive deal on the exchange of most-favoured-nation treatment for the relinquishment of the surplus disposal program, Australia had thus encouraged Japan to confirm its commitment to a trade strategy based on multilateral dealings.

On 6 July 1957, the Commerce Agreement was officially signed. It took six months to finalise the negotiations, after the settlement of the US surplus disposal problem at the end of the previous year because the Japanese firmly opposed the Australian proposal for an emergency clause and the binding of Japan’s free custom duty on wool imports. Japan resisted the Australian proposal for insertion of the emergency clause on the grounds that it contradicted GATT principles prohibiting selective import control measures targeting a particular country. These matters were finally settled when Australia agreed to review retention of GATT Article XXXV within three years after the Agreement coming into effect.\(^{17}\) This established an important precedent in Japan’s economic diplomacy up to the mid 1960s. Moreover, the Japanese government developed its determination to introduce GATT principles into Australian trade, emphasising the abrogation of the right to invoke Article XXXV. This approach was in sharp contrast with the passive attitude Japan had adopted when Australia in the preceding years, had offered to open trade negotiations and had proposed the exchange of most-favoured-nation treatment.

Japan’s commitment to bringing its economy into the freer international trade system under the GATT was in line with its growing confidence in economic self-reliance centred on self-help and trade on a more multilateral basis. The success in overcoming the crisis in the balance of payments in 1953–54 led the Economic Planning Agency to advocate further efforts for rationalisation and modernisation of production capacity, and to assert that the postwar period and ‘economic growth through reconstruction is over’ in the 1956 issue of its Economic White Paper.\(^{18}\) Gone was the early pessimism over the future of Japanese trade circumscribed by the loss of traditional Chinese markets, the decrease in US special procurement and the formation of international networks of trade barriers against Japanese exports. The bright prospects for the negotiations in Canberra boosted Japanese confidence

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17 Kajiki, 1957, p.36.
in the feasibility of normalising commercial relations with countries which retained Article XXXV, as they witnessed a positive response towards conclusion of the Commerce Agreement with Australia, which until then had adopted the toughest trade policies against Japan. It is no coincidence that in the first issue of *Diplomatic Blue Papers*, which was published two months after the conclusion of the Commerce Agreement, the Ministry of Foreign Affairs listed economic diplomacy to eliminate trade barriers against Japan as one of three diplomatic issues of immediate concern.

The 1957 Agreement triggered further liberalisation and expansion of Australia-Japan trade. The 1963 revision of the Commerce Agreement with Australia paved the way for an increase in Japan’s beef imports, in return for Australia’s formal abrogation of the right to invoke Article XXXV. The emergence of Australia as a major supplier of iron ore and coking coal contributed the diversification of Japan’s supply sources of strategic raw materials.

When US-Japan trade friction grew worse in the 1980s, the United States put strong pressure on Japan to improve American agricultural marketing opportunities through bilateral deals, even running the risk of infringing the principles of non-discriminatory treatment for other suppliers including Australia. It was Australia that called strongly for application of the GATT principles of non-discrimination in the US-Japan deals. As a result, in July 1988 the Japanese government finally agreed to the abolition of the quota system for beef and orange imports. Without Australia’s pressure the Japanese government might have preferred to make another bilateral deal with the United States to increase the existing US quotas. The proposal by the Australian Prime Minister, Bob Hawke, for the Asia Pacific Economic Cooperation (APEC) meeting in January 1989 can be interpreted as another attempt by Australia to entice Japan further towards commitment to the multilateral trading system.

As more diplomatic archival documents covering these issues are released, further studies of postwar Australia-Japan trade relations will emerge. In analysing these issues, researchers need to bear in mind Australia’s role in the evolution of Japan’s trade strategy on a more multilateral basis, as discussed in this thesis. It will also be of interest to look into the evolution and consistency of Australia’s commitment to a freer, non-discriminatory international trade system under the GATT and, from this year, the World Trade
Organisation (WTO). Without Australia’s full commitment to this trade strategy, there would not have been such rapid restoration of the postwar commercial links between Australia and Japan, nor Japan’s ‘miracle’ of economic recovery and high growth, both of which were sustained by trade on a more multilateral basis.

Drysdale points out that one of the main architects of the Commerce Agreement and the postwar development of Australia-Japan trade relations, Sir John Crawford, recognised Australia’s commercial interests in accommodation of Japanese industrialisation into a system of ‘collective agreements’ for freer international trade, especially in the Asia-Pacific region, as early as the late 1930s. Crawford tried to establish commercial links with Japan as Secretary of the Department of Commerce and Agriculture and later the Department of Trade during the 1950s, exactly in line with his original idea. The fact that the Commerce Agreement was signed by the Minister for Trade and leader of the Country Party, John McEwen, and that the leader of the Opposition Party, H.V. Evatt, later opposed it may give the impression that the Agreement was designed to safeguard the interests of the rural sector at the cost of domestic industry and that the Labor Party and the trade were against economic rapprochement with Japan. H.C. Coombs, who played an important role in working out Australia’s postwar economic and trade policies as Director-General of the Ministry of Post-War Reconstruction under the Labor government during the 1940s, reveals, however, that the Prime Minister, Ben Chifley, impressed Coombs himself with his recognition of the need to ‘help the Japanese find an economic place for themselves in the world’ despite the political difficulties. Coombs also notes the Chifley government’s support for the freer international trade system under the GATT and the mutual understanding on this issue between Chifley and the then Opposition leader and later Prime Minister, Robert Menzies. Crawford himself argues that Australia’s postwar trade policy underwent a revolutionary change from that of prewar economic nationalism symbolised in the 1932 Ottawa Agreement to commitment to the multilateral trade system. Despite some changes from the early postwar period to the mid 1960s, the ‘international centre of trade

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policy interest and activity for Australia remains the General Agreement on Tariffs and Trade.\footnote{J.G. Crawford, 1968, p.610.}

These episodes suggest that there was steady bipartisan support for pursuing Australia’s commercial interests within the freer multilateral international trade system under the GATT, despite the fact that industrial protection was a key element in policies underpinning Australia’s political foundations until recently.\footnote{Paul Kelly, The End of Certainty: The Story of the 1980s, St Leonards, Allen & Unwin, 1992, p.2.} So the study of Australia’s postwar trade policy history (and the commitment by Labor governments in recent years to trade liberalisation) reveals continuity in Australia’s commitment to the multilateral trading system.

The 1957 Commerce Agreement had a strong impact on the Australian public, both positive and negative. Both the textile industry and the trade unions, for example, announced their opposition because of their grave concerns about the inflow of Japanese goods threatening their industrial future.\footnote{Crawford, 1968, pp.377-380.} The Agreement was warmly welcomed in Japan. The major Japanese newspapers welcomed increased trading opportunities and the improvement of relationships between Japan and Australia. At the same time, there was a chorus of warnings that Japanese export drives might cause serious damage to the newly established liberal institutional framework for Australian trade and might affect subsequent negotiations with other parties retaining Article XXXV.\footnote{Editorials; ‘Nichi-Go kanno Atarashii Tsusho Kankei’ [New trade relations between Japan and Australia], Asahi Shimbun; ‘Shin Jidai ni Haitta Nichi-Go Kankei’ [New era of the Japan-Australia relations], Nihon Keizai Shimbun; ‘Nichi-Go Tsusho no Shin Kido wo Sodateyo’ [Establish a new orbit for Japan-Australia trade]; all these editorials appeared on 7 July 1957.} Japanese trading circles understood the warning well, and they made efforts to conduct orderly marketing to Australia, especially of textile exports.\footnote{Bunroku Yoshino, ‘Goshu Gyokai no Doko: Tai-Go Yushutsu Kisei Mondai wo Megutte’ [Current situation of the Australian industry: On the issue of export restraint to Australia], Yushutsu Menshifu Geppo, vol.8, no.4, April 1958, p.15.} As a result, Australia grew to be the single largest market for Japan’s cotton piece goods in 1960–64. The establishment of these active but steady commercial networks bore fruit in the shape of the inaugural Australia-Japan Business Cooperation Committee in May 1963 and the complete normalisation of Australian-Japan trade relations through the conclusion of the revised Commerce
Agreement in August 1963. This consolidation of commercial links led Australia and Japan into a so-called ‘honeymoon’ period from the mid 1960s as the Japanese public eventually came to recognise Australia’s position in Japanese trade as the main supplier of strategic raw materials.

Despite the large volume of trade exchanged between the two nations since the early postwar period, Australia’s profile among the Japanese has remained relatively understated. Japan’s rapid economic recovery and self reliance came to be premised on a multilateral-based trade strategy, as the options of excessive dependence on the United States and development based on domestic resources were ruled out. Central to this strategy was the network of trade and payments agreements focused on the Sterling Payments Agreements before the mid 1950s and, subsequently, the freer multilateral international trading system under the GATT. Australia played a significant role in convincing the Japanese of the feasibility of this strategy, as the dynamo of Japan’s sterling trade at the time of dollar shortage, and by taking the initiative in establishing the liberal trade framework incorporated in the 1957 Commerce Agreement. Though understated, it appears that, in the postwar period, Australia has played a consistent role in strengthening Japan’s commitment to the multilateral trading system. The nature of Australia’s trade with Japan and both countries’ position in the international economy have promoted this role. This history of Japan’s trade relations with the sterling area may provide some signposts for the future, as well as warnings, should these interests in the two countries’ trade relationships be neglected, as they were in the 1930s.