

U. S.-JAPAN ECONOMIC  
RELATIONS AND FUTURE PROSPECTS

Remarks by Robert P. Mayo, President  
Federal Reserve Bank of Chicago  
before the Third Joint meeting of the Chicago  
Association of Commerce and Industry and  
the Osaka Chamber of Commerce and Industry  
Chicago, November 8, 1973

It is, almost to the day, one year since I had the honor and pleasure to participate in the Joint meeting of the Chicago Association of Commerce and Industry and the Osaka Chamber of Commerce and Industry in Japan, and to share with the participants some of my thoughts on the close and friendly economic ties between our countries that have evolved over the years and the problems faced by our two great nations.

Today, as we meet again, this time in my home city, I cannot help but be deeply impressed by the dynamism that has characterized the course of events during the past year. Last year, one of the speakers at our meeting characterized the situation faced by our two countries as "the most critical juncture in our economic and political relations since World War II." This was not an exaggeration. The cumulative thrust of adverse developments in U. S. international accounts had placed great strains on our relationship. We were about to record the largest trade deficit this country had experienced in its history. Protectionist sentiment in the United States aroused by this development was rising rapidly, threatening not only to arrest, but even to reverse, the carefully constructed movement toward free exchange of goods and services that so many of us believed to be essential in the quest of the peoples of the world for a better tomorrow. Elimination of that payments deficit had become one of the top priorities of the U. S.

public policy.

Imbalance in our trade with Japan figured prominently in our overall adverse position. Indeed, almost two-thirds of our 1972 trade deficit could be traced to the imbalance in our trade with Japan. Elimination of that imbalance was the focal point of the overall effort to improve our balance of payments. This was the challenge posed to the Japanese and to American businessmen and governments who were genuinely interested in maintaining the momentum of increasingly close cooperation.

Today, one year later, we meet here in a substantially changed environment. Figures released by the U. S. Department of Commerce just a few days ago show that the United States has recorded a surplus--a modest one but a surplus nevertheless--in its foreign trade during the first nine months of this year; confidence is growing that we shall record a surplus for the year as a whole. The generally improved trade prospects in turn, have had salutary effect on the foreign exchange markets, leading to the substantial strengthening of the dollar. As this renewal of strength continues--and we have no reason to expect that it will not--the chances for an early resolution of problems still confronting the Group of Twenty, in its effort to restructure the international monetary system so as it may better serve the welfare of all trading nations, have been greatly enhanced.

There were, to be sure, many factors that contributed to this improvement. But the contribution made by the Japanese government and business certainly stand out. The revaluation of the yen, voluntary curtailment of certain exports, increased emphasis on the import--

all these stand out as significant monuments to mutually beneficial cooperation in solving mutual problems. The figures speak for themselves. While last year our trade deficit with Japan amounted to over \$2.7 billion during the first eight months, during the same period this year the deficit was cut to less than half, to about \$1.2 billion. Most significantly, the improvement in our mutual trade balance occurred not as a result of cut-backs in trade, but rather, as a result of acceleration in trade, with our exports to Japan rising more rapidly (at a phenomenal 70 percent in January-August over the same period in 1972) than our imports from Japan (that still rose at a highly respectable rate of almost 11 percent).

Even more impressive gains were scored in our "Basic Balance" with Japan which includes all current and long-term capital transactions. While in the first six months of last year we recorded a deficit on this basis with Japan of more than \$2.5 billion, in the same period this year we actually recorded a surplus of \$220 million. It was this swing that significantly contributed to the overall improvement in our basic balance where the deficit was cut to less than one-third in the first half of 1973 from what it was in the comparable period in 1972.

These developments were clearly beneficial for both our countries. For Japan, this swing in foreign accounts with the United States has meant that some of the sterile reserves you were accumulating over the past several years were being turned into goods and services for your people so that they could benefit directly as consumers from their thrift and productivity that made Japan over the past quarter century such a great economic power--second only to the United States in the free world.

For the United States, the general improvement in our trade account has been of great significance, particularly in our role of traditional world leadership toward freer trade. The threat of protectionism has largely disappeared as our trade improved; indeed chances are very good that the Congress will enact the enabling legislation to launch the United States toward another round of worldwide negotiations for further liberalization of world trade--the round that was formally initiated at the GATT meetings in Tokyo last month.

And so, in contrast with the rather gloomy background of our last meeting, today we can see brighter days ahead of us. If, indeed, last year we were at a "critical juncture" in our relationship, it appears that we chose the right road. And to the extent that the forum of the Chicago Association of Commerce and Industry and the Osaka Chamber of Commerce and Industry meetings, and frank exchanges of views for which it served, have contributed, however modestly, to this achievement, I think we all can be proud of our contribution.

But the road, clearly, does not end here. Indeed, now that the initial constructive steps are bearing fruits, new challenges and opportunities are becoming apparent along that road. It is an exciting road, one that holds great promises for all of us as citizens, consumers and businessmen. But it is also a road that will require continued effort from all of us to respond with vigor to these challenges, to continue to build upon the initial successes.

In the past year, we have opened a little wider the gates to mutually beneficial trade. Our peoples have and will continue to benefit from the better interrelationship of prices achieved through the realignment of the yen/dollar exchange values; they will also

benefit from freer trade, through freer access to markets. Our first task now is to assure that we don't lose the momentum that will help us to dismantle the still-existing barriers. We still have a long way to go--on both sides, to be sure. True, the Nixon Round of negotiations under the auspices of the General Agreement on Tariff and Trade just getting under way holds great promise, particularly in the area of non-tariff barriers. But in the final analysis, it will be the business leaders that will influence the outcome and implement the results. This, then, is one area where close cooperation and consultation can be very constructive. Also, we must guard against erosion of positive results already attained in the area of trade liberalization.

Trade, however free of restrictions it may be, is only one avenue through which benefits of productivity, inventiveness and of wealth and uniqueness of resources can be transmitted among nations. Nor is it, at times, the most efficient avenue, particularly in today's world of modern production methods where technology and managerial techniques can be transmitted more profitably and efficiently than the final products of these processes. The tremendous growth of multinational corporations and of foreign direct investment in general over the past decade is, I think, a living testament to the fundamental truth of this proposition. And it is in this area in particular that a broadly-based relationship between our two countries has been lacking. For example, at the end of 1972 the U. S. direct investment in Japan amounted to only \$2.2 billion--little over 2 percent of the total U. S. foreign investment--an amount equal to about 13 percent of the total two-way trade between the two countries. This contrasts sharply with the U. S. position vis-a-vis other industrial countries, for example, the European Economic Community. The book value of the U. S. direct investment in that area in 1972 (still

excluding U. K. and Denmark, who joined in 1973) amounted to almost 17 percent of total U. S. direct investment outstanding--an amount equal to about 89 percent of the two-way trade between the EEC and the U. S.

These figures speak for themselves. They reflect a disproportionately low participation by U. S. business in the Japanese economy--to the detriment, I believe, of both countries.

And even more distressing statistics exist on direct investment by Japan in the United States. The book value of that investment amounted to only \$229 million in 1970--only about one-eighth of the value of our investment in Japan. And in 1971 and 1972, the value of Japanese direct investment in the United States became actually negative as the Japanese trading companies' receivables from their parents rose sharply, apparently in anticipation of the appreciation of the yen. In contrast, the EEC's direct participation in the U. S. production processes at the end of 1972 amounted to almost \$4 billion, with Germany alone accounting for over \$800 million, and France for more than \$300 million.

In the area of portfolio investment--the holding of corporate stocks and bonds--Japanese involvement in the U. S. economy has been equally small. At the end of 1972, Japanese investment amounted to just over \$300 million, less than 1 percent of the total foreign investment in the United States.

These figures, perhaps more than anything else, underscore the "length of the road" that we still have to go to build, in a meaningful way, on the close economic ties that have been developing between our two countries; they focus on the vast area of still unexplored opportunities for businessmen on both sides of the Pacific.

In the area of U. S. investment in Japan, I earnestly hope that the recent moves toward liberalization of past restrictions will continue, and above all, that those liberalization measures already put on the books don't become engulfed in bureaucratic red tape.

In the area of Japanese direct investment in the United States, our door has been, and remains, wide open. All it takes is the initiative and the foresight of enlightened Japanese businessmen to take advantage of the opportunities that exist--opportunities that have been so much enhanced by the recent realignments of the yen/dollar exchange rate. And let me assure you, there is but a trace of regional provincialism when I say that no other area in the United States offers greater opportunities than the Midwest--the industrial and agricultural center of our nation. The availability of skilled labor, raw materials, transportation facilities as well as financial facilities is unequalled any place in this country--perhaps in the world--a fact that I believe needs no detailed elaboration to this audience.

We have already had some auspicious beginnings in this area. The \$6 million investment by Kikkoman Shoyu Ltd., in our neighboring Wisconsin to produce soy and teriyaki sauce, and the very recent announcement by Yamaha of plans to invest in production facilities for musical instruments in Grand Rapids and South Haven, Michigan are good examples.

In the financial area, it is not without significance that half of the foreign-affiliated banking institutions in Chicago so far operating are Japanese. The recently-enacted foreign bank branching law in our state of Illinois will facilitate better reciprocity in banking between Japan and Chicago, I am sure. Also, the recent opening in Chicago of a subsidiary of the oldest and largest Japanese securities firm, the Yamaichi, bodes well for future trade in securities between our

two countries.

All these are clearly only beginnings--first steps on that exciting road that lies ahead. Let us hope that the continued strengthening of our mutual ties, strengthening that is epitomized by the events of this week--and indeed by this very meeting--will provide a solid base for meaningful economic relationships for the benefit of the peoples of both our great nations.