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Perception of the Balance of Payments and Monetary Policy in the Late 1960s: Focusing on the Bank of Japan's Viewpoint before and after the Monetary Policy Shift

Hidekatsu Kamio* and Yasuko Morita**

Abstract

In the latter half of the 1960s, Japan's trade balance broke away from its traditional pattern of worsening during economic upturns. The decision to tighten monetary policy, implemented in September 1969, was made in the midst of a continuing balance of payments surplus, unlike previous tightenings aimed at improving the positions in the balance of payments. Previous studies have assessed that this tightening further increased the balance of payments surplus and led to the Nixon Shock. They have pointed out the delay in policy makers' recognition of the fundamental changes in balance of payments trends and the need to change the exchange rate. Focusing on the perspective of the Bank of Japan (hereafter BOJ) before and after this monetary tightening, this paper examines how the BOJ came to recognize trends in the balance of payments and the policy challenges of being a "surplus country," based on contemporaneous sources. In mid-1969, Japan was "for the first time in her history, experiencing the problems of surplus countries." During this period, the policy of restraining the growth of foreign exchange reserves had begun. However, foreign countries demanded more aggressive removal of import restrictions and the liberalization of capital exports on the premise that surpluses would be established. Domestically, this was perceived as the pursuit of responsibility of a surplus country. The BOJ tightened monetary policy with this responsibility in mind. At that time, the core of the responsibility of surplus countries for Japan was "getting out of the restrictive system," especially import liberalization and capital export liberalization. In this sense, the BOJ's awareness of the policy response at this point was not necessarily out of step with international standards.

Keywords: Balance of payment; Monetary policy; Responsibility of a surplus country

JEL classification: F68, N45

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I. Introduction

A. Background

In the latter half of the 1960s, Japan's trade balance broke away from the pattern of earlier years, in which imports surged and the trade balance deteriorated when the economy boomed. Even during boom times, exports grew at a faster pace than imports, and the surplus began to increase. During this period, although the deficit in the non-trade balance widened, the expansion of the trade balance surplus greatly exceeded it. As a result, the current account went into a surplus after the beginning of 1968, and remained in surplus for the next five years. On the other hand, the capital account in the late 1960s generally recorded deficits. The overall accounts¹ fluctuated between surpluses and deficits until the beginning of 1968, when the balance entered surplus territory and remained there for almost five years (see Chart 1 below).²

As for monetary policies, in September 1967 and January 1968, when the balance of payments worsened, the official discount rate was raised to curb aggregate demand, followed by a reduction in the official discount rate in August 1968. Subsequently, in September 1969, monetary policy was tightened by raising the official discount rate and the reserve requirement ratio with the aim of curbing economic expansion in order to achieve price stability. This tightening policy differed from previous ones which had aimed at improving the balance of payments, and was decided while the balance of payments surplus was continuing.³

Previous research on the September 1969 monetary tightening developed criticisms associated with the balance of payments surplus. Specifically, there is criticism that this tightening of monetary policy caused the surplus to increase further, leading to the Nixon

¹ In the statistics of the time, the short-term capital transactions of the public sector and authorized foreign exchange banks were separated from the capital account as the “balance of monetary movement” (below-the-line) and matched with the “overall balance” (above-the-line), which is the sum of other autonomous transactions (current balance + capital balance + errors and omissions) (Uchi-mura, Tanaka, and Okamoto [1998], pp. 119 and 131-134). In general, the “overall balance” was considered the most important figure as it provides a clear picture of changes in the international liquidity position and the factors behind these changes and is often referred to as simply the “balance of payments” (Kurabayashi and Watanabe [1975], p. 30). Even at the BOJ, the keynote judgment of the balance of payments was based on the “overall balance” (see BOJ Economic Research Department, “Kokunai Keizai Jousei [Monthly Economic Review],” *Chousa Geppo* [Monthly bulletin], June to October 1969 issues [in Japanese]). In later years, according to the International Monetary Fund (IMF) document, “Why Does the Current Account Matter?” (Research Department, IMF, 1979, Ref.: 212592), it is considered that “Since the onset of generalized floating in 1973, the current account has largely replaced the balance of payments as a barometer of the need for adjustment in a country's macroeconomic policies.”

² For reference details, see Itoh (2009), pp. 190-210 and 222. For more information on the policy of restraining the growth of foreign exchange reserves in 1969, see section VIII.

³ BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986), pp. 210-230.

Shock of 1971. It has been pointed out that policymakers were slow to recognize fundamental changes in the balance of payments position and the need for exchange rate changes.⁴

However, to the best of our knowledge, no previous literature has discussed in detail how the Bank of Japan (hereafter BOJ or simply the Bank) perceived the policy issues associated with Japan's balance of payments surplus in 1969.

This paper does not discuss the pros and cons of this monetary tightening itself, but instead attempts to present a different perspective, keeping in mind the criticisms of the post-Nixon Shock period as described above. Simply put, the process of the formation of perceptions of Japan's policy challenges as a "surplus country" is examined based on contemporaneous archival sources or other historical materials, focusing on the BOJ's point of view as revealed by the BOJ's materials and the comments of the Bank's governor before and after the monetary tightening of 1969.

In reviewing the awareness of policy makers at the time, this paper uses the expression of "responsibility of surplus countries" as a key phrase. This is because a closer look at domestic documents from the end of the 1960s shows that, along with this phrase, policy responses appropriate for such countries were recognized as a new issue. Although this key phrase is well known along with the "locomotive" ideas of the late 1970s,⁵ the fact that Japan was facing the problem of this responsibility even in the 1960s has not been widely introduced into discussions on the history of Japan.

The content of the responsibilities of surplus countries at the end of the 1960s discussed in this paper, unlike the "locomotive" ideas of the late 1970s, is not related to any macro-economic policy with current account surpluses in mind. It also does not include an understanding of the issues related to the necessity of exchange rate changes, which is a particular focus of previous studies. However, by relying on historical materials to confirm the process of recognizing the responsibility of surplus countries at the end of the

⁴ Nakamura (1993b), pp. 207-213 (pp. 197-205 in the 1995 English translation), and Horiuchi (1993), p. 105 (see section II for details). Krugman, Obstfeld, and Melitz (2018), pp. 599-601, argue that private financial flows were already expanding at that time and that the Bretton Woods resolution of the trilemma (allowing some degree of independence for monetary policy even under a fixed exchange rate by presuming that movements of private financial capital could be restricted) was gradually coming undone. Under these circumstances, the British trade deficit in 1964 led to intermittent speculation against the pound, which in turn led to the devaluation of the pound in 1967. In 1969, similar speculative attacks led to the devaluation of the franc and the revaluation of the Deutsche mark.

⁵ The "locomotive" ideas constitute an argument that countries with a surplus in their balance of payments should lead the global economic recovery under the low growth after the first oil crisis (MOF [2003], p. 14 [written by Akiyoshi Horiuchi], MOF [2004], p. 7 [written by Yoshio Asai]. BOJ Committee for Compiling the One Hundred Year History of the BOJ [1986], pp. 459 and 463-464). For the debate that led to the emergence of the "locomotive" ideas after the first oil crisis, see Yago (2020).

1960s, we attempt to clarify part of the historical background of the preliminary stages of the economic frictions that became increasingly acute thereafter.⁶

Incidentally, the BOJ's *Chousa Geppo* (Monthly bulletin) of 1966 contains a general statement on the responsibility of surplus countries, prior to the reference to the responsibility of Japan, which is discussed in detail in this paper. Specifically, it is argued, "given the reality that domestic inflationary pressures are increasing and the tendency to easily rely on deficit policies is growing along with the increasing demand for the realization of the welfare state, it is only natural that deficit countries should be held responsible [for correcting imbalances]. However, if we consider the fact that the constituent units of the world economy are mutually independent national economies, the country that caused the imbalance, regardless of whether it has a deficit or surplus, should take primary responsibility."⁷ At this stage, however, the discussion was limited to the sharing of responsibility for adjustment between deficit and surplus countries in general terms, and there was no reference to the responsibility of Japan as a surplus country, unlike the Governor's statement in 1969 and other statements discussed below. In addition, the report "The Balance of Payments Adjustment Process" of Working Party 3 of the Organisation for Economic Co-operation and Development (OECD), published in the same year as the above article in *Chousa Geppo* (Monthly bulletin), also discussed the responsibilities of surplus and deficit countries in general terms.⁸ However, there was no mention of the responsibility of Japan as a surplus country, which is the focus of this paper.⁹

B. Organization of This Paper

First, previous studies that discussed the relationship between the monetary tightening in September 1969 and the balance of payments surplus are introduced in section II. Subsequent sections III through VI follow the developments from April to October 1969, roughly in chronological order, and examine the perception of policy issues as a "surplus country," focusing on the perspective of the BOJ at the time. Based on the above, section VII confirms the Bank's decision on the outlook for the balance of payments in the relevant period. In section VIII, measures to control the increase in foreign exchange reserves

⁶ MOF (2004), p. 7 (written by Yoshio Asai), states that since 1976, Japan's exports to the U.S. continued to greatly exceed its imports from the U.S., and "the Japan-U.S. economic friction that had emerged at the end of the 1960s suddenly became more acute."

⁷ BOJ Economic Research Department, "Kokusai Shushi no Chousei Katei to Mondaiten (The Balance of Payments Adjustment Process and Issues)," *Chousa Geppo* (Monthly bulletin), May 1966 issue, pp. 9-10 (in Japanese) [Note: text in square brackets in the quotation is the authors' addition; the same applies hereinafter].

⁸ OECD (1966), pp. 20 and 25-26. Makino (1999, p. 50) commented that the report "pointed out the responsibility of surplus countries to adjust their imbalances along with deficit countries' one."

⁹ Prior to this, see Ishizaka (2006, 2014) for a discussion of the responsibility for the trade imbalance in West Germany in the 1950s and measures to adjust the surplus.

during this period are discussed. Section IX reviews and summarizes the 1969 issue of surplus country responsibility, and section X concludes this paper.

II. Previous Studies

The following are the previous studies that evaluate the monetary tightening of September 1969 in relation to the balance of payments surplus, that refer to the issue of the responsibility of surplus countries in the early 1970s, and that refer to statements made by participants in international conferences at the end of the 1960s. However, none of these approaches explain how the Bank's awareness of the "responsibilities of surplus countries" and the desired policy responses of surplus countries were formed before and after the monetary tightening of 1969.

A. Evaluation and Criticism of the Monetary Tightening in 1969 by Previous Studies

1. Evaluation according to the BOJ Committee for Compiling the One Hundred Year History of the BOJ

First, a historical assessment by the BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986)¹⁰ shows that several rounds of monetary tightening since 1953 were implemented with the direct aim of addressing and improving (or in the case of 1959 only, preventing) the deterioration in the balance of payments associated with economic upturn. It goes on to say that, considering that point, it was "highly distinctive" that the tightening policy in September 1969 was implemented from the perspective of restraining the pace of economic expansion in order to achieve price stability in the face of a continuing balance of payments surplus. In the first half of the 1960s, in particular, the BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986) assesses that "The situation was such that it was difficult to change policy to tighten without balance of payments reasons. Thus, the policy was managed in such a way that it was expected to result in a recovery of price stability through the implementation of a tightening policy on the grounds of improving the international balance of payments." In contrast, "This time, the central objective was to prevent the economy from overheating and to stabilize prices. Unlike in the past, the deterioration of the international balance of payments did not occur simultaneously with the excessive expansion of the economy and the rise in prices. This monetary tightening was taken in response to the situation where price stability was being undermined while a balance of payments remained in surplus. Therefore, this decision was significant in the history of the Bank's monetary policy."

With regard to the balance of payments, the BOJ Committee for Compiling the One

¹⁰ BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986), p. 230.

Hundred Year History of the BOJ (1986) states that “around 1969, when the Bank tightened its policy while running a balance of payments surplus, the debate [in Japan] centered on whether or not the surplus trend had been established.”¹¹ In this study, the Bank’s awareness of the responsibility of surplus countries is not introduced.

2. Criticism by Takafusa Nakamura

On the other hand, regarding the monetary tightening in September 1969, Nakamura (1978) noted that “Japan was at that time strengthening its international competitiveness and rapidly transforming itself from a debtor to a creditor nation.” Because of the monetary tightening at such a time, he also states that “[BOJ] cannot avoid censure that it [the Bank] underestimated [the risk of] further widening of the balance of payments surplus,” and that “although Japan’s international status was improving and its influence was growing, the significance of this [status and influence] was not fully recognized in Japan. It [the tightening in 1969] was clear evidence of this inadequate understanding.”¹² According to Nakamura (1993b), since the latter half of the 1960s, “There was a gradually widening gap between the Japanese perception of the Japanese economy as backward and underdeveloped and the much more positive way it was viewed by the international community.” In Japan, “The maintenance of the 360-yen to the dollar exchange rate was seen as a prerequisite for continued economic growth.” Further, it is considered that, “it was the monetary restraint of September 1969 which was directly responsible for making the Japanese posture a policy issue and giving rise to a major international problem.”¹³ He also states that the correct prescription to curb the penetrations of international price rises into domestic prices was to revalue the yen, but the revaluation was considered taboo, and monetary tightening was implemented. Consequently, “the monetary restraint . . . further expanded the international balance of payments surplus, inviting the so-called Nixon shocks.”¹⁴

The MOF (2000) (written by Takafusa Nakamura) argues in a subsection titled “Ripples from Precautionary Monetary Tightening Policies” as follows.¹⁵ First of all, regarding the domestic and international situation around 1969, foreign exchange speculation was rekindled when West Germany raised the official discount rate in April 1969, which led to the revaluation of the Deutsche mark in October 1969. Although there had been international calls for a revaluation of the yen, “differences in views on the yen rate between Japan and other countries eventually led to the Nixon Shock.”¹⁶ With regard to

¹¹ BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986), p. 303.

¹² Nakamura (1978), p. 315.

¹³ Nakamura (1993b), pp. 209-212 (1995 English translation, pp. 200-204).

¹⁴ Nakamura (1993b), pp. 213 and 293 (pp.141 and 204-205 in the 1995 English translation).

¹⁵ MOF (2000), pp. 337-342.

¹⁶ MOF (2000), p. 337.

Japan's tightening policy in September 1969, the literature states that "if the aim was to control prices [in terms of preventing the spread of global inflation to Japan], the correct course would have been to raise the exchange rate and lower yen-denominated import prices." Since there was opposition from the business community, "It was unavoidable that monetary policy was tightened as the next best course of action," it states, adding, "but the tightening of monetary policy should have been eased around May 1971 [note: this is probably an error for 1970, since the official discount rate was lowered in October 1970] when prices had settled down. However, as with the past several rounds of tightening, the Bank kept tightening [longer than necessary] in order to confirm its effects, which lasted until October and subsequently caused some unwelcome side effects."¹⁷

3. Akiyoshi Horiuchi's commentary

The MOF (1991) (written by Akiyoshi Horiuchi)¹⁸ summarizes the situation in 1969 as follows: "The Japanese economy faced a new problem of rising prices under a balance of payments surplus," based on the fact that the price hike showed signs of accelerating in the middle of 1969 and that the balance of payments surplus in 1969 was unprecedentedly large. It then argues as follows. If the rise in prices was caused by an overheated domestic economy (domestic factors), a tightening policy to curb such excess expansion of the domestic economy was justified.¹⁹ However, if the main cause of the price increase was inflation abroad (foreign factors), a tightening of the domestic economy may have helped to control prices but there was a great risk of causing an increase in the balance of payments imbalance. In such a case, a revaluation of the yen rate, instead of a tightening of the domestic economy, should have been considered. In the case of 1969, based on the trends in import and export prices, wholesale prices, consumer prices, and the trade balance, foreign factors appear to have been important, and exchange rate adjustment measures appear to have been a promising policy. However, in fact they were not implemented, and "the recognition of this point by Japanese policy makers was unfortunately lagging." In another chapter of MOF (1991),²⁰ it is mentioned that "the appropriate disposal of rapidly growing foreign exchange reserves was becoming an increasingly important issue for policymakers," but there is no mention of the Bank's recognition of the

¹⁷ MOF (2000), pp. 340-341.

¹⁸ MOF (1991), pp. 356-364.

¹⁹ MOF (1991), p. 358, citing an article in the BOJ's *Chousa Geppo* (Monthly bulletin) (November 1969 issue), argues that the BOJ at the time believed that rising prices were due to the overheating of the domestic economy. However, the article in question was published after the monetary tightening in September 1969. See Appendix for the Bank's perceptions before the decision to tighten. For trends in prices and interest rates, see Chart 2.

²⁰ MOF (1991), p. 352 (written by Akiyoshi Horiuchi).

“responsibility of surplus countries.”

Horiuchi (1993)²¹ points out, “The Japanese government was slow to recognize the basic change in the nation’s balance-of-payments position that occurred in the late 1960s.” He goes on to say that if the yen had been revalued in the late 1960s, it might have helped avoid the Nixon Shock of 1971.

B. Previous Studies Referring to the View of Surplus Country Responsibility in the Early 1970s

In the BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986), there is a reference to the discussion on exchange rate adjustment after 1970 and the “Opinion calling for surplus country’s responsibility” around 1971. Specifically, (1) the issue of the yen’s revaluation was squarely considered in the executive briefing materials as of February 1970, but it was assumed that the shipbuilding industry and other industries would be severely affected if the yen were revalued²²; (2) the economic report submitted to Congress by the President of the United States in February 1971 emphasized the “responsibility of surplus countries” even more than before²³; (3) by the time of the Nixon Shock in August 1971, the “argument for surplus country responsibility” —the view that the sensible solution to the problem was not to devalue the U.S. dollar, but to raise the Deutsche mark and the Japanese yen—had become dominant.²⁴

As for point (2) above, Makino (1999),²⁵ under the heading “The President’s Economic Report on the Responsibility of Surplus Countries and Japan’s Response,” introduces in detail the Japanese press reports of February 1971. For example, it cites newspaper articles critical of the “America First” doctrine, as well as a number of articles on the reaction of Japanese policy makers and business circles.

Moreover, the EPA (1976)²⁶ states under the heading “Responsibilities of Surplus Country”, “. . . as Japan became the world second economic power and its export drastically expanded, it became an actual issue to share the responsibility of balance-of-payments imbalance between the major advanced countries. From the summer to the winter of 1971, multilateral currency adjustment became a central issue between countries.”

²¹ Horiuchi (1993), p. 105.

²² BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986), p. 308.

²³ BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986), p. 299. For the U.S. President's economic report, see BOJ Economic Research Department, “Kaigai Keizai Youroku (Chronology of Overseas Events),” *Chousa Geppo* (Monthly bulletin), February 1971 issue, pp. 64-65 (in Japanese).

²⁴ BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986), p. 300.

²⁵ Makino (1999), pp.105-110.

²⁶ EPA (1976), pp. 222-224 (pp. 64-68 in the 1990 English translation).

In addition, according to the MOF (1992),²⁷ in the “New Economic and Social Development Plan” approved by the Cabinet in May 1970, it was recognized that an excessively large current account surplus was undesirable, and the plan included the phrase “pay attention to the efforts of each country to adjust its balance of payments.” As specific balance of payments measures, the plan introduced the abolition of export promotion measures, liberalization of remaining import restrictions, and liberalization of capital.

However, none of the above mentions the fact that Japan’s “responsibility of a surplus country” was being explicitly recognized in 1969, which was a preliminary step.

C. Previous Studies Referring to Statements Made by Attendees of International Conferences in the Late 1960s

In the sections entitled “A Fundamental Shift in Japan’s International Economic Status” and “Japan’s Initial Response to the New Surplus Situation,” in Angel (1991), there are some points that are related to the theme of this paper. Namely, in the 1969 OECD review of Japan, it states, “The report clearly demonstrated that the important members of the world trading system had concluded by mid-1969 that Japan had moved from deficit-prone to surplus-prone status, and hoped for domestic and international economic policy adjustments in Tokyo to cope with the new situation. The report specifically mentioned the need for more rapid trade and investment liberalization. . . . [O]fficials returning from international economic conferences in 1969, at which they had been scolded by the representatives of other countries for Japan’s combination of surpluses and domestic economic protection, announced upon arriving in Tokyo that trade and capital liberalization was urgently neededIncreasing international monetary instability later in the year heightened Japan’s sensitivity to the international resentment caused by her remaining restrictions.”²⁸ Nonetheless, it was assessed that regarding the progress of liberalization within 1969, “it came nowhere near the level of proposals suggested at airport press conferences by returnees from international economic meetings” and after that “the process dragged on throughout the period . . . even into the 1980s . . . and remained a point of vulnerability in Japan’s international relations.”²⁹

However, this prior research does not mention the fact that the “responsibility of surplus countries” was in the process of becoming explicitly recognized in Japan in 1969.

III. Events in Japan before the Decision to Tighten Monetary Policy (April to July 1969)

As mentioned above, to the best of our knowledge, there has been no prior research

²⁷ MOF (1992), p. 186 (written by Yoshio Asai).

²⁸ Angel (1991), pp. 60-61 and 64 (Japanese translation. pp. 30 and 34).

²⁹ Angel (1991), pp. 64-65 (Japanese translation. p. 35).

that focused on the recognition of the “responsibility of surplus countries” in 1969. However, a careful examination of documents from that time shows that policy makers in 1969 were aware of Japan’s position as a surplus country and were thinking about how to fulfill the “responsibilities of a surplus country.” In sections III to VI, we will examine developments since April 1969 in order.

A. April and May 1969

Within the Bank, there are indications of a growing awareness of the Japan’s position as a surplus country, but there is no indication that the Bank is explicitly aware of the “responsibilities of surplus countries.” The details are as follows.

First of all, in the paperwork prepared in April 1969 to be taken by the Governor to the Bank for International Settlements (BIS) Governors’ Meeting,³⁰ a note is found in the subsection “Current Situation and Outlook of Japan’s Balance of Payments” within the “Issues in International Finance” section. It states that the outlook for the balance of payments “is fraught with a variety of uncertain problems,” and “various assessments of the immediate increase in foreign exchange reserves are expected to be made not only by the United States but also by Western Europe, Southeast Asia, and other less-developed countries. In this case, while various external repercussions can be expected, how Japan itself evaluates the strong performance of its balance of payments and foreign exchange reserves, as well as how it will reflect this in its future balance of payments management, will be an issue for the future.”

The BIS Governors’ Meeting was held on May 11, 1969,³¹ and after returning from his trip to attend the meeting, Governor Makoto Usami attended a meeting of department heads held during the month of May and expressed his impressions of his overseas trip. A letter from the head of the Coordination and Planning Department (dated May 26 and addressed to general managers of branches)³² describes Usami’s remarks at the meeting as follows: “Prior to the Governors’ Meeting, a meeting of experts was held on May 10,

³⁰ “Sousai BIS Shucchou Shiryou (Governor’s BIS Business Trip Materials [papers]), April 26, 1969,” BOJ Archives, “Overseas Business Trip Materials in 1969 (Asian Development Bank, BIS Conference, IMF Annual Meetings),” No. 51276 (hereafter “No.” after a document name indicates a BOJ Archive Reference number corresponding to a folder with documents in the Archives).

³¹ “On [May] 11, the BIS Governors’ Meeting announced the immediate implementation of the short-term capital repatriation measures” (BOJ Economic Research Department, “Kaigai Keizai Jousei [Overseas Economic Situation],” *Chousa Geppo* [Monthly bulletin], June 1969 issue, p. 62 [in Japanese]).

³² “Sousai Kaigai Shucchou no Inshou ni tsuite (Impressions of the Governor’s Overseas Business Trip), May 26, 1969,” BOJ Archives, “Letter from the Head of the Coordination and Planning Department, 1969,” No. 10033.

which was attended by Mr. Maekawa, Executive Director, and Mr. Fujimoto, Deputy Director-General for Foreign Affairs, and discussions were held on the current currency situation. At the meeting, the topic of aid to the UK came up,³³ and I heard that the only countries with a strong balance of payments at the moment are Japan and Canada, in addition to West Germany, and that many attendees felt that aid to the UK should be borne by these three countries.” “[At the Governors’ Meeting,] the BIS first reported on the balance of payments and foreign exchange reserves of major countries over the past year, and it was noticeable that with the exception of West Germany and Japan, foreign exchange reserves had declined across the board.³⁴ This was followed by a discussion, but since almost all of the countries present were deficit countries, no active financial support was heard, and each country strongly requested West Germany to support the deficit countries.”

Thus, we can confirm that at the BIS Governors’ Meeting of May 1969, the discussion took the form of whether “surplus countries” should support “deficit countries,” and that Governor Usami informed his executives of that situation. However, there is no indication that the Bank is explicitly aware of Japan’s “responsibility as a surplus country.”

B. June 1969

The Bank’s internal circular states that the OECD Secretariat was emphasizing the “responsibilities of surplus countries.” At the same time, the “White Paper on International

³³ See BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986), pp. 260-262, for an account of how the BIS and other institutions stepped up measures to support the British pound between 1964 and 1969 in response to the decline in confidence in the pound caused by the deterioration of the British balance of payments.

³⁴ The trend of large trade surpluses in West Germany did not change mainly due to strong exports despite the introduction of import/export adjustment fee (from November 1968) and the overheating of the domestic economy (BOJ Economic Research Department, “Sekai Keizai no Kaiko to Tenbou [Developments and Prospects of the World Economy: 1969],” *Chousa Geppo* [Monthly bulletin], January 1970 issue [in Japanese]).

For the history of the introduction of the import/export adjustment fee, see BOJ Economic Research Department, “Kaigai Keizai Jousei (Overseas Economic Situation),” *Chousa Geppo* (Monthly bulletin), December 1968 issue, pp. 34 and 38-41 (in Japanese). For more information on the measures taken to deal with the country’s large current account surplus —such as low interest rate policy—and to prevent domestic economic overheating, see BOJ Economic Research Department, “Nishi Doitsu no Keiki Kanetsu Boushi Sochi no Haikai to Mondaiten (Background and Issues relating the Measures to Prevent Overheating in the West German Economy),” *Chousa Geppo* (Monthly bulletin), April 1969 issue, pp. 42-43 (in Japanese). For more on these “stalled” measures to resolve domestic and foreign imbalances, see BOJ Economic Research Department, “Maruku no Heika Kiriage ni tsuite (Revaluation of Deutsche Mark),” *Chousa Geppo* (Monthly bulletin), November 1969 issue, pp. 44-45 (in Japanese).

In addition, BOJ Economic Research Department, “Kaigai Keizai Jousei (Overseas Economic Situation),” *Chousa Geppo* (Monthly bulletin), May 1969 issue, p. 43 (in Japanese), refers to West Germany’s “obligation as a surplus country” (see section IX.B).

Economy and Trade” mentions the moderation of surplus countries. Details, including other related trends, are as follows.

In his remarks at the National Convention of Bankers on June 16, 1969, Governor Usami said, “The international environment surrounding our country has become increasingly severe, and we are now at a time when we must voluntarily take a proactive stance in promoting the liberalization of trade and capital transactions.”, referring to the need to liberalize trade and capital transactions.³⁵ The liberalization of imports and capital transactions is a point that the Governor later stated in October as a “responsibility of surplus countries” that they should actively work on (see section VI). However, it cannot be confirmed from the June address alone whether the Governor was aware of the “responsibility of surplus countries.” In addition, in the newspaper articles reporting on the convention,³⁶ the topic of liberalization was omitted from the summary of the Governor’s address, which seems to be a part that was not paid much attention at the time.³⁷

On the other hand, in his address to the convention,³⁸ Prime Minister Eisaku Sato began by noting that the international balance of payments was strong, based on a large surplus in the trade balance, and that the gross national product had “made a breakthrough to occupy the second place in the free world.” He stated that “Japan’s economy has entered a completely new phase and that it is time to pursue new goals,” and that “Japan, which has come to have the power to positively influence the world economy, must use that power for the development of the world economy and international society as a whole.” He also expressed the desire to obtain the understanding and cooperation regarding firstly “promoting the liberalization of capital and trade,” secondly “the promotion of economic cooperation [with Asian countries],” and thirdly “strengthening of self-defense.” The next day’s newspaper reported that the Prime Minister “emphasized our international responsibility.”³⁹

³⁵ FBAJ (1969a), pp. 21-23. The BOJ also published this speech (BOJ Economic Research Department, “Address by Mr. Makoto Usami, Governor of the Bank of Japan, at the Twenty-third National Convention of Bankers,” *Chousa Geppo* [Monthly bulletin], June 1969 issue, pp. 1-4 [in Japanese; We also referred to the English translation by the BOJ at the time]).

³⁶ *Nihon Keizai Shimbun* (Nikkei), June 17: “Zenkoku Ginkou Taikai, Jishu Bouei wo Kyouka, Shushou (National Convention of Bankers: Strengthening Self-Defense, Prime Minister).”

³⁷ The BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986), p. 227, discusses the Governor’s address as an indication of the BOJ’s cautionary view of the future on the way to the precautionary monetary tightening in September, but does not quote or mention the part about liberalization of trade and capital transactions.

³⁸ FBAJ (1969a), pp. 12-13.

³⁹ *Nikkei*, June 17: “Zenkoku Ginkou Taikai, Jishu Bouei wo Kyouka, Shushou (National Convention of Bankers: Strengthening Self-Defense, Prime Minister).”

In his address to the convention,⁴⁰ Takashi Yokota, President of the Federation of Bankers Association of Japan, said, “I believe that there’s only a small possibility we won’t be able to maintain a surplus in the balance of payments for the time being.” Adding that “with regard to the internationalization of the economy, there is a growing demand from overseas countries for the promotion of capital liberalization and economic cooperation with developing countries. I believe that Japan, as a member of the advanced countries, must fulfill its responsibilities.” From this address, we can see that the awareness of the issues of sustainability of the surplus trend and responsibility in the international community was not limited to policy makers.

This National Convention of Bankers was held at a time between the preliminary review (May 16, 19, and 20) and the main review (June 26) of the OECD Review of Japan, which is discussed in section V. The OECD Report on the Review of Japan was published in September, and there is no direct reference to the Review in the addresses above to this convention. However, the addresses have points in common with the contents of the review report in that there are references to liberalization of imports and capital exports based on Japan’s international status. The OECD Review of Japan is discussed in more detail in section V.A, together with the contents of the report released in September, but the Bank’s internal circular to governors as of June indicated that the OECD Secretariat was emphasizing “the responsibility of surplus countries” (see section V.A.2). In addition, the headline of a newspaper article in June that reported on the OECD Main Review included the phrase “Surplus Countries’ Obligations Under Pressure” (see section V.A.1).

The “White Paper on International Economy and Trade,”⁴¹ which was approved at a cabinet meeting the day after the above-mentioned convention, includes the phrase “moderation as a surplus country.” Looking at the “Issues facing the Japanese economy” (Chapter 2, Section 3)⁴² of the White Paper, the first paragraph, under the subheading “A New Stage for the Japanese Economy,” focuses on the fact that “balance of payments difficulties, which have constrained Japan’s economic growth in the short term on several occasions in the past, are now less likely to occur in the future.” As for the challenges of Japan’s foreign economic policy, the report says, “As the trend toward a surplus in the international balance of payments takes root, it is expected that a situation will arise in

⁴⁰ FBAJ (1969a), pp. 8-11. Mr. Yokota was the President of Nihon Kangyo Ginko (Hypothec Bank of Japan) (above-mentioned Nikkei, June 17).

⁴¹ According to the June 17 Nikkei evening edition, the 1969 edition of the White Paper on International Economy and Trade was approved at a cabinet meeting on June 17.

⁴² MITI (1969), pp. 72-80. On p. 79, it states that the trend toward a balance of payments surplus is the result of conventional efforts, and lists “promotion of export promotion efforts” as one of the issues to be addressed.

which Japan will be required to exercise moderation as a surplus country in the international economic community.” The final paragraph of this section states, “Japan should also actively work to promote liberalization in international economic transactions. Furthermore, it is expected that the demands on Japan in the international economic community will continue to increase.” It concludes, “We must correctly recognize our position in the international economic community and actively promote a foreign economic policy in line with our national strength voluntarily.”⁴³

C. July 1969

BOJ Governor Usami mentions “responsibility of a surplus country” at an informal meeting with regional banks. At the same time, the Economic White Paper, referring to “share of international responsibilities,” cites easing of residual import curbs and other issues as the “Direction of New Economic Policy” in “The Japanese Economy in a New Stage.” The following is a detailed description.

First, we take a closer look at Governor Usami’s remarks at a meeting with regional banks (held on July 17).⁴⁴ While noting that “Japan’s balance of payments continues to be favorable, supported by the growth of exports and the inflow of long-term foreign capital,” he added, “One thing that cannot be ignored is that recently there has been a sharp increasing demand from foreign countries for Japan to fulfill its responsibilities of a surplus country. Many people are critical of the fact that Japan’s large balance of payments surpluses are supported by various restrictions and protective measures on external transactions. It is expected that calls for easing of restrictions on remaining imports and liberalization of capital transactions and foreign investment will become more severe.”

In this speech, the phrase “the responsibility of a surplus country” is explicitly used, but unlike the October press conference described below, there is no statement that “we

⁴³ Makino (1999, pp. 85-86) writes of the 1969 edition of the White Paper on International Economy and Trade, “One of its features was that it was the first to provide a coherent description of the persistence of international currency instability, the development of competition among advanced countries and changes in their relative competitiveness, the improvement in Japan’s balance of payments, and the rapid increase in foreign exchange reserves. . . . The second feature was the emphasis on protectionist moves in the U.S. due to changes in competitive conditions among major industrialized countries and trade-restrictive moves in European countries due to currency instability. However, there was nothing worth mentioning in terms of policy proposals for these movements. The white paper merely emphasized trade and capital liberalization.”

⁴⁴ “Chihou Ginkou Shoutai Kondankai no Moyou (Informal Meeting with Regional Banks), July 19, 1969,” BOJ Archives, “Coordination and Planning Department Information, June to December 1969,” No. 9685. The BOJ Archives, “Coordination and Planning Department Information, January-June 1969,” No. 9684, and the same “Coordination and Planning Department Information, June-December 1969,” No. 9685, contain records of the informal meetings with regional banks (held four times during 1969).

should actively address this issue” or that we should seriously consider measures as a surplus country. In other words, although the Governor is aware of Japan’s responsibility as a surplus country, there is still a difference in terms of awareness of the need for action and a sense of urgency compared to when the Governor returned from his trip to the IMF/World Bank Annual Meetings in early October of the same year (see section VI.B for details).⁴⁵ Nevertheless, the statement by the Governor that “Recently, there has been a sharp increasing demand from foreign countries for Japan to fulfill its responsibilities of a surplus country” together with the White Paper on Trade (see subsection B above), the Economic White Paper (see below), and the documents on the OECD review of Japan (see section V for details), clearly shows how policy makers have come to recognize the “responsibility of surplus countries” at the request of foreign countries.

In the Economic White Paper⁴⁶ approved at the cabinet meeting held two days before the above meeting, the phrase “share of international responsibilities” is used, although the phrase “responsibilities of surplus countries” is not used. This white paper’s introduction⁴⁷ stated that “[in 1968] Japan has become the second largest economy in the Free World. . . . Japan’s improved international status calls for more Japanese effort toward fuller participation in the international society . . . it will . . . be the time when Japan can fulfill her share of international responsibilities.” The title of “Part II,” which describes the long-term issues facing the Japanese economy, is “The Japanese Economy in a New Stage.” In this context, “Expansion of International Interchanges” is one “Direction of International Economic Policy.” The report says, “With the expansion of our country’s economic scale and a rise in its international position, a further acceleration is increasingly called for from abroad in regard to the liberalization of external transactions and economic cooperation with other nations.” In particular, the following three issues are mentioned: (1) Trade liberalization (easing of residual import curbs), (2) Capital liberalization, and (3) Economic cooperation.⁴⁸

⁴⁵ This speech follows the passage quoted in the main text and concludes the paragraph with the words, “Looking at it this way, it is difficult to say that the foundation of our country’s balance of payments is already sufficiently strong, as some have said, and it is not permissible to assume that it will continue to be so just because it is good now.” In other words, the speech does not directly point out the need to promote liberalization.

⁴⁶ According to the July 15 Nikkei evening edition, the 1969 edition of the Economic White Paper was approved at a cabinet meeting on July 15. Makino (1999, p. 86), referring to the Economic White Paper, says, “The term ‘new stage’ in this year’s Economic White Paper was right on target. This is because in June of that year, the OECD, in its review of Japan, had in effect recognized Japan’s ‘structural imbalance’.”

⁴⁷ EPA (1969), front page.

⁴⁸ EPA (1969), pp. 282-291 (in the English translation, pp. 233-239).

IV. At the Time of Monetary Tightening (Decided at the End of August 1969, Implemented at the Beginning of September 1969)

At the time of the monetary tightening, there was no outward communication by the BOJ regarding the “responsibility of surplus countries.” On the other hand, there were several articles in the newspapers at the time that referred to the position of surplus countries, one of which stated that it was sufficient that the moderation of surplus countries would be considered through capital exports and goods import policies. The following is a detailed description.

A. Chairman’s Talk at the Time of Decision and Letter to General Managers of Branches

On Saturday, August 30, 1969, the BOJ decided to raise the official discount rate and the reserve requirement ratio, with the former to take effect on Monday, September 1, and the latter on Friday, September 5. Regarding this monetary tightening measure, the BOJ released a statement by the Chairman of the Policy Board on August 30, in which it referred to the “balance of payments surplus” as follows.⁴⁹

“In reviewing the recent economic conditions, while the nation’s balance of payments has been continuously surplus [The authors revised the English translation at the time, to conform to the Japanese version], it is to be noted that some disquieting phenomena, such as the continuous rise in prices and sharp increase in loans by financial institutions, have appeared in the wake of a fast expansion of domestic economic activity, and the overseas economic situation requires a careful watch. We have, accordingly, concluded that it would be appropriate to take action, in advance, to prevent the possible overheating of business activities in order to assure a long-enduring, stable growth of the economy.”

A letter to general managers of branches sent by the head of the Coordination and Planning Department regarding the above decision⁵⁰ was issued on September 1. In this letter, regarding “The emphasis in the case of external explanations”, the head of the department told general managers of branches, “Needless to say, this measure was taken as a precautionary measure with the aim of sustaining stable economic growth, or in other words, prolonging the current economic situation. I am sure there will be a lot of criticism because there is a balance of payment surplus, but I would like to ask you to make sure that this purpose is thoroughly understood outside the Bank.” The “Assumed Questions and Answers” attached to the private letter (prepared for public explanation and submitted to

⁴⁹ BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986), pp. 228-230 (This statement was translated into English by the BOJ in 1969).

⁵⁰ “Shitenchou ate Soumu Buchou Shishin (Letter from the Head of the Coordination and Planning Department to General Managers of Branches), September 1, 1969,” BOJ Archives, “Letter from the Head of the Coordination and Planning Department, 1969,” No. 10033.

the Governor by the Coordination and Planning Department) asked, “Is there any risk of criticism from abroad for implementing a tightening policy while the balance of payments is in surplus?” In response to this, the following answer was prepared: “It is natural for each country to place the balanced development of its economy as the first priority in its policy management. We don’t think there will be any criticism from abroad because this increase [in official discount rate] is not an attempt to increase the balance of payments surplus and we don’t think this level of hike will cause an inflow of short-term capital.”

B. Newspaper Reports

The following is a summary of newspaper reports following the announcement of the monetary tightening measures.⁵¹

1. Articles related to the Bank’s perception of the problem of surplus

At the time of this tightening, there are no reports suggesting that the Bank has made any special mention of the “responsibility of surplus countries.” Rather, Deputy Governor Tadashi Sasaki said, “One thing we were worried about was that next year, when exports to the U.S. are sluggish, if domestic demand is still strong, export sentiment might cool down even a little, with some companies’ stance being ‘If we cannot sell overseas, we will sell domestically.’”⁵²

It was also reported that Governor Usami would like to expect industrial circles to continue their “export efforts” in his statement,⁵³ which appears to have been made in part to soften opposition from outside the Bank to an increase in the interest rate related to export trade bills.⁵⁴

2. Articles related to domestic perceptions of the surplus issue

There were several articles in the press at the time that discussed the tightening, refer-

⁵¹ Based on clippings in BOJ Archives, “[BOJ’s] Base Interest Rates (Discussion of Commercial Bill Discounting System),” No. 9659 (compiled by the Coordination and Planning Department, the policy department at the time, from materials on the monetary tightening in September 1969).

⁵² Mainichi Shimbun (Mainichi), September 2: “Houdentou: ‘Kin’yu Seisaku wa Muzukashii...’ Sasaki Fikusousai (‘Monetary Policy is Difficult...’ Deputy Governor Sasaki).”

⁵³ Yomiuri Shimbun (Yomiuri), August 30 (evening edition): “Antei Seichou Iki Nagaku, Gyoukai Fukyu Toushi Yokusei wo, Usami Sousai Dan (Stable Growth, Longer Life, Industry, Curbing Unnecessary Investment, Governor Usami Says).” Asahi Shimbun (Asahi), August 30 (evening edition): “Niji Hikiage Kangaenu, Keiki no Koutai wa Sakeru, Nichigin Sousai (No Second Raise, BOJ Governor Avoids Economic Downturn).”

⁵⁴ See BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986), pp. 238-239, for the history of the BOJ’s decision to raise the interest rate on export trade bills only modestly at that time and subsequent developments.

ring to the international position as a surplus country. Specifically, “Moderation as a surplus country could be considered enough in other areas, such as the use of capital exports and goods import policies,”⁵⁵ and “Balance of payments surplus countries should have sufficient reasons to convince the international community believing in that surplus countries should not take measures to restrain the economy unless there are special reasons. . . . In terms of international cooperation and financial moderation as a surplus country, it is necessary to emphasize and convince the international community that this is a precautionary measure to sustain the current economic boom.”⁵⁶ “The U.S. wants surplus countries to adopt growth policies as much as possible. . . . It is said that the key to adjusting the fundamental imbalances of each country, which is the focus of the international monetary issue, is to achieve a comprehensive coordination of economic policies of each country. However, the fact that major industrialized countries, both deficit and surplus, have all taken steps to curb or prevent inflation has all the more brought the difficulty of comprehensive adjustment into focus.”⁵⁷

Furthermore, although there is no explicit reference to the position and responsibilities of a surplus country, some articles suggest liberalization of trade and capital based on an awareness of the problem at the level of foreign exchange reserves. For example, an editorial in the *Yomiuri Shimbun* said, “We must be careful that our tightening policy under the current balance of payments surplus will not result in us being accused by foreign countries of excessive hoarding of foreign currencies [foreign exchange reserves]. Specifically, the government should implement measures such as aggressively removing import restrictions and promoting foreign investment. The question is whether these measures will be actively pursued in the future,” concluding the final paragraph of the editorial.⁵⁸ The *Nikkei* editorial noted, “The fact that this tightening is not for balance of payments reasons but for purely domestic equilibrium reasons, as well as that it is a clear precautionary measure before the overheating stage, is a landmark in the history of Japan’s economic adjustment. . . . However, as a future issue, the fiscal and monetary authorities should make use of this opportunity to take second and third steps in a timely manner to promote imports and overseas investment in order to make effective use of foreign exchange reserves, which are expected to continue to grow.”⁵⁹

Another comment from the securities industry was, “[as for the timing of the tightening] there was talk [rumor] of tightening after the next IMF Annual Meeting. However, it

⁵⁵ The *Sankei Shimbun* (*Sankei*), August 31: “Shasetsu (Editorial: An Appropriate Policy Shift).”

⁵⁶ *Tokyo Shimbun* (*Tokyo*), August 31: “Shasetsu (Editorial: The New Meaning of Tightening).”

⁵⁷ *Nikkei*, August 31: “Sekai teki Hikishime Yuuryo, Beikoku Nihon no Seichou Saku wo Negau (Worried about global tightening, U.S. hopes for Japan’s growth measures).”

⁵⁸ *Yomiuri*, August 31: “Shasetsu (Editorial: Appropriate Monetary Tightening Policy).”

⁵⁹ *Nikkei*, August 31: “Shasetsu (Editorial: Precautionary tightening is natural).”

will be rather difficult to do so if the participants at that meeting call for our moderation as a balance of payments surplus country. Since the economy has been moving at such a high pace, it is logical to do so now.”⁶⁰ One article even included the opinion that, “The tempo of economic expansion has been accelerating, and we have reached the stage where we should take measures to adjust the economy. However, since the balance of payments continues to be strong, the monetary authorities were probably considering whether to tighten before the next IMF meeting at the end of October, out of international considerations as a surplus country. . . . Japan, as a surplus country, will be forced to promote liberalization and increase overseas investment.”⁶¹

3. Articles on evaluation and criticism of such tightening

The overall tone of the Japanese newspapers toward monetary tightening itself, including the articles listed in subsection B.2 above, is generally favorable as far as the editorials of the newspapers are concerned.⁶² For example, “Precautionary tightening is natural” (Nikkei),⁶³ “Appropriate monetary tightening policy” (Yomiuri),⁶⁴ “Considering various circumstances, it can be said to be an appropriate measure” (Asahi),⁶⁵ “Reasonable increase in official discount rate” (Mainichi)⁶⁶, and “A policy shift that was appropriate” (Sankei).⁶⁷

In contrast, only a few domestic newspaper articles critically discussed the possibility that such a tightening could widen the balance of payments gap. For example, one of the reasons cited by the Ministry of International Trade and Industry (MITI) for being critical of the official discount rate hike is that “the side effect would be to drive exports, which

⁶⁰ Tokyo, August 30 (evening edition): “Kabuka ni wa Kou Zairyō (Good news for stock prices).”

⁶¹ Nikkei, August 30 (evening edition): “Kouteibuai Hikiage, Kakukai no Hankyo, Jiki Haba tomo Datou, Kin’yu Shouken Kai (Hike in official discount rate: Reaction from various sectors, timing and range both appropriate, financial and securities industries).”

⁶² The BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986), p. 232, states, “Although there was opposition to the present round of monetary tightening by some in the industrial sector and others, the majority supported the policy action. This is also reflected in the fact that the editorials of the newspapers at the time all supported the Bank’s measures.”

⁶³ Nikkei, August 31: “Shasetsu (Editorial): Precautionary tightening is natural.”

⁶⁴ Yomiuri, August 31: “Shasetsu (Editorial): Appropriate Monetary Tightening Policy.”

⁶⁵ Asahi, August 31: “Shasetsu (Editorial): Challenges after raising the official discount rate.”

⁶⁶ Mainichi, August 31: “Shasetsu (Editorial): Reasonable increase in official discount rate.”

⁶⁷ Sankei, August 31: “Shasetsu (Editorial): A policy shift that was appropriate.”

could lead to an accumulation of balance of payments surpluses and a demand for a re-valuation of the yen.”⁶⁸ (However, another article shows that the Ministry had been active in promoting exports.⁶⁹)

As for critical commentary overseas, a Japanese newspaper reports that the Times newspaper on September 2 argued that, “Raising the official discount rate at a time when the balance of payments is running a large surplus will bring even wider international unpopularity.”⁷⁰

V. OECD Annual Review of Japan (Report Published in September 1969)

The establishment of a surplus, monetary “easing,” and the promotion of liberalization were the main issues in the June review, but the proposal for monetary “easing” was toned down in the report released in September. According to a publication by the Economic Planning Agency (hereafter EPA), there is a view that this review of Japan is the “first time” that Japan was officially required to fulfill the responsibility of a surplus country. The following is a detailed description.

A. Recognition of the Responsibility of Surplus Countries

1. Statements in the report and other documents related to the responsibility of surplus countries

The “Introduction” to the OECD’s Annual Review Report on Japan,⁷¹ released on September 1, 1969,⁷² immediately after the previously mentioned decision to tighten

⁶⁸ Nikkei, August 30 (evening edition): “Kouteibuai Hikiage Kakukai no Hankyo, Tsuusanshou wa Hihan teki (Hike in official discount rate: Reaction from various sectors, MITI is critical).”

⁶⁹ Tokyo, August 31: “Hikisage Hayame ni, Kouteibuai de Tuusanshou Kenkai, Keiki Mitoushi Kazu (MITI calls for early reduction in official discount rate; economic outlook unchanged).”

⁷⁰ Mainichi, September 2 (evening edition): “Nihon no Kouteibuai Hikiage Kakkoku no Hihan no Mato ni, za Taimuzu ga Ronpyou (Japan’s official discount rate hike draws criticism from many countries, The Times reports).”

⁷¹ OECD (1969), p. 5 (OECD/EPA translation [1969], pp. 27-28).

⁷² The preliminary review took place on May 16, 19, and 20, 1969. The main examination was held on June 26 and was attended by a delegation from Japan consisting of Mr. Setsuo Takashima, Administrative Vice Minister of the EPA (head of the delegation), Mr. Yusuke Kashiwagi, Vice Minister of Finance for International Affairs, and other officials from relevant ministries and the BOJ. As a result of this meeting, revisions were made to the Secretariat’s draft, and the report was published on September 1 (OECD/EPA translation [1969], pp. 7-8 and 14).

The EPA’s Japanese version expresses “Japan is . . . experiencing the problems of surplus countries trying to avoid . . .” as follows; “Japan is . . . experiencing the problems of surplus countries, and making an effort to avoid . . .” (OECD/EPA translation [1969], p. 28).

According to “OECD Tainichi Nenji Shinsa no tame no Jimukyoku Sakusei Repouto ni tsuite (Report Prepared by the Secretariat for the OECD Annual Economic Review of Japan), June 24, 1969,” BOJ Archives, “OECD Annual Economic Review of Japan, etc., FY 1969,” No. 9638, the person scheduled to attend the meeting from the BOJ was “Mr. Hirota, Head of Planning Division, Coordination and Planning Department.”

monetary policy, notes that, “Japan has become the world’s third biggest industrial nation next to the United States and the USSR and ranks fifth in the list of world trading countries.” “The current external surplus . . . is running at record levels and, . . . seems likely to remain substantial.” “Japan is, for the first time in her history, experiencing the problems of surplus countries trying to avoid undue strains on international liquidity. It is to be hoped that the Japanese authorities will take advantage of the present favourable economic situation to remove the remaining import restrictions and obstacles to capital exports.”

The above report was translated into Japanese by the EPA and published in December 1969, and the Japanese translation includes a “Preface” by the head of the Japanese delegation (Setsuo Takashima, Administrative Vice Minister of the EPA).⁷³ According to his preface, although he did not necessarily endorse the view that surpluses had taken root, he did suggest that the report’s recommendations for “international economic policies appropriate for surplus countries” were being accepted positively. This document is a comment made from the standpoint of the head of the Japanese delegation and can be said to show how the Japanese authorities perceived the situation at the time. To quote from the preface at some length, “A distinctive feature of this year’s [1969] report is that it focuses its analysis on the accumulation of balance of payments surpluses during economic expansion. In other words, the surplus at present in Japan’s balance of payments is not temporary but fundamental and structural, and Japan is one of the world’s largest surplus countries and should take international economic policies appropriate for surplus countries. Of course, this report presents the OECD’s view of the Japanese economy, which is not entirely consistent with the view of the Japanese delegation. In particular, there could be a great deal of debate as to whether the surplus has taken hold. However, there are many aspects of this view that should be affirmed in light of the current state of the Japanese economy. For example, the OECD points out that one of the international economic policies that should be adopted is the promotion of import liberalization, which, as you know, is also strongly urged to ensure price stability from the perspective of domestic economic policy.”

The above-mentioned Japanese translation is accompanied by a “Commentary” by the EPA. It states that there was a view among the delegation that this was “the first time that Japan has been pursued in public for its responsibility of a surplus country.” To quote from the “Commentary”, including before and after the remark above, “Against the backdrop of the demonstration of the establishment of surpluses, the core of this report is to ‘promote the liberalization of trade, capital exports, and non-trade transactions.’ It is reported that one of the delegates to this committee said that this was the first time that

⁷³ OECD/EPA translation (1969), pp. 7-8.

Japan had been pursued in public regarding its responsibility of a surplus country, and that in the five previous reviews [of the OECD], Japan had never been asked about the direction of its economic policy, especially its international economic policy, as intensely as it was this time. It is easy to imagine a heated scene at this committee meeting. . . . As the OECD is a forum for the coordination of national policies, it is only natural that it should seek to hold surplus countries accountable.”⁷⁴

Looking at the headlines of newspaper articles in June that reported on the OECD review prior to the release of the report, some of the headlines read, “OECD Review of Japan Conflicts Over Economic Outlook, Strong Wind for Liberalization, Obligations of Surplus Countries Under Pressure,”⁷⁵ while another read, “OECD to Recommend Liberalization and Increase Aid to Japan: ‘Balance of Payments Strong, Well-Established.’ The government argues that it is beyond Japan’s capabilities.”⁷⁶

2. The Bank’s recognition of the “responsibility of surplus countries” in the same examination process

The Bank’s archival materials confirm that the Bank’s internal view was that the OECD Secretariat was emphasizing the “responsibility of surplus countries” at the time of the main review in June. In the circular to the Governor issued just before the main review in June,⁷⁷ at the end of the section describing the outline of the draft prepared by the OECD Secretariat, it is summarized as follows: “Since the surplus in the basic balance is considered to be large enough to cause problems in the international financial situation, it is desirable to seize this opportunity to relax the remaining restrictions on imports and non-trade transactions and to promote capital exports, by which Japan fulfills the responsibility of surplus countries. The OECD emphasizes such points.” Together with the aforementioned speech by the Bank’s Governor in July (section III. C), we can confirm that the Bank explicitly became aware of Japan’s “responsibility as a surplus country” at that time.

B. Discussions on Monetary Policy in the Review of Japan

There is no indication that the “responsibility of surplus countries” in terms of monetary policy has been explicitly discussed. The following is a detailed description.

⁷⁴ OECD/EPA translation (1969), pp. 21-22. However, the name of the author is not mentioned in the “Commentary” above.

⁷⁵ Nikkei, June 27 (evening edition): “Keizai Mitooshi de Tairitsu OECD Tainichi Shinsa (OECD Review of Japan Conflicts Over Economic Outlook).”

⁷⁶ Yomiuri, June 21: “Jiyuu ka Sokushin shi Enjo Zougaku wo, OECD ga Tainichi Kankoku e (OECD to Recommend Liberalization and Increase Aid to Japan).”

⁷⁷ “OECD Tainichi Nenji Keizai Shinsa no tame no Jimukyoku Sakusei Repouto ni tsuite (Report Prepared by the Secretariat for the OECD Annual Economic Review of Japan), June 24, 1969,” BOJ Archives, “OECD Annual Economic Review of Japan, etc., FY 1969,” No. 9638.

1. Description of the report and its internal circulation within the BOJ

Part 4 of the report, released in September, “Policy Issues and Conclusions” described it as, “From the point of view of international equilibrium, it seems desirable in present circumstances to sustain a high rate of growth of the economy and to continue efforts to discourage borrowing from abroad. But, given the recent strength of domestic demand, the maintenance, up to now, of cautious demand management policies seems justified.” On the assumption that if the growth of exports stagnates in the future as shown in the official export forecasts, “the change might well have a depressive effect—particularly on the private investment boom, which is entering its fourth consecutive year. If such a situation were to arise later on, it would probably call for a reconsideration of demand management policy.”⁷⁸

In this regard, the BOJ’s internal circular to the Governor (dated August 28)⁷⁹ issued just before the release of the report explains that the description of the draft on monetary policy “easing” was toned down by the Japanese delegation’s objections. Specifically, in the initial draft, it was stated that “with exports expected to slow down and the investment boom entering its fourth year, it seems that the danger lies in the deficiency of anticipated demand, and that it would not be a problem to slightly ease demand management policies, especially monetary policy, in the near future.” However, “Japan emphasized at the annual review that the improvement in the balance of payments was not expected to be permanent, and that prudent policy management was absolutely necessary for the time being in view of the recent expansion in production and the remarkable upward trend in wholesale prices and wages.” For this reason, the expressions about the demand management policy in the final version “were toned down,” the circular describes.

2. The link between the OECD Review of Japan and the decision to tighten monetary policy

The date of the above circular is August 28, 1969, two days before the decision to tighten monetary policy.

The causal relationship between the OECD’s examination of Japan and the decision to tighten monetary policy is unclear, since this document does not confirm how the process of the OECD’s examination of Japan affected the decision to tighten monetary policy. However, the Bank’s actions in June, which will be described in detail below, indicate that the Bank had already taken a more cautious view of price hikes in June, and it is in

⁷⁸ OECD (1969), p. 41 (OECD/EPA translation [1969], p. 89).

⁷⁹ “OECD no Nihon Keizai ni Kansuru Houkokusho ni tsuite (OECD Report on the Japanese Economy), August 28, 1969,” BOJ Archives, “OECD Annual Economic Review of Japan, etc., FY 1969,” No. 9638.

this context that the Japanese delegation made its objections to the above draft. The decision to tighten monetary policy was made immediately after the internal paper, which described that OECD's draft was amended as a result of Japan's objections, was circulated to the Governor. This order of events seems to be meaningful. Specifically, it is possible to point out at least that the examination was underway at a time when it could have had some impact on the decision on monetary policy since June.

On June 16, 10 days before the main review, the Governor's address to the National Convention of Bankers (see section III.B) stated that "it is necessary . . . to pay due consideration to the domestic situation so that rising in consumer prices may be curbed to the greatest possible extent," and "we shall have to carefully manage monetary policies so that aggregate demand will not add to the rising pace of consumer prices."⁸⁰ In other words, it can be confirmed that at this stage, the Bank had already taken an increasingly cautious view of price increases.⁸¹

On the other hand, a closer look at the BOJ's archival documents showing the Japanese delegation's objections to the OECD review of Japan shows that the objections to monetary easing were made through the head of the Japanese delegation. The June 26 plenary session "started with an opening statement by Mr. Takashima, Administrative Vice Minister of the EPA [head of the Japanese delegation]," in which he "argued that monetary easing in the near future, as the paper [the Secretariat's draft] suggests, is not appropriate judging from the rapid expansion of production, the rise in wholesale prices, and the rapid rise in wages, and that the current prudent policy should be continued for the time being." This process of the objection is recorded in the circular to the Governor on July 5.⁸² This circular to the Governor (issued by the head of the Coordination and Planning Department) also stated that the aforementioned description regarding monetary easing in the draft was "absolutely unacceptable to the Japanese side."

3. The position of monetary policy in the review debate and its relationship to the "responsibility of surplus countries"

By looking at the "opening statement of the representative of Japan" attached to the

⁸⁰ FBAJ (1969a), pp. 21-23. BOJ Economic Research Department, "Dai 23 Kai Zenkoku Ginko Taikai ni okeru Sousai Aisatsu Youshi (Address by Mr. Makoto Usami, Governor of the Bank of Japan, at the Twenty-third National Convention of Bankers)," *Chousa Geppo* (Monthly bulletin), June 1969 issue, pp. 1-4 (in Japanese; We also referred to the English translation by the BOJ at the time).

⁸¹ The BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986), p. 227, explains that the Governor's address clearly indicates that the BOJ was taking a more cautious view of the outlook for prices, and regards his speech as "a noteworthy statement about the objectives of monetary policy management."

⁸² "OECD Tainichi Nenji Shinsa ni tsuite (OECD Annual Review of Japan), July 5, 1969," BOJ Archives, "OECD Annual Economic Review of Japan, etc., FY 1969," No. 9638.

circular to the Governor dated June 24 prior to this review,⁸³ we explore the position of monetary policy among the main issues of the review as a whole and examine the relationship between the proposal for monetary “easing” and the “responsibility of surplus countries” as follows. The document lists three particularly important points on which the Japanese delegation disagrees with the Secretariat’s draft. First, “We believe that the strong balance of payments performance in 1968 was due to the expansion of exports, which was supported by an exceptionally rapid increase in overseas demand, an extraordinary inflow of foreign capital, and moderate imports which was largely due to temporary rather than structural factors. We disagree with the Secretariat’s conclusion that the improvement in the balance of payments will be permanent,” and secondly, “The Secretariat’s draft suggests the conclusion that the Japanese economy will experience excess supply in the future. It is true that there are views in some parts of our country that are similar to this in terms of the long-term outlook. However, judging from the recent trends in the Japanese economy, such as the rapid expansion of production, the rise in wholesale prices, and the rapid increase in wages, it is unlikely that there will be a demand shortage in the near future as the Secretariat’s draft concludes. Therefore, in view of the domestic and international situation, monetary easing in the near future, as suggested by the Secretariat’s draft, is not appropriate, and we do not see the need to change the current prudent policy for the time being.” Finally, “the Secretariat’s draft raises the issue of promoting liberalization based on the conclusions referred to above, . . . but it should be approached from a more long-term and structural perspective.”

The content of the second of these arguments against monetary easing is discussed separately from the balance of payments issue.

On the other hand, as cited in subsection B.1, the OECD Secretariat’s draft considers a future “slowdown in exports” to be a lack of demand factor and cites it as the reason for the monetary “easing” recommendation. In other words, they are not calling for monetary “easing” to reduce surpluses because surpluses are “established.”

In any case, the OECD’s proposal to promote liberalization based on the judgment that a surplus had been established was the main issue in the review, and it was interpreted as the responsibility of surplus countries. However, there is no indication of any discussion on how monetary policy should fulfill the responsibility of surplus countries based on the judgment that a surplus had been “established.”

⁸³ “OECD Tainichi Nenji Keizai Shinsa no tame no Jimukyoku Sakusei Repouto ni tsuite (Report Prepared by the Secretariat for the OECD Annual Economic Review of Japan), June 24, 1969,” BOJ Archives, “OECD Annual Economic Review of Japan, etc., FY 1969,” No. 9638.

When we look again at the BOJ's assumed questions and answers at the time of its decision to tighten monetary policy (see section IV.A),⁸⁴ we find a presumably typical questioner who inquires whether there is a need for tightening, assuming that the expected "slowdown in exports" is a factor in the lack of demand in accordance with the OECD Secretariat's view. The questioner says, "if the pace of the global economic upswing slows down in the future, exports are likely to be sluggish, and the domestic economy is expected to fall in line with that. In that case, is there any need to tighten monetary policy now?" The assumed answer to the question is that there is a need to tighten monetary policy: "In view of the recent strong domestic demand, it is unlikely that the sluggish growth in exports will immediately bring about rapid changes in the domestic economy. Rather, we are concerned that the worsening of the export environment will make it impossible to expect the kind of export growth that we have seen so far, while domestic demand will remain strong, resulting in what we call a 'misalignment' of the domestic and foreign economies. Such a situation is quite possible in view of the experience of 1967, when the economy continued to rise at a rapid pace even while exports were stagnant, leading to a deterioration in the international balance of payments. The current measures are intended to take early action to prevent such a situation from occurring." In other words, the Bank considered the expectation of sluggish export growth to be one of the reasons for tightening monetary policy, as it is a factor that would worsen the balance of payments. Again, there is no discussion of monetary policy "responsibility" based on the premise of surplus "establishment."

VI. Before and after the IMF and World Bank Annual Meetings (September and October 1969)

A. Before the IMF and World Bank Annual Meetings (mid-September 1969)

We will now move on to examine the Bank's historical documents after the decision to tighten monetary policy. Looking at the assumed questions and answers prepared on September 18, 1969 for the IMF/World Bank Annual Meetings in Washington, D.C. from September 29 to October 3 of the same year,⁸⁵ it can be confirmed that the assumed questions and answers were prepared in case the "responsibility of surplus countries" was on the agenda. In other words, the question was posed, "If Japan's foreign exchange reserves continue to increase, what are your thoughts on the responsibilities of a surplus country?" The answer was, "We do not believe that its current surplus is sustainable or

⁸⁴ "Shitenchou ate Soumu Buchou Shishin (Letter from the Head of the Coordination and Planning Department to General Managers of Branches), September 1, 1969," BOJ Archives, "Letter from the Head of the Coordination and Planning Department, 1969," No. 10033.

⁸⁵ "Sousai Shucchou Wadai Jikou (Topics of the Governor's Business Trip), September 18, 1969," BOJ Archives, "Overseas Business Trip Materials in 1969 (Asian Development Bank, BIS Conference, IMF Annual Meeting)," No. 51276.

structural. However, it is true that Japan is regarded as one of the major countries with a surplus, so we will make even greater efforts to eliminate various restrictions on trade and exchange, increase aid to less developed countries, and repay our foreign debt.” According to the letter from the head of the Coordination and Planning Department dated September 19, 1969 (addressed to the Chief Representative in New York), which is preserved with the questions and answers, the questions and answers were prepared based on the summary of matters that the Chief Representative in New York expected to be discussed in the United States.

B. After the IMF and World Bank Annual Meetings (October 1969)

Governor Usami returned from the IMF Annual Meetings on October 8, 1969, arriving by plane at 4:45 p.m., and held a press conference at the airport at 5:20 p.m. on the same day.

At the press conference, Governor Usami clearly stated that international understanding of the need to tighten monetary policy even under surpluses has been obtained and that “the responsibility of surplus countries” should be fulfilled by promoting liberalization. Specifically, he said, “There were some who were concerned that the tightening measures taken in the midst of a balance of payments surplus might attract criticism from other countries, . . . but I think that the urgency of the tightening measures was easily understood by simply explaining the current situation of the domestic economy. While there was no condemnation of the tightening measures, there was very strong criticism of the restrictions on imports and capital transactions. In his speech to the General Assembly, Treasury Secretary [David M.] Kennedy said that deficit countries are working hard to eliminate their deficits, and that surplus countries should cooperate with them in this effort. We cannot help but consider that he made this speech with a strong awareness of the way Japan is going. We need to keep in mind the fact that there is a growing demand for us to fulfill our responsibilities as a surplus country, and I think that we should care about the position of the world as a whole and be more proactive in tackling the issue of liberalization of imports and capital transactions in the future.”⁸⁶

In response to this explanation by Governor Usami, a reporter asked, “How will Japan fulfill Japan’s responsibility as a surplus country?” Governor Usami started by saying, “I don’t think that surpluses have taken root like in West Germany,” before answering, “However, as long as there is actually a substantial surplus, we must seriously consider what measures we should take as a surplus country. Specifically, we need to promote the liberalization of imports and capital transactions. Frankly, I fear that if we continue to be

⁸⁶ “Sousai Kisha Kaiken Youshi (Summary of the Governor's Press Conference), October 8, 1969,” BOJ Archives, “Overseas Business Trip Materials in 1969 (Asian Development Bank, BIS Conference, IMF Annual Meeting),” No. 51276.

reluctant to break away from the current restrictive regime, there is a risk that our relations with other countries will become an emotional issue.” Incidentally, Governor Usami made no mention of the individual problems of specific industries at that time, but the following month, at a summit meeting between Prime Minister Sato and President Nixon, the issue of the reversion of Okinawa to Japan and the textile issue were discussed, and later, there was a dispute over the cleanup of the “rope (Okinawa) and thread (textile) deal” (e.g., Japan’s voluntary export control proposal), which is believed to have worsened U.S. sentiment toward Japan.⁸⁷

The following day’s Nikkei (page 4) reported the summary of the press conference under the headline, “BOJ Governor Usami Returns to Japan with a Keen Sense of Responsibility as a Surplus Country.”⁸⁸

Looking at the speech of Treasury Secretary David M. Kennedy, which was mentioned in the press conference,⁸⁹ it was stated that, “Sizable trade surpluses happen to be highly concentrated among only a few countries. We look to these countries not only to refrain from resisting adjustment but, where possible, to take actions of their own to assist and encourage it . . . it is equally clear that . . . much could be done to spread and diffuse existing surpluses in ways that support both the broad objectives of freer trade and internal stability. Import controls, systematic tying of aid, failure to share fully in the burdens of defense, preferences for domestic production, export incentives, and inhibitions on capital exports are all out of place for countries with current account surpluses ranging as high as 2 or 3 per cent of domestic production.”⁹⁰ In this speech, there is no explicit criticism of monetary tightening in surplus countries.

⁸⁷ Nakamura (1993a), pp. 544-548 (1998 English translation, pp. 381-385).

⁸⁸ Nikkei, Oct. 9: “Kurojokoku no Sekinin Tsuukan, Usami Nichigin Sousai ga Kikoku Dan (BOJ Governor Usami Returns to Japan with a Keen Sense of Responsibility as a Surplus Country).” In addition, in the upper part of the same paper (page 4) of this article, there is an article with the headline, “Kokusai Chouwa no Ninshiki Fukameru, Houou no Zoushou, Kuroji Hodo Hodo ni (Finance minister visits Europe to deepen awareness of international harmony, moderate surplus).” It reported that Takeo Fukuda, Minister of Finance, who toured Europe after the IMF Annual Meetings, was primarily interested in “finding ways to harmonize the international economy with Japan’s economy, which is gradually finding itself in the ‘difficult’ position of a surplus country amid turbulent currency instability.”

⁸⁹ For the speech by Treasury Secretary Kennedy and other key speeches, see IMF (1969b). In addition, “IMF Segin Soukai no Moyou (IMF and World Bank Annual Meetings),” BOJ Archives, “Foreign Exchange Monthly 20 (5) (September-October 1969),” No. 52200, contains a report on the meetings in Japanese. “Foreign Exchange Monthly” is a source marked “internal bank only” prepared by the Foreign Department.

⁹⁰ According to the OECD Review Report on Japan, “The [Japan’s] current surplus in 1969 is likely to amount to a nearly 1.5 per cent of GNP at current prices” (OECD [1969], p. 41, OECD/EPA translation [1969], p. 88).

VII. BOJ's Judgment on the Outlook for the Balance of Payments and the Relationship with "Responsibility of Surplus Countries"

At the same press conference in October 1969 as mentioned in section IV.B, BOJ Governor Usami stated, "I don't think the surplus has taken hold." In addition, Mr. Takashima, Administrative Vice Minister of the EPA said that the OECD review report was not entirely consistent with the Japanese delegation's view, and in particular, whether the surplus had taken root was highly controversial.

In this regard, the historical significance of focusing on the perception of "responsibility of surplus countries" can vary greatly depending on whether or not policy makers considered surpluses to be temporary. Therefore, in the following, a point in time before the establishment of surpluses was discussed at the OECD Main Review (June 1969) is returned to, and we will also confirm the evolution of the Bank's judgment on the future of the balance of payments, and present a summary of the relationship between this judgment and the "responsibility of surplus countries."

A. BOJ's Judgment on the Outlook for the Balance of Payments

The Bank did not have an optimistic outlook for the balance of payments (including the export environment), neither before or after the OECD Main Review nor before or after the monetary tightening, due to concerns about the impact on the global economy of the tightening policies of major countries. The details are as follows.

First, regarding the trends related to the balance of payments for the periods discussed in sections from II to V, we look at the "Kokunai Keizai Jousei (Monthly Economic Review)" in each issue of *Chousa Geppo* (Monthly bulletin),⁹¹ which is a monthly publication of the Bank. Prior to the OECD Main Review, "the international economic and financial environment is becoming increasingly challenging, with recent increases in official discount rates in major Western countries and a growing trend toward persistently high interest rates around the world" (May issue, dated May 2). "A large surplus trend has been witnessed in the balance of payments, but in view of the recent uncertainties in the international currency markets and the worldwide high interest rates, a cautious watch is necessary over the economic developments in overseas countries." (June issue, dated May 30). Even after the OECD Review, "interest rates overseas have risen further recently against the backdrop of the promotion of measures to curb inflation and improve the balance of payments in Europe and the United States, and the outlook for international economic and financial affairs is not optimistic." (July issue, dated July 1). "The overall account on the balance of payments in June produced a surplus . . . , the highest on record. . . ."

⁹¹ BOJ Economic Research Department, "Kokunai Keizai Jousei (Monthly Economic Review)," *Chousa Geppo* (Monthly bulletin), May-October 1969 issues (in Japanese; We also referred to the English translation by the BOJ at the time).

While the balance of payments has been continuously in surplus, no optimistic observation is warranted over the future of international economic environments in view of the persistence of high interest rates in overseas countries.” (August issue, dated August 5). And even after monetary tightening, “While the nation’s balance of payments has continued to be surplus, a disquieting phenomenon has appeared in the recent domestic economic conditions. In view of this situation and also of the necessity to keep a strict vigilance over the developments of the overseas economic condition . . . ” (September issue, dated September 5). “The overall balance of payments in August recorded a large surplus of \$197 million, but the seasonally adjusted trade surplus narrowed considerably, mainly due to the persistent rise in imports.” (October issue, dated October 3).

In addition, the “Recent Economic Trends and Future Prospects” contained in the internal paperwork for overseas business trips confirms the same view as above.⁹² Going back to the pre-OECD review period again, the following description was made: “For the time being, the balance of payments is expected to remain strong due to the growth of exports and the increase in foreign capital inflows, but in the longer term, imports will increase, and the export environment is likely to deteriorate due to the recession of overseas economies caused by the intensification of high international interest rates and moves to tighten import restrictions, and balance of payment trends thus needs attention” (April 24, 1969). “It is strongly believed that the overseas economy, which has been on an upward trend for some time, will gradually slow down its upward pace or face an inevitable recession as the effects of monetary and fiscal tightening measures taken by major countries spread. The export environment is also expected to worsen gradually, so there is no room to be optimistic about the outlook for the balance of payments” (June 4). Subsequently, the following internal review was also made: “It is inevitable that the overseas economy, which is currently on the rise, will eventually slow down, as all major countries are taking measures to tighten both monetary and fiscal policies. For this reason, the export environment is expected to gradually worsen, and we should not be optimistic about the balance of payments in the second half of the year and beyond” (June 27), “The balance of payments is expected to maintain a substantial surplus in the October-December period, as the trade balance continues to run a large surplus, supported by a high level of exports, and the inflow of long-term foreign capital such as securities investment continues to be strong. However, there is a possibility that securities investment will become a major disturbance in terms of both outflows and inflows, and in the longer term, exports are expected to stagnate due to the slowdown of the global economy as countries implement tighter policies, so future trends will require attention” (October 30).

⁹² “Saikin no Keizai Doukou to Kongo no Mitoushi (Recent Economic Trends and Future Prospects)” (April-October 1969), BOJ Archives, “Overseas Business Trip Materials, 1967-1970 (materials for WP3 and BIS monthly meetings),” No. 51275.

Furthermore, the annual review entitled “Showa 44 nen ni okeru Kin’yu/Keizai no Doukou (Economic and Financial Trends in 1969)” (printed in *Chousa Geppo* [Monthly bulletin], February 1970 issue), which was published in 1970 as a review of the year 1969, shows that, “there is an opinion heard recently that the surplus has now become settled on the balance of payments. In this regard, a review is made in the following of the trade balance in a longer range.”⁹³ This is a more detailed analysis than the monthly data. The conclusion of the report, quoted from the “Summary” at the beginning of the report, is as follows: “The strong performance of the balance of payments is mainly due to the large surplus in the trade balance, resulting from the inflationary boom overseas, the increase in Japan’s export competitiveness, and the decline in import elasticity. However, as the U.S. economy is slowing down, it is difficult to be optimistic about whether the economic boom overseas will last, and the deficits in the non-trade balance and capital account are widening, and, therefore, it is still difficult to determine if the balance of payments surplus has been established for sure. [Translated into English by the authors, as the English translation at the time did not include “Summary”.]” In other words, the judgment that it was not possible for the Bank to determine that the balance of payments would remain in surplus was clearly stated in the review on 1969 (*Chousa Geppo* [Monthly bulletin], February 1970 issue).⁹⁴

Incidentally, the IMF’s annual report,⁹⁵ published in September 1969, stated that “[Japan’s] current account surplus is smaller than Germany’s and is apparently of a less persistent nature.”⁹⁶

However, in February 1970, the same month that the above annual report clearly stated

⁹³ *Chousa Geppo* (Monthly bulletin), February 1970 issue, pp. 1 and 22 (in Japanese; We also referred to the English translation by the BOJ at the time).

⁹⁴ The previous year’s review entitled “*Showa 43 nen ni okeru Kin’yu/Keizai no Doukou* (Economic and Financial Trends in 1968)” (BOJ Economic Research Department, *Chousa Geppo* [Monthly bulletin], February 1969 issue, p. 2 [in Japanese; We also referred to the English translation by the BOJ at the time]) stated that, “By summer [in 1968], it was almost clear that the balance of payments was brought back to a sustained surplus position. The Bank rate was, therefore, lowered by 0.365 per cent [in August 1968].” Here, the expression “Sustained surplus position” was used. However, on page 1 of the same document, it is clearly stated that “Looking at the overseas environment [in 1968], . . . there are signs of a slowdown in the world economy, increasing moves to restrict imports in the United States, and various other circumstances that make it difficult to be optimistic about the future impact of these factors on Japan’s balance of payments. [The English translation of the passage at the time was not available, and the authors translated it into English.]” In other words, it can be confirmed that the expression “Sustained surplus position” here does not mean a judgment about the future.

⁹⁵ IMF (1969a), p. 13.

⁹⁶ According to the BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986), p. 303, “In the spring of 1968, there were still rumors of a devaluation of the yen overseas, even in some parts of the world; therefore, the view that the external balance would remain in surplus was not so common in 1969, one year later.”

the negative judgment on the establishment of surpluses, the Bank's internal report showed a different view from the external report. It said, "Although it is difficult to say that a fundamental imbalance exists in Japan at present, it cannot be denied that we are approaching that state. It is true that the surplus is surrounded [i.e., supported] by a wall of trade and exchange restrictions, but even if the wall was removed, the surplus would still be close to being a 'fixed surplus.'"⁹⁷ This internal paper was written to be a record of the outline of the explanation of the yen revaluation issue to the Governor, and its general contents are roughly the same as those introduced by the BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986) as an explanation document for executives as of February 1970.⁹⁸ According to the BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986),⁹⁹ BOJ directors and personnel at the time were prohibited from discussing the yen revaluation issue with outsiders, and there was a strong tendency to avoid conducting systematic internal surveys and research due to the risk of external leaks. This internal paper also states that the existence of internal discussion of the yen revaluation issue itself is "absolutely confidential."

With this delicate situation in mind, a closer look at the aforementioned monthly publications reveals that the statements regarding the outlook that existed before, such as "the necessity to keep a strict vigilance over the developments of the overseas economic condition," have disappeared in the monthly publications since October.

From this, it can be seen that the Bank's judgment on the future of the international balance of payments surplus began to waver around the second half of fiscal 1969.

B. Comparison with the OECD's Judgment to Establish a Surplus

On the other hand, the views on surplus in the OECD Review Report on Japan are generally as follows. Namely, "Although the sharp acceleration of exports has been, in quantitative terms, the most important element of the recent swing of the current balance of payments, the reason why this spectacular improvement could be achieved in conditions of continued boom is largely to be found on the import side."¹⁰⁰ Specifically (1) "[Movements in inventory change] suggests that the erratic behavior of steel purchases abroad was primarily caused by domestic capacity shortages in 1967, which were removed in 1968."¹⁰¹ (2) "The 'import saving' was concentrated on raw materials and semi-

⁹⁷ "En Kiriage ni tsuite (Regarding the Yen Revaluation), February 9, 1970," BOJ Archives, "Discussion on the issue of Yen's Revaluation," No. 30326.

⁹⁸ BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986), p. 308.

⁹⁹ BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986), pp. 306-308.

¹⁰⁰ OECD (1969), pp. 18-19 (OECD/EPA translation [1969], p. 50).

¹⁰¹ OECD (1969), p. 22 (OECD/EPA translation [1969], p. 53).

manufactures.”¹⁰² (3) “The relatively moderate growth of imports of materials since the beginning of last year [1968] has to a considerable extent been due to structural shifts of production towards less material-intensive branches or high net added value industries.”¹⁰³ In addition, regarding the outlook for the future, “If it is true that structural shifts in the pattern of production towards less import-dependent branches have been a major element behind the import-saving in the recent past, imports will persistently run below their previous trend lines so long as there is no reversal of the structural shift.”¹⁰⁴ On the other hand, in the case of the non-trade balance, “Some decline of relative import dependence also became manifest in services” and “the deficit on invisibles . . . rose relatively little in 1968.” From a longer-term point of view “the increase of the Japanese merchant fleet” has been cited as an important factor.¹⁰⁵ In the same report “Policy and Conclusions,” it says, “Given the recent strong foreign demand for Japanese securities and the likelihood of increased foreign direct investment in Japan, it may be difficult to reduce the basic account surplus to a size which would easily be offset by short-term capital exports.”¹⁰⁶ The prospects, therefore, are that Japan may remain an important surplus country for some time to come, though the size of the surplus may depend significantly on relative cyclical conditions at home and in the major foreign markets.”¹⁰⁷ The final paragraph of the report states, “Since, if present trends continue, a large surplus on Japan’s balance of payments may remain even though fast growth in the economy is maintained, further progress in liberalizing current external transactions and capital exports is highly desirable from the international point of view.”¹⁰⁸

To summarize, quoting from the EPA’s commentary at the time,¹⁰⁹ “The OECD authorities tried to explain the rationale for Japan’s established balance of payments surplus mainly by analyzing the import side. . . . It concludes that the decline in imports since 1968 is . . . basically due to the structural change of the Japanese economy to industries with less dependence on imported raw materials and higher value-added industries.”¹¹⁰

¹⁰² OECD (1969), p. 22 (OECD/EPA translation [1969], p. 57).

¹⁰³ OECD (1969), p. 22 (OECD/EPA translation [1969], p. 58). Looking at Table 8 attached to this explanation, “Machinery and equipment” and others are listed as specific examples of “industries with low material consumption.” On the other hand, “Textiles” and others are listed as specific examples of “industries with high material consumption.”

¹⁰⁴ OECD (1969), p. 24 (OECD/EPA translation [1969], p. 59).

¹⁰⁵ OECD (1969), p. 25 (OECD/EPA translation [1969], p. 59).

¹⁰⁶ The basic account excludes transactions of short-term capital from the overall account (Kurarayashi and Watanabe [1975], p. 30).

¹⁰⁷ OECD (1969), p. 41 (OECD/EPA translation [1969], p. 88).

¹⁰⁸ OECD (1969), p. 42 (OECD/EPA translation [1969], p. 91).

¹⁰⁹ OECD/EPA translation (1969), pp. 19-20.

¹¹⁰ In response to the OECD’s view, the EPA’s commentary says that the OECD’s view has problems as follows: “(1) the extent the OECD evaluates temporary and special factors, particularly on the point that Japan’s industrial production in 1968 was stagnant in the steel industry and other import-

The same commentary also introduces the OECD's assertions regarding the increase in Japanese shipping capacity and overseas demand for Japanese securities.¹¹¹

In contrast, the BOJ's annual report "Economic and Financial Trends in 1969" (*Chousa Geppo* [Monthly bulletin], February 1970 issue) made the following comments on the above issue.¹¹² First of all, with regard to imports, the report says, "As industrial sophistication advances, dependence on imports of agricultural and fishery products and less-processed industrial products will tend to increase, but on the other hand, dependence on imports of industrial raw materials will decline against the backdrop of an increase in the overall rate of value added, and, therefore, it is unlikely that the increase in total imports will exceed the tempo of production expansion." However, the following points should be noted. Namely in, "The problem of trade regulations and the invisible trade balance," it says that, "Progress in the relaxation of remaining import controls and the granting of preferential tariffs will bring about an expansion in the scale of import trade, and the expansion in the total trade volume will very possibly entail an increase in the deficit on the invisible trade account for structural reasons, centering on marine transportation accounts." Further, regarding the long-term capital transactions, "it has been supported considerably by sharply increased inflows of unstable foreign capital in the form of stock investments by foreigners. Credits extended on export by deferred payments have been expanding rapidly accompanying the increase in exports. Furthermore, Japanese investment and loans overseas, and economic aid abroad as well, are expected to increase hereafter. All in all, the present conditions warrant a further increase in outflows of Japanese capital."

As described above, while the Bank largely accepted the OECD's assertions on the import side of the industrial structural shift, it took a different view from the OECD on the non-trade balance and the long-term capital account, among others. In addition, as shown in subsection A, the Bank was more wary than the OECD about a slowdown in the global economy due to tightening policies in major countries.

related industries, (2) whether the trend of total imports can be explained only from raw material imports, and (3) the need to evaluate the recovery of inventory investment and the trend of food imports." (OECD/EPA translation [1969], p. 20).

¹¹¹ OECD/EPA translation (1969), p. 21.

¹¹² BOJ Economic Research Department, "Showa 44 nen ni okeru Kin'yu/Keizai no Doukou (Economic and Financial Trends in 1969)," *Chousa Geppo* (Monthly bulletin), February 1970 issue, p. 24 (in Japanese; We also referred to the English translation by the BOJ at the time).

C. Relationship between Judgment on Establishing Surpluses and “Responsibility of Surplus Countries”

In the “Summary” of the Bank’s annual publication (in *Chousa Geppo* [Monthly bulletin], February 1970 issue),¹¹³ the statement quoted in subsection A that, “it is still difficult to determine if the balance of payments surplus has been established for sure” is followed by the statement that, “However, there is no doubt that we have reached a stage where the responsibility in the international economic community as a country with a balance of payments surplus has increased for the time being, and that liberalization of restrictions on residual imports and promotion of foreign direct investment are necessary.” Here, the Bank refers to “surplus country responsibility” as a matter that is an “issue for the moment.” In the text of the annual release,¹¹⁴ the balance of payments for 1969 was described as “an unprecedented improvement of more than one billion dollars for the second year in a row.” After referring to the “shift to yen,”¹¹⁵ the report says that, “With a sizable balance of payments surplus, Japan’s foreign currency policy has entered a new phase that it has never experienced before. Considering that Japan’s place in the international economic world has been elevated more than ever before, accompanied by increasingly larger responsibilities, it seems necessary hereafter for Japan to actively promote import liberalization, foreign direct investment and foreign aid.”

In summary, this annual report, while taking into account the “unprecedented” large surplus and the delicate situation regarding the future of the balance of payments, states that at least in external explanations, it is not possible to determine that the surplus has been established and positions the growing “responsibility of surplus countries” as a problem “for now.” As a result, the impact of the “responsibility of surplus countries” argument itself is weakened. Having said that, it is also true that the report did not end the story with the conclusion that surpluses could not be determined to have taken root but dared to continue the story with the contradictory conjunction and referred to the “responsibility of surplus countries” as a set. In other words, the BOJ, while externally stating that it could not definitively determine whether a surplus would be established, was conscious of the arrival of “a new phase that has never been experienced before” and seems to have emphasized the “responsibility of surplus countries” after largely acknowledging

¹¹³ BOJ Economic Research Department, “Showa 44 nen ni okeru Kin’yu/Keizai no Doukou (Economic and Financial Trends in 1969),” *Chousa Geppo* (Monthly bulletin), February 1970 issue, p. 1 (in Japanese; translated into English by the authors, as the English translation at the time did not include “Summary”).

¹¹⁴ BOJ Economic Research Department, “Showa 44 nen ni okeru Kin’yu/Keizai no Doukou (Economic and Financial Trends in 1969),” *Chousa Geppo* (Monthly bulletin), February 1970 issue, pp. 19-20 (in Japanese; We also referred to the English translation by the BOJ at the time).

¹¹⁵ For more information on the policy of restraining the increase of foreign exchange reserves through the “yen shift” and other measures around 1969, see section VIII.

changes in the industrial structure. This is in some ways similar to the position of the Administrative Vice Minister of the EPA, as described in section V.A.¹¹⁶

Here, the passage quoted above says that “foreign currency policy” has entered a “new phase that has never been experienced before,” but it should be also noted that the “Conclusion” of the same document suggests that monetary policy has entered a phase different from the conventional pattern. Specifically, “it cannot be said with certainty that presently the basic surplus tone of the Japan’s balance of payments has already developed into a steady trend. Nevertheless, it is a fact that the “ceiling” of the balance of payments has, at least, been elevated. Therefore, it may readily be said that Japan is now less required than before to restrict the pace of economic growth from balance of payments point of view.”¹¹⁷ This is another sentence with a disjunctive conjunction or adverb (“but” or “nevertheless,” etc.) that continues in the opposite direction of the negative judgment about establishing a surplus.

VIII. Relationship between Measures to Control the Increase in Foreign Exchange Reserves and the “Responsibility of Surplus Countries”

As in the annual publication mentioned in section VII.C, “foreign currency policy”¹¹⁸ entered a “new phase” in 1969. According to the same report,¹¹⁹ the increase in official reserves during 1969 was much lower than the balance of payments surplus, “This was ascribable to the special attempts made by the authorities in 1969 to amend the short-term external position of Japanese foreign exchange banks during a period of a large balance of payments surplus while giving due consideration to the prevailing international monetary situation.” In this regard, previous studies have shown that the foreign exchange reserve policy was changed in 1969 to curb the growth of foreign exchange reserves.¹²⁰ In the following, an overview of the measures taken to control the increase in foreign ex-

¹¹⁶ Incidentally, in the 1969 edition of the Economic White Paper, it is said, “While the economy was pursuing a high growth, the rise in imports was relatively moderate.” The reasons for that pointed out include “(1) an increase in domestic supply capacity caused saving on imports, (2) the highly processed goods industry developed” (EPA [1969], pp. 122-123, English translation, p. 100).

¹¹⁷ BOJ Economic Research Department, “Showa 44 nen ni okeru Kin’yu/Keizai no Doukou (Economic and Financial Trends in 1969),” *Chousa Geppo* (Monthly bulletin), February 1970 issue, pp. 30-31 (in Japanese; We also referred to the English translation by the BOJ at the time).

¹¹⁸ In this annual publication, the term “foreign exchange policy” is used to explain why the increase in foreign exchange reserves has been much lower than the surplus in the balance of payments (overall balance). The content of “foreign exchange policy” here can be interpreted to mean, in effect, “foreign exchange reserve policy” (see section VIII.A for details).

¹¹⁹ BOJ Economic Research Department, “Showa 44 nen ni okeru Kin’yu/Keizai no Doukou (Economic and Financial Trends in 1969),” *Chousa Geppo* (Monthly bulletin), February 1970 issue, pp. 19-20 (in Japanese; We also referred to the English translation by the BOJ at the time).

¹²⁰ Itoh (2009), pp. 223-232, MOF (1992), pp. 208-211, MOF (1991), pp. 350-354, BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986), pp. 268-270.

change reserves during 1969 is presented, based on previous studies, and then the relationship with the recognition of the “responsibility of surplus countries,” which is the focus of this paper, is discussed. From the perspective of the “the prevailing international monetary situation” mentioned in the annual report, a comment on the yen revaluation argument is briefly added.

A. Outline of Measures to Control the Increase in Foreign Exchange Reserves during 1969

According to Itoh (2009), foreign exchange reserves surged from mid-1968 on the back of a balance of payments surplus, but it was not until 1969 that the policy issue of curbing the growth of foreign exchange reserves became explicitly recognized. It is said that this was triggered by the need to avoid a sharp increase in Japan’s foreign exchange reserves from an international perspective, as many countries around the world were suffering from declining foreign exchange reserves, and by the fact that the inflow of short-term capital as a factor for increasing foreign exchange reserves began to have a disruptive effect on not only the foreign exchange market but also the domestic financial market.¹²¹

First, on April 7, 1969, the Ministry of Finance and the BOJ adjusted their policies to gradually allow the “yen shift,” which had been suppressed until then.¹²² A yen shift is a shifting of trade finance from dollar finance to yen finance. Specifically, the government decided to allow the Japanese foreign exchange banks to switch part of their foreign currency borrowing or Eurodollar funding for imports to yen financing in the call market, for example, and to allow the Japanese foreign exchange banks to use the yen financing to acquire foreign currencies in the foreign exchange market.¹²³ According to the BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986), “It is undeniable that the reason for this guidance was not only to improve the foreign currency position of the [foreign] exchange banks, but also to control the growth of Japan’s foreign exchange reserves to some extent.”¹²⁴ While advocating the improvement of the foreign exchange bank's foreign currency position (i.e., the reduction of the private sector’s foreign liabilities), the policy intention was to curb the increase in the public sector’s foreign assets (foreign exchange reserves).

¹²¹ Itoh (2009), p. 224.

¹²² MOF (1991), p. 350. Itoh (2009, p. 230) states that “the first step [in changing the policy on the yen shift] was this resilient policy responses.”

¹²³ MOF (1991), p. 350. For an example of material published by the BOJ at the time, see BOJ Economic Research Department, “Kawase Ginkou no En Shifuto ni tsuite (On the Exchange Bank's Shift to the Yen),” “Kokunai Keizai Youroku (Chronology of Domestic Events),” *Chousa Geppo* (Monthly bulletin), May 1969 issue, p. 41 (in Japanese).

¹²⁴ BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986), p. 269.

Furthermore, on September 22, the Ministry of Finance and the BOJ introduced new measures to promote the shift to the yen.¹²⁵ The BOJ decided to introduce a measure to supply yen funds, which would be needed for the foreign exchange banks to procure foreign currencies from the Special Account for Foreign Exchange Funds.¹²⁶ The next day's Nikkei (front page top)¹²⁷ reported, "This is a new measure to improve the foreign exchange position of the foreign exchange banks, as the monetary tightening measures are stopping the yen shift (the switch from foreign currency to yen financing)." However, "it is generally believed that the aim is to prevent a rapid increase in foreign currency [foreign exchange reserves]," the report said. The Ministry of Finance's document "Measures to Promote the Shift to the Yen," dated September 20, 1969,¹²⁸ clearly states that "measures will be taken to promote the shift to the yen" and that these were "with the aim of easing the increase in foreign exchange reserves." According to the BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986),¹²⁹ the BOJ "raised the official discount rate [on September 1] under a balance of payments surplus", and the BOJ decided to supply yen funds "with a view to promoting a shift to the yen" "in order to avoid a sharp increase in foreign exchange reserves under these [rising interest rate] circumstances." Taking into account the annual report released at the beginning of the following year and the newspaper articles focusing on the "domestic-foreign interest rate differential" as described in subsection B, it can be said that under the circumstances where the voluntary shift to the yen by the foreign exchange banks stagnated due to the narrowing of the domestic-foreign interest rate differential caused by monetary tightening, the government and the BOJ intended to avoid a sharp increase in foreign exchange reserves by

¹²⁵ Itoh (2009), p. 231. According to the Nikkei article of September 23, "Gaika Kyuuzou Boushi ni Kinkyuu Taisaku, Yuro Dara Hensai ni Kai Ope de En Shikin (Emergency measures to prevent surge in foreign currency[foreign exchange reserves]: Yen funds through purchase operations to repay Eurodollar)," the Ministry of Finance announced that it would supply foreign currency funds necessary for foreign exchange banks to repay Eurodollar from the Special Account for Foreign Exchange Funds.

¹²⁶ BOJ Economic Research Department, "Gaikoku Kawase Ginkou ni taisuru Taigai Pojishon Kaizen no tameno Urimodoshi Jouken Tsuki Saiken Kaiire no Jisshi ni tsuite (On the implementation of bond purchases with repurchase conditions to improve the external position of the country's foreign exchange banks)," "Kokunai Keizai Youroku (Chronology of Domestic Events)," *Chousa Geppo* (Monthly bulletin), October 1969 issue, p. 39 (in Japanese). According to this document, "In view of the current situation of Japan's balance of payments, the aim is to further improve the external position of the foreign exchange banks through the repayment of Euro money, etc., and also to contribute to the stability of the international financial situation."

¹²⁷ Nikkei, September 23: "Gaika Kyuuzou Boushi ni Kinkyuu Taisaku, Yuro Dara Hensai ni Kai Ope de En Shikin (Emergency measures to prevent surge in foreign currency [foreign exchange reserves]: Yen funds through purchase operations to repay Eurodollar)."

¹²⁸ MOF (1998), pp. 243-244. The phrase "*Honkou* [the BOJ calls itself "*Honkou*" in Japanese]" is used in this document, and the author of the document is believed to be the BOJ.

¹²⁹ BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986), pp.269-270.

promoting the shift to the yen from the policy perspective.¹³⁰

Itoh (2009) points out that “if foreign exchange reserve policy shifted from increasing to restraining, then the policy for shifting the yen would also have to shift from restraining to tolerating and promoting.”¹³¹ As a result of this policy shift, although, in 1968, more than 80% of the overall account surplus was directed toward building up foreign exchange reserves, in 1969, about 65% of the overall account surplus was directed toward improving the foreign exchange bank’s external position (reducing external liabilities and increasing external assets).¹³²

In addition, the same year in October, “another attempt was initiated by the monetary authorities to help expedite outflows of Japanese capital through purchases of foreign currency securities.”¹³³ In this way, the “reduction of foreign currency [foreign exchange reserves]” was promoted.¹³⁴

B. Relationship between Measures to Control the Increase in Foreign Exchange Reserves and the “Responsibility of Surplus Countries”

The BOJ did not consider the above measures to control the increase in foreign exchange reserves to be a policy to fulfill the “responsibility of a surplus country.” The promotion of yen shift and acquisition of foreign currency securities had a different meaning from the promotion of liberalization. In the aforementioned annual release,¹³⁵ the text is structured to distinguish the discussion of the active promotion of imports and other liberalizations from the explanation of the “foreign currency policy” of shifting the yen and acquiring foreign currency securities. In addition, the “Summary”¹³⁶ of this annual

¹³⁰ The annual publication at the beginning of the following year (BOJ Economic Research Department, “Showa 44 nen ni okeru Kin’yu/Keizai no Doukou [Economic and Financial Trends in 1969],” *Chousa Geppo* [Monthly bulletin], February 1970 issue, p.20 [in Japanese; We also referred to the English translation by the BOJ at the time]) shows that, “The improvement in the short-term external position was initiated by foreign exchange banks with a voluntary shift to yen currency from foreign currencies in borrowings owing to higher interest rates overseas. Subsequently, however, as such voluntary means proved to be less feasible due to the stringent credit policy and rises in domestic interest rates, the Bank in September introduced a supporting measure to supply yen funds by means of purchases of securities.”

¹³¹ Itoh (2009), p. 230.

¹³² MOF (1992), pp. 210-211.

¹³³ BOJ Economic Research Department, “Showa 44 nen ni okeru Kin’yu/Keizai no Doukou (Economic and Financial Trends in 1969),” *Chousa Geppo* (Monthly bulletin), February 1970 issue, p. 20 (in Japanese; We also referred to the English translation by the BOJ at the time).

¹³⁴ Itoh (2009), p. 226.

¹³⁵ BOJ Economic Research Department, “Showa 44 nen ni okeru Kin’yu/Keizai no Doukou (Economic and Financial Trends in 1969),” *Chousa Geppo* (Monthly bulletin), February 1970 issue, p. 20 (in Japanese; We also referred to the English translation by the BOJ at the time) (see section VII.C).

¹³⁶ BOJ Economic Research Department, “Showa 44 nen ni okeru Kin’yu/Keizai no Doukou (Economic and Financial Trends in 1969),” *Chousa Geppo* (Monthly bulletin), February 1970 issue, p. 1 (in Japanese) (see section VII.C).

release lists “liberalization of remaining import restrictions and promotion of foreign direct investment” as measures related to the responsibility of surplus countries, but does not list promotion of yen shift or acquisition of foreign currency securities.

The newspapers at the time indicated that the shifting of the yen and the purchase of foreign currency securities to control the increase in foreign exchange reserves were merely “superficial” measures and not proactive measures to deal with the surplus. For example, an article reporting a question-and-answer session with Takeo Fukuda, Minister of Finance, stated, “There is a strong possibility that the narrowing of the gap between domestic and foreign interest rates [as a result of monetary tightening] will halt the shift to the yen, and that the surplus in the balance of payments will be directly reflected in an increase in foreign exchange reserves. Do you think criticism from abroad is likely to appear?” In response to the question, the minister replied, “I think that there will be more pressure for liberalization of imports and capital transactions rather than orders for domestic economic stimulus. In particular, there is a strong possibility that the Nixon administration will not seek window dressing, such as the purchase of medium-term bonds, as a balance of payments measure, but will demand the removal of various restrictions head on. Since our country stands on the strength of trade, the entire country must actively engage in liberalization.”¹³⁷ Another article said, “[With the increase in the official discount rate,] the gap between foreign and domestic interest rates has almost disappeared, and the so-called yen shift, in which Japanese companies and banks repay foreign debt and switch to yen debt, has virtually stopped. . . . Since April, Japan has prevented an increase in foreign exchange reserves superficially by shifting to the yen, but when the yen shift stops, foreign exchange reserves will increase noticeably. It is certain that Japan's balance of payments will continue to run a large surplus for the foreseeable future, and if left unchecked, this will translate directly into an increase in foreign exchange reserves.”¹³⁸ These articles do not give a positive assessment that Japan can fulfill its responsibility as a surplus country by taking those measures to control the growth of foreign exchange reserves.

On the other hand, in the “Introduction” to the OECD Review Report on Japan, there is a reference to appreciating Japan’s attitude of showing consideration for “international liquidity” by stating “Japan is, for the first time in her history, experiencing the problems of surplus countries trying to avoid undue strains on international liquidity. It is to be

¹³⁷ Nikkei, August 31: “Zaimu no Kenzen sei Zettai Mamoru, Fukuda Zoushou tonon Kaiken Naiyou (Financial Soundness Absolutely Protected in Meeting with Finance Minister Fukuda).”

¹³⁸ Asahi, September 2: “Gaika Junbi, Naigai Kinrisa Kaishou de Kyuusokuni Fueso (Foreign currency reserves likely to increase rapidly as domestic and foreign interest rate differentials are resolved).”

hoped that the Japanese authorities will take advantage of the present favourable economic situation to remove the remaining import restrictions and obstacles to capital exports” (see section V.A). In addition, Part 4 of the report, “Policy Issues and Conclusions,” also mentions that “it seems desirable in present circumstances . . . to continue efforts to discourage borrowing from abroad” (see section V.B.1) and “further progress in liberalizing current external transactions and capital exports is highly desirable from the international point of view” (see section VII.B).

In light of the above, from the perspective of consideration for “international liquidity,” restraining foreign borrowing and promoting repayment were desirable measures as a matter of international sentiment, as many countries around the world were suffering from declining foreign exchange reserves.¹³⁹ Nevertheless, the Bank, like the Ministry of Finance and the OECD, recognized that consideration of “international liquidity” alone was insufficient, and considered the promotion of liberalization to be more important.

Even before that, Governor Usami believed that “international liquidity” was important, but that it was not enough alone to solve the problem. At the National Convention of Bankers in July 1968, the address by the Governor stated that, “The international agreement on the creation of the Special Drawing Rights has been acclaimed, but SDRs are not a panacea for all the problems facing us in international financing. It must be noticed especially in this connection that countries with a deficit balance of payments must adjust their domestic economy as well.”¹⁴⁰ Then, a year later, he referred to the “responsibility of surplus countries” (see section III.C).

In any case, the policy response to the yen shift and the recognition of the responsibility of surplus countries together suggest that the Bank, like other policymakers, was in the process of deepening its awareness of the problem of surpluses during this period. The BOJ tightened monetary policy in 1969, but if we look at the situation before and after the tightening, we can see that the Bank did not neglect the expansion of the international balance of payments surplus.

C. International Currency Situation and the Issue of Yen Revaluation

In general terms, an increase in foreign exchange reserves is considered to be a factor bringing the revaluation of the local currency. However, there is no indication that the

¹³⁹ It has been pointed out that one of the inherent flaws of the Bretton Woods system was that it lacked a mechanism to provide international liquidity in a manner consistent with the expansion of world trade (BOJ Committee for Compiling the One Hundred Year History of the BOJ [1986], p. 294).

¹⁴⁰ BOJ Economic Research Department, “Dai 22 Kai Zenkoku Ginko Taikai ni okeru Sousai Aisatsu Youshi (Address by Mr. Makoto Usami, Governor of the Bank of Japan, at the Twenty-second National Convention of Bankers),” *Chousa Geppo* (Monthly bulletin), August 1968 issue, p 1 (in Japanese; We also referred to the English translation by the BOJ at the time).

BOJ was aware of the need to revalue the yen as early as 1969. In June of the same year, at the National Convention of Bankers (see section III.B), Governor Usami said, “there are some who over-estimate the Japanese yen and claim that it should be revalued. I do not think their view is correct, and I think this is evidence of how much interest our country has received from the world.” He also explained that, “An important step to solve the international monetary problem is to replenish international liquidity through the deliberate creation of Special Drawing Rights. International cooperation among major countries is also an important step towards a solution. These measures will of course prove to be beneficial, but what is more important than anything else is that all countries should adopt a strong policy to curb inflation and should observe discipline concerning the balance of payments.”¹⁴¹ After leaving office, he said in his reminiscing, “I went to a number of international conferences and exchanged opinions, but no other country pressed me to revalue the yen.”¹⁴²

During the IMF Annual Meetings in 1969, West Germany provisionally suspended its parity maintenance operations, which stimulated discussion on the elasticity of the fixed exchange rate system, but the IMF said it would continue to study the issue.¹⁴³ The main topic of the IMF Annual Meetings was the determination of the initial allocation of Special Drawing Rights. The expansion of international liquidity was an agreement to maintain the Bretton Woods system. At least during this period, revaluation of the yen was not a policy issue that was explicitly called for in official international discussions, unlike the issues of international liquidity and liberalization.

In other words, the 1969 issue of surplus country responsibility did not explicitly call for Japan to revalue the yen. The content is different from that of the 1971 dispute of the responsibility of surplus countries (see the previous literature in section II.B). It was during the late 1960s that Japan became the new “surplus country.” In this period, it was exactly the kind of situation about which had been said, “Japan is, for the first time in our history, experiencing the problems of surplus countries trying to avoid undue strains on international liquidity” (see subsection B). The fact that the BOJ and other policymakers did not recognize the need to revalue the yen at this time does not necessarily seem to imply a delay in recognition of balance of payments position and policy issues.

¹⁴¹ BOJ Economic Research Department, “Dai 23 Kai Zenkoku Ginko Taikai ni okeru Sousai Aisatsu Youshi (Address by Mr. Makoto Usami, Governor of the Bank of Japan, at the Twenty-third National Convention of Bankers),” *Chousa Geppo* (Monthly bulletin), June 1969 issue, p. 1 (in Japanese; We also referred to the English translation by the BOJ at the time).

¹⁴² Usami (1971), p. 80 (“My Personal History”, serialized in the newspaper in January 1971).

¹⁴³ BOJ Economic Research Department, “Kaigai Keizai Youroku (Chronology of Overseas Events),” *Chousa Geppo* (Monthly bulletin), October 1969, p. 56 (in Japanese). BOJ Economic Research Department, “Sekai Keizai no Kaiko to Tenbou (Developments and Prospects of the World Economy),” *Chousa Geppo* (Monthly bulletin), January 1970 issue, pp. 14-15 (in Japanese).

IX. Some Reflections on the Issue of Surplus Country Responsibility and Monetary Tightening as of 1969

A. Contents of the Issue of Responsibility of a Surplus Country as of 1969

Summarizing sections III to VIII, Japan's "responsibility as a surplus country" in 1969 was, in short, to promote liberalization. To use Governor Usami's words from section VI.B, this means "getting out of the restrictive system," or more specifically, "liberalizing imports and capital transactions." Here, we discuss some of its meanings and background.

1. Import liberalization

First, we will look at import liberalization. The *Chousa Geppo* (Monthly bulletin)¹⁴⁴ of the beginning of the following year, which reviewed the world economy in 1969, stated that "trade in the free world" had expanded rapidly for the second year in a row due to a marked increase in imports by industrialized countries. It also pointed out that there had been "moves to effectively restrict imports" in some countries. As a prime example, it cited that the U.S. government had demanded that countries "self-regulate" their steel exports to the U.S., and then further intended to demand that they extend the same restrictions to other items, including textiles. In addition, it expressed belief that the U.S. government was "getting flustered (*aseri*, in Japanese) with the delay in improving the trade balance." Here, we find the word "*aseri*" which is not typical for official economic reports.

The background to the recognition of the "responsibility of surplus countries" in Japan in 1969 can be considered to be such an international situation. In the process of moving toward a sensitive environment, Governor Usami, citing the U.S. speech at the IMF Annual Meeting, said that the reluctance to "break away from the restrictive regime" could lead to "emotional problems" in relations with other countries (see section VI.B).

The BOJ was not alone in emphasizing import liberalization (the issue of remaining import restrictions) as a foreign policy priority. The EPA also emphasized trade liberalization. The 1969 Economic White Paper,¹⁴⁵ after pointing out the international status of Japan as the "second largest economy in the free world" as background, placed "trade liberalization" at the top of its list of foreign policy issues. It is argued in the White Paper that "there are still 120 items under the residual import curbs And this number is the largest among principal advanced countries. . . . From the standpoint that a further acceleration of trade liberalization will after all serve to strengthen the structure of the Japanese

¹⁴⁴ BOJ Economic Research Department, "Sekai Keizai no Kaiko to Tenbou (Developments and Prospects of the World Economy)," *Chousa Geppo* (Monthly bulletin), January 1970 issue, pp. 9 and 11 (in Japanese).

¹⁴⁵ EPA (1969), pp. 100 and 284 (pp. 85 and 233 in the English translation).

economy, it will be essential to lift the present restrictions as soon as possible. And this would also be instrumental in checking the protectionist moves, which have been mounting in recent years.”

The white paper itself does not provide a more detailed explanation for the issue of the remaining import restrictions, but the 30-year history of the EPA¹⁴⁶ explains this issue as follows: “In order to prevent reduction of reserve assets (mainly gold) and to improve the international balance of payments, the U.S. announced the measures to defend dollars in the presidential statement in 1968. It declared that countries with surplus had a special obligation for equilibrating international balance of payments. . . . It also demanded Japan to take a drastic step to eliminate the remaining import restrictions. After then, negotiations were repeated. . . . Import liberalization for which the first step was completed during Showa 30’s [1955-1964] was taken up a new policy issue as Japan became a surplus country. . . . The EPA played a coordinating role on the issue of remaining import restrictions. [The last sentence is not in the 1990 English translation, and, therefore, the authors translated it into English to match the Japanese version.]”¹⁴⁷

On the occasion of the announcement of the above measures to strengthen the defense of the dollar, a press conference was held by President Johnson on January 1, 1968, and special envoys were dispatched to the countries concerned, including Japan. The BOJ argued that “this is an unusual measure that has not been seen in the past four invocations of the dollar defense measure, and in this respect, it is perceived by many countries as a sign of the U.S. government’s firm determination to defend the dollar this year [1968].”¹⁴⁸

In short, the U.S. balance of payments problem was the background to the new issue of another round of import liberalization in Japan in this period.

2. Capital export liberalization

Next, we turn to the liberalization of capital exports. As mentioned above (see section V.A.1), the OECD Review Report on Japan calls for liberalization of capital exports (removal of obstacles to capital exports) along with import liberalization (removal of remaining import restrictions).¹⁴⁹ The “Summary” of the Bank’s annual release argues that

¹⁴⁶ EPA (1976), pp. 219-220 (pp. 60-61 in the 1990 English translation).

¹⁴⁷ Furthermore, in EPA (1976), pp. 284-285 (omitted in the 1990 English translation), an outline of the U.S. request and Japan’s response after 1968 is introduced, stating that “especially due to the deterioration of the U.S. balance of payments, the movement for import liberalization became active again around 1968.”

¹⁴⁸ BOJ Economic Research Department, “Kaigai Keizai Youroku (Chronology of Overseas Events),” *Chousa Geppo* (Monthly bulletin), January 1968 issue, p. 87 (in Japanese).

¹⁴⁹ As mentioned in section VIII.B, while the report states that “it seems desirable in present circumstances . . . to discourage borrowing from abroad,” there is no explicit reference to direct investment from abroad (inward direct investment). At that time, Japan was in the middle of a gradual and

surplus countries need to “liberalize remaining import restrictions and promote foreign direct investment” as their responsibility (see section VII.C). In other words, capital export liberalization, along with import liberalization, was recognized as one of the two pillars of surplus country responsibility.

The Bank’s research on foreign economies focused on “long-term capital exports” as an “obligation of surplus countries” in West Germany even before the Bank’s policy department mentioned the “responsibility of surplus countries” at the time of the OECD’s review of Japan. This point is discussed in detail in subsection B.

The liberalization of foreign direct investment was being considered by the government from an even earlier stage.¹⁵⁰ The “Technical Methods for Controlling the Increase in Foreign Exchange Reserves,”¹⁵¹ drafted by the International Finance Bureau of the Ministry of Finance in March 1969, does not refer to the “responsibility of surplus countries,” but does include the following measures as part of “1. Suppressing the generation of foreign currency surpluses,” in order: “(1) easing of import restrictions, (2) easing of restrictions on foreign investment, (3) curbing the inflow of medium- to long-term foreign capital (impact loans and foreign bonds), and (4) other measures.”¹⁵² This shows that the emphasis was not only on the trade balance but also on the capital account.

The Bank’s recognition of the responsibility of surplus countries was consistent with these government considerations.

step-by-step process of liberalizing inward direct investment (foreign capital entering Japan) since 1967 at the request of the OECD and the United States (MOF [1992], pp. 216-289, Itoh [2009], pp. 210-214). In other words, in the process of liberalizing inward direct investment, there was also a need to liberalize capital exports. With regard to foreign investment, the first round of liberalization measures was implemented in September 1969 and these continued to the fourth round of liberalization measures in June 1972. After these rounds, most of the outward investment shifted to an automatic approval system (MOF [1992], pp. 299-300).

¹⁵⁰ According to FBAJ (1969b), pp. 66-67 (“Measures to Liberalize Foreign Direct Investment”), the government internally studied foreign capital transactions from February to July 1967, but the study was abandoned due to the worsening of the international balance of payments. Around November 1968, the study was resumed. In February 1969, the Council on Foreign Investment submitted its opinion to the government that the government should “seek the opinion of the appropriate government council” on the liberalization of foreign investment. In September of the same year, the Council on Foreign Investment compiled its “Opinions on Foreign Investment and Related Matters.” The liberalization of foreign direct investment was implemented in line with this opinion, and Japan’s position under the OECD Code of Liberalisation of Capital Movements shifted from full reservation to partial reservation.

¹⁵¹ MOF (1998), p. 233.

¹⁵² In this document, following the above measures, measures related to the yen shift are also listed as “(1) Absorption through improvements in the foreign exchange banking sector” at the top of “2 Curbing the concentration of foreign currency surpluses in foreign exchange reserves.”

3. Summary on the responsibility of a surplus country

As mentioned above, the main focus of the issue of the responsibility of a surplus country in 1969 was “getting out of the restrictive system,” especially through import liberalization and capital export liberalization. This was consistent not only with the OECD’s recommendations but also with the government’s considerations. The phrase “getting out of the restrictive system” was used in the Governor’s press conference in October, but as mentioned in section V.A.2, the Bank had been aware of such an issue of surplus country responsibility since the occasion of the OECD Review of Japan in June.

B. Relationship between the Recognition of the Responsibility of a Surplus Country and the Decision to Tighten Monetary Policy

Based on the summary in subsection A.3, the relationship between the recognition of the responsibility of a surplus country and the decision to tighten monetary policy is further discussed here.

As already mentioned (see section V.B.2), the BOJ decided to tighten monetary policy two days after it became aware of the contents of the final version of the OECD Review Report on Japan. This fact leaves room for interpretation that the BOJ confirmed the final content of the OECD’s policy recommendations before deciding to tighten monetary policy. This is because the Bank’s policy department (Coordination and Planning Department) believed that “the OECD Secretariat emphasized various points, such as the desirability of fulfilling the responsibilities of surplus countries,” from the time of the main review in June. The role of monetary policy was not emphasized in this review of Japan after all.

For Governor Usami, the issue of the responsibility of surplus countries does not seem to have been an argument unrelated to monetary policy, since at the press conference after the IMF Annual Meeting, he referred to the responsibility of surplus countries to promote liberalization, immediately after his explanation that there was no criticism of monetary tightening in surplus countries from abroad (see section VI.B). In general terms, the issue of liberalization is probably outside the Bank’s purview. For Governor Usami, however, criticism from abroad over the delay in liberalization was an argument that could not be ignored. This seems to have been evidence that Governor Usami was conducting monetary policy with a clear awareness of the country’s status as a surplus country.

Even before the OECD review of Japan, the Bank’s overseas research section had focused on the “obligations of surplus countries” when West Germany raised its official discount rate. The BOJ’s *Chousa Geppo* (Monthly bulletin)¹⁵³ explains that the reason

¹⁵³ BOJ Economic Research Department, “Kaigai Keizai Jousei (Overseas Economic Situation),” *Chousa Geppo* (Monthly bulletin), May 1969 issue, p. 43 (in Japanese).

that the Bundesbank decided to raise interest rates in April 1969 is that “while economic overheating is finally becoming noticeable, the rise in the level of global interest rates has opened up room for both domestic interest rate hikes and capital exports.” It then refers to the Bundesbank’s explanation that long-term capital exports could offset current account surpluses and argues that the Bundesbank “emphasizes that it does not neglect the obligations of surplus countries.” With the rise in global interest rates, capital exports were still possible even after domestic interest rate hikes. Therefore, West Germany was trying to fulfill its “obligations as a surplus country” by exporting capital. The BOJ understood in that way.

Regardless, it is a fact that the BOJ was at least aware of the “responsibility of surplus countries” even before it decided to tighten monetary policy. Returning to the topic of Japan as of 1969, the OECD review of Japan called for liberalization of imports and capital exports on the assumption that a surplus would be established. Since the time of the June Review, the Bank’s policy department had taken this as a pursuit of “responsibility of a surplus country.” However, at this stage, currency revaluation was not yet regarded as “the responsibility of surplus countries.” Under these conditions, the BOJ decided to tighten monetary policy at the end of August.

X. Conclusion

Prior studies have criticized the monetary tightening of September 1969 by pointing out the delay in recognizing the fundamental changes in balance of payments trends and the need to change the exchange rate. Focusing on the BOJ’s perspective before and after the tightening, this paper examines the process of the formation of the Bank’s perceptions of balance of payments trends and policy issues as a “surplus country,” using the phrase “responsibility of a surplus country” found in sources from 1969 as a clue.

The period mainly examined in this paper is only about six months, around the policy shift. However, as far as the data presented in this paper are concerned, the policy issues recognized by the BOJ at that time were generally consistent with the recommendations of the OECD Review of Japan and the perceptions of the Japanese delegation at that review.

Looking at the White Papers of that time and the materials related to the OECD’s review of Japan, it can be seen that by the middle of 1969, Japan’s policy makers were aware that the improvement in international status that accompanied the expansion of the size of the economy had ushered in a “new stage” and that the issue of the responsibility of a surplus country was becoming a new policy challenge for Japan. Japan was “for the first time in her history, experiencing the problems of surplus countries,” and Japan had begun to search for an “international economic policy appropriate for a surplus country.” In the process of the OECD’s examination of Japan from June 1969 onward, the removal

of import restrictions and the liberalization of capital exports were called for on the premise that a surplus would be established. In Japan, this was perceived as the pursuit of responsibility as a surplus country. Just prior to the main review, the Bank's internal circular to the Governor indicated that the OECD Secretariat was emphasizing the responsibility of surplus countries. In addition, a publication by the EPA mentioned the view that the responsibility of surplus countries was being officially pursued for the first time. To add more detail, import liberalization had once again become a new issue with the U.S. since the strengthening of the dollar defense in early 1968.

In the same review process, monetary easing was also recommended. However, the OECD Secretariat had assumed a lack of demand due to a "slowdown in exports" in the near future. At this time, there is no indication that the issue of how to conduct monetary policy based on the establishment of surpluses was discussed as the responsibility of surplus countries.

At that time, inflation was a global concern and interest rate levels were rising. In such a situation, West Germany was trying to fulfill its obligations as a surplus country by exporting long-term capital even after the official discount rate hike in April. At least, that was how the BOJ understood it.

At the timing of the decision to tighten monetary policy at the end of August, there is no indication that the Bank made any special mention of the responsibility of surplus countries. On the other hand, there was an editorial in newspapers at the time that argued that it was sufficient that the moderation of surplus countries would be considered through the use of capital exports and goods import policies.

Later, at a press conference in October upon his return from the IMF/World Bank Annual Meetings, BOJ Governor Usami asserted that international understanding of monetary tightening under surpluses had been achieved, but that surplus countries should fulfill their responsibilities by promoting liberalization. The governor was clearly aware of the country's status as a surplus country when he conducted monetary policy.

Additionally, in its annual assessment of balance of payments trends at the beginning of 1970, the BOJ, while explaining to the outside world that it could not definitively determine whether a surplus would be established, recognized that "foreign currency policy has entered a new phase that we have never experienced before," and emphasized the responsibility of surplus countries, largely acknowledging changes in industrial structure.

Although the Bank tightened monetary policy during this period, it did not neglect the problem of the balance of payments surplus. For example, in response to the narrowing of the gap between domestic and foreign interest rates, it worked to promote a shift to the yen. Such a response was desirable from the perspective of consideration for "international liquidity," but was perceived as insufficient to fulfill the "responsibility of surplus countries." The Bank, like other policymakers, recognized the need for a more proactive

response. Specifically, the need was mainly import liberalization and capital export liberalization. In short, the need was “getting rid of restrictive regimes.” This was the core of the “responsibility of surplus countries” as of 1969. Even before the decision to tighten monetary policy, the BOJ was aware of such responsibility in the course of the OECD review of Japan. At that time, the reform of the international monetary system was still under discussion. During that time, the assumption was that the Bretton Woods system would be maintained. In official international discussions, exchange rate changes were not considered a priority issue.

As mentioned above, the content of the responsibilities of surplus countries at the end of the 1960s does not include a discussion of the need for exchange rate changes. It is also different from the “locomotive” view of the late 1970s, which was a macroeconomic policy issue with an eye on current account surpluses. However, it can be said that this reflects the awareness of the importance that policy makers at the time actually felt firsthand in situations such as the OECD’s review of Japan.

In this sense, the Bank’s perception of its policy response at this time was not necessarily out of step with the international trends.

The BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986) shows the subsequent developments following the period mainly discussed in this paper. According to the committee’s work, after the revaluation of the Deutsche mark in October 1969, there was a growing view overseas that the yen would be next, and the BOJ internally discussed the idea of a revaluation of the yen in February 1970, but it was feared that the shipbuilding industry would be severely affected. This committee remarks that “excessive anxiety about the yen revaluation” caused the delay in closing the foreign exchange market at the time of the Nixon Shock and the subsequent problem of massive intervention.¹⁵⁴ Including such issues, it will be a future task to examine how the BOJ and others have changed their perceptions of the appropriate way to deal with surpluses and how this has affected their actual policies.

¹⁵⁴ BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986), pp. 298, 303, 308, and 327.

Appendix. BOJ's View of the Drivers of Price Increases

The MOF (1991), introduced in this paper, states, “When the main cause of price increases is inflation abroad, there is a great danger that a tightening of the domestic economy will lead to a widening of the balance of payments imbalance, even if it helps to suppress prices. In this case, the most direct policy instrument is the revaluation of the yen rate,” and it argues that the monetary tightening in September 1969, “of course, must have been based on a judgment that the problem of rising prices, which was the policy issue at that time, originated in domestic factors.” As a typical example of the “view that price inflation at that time originated mainly from the overheating of the domestic economy,” it cites the article “Issues regarding Recent Rise in Prices” published in *Chousa Geppo* (Monthly bulletin), November 1969 issue, which “seems to have been the official view of the BOJ at that time.” It says, the paper “emphasizes that price increases are caused by overheating of the domestic economy, which implicitly asserts that exchange rate evaluation is not an appropriate policy tool.”¹⁵⁵ In addition, the BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986),¹⁵⁶ in explaining the circumstances leading to the September 1969 tightening, stated, “The Bank believed that the main cause of the sharp rise in wholesale prices since spring was the tightening of domestic supply-demand conditions. A simple estimate made by the Economic Research Department at the time showed that foreign factors were much smaller than domestic factors.” The above-mentioned November 1969 paper is given as the source of the estimate.

Indeed, the paper clearly states that “the main cause of the recent surge in wholesale prices appears to be the domestic tight supply-demand balances for commodities” and that “overseas factors do not appear to be the main cause of the rise in wholesale prices.”¹⁵⁷

However, this paper was published in November of the same year, after the monetary tightening in September 1969. Moreover, as stated in the “Introduction” to the paper, it was written in response to “some criticism” of the “current tightening” (e.g., that tightening is not appropriate since the main causes of rising prices are overseas factors and structural factors).¹⁵⁸

To review the views before and after the Bank’s decision to tighten monetary policy (at the end of August), at the time of the decision, the Bank did not conduct a numerical

¹⁵⁵ MOF (1991), pp. 358 and 362-363 (written by Akiyoshi Horiuchi).

¹⁵⁶ BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986), p. 225.

¹⁵⁷ BOJ Economic Research Department, “Saikin ni okeru Bukka Jousho wo Meguru Shomondai (Issues regarding Recent Rise in Prices),” *Chousa Geppo* (Monthly bulletin), November 1969 issue, p. 1 (in Japanese).

¹⁵⁸ BOJ Economic Research Department, “Saikin ni okeru Bukka Jousho wo Meguru Shomondai (Issues regarding Recent Rise in Prices),” *Chousa Geppo* (Monthly bulletin), November 1969 issue, p. 2 (in Japanese).

analysis or provide an explicit explanation on the issue of whether price inflation originated from domestic or foreign factors, but rather seemed to clarify this point after the fact.

Specifically, it is as follows (see Chart 2 for price and interest rate trends at the time).

I. Recognition before the Decision to Tighten

Judging from the references to domestic supply-demand conditions, supply and demand in the labor market, and the tempo of wage increases, it seems that the Bank was strongly conscious of domestic factors while regarded overseas factors as additional. However, there is no explicit explanation or analysis of the numerical aspects to determine that domestic factors are the main cause of price increases. Specifically, they are as follows.

In the August issue “Kokunai Keizai Jousei (Monthly Economic Review)” (published on August 5, 1969),¹⁵⁹ the opening paragraph states, “Aggregate demand, primarily equipment investment and private consumption, has continued to expand at a fast rate. Industrial production has followed a sizable uptrend, while a steady demand has been continuously maintained. The commodity market has been generally bullish, and wholesale prices, aided by the gain in overseas prices, have risen notably since the beginning of spring. Consumer prices have recently advanced with a renewed strength partly because of unfavorable weather. The supply-demand balance of labor has become tighter, and wages have risen faster.”

As for prices, it is explained that, “Wholesale prices have risen at about an annual rate of 4 per cent since the spring of this year. This fast increase is because the domestic supply-demand relation of commodities has tended to be tight, following the fast expansion of aggregate demand, and because the prices of imported goods have been upward.”

In the “Business Conditions and Prices” section of the Bank’s internal “Reference Materials for Monthly Report” (August 5, 1969),¹⁶⁰ it is stated that “For some items, in addition to domestic [tight] supply-demand conditions, the continued tightening of overseas supply-demand conditions has been a major factor in the strength of the market. For example, exports of excess copper have been a factor in the rebound of the copper market, and strong exports of steel sheets to non-U.S. regions have been a factor supporting the market.”

¹⁵⁹ BOJ Economic Research Department, “Kokunai Keizai Jousei (Monthly Economic Review),” *Chousa Geppo* (Monthly bulletin), August 1969 issue, pp. 22-23 (in Japanese; We also referred to the English translation by the BOJ at the time).

¹⁶⁰ “Getsurei Houkoku Sankou Shiryou (Reference Materials for Monthly Report), August 5, 1969,” BOJ Archives, “Monthly Report 2/2 (12-year transfer),” No. 11091, p. 26.

II. Recognition at the Time When the Decision to Tighten was Made

Although the Policy Board Chairman's statement at the time of the decision to tighten the monetary policy¹⁶¹ seems to have been strongly conscious of the rapid expansion of the domestic economy, there is no explicit explanation of whether domestic factors are the main cause of the price increase or not. Specifically it says, "In reviewing the recent economic conditions, it is to be noted that while the nation's balance of payments has been continuously favorable, some disquieting phenomena, such as the continuous rise in prices and sharp increase in loans by financial institutions, have appeared in the wake of a fast expansion of domestic economic activity, and the overseas economic situation requires a careful watch. We have, accordingly, concluded that it would be appropriate to take action, in advance, to prevent the possible overheating of business activities in order to assure a long-enduring, stable growth of the economy." In addition, in the letter to general managers of branches sent by the head of the Coordination and Planning Department and the "Assumed Questions and Answers" attached to the letter, there was no particular internal preparation for questions such as "Isn't the main cause of the price increase overseas?"¹⁶²

It should be noted that the phrase "the overseas economic situation requires a careful watch" in the above-mentioned Chairman's statement does not refer to concerns that rising prices overseas would spread to Japan, but rather to concerns about the slowdown of the global economy and the deterioration of the export environment (see section VII.A of the main text).

III. Perceptions Immediately after the Implementation of the Tightening Measures

A. Newspaper Reports

Among the newspaper reports immediately after the implementation of the tightening policy, there was an article pointing out that Deputy Governor Sasaki was concerned about the view that "overseas factors are the main cause."¹⁶³ According to the same article, Deputy Governor Sasaki said, "If wholesale prices do not fall easily in the future, we need to analyze the causes of the rise in wholesale prices again. The BOJ's analysis so far has shown that strong domestic demand is the main factor, but I'm wondering what will happen if overseas factors are the main factor this time" on September 1 (although it is

¹⁶¹ BOJ Committee for Compiling the One Hundred Year History of the BOJ (1986), pp. 229-230 (We also referred to the English translation by the BOJ at the time).

¹⁶² "Shitenchou ate Soumu Buchou Shishin (Letter from the Head of the Coordination and Planning Department to General Managers of Branches), September 1, 1969," BOJ Archives, "Letter from the Head of the Coordination and Planning Department, 1969," No. 10033.

¹⁶³ Mainichi, September 2: "Houdentou: 'Kin'yu Seisaku wa Muzukashii' Sasaki Fukusousai ('Monetary Policy is Difficult...' Deputy Governor Sasaki)."

unclear at what occasion he said this).

B. “Kokunai Keizai Jousei (Monthly Economic Review)”

In the September issue (published on September 5, 1969) of the “Kokunai Keizai Jousei (Monthly Economic Review),”¹⁶⁴ it can be read that domestic factors are the main reason for the strong performance of the commodity markets, but as this is a normal monthly publication, there is no numerical analysis of the factors.

In the same document, the opening paragraph states, “Sustained by private equipment investments and personal spending, aggregate demand has continued to expand, and shipments have increased at a notably high rate. In this situation, although industrial production has increased substantially, the supply-demand balance of goods has become increasingly tight in many industrial lines. The commodity market has stiffened and wholesale prices have continued to rise notably. Against the background of this situation, . . . strong moves among enterprises to increase their existing equipment investment programs have appeared. Consumer prices have persistently risen. The supply-demand balance of labor has become tighter and wages have risen sizably. The rate of increase of the bank note issue has become sharper.”

The document states the following. The underlying trend of the commodity market “has become steadier” and, “This steadiness in the market condition was influenced by such factors as a natural decrease in production during summer (steel products) and a rise in overseas quotations (non-ferrous metals), but basically responsible for it was the fact that the supply-demand relation of commodities has become tighter against the background of a remarkable growth in the total domestic demand.” Wholesale prices “continued to rise” and, “Classified by items, the prices of steel products, non-ferrous metals, and lumber advanced continuously, influencing the recent general price rise. In addition, the prices of machinery, chemicals, and synthetic fiber, which had heretofore fallen, began to rise because of the stringency of their supply-demand balance. The gains in the prices of these commodities have combined to push up the price level on the whole.” Also, “[according to the Bank’s Short-Term Economic Surveys], the percentage of businesses, which felt an excess demand over the supply of products, has increased among many industries, such as” As for consumer prices in Tokyo, “Excluding seasonal commodities, consumer prices continued to advance in August by 0.3 per cent, following a 0.4 per cent rise in July, due to increases in clothing and housing. When compared with a year ago, they maintained a persistently strong rise of 5.6 per cent.”

¹⁶⁴ BOJ Economic Research Department, “Kokunai Keizai Jousei (Monthly Economic Review),” *Chousa Geppo* (Monthly bulletin), September 1969 issue, pp. 12-13 (in Japanese; We also referred to the English translation by the BOJ at the time).

C. Documents That Clearly State That Domestic Factors Are the Main Cause and the Figures That Show This.

In the internal paperwork for the overseas business trip dated September 12 (referred to as “WP III materials” in the table of contents, which appears to be a preparatory paperwork for the OECD Third Working Party),¹⁶⁵ the “Purpose and Background of the Current Tightening” first mentions “the continued rise in wholesale prices” and then goes on to explicitly state that “although there are effects of high prices overseas (both in terms of exports and imports), it is mainly due to the tightening of domestic supply and demand.” At the bottom of this statement is a table listing month-on-month changes in wholesale prices from February to August 1969, which shows that the total average month-on-month change during the same period was 2.0% and the total average excluding imports was 1.9%. This table seems to have been created in order to show numerically that the contribution of imports to price inflation (overseas factors) is small, but a note is attached to the count of “total average excluding imports” as “only for internal use.”¹⁶⁶

IV. Supplementary Information on the View of the EPA

The MOF (1991),¹⁶⁷ cited at the beginning of Appendix, argues that the EPA’s Economic White Paper, 1970, “is emphasizing overseas factors as the main cause of price increases,” because the White Paper states, “partly owing to the inflationary expansion of overseas economies, export demand pressure has become stronger and costs of imported raw materials have risen in Japan. These developments constituted an important factor for Japan’s price rises.”¹⁶⁸

However, in the “Commentary” attached to the Japanese translation by the EPA (published in December 1969)¹⁶⁹ of the OECD Annual Review Report to Japan, it is stated that “the OECD authorities seem to consider that the recent rise in wholesale prices is largely due to overseas factors, but it should also be emphasized that, even if import-related goods are excluded, prices are still strong, reflecting the strong domestic demands.” In other words, the EPA had not always emphasized overseas factors.

¹⁶⁵ “Konji Kin’yu Hikishime Sochi ni tsuite (The Current Monetary Tightening Measures), September 12, 1969,” BOJ Archives, “Overseas Business Trip Materials, 1967-1970 (materials for WP3 and BIS monthly meetings),” No. 51275.

¹⁶⁶ It should be noted that in the aforementioned “Saikin ni okeru Bukka Jousho wo Meguru Shomondai (Issues regarding Recent Rise in Prices),” *Chousa Geppo* (Monthly bulletin), November 1969 issue (in Japanese), p. 3, it is clearly stated and announced that the contribution of imports to the increase in wholesale prices from March to September was “extremely small at 6.3 percent.”

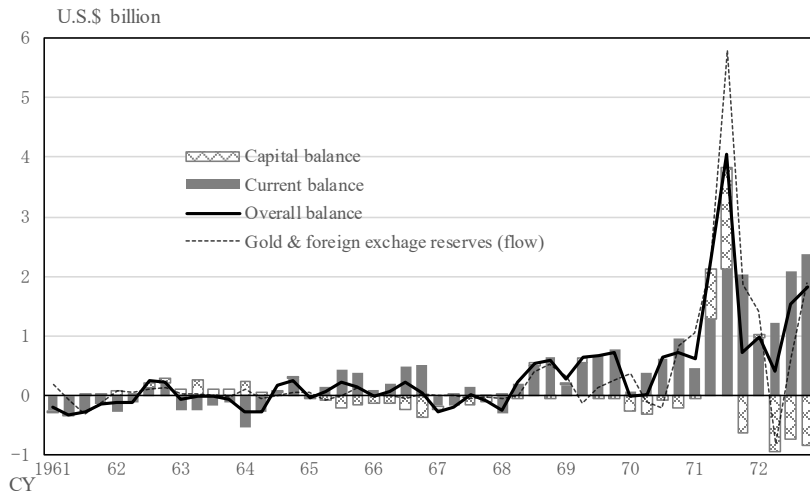
¹⁶⁷ MOF (1991), pp. 358 and 363 (written by Akiyoshi Horiuchi).

¹⁶⁸ EPA (1970), p. 49 (p. 40 in the English translation).

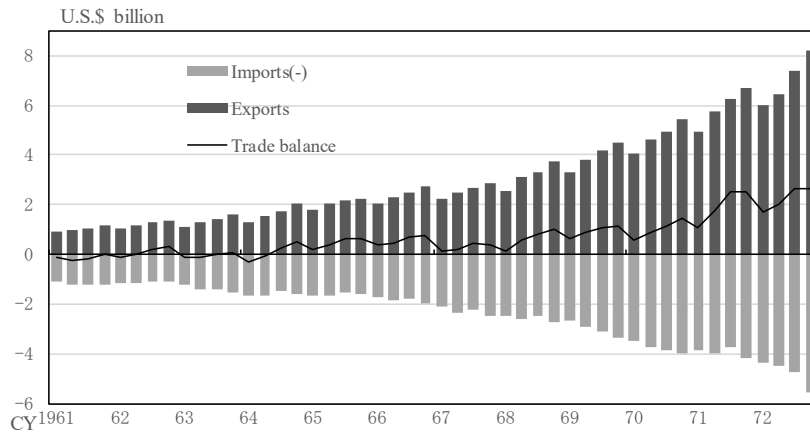
¹⁶⁹ OECD/EPA translation (1969), p. 24. The name of the author of the “Commentary” section is not given.

Chart 1 Balance of Payments

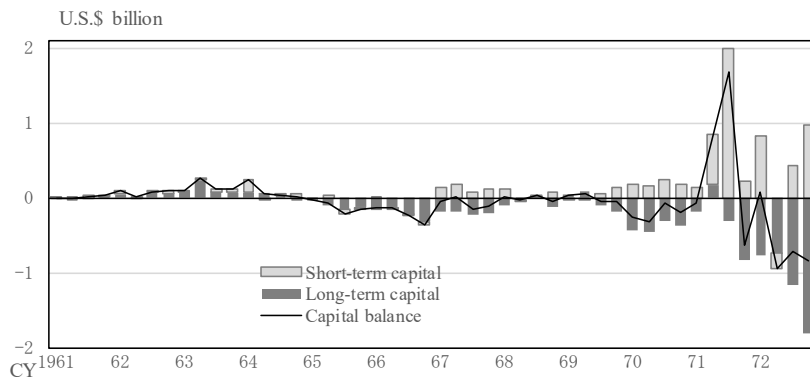
(1) Overall Balance



(2) Trade Balance



(3) Capital Balance



Sources: For figures between 1961 and 1966, Statistics Dept., The Bank of Japan, *Economic Statistics of Japan (1966)*.

For figures between 1967 and 1972, Statistics Dept., The Bank of Japan, *Economic Statistics Annual, each issue*.

Chart 2 Prices and Interest Rates

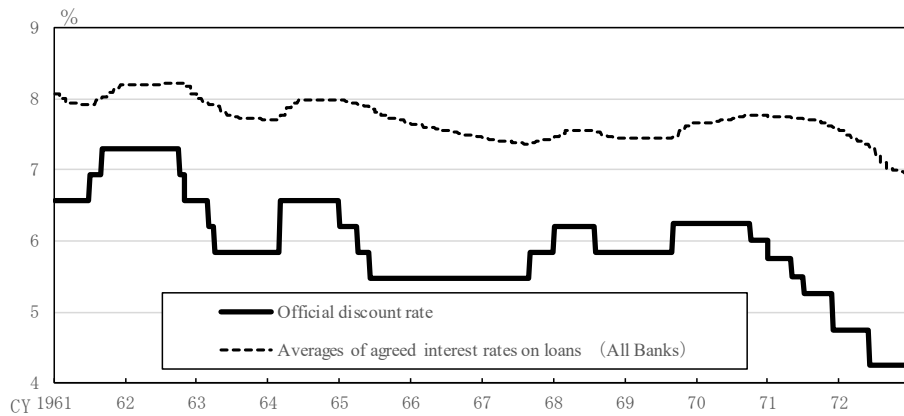
(1) Prices



Note : For wholesale price index, export price index, import price index, 1995=100.
For consumer price index, 2015=100.

Sources : The Bank of Japan, *BOJ Time-Series Data Search*
Statistics Bureau, Ministry of Internal Affairs and Communications, Japan,
2019 Annual Report on the Consumer Price Index

(2) Interest rates



Sources : [Official discount rate]
The Bank of Japan, BOJ Time-Series Data Search

[Averages of agreed interest rates on loans]
For figures between 1961 and 1966, Statistics Dept., The Bank of Japan,
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