

**GHQ/SCAP Records(RG 331)**  
**Description of contents**

THE  
NATIONAL ARCHIVES  
OF THE  
UNITED STATES

- (1) Box no. 2312  
(2) Folder title/number: (36) (end)  
Johnston Report

(3) Date: Apr. 1948

(4) Subject:

Classification	Type of record
111, 500	d

- (5) Item description and comment:  
"Report on the Economic Position and Prospects  
of Japan and Korea Measures Required to Improve  
Them"

(6) Reproduction:  Yes  No

(7) Film no. \_\_\_\_\_ Sheet no. \_\_\_\_\_



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REPORT  
on the  
ECONOMIC POSITION AND PROSPECTS OF  
JAPAN AND KOREA  
MEASURES REQUIRED TO IMPROVE THEM

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Committee to Inquire into  
Economic Problems of Japan  
and Korea.

26 April 1948



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### SUMMARY

In Japan General MacArthur, Supreme Commander for the Allied Powers, is administering the occupation of the four main islands which have a population of nearly 80,000,000.

The Committee has been greatly impressed with the complete demilitarization of Japan and with the progress made in developing representative government in that formerly feudalistic country. A thoroughly democratic constitution has been adopted and an elected Diet, or Parliament, is actively functioning. Unlike the situation in Germany and Korea, Japan is not cut up in separate zones of occupation, and a Japanese Government is actively dealing with the daily problems of its people. The Japanese people themselves seem to be fully cooperating with the occupation authorities. These are outstanding achievements.

Although two and one-half years have passed since the surrender, no treaty of peace has yet been signed. The United States has been paying the military costs of occupation and in addition, under its international law obligation as occupying power to prevent disease and unrest, has been furnishing food and other relief supplies to keep the Japanese people alive. These relief costs run to nearly \$400,000,000 a year. In our opinion the United States must now face squarely the problem of assisting the Japanese people to become self-supporting.

Japan has been shorn of its empire and no longer has under its control resources of food and raw materials which formerly contributed to its



prosperity. It has been expelled from China, Manchuria, Korea and Formosa, southern Sakhalin, the Kurile, Marshall and Marianna groups of islands. It grows only 80 per cent of its minimum food requirements. Its population is increasing a million a year. It must produce and export industrial products in large volume to live. It is short of natural resources and raw materials.

The Committee believes that the United States should now assist the recovery of Japan. Japan's industrial products are needed throughout the Far East, whose countries also need Japan as a market for their potential exportable production - their tin, rubber, copra, wool, cotton, iron ore, bauxite, sugar and rice. Japanese industry is operating at a very low level - - less than 45 per cent of the 1930-1934 average. Shortage of needed raw materials is a major reason. However, despite the upheaval of war and defeat and the changing social outlook, the traditional will to work of the Japanese people themselves is still in evidence. Food production and coal production have been rising, although both are still far below minimum needs. Food collections are better than at any time since the occupation - - in fact rice collections reached 100 per cent of this year's quota while the Committee was in Japan.

The reparations issue has not been settled. The Japanese do not yet know which plants and which equipment will be left to them, so, within industries thought to be subject to reparations, incentive to restore and reconstruct is suppressed. Plants which are needed in bringing about the recovery of Japan should be retained and only excess capacity removed.



Otherwise the United States, which is now extending relief to Japan, would in reality be paying the reparations bill. In our opinion, the capacity that can be spared without affecting Japan's useful peacetime productivity is not great. It is most important that the present uncertainty be removed and the reparation issue be finally settled.

Japanese exports have been growing and reached \$173,000,000 last year. Most of these exports, however, were made possible only by a special scheme of American assistance -- particularly in cotton manufacture. A beginning has been made, nothing more. Total exports will have to increase to eight to nine times present levels to provide payment for the imported food and raw materials needed to sustain a reasonable standard of life in Japan. In our opinion, it should be possible to accomplish this if tranquility is restored throughout the Far East, if present restrictions on Japanese trade and travel are lessened, and if help is given to import raw materials and get production going. An eventual shift in Japanese food and other imports from the dollar area to the sterling and Far Eastern areas, with compensation in Japanese industrial exports, is essential to any permanent Far Eastern recovery.

The Japanese merchant marine has been reduced by war losses to 20 per cent of its prewar size. Most of the larger ocean-going Japanese ships have been lost with the bulk of the remaining fleet consisting of small coastal and fishing vessels. Payment to non-Japanese shipping of present-day inflated freights on essential imports is a large factor in Japan's foreign trade deficit. We believe that Japan should be encouraged to increase its merchant shipping both by new building and by bareboat



chartering of available vessels.

Principal among Japan's internal problems is the inflationary spiral resulting from the extreme scarcity of raw materials and consumer goods, the constant upward pressure of wages and other costs, and the heavy budgetary deficit. The internal cost of the occupation adds to this problem. Until this inflation problem can be solved by greater production, increased tax revenues, and more rigid control of governmental expenditures, the establishment of a stable foreign exchange rate, and even of a stable internal economy, can hardly be achieved. Here again, the importation of greater amounts of raw materials and the resulting increased production will assist in a solution.

Drastic and continuing efforts by the Japanese themselves are necessary to balance the national budget. Self-help and self-sacrifice in clarifying and controlling internal price and wage relationships, in reducing national expenditures and increasing tax revenues, in expanding domestic production of food, coal and products from other Japanese resources, are essential to proper use of any American assistance and, of course, to economic recovery itself. The Japanese people will have to work hard and long, with comparatively little recompense for many years to come; in order to survive and support their growing population.

In conclusion the Committee agrees with General MacArthur and the Department of the Army that industrial recovery of Japan on a peaceful basis is necessary to bring about a self-supporting economy; that this program has now properly become a primary objective of the occupation;



and that the American Government in the national interest should support a reasonable recovery program.

In Korea the problem is complicated by the artificial division of the country into two zones of military occupation. The Koreans are eager for the independence to which our Government is committed. It has been impossible so far to hold elections throughout all Korea, but an election is soon to be held in the South Korean (American) zone, under the auspices of the United Nations. After the election and the establishment of a representative government it is proposed under the United Nations resolution to work out arrangements for the withdrawal of occupation troops.

Korean food production is improving and South Korea should eventually be able to supply its own food requirements if fertilizer requirements can be met. Other problems, however, are most acute. Lack of raw materials is greater even than in Japan. South Korea is dependent on North Korea for most of its electric power supply. The Korean railroads would stop if coal supplied by our occupation authorities in Japan were cut off. The industries which Japan developed during 40 years of Japanese control are operating at only about 20 per cent of capacity. South Korea is short of raw materials, and equally short of management and technical supervision formerly supplied by the Japanese. As in Japan, the United States has been supplying food, fertilizer, and petroleum products to keep the economy from collapse and to prevent widespread disease and unrest.

Here again the Committee believes, with General Hodge, our Military Commander, that reasonable assistance should be given to finance importation of raw materials necessary to increase production of agricultural and industrial goods. An interim aid program, not limited solely to relief,



should give a new Korean Government, when it is formed under the supervision of the United Nations, the needed help to establish the stable economic conditions so necessary to encouraging the development of free democratic government.

Finally, our Committee has examined the proposed recovery program prepared by the Department of the Army and supported by the State Department. The program would provide a total of \$220,000,000 for a twelve month period for raw materials and other recovery items for Japan, Korea, and the Ryukyu Islands. We believe such a recovery program essential in order to reduce and eventually eliminate spending in these areas for relief.

As an occupying power we have accepted a flag responsibility. We believe the United States can discharge this responsibility better, and end it earlier, by concentrating on economic recovery and by gradually reducing relief. Our Committee therefore recommends approval and execution by our Government of the suggested recovery program at the earliest possible date.



## GENERAL ANALYSIS OF THE SITUATION IN JAPAN

Japan's prewar social and economic policy was developed to serve political and military purposes. Growth in population continued without regard to the limited resources of the four islands which are the homeland of Japan. A large part of Japanese working effort, capital and resources were absorbed in the maintenance of armed forces and the construction of arms plants. Part of the rest was used to develop railways, mines, factories and other sources of supply in the conquered lands — Formosa, Korea, Manchuria and North China. Industry was forced to conform to military needs and purposes and became subject to government orders.

Economic development within Japan and peacetime needs suffered; much of the effort, capital and resources that might have served to improve industry and agriculture within Japan proper were diverted. The stocks of gold, foreign exchange and raw materials were expended in the same effort. Japan supported her expanding population by getting food, raw materials and the product of controlled labor from the countries brought under its domination.

In short, Japan's economic life was shaped to fit its attempt to become the dominating center of Asia and of the whole Pacific world. The working lives and prospects of the Japanese people crowded on the home islands were put on the gaming table of expansion and war. This reckless gamble was lost.

Defeat left Japan a ruined nation. The conquered empire was lost;



with it, the great investments which Japan had made. Within Japan proper, there was great destruction of houses, cities and factories. The merchant fleet, by means of which Japan carried on its trade, was also lost. Remaining inventories of raw materials, especially imported raw materials, such as oil, cotton, wool, coking coal, rubber and salt were small. Farm lands were neglected and supplies of fertilizer, seeds and tools insufficient. Food production within Japan was insufficient to supply even a minimum subsistence for the increased population; for, besides a rate of growth of about one million per year, some five or six million Japanese were returned from the lost territories. Coal production within Japan was completely inadequate for minimum needs of power, fuel and transport.

Finances of the government were in disorder. The financial situation of many banks and corporations was shattered because of the loss of assets abroad, war destruction, or depreciation of properties.

Such were the consequences of Japan's gamble in the use of force as a way of building a satisfactory economic life. Such is the situation which the Japanese people of today have inherited.

It is needless to emphasize the great measure of sober understanding, hard work, endurance and patient cooperation that will be necessary to correct it. In judging the Japanese effort to do so, it should be borne in mind that success or failure will not lie entirely within Japan's control. Peace and productive progress in the outside world, especially in the rest of Asia, will make Japan's task easier; a continuation of international dissension and world-wide shortages of goods will make Japan's task harder.

The American Government has accepted and is discharging broad



responsibilities as the occupying power. It has sustained order without which the effort of recovery could not go on. It has encouraged the adoption of a new basis of government in which individual energies and abilities may find greater growth and opportunity. It has prevented starvation and disease, making more generous appropriations for such essentials as food, oil, fertilizers and seeds than any victor has ever before given any conquered enemy. It is aiding the Japanese people in their effort to adjust their economy to the circumstances that confront them. Congress is now being asked to consider a program for providing Japan an essential minimum of supplies, particularly raw materials, required to make progress toward self-support. This would be a new departure in American policy in Japan. It is based on a common sense approach: Some branches of Japanese industry could be making goods that other countries need if these industries had the raw materials; but Japan cannot pay for them now; we could send them; Japanese industry could convert them into finished goods; by selling part of these goods abroad it could get the dollars to pay for the raw materials; the rest of the product could remain in Japan where it is badly needed.

This program should be carried forward by the American Government. The accepted responsibility has been to maintain order, to stimulate reform, to prevent disease and unrest. Now we should concentrate upon the ways of revival and provide certain minimum essentials without which Japan can not become self-supporting.

The first economic need of Japan is increased production. The production of domestic industrial raw materials and fabricated goods now is less than 45 per



cent of what it was during the years 1930-1934. Exchange of Japan's fabricated products for such raw materials as oil of the Dutch East Indies, iron ore of North China, sugar of Formosa, wool of Australia, rubber of the Malay States, rice of Indo-China, all have almost ceased for the time being. Domestic cereal production takes care of only 80 per cent of Japan's current need. Fishing, the other main source of food in Japan, is only half what it was; the Japanese fishing fleet is reduced and unable to fish in many waters hitherto open to it.

The Committee, therefore, looked into the present obstacles to production to discern the means by which they could be lessened. There are many deterrents and each affects the rest. But for the purpose of examination, they may be divided into two main groups. One of these may be called physical, the other institutional.

The three main deficiencies in the physical means available to Japan are: (1) lack of essential raw materials, (2) the bad condition of many existing factories, (3) the poor state of transport. The deterrent effect of each of these upon production is evident, but it may be useful to illustrate each briefly.

1. Because of a shortage of coking coal even such parts of the Japanese steel industry as are in physical condition to operate, cannot do so fully. Cotton looms and spindles stood idle because of lack of raw cotton until the United States provided some. Without enough wood pulp, the rayon mills must remain largely without work; without enough hides, the shoe and leather industries cannot resume satisfactorily; without rubber, all branches of industry making vehicles suffer; without enough salt, operations of the chemical industries cannot provide the chemicals



needed by other branches of manufacture; without enough oil, machines cannot be lubricated, ships cannot run, trucks cannot carry products from place to place.

The existing shortage of raw materials today is keeping Japan's production much below its potentialities. Despite all the other existing defects of the Japanese economic situation, a marked improvement will result if and when raw material supplies are more adequate. Processed and sold abroad, they could provide the financial means for successive steps forward; in contrast unless these raw materials are secured, trade will be very small and Japan cannot avoid a long period of suffering and dependency.

An increase in the production of all raw materials that can be produced within Japan (such as coal, copper, brick, cement and wood products) should be the first order of Japanese business. There should be, as far as possible, an adaptation of the Japanese economy and life to the use of local materials, since even if trade grows rapidly, available imports are almost sure to be less than the total needs of a fully employed Japan.

2. During the war, and since, equipment in many important industries, suffered war damage, fell into disrepair, or had vital parts broken or vital machinery removed. For example, the present initial output of aluminum is handicapped by the state of the lining of the furnaces; coal production is much lower than it would be if the machinery at the mines were in good shape. Next to the acquisition of raw materials, the repair and modernization of such plants and equipment offers the best and quickest contribution to recovery.

3. Production is suffering many delays and interruptions because



of the poor state of the railways and railway equipment and lowered operating efficiency. Also contributing is the extra burden placed upon the railways by the dearth of coastwise shipping. Many branches of industry in the Tokyo region, for example, recently were forced to suspend operation because of the failure of charcoal shipments to arrive from other parts of Japan; much cut timber is lying in the forests of Hokkaido, waiting to be taken away; movement of badly needed iron pyrites to the fertilizer plants has been delayed.

These physical deficiencies can be overcome gradually as Japan makes fuller use of its natural resources, improves its methods of production and rebuilds trade with the outside world.

Despite all physical limitations, production could even now be at a higher level, were it not for other deterrent influences affecting adversely the desire to produce, work, plan and invest. These mount up to a lack of reasonable assurance of reward and incentive. The whole production effort is taking place in an atmosphere of uncertainty, which affects workers, managers and owners. It is causing production and effort to be reduced, fitful and unsteady. This uncertainty must be eliminated.

The Committee has studied its several causes attentively. Some are the direct and unavoidable consequences of the war and war settlements. Important enterprises in Japan suffered great losses through war damage, cessation of arms production or when their property outside Japan was lost.



Their financial bases have been weakened or destroyed and their organization disrupted. The necessary financial reorganization of these enterprises should be carried out rapidly.

The threat of removal for reparations hangs over much of Japan's industry, especially heavy industry. Owners and directors who fear that their property may be taken from them will not exert themselves to bring that property back into production or to use it fully. It is, therefore, imperative that decision be reached promptly as to which excess Japanese plants and equipment are to be subject to removal as reparations and that the rest be given assurance that they will remain untouched.

Another element of uncertainty derives from the changes being effected in the control of Japanese industry. A very large part of Japanese industry before the war was dominated either by the government or by private monopolistic groups. Many of the principal enterprises established in conquered countries such as Formosa or Manchuria were creatures of the government. A great part of Japanese industry, trade, shipping, and banking were under the control of a few small family groups collectively known as the "Zaibatsu". These and other interests were linked together in many and close associations and groups to regulate production and control competition.

Japan has a well established social structure and code of economic rights and duties, especially as between workers and employers, quite different from that prevailing in the United States. Some important industries, for example, carry out stages of their production in thousands of small family workshops; the organized handling of their products was customary and in some ways useful. It was customary for some industries to continue employment and wage payments to all employees, whether there was work for



them or not; and wages were graded according to the personal and family needs of the workers. These and other customary practices naturally led to limitations on the intensity of competition. Such customs and practices cannot and should not be violently disregarded or abruptly terminated and must be borne in mind when judging agreements among employers.

But the practices of combinations, monopoly and concentrated control in Japan went far beyond arrangements required to utilize the family workshops or maintain customary social protection. As already observed, a small number of family groups, through holding companies and controlled banks, owned and directed a large part of all Japanese industry, shipping and finance. In various basic fields such as steel and paper, one company controlled 80% or over of all production, maintaining a suppressive monopoly. Such excess concentration of power and ownership had bad economic, political and social effects. They could, and sometimes did, dominate the government. They could be inefficient and still survive. They could and did repress the emergence of business ability. This concentration of control lent itself to easy domination over production for aggressive war.

For these reasons the Japanese Government, under the Allied policy, is seeking to diffuse the ownership and control of Japan's productive plants more widely and to develop greater competition. This policy should, after the adjustments have been made, bring greater and more effective production — if care is taken in carrying out the necessary measures of reorganization. But during the process of deconcentration, which is now going on, uncertainty is inevitable and may now be holding back production in some fields, since existing managements <sup>do not</sup> ~~cannot~~ know how to plan.

The period of uncertainty caused by this economic reform should be



made short and the area of uncertainty lessened as rapidly as possible. The possible disturbing effects should be allayed by care not to hurt production, and by limiting reorganization to the minimum necessary to insure reasonable competition. This we understand is the intention of the occupation authorities and is further assured by their establishment of an American review board to see that deconcentration plans do not adversely affect production and the broad program to achieve economic recovery. Care must also be taken that breaking up of the Zaibatsu monopolies does not lead to the growth of governmental monopolies.

Such are some of the elements of uncertainty bearing on the conduct of business enterprise. There is another of a general character -- the serious inflation prevailing in Japan. Prices of essentials (food, clothing, housing, fuel and light) are about four times higher than they were at the beginning of 1946, despite official controls and subsidies. The increase in prices and the general level of costs of production would be much higher still if the American government had not, under the relief program, supplied large amounts of essential products such as food, fertilizer, seeds and oil. These have made it possible to prevent prices of food and other consumer goods and of goods used in production from rising so greatly as to destroy trust in the value of money. Paper money outstanding has increased many more times than the volume of goods; in 1939 it was less than four billion yen, at the end of the war it was about 55 billion yen, and in March 1948 it was about 220 billion yen.

This inflated price situation means that employees of factories and offices and farmers, whose money income has vastly increased but who cannot buy many of the things they want, live anxious lives. Their real return



for work ceases to be related to effort and becomes subject to chance and sudden change. This discourages steady effort, diverts activities and products to the black market where shrewdness and selfishness count more than usefulness. It penalizes integrity and rewards chicanery. Similarly, the managers of business, large and small, often cannot tell whether they are making a profit or loss. Costs become uncertain and long-term contracts impossible. Business becomes dependent on the government or banks for working capital. Interest rates become so high that only those who know they can sell at an advanced price can borrow. Goods are hoarded. The costs of government are forced up revenues lag, deficits grow, and the inflation and its demoralizing effects are extended.

It has become imperative that the course of extreme inflation within Japan be arrested. Moderate general price increases may sometimes stimulate production; and relative increases in particular prices may stimulate the production of goods particularly needed. But the price situation and trend in Japan is now retarding industrial production and causing wide-spread anxiety for the future.

The Japanese Government, encouraged and supported by the American occupation authorities is making strenuous efforts to curb the inflation and not without success in certain strategic elements of the problem. Collection of foodstuffs has been much better than before; the rationing system has become more effective; coal production has been substantially increased; tax collections have improved and the will to restrain public spending has strengthened. These are encouraging signs.

The Japanese people must adjust their supply of monetary means of payment to their supply of goods. This can only be done by ceasing to add



to their supply of money and increasing their supply of goods. Neither can be done entirely by gentle means; each group, section and part of Japanese life will have to reconcile itself to getting along with little until there is more to share. There must be a government strong enough to stand out against those who will not do so voluntarily.

Basically, the inflation is the result of the scarcity of goods. But it has been cumulatively increased by meeting government deficits by additions to the volume of currency. Even under the present straitened circumstances the attainment of a balanced budget, or substantial progress toward that goal, should be possible. The vast outlay previously carried by the Japanese Government for military purposes is now saved although this is partially offset by necessary occupation costs. Nonetheless, the attainment of a budget balance will require the most stubborn will, great political courage on the part of the government, and great patience on the part of the Japanese people.

No matter how determined an effort may be made to limit the supply of money, it is certain to fail unless Japanese production grows. Reference has already been made to certain deterrents to this urgently needed increase in production. There are still others to which attention might well be directed.

The output of workers in various branches of industry and mining is lower than before the war. This is due in large part to defective tools, interruptions in the supply of raw materials, inadequate food, housing and clothing. Output will probably increase when and as these conditions are improved. But in some measure it appears to be caused by lessening of effort



and hindering rules or terms of work. Such tendencies appear whenever, as now, there is fear of lack of work to go around.

It is essential that the Japanese workers should during this period of strain and scarcity labor hard and well, as they have in the past. Japan needs their product, both to supply the domestic market and to provide the means of trade. To rebuild the required volume of trade, Japanese industries will have to meet external competition, and find their way into foreign markets by offering goods on attractive terms. The alternatives are for the Japanese people to endure an even lower standard of living on their crowded islands, or to be permanently dependent on outside charity.

Resumption of Japanese trade will be affected by the attitudes and policies of other countries, their willingness to permit Japanese shipping to carry a reasonable tonnage, and recognition that discrimination against Japanese trade would not be in the long-range interests of world trade and prosperity. Again, if production and trade of other foreign countries increase, Japan's prospects will benefit; if they lag, Japan's task of regaining balance and stability will be the harder. Reciprocally, an improvement in Japan's production and trade will aid other countries if they make use of Japanese goods and services.

The return of tranquility and settled political conditions in those other Asiatic countries which are among Japan's natural customers would help greatly. An increase in total world supplies of raw materials would help Japan by encouraging other countries to enter into trade agreements with Japan and by reducing the prices of needed materials. So also Japan's exports sales would be aided if the present world-wide dollar shortage is alleviated.



For this reason the European Recovery Program should benefit Japan as well as the countries directly helped.

In essence, it may be said that the three connected problems that Japan must solve are: (1) to increase production, (2) to end inflation, and (3) to develop trade. All will take time and all originated in a condition of disturbance and scarcity. The means of production are scarce. It is therefore necessary that they be put to the best use, that available supplies of tools, parts and raw materials be allocated to those who can make them yield most, and that food and consumers goods be fairly and honestly shared.

This justifies the controls now being exercised by the government over the supply and use of such goods. But it places upon the Japanese people and government the duty and burden of seeing that the controls are intelligently and honestly exercised.

Controls on prices are also necessary for the present to combat the inflation and to promote the general welfare. Again they call for moderation and patient acceptance by all. Constant pressure by wage-earners for higher money wages will either force constantly rising prices or require larger and larger government subsidies. Unjustified demands by producers of industrial goods for higher prices will intensify pressure for higher wages and increase social unrest. Cost-price relationships in industry must give producers some incentive but no excess gain. They cannot be expected to operate at a loss, as some are doing at present; but they cannot expect to rebuild their business or fortunes quickly in this time of scarcity.

The same comment applies to the farmers of Japan. Before the war and before the reforms encouraged by the occupying authorities they were an oppressed.



group within Japan. Making up about 45 per cent of the Japanese people, they received little more than 10 per cent of the national income. Now they are comparatively much better off; it is roughly estimated that they receive nearly 35 per cent of the reduced national income. It is of first importance that they (1) continue to increase food production, (2) deliver their products into regular channels and (3) recognize that higher prices for the food they produce will only increase inflation.

Trade unions in Japan are being given a chance to prove that they can protect the interest of employees without frustrating production. Business under government control is being given a chance to prove that it can gradually reconstruct a self-supporting and socially satisfying situation on the ruins of war. Each is dependent on the other and both must accept governmental controls on their private desires as long as they are necessary. As scarcities diminish, these controls should be relaxed or removed. They are, it is to be hoped, only temporary aids on the road to the establishment of a free enterprise system.

Our Committee, in its studies of the Japanese economy, has assumed that peace will continue, that the cooperative relationship between the Japanese and the occupation authorities will be maintained, and that Far Eastern countries, along with other areas of the world, will gradually recover from the dislocation and shortages caused by the war. Discussion and specific recommendations dealing with the various subjects to which the Committee addressed itself follow.



## RAW MATERIALS AND FOREIGN TRADE

To achieve economic recovery, Japan must secure a far greater volume of raw materials than at present. It can, by careful planning and effort increase the supply of a limited group of raw materials found within Japan: bituminous coal, copper, lumber and other building materials. But most of the products required by industry are not found within Japan. These are too numerous fully to list: textile fiber and wood-pulp for its cotton and rayon industries; iron ore, manganese and coking coal for her iron and steel industry; bauxite for the aluminum industry; rubber, tin, zinc, lead for the manufacture of vehicles, farm tools and machines; salt and other chemicals for her fertilizer plants; copra for soap-making; oil for the whole of her economy. To secure these Japan must begin to trade again with the rest of the world on a large scale. Hardly less important is Japan's need for certain essential parts and components for its industrial plants, which Japan will have to import until its own industries are repaired and re-established.

The relatively meager revival of Japanese foreign trade has until now been largely dependent upon raw materials and supplies made available by the United States. Failure to press vigorously for restoration of foreign trade would prolong the expensive necessity of underwriting Japanese deficits.

SCAP\* has estimated that under favorable conditions and with reasonable aid from the United States, a balance between exports and imports should be attainable by 1953.

It has been estimated that Japan will require about \$1,575,000,000

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\*Supreme Commander for the Allied Powers, General MacArthur. SCAP is also used, as indicated by the context, to refer to his staff.



of exports each year (at current prices) to pay for essential imports of food and raw materials (and necessary invisible imports) to maintain a tolerable food ration and standard of living at home. A balance of payments could, of course, be maintained with lower exports and imports, but at the cost of a lowered and perhaps unbearable standard of living in Japan. An increase of at least eight to nine times 1947 exports is necessary to meet the goal set. Under favorable circumstances of world and Japanese trade the Committee considers that this goal may be attainable, although the realization of these estimates is obviously subject to many uncertainties both in Japanese and in world wide economic and political conditions.

During 1947, imports into Japan were \$526,130,000 and exports were \$173,568,000. Approximately 25% of the imports were financed by foreign exchange created by the sale of Japanese exports, the balance being the value of relief supplies procured with United States appropriated funds. It will be seen, therefore, that the most strenuous efforts will have to be employed to reach the 1953 targets. The Committee makes the following comments and suggestions which, if successfully carried out, should assist materially toward this end. It recognizes fully that the occupation authorities have been striving to overcome many of the obstacles involved.

First, Japan's merchant fleet should be substantially enlarged. Out of 5.75 million gross tons of steel vessels over 1,000 gross tons before the war, there are now afloat in the hands of the Japanese 1.15 million gross tons of serviceable or repairable vessels. Since a large number of these vessels are necessarily engaged in domestic coastwise services, the reduction in vessels available for overseas foreign trade has been greater than the overall 80% loss indicated by this tonnage comparison. Even if



given every opportunity to increase merchant shipping, by building, purchasing and bareboat chartering, it will be many years before Japan's merchant tonnage can be reasonably adequate for its needs.

Prevailing costs of transporting goods to Japan are extremely high. For instance, salt, which sells at \$3.00 f.o.b. Mediterranean port, costs \$14.00 additional to land in Japan. Iron ore, at \$7.00 f.o.b. Hainan, costs \$9.25 additional to land in Japan. Coking coal, at \$12.00 f.o.b. Canada, involves a freight charge of \$14.00 to \$16.00 to deliver in Japan. The Japanese have always been effective ship operators and builders. Their shipbuilding and ship operating costs have been low as compared with other countries. They have the know-how and the manpower. To the extent that they are able to employ domestic shipping and shipbuilding facilities, they will be enabled to reduce their substantial need for foreign exchange now required for shipping services.

Japan has valuable facilities for the construction of ships of all <sup>2</sup>sizes. Present restrictions on building vessels of six thousand gross tons and more should be lifted to permit building for their own use and on contract for foreign buyers. There are indications that such orders would be available to them.

The argument has been made that Japan's shipping should be limited because of its war potential. However, Japan's army, navy and air force have been abolished so there should be little fear of future Japanese aggression from the mere existence of a merchant fleet. Also, it has been historically the American position, and generally recognized by maritime nations, that world trade and the long range interests of all nations are best served when the high seas are open to all. Purely competitive considerations do not, in our opinion, justify a prohibition that would prevent the Japanese from



developing the necessary merchant shipping to assist in balancing their foreign trade.

Second, the Committee recognizes that by reason of the economic upheaval stemming from war, Japan will, of necessity, be forced to seek export business throughout the world. Besides textiles, it is capable of producing modern machinery and metal products of diversified character. Chemicals, rubber products, pottery, toys and handicraft all are potential exports. Where its products are fairly competitive and it uses fair methods of marketing, they should be admitted to the world's markets.

It is important to the Japanese (and to the American taxpayer) that we use our influence to overcome the understandable trade discriminations which are practiced against Japan, especially in markets in which they have heretofore enjoyed large trade. In the judgment of the Committee the countries involved are impairing their own well-being by refusing to trade with Japan and are retarding the reactivation of a potentially valuable economic asset for the benefit of all Asiatic countries. We, in the United States, have been called upon to overcome deep and justifiable resentment in our attitude toward Japan. Neighboring nations have much to gain by the adoption of a now and more receptive attitude. The reciprocal advantages ensuing are unmistakable.

Third, our financial assistance to both China and Japan can be most productively employed if active trade between them is resumed. However, China is not at present trading any important volume of goods with Japan. Many raw materials can be sold by China to good advantage in Japan; in turn, Japan has many commodities and facilities which China needs. United States trade policy is emphatically in accord with this philosophy. The European Recovery Plan is based upon it.



Fourth, it would be advantageous if Japan could obtain the foods it imports from nearby sources as in the past, rather than from the more expensive dollar areas as at present. Perhaps this cannot be arranged immediately, but, as these neighboring countries move toward more normal production, restoration of these trade patterns should be possible. This will be helpful to both the Far Eastern and American economies.

Fifth, the Committee recognizes that, in a scarcity economy requiring equitable allocations of available raw materials and other products, government must continue to play an important supervisory role over trade. However, the restrictions and red tape now required by the Japanese authorities are undoubtedly hampering trade. Although the Committee has been informed that both the Japanese Government and the occupation authorities are taking steps to simplify and streamline the methods of handling business transactions, it urges that this be done quickly and thoroughly. Direct business contracts between buyers and sellers should be encouraged. Liquidation of the Foreign Trade Kodans (government buying and selling monopolies) as soon as the acute need for raw material allocations ends, and limitation of the operations of Boeki Cho (government foreign trade agency) to the minimum, seem to be well advised.

It is also desirable to establish direct contact between Japanese businessmen and their potential customers by permitting the movement of Japanese nationals to foreign markets.

Sixth, all export possibilities must be stimulated. As has been already stated Japan historically has always been a processing nation which purchased raw materials abroad, manufactured them in Japan and sold a major portion of the finished products abroad to pay for its necessary imports of raw



materials and food. This economic pattern has been even more true of Japan than of Great Britain or Western Germany, and must be revived on a large scale for Japan to live.

Prior to the war textile products constituted <sup>60%</sup>~~80%~~ of Japan's exports. The remaining 40% comprised mainly machinery, metal products, chemicals, rubber products, pottery, toys and handicraft articles.

The cotton textile industry represents a vital force in the creation of a healthier Japanese economy. There is a present demand for its products, but great difficulties have been experienced recently in making foreign sales in dollars because of the world-wide dollar scarcity. Under existing circumstances, attention should be given to three-way transactions, such as shipment of cotton from the United States to Japan, manufactured textiles from Japan to the Netherlands East Indies and tin from there to the United States in an amount sufficient to repay the cost of the raw cotton. Normally, the cotton industry is highly competitive to operate successfully, Japan must be in a position to adjust its marketing practices to this reality.

The Commodity Credit Corporation contract for the manufacture and sale of cotton yarn and goods products from raw cotton supplied by it has not yet been liquidated. All possibilities of sale must be vigorously pursued. The large potential United States market should not be excluded from this effort. The possible volume of Japanese cotton textiles that might be offered for sale in the United States would be only an insignificant percentage of United States production and constitutes no threat to American producers as long as present fair merchandising methods are pursued.

It is obvious that unless a sufficient portion of the textiles manufactured from American cotton to repay the cost of the raw cotton is sold for dollars or some commodity or currency which can be converted into dollars,



Japan will be unable to buy American cotton. Historically, the Japanese used a large percentage of American cotton and it is of great interest to American cotton growers that this problem be solved realistically so that the large potential Japanese market not be lost.

We endorse the cotton credit now pending in the Congress; it should include only sufficient limitations requiring direct or indirect dollar sales of goods to assure repayment of the credit. Japan should be permitted to accept sterling for that portion of fabric and yarn sales not needed for dollar repayment, purchasing therewith necessary imports from sterling areas. Japan's textile manufacturers are at present unable to employ the hedging facilities of the cotton futures markets, and this disadvantage should be overcome as soon as possible.

The expanded use of the woolen and worsted facilities of Japan can produce substantial benefits and should be encouraged.

The rayon industry has been dependent in large measure upon domestic pulp supply. Arrangements have been recently completed for a substantial tonnage of Swedish pulp, with which it is hoped to improve the quality and quantity of rayon production. Inasmuch as Japan has no facilities to supply rayon yarn in cone form, it is limited to skein packaging. This fact, plus the fact of the comparatively inferior quality of the Japanese product, puts it at a disadvantage in world markets, more especially in countries equipped with high speed processing facilities. While the export of rayon yarn is desirable, too much early hope should not be built up in this direction. The relatively low price of rayon staple fiber throughout the world and the fact that the Japanese product is not favored because of its poor quality do not encourage the belief that they can quickly develop large export demand. Therefore, in the judgment of the Committee, rayon yarn and staple



fiber production should be planned with primary emphasis on spinning and weaving these rayon products in Japan. A large percentage of this fabric production should be readily salable in this form to foreign buyers.

Raw silk and silk products were one of Japan's chief prewar trade assets. Export sales of raw silk for 1935-39 ranged between 400,000 and 500,000 bales annually and those of silk fabrics ranged between 75 and 125 million yards annually. From the surrender to the end of December 1947 (over two years) only 44,210 bales and 12.5 million yards were sold. Since January 1, 1948, with more realistic pricing and sales policies, 20,000 bales and approximately 5.2 million yards were moved.

Before the war, and increasingly during the war and since, silk has lost favor. Growing nylon and rayon competition has been largely responsible for this decline.

The Japanese are using all their ingenuity to overcome some of the technical difficulties which the use of silk involves in competition with other fibers. It is likely that the situation is now at its worst and that gradual improvement both in raw silk and silk fabric sales will be experienced.

In addition to gradually increasing textile exports, it is planned to expand largely export sales of machinery and metal products, ceramics, minerals, chemicals, drugs, handicraft, toys, processed fish, and paper and wood products.

Fundamental to any successful export program is control of inflation, which is dealt with in another section of this report, and the supply of the necessary imported raw materials to get the program under way.

We find a difficult circle of circumstances in the Japanese productive economy. Insufficient necessary raw materials result in insufficient production; insufficient production results in insufficient exports; insufficient exports result in insufficient foreign exchange to pay for the necessary



raw materials. Until this circle is broken Japan's economy will remain prostrate and dependent upon a food dole such as the United States is presently supplying. The best way to break the circle is by supplying sufficient dollar exchange to enable Japan to purchase the initial foreign raw materials.



## REPARATIONS

Reparations policy toward Japan has been in the process of development since the surrender in August 1945. Reports of the Pauley Committee, the National Engineers Council, the Special Committee on Japanese Reparations (Strike Report), the Economic Analysis of the State Department, reparations studies of SCAP, studies made by the members of the Far Eastern Commission and finally the comprehensive report of Overseas Consultants, Inc., all have contributed to a better understanding and clarification of the problem.

These reports differ in many respects, yet all are in agreement on these two promises:

- (1) Japan's industries must be so demilitarised as to prevent it ever again becoming a threat to the peace of the world.
- (2) Japan should be left sufficient industrial capacity so that it will have an opportunity to develop an economy which will provide a tolerable standard of living.

In seeking to determine the amount and character of industrial plants required to meet the objective stated in (2) above, various estimates were offered. The earlier estimates differed so widely that the occupying authorities decided there was need for an all-inclusive and detailed analysis of the Japanese plant and its potential. Consequently, in June 1947, Overseas Consultants, Inc., an organization of eleven distinguished industrial engineering and appraisal companies, was formed and engaged by the Secretary of War to make such an analysis.

Its report, presented on February 26, 1948, consisted of two major sections described as follows in letter of transmittal:



"Section A presents designations of those plants and facilities which should be retained and those which should be made available for reparations under the terms of State-War-Navy Coordinating Committee 236/43, together with estimates of the value of the facilities available for reparations. These designations were based upon a literal interpretation of original instructions, as amended, establishing the productive capacities in certain industries to be retained in Japan, outlined in State-War-Navy Coordinating Committee 236/43. In this section we express no opinions in regard to the adequacy of such retained capacities for achieving a self-sustaining civilian economy.

"In Section B, we make recommendations and name plants and productive capacities which, in our opinion, should be retained. These are the results of a study of economic conditions in Japan, made by our representatives, based upon data made available to us by the Economic and Scientific Section, (hereinafter referred to as ESS), the Natural Resources Section and other divisions of SCAP, and by various Japanese agencies, and upon our analysis of basic requirements of food, clothing and raw materials, the need for rehabilitation of industrial plants and utilities, and the restoration of areas damaged during the war."

The report of Overseas Consultants, Inc., in effect advised against the removal of productive facilities (except primary war facilities) which might effectively be used in Japan; this view was derived from the judgment that, only if Japan was permitted to retain all facilities that might contribute to its production and potential trade, could it by its own efforts maintain a satisfactory minimum standard of living.

The value to the recipients of the industrial reparations which would result from the new formula recommended by Overseas Consultants, Inc., would be disappointingly small in contrast to that which has been requested and expected by some of the Allied Powers. It must be remembered that much of the industrial plant within Japan was either destroyed or badly damaged by the war and that actual productive excess, except in a very few fields, is correspondingly small. In our opinion, even if the Allied Powers received all the reparations requested from the home islands of Japan, they



would gain little because experience has shown that the costs involved in moving plants and equipment from a conquered nation and reestablishing them in a victorious nation are high and that the ultimate usefulness and value of such plants are small, being poorly adapted to needs of the new owners. World War I experience proved that reparations paid out of current production were illusory and most difficult to collect; World War II is proving that reparations paid in the form of plant equipment are also of dubious value.

Japan did have one form of assets of real value as reparation. These assets were investments throughout the world and particularly in Japanese territories and protectorates. They have a value of many billions of dollars. Both Soviet Russia and China have benefited from the billions in assets, undamaged by war, which Japan invested in Sakhalin, Manchuria, North China and Formosa.

The cost in lives and treasure to bring about the surrender of Japan was enormous. The United States bore a heavy share of that cost. Since victory was achieved, military government and relief costs have been borne almost entirely by the United States. Until the new Japan, shorn of its empire, can become self-supporting it will continue to be a burden. The loss of plants, equipment or machine tools needed to help Japan achieve a self-supporting basis would result in an increased necessity for the United States to make up the deficiency or lessen the chances of attaining economy solvency. Under such circumstances, reparations become a direct charge on the United States.

The United States is also paying a high price for delay in the settlement of the reparations question. As long as uncertainty prevails as to



what is to be taken as reparations it is impossible to plan intelligently for the rehabilitation of Japan's industry. The Congress of the United States is considering an appropriation of some \$144,000,000 for the economic revival of Japan, in addition to nearly \$400,000,000 for general relief purposes for the fiscal year of 1948-1949. Accordingly, an early definitive and authoritative action on reparations problems is imperative; the success of the entire recovery program will be affected thereby.

During the past two and one-half years, the Far Eastern Commission has agreed to but few policies affecting certain phases of the reparations program. An "advanced delivery program" was adopted by the United States to provide foreign nations with some badly needed equipment. To date this program has made available 19,032 machine tools and 3423 pieces of laboratory testing and measuring equipment.

The Committee has given careful consideration to studies and recommendations made by the various groups heretofore, and, after carefully considering on-the-scene data, recommends that:

- (1) External assets formerly owned by Japan be formally released to the countries holding jurisdiction over the territories in which these assets are located.
- (2) There be made available as reparations from the home islands of Japan the machinery and industrial equipment in all government-owned arsenals except for (a) such equipment ~~as~~ is deemed necessary by SCAP for the Japanese economy or for occupation use, and (b) such non-armament facilities (fertilizer, fuel, oil storage, etc.) as were exempted from the interim reparation program by the FEC policy decision of 13 May 1946.



- (3) There be made available for reparations certain other plant and equipment listed at the end of this section.
- (4) These recommendations be made effective at the earliest possible moment by appropriate directives to SCAP, which directives should include (a) percentage shares of the total to be allotted to each FEC nation or a limiting date prior to which those nations should settle the division between them of the total available items, (b) a limiting date for the acceptance by each nation of the items allocated to it, and (c) a statement that these directives supersede all previous directives on the same subject.
- (5) No industrial equipment in addition to that included in those recommendations be made available for reparations: Provided, however, that SCAP should be authorized to substitute for any item specified in these recommendations any other item of equivalent productive capacity.

If the above recommendations for a final reparations settlement are carried out, the amount of plant equipment and the number of machine tools available for reparations will be reduced below the level recommended by Overseas Consultants, Inc. Our major purpose in recommending this reduction is to retain for the rehabilitation of Japan's peacetime industry a substantial number of machine tools of modern design. Only by retaining such tools can the peace-time industry of Japan quickly be rehabilitated on an efficient basis. In view of the developments of the last two years and the continuing deficit economy, there is, in our opinion, a cumulative urgency for the rapid rehabilitation of Japan's industry.



Paramount to all other considerations is the need for prompt and final action. Further delay in the settlement of the reparation problem will not help the claimant nations and will hurt Japan greatly.

SUMMARY OF RECOMMENDED REMOVAL FOR REPARATIONS

<u>Industry</u>	<u>Capacity</u>	<u>Value (1939 yen)</u>
Nitric Acid	Metric tons 83,000	8,000,000
Synthetic Rubber	Metric tons 750	10,000,000
Shipbuilding	Gross Tons 162,000	50,000,000
Aluminum and Magnesium Fabricating	Metric tons 50,000	21,688,000
Magnesium Reduction	Metric tons 480	<u>12,559,000</u>
Sub total		102,247,000
Primary War Facilities		<u>560,000,000</u>
Total		662,247,000

PRIMARY WAR FACILITIES

Valuation of Facilities to be Made Available -- ¥560,000,000.

NOTE: Only those primary war facilities in government owned arsenals should be made available for reparations. Those facilities within the government owned arsenals designated by the Supreme Commander for the Allied Powers, as essential for the rehabilitation of Japan's industrial economy, should be exempted.



## THE POSITION AND PROSPECTS OF FOREIGN INVESTMENT

The present situation in Japan as to capital needs is somewhat obscured by the uncertainty about reparations. However, assuming a reasonable and prompt settlement of that problem, Japan would retain sufficient industrial plant and machine tools for the production of a volume of most products needed to meet internal needs and produce a surplus for export. A very different situation prevails as to working capital. Most Japanese concerns, both industrial and marketing, because of operating losses and inflation, are hampered by a dire lack of funds to purchase raw materials, to replenish inventories and for similar purposes. This is a problem chiefly of foreign currency needs which could best be met by equity investment. Unfortunately, almost no new foreign investment is permitted in Japan at the present time.

Foreign private commercial representatives have recently been authorized by SCAP to enter Japan to seek restitution of prewar holdings and to engage in export-import trade. They may now work out arrangements under which raw materials are shipped into Japan and finished products shipped out, the object being to provide an opportunity for profit both to its suppliers of raw materials and the Japanese economy. They may also send in management or technical personnel for discussion with Japanese firms in which investments might be made later, and supply these firms with knowledge of modern management methods and technical know-how.



SCAP has been considering proposals which would permit foreign nationals to engage, on a non-discriminatory basis with Japanese nationals, in foreign trade with Boeki Cho (the Japanese Government foreign trade agency), and in those specific business activities in Japan which positively aid in Japanese economic rehabilitation or provide a source of foreign exchange for Japan or are otherwise in furtherance of occupation objectives.

Any acquisitions of business property from Japanese nationals should be permitted only under adequate supervision and only if the Japanese Government certified that the acquisition was not made under conditions of fraud, duress or undue influence attributable in any way to the occupation. Conversion of yen return on investment into foreign currencies would, under existing circumstances, be permitted only under special SCAP license, but it is not proposed that such permission be granted for the time being.

Your Committee recommends that the Department of the Army and SCAP approve proposals of this type.

Various obstacles to foreign private investment remain which must be removed before any substantial flow of such investment can be anticipated. The absence of a peace treaty is one of the most difficult of these. Prior to the completion of a treaty - or thereupon - if the Japanese Government desires to attract large scale foreign private investment, its laws and policies should, in our judgment, provide:



- (1) Protection of foreign investments from confiscation and discriminatory taxation.
- (2) Reasonable freedom of export of dividends and profits.
- (3) A tax structure which would permit the earning and payment of reasonable profits.
- (4) Permission to foreign nationals to control enterprises proportionately to their investments.

While the United States Government is supplying with its funds the necessary food and other imports, it is obviously too early to consider granting permission to export foreign exchange.

As a practical matter, the first important inflow of foreign capital may well be for factoring purposes under which imported raw materials and inventories would be financed. Capital of this type has contributed most importantly to building up of new industries in the United States and elsewhere. If investment funds used for factoring earn a satisfactory return, that fact would serve to acquaint investors with the potentialities of the Japanese economy and encourage the making of funds available in increasing volume and later lead to investment and equity financing.



### BUDGET AND FOREIGN EXCHANGE POLICY

The Japanese Government has failed to balance its budget since the fiscal year 1930-31. The more serious excess of expenditures over revenues began to appear in the fiscal year 1937-38 and reached a peak in the fiscal year 1945-46 when expenditures approximated six and one-half times revenues.

The unbalanced state of the Japanese budget is an integral part of the inflationary processes which dominate the economy today. The origin of the inflation goes back to wartime excesses and distortions. By the summer of 1945 prices had risen to about fifteen times prewar levels. The economic collapse of Japan immediately following the surrender powerfully stimulated this inflation. When the American forces arrived in September 1945, the economy was highly disorganized. Production was almost at a standstill, the distribution process had broken down and governmental machinery, including the tax collection organization, was disrupted. The task of restoring order in all these fields devolved upon the occupation forces, but it was some little time before the necessary measures began to have some effect. Thus, inflationary pressure continued to grow in strength and by February 1948, prices were more than seven times the September, 1945, levels.

As a consequence of this immense rise in prices and the growth of government outlay (partly for extraordinary termination of the war purposes) the budget deficit has been great. It has been met by the issuance of currency, which has in turn carried the inflation forward.



SCAP has been fully aware of the desirability and necessity of achieving a balanced budget. Five principal factors have interfered with the achievement of this objective:

- (1) The number of personnel employed in national and local government enterprises, at continuously mounting money wages, has approximately doubled since 1945. Reemployment of former employees released from the armed forces and employment of repatriates from the colonial possessions account for much of this increase.
- (2) Increasing subsidies have been paid to agriculture and industry, directly and indirectly, for the purpose of holding down prices and the cost of living and assuring the masses of poor Japanese of minimum essentials. Similarly, the services of government enterprises, such as transportation and communications, are rendered at prices which fail to provide sufficient income to meet expenses. This also is a subsidy but in different form.
- (3) Taxes have not been satisfactorily collected because of an inefficient and antagonistic tax collecting agency and failure of the authorities to force those who file income tax returns (as opposed to those wage-earners whose taxes are withheld) to report their full incomes.
- (4) The usual lag exists in obtaining increased tax revenues to meet rising costs accompanying the inflationary spiral.
- (5) Occupation costs have constituted a substantial percentage of total governmental expenditures.



The Committee recommends that:

- (1) Efforts should be continued to establish a balanced budget at the earliest possible moment.
- (2) The Japanese should be encouraged to take advantage of every opportunity rapidly to reduce governmental expenditures.
- (3) The occupation authorities should continue their efforts to reduce occupation costs.
- (4) Controlled prices should be adjusted, as expeditiously as possible, to costs of production. Many basic industries now operating with losses are being supported by subsidies and government loans. Continuation of such subsidies is justified only to the extent that they are essential during this period of scarcity to keep living costs from rising to a point which would cause further inflation.

While, normally, controls hamper recovery and should be eliminated, the Committee recognizes that the existing scarcities make their continuation necessary for those few commodities basic to the existence of the great majority of the Japanese people. This applies particularly to the allocations of scarce raw materials and the rationing of food.

Cost of services rendered by most government enterprises should be established on a basis which will permit them to cover expenses.



So long as price controls are retained, wage controls are essential.

- (5) Military teams should continue vigorously to insure that Japanese tax collecting forces maintain and augment collection of taxes. These efforts recently have shown marked success.
- (6) Greater effort by the Japanese should be made to reach the undisclosed income undoubtedly present among those groups who file their own tax returns and do not have their taxes withheld at the source. Substantial profits made in black market operations largely escape their fair share of tax burden.

The Committee recognizes that the present foreign exchange situation is unsatisfactory and that a definitive exchange rate is badly needed. Judgment as to the appropriate solution is difficult, not only because of its inherent nature, but also because of the advisability of relating American foreign exchange policy in Japan to American policy in general. It is understood that the United States Government and SCAP are at present considering the questions involved.

The Committee, therefore, limits itself to recommending generally that:

- (1) Policy should be directed toward the establishment of a definitive exchange rate as soon as monetary and economic conditions become sufficiently stable, which in the Committee's opinion is not yet the case.
- (2) Foreign trade, now carried on almost exclusively by the Japanese Government, should be returned to private channels as soon as feasible, recognizing that this cannot be fully accomplished



until an effective commercial exchange rate has been established.

- (3) The present rate of fifty yen to the dollar, known as the "military exchange rate", should be modified to reflect more nearly the relative purchasing power of the yen, and its use should be extended to buyers of yen for educational and missionary purposes, for private and personal remittances, for authorized yen expenditures of foreign enterprises doing business in Japan, and to new foreign capital which may desire to make authorized investments in Japan. It is recognized that such a modification in rate involved various important governmental financial policies and that the position of the Washington authorities, including the Treasury Department, is not known to the Committee.



### CONCLUDING COMMENTS

The Committee is confident that Japan's economic difficulties -- great as they are at present -- are manageable; that Japan can in due course find the ways and means to sustain its people by peaceful pursuits at levels equivalent to those which prevailed in the past; and that the Japanese people are capable of making an orderly transition to a more democratic kind of life and economy.

The task will be hard and the required effort and talent great; Japanese self-help is demanded to work out their own salvation. Continuation of support and guidance by the American occupying <sup>a</sup> authorities is essential; willingness of other countries in the Pacific area to permit Japan to resume trading and shipping activities is hardly less so.

Our recommendations result mainly from our interest in seeing a revival of economic activity which can contribute to the revival of the Far Eastern area and provide the Japanese people with a tolerable livelihood, workmen in Japan and elsewhere with employment, business interests with fairly earned profits -- while diminishing as rapidly as possible the burdens that have fallen upon the United States.

The program of the Department of the Army, approved by the Department of State, provides the key to increased production by making available the initial imported raw materials required to augment production quickly and to restore trade relations. It is indispensable to reviving the economy so that the burden on the American taxpayer for providing the bare essentials to prevent "disease and unrest" may be decreased at an early date and, eventually, eliminated.



We express our conviction that a recovering and hopeful Japan will be more inclined to be a good neighbor and to contribute its share to the general welfare of the world and to the maintenance of peace.

Accordingly, the Committee recommends prompt <sup>e</sup>nactment by the Congress of <sup>e</sup>pending bills carrying out this recovery program.



## BRIEF NOTES ON THE ECONOMIC SITUATION IN KOREA

It is impossible in three days to make a comprehensive and detailed appraisal of the economic situation of a nation. The Committee was dependent, during its short stay in Korea, upon facts and figures made available by General Hodge and his staff, upon sketchy glimpses of the city of Seoul and its environs, and upon individual discussions with Korean business, economic and political leaders. Our review was largely limited to an analysis of the resources, economic potentials and needs of South Korea and to an examination of the fiscal and budget situation.

The Committee was impressed by the strong desire of the Korean people for self-government. They are an intensely nationalistic people who have experienced the bitter taste of suppression. Appreciative as they are for what the United States has done for them in the American zone in Korea, they are anxious to guide their own destinies as an independent nation.

### Korea's Assets

Korea is not heavily endowed with natural resources, but has considerable agriculture, fisheries and mineral deposits. 75% of the industrial production, the bulk of the electric generating capacity, the larger portion of anthracite coal deposits (there is no bituminous), and 95% of the fertilizer production, however, are found in North Korea. With the exception of electric power transmission, the 38th parallel border between the American Zone and the Russian Zone effectively excludes these benefits from South Korea. At present South Korea is able to supply only 80% of the food required to maintain a minimum subsistence level for its enlarged population.



The deficit, as in Japan, is being supplied by the United States under its occupational responsibilities. The agricultural and food situation may be greatly improved if adequate supplies of fertilizer are made available to the farmers.

The fishing industry offers real promise both by way of food for domestic consumption and for export as well, providing Korea can increase her fishing fleet and equipment. No sizable export surplus will emerge, however, unless a considerable investment in the fish catching and processing industries is made. A large proportion of the Korean fishing fleet was taken to Japan by repatriated Japanese and, as a consequence, the Korean fishing industry has been severely handicapped since 1945.

The mineral resources of South Korea, such as tungsten, gold, zinc, copper and graphite, together with her ceramic clays, are of substantial value and should be developed as soon as possible. Here again, there is a need for sizable investment inasmuch as the underground structures have deteriorated and many of the refining processes are obsolescent.

Large investments in public improvements, productive facilities and buildings, made by the Japanese during their occupation have given this essentially agrarian economy an industrial nucleus which can be advantageously utilized if raw materials are made available, if physical plant is converted from war uses to peacetime purposes, and if an adequate corps of managers and technicians can be trained.

#### Major Economic Problems

The problems of the Korean economy are similar to those in many underdeveloped parts of the world today, but are greatly aggravated by the



unfortunate division of the country into two zones north and south of the 38th parallel. Serious problems of inflation, unbalanced budget and excessive currency circulation are being experienced in South Korea. The future government must meet these fiscal problems with vigor, but they can only finally be satisfactorily overcome when the economy of all Korea is integrated and when production has been substantially increased.

The inadequacy of fuel and power, the scarcity of raw materials and the lack of competent managers and technicians have combined to reduce South Korea's industrial production to about 30% of capacity.

No indigenous bituminous coal is produced, and South Korea is now importing from Japan 60,000 tons per month, primarily for railroads and steam electric plants. Of the anthracite coal, which must be briquetted before it can be used industrially, the larger deposits are in North Korea. This briquetting will require the continued importation of asphalt pitch.

South Korea produces less than half of her minimum electric power needs, the remainder being supplied from the northern zone.

Next to coal, the two most important raw materials which Korea must import are raw cotton and salt. South Korea alone will need the importation of 50,000,000 pounds of raw cotton annually to provide the population with the very minimum needs of cotton textiles. Korea's domestic salt production supplies less than one-third of her minimum requirements. No substantial increase in fishery output can be had unless salt imports of 200,000 metric tons are provided.



Other vital raw material needs are raw rubber, petroleum products, and wool.

The future of Korea's economy will depend upon the development of experienced managers and technicians now lacking as a result of approximately 40 years of Japanese imperialistic domination and exploitation. Koreans will need all possible assistance to overcome this deficiency. It would be most desirable to make available top flight industrial consultants and business advisors from the United States, but it is highly doubtful if the services of sufficient numbers of such men with the required qualifications can be obtained. Since the most immediate field from which assistance can be obtained is Japan, the new Korean government should seriously consider, in its own interest, and in spite of the understandable hatred remaining from the war, recruiting key technicians and technical instructors from Japan.

While able guidance is obviously essential to meet the immediate managerial problem, it is most important from the long range point of view that conditions be established which will encourage the Koreans themselves to learn to deal with all phases of their economic and industrial activities as soon as possible.

The occupation authorities have, to the extent personnel and facilities are available, undertaken training programs, but these need expansion. Korean technicians should also be given an opportunity to receive training outside the country. There are considerable numbers of qualified candidates, and steps should be taken at once to help Koreans obtain the necessary education in foreign schools.



Revival of a flourishing trade will, of course, be extremely difficult under the present unsatisfactory conditions. In addition, the Koreans must face the problem of developing an entirely new pattern of trade relationships since, under Japanese domination and exploitation, Korean trade was an adjunct of the Japanese economy. Korea must necessarily be an integral part of the Far Eastern economic system. It is dependent for many of its requirements upon Japan, and for others upon China and Manchuria. The resources and industries of Korea, in turn, can supply products valuable to other Far Eastern areas. With additional coastal shipping facilities, Korea should be able to develop her trade with Far Eastern areas on an equitable basis and with considerable saving in cost.

#### Conclusions

Many of Korea's problems would be solved, and others ameliorated, if the country were united. The United States must, however, face existing political realities in the Far East. We have publicly affirmed our intention that the Korean people should be free and independent as soon as possible. Pursuant to a General Assembly resolution, a United Nations Commission is now in Korea for the purpose of expediting Korea's independence. Although they have been refused admittance to the northern zone, the Commission has been instructed by the U.N. Interim Committee to supervise elections in South Korea. When an independent government is established as a result of these elections, the basic United Nations



General Assembly resolution contemplates the early subsequent withdrawal of occupation forces.

For a time after the withdrawal of United States forces the new independent Korean Government will require continuing American aid, advice, food and raw materials in order to maintain at least the present ration level and to achieve necessary rehabilitation and governmental effectiveness. This assistance we feel should be provided for an interim period, with steps taken to assure that it is properly utilized. The Committee believes that firm support by the United States and the United Nations to the new Korean Government will inestimably help to develop participation in future Far Eastern trade on a basis valuable to the Korean people and to their neighbors.