

GENERAL AGREEMENT ON TARIFFS AND TRADE

RESTRICTED

L/1347

10 November 1960

Limited Distribution

CONTRACTING PARTIES
Seventeenth Session

REPORT OF THE COMMITTEE ON BALANCE-OF-PAYMENTS RESTRICTIONS ON THE CONSULTATION UNDER ARTICLE XII:4(b) WITH

J A P A N

1. In accordance with its terms of reference the Committee has conducted the consultations with Japan under Article XII:4(b). The Committee had before it: (a) a basic document (MGF(60)57), including the following annexes: Foreign Exchange Budget for Commodity Imports 1956-60; excerpts from the Foreign Exchange and Foreign Trade Control Law; lists of products subject to the Automatic Approval and the Automatic Fund Allocation System; (b) documents provided by the International Monetary Fund as mentioned in paragraph 2 below. In conducting the consultation the Committee followed the "Plan" recommended by the CONTRACTING PARTIES; The consultation was completed on 25 October 1960. The present report summarizes the main points discussed during the consultation.

Consultation with the International Monetary Fund

2. Pursuant to the provisions of Article XV of the General Agreement, the CONTRACTING PARTIES had invited the International Monetary Fund to consult with them in connexion with this consultation with Japan. In accordance with the agreed procedure the representative of the Fund was invited to make a statement supplementing the Fund's documentation concerning the position of Japan. The statement made was as follows:

"The International Monetary Fund has transmitted to the CONTRACTING PARTIES the Executive Board decision relating to the last consultation with Japan under Article XIV of the Fund Agreement¹ and the background material prepared in connection with that consultation.

"With respect to Part I of the Plan for Consultations, relating to balance of payments position and prospects, and with respect to Part III, relating to system and methods of the restrictions, the Fund draws the attention of the CONTRACTING PARTIES to the Executive Board decision of September 16, 1960, taken at the conclusion of its recent consultation with Japan, and particularly to paragraph 4 which reads as follows:

¹See Annex II.

'Japan has established partial external convertibility of the yen and made further progress in reducing restrictions and discrimination, including the termination of two bilateral payments arrangements. The scope of minor restrictive practices has again been reduced; it is intended in 1960 to terminate the retention quota practice and to reduce further the scope of barter trade, and as soon as possible in 1961 to terminate the linking system. The Fund welcomes these steps and urges the early elimination of the remaining discriminatory practices. Japan has drawn up a program for substantially liberalizing trade and exchange restrictions within the next three years. The Fund notes the intention of the authorities to accelerate this program as economic conditions permit, and believes that Japan's external position would permit a speedier liberalization of restrictions.'

"With respect to Part II of the Plan for Consultations, relating to alternative measures to restore equilibrium, the Fund draws attention to the decision taken at the conclusion of its last consultation with Japan. The Fund has no additional alternative measures to suggest at this time."

Balance-of-payments position and prospects

3. The full text of the opening statement made by the head of the Japanese delegation is attached as Annex I to this document. In the statement he described Japan's economic conditions and foreign exchange position in recent years. Remarkable rises had been witnessed in national production, particularly in the industrial sector. Monetary reserves had continued to increase; a favourable balance of payments had been realized over the past two years although recently this had to a considerable extent been due to the inflow of short-term capital. On the other hand, Japan was faced with the problems of a rapidly growing population, chronic under-employment, and widely different levels of productivity in different sectors of the economy. The agricultural sector, where productivity and income level were much lower than in the industrial sector, was holding a large number of potentially unemployed. In order to meet these and related problems the Government of Japan had embarked on a programme of development aimed at doubling the GNP by 1970. The principal feature of this programme was to lay more emphasis on the heavy and chemical industries. Expansion of Japan's exports was faced with a number of obstacles, such as, the lack of large and stable adjacent markets, the long-term tendency of declining world exports of light industrial products, notably textiles, and the discriminatory treatment of Japanese goods in many countries. The Japanese Government wished sincerely to appeal to contracting parties to consider terminating any restrictions and discrimination against Japanese products. He outlined the steps taken to date to restore equilibrium and to reduce restrictions in Japan and plans for future liberalization, points which are noted in the relevant sections of this report. In concluding his

statement the representative of Japan stated that his Government was fully prepared to ease import restrictions, increase the allocation of foreign exchange available for imports, and constantly to review the liberalization programme for the removal of quantitative restrictions with a view to accelerating that programme as far as economic and social conditions permitted.

4. Members of the Committee complimented the representative of Japan on his very interesting and informative statement. They noted that the Japanese economy in the last year had been characterized by a considerable growth in investment and consumption. Exports seemed to have been growing very fast and, notwithstanding the rise in imports which had also occurred, foreign exchange reserves had continued to rise; although the rate of increase had been slower in the last few months, reserves had now reached a record level. Members recalled that at the last consultation with Japan, members of the Committee had felt that Japan's approach towards liberalization was over-cautious and they had urged Japan to liberalize imports at a speed consistent with the requirement of paragraph 2(b) of Article XII and commensurate with the progress made by other industrial countries. Since then, events had made these views even more pertinent, and a sense of urgency was justly reflected in the relevant passage in the IMF Executive Board decision of 16 September 1960 as quoted in paragraph 2 above. Against this background contracting parties had reason to be disappointed at the limited progress that had been made in Japan's import liberalization. To date, only 40 per cent of total imports had been placed under automatic licensing. Some members were particularly concerned at the reference made by the Japanese representative to economic and social factors as relevant factors in considering future liberalization, whereas the only valid criteria for the use of import restrictions under Article XII were the balance of payments and the monetary reserve situation.

5. In answer to these questions the representative of Japan advanced various reasons why his Government was not at present in a position to advance faster in the removal of restrictions, including:

- (a) That the Japanese economy was exceptionally susceptible to unpredictable wide fluctuations in economic activity; investments in fixed capital and inventories varied from year to year, and the ensuing variations in import demand were often accentuated by speculation.
- (b) That the Japanese economy depended predominantly on imported raw materials; prices of primary commodities being unstable, a wide margin must be envisaged for variations in the import bill on this account.
- (c) That the present high rate of expansion called for heavy imports of machinery and capital goods of all description; these requirements had no reason to abate but would, on account of the economic development programme that had been adopted, increase and stand at a high level for some years to come.

- (d) That Japan had no large and stable markets and raw material sources which were within economic distances from Japan so that freight costs were an important element in the import bill; present indications were that freight rates would be on the rise.
- (e) That United States procurement and special expenditures in Japan were on the decline.
- (f) That there still existed external obligations arising from the last war, including reparations.
- (g) That the recent rises in the foreign exchange reserves reflected principally increases in the inflow of short-term capital, mostly in the form of Euro-Dollars and usance credits, while the trade account continued to be in deficit.

6. The Committee discussed with the Japanese delegation these various factors as well as certain other matters relevant to Japan's balance of payments. Members observed that since 1957 the Japanese economy seemed to have displayed a remarkable degree of stability characterized by steady expansion at what was a very high average rate of growth; that stocks of imported raw materials seemed to have declined recently; that although speculative importation and variations in stocks might place a burden on the balance of payments in a particular year, it should have no such effect in the longer run, as increased imports arising from these factors in one year must be offset by reduced imports in subsequent years. A member of the Committee also pointed out that information available to the IMF seemed to indicate that the Japanese authorities did not consider that there was a speculative element in the inventory accumulation in 1959/60. The recent rise in Japanese imports seemed to have been concentrated in the raw materials sector, apparently resulting from the high demand for Japanese exports. In reply to this the Japanese representative emphasized the complex causes of speculation and insisted on the desirability of preventing speculative action through a closer watch on imports. While it was true that part of the increase in raw material imports was related to the increase in the exports of manufactured goods, a large proportion of such goods was nevertheless destined for the home market. Further, the rising standard of living had been requiring more imported material and equipment, and had been reflected in reduced resources for export production and in an increased demand for imports of consumer goods.

7. It was noted by members of the Committee that while Japan's foreign exchange receipts derived from procurement for the United States forces in Japan might decline, there should be no danger of a precipitous or disruptive fall, and that war reparations constituted a relatively unimportant and diminishing item in Japan's balance of payments. The Japanese delegation reiterated the points (e) and (f), noted in paragraph 5 above, and maintained that the reparations, even though of limited dimension, nevertheless were a significant factor, not existing for most other countries.

8. As regards short-term capital movements, some members suggested that usance credits, being a function of imports, might be expected to remain and perhaps to increase. Since the yen had become partially convertible, there should be an increasing tendency for short-term funds to be held in Japan. The representative of Japan replied that the present level of usance credits was expected to be maintained but it would, of course, fall if there should be any drop in imports. Short-term capital, in the view of the Japanese representative, while swelling the monetary reserves, could hardly be relied upon. In reply to a question, the Japanese representative said that after the phenomenal increase in the past year up to the end of September 1960, the inflow of Euro-dollars had shown signs of decline.

9. At the request of a member of the Committee, the Japanese delegation supplied estimates for the balance of payments for the fiscal year 1960-61 (ending 31 March 1961). These showed that, whereas for the first half of the fiscal year steadily expanding exports coupled with steeply increased imports had resulted in some trade deficit, a small trade surplus was expected for the whole fiscal year. The invisibles account would show some deficit in the first half but an even balance was expected for the second half-year. A small surplus was expected on long-term capital account, which reflected a sustained level of inflow, offset partly by repatriation of investment. As regards short-term capital, substantial inflow in the form of usance credits and Euro-dollars had resulted in a surplus of \$325 million in the first half-year, but no further increase was forecast for the second half-year. For fiscal 1960/61 as a whole, an even balance was expected on current account, and a significant surplus was expected on capital account. The net surplus should amount to \$300 million in the first half-year and \$140 million in the second half-year. The total gold and foreign exchange reserves, amounting to \$1,658 million at the end of September 1960, should rise to about \$1,800 million at the end of March 1961.

10. A member noted that the figures relating to Japan's external reserves given in the documents before the Committee, covered only official gold and foreign exchange reserves and did not, as in certain other cases, include other balances such as holdings of commercial banks. The attention of the Committee was called to the statement in the IMF document to the effect that, in addition to the official holdings, the Ministry of Finance of Japan held certain foreign exchange deposits with banks, and commercial banks had their own holdings, and that data in respect of these were not available. The representative of Japan noted that the recent slowing down in the rate of growth of official reserves was not compensated by any marked increase in commercial bank holdings and assured the Committee that the amount involved was in any event insignificant.

11. On the basis of data supplied by the Japanese delegation, a member of the Committee noted the fact that in the first half of 1960 Japanese exports to the United States increased by some 18 per cent over those in the

corresponding months in 1959. In his view, this was a remarkable achievement, considering the pause in the growth of production in the United States economy which had occurred this year and the general decline in the rate of increase of world exports which had also taken place. This augured well for Japanese exports to the United States, Japan's largest market, in the future. There were similar grounds for confidence regarding the future of Japanese exports more generally. The representative of Japan commented that the 18 per cent increase in exports to the United States in the first half of 1960 was substantially lower than the increase of nearly 50 per cent in the preceding half-year. Even discounting seasonal factors, the fall in the rate of increase was too drastic to warrant optimism. The Committee member thought that the second half of 1959 was no suitable basis for comparison in view of seasonal factors associated with Christmas trade and particularly because of the exceptionally high imports into the United States during that period consequential upon the steel strike.

12. Members of the Committee noted the solid progress that had been made in economic expansion and the increase in the monetary reserves. The present level of the reserves, equivalent to the value of four to five months' imports, was more favourable than in many countries which had forgone the use of restrictions on balance-of-payments grounds. Account should also be taken of the supplementary reserves available in the case of need in the form of drawing rights in the IMF. In the case of Japan, these had been substantially increased during the recent adjustment in the Fund's quotas, by according to Japan a special increase of 100 per cent units, thereby raising its total quota in the Fund to \$500 million. Japan's exports had been and were still growing at a remarkable rate and the outlook for them appeared most favourable. In the light of these considerations, most members of the Committee considered that there was no reason why Japan should not take immediate steps to speed up the relaxation of restrictions as believed to be possible by the Fund, and to eliminate discrimination as urged by the Fund.

13. The representative of Japan thought that undue emphasis should not be placed on the size of Japan's foreign exchange reserves, including potential secondary reserves in the form of drawing rights on the IMF, particularly in view of the inflow of short-term capital in recent months. The Japanese representative considered that basically no confidence could be achieved unless there should be a steady surplus on current account. He assured the Committee, however, that the Japanese Government would constantly review its programme of liberalization in the light of any further improvement in its balance-of-payments position; in fact, a Ministerial Council for Furthering Liberalization had been appointed precisely for this purpose. Import restrictions and discrimination would be removed as rapidly as circumstances would permit. Members of the Committee referred again to the Fund decision and urged Japan to accelerate the liberalization programme in the light of the present reserve position.

Alternative Measures to Restore Equilibrium

14. Members of the Committee congratulated the Government of Japan on the effective implementation of fiscal and monetary measures to restrain excessive internal demand, and ensure a desirable rate of growth which had led to stability and an improvement in the balance of payments. The Japanese representative recalled in this connexion the recession in the Japanese economy in 1957 and the slow recovery in spite of the strenuous fiscal and monetary measures. Although the present economic conditions were satisfactory, the balance could be easily upset by any immoderate manipulation or trade liberalization. Account had to be taken of the persistent problem of unemployment and under-employment. Members of the Committee considered that, in view of its success and experience gained in this regard, the Japanese Government could confidently rely more heavily on internal fiscal and monetary policies and consequently could proceed more rapidly in removing restrictions.

15. A member of the Committee noted with satisfaction the impressive rate of growth in Japanese production in recent years and asked whether, in the view of the Japanese Government, it would be possible to sustain such a rate in future. The representative of Japan said that after reaching a peak in February 1960, the rate of increase in industrial production had levelled off in subsequent months. While it was hoped that a high rate of expansion in economic production could be continued, this would depend upon variable internal and external economic factors; thus it was premature to anticipate at this point the results of the measures taken to date.

16. In view of the emphasis apparently being placed on heavy and chemical industries in the future development of the Japanese economy, the Japanese representative was invited to comment on the choice of such capital intensive industries, considering the shortage of capital and abundance of labour supply in Japan. The representative of Japan stated that his Government had under consideration a plan to double the gross national product by 1970. In order to raise the level of national income, to increase employment opportunities and to diversify the economy, it had been decided to promote the expansion of the heavy and chemical industries. In the past, Japan had succeeded in building up very competitive industries in certain fields, e.g. polyvinyl chloride, which were capital intensive. The shift in the emphasis was also necessitated by the general decline in international trade in products of light industries, notably textiles, in which many under-developed countries were striving to attain self-sufficiency. The change was also needed in order to increase its standard of living, to solve the problem of chronic unemployment and to increase the level of national income. While capital shortage might be a limiting factor, there were other advantages, such as the availability of adequate electricity supply, convenient location of industrial centres from the point of view of shipping, etc. which compensated for that disadvantage. Members of the Committee noted that all these advantages cited by the Japanese representative existed equally for other industries. The question was not whether Japan could produce steel and chemicals competitively with other countries, which there seemed to be no reason to doubt, but whether, in concentrating new investment on these industries, the Japanese authorities were making the best use of their relative resources of capital and labour respectively. In reply to other questions, the representative stated that the policy was to encourage the inflow of investment capital.

Among other things, capital repatriation, previously permitted in five annual instalments after completion of a two-year waiting period, would henceforth be allowed in three annual instalments following a two-year waiting period. The representative of Japan indicated that a further shortening of the periods was under consideration.

17. As regards trade promotion, the representative of Japan stated that the retention quota system had been abolished on 30 September 1960; that the "linking" system and barter arrangements would be virtually abolished by 1 April 1961; that the Government had no intention of subsidizing exports, or of permitting marketing practices involving dumping. The system of granting tax exemption for exports had, however, not been abolished.

18. Members of the Committee pointed out that while the development programme was being put into operation, it would be in the interest of the economy if industries were exposed more extensively to foreign competition, which would help to discourage uneconomic production and ensure a more rational utilization of the resources. The representative of Japan assured the Committee that it was not the intention of his Government to protect inefficient industries. Japan was fully aware that it could not afford the luxury of self-sufficiency based on uneconomic production. Liberalization would be pushed as far ahead as permitted by the external payments situation.

System and Methods of Restriction

19. Members of the Committee noted that Japan had taken certain welcome steps in liberalizing imports since the last consultation. Members of the Committee expressed concern over the fact that discrimination had not been totally eliminated and that it even persisted in the Automatic Approval System, although nearly two years had elapsed since the introduction of external convertibility. They enquired as to the future programme of liberalization. The representative of Japan replied that the Automatic Approval System had been extended to include more products, the Automatic Fund Allocation System had been introduced and discrimination had been further reduced. Some 45 per cent of current Japanese imports (excluding imports on Government account) were now covered by the AA and AFA systems; this proportion would be increased to 65 per cent in April 1961, when wool and cotton are placed on Automatic Approval. In accordance with the recommendations made by contracting parties at the last consultation, Japan had made every effort to eliminate discrimination. Under the AA system all imports except for two items were now admitted without discrimination. The discrimination remaining on the two items would be eliminated as soon as certain internal difficulties were resolved, which should be in the near future. As regards liberalization in the future, the Government had formulated a programme under which imports at present subject to restriction might be considered as falling into four categories:

- (a) Items to be liberalized shortly;
- (b) Items which could not be liberalized shortly but would be liberalized as soon as possible within the coming three years;

- (c) Items to be liberalized as soon as possible, though their liberalization in three years was considered difficult at present;
- (d) Items for which no liberalization was envisaged at present.

20. The representative of Japan stated that in determining the time schedule and the method of liberalization of imports of each commodity, all the following factors would be taken into consideration:

- "(i) import liberalization should be carried out in such a way that its initial effect of reducing the cost of raw materials will spread to all products. Liberalization of imports of raw materials, therefore, should be carried out as soon as possible, in principle, together with necessary measures to support it;
- "(ii) imports of those items which are less in competition with domestic production or which have less competitive power with domestic products are to be liberalized first. On the other hand, however, those items which, if liberalized, will considerably add to the benefit of consumers or industries using them, are to be liberalized as soon as possible together with necessary measures to support the liberalization;
- "(iii) as for commodities produced by industries which are making efforts of technical development or rationalization under the rationalization programme or promotion programme based on law or other governmental measures, import liberalization will be carried out taking into account the results of such efforts;
- "(iv) as for those items of which it will be difficult to liberalize imports at a time; import quotas for each commodity will be increased taking into consideration the requests of exporting countries and the effects of trade expansion, and import liberalization will be achieved after the domestic economy gets used to the increasing imports."

21. The representative of Japan further stated that as a result of action under (a) and (b), the proportion of Japanese imports liberalized by July 1963 would be about 80 per cent, or about 90 per cent if it were also decided to liberalize oil and coal items. He emphasized, however, that this programme had been conceived in the light of the present estimate of the country's balance of payments and that it would be subject to constant review in the light of developments in payments. The Government would not hesitate to speed up the programme if there should be any further improvement in the external financial position or outlook. As mentioned above, the Ministerial Council had been established for this purpose.

22. Members of the Committee, while noting the programme formulated by the Japanese Government for the further liberalization of restrictions, observed that, if this programme were adhered to, a considerable time would elapse before other GATT members could expect to obtain full access to the Japanese market. They welcomed the statement by the Japanese representative that the programme of liberalization would be speeded up in the event of further improvement in the

balance-of-payments position, and reiterated the view expressed earlier that scope for such action already existed. A member of the Committee pointed out that, despite Japan's need for imported materials, a number of major industrial materials such as certain non-ferrous metals, pulp, and rapeseed were not at present on the AA list. Japan could appropriately place all restricted industrial materials on the Automatic Approval List as a first step in further liberalization. It was also desirable that materials employed for similar end-uses, such as rayon pulp, as well as cotton and wool, should be liberalized at approximately the same time. The representative of Japan undertook to convey these views to the attention of his Government.

23. The Committee discussed with the Japanese delegation various aspects of the Japanese import control system. The points made relating to the different control methods are noted below. Regarding the Automatic Approval System members of the Committee wished to know why it was necessary, for this section of imports, to retain the licensing requirement. They further suggested that Japan should consider the possibility of replacing the present system of restrictions by the "negative list" method which had been adopted by many industrial countries continuing to apply import restrictions. The Japanese representative explained that under the existing legislation the Government was obliged to draw up a semi-annual foreign exchange budget covering all expenditure in foreign currencies, including all imports. Insofar as an estimate had to be included for the liberalized sector of imports, it was necessary to draw up a list of such imports, as well as lists of products subject to restriction. Members of the Committee said that the need to estimate expenditure on the liberalized sector of imports existed in all cases in which restrictions were used for balance-of-payments reasons. The usual practice was to estimate the total funds needed to meet this requirement, but in most cases such imports had been made free of licensing control. If the Automatic Approval procedure meant what it said, namely that licences for imports were automatically approved without foreign exchange limit, the estimate of the requirement under this sector of the foreign exchange budget could be equally well made in the absence of licensing. The foreign exchange budget required by the Japanese foreign exchange control law did not seem to involve any significant difference from this general position and there was no reason why these products must be subject to licence, or why the "negative list" method could not be used instead. The representative of Japan maintained that the licensing requirements was indispensable under the foreign exchange control law and that being a mere formality it should not be regarded as an impediment to trade. Whenever the amount allocated for a product was exhausted a supplementary allocation would be made without delay. Members of the Committee recalled past discussions on the subject of licensing requirement, the general view regarding which had been that it did constitute an additional barrier to international trade. They urged the Government of Japan to consider its early abolition for the freed sector of imports. The Japanese representative said that, although the licensing requirement for products under the AA system, in the view of his Government, did not constitute a barrier to trade, his Government was studying for procedural purposes the feasibility of adopting the "negative list" technique.

24. With regard to the Automatic Fund Allocation System, the representative of Japan explained that this had been introduced in October 1959 on an experimental basis as a transitional measure in preparation for transfer to the AA system. Under this system exchange allocations were freely granted and the purpose was to enable the Government to watch the trend of imports of certain commodities. In answer to questions, the representative of Japan stated that, although this system had been conceived as a measure of preparation for transition to the AA system, no items on the list had thus far been so transferred but that this was principally due to the short time that had elapsed since the introduction of this system. Some members of the Committee noted that according to the document supplied by the Fund, allocation of foreign exchange under this system was granted automatically and without restriction by the government "unless it believes the importation to be harmful to domestic producers or that it might have an adverse effect on the balance of payments". Requested to comment on the consistency between this statement and his earlier statement regarding the totally unrestrictive nature of the AFA system, the representative of Japan explained that the qualifications were provided for in the relevant regulations, but in practice the Government had found it unnecessary to take them into consideration in administering the system, because all applications for foreign exchange fund under this system had been approved. While this statement was welcomed by members of the Committee, the view was expressed that the greater possibilities of administrative discretion in the issuing of licences under this system gave rise to some doubt as to whether imports under it could be said to be truly liberalized in the fullest sense of the word.

25. In discussing the Exchange Fund Allocation System, the representative of Japan explained that this covered a major part of imports of foodstuffs, raw materials and other essentials and comprised some 55 per cent of current total Japanese imports. The importer was required to obtain in the first place an allocation of foreign exchange. For this purpose global quotas were provided for all the items covered. In answer to questions, the representative of Japan confirmed that under the Japanese import control system all products not covered by the AA or AFA system would be importable under the EFA system. Any products for which quotas were not specifically provided would fall within a general category under the heading of "Miscellaneous" and application for licences would be considered within the general quota allocated for that item. Apart from certain prohibitions which were consistent with Articles XX or XXI of the General Agreement, no imports were prohibited. Members of the Committee pointed out that the device of providing a general allocation under a "Miscellaneous" category which appeared to cover a variety of products, some of them of a not insubstantial nature, could hardly be considered a fully satisfactory method of meeting the provisions of the GATT with regard to minimum access. It seemed inevitable, under such a method, that some products would in effect be prevented from entering the country. The Japanese representative explained that a "First-Come-First-Served" method of restriction was in use at one time after the war and was found sometimes to be open to abuse. Under the new system this had been reduced to a minimum and could arise only in relation to very minor items, since global quotas had been provided for thousands of items on the basis of past imports. Members of the Committee considered that the possibility of abuse cited by the Japanese representative applied to other than merely minor items and was in any case capable of removal through a stricter adherence to the provisions of Article XII:3(c)(ii) of the General Agreement.

26. Members of the Committee took note of the very large proportion of Japanese imports which would still remain subject to the Exchange Fund Allocation System, even after 1 April 1960, and of the wide discretionary powers which appeared to be available to the licensing authorities under that system. The fact that there were formally no prohibitions in the Japanese import system had little practical relevance in a situation in which quota allocations for a range of products were such as to render it certain that imports for a large proportion of such products would not be possible. Moreover, it was inevitable that in a situation in which it was known that licences were for all practical purposes unavailable, importers would not even seek to obtain them.

27. Members of the Committee recalled the discussions at the previous consultation with Japan concerning the inadequacy of published information on the Japanese import restrictions and the complexity of the system. Especially with regard to imports under the Exchange Fund Allocation System, members considered that the information provided in the foreign exchange budget was framed in terms of the broadest possible categories of imports, and would seem to be of little or no informative value to the trading community. Attention was drawn to the provisions of Article XIII:3(b) which laid upon contracting parties certain specific obligations regarding the full publication of information concerning quotas established for the importation of goods. In view of this, the Japanese Government should provide importers and foreign exporters with much more detailed information of import possibilities. Furthermore, in order that any future consultations with Japan might be more meaningfully and effectively carried out, the Japanese Government should be prepared to submit to the Committee much fuller details of the restrictions applying to the import subject to quotas. Members of the Committee, while recognizing that such information might be of a highly complex nature, considered that it was precisely because of that complexity that it was necessary for the Committee to be in a position to explore this sector of the Japanese licensing system with much greater thoroughness than was possible on the basis of the background data at present provided. The representative of Japan stated that, while for practical reasons the Japanese delegation had not been able to supply the Committee with a detailed list of items under the Exchange Fund Allocation System, this did not mean that detailed information was not available to importers in Japan. The Ministry of International Trade and Industry published very detailed notices and other forms of announcement to importers on a regular basis, giving information regarding conditions of importation and the like. So far there had been no complaint on the part of the Japanese trading community on this count. He would admit, however, that most of such publications being available in the Japanese language only, there might be a limit to the amount of information that could be made use of by foreign exporters. Members of the Committee observed that the information referred to did not appear to be as full as was specified under the terms of Article XIII:3(b); in particular, detailed information on the size of quotas established for many individual commodities did not appear to be made publicly available; some exporters to Japan found it extremely difficult in such cases, and practically impossible in some cases (largely the "miscellaneous" and machinery sectors), to ascertain what, if any opportunities for trade existed for items in which they were interested. The existence of such a situation, in the view of these members of the Committee, constituted a hindrance to trade.

28. A member of the Committee referred to the statement in the basic document that importers of goods subject to the Exchange Fund Allocation System must meet certain requirements and that the Ministry, in allocating foreign exchange, was entitled to impose certain conditions in regard to delivery time, prices and "other matters". Requested to comment on these points, the representative of Japan stated that the requirements which an importer must meet before he could avail himself of the allocations had been imposed in order to ensure that the foreign exchange would be available only to importers with the necessary experience and end-users with the necessary facilities. As for the conditions which the Ministry might impose, these conditions were all published in the public announcements of the Ministry and were designed to ensure a proper utilization of the quotas allocated; there was no restrictive motive involved.

29. It was suggested by a member of the Committee that the systems and methods used by other contracting parties might be referred to by the Japanese Government in any attempt at simplifying the Japanese system and reducing the complexity of the procedures. For example, in certain countries raw material imports were allocated to industrial users as a percentage of past requirements and quotas for imports of consumer goods might be given with reference to imports in past years. These systems had the effect of minimizing the arbitrary element in the licensing system. The representative of Japan pointed out that the existence in Japan of thousands of trading firms and the diversity of their trading interests would seem to make it necessary for Japan to adopt more complicated techniques of allocating foreign exchange than in certain other countries. In the view of the Japanese Government, the methods used in allocating foreign exchange in Japan were not unnecessarily cumbersome. With the improvement in the balance of payments resulting in larger amounts of foreign exchange being available for import purposes, there had been a diminishing need for stringent rationing. At any rate it was envisaged that more and more imports would be freed from restriction and that the area covered by the quotas would be substantially reduced in the near future.

30. A member of the Committee pointed out that according to the information supplied by the Japanese Government actual commitments fell short of the provisions of the foreign exchange budget during almost all the licensing periods in the past four or five years. The representative of Japan explained that this was partly due to the liberal provision of funds in the budget, both under the AA system and under the AFA system, and partly due to the fact that importers applying for allocations often allowed themselves a margin of 5-10 per cent, especially in cases of bulky cargoes for which the c.i.f. value might vary with freight and other expenses connected with the importation. The member of the Committee noted that this would seem to bear out the view that the foreign exchange reserve position of Japan was capable of meeting the requirements of a more liberal and flexible system of restrictions.

31. With regard to bilateral commitments the representative of Japan stated that the payments agreement with Greece had been terminated and that only two other agreements providing for import quotas were at present still in force. These provided for imports of sugar from Taiwan and rice from Taiwan and Korea and the Japanese Government expected shortly to negotiate for the termination of the agreement with Taiwan. Apart from these bilateral agreements entered into by Japan usually provided for no more than "targets" which the partners expected to reach in the normal course of trade between them. In answer to questions the representative of Japan stated that the provision of such targets in no way affected the access to the Japanese market of imports from other countries. Imports from the partner countries were licensed under the global quotas and account was taken of the targets merely through the enlargement of the global quotas. There being no special treatment of imports from such bilateral partner countries, these must compete on equal terms with imports from other sources on the Japanese market. The proliferation of such agreements was due to the following reasons: first, bilateral arrangements were necessary in the trade with the State-trading countries. Secondly, a number of countries had either withheld the application of the provisions of GATT to Japan or, if they did not invoke Article XXXIV of GATT, applied discriminatory restrictions against Japanese products. Some of these countries had insisted on negotiations for the establishment of bilateral quotas for the trade between them and Japan, thus compelling Japan to rely on bilateral arrangements. In any case Japan was anxious to explore and diversify markets for its expanding industrial production and bilateral negotiations seemed in some cases to be a necessary means for this purpose.

32. Members of the Committee welcomed the statement about the absence of exclusive bilateral quotas, but noted however that complaints arose in connexion with alleged discriminatory practices deriving from Japan's obligations under bilateral agreements. It was pointed out that the objections raised against the operation of bilateral agreements, even those which only entailed the setting of "targets", were not unreasonable. Whatever the juridical position might be, in practical terms the existence of such "targets" provided a powerful incentive to the partners to such agreements to ensure that the "targets" were in fact achieved. Fears of this kind were particularly strong where the nature of the licensing system was such as to provide great scope for the exercise of administrative discretion enabling such practices.

Effects of the Restrictions

33. The representative of Japan stated that while the import restrictions currently imposed by Japan were necessitated by balance-of-payments reasons, it might not be denied that they sometimes tended to have certain incidental protective effects on her domestic industries. While Japan was having recourse to Article XII, it was the firm policy of the Japanese Government to minimize the incidental protective effects of the import restrictions by relaxing or eliminating the existing restrictions as far as the balance-of-payments position permitted. Members of the Committee expressed gratification at Japan's assurance that incidental protection would be kept to a minimum, in view of the fact that such protection could allow industry and agriculture to operate at cost levels which in many cases would not be economic in the presence of intensive international competition. They were also gratified that Japan was aware of the desirability of stimulating efficiency in industry by trade liberalization measures which would permit greater competition.

34. Some members noted that at present there existed only a very low level of licensing for consumer goods and that recent applications for such licences had very greatly exceeded the amounts available, notwithstanding that applications had remained open only for a very short time. They suggested that liberalization of such products would have a salutary effect on the economy. Another member suggested that the present system of allocating exchange to individual items might with advantage be changed to the provision of quotas valid to wide ranges of products on which choice could be made by the importer in the light of supply and demand. Another member considered that although the Japanese Government had no intention of subsidizing exports, the protected domestic market might have the effect of unduly strengthening the cost advantage of producers and enabling them to sell abroad at prices lower than would have been obtained in the absence of the incidentally protective restrictions. The representative of Japan replied that liberalization would be pursued in all directions and in all possible ways, and that as regards the last point, it should be noted that no Japanese industry relied on practices of dumping.

35. One member of the Committee pointed out that it would also be appropriate for the Japanese authorities to prepare Japanese agriculture for the day when Japan would no longer be in balance-of-payments difficulties. It was suggested that pending liberalization, provision should be made for steadily increasing quotas so as gradually to expose domestic producers to more competition. In addition, steps should be taken with a view to diversifying Japanese agriculture and raising productivity. The representative of Japan advised the Committee that a Research Council for Agriculture, Forestry and Fisheries had been established last year to study the fundamental problems of Japanese agriculture, forestry and fisheries and to formulate plans for the improvement of those sectors of the economy.

General

36. Members of the Committee expressed appreciation for the co-operative manner in which the delegation of Japan had participated in the intensive discussion during this consultation. The discussion had shown that the balance of payments of Japan was developing most favourably; not only had reserves reached a record level, but there was a bright outlook for the future; this was particularly illustrated by the present performance of, and future prospect for, exports. The Committee recalled the IMF Executive Board decision of 16 September 1960 in which the Fund noted the intention of the Japanese authorities to accelerate their programme of import liberalization as economic conditions permitted and expressed the belief that Japan's external position would permit a speedier liberalization of restrictions. The Committee fully endorsed this view of the Fund and strongly urged the Government of Japan to take immediate steps accordingly. While the Committee welcomed the progress that had been made since the last consultation in the relaxation of import restrictions and in the reduction of discrimination, it observed that more than half of Japanese imports still remained subject to quantitative restrictions, and that even under the AA and AFA systems there remained some not completely satisfactory features (e.g. those mentioned in paragraph 23 and 24 of the report). The Committee noted the intention of the Japanese Government to pursue liberalization according to a programme providing for the removal of restrictions by stages, and to keep constantly under review the possibility of accelerating that programme insofar as the balance of payments position might permit. However, in the view of the Committee this policy did not adequately reflect the strength of the present balance of payments situation of Japan, and a more substantial and immediate removal of restrictions seemed clearly warranted. The continued existence of a substantial body of restrictions in the Japanese import system in present circumstances presented great difficulties to certain contracting parties in resisting pressures for adjustments in their commercial policies towards Japan. The Committee noted that at present the Japanese restrictive system was still subject to a considerable degree of administrative discretion, which provided substantial scope for protection to domestic producers and which, especially where bilateral agreements were involved, gave rise to misunderstandings regarding possible distortions of the pattern of trade. Members noted that since the introduction of external convertibility of currencies, nearly two years ago, there were no longer grounds for the continuation of discrimination, which the Committee urged should be eliminated. Noting the complexity of the import licensing system, the Committee urged the Japanese Government, pending the removal of restrictions, to simplify the control system, for example through the adoption of the negative list method, and to reduce the incidence of the restrictions, for example by enlarging quotas and by making provision for token imports. The Committee asked the Japanese delegation to convey to its Government the sense of urgency felt by the Committee regarding all the above-mentioned matters.

37. The representative of Japan said that his delegation had taken careful note of the views and suggestions that had been expressed at this consultation and that these would be reported to his Government, which would no doubt give them careful consideration.

ANNEX I

Opening Statement by the Japanese Representative

In recent years, Japan's economic conditions and foreign exchange position have been fairly favourable. Particularly, the economic growth during last year was so remarkable that the over-all national production increased by about 17 per cent while the industrial and mining production marked a sharp rise of 29 per cent. Last year our balance of payments recorded a surplus of \$348 million and our monetary reserves reached \$1,361 million. Against this background, the Japanese Government has taken a series of measures of further liberalization of trade and payments.

In accordance with the increase in import demands and the progress of liberalization, the foreign exchange made available for imports was augmented from \$2,328 million for the latter half of 1959 to \$2,624 million for the first half of 1960, and \$2,800 million for the latter half of 1960. In October 1960, 200 items, including cocoa beans and zinc ore, were added to the automatic approval system and the foreign exchange earmarked for this system was increased from \$970 million for the first half of 1960 to \$1,100 million for the second half. The Automatic Fund Allocation System was created in October 1959 and about 400 items were originally placed under this system. About 200 items, including jewellery and personal consuming goods, have been added to the list since October 1960. While the foreign exchange allocated for this system for the first half of 1960 was only \$30 million, the amount allotted for the subsequent half year was substantially increased to \$50 million. Last July the Japanese Government adopted a programme for liberalizing payments and trade, together with an economic policy to facilitate the implementation of the liberalization. The programme provides for the dismantling of the existing exchange control over invisible account within two years, the liberalization of wool and cotton imports in April 1961, and the attainment of an import liberalization percentage of 80 per cent of total imports within three years. If coal and petroleum are also liberalized the percentage will be increased to 90 per cent. Most of the discriminatory restrictions against dollar goods have been eliminated and single country licensing has been generally replaced by global allocations. Now the single country licensing remains only in relation to countries with which we maintain bilateral payments agreements and over a few commodities including rice.

Keeping pace with such progress in liberalization measures, the import procedures have been simplified step by step. The retention system was abolished in October 1960; the linking system will be practically removed in April 1961 as a result of the liberalization of raw cotton and wool; barter trade system will virtually cease to exist by April 1961 except with Eastern European countries, since most of the commodities dealt with under this system have been, or will be liberalized by April 1961. The payments agreement with Greece has been terminated. Consequently, such agreements remain only with Taiwan and Korea. Negotiations to do away with such agreement with Taiwan will soon get under way.

I will now, Mr. Chairman, turn to the problems which call for our careful consideration in the pursuance of the policy of import liberalization. These problems bear on Japan's balance-of-payments position and the unique industrial structure of my country.

As I stated earlier, in 1959 our foreign exchange receipts exceeded payments by \$348 million. It should not be overlooked, however, that \$182 million - a greater part of the surplus - was attributable to the inflow of short-term capital. The surplus in the current account on the other hand was no more than \$155 million. During 1960, our monetary reserves continued to increase and the reserves on hand at the end of September 1960 stood at \$1,658 million. Here again, most of the surplus acquired in 1960 was due to the inflow of Euro-dollars and increase in import usance facilities. Meanwhile, the current account was only barely balanced.

The turn in our favour of the terms of trade largely contributed to the improvement on the trade balance in the past two years. Though the volume of imports rose sharply, the value of imports did not go up as much, owing to the fall in the price of fuel, raw materials, and freight rates. On the other hand, the price of export goods went up slightly during the period. It is worthy of note in this context that increase in exports to markets in North America accounted for 67 per cent of the increase in total exports during last year. Apparently, such increase was on the whole the result of the expansion of demands in United States markets.

Now a few words on our invisible account. Our invisible account is turning unfavourable. In fact, the special procurements by the United States which have always been the most important item in the invisible trade receipts tend to diminish in the future.

Unlike most Western countries, our economy is conditioned by the following three peculiar factors which eventually may well affect our balance-of-payments position. They are: (1) rapidly growing population which will be supplying increasing numbers to the labour force for some years to come; (2) marked difference of productivity between big business on one hand and medium and small size industries on the other, and between agriculture and industry; and (3) the need of modernizing our chemical and heavy industries.

The level of national income in my country is still lower than that in a number of Western countries. Moreover, chronic under-employment exists due to over-population. Behind the fact that 600,000 are jobless and 6,000,000 are under-employed in Japan looms large the dual structure of Japanese economy - the imbalance between big business and small business, and between agriculture and industry.

The agricultural sector, where productivity and income levels are much lower than in the industrial sector, is holding a large number of potentially unemployed. The ratio between the productivity in the

agricultural sector and that in the industrial sector in Japan is 1 : 5, and the level of per capita income in the agriculture sector is only 37 per cent of the non-agricultural sector.

In Japan, the productivity of small enterprises, for example, hiring ten to nineteen employees is merely 44 per cent of that of big enterprises with over 1,000 employees. I understand the corresponding percentage in Europe is as high as ninety. I would like to invite your attention to the fact that such small enterprises with low productivity absorb over 70 per cent of the total labour force in Japan.

In order to raise the level of our national income, to increase employment opportunities and to liquidate the dual structure of our economy, Mr. Chairman, the Japanese Government considers it imperative to oriente the Japanese industrial structure toward the heavy and chemical industries, and to sustain a high rate of economic growth. Taking the above elements into consideration, the Japanese Government has set to work on a plan to double the GNP by 1970. In order to accomplish this plan, we must increase our imports on a large scale. In turn, to prevent the increase in imports from adversely affecting our balance-of-payments position it is apparent that we must boost our exports.

A number of difficulties are lying ahead of us in promoting our exports. I will now briefly touch on this subject.

Firstly, Mr. Chairman, Japan does not have large and stable markets in its adjacent areas as do the European countries who are in the process of forming prosperous economic groupings. Secondly, the composition of our export merchandise was such that, in 1959, light industry goods like textiles and sundries made up 49 per cent of total exports while the share of heavy and chemical industry products has been smaller than in highly industrialized countries. In the light of the tendency in world trade that the share of textiles and other light industry products is declining while the share of the products of heavy and chemical industries is rising, it is the view of the Japanese Government that we should in the future shift the emphasis of our export efforts from light industry goods to heavy and chemical industry products. Thirdly, in a country like Japan where natural resources are scarce, labour force is abundant and the general standard of industrial technology is fairly advanced, it is logical to develop heavy and chemical industries for raising the national income level, for the rate of value to be added is the highest in these industries. In reality, however, some of our heavy and chemical industries are not highly competitive on account of shortage of capital and lag in the modernization of plants and equipment, and in some cases in technological standard.

Fourthly, a number of our light industry products including textiles and sundries, and light machinery are often subject to discriminatory import restrictions. Particularly, the liberalization measures have not been

extended to Japanese products in some industrialized countries. Furthermore, some contracting parties to the GATT, unfortunately to Japan's regrets, are still refusing to enter into GATT relationship with Japan by invoking Article XXXV.

Taking this opportunity, and on behalf of the Japanese Government, I will earnestly appeal to all these countries to give thought to terminating undue restrictions and discriminations against Japanese products.

I hope I have been able to elucidate to you, Mr. Chairman and members of the Committee, the unique and difficult circumstances in which Japan finds herself regarding her balance-of-payments position and her industrial structure. In expediting the liberalization of imports, we cannot help taking these into consideration. I will assure you, however, that we have no intention of using this as a pretext for delaying our liberalization. We are all fully aware that liberalization of imports will be in our own ultimate interest.

Mr. Chairman, in concluding I wish to emphasize that my Government is fully prepared to ease the import restrictions, increase the allocation of foreign exchange, keep the liberalization programme under constant review, and speed up the liberalization, as far as our economic and social conditions allow.

ANNEX II

IMF Executive Board Decision of 16 September 1960 relating to Japan

1. The Government of Japan has consulted the Fund under Article XIV, Section 4, of the Fund Agreement, concerning the further retention of its transitional arrangements.
2. The Japanese economy made remarkable progress in 1959 and the early part of 1960. A sharp increase in output was secured under relatively stable monetary conditions. A substantial increase in imports in 1959 was matched by an increase in exports, and the balance of payments remained in sizeable surplus. Domestic financial policies contributed to this achievement. The credit policy of the Bank of Japan was aimed at avoiding the development of a boom, and government cash transactions with the public resulted in a small surplus in fiscal year 1959/60.
3. Recently, the rate of growth of the economy seems to have somewhat slackened. On the other hand, the demand for funds has continued to be strong. Also, with a further sharp increase in imports, a deficit has emerged on the current account, despite continued growth in exports. The increase in reserves that has recently occurred was principally due to a large inflow of foreign short-term capital. The Fund hopes that the authorities will continue to pursue budgetary and monetary policies appropriate to economic growth under conditions of monetary stability.
4. Japan has established partial external convertibility of the yen and made further progress in reducing restrictions and discrimination, including the termination of two bilateral payments arrangements. The scope of minor restrictive practices has again been reduced; it is intended in 1960 to terminate the retention quota practice and to reduce further the scope of barter trade, and as soon as possible in 1961 to terminate the linking system. The Fund welcomes these steps and urges the early elimination of the remaining discriminatory practices. Japan has drawn up a programme for substantially liberalizing trade and exchange restrictions within the next three years. The Fund notes the intention of the authorities to accelerate this programme as economic conditions permit, and believes that Japan's external position would permit a speedier liberalization of restrictions.
5. In concluding the 1960 consultations, the Fund has no further comments to make on the transitional arrangements maintained by Japan.

