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reconstruction program.

(4) The "Dodge Policy" abruptly stopped activities of the Reconstruction Finance Bank and the use of deficit budget on public work without formulating concrete transitional measures to meet with changes and confusions expected to arise from such a drastic departure from the existing policy.

3. Poor operation of the "Dodge Policy"

The operation of the "Dodge Policy" on the part of the Government has been much to be criticized. Certain results of the Policy seem definitely contrary to Mr. Dodge's intention or expectation.

(1) The most important thing about direct loans to industries out of the U. S. Aid Counterpart Funds was their immediate accommodation. Yet clumsy formalities of the Government have delayed the much expected supply of industrial funds from this source, causing otherwise unnecesary confusions.

(2) Emergency measures to meet with drastic changes in the world trade market and to relieve unfavorable pressures on our export have been extremely inadequate.

4. Under the above circumstances in spite of Mr. Dodge's aim at the policy of disinflation to check inflation severe deflationary tendencies have resulted out of his policy. Economic activities have been paralysed and the reconstruction of Japanese economy, it is feared, has been halted.

(1) Tremendous increases in stock-piles of commodities under sub-standard industrial operation and considerable decreases in the amount of goods transported by rail and ship clearly show the suffocating state of business transactions.

(2) The decrease of production that has been camouflaged by increases in stock-piles has become apparent and inevitable.

(3) The accute shortage of industrial funds has resulted under the

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the above circumstances. Outstanding accounts receivable are increasing rapidly in amount and dishonored bills are also increasing in amount and number. An increasing amount of raw materials, allocated by the Government under the coupon system, is refused by the allocated due to the lack of funds. Financial difficulties have brought about dumping of goods, causing abnormal drops in commodity prices. The recent stock market conditions have been semi-panicky. All these tend to show the serious state of our economy today.

(4) Unemployment has become a serious social problem, coupled with an increasing difficulty for graduating students in getting employment.

III. On Finance

The monetary stringency in the industrial circles has been so serious that some immediate measures are urgently needed to alleviate the situation. The matter is taken up below from a general point of view as well as from the standpoint of industry in particular.

1. General observations.

The fundamental idea composed into Minister Dodge's Plan was to restrict entirely the supply of any amount of funds in addition and in excess to the normal incomes of the Government that might lead into inflationary tendencies by Government expenditures but it was not intended to cause any financial deflation. But as described in II On "Dodge Policy" deflationary tendencies have been apparent in various respects, chief causes of which may be summarized as follows:

(1) Mr. Dodge's plan to offset the deflationary effects arising out of his policies by the use of the U. S. Aid Counter-part Funds has been realized only to a very disappointing extent because of the following two reasons.

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(a) The amount of credits directly extended to industry out of the Funds has been inadquately small.

The key-point as well as generating power of our present economic activities may well be found in the supply of equipment funds to our basic industries. Such equipment or construction funds that by nature are supplied on long term credit basis cannot be expected to be supplied by ordinary commercial banks under the abnormal post-war conditions in Japan. They must, therefore be supplied by some special means. With the Reconstruction Finance Bank out of picture direct loans out of the Counter-part Funds are the only source of such funds now available to industry. Too small an amount supplied from this source has immediately caused an acute shortage of industrial funds and in turn invited a sudden decrease in the demand for production goods, causing a further shortage of industrial funds.

(b) Furthermore, procedures required for the accomodation of credits out of the Counter-part Funds have been altogether inadequate, holding up results of the much expected policy. About ¥60,000,000,000 have been made available out of the Counter-part Funds, while only ¥18,300,000,000 have been utilized, leaving an astounding sum of about ¥48,000,000,000 still out of the financial market untouched.

(2) The principals and interests collected by the Reconstruction Finance Bank and a considerable portion of the funds of the Deposit Bureau, Finance Ministry, totalling about ¥40,000,000,000 have been withdrawn from the money market and have not been made available to industrial uses. A tighter money market is a natural consequence under such circumstances. It is difficult to understand why funds of the Deposit Bureau, which originally came from industries through postal savings should not be converted into industrial funds. It is, therefore, earnestly desired to convert the Deposit Bureau funds back into industrial funds.

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(3) As a result of the above two, some ¥90,000,000,000 have been out of the money market, causing definitely deflationary tendencies. The expansion of credits by the Bank of Japan to commercial banks has been a natural consequence despite the policy of the Bank to minimize it. Credits thus accommodated by the Bank of Japan have not, of course, been sufficient to satisfy the general demand for funds and an acute shortage of industrial funds still remains to be satisfied. One of the most important financial problems today is how to relieve the pressure centered upon the Bank of Japan for accommodating funds.

(4) The shortage of monetary supplies appears to be intensified towards the year end. While the rise in the index-number of commodity prices for the past one year was 12 to 13 per cent that of production was computed at some 46 per cent over the previous year. The amount of monetary circulation showed an increase of only 24.7 per cent as of the month of September last over the period of one year. From this fact alone it may be seen easily that the monetary supplies have been inadequately small. At the same time the stockpiles of goods have enormously increased and are now estimated to be well over ¥80,000,000,000 and the rate of currency turn-over has definitely slowed down.

Under the above circumstances the present amount of money in circulation is already too small to meet with legitimate demands for it. Furthermore, even under the stringent policy on the monetary circulation, as described above, the currency circulation as of last September showed an increase of 25 per cent as compared with the same month of last year. Just at this time and under such circumstances we hear of the policy of the authorities concerned to limit the maximum amount of money in circulation at the end of this year at ¥355,000,000,000 or the same amount allowed for the end of last year. It has been a customary phenomenon of

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our economy to find the money circulation increase over the year end by some 40 percent only to shrink back to the normal figure during the months of January and Feburary. When with the increase of 25 per cent in the monetary circulation the shortage of funds is keenly felt as it is, if the maximum issuance of money over this coming year end is limited to the same amount as last year, deflationary effects of such an arbitrary policy may most likely prove fatal to our economy. The logical and realistic adjustment of the year-end monetary situation is, therefore, regarded as the most important and urgent financial problem.

(5) Another financial problem of the present day Japan is how to supply funds where most needed and when needed for the reconstruction of its economy. Our industry, especially basic industries, suffered a great loss during the war and have in many ways been placed at the mercy of the economic stabilization policy. It has not yet recuperated, so to speak, from the serious sickness of the war. As found in many countries after the war, under such circumstances some special financial measures must be employed to get the industry back on its feet. When our economy is confronted with the situation where such special measures are most effective and most needed, nothing adequate has been done to fill up the vacancy created by the abrupt abolition of the Reconstruction Finance Bank activities. It is only natural, therefore, financial supplies have been extremely short to our industry especially key and basic industries. The rectification of this situation is urgently requested.

2. Results of the stringent monetary policy in the industry.

(1) As a result of the extreme financial stringency it has been found in many instances necessary to abondon or postpone plans for the reconversion, expansion or repair of industrial facilities so vitally needed for the reconstruction of our economy.

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Thus effective demends are decreasing while stockpiles are increasing when the industry is operating far below its normal rate of operation. At the same time the monetary situation is forcing the already low rate of operation still further down and is resulting in an alarming increase in the amount of accounts receivable outstanding. The shortage of industrial funds is nothing but serious and critical.

(2) Furthermore, the situation arising from the devaluation of Pound Sterling, as fully described in I The Devaluation of Pound Sterling and the Exchange Rate of Yen, has affected our export industry to no small extent, intensifying the tendencies given above.

(3) There are many companies of fame that are behind in the payment of wages. Others are dumping their products in an effort to get cash necessary day to day. Still others are relying upon black market loans at interest rates ever 10 per cent a month or are trying to increase capital under obvious difficulties, throwing the stock market into a semi-panicky confusion. These circumstances must be called in whatever way they may be looked at "Panic Around the Corner."

(4) Measures urgently demanded by the industry to take effect immediately are:

(a) Supply of necessary funds for the reconversion, expansion and repair of industrial facilities vital to the reconstruction of our economy and to increasing effective demands.

(b) Easy accommodations of loans at a low interest rate for the disposition of accumulated stockpiles.

(c) Emergency measure on the part of the Government to gurantee part of the risk involved in such loans as above by the effective use of funds made available from the Counter-part Funds and funds withdrawn by the Reconstruction Finance Bank.

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(5) The immediate application of the above measures is regarded more important than the question of how much funds should be made available by them. It is no exaggeration to say unless some effective measures are taken to relieve the situation, it may develop into a serious financial panic. Early symptoms of the crisis seem already apparent in the recent behaviors of the stock market.

IV. On Interests Rates

1. High interest rates, a burden on industry.

As a rule, when inflation is advancing, interest rates are bound to go up but as soon as inflationary tendencies are checked, they are expected to go back to their normal standard. In this respect interest rates in Japan should go down nowwhn the post-war inflation has been finally stopped. But demands for capital have been so large in amount and urgent in nature that high interest rates of today may be regarded natural from the stand point of demand-and-supply. It is, however, quite another problem how high interest should be under the present conditions. As long as the interest payment is a burden on the industry, the prevailing rates are regarded too high. For instance, the official figures for the cost of processing a bale of 20-count cotton yarn include over ¥2,000 to be paid as interest against the total cost set at ¥7,000 for the process. This shows clearly the burden of paying interest is too much for the industry. Under such circumstances there is little doubt that interests rates should be lowered as much as possible.

2. Room for lowering interest rates.

Before the war the ratio of expenditures and interests paid by commercial banks against deposits averaged around 1 per cent while it is said to be over 5 per cent now. This advance may be attributed partly to the more complicated operation required for banking business since after the war. But the chief reason for the rise in deposit-expenditure ratio is found in the expanded banking business when activities of our economy are

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far below the pre-war level and financial transactions are being much limited. It is, therefore, necessary to rationalize banking operation, making room for lowering interest rates. A few suggestions are given below:

(1) A minimum requirement should be set for the amount of deposits and loans for bank branches and all branches not meeting with the requirement should be closed.

(2) The rationalization of banking operation such as personnel retrenchment should be accelerated.

(3) The issuance of ¥1,000 notes, simpler tax procedure on small deposits and such measures should be considered to simplify banking operation.

V. On the Shoup Recommendations

We do not hesitate a minute to accept the fundamental ideas and principles contained in the Shoup Recommendations with profound respect to the work of the Mission. But in order to carry out objectives of the Recommendations most successfully it must be pointed out that there are some serious defects in the concrete program presented to reform our tax system.

1. Actual conditons in Japan are not fully grasped.

(1) The abolition of consumption tax on silk and woolen fabrics and sugar, as recommended, seems to reflect the lack of information on the living standard and conditions in Japan which are unbelievably low as compared with those in U. S. A.

(2) Though the high rate of 55% on personal incomes would stimulate the accumulation of capital, its application on annual incomes of ¥300,000 does not appear logical when such incomes are considered not sufficient to support middle-class families.

(3) The imposition of net-worth tax on property of ¥5,000,000 or more in value seems to come from the same misconception of the value of Yen. ¥5,000,000 is only $14,000. It is difficult to understand why men with such small properties should be classed among the well-to-do and taxed on their belongings. Moreover,

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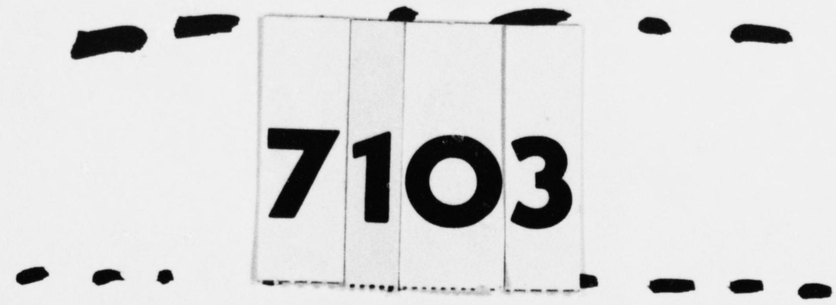

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INCOMING AIRGRAM

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DEPARTMENT OF STATE DIVISION OF COMMUNICATIONS AND RECORDS TELEGRAPH BRANCH

NORTHEAST ASIAN AFFAIRS
DEC 16 1949
1665

AIRGRAM

Action Assigned to NA
Action Taken Acknowledged

CONFIDENTIAL 12/19/49

12/19/49
NA

Action Office Symbol

FOR DEPARTMENT USE ONLY
Name of Officer
Not file
Action to DC/R

DEPARTMENT OF STATE
FROM: USPOLAD, Tokyo

Date of mailing: December 9, 1949.

Rec'd: Dec. 14, 1949 4:24 pm

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Secretary of State,

Washington.

A-347, December 8, 1949.

(This airgram supplements this Mission's A-333, December 2, 1949, and earlier airgrams in this series. Request distribution be limited to Department for reasons stated in A-21 of January 28, 1949.)

1. Great Northern Encouraged by Communist Feelers. Mr. Lars P. TILLITSE, Danish Diplomatic Representative, Tokyo, stated on Dec. 6, 1949, to officer of this Mission that he had recently received from Mr. E. C. POULSEN, representative in Shanghai of (Danish) Great Northern Telegraph Company, indications to effect that Chinese Communists at Shanghai had expressed interest in opening negotiations for restoration of Great Northern's telegraph service out of that city. Mr. Tillitse requested that this report, which he said should be accepted with reservation, be treated as confidential for time being. Dept will recall that Great Northern, (British) Cable & Wireless, and (American) Commercial Pacific Cable Company had conducted unsuccessful negotiations with Communications Ministry of Chinese Nationalist Govt for almost two years prior to Nov. 1948. Mr. Tillitse mentioned receipt of foregoing report at luncheon given by him and attended, among others, by Mr. Frank FLYNN, President of Commercial Pacific Cable Company, and by Tokyo representatives of Cable & Wireless and of Great Northern.

2. President of Commercial Pacific Optimistic. Mr. Flynn, who has been in Tokyo for about 10 days, on same occasion stated to officer of this Mission that he was optimistic over prospects for successful negotiation with Japanese Communications Ministry for restoration of his company's service from Tokyo to Guam. Details regarding these negotiations will be reported in due course.

3. Status of Trade Accounts with Nationalist China. According to data supplied upon request to this Mission by Mr. Frank R. J. GERARD, Chief, Foreign Exchange Funds Division, Economic and Scientific Section

DEPARTMENT OF STATE JAN 17 1950 DC/L LIAISON OFFICER

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INCOMING AIRGRAM

DEPARTMENT OF STATE DIVISION OF COMMUNICATIONS AND RECORDS TELEGRAPH BRANCH

NORTHEAST ASIAN AFFAIRS 1665
DEC 16 1949
DEPARTMENT OF STATE

AIRGRAM

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CONFIDENTIAL 12/19/49

12/19/49

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FROM: USPOLAD, Tokyo

Date of mailing: December 9, 1949.

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Secretary of State,

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(ESS), General Headquarters, SCAP, total trade between Japan and "Nationalist China since the Japanese surrender to date amounts to $40,407,769.91, including $21,633,420.85 for exports and $18,774,349.06 for imports. SCAP's China "A" account, covering govt-to-govt trading, shows exports to China valued at $20,561,626.47 with imports at $15,893,288.89; accordingly, the amount which Chinese Nationalist Govt owes Japan is $4,688,337.58. SCAP's China "B" account, covering private trading, shows exports to China at $1,071,794.38 and imports into Japan of $2,881,060.17, there being thus a credit in favor of Chinese merchants of $1,809,265.79. Mr. Gerard states that this credit cannot be used as offset to debt owed Japan by Chinese Nationalist Govt. Some payments, mainly in form of credits derived from sale of industrial salt from Taiwan, are being made against that debt, however.

4. No Railway Ties Available for Taiwan. Lieut. Gen. CHU Shih-ming, Chief, Chinese Mission in Japan, under date of Nov. 16, 1949, asked Chief of Staff, GHQ, SCAP, as to availability in Japan of 300,000 railway ties for use in rehabilitation of Taiwan railway system. In letter dated Nov. 26, 1949, Chief of Staff replied in part that number of railway ties currently stockpiled in Japan amounts to only a fraction of requirements of Japanese railways; that there are no surplus ties available for export; that "extremely critical" forest situation in Japan precludes felling of trees and production of sleepers for Taiwan; and that Taiwan might wish to investigate possibilities of obtaining ties from Philippines or U.S.

5. Private Import Program Begins to Take Shape. Serious work began this week on regulations for return to private imports, scheduled to take place on Jan. 1, 1950. Although details not yet available, it appears that licenses will be granted through banks, which will receive exchange allocations from Japanese Govt's Foreign Exchange Control Board; latter, it is hoped, will grant such allocations on first-come-first-served basis within general framework of quarterly import budget to be drawn up by special "Council of Ministers." Council to have Prime Minister as chairman, with Ministers of Finance, International Trade and Industry, Agriculture and Forestry, and Transportation, and Director General of Economic Stabilization Board as members. budget as drawn up will, of course, require SCAP approval. Special problem presented by materials for which importer will require allocation; allocated commodities as specified (list of such commodities has not yet been drawn up by ESS, and will no doubt involve considerable inter divisional feuding in ESS), must be covered by certificate to be issued by Ministry of International Trade and Industry (MITI); it is not contemplated that additional import license will be required, since MITI will have control over exchange budgeted for allocated items. Problem of how to prevent favoritism and discrimination in operations of both MITI and Foreign Exchange Control Board looms large. Meanwhile, first shipments under

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license-free export system have begun to move, with no evidences yet of serious shortcomings in system.

6. Details of Export Controls being Forwarded. Reference made to this Mission's despatches no. 819 of Nov. 25, 1949, "Transmittal of Final Draft of 'Foreign Exchange and Foreign Trade Control Law'," and no. 824 of Nov. 28, 1949, "Transmittal of Copy of Foreign Exchange Control Board Establishment Law." According to telegram sent by ESS to Dept of Army, 20 complete sets of all regulations, ordinances, et cetera, covering export phase of trade controls have been airmailed to Washington for distribution to interested agencies. Additional copies being transmitted by this Mission, together with despatch summarizing these enactments and giving much-needed interpretation.

7. Application of Rountree Steamship Lines. ESS Foreign Investment Board under date Nov. 21 referred to this Mission for comment application by Rountree Steamship Lines, New York, to engage in business and investment activity in Japan involving creation of Japanese corporation to procure and operate ocean shipping under Japanese or SCAJAP flag with Japanese crews. Proposal envisages creation of Japanese concern to be called International Steamship Lines, with 60 per cent of capital held by Rountree, remainder by Japanese; International Steamship would charter fleet of 500,000 tons to ply between Japan and U.S. Proposal also asks for guarantee from Japanese Govt of ability to convert yen into dollars at rate of $16,000,000 per year, to cover amortization of vessels and overseas expenditures, for period of 15 years. In its response to FIB, this Mission, as Diplomatic Section of GHQ, SCAP, under date of Nov. 29 made following observations; "(1) If Japan were unable to meet its own shipping requirements for 15 years, this proposal might merit consideration. However, Japan normally supplied not only its maritime needs but so developed this economic activity that it became important as a source of invisible foreign receipts. Currently and in the immediate future Japan faces continued and severe deficits in its balance of payments. It must, therefore, guarantee convertibility only as to such goods and services as it cannot itself supply. Shipping does not fall into this category. Accordingly, DS does not believe that the present proposal, which calls for an exchange guarantee of $16,000,000 annually for 15 years, should receive favorable consideration; (2) establishment by General Headquarters of this plan whereby an American steamship company establishes and controls a Japanese shipping company would undoubtedly have unfavorable repercussions, not only in Japan but also in the United States. In Japan, anti-American propagandists would very likely be quick to seize upon this plan as typical of so-called American imperialistic and capitalistic operations. In the United States, it appears fairly certain that American labor

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interests would make strenuous protest on the ground that an American shipping company was trying to evade United States labor standards laws. On the other hand, while most foreign shipping companies, including well-established American concerns, are probably reconciled to eventual return of Japanese merchant shipping to the high seas, it seems certain they would not like to have one of their number operating an controlling a Japanese subsidiary concern, and taking over all the competitive advantage which a Japanese shipping company might be expected to have; (3) for the reasons stated above, DS recommends that the application of the Rountree Steamship Lines be rejected." Press report on this subject published Dec. 7 by Nippon Times concluded with following paragraph: "Transportation Ministry circles, however, believe that the plan will not be realized in view of the progress being made in the fifth Shipbuilding Program and the remodelling of wartime vessels."

8. Possible Trade Arrangement between Denmark and Japan. An outcome of recent unofficial Denmark-Japan trade encouragement conferences and public statements on "projected barter plan" by Mr. Tage NIELSEN, director of Danish Merchants and Industries Trading Association and presently in Japan, has been a series of exploratory conferences between Danish Diplomatic Mission and ESS officials on formulation of Denmark-Japan trade arrangement. Danish Mission representative, informed by ESS that barter plan of type publicized by Mr. Nielsen cannot be considered, has stated informally to officer of USPOLAD that he now awaits instructions from Copenhagen to proceed with trade arrangement discussions. ESS officials interested in development of trade with Denmark which country reportedly seeking imports of Japanese textiles, machinery parts, optical instruments and porcelain.

9. ESS Still Considering Acquisition of Kailan Coking Coal. According to statements made Dec. 6 to officer of this Mission by Mr. W. S. VAUGHAN, ESS industrial adviser, ESS has not definitely rejected offer made two months ago by Mr. Wilfred PRYOR, general manager of Kailan Mining Administration, Tientsin, for supply of moderate amount of Kailan coking coal to Japan, sale to be made in sterling (see item 1, A-267, Oct. 14, 1949). Mr. Vaughan said that ESS was sympathetic and might still authorize purchase by Japan of 100,000 tons. He added that question of future use by Japan of Kailan coal was dependent upon price as opposed to local coal; he indicated also that "coalite" process in use by Wanishi Works of Japan Iron and Steel Company might not prove financially advantageous were Japan in position to acquire large amounts of Kailan coal at reasonable price.

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10. Exchange Rate for Ryukyus. SCAP mission to Okinawa to examine exchange rate problem, wage levels, domestic and import pricing procedures has returned to Tokyo and is now preparing recommendations for Commanding General, Ryukyus Command. There now exist such wide-spread distortions between wages, prices of imports and domestically-produced goods that any single exchange rate appears impractical. Moreover, sharply expanded U.S. construction program utilizing imports from Japan, US and other foreign areas, as well as indigenous labor and materials, will aggravate already serious economic problems unless positive action is taken to stabilize wage and price levels and establish an effective rate of exchange. Present rate of Yen 50 equal to $1.00 in no degree reflects relative currency values and preliminary view of SCAP mission is that rate of perhaps 120 yen to dollar would be appropriate. This rate applied to GARIOA imports, however, would require yen payments regarded as beyond capacity of Ryukyus to pay. Mission is therefore considering either a multiple rate system or one rate with provision for subsidy payments. There is general agreement that current military rate of conversion is obsolete and burdensome, and should be abandoned. Mission members consider it essential to achieve stability as rapidly as possible so that contractors may bid on a competitive basis with some degree of certainty as to their costs.

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FORM DS-323
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OUTGOING AIRGRAM

Department of State

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USPOLAD,

TOKYO.

A-239, Dec. 20, 1949

With reference to paragraph 10 of your A-347 of December 8, 1949, the Department would like to see a copy of the recommendations of the SCAP mission to Okinawa if it is possible for you to obtain one.

ACHESON

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DEC 20 1949

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INCOMING AIRGRAM

DEPARTMENT OF STATE DIVISION OF COMMUNICATIONS AND RECORDS TELEGRAPH BRANCH

POLICY

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FROM: USPOLAD, Tokyo.

CONFIDENTIAL

Acquired Dec. 28 1949

Date of mailing: December 16, 1949.

Rec'd: Dec. 22, 1949 8:03 a.m.

Secretary of State,
Washington.

Direction of Officer XMP
Direction to DC/R file

DEPARTMENT OF STATE JAN 1 1950 DC/L LIAISON OFFICE

XR 840.60

A-365, December 14, 1949.

Reference Department's airgram no. A-209, November 17, 1949, and paragraph 4, this Mission's airgram no. A-333 of December 2. Latter informed Department that Economic and Scientific Section (ESS), GHQ, SCAP, definitely assured Mission that no evidence exists pointing to cartel or other agreement between Japanese and European producers on division of markets for non-ferrous metals.

EOS has attempted unsuccessfully to secure for Mission tangible proof that Japanese producers have made offers on European market. Unable to secure documentary evidence, ESS still maintains that Europeans and Japanese are definitely competitive in non-ferrous metals and that lack of Japanese sales in Europe stems only from rejection of offers due to low quality uncompensated by lower prices. ESS feels that apparent limitation to Asiatic markets is not due to any division of markets agreement but rather to acceptance of Japanese non-ferrous export items by buyers not insistent on high quality, unlike European consumers, and interested primarily in Japanese quotations at about 20 per cent under world prices.

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FILED DEC 30 1949

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RWAdams:keb

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INCOMING AIRGRAM

DEPARTMENT OF STATE DIVISION OF COMMUNICATIONS AND RECORDS TELEGRAPH BRANCH

DIVISION OF WESTERN AFFAIRS
NORTHEAST ASIAN AFFAIRS
DEPUTY DIRECTOR
Department of State

Assigned to NA

Action Taken none required

Date of Action 12-22-49

Action Office Symbol NA

Name of Officer EWD

Direction to DC/R file

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AIRGRAM 2516 DEC 21 1949

DEPARTMENT OF STATE

FROM: USPOLAD, Tokyo.

Date of mailing: December 17, 1949.

Rec'd: Dec. 22, 1949 8:03 a.m.

FOR DEPARTMENT USE ONLY

Secretary of State,

Washington.

A-375, December 17, 1949.

(This airgram supplements this Mission's A-347, December 8, 1949, and earlier airgrams in this series. Request distribution be limited to Department for reasons stated in A-21 of January 28, 1949.)

1. Payment of Bonus to Government Employees. Finance Minister Hayato IKEDA, in an informal and confidential conversation with an officer of this Mission on Dec. 15, stated that he was standing firmly but alone in opposition to wage concessions which would require a "reworking" of the national budget. It may be noted that two groups, namely, the railway workers and Govt employees, have received official encouragement in their efforts to obtain increased compensation. Recommendation of Public Enterprise Arbitration board for substantial wage increases for railway workers has been passed on to Diet by the Cabinet. Latter also in almost complete agreement, according Ikeda, that wage increase for Govt employees is advisable. Ikeda feels that he is in strong position to fight any general wage increase in view of public statements made by Financial Adviser Joseph M. DODGE. However, Ikeda stated that SCAP had assured Prime Minister YOSHIDA that there would be no opposition to wage adjustments within the confines of a balanced budget. With this leeway, Ikeda feels that it will be impossible to resist the granting of certain wage bonuses, notably a year-end payment of Yen 1,000 to Govt employees.

2. Status of Application of Rountree Steamship Lines. Reference made to item (7), A-347, Dec. 8, concerning application of Rountree Steamship Lines, New York City, to engage in business and investment activity in Japan involving creation of Japanese corporation to procure and operate ocean shipping under Japanese or SCAJAP flag with Japanese crews. Under date of Dec. 6, General Headquarters sent letter [illegible] portions

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DEPARTMENT OF STATE FEB 23 1950 DC/L LIAISON OFFICE

DECLASSIFIED E.O. 11652, Sec. 3(E) and 5(D) or (E) NND 760125 By lyn NARS, Date 6/30/77

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of which given herewith: "Inasmuch as the proposed investment may reasonably be expected to extend beyond the tenure of the Supreme Commander for the Allied Powers, no assurances can be given by this Headquarters beyond such tenure. Validation will be accorded to the proposed investment provided: (2) formal application is filed with and validated by the Japanese Govt; (b) the investment complies with foreign investment regulations presently contained in Circular 2, GHQ, SCAP, 14 Jan. 1949, and minimum standards issued in conformance therewith; (c) the investment and business activity complies with and is conducted pursuant to the regulations of the Supreme Commander for the Allied Powers and Japanese laws, including, but not limited to, Anti-Monopoly, Corporation, and Fair Trade Laws; (d) requisite authority is obtained from the United States Govt to engage in the business activity within Japan; and (e) remittances of foreign exchange are obtained in conformance with the foreign exchange control regulations of the Japanese Govt. Subject to and dependent upon future events, no objection is perceived to the employment of Japanese personnel for service beyond the territorial limits of Japan provided prior permission for the entry of Japanese nationals is secured from the countries where such vessels will visit. The employer will be required to establish and maintain adequate safeguards for the welfare of the Japanese employees. You will be permitted to engage in the business activity on a non-discriminatory basis with Japanese shipping enterprises. Use of the Japanese flag is not permitted on the high seas at this time and probably will not be authorized until after the peace treaty. In the interim you may apply to use the SCAJAP flag pursuant to regulations prescribed by Headquarters, Supreme Commander for the Allied Powers." Most significant feature of foregoing letter appears to be condition for validation stating that remittances of foreign exchange be obtained in conformance with foreign exchange control regulations of Japanese Govt; this serves to reject proposal made by Rountree Steamship Lines for guarantee from Japanese Govt of ability to convert yen into dollars at rate of $16,000,000 per year.

3. Chase Bank Asked to Send Expert to Ryukyus. Re item (10), A-347, Dec. 8, on exchange rate for Ryukyus. As result recent discussions here between Under Secretary of Army VOORHEES and Mr. William DRAPER, former Under Secretary of Army, latter sent personal telegram to chairman of Chase National Bank, asking whether that Bank's Mr. McKITTRICK might be made available for detail of not over 60 days to work on fiscal and currency problem in Ryukyus. It was added that Mr. Voorhees would be prepared to discuss this matter personally with chairman of Chase Bank following his return to Washington on about Dec. 13.

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4. Efforts to Reduce Import-Export Stockpiles. Economic and Scientific Section (ESS) now working actively with Ministry of International Trade and Industry (MITI) on plans to release for sale on domestic market accumulated Govt-purchased import items, especially industrial raw materials, long held in stockpiles (see this Mission's A-232, Oct. 27, item 3). ESS believes that import stockpile can be disposed of successfully to local consumers if items are sold at prices no higher than future CIF quotations under projected free import plan scheduled to go into effect Jan. 1, 1950. Since many import items originally purchased at higher prices, however, Govt inventory losses will result. Stockpiles of certain export items, also source of concern to ESS, have now been released from inventories for local sale, and increased individual ration is planned by Japanese Govt, especially for textiles, to permit absorption of stockpiled exports by Japanese consumers.

5. Army Post Exchange Goods to be Released on Local Market. ESS has released press statement indicating that negotiations are now in progress with MITI for release of "slow-moving" goods presently on inventory of Army Post Exchange for use in "incentive goods program" of Japanese Govt. Said to be valued at ¥3,000,000, PX goods to be diverted to Japanese market include such items as large-sized shoes, 100,000 money belts, outdated photographic paper, cookies and perfume. MITI officials admitted discussions were under way but that careful inspection of goods was desired by Japanese authorities. In opinion of this Mission, seems questionable whether Japanese will agree to take over many of these PX supplies since their economic rehabilitation value appears doubtful.

6. Spain-Japan Trade Discussions. Preliminary discussions have recently been held between ESS officials and Spanish Diplomatic Representative on possible one-year trade agreement between Spain and Japan, with indications that Spanish Govt, which took initiative in opening discussions, would favor open or "swing" account arrangement. ESS informed Spanish Diplomatic Representative, who now awaits further instructions from Madrid, that greatest interest here lies in imports of potash, salt, cork, and olive oil, and has requested indication from Spain as to availability of these products and interest in specific Japanese export items. Prewar trade pattern between Japan and Spain was of about $1,000,000 annually on each side, compared with 1948 importation of about $2,500,000 of potash from Spain under U.S. aid program.

7. Japan-Netherlands Agreement Still Pending. Present draft of Netherlands-Japan Trade Agreement contains statement that trade will be conducted in accordance with GATT principles (REDEPTEL 620 of Dec. 1). ESS officials believe Dutch may be reluctant to accept provision for blanket clearance and non-discriminatory treatment of Japanese merchant

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vessels. Conferences between ESS and Netherland representatives have been suspended pending receipt of further communications presently expected from The Hague and Batavia. ESS somewhat pessimistic regarding early resumption of conferences, believing that present political problems militate against speedy coordination between The Hague and Indonesia on trade matters.

8. Other Foreign Trade Notes. (a) Conferences between Swedish Diplomatic Representative and ESS Foreign Trade and Commerce officials on Sweden-Japan Trade Plan for 1950 will be resumed late Dec. or early Jan., present 12-month Trade Understanding of Nov. 2, 1948, being extended at Sweden's request until 1950 Plan formalized. While ESS officials state that present "back-to-back letter of credit" system between Sweden and Japan has operated much better than first expected, they now believe that 1950 Plan may be based on less cumbersome system, probably modified open account with low level "swing" ceiling. (b) Not yet officially released by ESS is outcome of negotiations in Bangkok between Thai Govt and SCAP Mission headed by Mr. Frank E. PICKELLE, Chief, ESS Foreign Trade and Commerce Division, on Thai-Japan Trade Agreement (see item 9, A-323, Nov. 26). Local press, however, has publicized "finalization" in Bangkok of Trade Agreement involving total exchange of $90,000,000 worth of goods, balanced at $45,000,000 each way, principally 150,000 tons of rice, as well as mineral ores, rubber and lacquer for Japan; latter will export principally manufactured goods to Japan. (c) Notwithstanding recent announcement by P.I. Govt that annual imports would be reduced by $200,000,000, with luxury and non-essential goods, including textiles, to be cut to minimum, ESS has been approached by Philippine business man presently in Japan who asserts he is authorized to explore possibilities for Japan-PI trade arrangement. Individual is Mr. Jesus CABARRUS, reportedly president of Samar Mining Co., Marinduque Iron Mines, and Philippine Chamber of Mines, who has informed ESS trade officials that he was instructed by P.I. Finance Minister to discuss trade plans with SCAP. ESS, interested in formalizing trade agreement with P.I., has requested Amembassy, Manila, to supply info on Cabarrus prior to opening discussions with him. (d) ESS has extended invitation to Israel Trade and Communications Mission, presently in Manila, for trade conference in Tokyo. ESS feels, however, that in order to avoid arousing Arab susceptibilities, Israel-Japan trade agreement should not be formalized until April or May, 1950, when SCAP trade mission expected to tour Near East.

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STANDARD FORM NO. 64

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Office Memorandum • UNITED STATES GOVERNMENT

STATUS OF FAR EASTERN AFFAIRS DEC 21 1949 RECEIVED Department of State

TO : FE - Mr. Butterworth DATE: December 21, 1949

FROM : NA - Mr. Allison

SUBJECT: Japanese Economic Review and NA Economic Summary for November, 1949.

DCR file

"Monthly Econ. Summary"

As stated in my memo to you of December 21, NA has been preparing a monthly economic review as well as a monthly political review. There are attached hereto two documents: (1) a summary of the work on Japanese economic matters carried out during the month of November; and (2) a review of the Japanese economic situation as of November 30. Both of these papers have a one-page summary attached so that, unless you particularly wish, it will not be necessary for you to read the whole document in either case.

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NA ECONOMIC SUMMARY FOR NOVEMBER, 1949

JAPAN

Brief Summary

GARIOA FY 1951 appropriation. NAC working group inclined to reduce $300 million Army request by $150 - 200 million. Army requested consideration by NAC Staff Committee be postponed until Mr. Voorhees' return from Japan on December 12.

Abolition of floor prices. Department has answered complaints from British and Dutch Embassies and U.S. businessmen, pointing out that abolition of floor prices does not imply dumping by Japanese.

Fair Trade Practices. Letter sent to Army, for attention of SCAP, pointing out desirability of impressing Japanese Government with undesirability of export control associations. General statement on restrictive practices included in State Department press statement.

Japanese trade agreements. Efforts made to be sure MFN provision and provision for acceptance Japanese shipping be included in Thai and Netherlands agreements.

Technical Assistance. Letter to Army pointed out desirability of liberalizing SCAP's policy on travel of technicians abroad.

Restitution and property matters. Problems of looted gold and restituted property paid for by earmarked gold worked out with SCAP, removing all obstacles to delivery to Thailand and France. Application of gold restitutable to China to Chinese trade deficit under consideration in FE. Recommendation made to SCAP on program for restitution of diamonds. Conference held with British and Dutch to settle compensation for restitutable commodities exported to U.S. Liquidation of German assets in Japan under agreed principles to commence soon. Korean claims for ships in Japan pursuant Korean vesting decree still unresolved. Possibility rehabilitation of Italian S.S. Conte Verde raised informally with POLAD.

Petroleum Imports for Sterling. Reply made to Senator Downey pointing out necessity to maximize SCAP's imports for sterling.

IBRD Mission to Far East. Possibility use IBRD loans to countries in Southeast Asia for purchases in Japan discussed with Bank's mission to Far East, and visit to Japan suggested.

U.S. Commercial Conference Tokyo. A conference of U.S. Far East economic reporting officers is being planned for April in Tokyo.

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December 13, 1949

DEPARTMENT OF STATE

Office of Northeast Asian Affairs

Economic Summary for November, 1949

JAPAN

1. Peace Treaty: (See political summary).

Revisions have been made in collaboration with the Legal Division of many of the Economic Sections of the draft treaty, in particular Article 39, Annex VII and Article 41, Annex VIII.

2. GARIOA Appropriation for Fiscal Year 1951.

At the request of the Department of the Army, the Department of State requested the National Advisory Council to review the Department of the Army's appropriation request for Japan for the fiscal year ending June 30, 1951. Analysis by an NAC working group on which the Department was represented indicated that the requested appropriation might be excessive by as much as $150 million to $200 million if consumption levels established in the Army Department's basic program of January 1949 (the so-called Blue Book) were to be strictly adhered to. Questionable items included (a) the so-called investment guarantee fund for which $25 million is provided in addition to the $25 million already set aside during the current fiscal year; (b) the food grain reserve established in the current fiscal year at a cost of approximately $65 million; (c) the projected increase in cotton textile consumption to 4.21 pounds per capita as compared with the current level of 3.5 pounds; (d) the increase in raw cotton inventories to what appears to be a 5-months' supply in terms of mill requirements from the current 3-months' supply.

After the release of the NAC working group paper the Department of the Army solicited the State Department's unqualified support in the NAC of the $300 million figure. The Army Department representative was informed that the Department was predisposed to give every possible support to the Army Department's appropriation request, but that the responsibility for furnishing detailed justification rested on the Army Department. Before the matter came to the NAC Staff Committee, Mr. Voorhees requested Mr. Snyder to postpone consideration until the former's return from Japan on December 12.

3. Abolition of Floor Prices:

Officers of the British and Dutch Embassies called at the Department to express the perturbation of their Governments at the abolition of

floor

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floor prices; reports of inquiries made in the House of Commons (U.K.) were also received, and a number of businessmen called at the Department or wrote letters in this regard. The general tenor of these expressions was that Japan was guilty of dumping, and without some type of controls the Japanese would revert to former practices. "Social" dumping also was charged, and "cheap" labor in the textile industry was almost always noted in this connection.

In reply to these comments, it was pointed out that (1) labor cost is not the only cost of production, and even low wage rates do not ensure low labor costs; (2) the establishment of a free labor movement has tended to remove exploitative labor elements; (3) businessmen tend to fear competition unduly, and when most allegations of unduly low prices made by our own businessmen have been investigated they have almost invariably been found to be unwarranted; (4) there will continue to be surveillance of prices in Japan in the form of a "post audit" based on the general principle that export prices should not be less than comparable prices for like products offered in Japan, and that for items produced solely for export not less than cost to the manufacturer plus an addition for handling charges and a reasonable profit; (5) the best method of assuring fair pricing is to preserve compeitition in export markets; (6) the Supreme Commander is, of course, desirous of maximizing receipts of foreign exchange and has no desire to see unduly low export prices, and (7) there will undoubtedly be some industries which can compete abroad on a sound economic basis, and since Japan cannot become a politically and economically stable and self-supporting country without a restoration of this type of trade, it is in the interest of all countries that it be promoted.

4. Fair Trade Practices:

The status of the program for democratization of industry in Japan was discussed at length by various officers of the Department with Dr. Welsh, Chief of the Fair Trade Practices Division, ESS, GHQ, SCAP.

By reason of repeated reports from Japan that the Japanese were determined to revive export control associations, a letter was sent to the Department of the Army, to be brought to the attention of SCAP, urging that the Japanese Government be impressed with the strength of this Government's opposition to restrictive trade practices and stressing the detrimental effects which restrictive practices can have on the receptiveness of other countries to Japanese trade and traders.

The following paragraph was included in a statement given to the press by the Department primarily on the subject of European cartels:

> "In Japan, where economic recovery is also of major importance, it is clearly our policy to eliminate, and prevent the reestablishment of restrictive practices and the monopolistic combines with

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which you are familiar. Competition, spur to efficiency, is the catalyst of economic recovery there as in Europe."

A reply to Soviet inquiries in the Far Eastern Commission on the deconcentration program was submitted on the basis of a cable from SCAP and details supplied by Dr. Welsh, without awaiting a detailed letter being prepared by SCAP. The reason for not waiting for the letter was that the Soviet inquiries were already almost two months old, and it was believed that if a reply was not made quickly it would not be possible to state that no shares transferred to the Holding Company Liquidation Commission had been purchased by foreigners.

5. Japanese Trade Agreements:

Messages were sent to Tokyo and Bangkok urging that the trade agreements being negotiated with Thailand and with the Netherlands include provisions for reciprocal MFN treatment and for the acceptance of Japanese ships in the ports of the countries concerned, similar to the provisions of the Korean Trade Agreement.

6. Technical Assistance:

A letter was sent to the Department of the Army commenting upon the SCAP directive governing the travel of Japanese technicians abroad, and suggesting that provisions governing such travel be liberalized further. In particular, it was suggested that restrictions on travel on the ground that it may contribute to the development of competing industries abroad are inconsistent with U.S. foreign economic policy; that limitations in contracts of employment providing that technicians may work only on equipment made in their country should not be prescribed; that the requirement for payment in acceptable currencies should be liberally construed; that prescription of detailed conditions of labor may be unnecessary; and that the approval of the country of destination be obtained through normal visa procedures.

7. Thai and French Earmarked Gold:

The Department concurred in SCAP's proposal to release the gold earmarked for Thailand and France pursuant to the U.S. directive with minor deductions for gold determined to have been looted. With respect to the provision for the deduction of the value of any property restituted to France which had been paid for by the earmarking of gold, the Department concurred in the application by SCAP of a presumption that the commodity restituted was brought in after the earmarking provided there is some factual basis for such presumption.

8. Gold Restitutable to China:

The Department has under study SCAP's proposal that gold restitutable to China be applied to the default in the Chinese trade account or retained as security for payment of the trade balance. Although sympathetic to SCAP's objective, the Department is inclined to the view that the

legality

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legality of a unilateral application of the gold to the trade account is too doubtful, and that retention of the gold would lead to an indefinite stalemate.

9. Restitution of Diamonds:

SCAP's proposals for the restitution of diamonds of doubtful ownership were generally approved, with the following qualifications - that the matter be fully discussed with the Netherlands Mission before submission to the Restitution Advisory Committee; that the several alternative methods of distribution on a percentage basis be submitted to the RAC without a commitment by SCAP to the support of any particular one; and that SCAP treat the diamonds as unidentified loot if a unanimous (or nearly unanimous including the U.K., the Netherlands and France) recommendation by the RAC is not made. The Department considered that strictly speaking the diamonds are unidentified loot, and that the question of distribution is therefore beyond SCAP's competence under the FEC directive. It was appreciated, however, that there may be advantages to treating them as identified loot, if RAC agreement can be obtained, both from the point of view of GHQ, SCAP, which desires an expeditious decision, and from the point of view of the principal claimants, who may have more difficulty getting an equitable decision under the procedures established for the distribution of the proceeds of unidentified loot. The Committee of the seven interested FEC delegations which is now considering the latter question in Washington is bogged down by the insistence of a number of delegations, particularly the Chinese, on principles for distribution which appear to involve political considerations and considerations of prestige.

10. Compensation for Looted Property:

Intensive study has been given in collaboration with the Department of the Army and the RFC to the problem of compensation to the British, Dutch and French for looted tin, rubber, and lead, which was exported by SCAP to the U.S. Conference has been held with the British and Dutch in an endeavor to gain their acceptance of proposals, including the reduction of commissions and certain other adjustments, which have been approved by SCAP, and a detailed written statement is being prepared for them.

11. German Assets in Japan:

The British and French have replied officially to the U.S. request that they approve proposed principles for the liquidation of German assets in Japan. The French concurred; the British made a number of suggestions for amendments. An informal agreement was made with the British that SCAP would be requested to proceed to put the principles into effect and be informed of the proposed amendments while they are considering further. SCAP's reply to this suggestion is presently awaited. In the meantime, a draft of the proposed amendments has been prepared and will be sent to SCAP for comment soon.

12. Korean

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12. Korean Claims for Ships under Korean Vesting Decree:

No formal reply has been received by the Department to its proposal to the Korean Embassy, which was approved by SCAP, that the controversy on this subject be settled by the application of a presumption that ships of Korean registry were in Korean waters on August 9, 1945, and that without prejudice to the eventual rights of the parties no action be taken by SCAP on further Korean claims. The Korean Ambassador has indicated informally that the proposal is unacceptable and that Korea stands on its claim for all ships, whether of Korean or Japanese registry that were in Korean waters on August 9, 1945. He has protested a statement reported to have been made by GHQ, SCAP that this principle is no longer in effect.

13. FEC Decisions on Reparations and Level of Industry:

It has been decided that no formal proposals will be made in the FEC to bring its previous decisions into line with the U.S. statement of May 12, 1949. Any limitations on Japanese industries such as shipbuilding and aircraft manufacture considered necessary on security grounds will be taken up with the interested governments in connection with the treaty of peace.

14. Imports of Petroleum into Japan.

A reply was made to a letter from Senator Downey based on a complaint from the American Petroleum Export Company. The Department's reply explained the need of maximum purchases by Japan for sterling.

A Standard Oil official inquired whether the Japan-Sterling Area trade arrangement would result, as reported from London, in eliminating American companies from supplying oil to Japan for sterling. The Department does not yet have clear information on this point.

15. IBRD Mission to the Far East.

Representatives of the Department have discussed with officers of the IBRD comprising the Bank's mission to the Far East, the Department's interest in the possible use of IBRD loan funds (along with other sources of outside financial assistance) to stimulate expanded production of raw materials and foodstuffs needed by Japan. The Department also suggested that some of the members of the mission might usefully visit Tokyo for the purpose of discussing with SCAP officials the availabilities in Japan (a) of equipment needed in connection with any of the projects which the bank might be interested in financing and (b) of other manufactured goods for purchase by the borrowing countries in exchange for their expanded output of foodstuffs and raw materials. In this connection the Bank indicated that expenditure of loan proceeds in Japan in dollars would probably present no difficulties and inquired about the possible extension by Japan of short-term and intermediate-term export credits in conjunction with possible IBRD loans.

16. Repair

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16. Repair of S.S. Conte Verde.

The Italian Embassy has continued to press the Italian case for repair of the S.S. Conte Verde to put into condition to move under its own power, instead of condition for overseas tow, at the expense of the Japanese Government. The Department has informally asked USPOLAD whether there is any use raising the question again with GHQ, SCAP.

17. Proposed Conference of US Economic Reporting Officers Stationed in the Far East.

The Department of Commerce has proposed that a six-day conference of Far East reporting officers be held in Tokyo in April. The Department is in agreement that this is desirable and State and Commerce are now preparing an agenda. It is State's belief that the conference should devote itself largely to a discussion of sound measures for the promotion of intra-regional trade.

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THE RYUKYUS

At the instance of the Department of State the Department of the Army has sent a proposed new directive for the Ryukyus to CINCFE for comment (WAR 97286, December 3, 1949). The directive is substantially as originally drafted in the Department of State and is based in large part on recommendations in the Oliver report.

The Department is discussing with the Department of the Army the recruiting of abler personnel (including the possibility of appointing a civilian as head of the civil administration), the scope of pay-as-you-go, and the establishment of a coordinated economic and fiscal plan.

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INCOMING AIRGRAM

DEPARTMENT OF STATE DIVISION OF COMMUNICATIONS AND RECORDS TELEGRAPH BRANCH

OFFICE OF FAR EASTERN AFFAIRS JAN - 3 1950

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DEPARTMENT OF STATE AIRGRAM

Action Assigned to - NA

Action Taken no action

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Date of Action 1/4/50

Action Office Symbol NA

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Name of Officer ----

Direction to DC/R -- file

Secretary of State,

Washington.

3264

FROM: USPOLAD, Tokyo

Date of mailing: December 24, 1949.

Rec'd: Dec. 28, 1949 5:01 p.m.

OFFICE OF FAR EASTERN AFFAIRS DEC 28 1949 DEPUTY DIRECTOR Department of State

894.50/12-2449

A-387, December 23, 1949.

(This airgram supplements this Mission's A-375, December 17, 1949, and earlier airgrams in this series. Request distribution be limited to Department for reasons stated in A-21 of January 28, 1949.)

DEPARTMENT OF STATE JAN 17 1950 DC/L LIAISON OFFICE

1. Payment of Year-End Bonus to Government Employees. Reference made to item (1), A-375, Dec. 17, on this subject. Fortified with a SCAP memo specifically authorizing payment of provisional year-end bonus to Japanese Govt employees, Prime Minister Shigeru YOSHIDA promptly announced that a bonus payment of Yen 5,382,000,000 to 1,783,937 national govt employees would be made. Legislative bills for necessary Diet approval were submitted to that body on Dec. 19. Above cited SCAP memo, which was dated Dec. 18, stated that investigation by GHQ, SCAP, indicated that bonus payment would not unbalance budget and was not in violation of Nine-Point Economic Stabilization Program. It is notable that Japanese Finance Division, Economic and Scientific Section (ESS), opposed bonus payment and regards Japanese Govt insistence on this issue as a breach of confidence. As recently as one month ago Govt refused to budget such a payment, stating that precedent had been established in 1948 for abandonment of this practice and that hence bonus would not be paid. Funds for payment of bonus will be garnered from wide variety of sources; for example, funds will be realized by reduction in maintenance and equipment charges and by further reductions in personnel. Interesting to note that this issue was settled on political rather than economic grounds, the real improvement in standard of living being generally admitted. Individual payments will range from 2,600 to 5,000 yen and will average 3,017 yen, an amount about 700 yen lower than that stipulated by the Public Enterprise Arbitration Board (PEAB). Dr. Itsutaro SUEHIRO, Chairman of PEAB, promptly attacked Cabinet decision as a violation of National Public Service Law in that Cabinet fixed a wage payment when it had no authority to do so. Leaders of National Railway Workers Union announced that

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bonus was unsatisfactory and that recently launched hunger strike by members of that Union would be continued.

2. Disposal of Looted Gold Sought by CPC. Office of Civil Property Custodian (CPC), General Headquarters, has raised with officer of this Mission question of disposal of unidentified looted gold and silver now held by CPC. Involved are 21,313.8 grams of gold, nine-tenths fine; 2,198,066.8 grams of silver, and bars of mixed gold and silver containing 784,429.3 grams of gold and 7,188,667.4 grams of silver. CPC official indicated CPC would like to liquidate these precious metals without further delay in manner acceptable to United States Govt as well as to other members of Far Eastern Commission but is hesitant to have issue raised in FEC for fear of prolonged wrangling and probable ultimate indecision.

3. ESS Official Suspended Because of Press Statement. Reference made to item (5), A-375, Dec. 17, regarding proposed release by Army Post Exchange of goods to Japanese market. Issuance by ESS of press statement cited considered by higher echelons of General Headquarters to have been needlessly critical of proposed PX action. As a result, Major General W.F. MARQUAT, Chief, ESS, obliged indefinitely to suspend Mr. M. H. HALFF, ESS Control Officer, who issued statement. Responsible ESS officials have indicated to officers of this Mission that they are altogether sympathetic as regards Halff's action, and that proposed PX deal cannot be considered to be in best interests of Japanese economy. They also stated that PX probably more concerned with removal of undesired items from its inventory than in making worth while contribution to Japan's economic rehabilitation.

4. SCAP Ship Chartering Office in New York. At weekly ESS staff meeting on Dec. 19, General Marquat referred to recent opening of SCAP ship chartering office in New York, with Mr. R. L. VERKROFF, representative of Civil Transportation Section, General Headquarters, in charge. Discussion brought out fact this action approved in ESS by Mr. P. M. McDERMOTT, Director for Trade and Commerce, and subsequently by Chief of Staff. General Marquat indicated that he had personally not been consulted in regard to this matter; that he failed to see why SCAP had to have an office in U.S. for this purpose, especially since foreign shipping firms have been licensed by SCAP to do business here; and that he intended to have matter reopened for further discussion in General Headquarters.

5. ECA Plans to Open Procurement Office in Tokyo. At same meeting, General Marquat stated that Dr. Arthur BUNCE, Chief, ECA Korean Mission, had recently discussed with him question of opening procurement office in Tokyo. General Marquat stated that ESS was willing to give ECA officials office space in ESS Foreign Trade and Commerce Division in order to expedite sale of Japanese products for ECA account.

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6. Export Bazaar to be Opened in Okinawa. ESS now planning to send several representatives to Okinawa to open export bazaar there. Mr. Halff (see item 3) originally slated to make trip, accompanied by Mrs. Dorothy EDGERS, formerly in ESS Textile Division and now in Foreign Trade and Commerce Division. Not known at present who will be picked to replace Halff.

7. Anglo-American Textile Mission to Japan. Reference made Deptel no. 652, Dec. 14, regarding projected visit to Japan of Joint Anglo-American Mission sponsored by British Textile Institute and American Cotton Manufacturers Institute. Dept. of Army, by telegram to GHQ dated Dec. 17, stated that Deptel had been sent to Tokyo "through misunderstanding" and that it had not been properly cleared in Dept of Army. Opposition to plan of having Mission visit Japan was voiced by Dept of Army, although views of General Headquarters were requested. At ESS staff meeting on Dec. 19, General Marquat stated that he saw no reason why Mission should not come to Japan and that he intended to make response accordingly to Dept of Army.

8. Private Import Regulations Nearing Completion. ESS officials state that studies and draft regulations for private import system will be completed by Dec. 22. Although list of commodities requiring allocation (see item 5, A-347, Dec. 8) not yet completed, ESS believes final regulations and memoranda to private importers may be ready for distribution by Dec. 26. Target date for private import system remains Jan. 1, 1950, with general framework as reported in A-347. ESS Foreign Trade and Commerce Division officials pressing for finalization of all pending SCAP-processed import contracts by Ministry of International Trade and Industry (MITI) before Dec. 21, since ESS does not wish to be subjected to criticism for over-lapping into private import program. MITI presently delaying action on contracts and negotiations, according to ESS, presumably awaiting establishment private import system next year.

9. Future of Dollar Retail Outlets Uncertain. In connection with private imports and projected quarterly import budget to be drawn up by "Council of Ministers" with SCAP approval, ESS now reviewing draft budget which includes 1950 first quarter allocation of $3,600,000 in foreign exchange for Overseas Supply Store (OSS) and Overseas Automotive Supply (OAS), SCAP-organized imported food and drygoods outlet, and automobile agency, respectively, for non-Occupation foreigners, as well as other private concessionaires selling imported goods for dollar-backed Military Payment Certificates (MPCs) and Traders' Certificates. While ESS believes 1950 first quarter exchange allocation for OSS, OAS and private dealers will be granted, plans are now under way to cut off their dollar budget after March 31, 1950. Firms concerned may then be permitted to continue operations on yen basis but with no guarantee of foreign exchange allocation. ESS officials, admitting that some presently authorized dollar-sale stores

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may be forced to close, point out that present ESS plans call for abolition of Traders' Certificates by March 31, and that use of MPCs will be greatly restricted at that time. ESS believes Post Exchanges and other Army-administered installations may also sell imported goods for yen, with MPC dollars being used for purchases of rationed items such as cigarettes. This plan admittedly difficult to institute since opposition is expected from other interested Sections of General Headquarters. ESS Foreign Trade and Commerce Division officials feel that abolition of Traders' Certificates and limitation of MPC use is one of most important single steps towards return to normalcy of Japanese economy.

10. Offer of Burmese Rice to Japan. Mr. Maung Maung TIN, Govt of Burma representative on Japanese reparations matters, has informed ESS that Burma, recently accepted as member of Far Eastern Commission, has appointed him official Burmese Trade Representative in Japan as prelude to possible establishment of full diplomatic mission here. With two Burmese business men scheduled to arrive in Tokyo shortly, Tin will discuss with ESS possibility of selling to Japan Burmese goods valued at about $15,000,000 including 100,000 tons of rice. Quotations for latter reportedly about 20 per cent above world prices, but Tin hopes that SCAP will accept offer since Burma greatly interested in purchasing equal value of Japanese light machinery and communications equipment.

11. Reparations Committee Holds Final Meeting. Reparations Technical Advisory Committee (RTAC), with only seven of 13 member nations represented, held its final meeting on Dec. 20, with Colonel E. C. MILLER, Jr., Deputy Chief, Office of Civil Property Custodian, in chair. Colonel Miller stated that work of RTAC had been completed and that Supreme Commander, no longer requiring its technical assistance, had ordered Committee's dissolution as of Dec. 31, 1949. RTAC has done little except of routine nature since June, 1949, when reparations program suspended, having limited itself recently to giving technical advice on dismantling of previously selected Japanese plants, and actual shipment of reparation items to countries of destination; latter reportedly will be completed by about Jan. 31, 1950.

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if effected as proposed, there would be too many objects for taxation, involving much technical difficulties. At least ¥10,000,000 should be the lowest level for the imposition of this tax.

(4) The Recommendations show an excellent tax system to be applied parmanently but lack necessary consideration to meet with the present emergency period. Some transitional measures must be employed before a parmanent system is established under a stabilized state of economy. Fabrics, sugar, shoes and such may well be necessities of living under a normal economic condition but when 60-70 per cent of incomes is being spent on food these items should be classed as semi-luxuries. A special consideration is necessary on personal income tax especially on small incomes.

(5) When the ability of our local governments in assessing and collecting taxes is so poor as it is, the new and complicated added-value tax should not be created.

(6) Taxes on added-value and fixed assets would be too much of a burden on our already critically weakened industry.

(7) One of the aims of the Recommendations is found in the prevention of tax evasions. The chief reason for the prevalent tax-dodging today is that taxes are too heavy. This is the cause to be eliminated before reforming the tax system.

2. Points to be re-considered.

(1) Until our economy is restored to normalcy, indirect taxes, renounced by the Recommendations, should be continued so as to lessen personal tax and its supplementary tax burdens.

(2) The enforcement of added-value and fixed asset taxes should be postponed at least a year and be carefully studied.

(3) Should not be abolished nor should shareholders' blank power of attorney be limited in order to avoid unnessary confusion and ill-effects from such actions under the present conditions.

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Encl. No. 2 to Despatch No. 859, 12/7/49, from USPOLAD, Tokyo, on subj. "Financial & Economic Recommendations made by the Japan Management Association."

Proposals concerning the Enforcement of Tax Reform Recommended by the Shoup Mission.

-- In Particular Reference to Corporation Taxes --

Keizai Doyu Kai

(The Japan Management Association)

While we do not hesitate to accept the general ideas underlying the recommendations for a tax reform made by the Shoup Mission, it is considered that the suggestions in their concrete details do contain -- presumably because of the difficulty to grasp the actual conditions in this country during the Mission's brief stay -- a few problems which should be carefully re-examined from a basic and comprehensive viewpoint. We believe that it is incumbent upon us, who are best acquainted with the current conditions of this country, to carry out such re-examination in earnest in order to absorb the cream of the great work of Dr. Shoup, and that such a step is the best way to pay respects to his recommendations.

However, for one reason or another we are not allowed enough time to make a basic re-examination of the recommendations and are confronted with the possibility of having to accept a tax reform immediately along the lines as suggested by the Mission at all events. In view of such a possibility, we submit hereunder our proposals, giving expression to our desires in particular reference to taxes imposed on corporations.

1. Reappraisal of Fixed Assets.

(1) Measure Preparatory to Enforcement of Reappraisal.

A. As a measure preparatory to enforcement of reappraisal of fixed assets, the fundamental principles should be established immediately in regard to the stabilized price structure in the post-war economy of the nation.

A proper revaluation of fixed assets depends to a large extent on how their standard earning power should be estimated in each line of business under the changed conditions after the termination of the war. However, at the moment the prices and charges are fraught with unnatural unevennesses created by government controls and other artificial measures,

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and besides so far nobody can tell in what altered relations those prices and charges would be stabilized in the future. In the circumstances, it will be extremely difficult to estimate a fair and reliable earning power of the respective fixed assets. Thus one of the main objectives of the mission in recommending the reappraisal of fixed assets, i.e. the objective to enable the enterprises throughout the country to start on a uniform footing in reference to their assets, will be seriously jeopardized. It is desired, therefore, that in directing reappraisal of the assets, a price structure consistent with the reappraisal value of the assets will be immediately set up, as an inseparable measure.

B. In enforcing revaluation of fixed assets, the depreciation cost on the basis of the reappraisal value should duly be incorporated in the relative official prices.

It is understood that one of the chief objectives of the revaluation of fixed assets is to establish a sound basis for enabling a reasonable depreciation accounting to be made in each line of business. In regard to such commodities and services as are officially priced, measures should duly be taken to include the depreciation cost in the prices on the basis of the reappraisal value of the relative assets. In other words, the tax policy and the price policy should be executed in close relationship with each other.

(2) Method of Reappraisal of Fixed Assets.

A. In making reappraisal of assets not yet in operation or in determining the degree of moral deterioration of assets, a special arrangement should be made, giving a certain proportion of allowance to their reappraisal values and enabling the final revaluation to be made within five years thereafter.

What proportion of the equipments, not yet operative, can be brought into effective operation? To what extent are the production facilities now in operation to be regarded as outmoded from the international point of view? The answere to those questions largely depends on the existing conditions of similar industries in foreign countries, and also on the

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outlook on how our national economy is to be finally linked with them. At the moment, however, not only the overseas conditions are unknown to us, but there are also numerous indefinable factors in regard to the prospective trades with the pound bloc area and Communist China, so that a stage has not as yet been reached in which the business at its own responsibility is able to work out reasonable reappraisal values of its assets. Therefore, it is desired the following provisional measures be adopted for the present.

a. Reappraisal value of fixed assets will be determined provisionally by a certain prescribed date, but a certain proportion thereof (say 30 per cent) will be allowed as an undetermined portion, which may finally be dtermined sometime within five years (the time-limit for disposition of "special capital").

b. In regard to all the assets not yet in operation and to that portion of the reappraisal value, given as allowance, of the assets in operation, the time-limit for payment of the tax on revaluation write-ups will be deferred until such time as their values are finally determined, (Namely: they will be treated in the same way as the production facilities designated for reparations.) During such interim period the relative assets will be required to be depreciated on the basis of their former book-values.

B. In the case of special assets such as wartime standard ships and the like, which have to be quickly written off, the reappraisal value should be reduced to the minimum, and a high rate of depreciation should be specially prescribed for them.

Many of the assets may possess considerable earning powers in the existing conditions and be made the objects of revaluation accordingly, but they are distined to be scrapped in the near future, on account of the expected recovery of normal world economy or otherwise. It is necessary, therefore, to fix a special high rate of depreciation for those assets, as

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the objective of depreciation accounting is unattainable by taking only their moral deterioration into consideration.

(3) Reappraisal Gains Tax and Method of Payment.

Theoretically speaking, a tax on gains should be levied only on profit surpluses; and the capital surplus such as the reappraisal gains should be exempted therefrom. This is a principle actually confirmed in the U. S. taxation system. Therefore, should it be the case that the proposed tax on revaluation gains is to be levied on the understanding that such gains are regarded as acquired profits, we are diametrically opposed to it.

It is understood, however, that the tax recommended by Dr. Shoup is simply a "reappraisal gains tax," without any inference of a "profit margins tax," and that it has been suggested as a kind of temporary property tax, as the only alternative under the existing circumstances, with a view to equalization of tax burdens, and also in order, to meet the financial requirements to make up for the expected sharp decline in the corporate tax receipts as a result of reappraisal of assets. Only in such a sense, can we recognize the necessity of introducing the reappraisal gains tax as suggested.

As at present the business in general is suffering from serious shortage of money supply, it may readily be admitted that the imposition of the tax will create heavy burdens on business, and that it will be extremely difficult to raise the necessary fund for its payment. Since the tax is considered to possess the nature of a temporary property tax, it is desired the undermentioned special measures be adopted in regard to its payment.

A. No time-limit should be prescribed for the payment of reappraisal gains tax. Instead, the payment will be made in every accounting period in the amount of the difference by which the burden of corporate tax on each operating unit is reduced, on account of the revaluation of its assets, below what it has borne in the form of corporate tax under the current regulations, until such time as the full amount is paid up.

It is understood the main financial objective of the reappraisal gains tax is to cover the expected decrease in the corporate tax

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receipts, resulting from revlauation of assets.

If so, such an objective may be mostly achieved through the abovementioned formula of payment. Besides, the formula will work in keeping with the ability of the business to pay, and accordingly will ensure satisfactory tax coolections. For instance, business units with a large earning capacity will automatically make tax payment in the full amount at one time, while others with inferior earning capacity will take longer time in making full payment.

We believe the abovementioned method is most reasonable and practical. But if for some overriding reasons it is difficult to adopt such a formula, we desire that the measures as described next be taken as the second best policy.

B. While according to the Mission's report it is prohibited for the period of five years as a general rule to issue additional stocks by way of an increase in "special capital fund," an exception will be recognized to permit the corporation concerned to raise the fund for the payment of the reappraisal gains tax, by issuing additional stocks through allotment to the stockholders, only up to the required amount.

In the above connection, if the current stock price of the corporation concerned is below a certain amount, say ¥100, issuance at a discount will be recognized according to a certain reasonable schedule.

C. In regard to such types of business as electricity, electric railway, shipping, etc., where large amounts of assets with compratively long service life are fixed and the rates of profit are generally low, measures will be taken:

a. To reduce the rate of tax from 6 per cent to say 4 per cent.

b. Or to extend the time for payment of tax from 3 years to say 6 years and to allow instalment payment accordingly, if the adoption of the measure as mentioned in a. above is

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difficult.

D. As the measure as proposed in A. above cannot reasonably be applied to small-scale business, special financial facilities will be extended to the entrepreneurs of such business to raise fund, equivalent to the amount of the reappraisal gains tax, on the security of their fixed assets.

E. In case the Minister in charge recognized the actual state of the assets is such as to render the payment of the prescribed tax on reappraisal gains impossible, he will approve special deferred and/or instalment payment, reducing the daily interest for arreage and rescinding additional levies. However, until the tax is paid, the entrepreneurs concerned will be precluded from depreciating the relative assets on the basis of the full reappraisal values.

2. Enterprise Tax on Value-Added Basis.

The value-added tax is literally without precedent throughout the world. It happens the first experiment of this new tax is now going to be made in this country still exhausted after the War's ending. Both theoretically and technically or in relation to the capacity of the taxpayers, the proposed tax poses numerous problems. To make the situation apparently more difficult, it is proposed to place such an entirely new tax in the hands of the local governments, whose tax-collecting functions are decidedly inferior and inadequate as compared with those of the national government. Therefore, no small measure of difficulties are expected in imposing the proposed tax. Frankly speaking, we are of the opinion that the imposition of the tax had better be deferred for the present, if possible, until such time as the local taxes as a whole are subjected to a thorough and careful re-examination.

• But if the value-added tax must be enforced forthwith at all, the tax should be simplified, for reasons given above, in order to facilitate its application, taking the ability of the local governments into

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all account. If this point is not only considered, we are afraid the imposition of the tax is likely to lead to frequent confusions in the business of tax collection, corruption of taxation officials taking advantage of such confusions, and to other evils of immeasurable gravity.

Besides, the tax is expected to have such far-reaching effects on the business that as a result the nation's economy itself might be crippled in the long run. The main subjects of importance, which require re-examination from our standpoint, along with our counter-proposals, are as enumerated below.

(1) In consideration of the administrative ability of the local governments, the objects of the value-added tax should be confined as far as practicable to those which can be clearly and unequivocally defined.

According to the Mission's report, the objects on which the imposition of the value-added tax is recommended are considerably multifarious. Many of them cannot easily be defined. The collection of such a tax is expected to involve a plenty of work, give rise to disputes and necessitate discretionary considerations, inevitably leading to corruptions. It is therefore proposed to simplify the tax as follows.

A. The objects of the value-added tax will be limited to profit and wage.

B. Instead of applying a uniform rate, differential rates will be established, for instance, in the ratio of 5 on profit and 3 on wage.

(2) The standard rate of the tax should be determined only after a thorough examination of the actual conditions.

It is stated in the Mission's report: " It is likely that an average rate of somewhere around 4 per cent to 6 per cent will be needed to assure the prefectures a yield of 44 billion yen." However, according to our tentative calculation, the tax is considered to yield a far greater amount than what was estimated by Dr. Shoup, even if it is

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levied at the rate of 4 per cent. Therefore, in fixing the rate, it is strongly desired that the objects of taxation be thoroughly examined and defined, in order to establish a fair and equitable standard. (In this connection, it should be pointed out that the local governments at the moment are not equipped with an adequate ability to carry out the required inquiries.)

(3) The rates as mentioned in (1) above will be made to vary with each section of industry in conformity with the actual conditions, instead of being applicable on a uniform basis.

Presumably, the idea of the value-added tax is supported by at least two conditions. The one is the anticipation that the major portion of the tax may be transferable to consumers, and the other is the necessity to modernize the production equipments of this country as soon as possible. But as a matter of fact, those two conditions have not their full validity in this country in connection with some important types of business. Therefore, it is considered advisable that the rate of taxation be made flexible under special arrangements to meet the actual conditions. For instance:

A. In the case of charges for electricity, gas, etc. and fares for electric railways and busses, it is almost impossible, in the nature of things, to shift the value-added tax to the consumers. So is the case also with international commodities. Further, the possibility of shifting the tax to consumers may vary with whether the business is conducted on a local scale or on a nation-wide scale. It would be most desirable to establish a schedule of equitable rates for respective fields of business, taking the above into full account. In our opinion, that is exactly what the Mission's report has in mind.

B. To be sure, as pointed out in the Mission's report, our industrial equipments have to be urgently modernized. But that is not the whole of the requirements of our national economy

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at the moment. Japan, with her surplus of population, has to foster also such types of industry as in their nature employ a large number of workers. Such types of business, however, are at present in a more difficult situation than are other types. If the value-added tax would be enforced exactly as suggested, it will hit them the hardest. Therefore, a set of moderate rates of taxation, with graduation according to types of business, should be formulated in regard to those lines with large payrolls.

(4) In introducing the value-added tax, transitional measures should be formulated, giving due allowance to the past capital investments. (The measures naturally become superfluous, if the simplification as proposed in (1) above is carried out.)

In the Mission's report it is suggested in reference to new investments in business that the so-called "negative value-added" should be carried forward to be offset against value-added amounts in succeeding years. Applying the same principle, some transitional measures should be taken, in introducing the new tax, also in regard to past investments, permitting the tax applicable to them to be offset in accordance with a certain schedule against value-added amounts, for instance, over a succeeding period of five to ten years.

(5) Interest payable should be exempted from the value-added tax. (This proposal becomes superfluous, if thorough examination of the actual conditions is satisfactorily carried out and fair and equitable rates are established as mentioned in (1) above.)

The merit of the proposed value-added tax is to eliminate dual taxation. But if interest payable on money borrowed by business concerns in general is taxed as shown in the Mission's report, it will constitute an evident case of dual taxation, as the relative amount is again subjected

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to the value-added tax in the banking business. In the circumstances, of the amount payable as interest by entrepreneurs, the interest on loans borrowed from financial institutions should properly be exempted from the value-added tax. Such a step is also necessary for the sound development of the nation's economy.

3. Tax on Land and Depreciable Assets.

A tax of such a high rate as suggested by the Mission imposed on all fixed assets, that are depreciable, in addition to land and house, is expected to weigh heavily on the business in general. Besides, the burden borne by the business is likely to vary to a considerable extent from one locality to another, giving rise to no small measure of difficulties. Therefore, we are basically of the opinion for the reasons as stated in connection with the value-added tax that the imposition of the expanded real estate tax had also better be postponed for the time being, and that a fundamental and comprehensive re-examination be carefully carried out in the first place.

But if the tax must be enforced forthwith, we strongly propose the adoption of the undermentioned measures.

(1) The objects of the new real estate tax should be simplified.

The undermentioned measures will be taken to simplify the taxable objects for the same purposes as already stated in reference to the value-added tax.

A. For the sake of simplification, the valuation of fixed assets for tax purposes will be based on their book-values, although some measure of unfairness may result in certain cases.

B. In case the tax is levied on a valuation reached otherwise than the method as mentioned in A. above, the value of the tools, implements and furnitures will be exempted from taxation.

(2) The rate of the tax for the first year should be made lower than the recommended rate.

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It is proposed in the Mission's report that the tax rate for the first year should be 1.75 per cent of the real estate value and that the rate may be increased to a maximum of 3 per cent thereafter. However, according to our rough calculation, even the rate of 1.75 per cent in the first fiscal year is expected to yield a revenue far in excess of the amount as estimated by Dr. Shoup, and is likely to lead to reckless spending by local governments. Moreover, the rate of 1.75 per cent in the first year already weighs on the business as heavily as does the tax on revaluation write-ups, and besides the tax, unlike the latter, has to be paid every year. If account is taken of the fact that, even in regard to payment of the reappraisal gains tax, special measures as stated before have to be asked for to relieve its effects on the business, it may be easy to assess the magnitude of the pressure the new real estate tax would bring to bear on the nation's economy.

Assuming that in so far as the tax rate for the first year is concerned the suggestion of the Mission is merely a tentative one based on certain hypothetical conditions, it is desired that in enforcing the tax the objects of taxation be thoroughly defined and a reasonable rate be established with care, so that any collection over the required amount may be forestalled.

(3) On fixed assets, other than land and house, the new real estate tax should be levied at special moderate rates, with variations with each line of business.

The new real estate tax on production facilities such as machines, railway lines, vessels, etc., affects the business far more seriously than the tax on land and house. Besides, different types of business will be affected differently. For instance: The effects may vary with electric railway business and electricity supply business; iron-manufacturing and chemical industry of high degree; and other light industry in general. The new real estate tax accordingly should be varied in its rate according to each type of business, and the equipments directly employed in production, un-

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like land and house, should be taxed at moderate rates.

In view of the intention of the Mission's report in providing special measures for farm land by exempting it from the enterprise tax, we believe our proposal as stated above may be quite justifiable.

(4) Dual taxation resulting from the imposition of the new real estate tax should be eliminated.

Among the local taxes there are railway line tax, automobile tax, electric pole tax, etc., which with the introduction of the new real estate tax will constitute dual taxation. It is desired that measures be adopted either to abolish the formar or abandon the latter, to do away with duplicity.

4. Anonymous Ownership of Securities.

It is desirable the present practice of anonymous ownership of bonds be continued and the proposed restrictions on the transfer of stocks be eased.

The Mission's report recommends for the purpose of preventing tax evasion that bearer bonds should be barred. But it is understood the report does not deny the anonymous ownership of public loan bonds, If so, those who want to evade taxes may attain their aim by means of owning the latter. Thus the objective of the proposal in denying the anonymous ownership of securities in general and imposing restrictions on the transfer of stocks is easily defeated. To say the least, the proposed restrictions are likely to bring about larger evils by eliminating smaller inequities.

However, as the unrestricted transaction in stocks under blank letters of attorney, as at present, is not without its undesirable effects, some measures may properly be taken to check the abuses, f.i. by making it compulsory to make formal transfer of stocks in each business period of the corporations concerned.

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5. Provisional Measures Attendant on the Proposed Discontinuance of Percentage-wise Undervaluation of Inventory Assets, Securities, etc.

The valuation of inventory assets, securities, etc. owned by business units at present should be made in accordance with the new method of inventory accounting.

The Mission's report recommends immediate discontinuance of the practice as permitted by the Ministry of Finance in the past to make valuation of inventory assets for tax purposes on the basis of actual purchase prices less certain percentages (5 per cent for land, if included in inventory, and securities, and 10 per cent for other assets).

For the interim period of alteration in the practice, it is desired the undermentioned measures be taken.

A. In so far as the relative valuation accounts held by respective business units at present are concerned, it should be clearly established, though more or less a matter of self-evidence, that when a business unit has elected one method or another from among the straight-line method, the first-out method, the last-in first-out method, the normal stock method, etc., the practice of setting up a separate valuation account as in the past will be discontinued, and the method of depreciation as elected will be applicable without exception, and that only when the assets as evaluated are sold or otherwise disposed of the gains realized will become taxable.

B. The valuation accounts held at present by security dealers in reference to securities, pruchased by them for re-sale, should also be treated as mentioned in A.

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INCOMING AIRGRAM

DEPARTMENT OF STATE DIVISION OF COMMUNICATIONS AND RECORDS TELEGRAPH BRANCH

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ACTION: FE
INFO:
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(FOR DEPARTMENT USE ONLY)

FROM: USPOLAD, Tokyo.

Date of mailing: December 30, 1949.

Rec'd: January 11, 1950 10:28 A.M.

Secretary of State,

Washington.

A-399, December 30, 1949.

(This airgram supplements this Mission's A-387, December 23, 1949, and earlier airgrams in this series. Request distribution be limited to Department for reasons stated in A-21 of January 28, 1949.)

Action Assigned to NA

Action Taken 20 Jan

1/12/50 NA

Ret file

Direction to DC/R

DEPARTMENT OF STATE JAN 28 1950 DC/L LIAISON OFFICE

1. Presentation of Budget to Diet Postponed. Japanese Govt national budget for fiscal 1950-51, which Yoshida Administration was to have presented to the Diet on Dec. 23, has been withheld pending decision on wage and salary schedules for Govt workers. One of basic assumptions on which budget was formulated was that there would be no increase in wage level of Govt employees. Prime Minister Shigeru YOSHIDA has made commitment to General Headquarters, SCAP, to hold the line on wages--a commitment which has been kept as guarded secret. Opposition parties, however, have seized upon "wage increases for Govt employees" as major issue and Mr. Yoshida has let it be known to GHQ, SCAP, that he is not certain of complete support from his own party in opposing any increase.

2. Status of Anglo-American Textile Mission to Japan. Reference item (7), A-387, Dec. 23, regarding proposed Anglo-American textile mission to Japan. UP report from Washington dated Dec. 29 states that "General MacARTHUR has granted permission for members of a joint British-American textile mission to visit Japan and inspect the textile industry if they come as individuals and not as an 'official or quasi-official' group." Dept may be interested to note that GHQ response to Deptel 652, Dec. 14, made personally by Major General W. F. MARQUAT, Chief, Economic and Scientific Section (ESS). For purposes of record, full text of General Marquat's telegram, sent Dec. 25 to Dept of Army, quoted herewith: "As trading individuals, exploring possibilities for trade, clearances will be granted on application to those persons concerned, if they meet the individual requirements prescribed. Such individuals will be extended the same privileges, and will be subject to the same obligations, neither more nor less, as are others in a similar status. No official recognition

PERMANENT RECORD COPY.—This copy must be returned to DC/R central files with notation of action taken.

JAN 18 1950 FILED

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will be given them as a national or international body, nor will they be permitted to assume any prerogatives in excess of those of any other traders. The group as such can have no quasi-official rating. As individuals they will be entirely welcome." Dept may note that, although General Marquat has stated in unmistakable terms private character of Anglo-American mission, he may have been prompted to follow that line as means to combat influence in Dept of Army of Mr. F. A. WILLIAMS, former Chief, ESS Textile Division, who has steadfastly been opposed to idea of having any such mission visit Japan. Mr. Williams, who apparently is still consulted by Dept of Army on Japanese textile matters, was quoted in that Dept's Dec. 17 telegram (cited in A-387) as questioning need for such mission to visit Japan.

3. Japanese Wool Glove Exports to U.S. In confidential telegram to Dept of Army dated Dec. 21, ESS gave following data on exports of Japanese knit wool gloves to U.S.: (a) shipped during period Jan. 1 to Dec. 16, 1949, total of 326,400 dozen valued at $945,973.30; (b) scheduled for shipment balance Dec., 10,700 dozen valued at $31,870 at 360-1 exchange rate; also 51,307 dozen valued at $100,952.90 against contracts validated prior to establishment 360-1 rate; (c) scheduled for shipment during Jan. 1950, approximately 8,600 dozen at $21,945 at 360-1 exchange rate. At recent ESS staff meeting, General Marquat read letter from official of American Wool Glove Manufacturers Association, who visited Japan recently, expressing appreciation for opportunity to study Japanese production and discuss future prospects for exports to U.S. Dept will recall that question of Japanese knit wool glove exports to U.S. received wide publicity last spring, matter being aired in Congressional hearing.

4. Japan-Thailand Trade Agreement. ESS Foreign Trade and Commerce Division officials and Thai Govt Trade Representative Suphot IGANINANDA have completed work on Thailand-Japan Trade Plan for 1950, which, with Trade and Financial Agreements, were submitted by ESS to Chief of Staff, GHQ, SCAP, for approval on Dec. 28. Trade Agreement calls for development of trade between two countries to largest extent practical, with initial estimates placed at $45 million each way during 1950 (see item 8b, A-375, Dec. 17). Principal imports from Thailand to be rice, soybeans and raw materials, and Japan's exports chiefly textiles, chemicals, rolling stock and other manufactured goods. Most-favored-nation treatment is accorded mutually under Agreement as regards customs tariffs. Financial Agreement calls for immediate payment on demand of creditor of any excess over net balance of $5,000,000.

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5. British and Danish Objections to Marine Transportation Law. United Kingdom Liaison Mission and Danish Diplomatic Mission have submitted protests to General Headquarters on behalf of Far Eastern Freight Conference and British and Danish shipping lines against authority over foreign shipping by Japanese Govt under provisions of Marine Transportation Law, made effective on Aug. 25, 1949. Both Missions point out that shipping conferences were not subject to specific pre-war Japanese legislation, and that restrictive clauses of present Law will not only place conferences and non-Japanese shipping enterprises under possible discriminatory Japanese authority, but may also permit resurgence of undesirable Japanese pre-war maritime practices. Missions request that General Headquarters take action to institute new legislation or amend present Law to exempt foreign shipping from all restrictive provisions of the Law. Officials of ESS Fair Trade Practices Division, now drafting replies to Missions, state that enactment of Law was due principally to British and Far Eastern Freight Conference requests for legislation which would authorize conference operations, previously banned under Anti-Monopoly Law. ESS officials concerned add that replies will be to effect that Japan has jurisdiction over shipping conferences and that latter must accept restrictive clauses of Marine Transportation Law (which, in large part, is based on U.S. Shipping Act of 1916), the enactment of which Law first legalized their operations in Japan. Despatch on this subject will be prepared upon receipt of ESS replies to Missions.

6. Open Account Audits Near Completion. ESS is nearing completion of its audits of open accounts under trade arrangements with various countries, notifying govts concerned of balances as of Oct. 31, 1949. For example, ESS informed Swedish Diplomatic Mission that Oct. 31 audit showed balance due Sweden of $21,016.62, representing excess of imports from Sweden totalling $1,199,113.79 over Japanese exports in amount of $1,178,097.17, during 1949.* Undelivered portions of Japanese export contracts with Sweden as of Oct. 31 amounted to $304,361.90, there being no outstanding import contracts. ESS has also informed French Mission that Oct. 31 audit disclosed balance in favor of French Union of $596,256.95, this sum representing difference between Japanese imports under Trade Agreement with French Union of $7,866,760.39, and exports totalling $7,270,503.44. ESS Foreign Exchange Funds Division states Oct. 31 audit is final one to be made by ESS, with future audits to be responsibility of Bank of Japan in accordance with private import-export trade system. (*first 10 months)

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7. Legislation for Private Import System. Ordinances, regulations and memoranda prepared by Japanese Govt on private import trade system to be instituted Jan. 1, 1950, are now in final draft form but will not be released until on or shortly after Jan. 5. Previously reported these enactments, et cetera, would be released prior to end of 1949; delay in issuance said due to week-long new year's holiday being observed by Japanese Govt offices.

8. Conferences on New Japan-Sweden Trade Arrangement. Conferences between Swedish Diplomatic Representative and ESS foreign trade officials scheduled to commence Jan. 10 in connection with new Trade and Financial Arrangements and Japan-Sweden Trade Plan for 1950, these to replace present agreements which expire Dec. 31 but which will remain in effect until finalization of 1950 Trade Plan (see item 8a, A-375, Dec. 17).

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Art Stuart wrote this orig.

THE FOREIGN SERVICE
OF THE
UNITED STATES OF AMERICA

Office of the U. S. Political Adviser
for Japan

Tokyo, December 30, 1949.

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No. 911

6 DIVISION OF NORTHEAST ASIAN AFFAIRS JAN 1 1950 DEPARTMENT OF STATE

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Subject: Transmission of Report of SCAP Mission to Okinawa.

The Acting Political Adviser has the honor to refer to the Department's airgram instruction no. 239, December 20, 1949, requesting a copy of the recommendations of the SCAP mission to Okinawa, mention of which was made in item (10) of this Mission's A-347 of December 8, 1949.

Enclosed is a copy of the report in question, comment upon which is given in this Mission's A-347.

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Enclosure: as

✓ Copy of memorandum entitled "Report of SCAP Mission to Okinawa."

JWPM

Parchment Mat to Department.

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RETURN TO DC/R FILES WITHIN 14 DAYS, WITH A NOTATION OF ACTION TAKEN.

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Enclosure to Despatch No. 911, December 30, 1949, from the Office of the U.S. Political Adviser for Japan, Tokyo, on the subject "Transmission of Report of SCAP Mission to Okinawa."

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(COPY)

Report of SCAP Mission to Okinawa

This report proposes:

1. An exchange rate of 120-1 to be used for all commercial trade and for internal purposes.

2. A conversion ratio of approximately 50-1 for the purpose of pricing GARIOA aid.

3. A minimum wage of ¥2,000 per month. This would result in an average wage of about ¥2,100 at present work hours. It is hoped that the scale will provide an incentive for longer work hours resulting in an average monthly wage of ¥2,400.

4. That the special supply stores be abolished and that preferential pricing of meals for workers in compounds be abandoned. Using the 50-1 conversion ratio for GARIOA imports still makes this a low figure.

5. That domestics and club workers who have meals furnished also have deducted a sum equivalent to the deductions for compound workers.

6. That workers on public works be paid a scale roughly 10 per cent under the military scale. In outlying areas, however, such work should be at the prevailing rate of the area.

7. That OCA provide wages comparable to the "military", the financing of this made possible by increased income taxes from "military" workers.

8. That the reclassification of workers now under consideration be expedited.

9. That the money supply be properly distributed as between the several geographic areas by proper budgeting and allocations of the RMG budget.

10. That a separate R.F.C. not be established, but the present banking system provide "counterpart" loans to private industry. The report discusses how such loans are to be made without tying up funds unnecessarily and without creating inflationary pressures.

11. That an adequate supply of Japanese consumer goods be provided even if it means utilizing GARIOA funds and excluding other GARIOA items.

12. That

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12. That the principle of reducing GARIOA by dollar earnings be modified.

13. That every impediment to inter-island trade and trade with Japan be eliminated.

14. That every effort be made to improve present manpower utilization, so as to keep the expansion of the labor force to a minimum.

15. That budgeting and planning, both U.S. and RMG, be coordinated.

16. That a budget mission from Tokyo be called in as soon as possible to revise the budget and place the RMG budget so as to coincide with the U.S. budget year as an aid to budget and planning coordination.

Mission

This SCAP mission to Okinawa is "for the purpose of making recommendations to the Commanding General, Ryukyus Command, on the internal exchange rate, wage levels, prices of imported foods and financial procedures to be established in the Ryukyus Islands."

Statement of the Problem

Widespread distortions as between wages, prices, the exchange rate and other factors now are evident throughout the Ryukyuan economy threatening the existing program in the Ryukyus. The expanded construction program cannot help but aggravate the already serious economic problems. The success of the construction effort is dependent upon achieving stable wage and price levels and establishing a satisfactory rate of exchange between the Ryukyuan yen, the dollar, the Japanese yen, and the Philippine peso. It is essential that stability be achieved so that contractors can bid with some degree of certainty as to their costs.

Assumptions

1. That the Ryukyuan yen must continue to be utilized.

2. That the peak labor force will approximate 55,000 Ryukyuan workers including additional new service workers for the expanding American community.

3. That the present cost of living will be maintained or reduced.

4. That the fiscal policies for the Ryukyus must be planned on the basis of the volume of dollar expenditures in the Ryukyus with due consideration of the expansion of trade.

5. That

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5. That the maximum dollar expenditures to the Ryukyus ($10.3 million) for construction will be made in U.S. Fiscal Year 1951.

6. That the U.S. will provide adequate funds for the welfare of the people and the rehabilitation of the economy.

7. That the size of the "military" construction program precludes the immediate and full reconstruction of the south half of Okinawa and that reserves in yen and dollars must be set aside against the day when the "military" construction program has ended and the reconstruction can be undertaken.

General Findings

In general it has been very difficult to obtain the data necessary for a fully adequate review of the several problems. It is necessary, therefore, to base the analysis upon estimated or incomplete data. To be sure, estimates have been checked from several sources in an effort to obtain the basis for the evaluation of the existing situation, and recommendations. The paucity of data, the uncertainty of many conditions, and the limitations of time preclude long-range recommendation with regard to the problems. It is the unanimous opinion of the group that the success or failure of the program of recommendations is contingent upon the proper timing and coordination of the several segments. The most important single element, however, is the speed with which an adequate supply of a variety of consumer goods suited to the Ryukyuan needs and tastes can be made available. The economic pressures to be anticipated from an expanded construction program are such that the present economic distortions will be further aggravated unless action is prompt, direct, and sound.

Recognition should be given to many of the RMG personnel who see their individual problems clearly, and to many who also understand the overall problems. Much of the present situation arises from faulty coordination of effort and lack of delegated authority to take action.

Exchange Rate

At the present time an internal exchange rate of ¥50 to the dollar is in effect. Yen are purchased with dollars and utilized to pay for labor and supplies furnished to the "military" establishment by the Ryukyuan economy.

Imports have been priced, in theory, at ¥50 to the dollar; in practice there has been considerable variation. Typical rates follow: medical supplies (¥10 rate), fertilizer (¥25 rate), food for compounds (¥33 rate), POL (¥40 rate), industrial equipment (¥40 rate), food through mura stores (¥95 rate), etc., etc. A small quantity of imports from commercial accounts sold on the free market average about ¥250 to the dollar, with individual commodities going as high as ¥450. The incentive goods for special trade stores range from ¥40 to ¥60 in their rates.

Exports

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Exports (exclusive of phosphate rock) average around ¥200 to the dollar with wide ranges between individual items. There exists a black market for Military Payment Certificates at about ¥140 to the dollar. M.P.C.'s circulate freely, though illegally, among the Ryukyuans.

The present exchange rate is unrealistic for the purpose of employing Ryukyuan labor. It is also unrealistic for commercial imports and exports and military conversion. For purposes of exchange with the Japanese yen 1 to 1, it is most inequitable. For all these purposes the present rate does not reflect the true value of the currency in terms of goods.

For American Aid imports to the Ryukyus the problem is not one of the value of goods landed in Okinawa at an exchange rate. These goods purchased primarily from high cost producing areas and carried to Okinawa with high cost shipping are for the welfare of the people and the rehabilitation of the economy. The maximum limitation on this exchange rate should be the quantity of yen required to operate the military government in lieu of a central Ryukyuan government and to provide a "counterpart" fund to aid the reconstruction and rehabilitation of the Ryukyuan economy through grants-in-aid and/or loans. Because imports under GARIOA have such a high per capita dollar value as related to the per capita dollar value of domestic production, they cannot be translated to yen at the exchange rate used for other purposes without provision for accumulating excessive quantities of yen. An attempt to provide the public with the required purchasing power at such an exchange rate would create drastic inflationary pressures. Further, it is essential that the cost of living be maintained or lowered to insure the success of the military construction program. (An analysis of the yen rate as applied to GARIOA imports and the budget appears later in this report.)

It is recommended that the internal exchange rate should be altered to some point within the range of ¥120 to ¥140 to the dollar with a distinct preference for the lower rate. Gross rates to the Japanese yen and Philippine peso should be in terms of dollars. Export considerations do not warrant the highest rate in the range. The lowest rate in the range is preferred so as to favor low prices on incentive goods purchased from Japan with Ryukyuan dollar earnings. Finally, the lower the rate the less the inflationary pressures therefrom.

Wage Levels

At present there are approximately 40,000 Ryukyuan workers employed by the military, its agencies, contractors, and authorized individuals. Of these from 26,000 to 27,000 are Category I workers who are paid from yen "purchased" with appropriated funds. The remaining 13,000 are Category II workers who render those services which are considered of a personal nature and are paid from funds collected from individuals or agencies utilizing these services.

Present

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Present average cash wage levels for Category I and II Okinawan workers range from ¥650 to ¥700 per month. This represents $13.00 to $14.00 per month at the 50 to 1 exchange rate. In addition to cash wages there are hidden wage payments in terms of authorized (and unauthorized) payments in kind. Goods purchased at special trade stores at preferential low prices are generally resold in the free market and give the workers an estimated average profit of ¥200 per month. Workers in compounds have deducted from their pay ¥4 per day for three meals provided from food purchased by using units at prices which are unduly low. In some instances workers and their families are provided with living quarters, provided they work 160 hours per month.

Many Category II workers in homes, clubs, etc. are furnished with food, clothing, and incidentals. Workers in some locations obtain salvage, dunnage, etc. by virtue of their employment. Finally, there is stealing of supplies from warehouses, stores, docks and other facilities.

Most significant in the low average money earnings is the high concentration of workers employed at a ¥3.0 to ¥3.5 (6 to 7 cents) per hour. A second significant factor is the low average hours per month (140 to 160) for a large proportion of Category I workers. This absenteeism is due to higher hourly wages for part time work in private industry, or on public works, and to temporarily more profitable work on farms.

It should be pointed out that wages in cash and kind (in dollars) currently approach $17.50 per month. The average monthly wage is $13.00 to $14.00. The profit from "incentive" goods is equivalent to $4.00. For compound workers the cost of compound food is $2.40 per month, and its value is somewhat higher. These dollar rates at the present time are 50 to 1 exchange rate.

Wage rates for workers in private enterprise range from three to four times those paid by the military, its agencies and contractors. Hours of work, however, in private enterprise are reported to be substantially above the hours presently worked by employees of the "military". Hourly and daily wage rates on public works are reported to be two to three times the "military" rate. For selected skills in short supply (carpenters, plasterers, etc.) the rate on public works and in private construction ranges to above four times the "military" rate.

Data on the cost of living have been most difficult to obtain. Further, ranges presented by various sources are extremely wide for so important an element of data. The range is from ¥2,000 per month to well over ¥4,000 per month for a family of five. Our best estimate is that a minimum cost of living is approximately ¥2,500 per month for a family of this size. This computation assumes roughly that 25 per cent of total calories are obtained from the free market. The Labor Section of Military Government has made an estimate of food for a family of five at official prices. This estimate of ¥1,030 per month with all purchases at official ration prices, if doubled for

non-food

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non-food items, provides a ¥2,060 figure. (Internationally accepted rate of 45% for food; Japan over 60% for food).

It is recognized that the range as between these two estimates is still wide. However, if the practices followed are similar to those in Japan, it is probable that there are from 1.3 to 1.4 workers per family which presupposes a larger income for a family than is obtained solely through the earnings of the head of the family. The second worker, however, is usually a child or wife of the head of the family working at a very low wage. It must be assumed further that many of the lowest wage groups are single persons. Furthermore, in many other instances year-round small farms supplement family income in terms of goods.

It is recommended, therefore, that a minimum wage of approximately ¥2,000 per month be established for Categoryl workers working 48 hours per week. This can be accomplished by setting a new rate of ¥10 per hour for the lowest grade Category 1 worker now classified in R-2 at a rate of ¥2.50 per hour. This approximates the estimated cost of living for a family of five (on the low side) and is in line with the common labor rate in private industry. It is assumed that with the increased scale, workers will have sufficient incentive to work at least 48 hours per week instead of the present average 40 hours. This should also deter the need for seeking supplementary employment.

It is recommended further that in general a straight "across the board" increase be given to the other classifications in Category 1 equivalent to the increase from the present to the new R-2 rate. This should be modified by a slight widening of the differentials between the unskilled, semi-skilled, skilled and professional grcups, with a view towards reducing the "compression" of the "across the board" increase above. It is suggested that the following differentials be applied:

Amount of Increase from Present to Recommended Rates:

Unskilled R Grades	7.50 yen per hour
Semi-skilled R Grades	7.70 " " "
Skilled R Grades	7.90 " " "
Professional R Grades	8.10 " " "

It is estimated that the net result of this recommendation would be roughly a three-fold increase (including reclassifications of jobs now out of line) or an average of approximately ¥2,100 at present work hours, (40 hours per week).

If longer hours are worked, as is anticipated, it will result in average earnings of about ¥2,400 per month. ¥2,400 per month represents a dollar purchasing power of $20.00 at the exchange rate of 120 to 1.

It is also recommended that the job reclassifications under consideration be expedited so as to be effective simultaneously with other actions, and that at the same time consideration be given to

reducing

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the time required for "step" rate advances. It now takes a worker three and one-third years to advance in five steps from the minimum to the maximum of an exceedingly narrow rate range.

Problems may be anticipated in increasing the wages of monthly paid workers in Category II. The present scale for these workers' wages was calculated in general on the basis of a 40-hour work week. No limitation on hours was specified, other than the overall limitation of 250 hours of work per month. To simplify the immediate problem and as a matter of equity with workers in Category I whose recommended wage rates have been calculated on the assumption of a 48-hour basic work week, it is recommended that the increase to monthly paid workers in Category II be calculated by multiplying 173 hours per month (40 hours per week) times the hourly yen increases granted in the comparable Category I classification. It is recommended, however, that these classifications be reviewed with a view to establishing a basic work week wherever possible. For those classifications where a basic work week is established at 48 hours, adjustments should be made in the wage scale for the additional hours over 40. In general a basic work week can be established for the vast majority of classifications. The exception is primarily domestic servants.

For workers in Category II, presently paid on a hourly rate basis, it is recommended that increases be given equivalent to increases in the comparable grades of Category I workers. It is assumed that job classification standards now under consideration for Category I workers will be applied also to workers in Category II. It is further recommended that when meals are provided either to monthly or hourly paid workers in Category II, deductions be permitted not to exceed the amount authorized for deductions for meals for workers in compounds. (To be discussed later.)

Present money wages on Okinawan public works projects are far above wages paid by the military, its agencies and contractors. It is essential that hourly, daily and monthly wages on the public works program be below the "prevailing" wage. Because of the preponderance of "military" workers on Okinawa, the prevailing wage is the "military" scale. Care must be exercised to see that malpractices such as "automatic" overtime, "credit" for time not worked, and superior "classifications" are not resorted to on the public works program in order to circumvent the intent of the regulation growing out of this recommendation. Public work wages outside of Okinawa should be at wages prevailing in the areas of the projects for reasons discussed elsewhere.

Okinawan civilian administration employees should be paid wages and salaries <u>comparable</u> to the "military" scale in an effort to improve their quality (reference to financing the increases involved will be made later). OGA is <u>not</u> following the American and "military" pattern of paying the worker in accordance with the type of work performed. It is continuing the Japanese practice using sex, age, education, and experience as criteria for determining the salary to be paid each employee. Whether OGA provides <u>comparable</u> wages by adopting the "military" scale and method or adapts the Japanese method to accomplish this end is not considered within the purview of this mission.

In view

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In view of the recommended increases in money wages and other compelling factors, it is proposed that the preferential treatment in price and availability of consumer goods now afforded Category 1 and 11 workers be discontinued. (Reference to factors other than wages and distribution problems are made elsewhere.) It is recommended also that wage deductions for meals for workers housed in compounds be equivalent to the cost of food without preferential treatment. It should also be pointed out that elsewhere where such feeding has been used, it has been considered a proper charge against military rather than relief funds.

This mission recognizes that its recommendations with regard to wages provide only a minimum improvement in the present low standard of living for Okinawans employed by the "military". Any reduction in the recommended wage level would place the United States in the position of exploiting the labor of a liberated area. In making these recommendations, the mission was also influenced by many other economic considerations, principally the danger of inflation involved in a too drastic increase in wage levels. It is hoped that when consumer goods in large supply are available and other forms of economic stabilization have been achieved, that it will be possible to grant further wage increases and to make provision for premium pay for overtime hours worked on the basis of international accepted standards.

Prices of Imported Foods and Financing Procedures

The mission directive contained the statement "for the purpose of making recommendations on .....prices of imported foods ....." Inter-relationships with other factors required that a review be made of pricing practices for all GARIOA goods to be distributed to the Ryukyuan people.

The financial problem is one of establishing a relationship between the several elements of the whole. GARIOA goods are imported without cost to the Ryukyuan pople. Non-GARIOA consumer goods are purchased with dollar earnings. The sum of these goods are sold to the Ryukyuan people, who have two sources of yen income - work for the "military" and work for the government, including government public works. Wages paid by the military and the government (with some adjustment for non-wage government expenditures) sets the limit in yen needed by the people to purchase the goods available.

If one assumes that consumer goods purchased with dollar earnings of the Ryukyus should move at the exchange rate and thus balance the gross wages paid by the military at the exchange rate, then the problem centers on balancing government expenditures with revenues derived from GARIOA goods distributed. A high exchange ratio for GARIOA goods distributed could generate far more yen than the government can possibly spend currently for goods and services, and carries a tremendous inflationary potential. Such GARIOA goods distributed therefore must be at an conversion ratio which will produce only the quantity of yen desired. The question then becomes one of determining the size of the RMG budget so as to establish the exchange ratio. This RMG budget should not compete or interfere with the "military" construction program. A way must be found, then, to determine what the RMG budget should be. The problem requires a national income approach. Although the national income is not known, it is possible to estimate roughly what is to be added to the national income by virtue of the GAIOA and "military" programs. Dollar earnings or

additions

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additions to the national income can be removed from consideration because the item is "balanced" by consumer goods purchased at the proposed exchange rate of 120 to 1.

The value of GARIOA goods entering the economy must then be directly related to the average wage paid by the "military". At ¥2,400 per month the average "military" worker will receive a wage equivalent to $20.00 per month at 120-1. An initial assumption made in this study was that prices would be maintained or lowered. This would call for retaining the present average conversion ratio for GARIOA commodities. This average appears to be somewhere between 40 and 60. It should be remembered that much of the goods is, in fact, "purchased" by the government, and the ratio for such goods has little meaning because of the counterbalances. The distributable portion is the significant part. An important corollary must be point out. Assuming a fixed dollar wage, an increase in GARIOA aid distributed to the people would require automatic lowering of the prices of GARIOA aid goods.

It is felt that the revenue to be derived from the present price scale on present distributed GARIOA imports will be sufficient to support a government budget estimated to be in the range from 665 to 650 million yen for this year. This excludes the value of GARIOA imports consumed by the government. The relationship of these figures to the U.S. "military" expenditure program is of significance. The latter ($10.3 million) at 120 to 1 will be ¥1,236 million in 1950. For this year the revised "military" expenditure of $4.0 million will be ¥480 million. A comparison should be noted. The original 1950 RMG budget was ¥1,242 billion, as contrasted with a U.S. "military" program of ($4.0 million) ¥200 million at 50 to 1.

The problem can be approached in another manner. Assuming a population of 960,000, GARIOA aid and construction expenditure on 1950 and 1951 represents $35 per capita per year. If the 55,000 military workers were to produce the dollars to generate sufficient purchasing power to enable the islands to match American aid expenditures in dollars (or yen at any exchange rate) it would require an annual wage of $540 per worker.

The proposed wage scale should provide an average monthly wage of $240 per year with an increase in the monthly work hours. The relationship between the $540 and $240 annual wage indicates that the import conversion ratio for GARIOA should be 44 per cent of the exchange rate whatever that rate might be. This computation would require a ratio of 33-1 if the 120-1 exchange rate is accepted. Some cushion in the ratio would have to be provided for shrinkage, loss, etc., and for some provision for the accumulation of yen in the hands of the public.

It should be noted that by holding the conversion ratio on GARIOA to 50-1, while advancing the wage scale and shifting the exchange rate to 120-1 is equivalent to providing a wage with a $540 per annum purchasing power at a $240 per annum wage rate. When the sources of

supply

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supply again become normal, roughly the same amount of goods should be available from nearby sources at the exchange rate between the 50-1 and 120-1. Further, also it should be noted that a conversion ratio of 50-1 does not alter the total for all programs in U.S. dollars. If the 50-1 ratio were not used, wage expenditures would have to be increased to compensate for the total cost of the GARIOA aid involved.

It should be pointed out that the budget problem has been most complex. Differences between the U.S. and RMG budget years only complicate an already very difficult problem. It would be well to develop a new budget now which would run to 30 June 1950, in order to coordinate budgeting and programming.

It is recognized, of course, that the ¥1,242 million RMG 1950 budget, in fact, has been drastically altered. The pay-as-you-go principle introduced an important safety element into the budget. It introduced the proper relationship between government income and expenditures but inadvertently neglected the problem of magnitude of both as related to other factors.

In the discussion of wages the recommendation has been made to apply a wage scale comparable to the "military" pay scale to Okinawa Civil Administrative employees. The increased income tax receipts from increased wage levels of "military" personnel are sufficient to raise the wage level of OCA employees to the military rate (discussion in public finance appendix).

It appears that the RMG yen budget for RMG Fiscal Year ending 31 March 1950 was set up without a translation of that budget to dollars at the then 50-1 exchange rate so as to facilitate comparison with the U.S. construction program as then evisioned. (This supposition has been confirmed.)

No discussion of financial problems can be complete without considering the distribution of the money supply. The money supply should be directed and controlled so as to facilitate overall economic recovery, to provide the outlying areas with purchasing power with which to purchase the GARIOA supplies, and to consolidate the geographic area involved into a single economic entity. Virtually all of the "military" expenditures are on Okinawa. Outlying areas, however, need funds with which to purchase their equitable share of the GARIOA imports, whatever their share may be. The only device available (in addition to the limited trade) is the RMG budget with its grants-in-aid, public works, etc.

If the requirements of the several geographic areas are programmed and distributed properly, the RMG budget can schedule expenditures in each area accordingly. (The trade problems will be discussed later in this report.) It should be pointed out that the allocation of funds for expenditure can be developed so as to include grant-in-aid, public works, and "counterpart" rehabilitation loans to industry.

"Counterpart"

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"Counterpart" as used here for the Ryukyus is intended to be only that counterpart of American aid that is loaned on a long-term basis for the rehabilitation of Ryukyuan private enterprise. Deposits are made for loans only after the loan is approved, and only to the extent that the borrower is prepared to spend such borrowings. The purpose is to provide private organizations with rehabilitation funds and to distribute purchasing power.

In Japan the counterpart fund has a different purpose. There it draws off excess currency in circulation and is then used primarily to reduce the national debt. Only a part of the total is re-introduced into the economy through loans to private (and public) enterprise. None of the Japanese counterpart fund is used to finance the government.

Large advance payments out of the central treasury should be avoided. Relatively short-term needs should determine the amount of currency made available to outlying areas. The Bank of the Ryukyus (a quasi-public institution) can be utilized as the lending institution for long-term "counterpart" loans for the rehabilitation of private enterprises. Ear-marked government deposits can be made available for loans to qualified borrowers at low interest rates for sound projects. Small loans should be at the discretion of the bank within a framework of public policy, and only large projects and supplemental loans should require RMG attention. In actual practice loans could be approved before the ear-marked government deposits need be made. In Japan a separate Reconstruction Finance Bank (operated to a large degree for political considerations) was not successful, and a similar institution is not considered advisable for the Ryukyus.

The amount of currency now in circulation is below that needed for the actions to be taken under the recommendations of this report with respect to wages, prices, etc. Because no velocity data are available, and because there is no way to measure other aspects of the problem, it is impossible to compute how much currency will be required. Certainly, the ¥266 million currently "blocked" in the Bank of the Ryukyus could be released gradually and the effects studied with care.

Trade and the Supply of Goods

Other than maintaining present or lower prices on GARIOA imports distributed to the people, an adequate supply of foreign (Japanese) goods of types desired by the Ryukyuans is the most important element in combating inflation so as to assure the success of the U.S. construction program. It is believed to be so essential that it is felt that substantial GARIOA expenditures should be made for this purpose, even if it means eliminating something else from the GARIOA program. Failure to provide consumer goods for wide distribution will result in drastic inflation as the U.S. construction program reaches its peak in 1951.

The drain of yen from outlying areas is believed to be cause in part by the preferential treatment of "military" workers and the resale of their incentive goods. The initial problem here is the concept lying behind the special trade stores. The ability to sell incentive

goods

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goods at a profit to an extent that yen are drained from outlying areas is indicative of the demand for incentive goods in those areas. It is believed that incentive goods (Commercial account and GARIOA procured) should be distributed in volume to the population at large at reasonable prices, as represented by the 120-1 exchange rate.

It is believed that the principle of reducing U.S. appropriations by the amount of Ryukyuan dollar earnings should be modified, because U.S. appropriations have never been programmed so as to include either reserves or reasonable consumer goods requirements of the Ryukyuan economy. While it is sound with respect to Japan, it is unsound with respect to the Ryukyus. The immediate need for Japanese produced consumer goods is so great in the Ryukyus that all current Ryukyuan dollar earrings plus necessary GARIOA funds should be made available at the earliest possible date to start the program. Heretofore in this report, an attempt has been made to balance wages, prices, budgets, etc. in terms of yen. Balancing dollar earnings with an inflow of consumer goods is just as essential. These dollar earnings are real earnings of the Ryukyuan economy, and should accrue to the Ryukyuans who are desperately short of consumer goods.

Finally, it should be pointed out that trade between the several islands must be facilitated so as to even out the supply of indigenous goods over the area, every impediment to such trade should be abolished, and every encouragement should be given to the development of a Ryukyuan fleet under private ownership with competitive shipping companies. Loans should be extended for the construction of such a fleet in the Ryukyus, and dollar earnings should be utilized if required for purchases from the outside. In view of the limitation (probably of long duration) on port facilities at Naha, it should be possible to promote the substitute use of other ports. Trade between the islands and Japan should also be facilitated to the greatest extent possible. With respect to trade with Japan the simplest possible procedures should be instituted so that traders, rather than government officials, do the trading.

Recapitulation

There is much in the Ryukyuan economy which is best characterized by the word "artificial." The support of its currency, however, lies in the long range prospect of continued dollar earnings resulting from the presence of the U.S. military on the island. There follows herewith a presentation showing the inflationary and deflationary elements in the recommendations made.

Inflationary

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Inflationary	Deflationary
1. Direct expansion of labor force requirements.	1. Increased supply of consumer goods.
2. Reduction in production by removal of workers from usual jobs.	2. Reduction in exchange rate for trade goods.
3. Change in exchange rate from 50-1 to 120-1	3. Holding Public Works wage line to 90% of "military" wage.
4. Increase in wage level.	4. Rise in prices for "compound" food and the elimination of trade goods stores.
5. Pressure for more hours of work.	5. Probable increase of cash balances in hands of the people.
6. Increase in budgets for outlying areas.	6. Budget control through deposit of part of the receipts of total aid.
7. Extension of rehabilitation loans.	7. Adjustment of Public works expenditure to compensate for rehabilitation loans.
8. Expansion of currency issue.	

It should be pointed out that much of the inflationary pressure resulting from an expanded construction program can be offset by improvements in the utilization of the present manpower so as to keep the expansion of the labor force to a minimum. Manpower management also plays a role in the public works programs. Proper phasing of some of that employment to coincide with those periods in which indigenous food production is at a minimum should help. Care must be taken so that hours of work and wages paid on such temporary work assignments cannot be considered superior to the usual occupation.

It is difficult to judge the net effect of all of the above as tempered by current trends. It is hoped that the net effect is to establish an equilibrium. It was pointed out initially that there is a tremendous need for consumer goods at this time. It is reported that the supply of such goods in the special trade stores is sufficient to satisfy the needs for less than two payroll periods. Immediate action should be taken to satisfy the present need and provide a continuous flow of consumer goods. A minimum of $2.0 million worth of goods should be procured immediately from GARIOA funds, and the machinery set in motion for a flow of goods at least equivalent to the dollar earnings. When this has been accomplished the changes in the wage scale and exchange rate as recommended may be made. This does not necessarily preclude negotiation on construction contracts, since the recommended wage scale may be developed immediately and converted to dollar value at the proposed exchange rate for use in cost estimates.

There

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There is considerable evidence of a lack of broad vision coordination in the overall planning to date. All programs and budgets should be brought together into a coordinated plan, within which the maximum of economic freedom and opportunity should be permitted the Ryukyuan people.

Finally, because of the lack of public confidence in the Ryukyuan yen, it might be wise to set aside a small proportion, of present dollar earnings as a fund to provide backing for the yen. Such backing should be at least equal to and perhaps greater than the exchange rate equivalent of "counterpart" loans.

Over time, as part or all of these "counterpart" loans are repaid, there would be dollar funds with which to purchase materials, supplies, and equipment from outside the Ryukyus. The overall effect would be to extend in time the force of their present dollar earnings so that some would be available after the construction program has been completed.

It is essential that the RMG budget be received and that the RMG budget year be changed so as to coincide with the U.S. budget year as an aid to budget and planning coordination.