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JAPAN

THE PROBLEM

To estimate the political, economic, and foreign policy prospects for Japan over the next two or three years.

CONCLUSIONS

A. Prime Minister Sato's position is probably secure for the period of this estimate. It is unlikely that his conservative majority will shrink significantly in the next lower house elections, which will probably be held in 1966. The major threat to his position is the current business slowdown, but we believe that his administration's fiscal measures and the basic strengths of the economy will prevent further deterioration and permit a modest recovery within a year or so. (*Paras. 4-18*)

B. Another major problem for Sato is his identification with generally unpopular US policies in Vietnam. If extremists who now lead the opposition Socialist Party succeed in exploiting the issue to mount mass demonstrations on the scale of those in 1960, Sato might be forced to resign in favor of another, less identifiably pro-US conservative leader. On balance, however, we believe that the leftists will not succeed in removing Sato with these tactics under foreseeable circumstances. (*Paras. 4-11*)

C. Economic conflicts between Japan and the US will remain, but none has so far caused or is likely to cause any serious or lasting damage to a generally friendly relationship, or jeopardize the political stability of the Sato administration. The main problems in Japanese relations with the US will continue to be those of Communist China, Vietnam, and Okinawa. Japanese trade with Peking will continue to increase, though at a less spectacular rate than in recent months. In 1966, Sato will probably extend credit guarantees to cover exports to Com-

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munist China. He will seek to avoid diplomatic recognition of Peking as long as possible; but if Peking gained significant further international recognition, he would probably follow suit, hoping that any impairment of Japan's relationship with Taiwan would be temporary. (Paras. 19-34, 42-51)

D. Japan will continue to rely on the Security Treaty with the US for military protection. While some qualitative improvement is in prospect, there is little chance that Sato will press for any major increases in Japan's own defense forces over the next two or three years. He will remain sensitive to public concerns on Vietnam and will continue to oppose the use of Okinawan bases for direct bombing attacks, particularly on North Vietnam. We foresee a growth of Japanese nationalism and self-assurance, which will be reflected in a somewhat more independent policy toward the US on these and other issues, and in a more active political role in general in East Asia. (Paras. 35-41, 52)

E. Nonetheless, Japan's initiatives in foreign affairs are apt to be cautious and pragmatic, designed to further its efforts to expand trade in as many directions as possible. Willingness to support plans for development of Southeast Asia will be similarly conditioned; Japan is not prepared to accept US direction on its economic assistance role in the area. (Paras. 24-26)

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DISCUSSION

I. INTRODUCTION

1. Japan's phenomenal economic growth has thrust it into the ranks of the world's leading industrial and trading nations, and enabled the Japanese people to achieve living standards closely approaching those of Western Europe. Economic success has been accompanied by a remarkable degree of political stability. Yet 20 years after World War II, Japan still does not exert an influence in East Asia commensurate with its assets.

2. There are important reasons for Japanese temporizing on major foreign policy issues. The government has pursued a pragmatic foreign policy, consciously executed to further Japanese commercial interests by taking as few actions as possible that would create enemies in any quarter. At home, despite substantial parliamentary majorities, the ruling conservatives have chosen to operate in accordance with the Japanese tradition of basing decisions wherever possible on a broad popular consensus. Socialists have consistently been ideologically opposed to the US alliance. Of equal importance has been the extraordinarily slow postwar revival of militant nationalism; and there has been widespread opposition to the development of powerful military forces. Finally, Japanese leaders themselves have been ambivalent about what the nation's international role ought to be. On one hand, they are generally sympathetic to US containment of Communist China and reluctant to dilute US efforts in this direction. On the other, they want to assert independence of the US and to restore Japan's Asian identity by improving contacts with neighboring Asian states, both Communist and non-Communist.

3. There are many signs that Japan is moving toward the assumption of somewhat greater international responsibilities: the forthcoming treaty with South Korea and the substantial Japanese economic aid which accompanies it; an aid agreement with Taiwan; favorable responses to certain other Asian developmental needs; attempts to mediate the conflict between Indonesia and Malaysia; participation in several Afro-Asian conferences; and an effort to gain a seat on the UN Security Council. Apart from the Korean treaty, these are all issues where Japan can afford to take initiatives without affecting the basic direction of its foreign policy or arousing serious political opposition at home. Remaining largely unresolved are the critical long-range issues of Japanese foreign policy: relations with Communist China; the future of Okinawa; and the mission of the nation's armed forces. Over the next decade, the Japanese leadership will have to face up to these issues, but in the next two or three years, unless Japan encounters depression or war, it is likely that most of these decisions will again be postponed.

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II. POLITICAL

4. *The Liberal-Democratic Party.* For almost 20 years, conservatives have held between 55 and 65 percent of the seats in the all-powerful lower house of the Japanese Diet; the ruling Liberal-Democratic Party (LDP) now holds 61 percent¹ and seems in no danger of losing its commanding position over the next two or three years.² In November 1964, Eisaku Sato succeeded the ailing Hayato Ikeda as president of the LDP and prime minister of Japan. Though Sato's accession to power was contested within the party through most of 1964, his leadership is now reasonably secure. Serious competition has been virtually eliminated by the deaths over the past year or two of three other party leaders: Ichiro Kono, Bamboku Ono, and Ikeda himself. Other rivals, such as Takeo Miki, the Minister of International Trade and Industry, would require several years to cement a following strong enough to challenge Sato.

TABLE 1

Elections to the House of Representatives (Lower House) of the Japanese Diet, November 1960 and November 1963

PARTY	SEATS		PERCENT OF POPULAR VOTE	
	1960	1963	1960	1963
Liberal-Democratic	296	283	57.5	55.1
Socialist	145	144	27.5	29.0
Democratic Socialist	17	23	8.7	7.3
Communist	3	5	2.9	3.9
Independent and Other	6	12	3.4	4.7
	<u>467</u>	<u>467</u>	<u>100.0</u>	<u>100.0</u>

5. Various developments of the past year have put the party on the defensive and made Sato somewhat more cautious in pressing his programs than was expected when he took office. The Japanese public is generally apprehensive that US actions in Vietnam, particularly the bombings of the North, will lead to the military involvement of Communist China and, ultimately, of Japan. Sato endorses the general line of US policy on Vietnam (though with reservations), and is exposed to heavy domestic pressure on this account. Another major LDP problem is the state of the economy, marked by stagnating production and a wave of bankruptcies, primarily among small businesses. Finally, a succession of political scandals in the LDP, though not involving top party figures, added to Sato's problems. The losses in popular esteem have been reflected to some extent in a lackluster LDP showing in the House of Councillors (upper house) election in July 1965.

6. *The Socialists.* The core of Sato's political opposition is the Socialist Party (JSP) which holds only about one-half the number of seats in the lower house held by the LDP (and about the same proportion in the upper house). The

¹ See Table 1.

² The next lower house election must be held by November 1967; it will probably be held during 1966.

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more moderate Democratic Socialist Party (DSP), which broke off from the JSP in 1959, has had difficulty maintaining its strength and is not now a serious competitor. However, the DSP does provide a political home for significant categories of workers and intellectuals who occasionally support the government, thereby contributing to the "consensus" sought by the LDP on certain major legislation. Behind the JSP stands SOHYO, Japan's major trade union confederation with 4.2 million members. SOHYO provides most of the JSP's funds and street demonstrators, and about one-half of its members and one-third of its Diet representatives.

7. A four-year trend toward moderation in JSP policies was reversed in late 1964 when the leadership of the party was captured by radical elements. Their control was confirmed in May 1965 with the election of Kozo Sasaki as party chairman. Sasaki's leadership is not a reflection of some sudden mass swing to the left of the party rank-and-file, but rather the result of poor convention tactics and overconfidence on the part of his moderate opponents. To some extent, Sasaki was aided by prevailing frustrations over the party's continuing inability to seriously threaten the overwhelming LDP parliamentary majority in a prosperous Japan.

8. Since taking over, Sasaki has attempted to turn the political clock back to the turbulent years 1959-1960; he has resurrected the party's anti-US policy, strengthened ties with Peking, advocated non-cooperation in legislative affairs, and worked to revive JSP cooperation with the Communist Party (JCP) in anti-government activities. He views united front tactics with the well organized Communists as the key to the success in the streets with which he hopes to embarrass the Sato government and attract added popular support.

9. The Sasaki group has seized upon the Vietnam issue as the vehicle to bring the JSP out of the political wilderness. For example, the JSP claims that the South Korean treaty, now in the last stage of ratification, is designed to link Japan more closely with US security arrangements in the Far East. The JSP also injects Vietnam into parliamentary discussions on Okinawa and on US bases in Japan proper. In exploiting the Vietnam issue, the JSP seeks also to lay the groundwork for a campaign to terminate the US-Japanese Security Treaty in 1970, when it first becomes open for suggested revision. Moderate JSP leaders, including many in SOHYO, are opposed to Sasaki's parliamentary obstructionism and, particularly, his new emphasis on a united front with the Communists. The moderates, however, are in political disarray and will probably be unable to do more than slow Sasaki's pace, at least so long as the war in Vietnam remains a major popular concern in Japan.

10. It is unlikely that Sasaki will succeed in his efforts to repeat the JSP's success of 1960 in creating chaos in the streets of Tokyo and forcing the resignation of an LDP prime minister. Sato has already showed signs of greater dexterity than his brother Nobusuke Kishi in handling such tactics; policing of demonstrations has been vastly improved and parliamentary traditions are being

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better observed to avoid provoking public opposition. While not so popular as former Prime Minister Ikeda, Sato has not attracted anything like the hostility that accrued to Kishi and contributed to his downfall. Sato's adroit handling of the issues of Vietnam and Okinawa thus far indicates that he possesses sufficient political sensitivity to weather foreseeable criticism on other foreign policy matters. In any event, the Japanese press and public seem to have matured somewhat since 1960 and apparently want to avoid repeating the excesses of that year. Another favorable element is the absence of zeal for disruptive tactics on the part of the DSP and other minor parties, and among JSP moderates as well. We cannot exclude the possibility that some development in the Vietnamese war—e.g., significant escalation, particularly greatly increased US use of Japanese bases for support or of Okinawan bases for direct air attacks—would create enough public apprehension to support a massive campaign against Sato.

11. *The Communists.* The JCP maintains an uncompromisingly militant line and closely supports Peking in its attitudes toward both the US and the USSR. The party's Chinese bias became more pronounced in 1964 with the expulsion of several ranking members who had Soviet sympathies, including two Diet members who voted in favor of Japanese ratification of the limited nuclear test ban treaty. Communist electoral strength has grown steadily since 1958, due mainly to support from former JSP extremists. Nevertheless, the JCP polled only about seven percent of the vote in the most recent nationwide elections, those of July 1965 for the upper house. In the next lower house election, the Communists could probably not secure more than an additional three to five percent of the vote and this much only if there are wholesale defections from the JSP. The importance of the JCP in Japanese politics, however, rests partly upon its ability to muster agitators and street demonstrators in the major cities and principally upon its function as a transmission belt for ideas, and probably material assistance, from Peking to the radical wing of the JSP.

12. *Soka Gakkai and the Rightists.* The militant Buddhist organization, Soka Gakkai, operating through its political arm, Komeito (Clean Politics Party), is now an important force in Japanese politics. Komeito is the third largest party in the upper house and holds the balance of power between the dominant JSP and the LDP in the Tokyo Metropolitan Assembly. In the next lower house election, the first it will enter, Komeito will probably elect about one-half of the 35 to 40 candidates it is expected to field.

13. Komeito's political platform reflects opportunism more than ideology; the party seems more intent on identifying itself with popular sentiments than on pressing the government to any particular line of action. Despite a vague commitment to socialism on behalf of the rootless and impoverished classes which it represents, Komeito has much better working relations with the LDP than with the JSP and JCP with which it competes for adherents. [redacted]

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Gakkai's phenomenal growth rate of the 1950s has apparently slackened in recent years. Hence, barring a major deterioration in the domestic economy, Komeito is unlikely to grow much beyond its current strength. In seeking to develop and expand its strength in the lower house, Komeito would also be hampered by the operations of a constituency system less advantageous than that under which it has made steady gains in upper house elections. At best, Komeito can hope to gain sufficient Diet seats to give it some bargaining power with LDP legislative leaders.

14. Rightwing extremists in Japan are divided, their numbers are small, and there is widespread public opposition to the violent tactics which they advocate. They could probably gain substantial support from conservative quarters only if the JSP came to power.

III. ECONOMIC**A. The Domestic Economy**

15. The Japanese economy has been growing at a phenomenal rate; the growth of GNP averaged 10 percent annually from 1955 to 1964, reaching almost 14 percent in 1964. In the past year or so, however, there has been a marked slowdown in economic growth and the GNP will probably show an increase of only about 4 percent for 1965. The current situation is characterized by the levelling off of industrial production, decline in new orders, excessive inventories, and reluctance among businessmen to make new investments. There have also been serious difficulties in the stock market and among securities companies, an unusually high rate of bankruptcies in small and medium-sized firms, and a sharp profit squeeze for many large corporations caught between declining sales revenues and heavy burdens of debt service. Indeed, most of the recent business failures have resulted from overextended credit positions, a prominent characteristic of Japan's postwar business enterprises whose financing has come largely from banks rather than internal sources of funds.

16. The current slowdown was preceded by an overly rapid expansion of credit during 1963, which spurred the economy into overextension of capacity and producers' inventories, an upsurge in imports, and a consequent balance of payments crisis. In early 1964, the application of the traditional remedy of credit restraints slowed the rate of increase of imports and helped ease the balance of payments problem. However, the reversion to easy money later in the year failed to bring about anticipated increases in industrial investment and production, largely because of earlier satisfaction of the demand for consumer durables and the drag of large producers' inventories of finished goods. A further loosening of credit restrictions in early 1965 did not relieve a growing "recession mood" among Japanese businessmen.

17. The failure to overcome the slowdown through relaxation of credit restrictions has led the Sato government to explore fiscal techniques new to postwar Japan. In order to stimulate the economy, the government plans

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bond issues to finance an anticipated budget deficit; this marks a departure from the postwar policy of balancing the current account of the budget from year to year. The only significant action so far has been an increase of about \$550 million in its loan and investment program which will work its way into the economy in early 1966. The government is also contemplating more investment in long neglected "social overhead"—housing, transportation, water supply, and sanitation. In order to cope with the current economic slowdown and to avoid wide cyclical swings in the economy, Sato is stressing the achievement of a "stable" growth rate rather than a return to the rapid growth and periodic overheating of the economy characteristic of the Ikeda period. His course is favored by a growing recognition among Japanese businessmen that the extremely rapid growth rates of the past decade could not have been maintained indefinitely.

18. By careful manipulation of fiscal measures and business stimulants available to him, Sato will probably manage to prevent any significant worsening of the economic situation. Indeed, there will probably be a modest upturn during 1966 in view of the fact that, despite the slowdown, exports have maintained record levels and unemployment has remained very low. Resolution of such basic problems of the overstretched economy as heavy debt burdens and high interest rates will require additional years of governmental effort. In any event, Japan's economy will continue to be extraordinarily vulnerable to fluctuations in both domestic and foreign demand. Over the next year or two, however, economic problems are unlikely to put Sato's position in serious jeopardy, much less shake the LDP grip on the government.

B. Foreign Economic Relations

19. Japan's foreign trade now totals about \$16 billion annually and is crucial to the economy. Japan's natural resources are severely limited and its industry survives and expands largely by processing foreign raw materials. However, the record of the past decade indicates that Japan can pay for overseas commodities through the export of a wide variety of manufactured goods while steadily improving living standards. A record surplus was achieved in Japan's merchandise trade balance in the first nine months of 1965 and further growth is likely over the next year or so. On the other hand, Japan continues to suffer from a steadily growing deficit in invisible balance of payments items—freight and port expenditures,³ insurance, and credit costs—and, except during the last few months, this has resulted in substantial deficits in the current account of the balance of payments. The Japanese remain generally apprehensive about their balance of payments and view any threat to export growth with alarm.

³ Although Japan led the world in the tonnage of ships launched from 1956 through 1964, Japanese ships currently carry less than one-half the annual volume of the nation's exports. This apparent paradox results from the devastation of Japanese shipping during World War II, the rapid growth of trade since the war, and, particularly, the fact that 63 percent of the tonnage launched in 1956-1964 was sold to foreign shipowners.

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20. *The US.* The US is Japan's leading trading partner by a substantial margin; bilateral trade has reached a level of almost \$4 billion a year and the US customarily takes 25 to 30 percent of Japan's total exports. Because of this heavy dependence on US markets, the Japanese are acutely sensitive to fluctuations in the US economy and react sharply to every manifestation of protectionist sentiment in the US. To anticipate and avoid the development of such sentiment, Japanese businessmen have been persuaded to accept "voluntary" restrictions on certain exports, particularly textiles, and in the case of cotton textiles these have been formalized in bilateral agreements for periodic fixing of quotas for Japanese products destined for the US market. While the steady overall growth of exports to the US has helped minimize complaints from Tokyo, these arrangements have caused resentment among Japanese businessmen.

21. The US also plays an important role in the Japanese economy as a provider of both long-term and short-term capital. Long-term capital inflow from the US has been concentrated on issues of bonds and debentures as a result of the unreceptive Japanese attitude toward foreign equity investment. A US "Interest Equalization Tax" enacted in 1964 and applicable to foreign securities and commercial bank loans of over one year has contributed to a decline in the availability of such funds for Japan. The impact of the tax was softened by the granting in 1965 of a \$100 million annual exemption for US purchases of securities issued or guaranteed by the Japanese Government. Even though the full exemption is unlikely to be used in 1965, the Sato administration remains concerned over the continuing decline in US long-term bank loans and the possibility of further US governmental limitations on bank lending abroad.

22. Other persistent economic problems between Japan and the US concern civil air routes and fishing rights. Japan seeks the right to fly passenger aircraft from the west coast of the US to New York and beyond so as to compete in round-the-world service. The Japanese argue that the existing bilateral civil air agreement is unfair since it was concluded more than a decade ago when Japanese negotiating power was weak. The same argument is made in regard to the Convention which restricts Japanese salmon fishing in the northern Pacific. While prospects are good for a resolution of the civil air dispute, the fishing issue will almost certainly continue to be a source of friction.

23. Thus far, economic problems between Japan and the US have not caused serious or lasting damage to a generally friendly relationship nor jeopardized the political position of the Sato administration. US economic leverage provides a potent restraint against excessive Japanese stubbornness, but commercial irritants of various sorts are bound to arise from time to time, and Sato will probably become somewhat harder to deal with as part of the overall Japanese tendency toward greater independence in foreign affairs. Japan's importance as a market for US exports and as a logistical base gives Japan substantial leverage of its own.

24. *Southeast Asia.* Japan's emergence as a prosperous industrial nation has brought pressure from the US for more liberal economic assistance to less de-

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veloped countries. Japan has moved very cautiously in assuming such responsibility, even in Southeast Asia where it is second only to the US in total trade. Reparations and other war-related payments have so far been the major form of Japan's aid in this region. Its \$1.3 billion program is about half completed, with payments to South Vietnam, Thailand, Laos, and Cambodia almost entirely disbursed, and the much larger commitments to Indonesia, the Philippines, and Burma almost half fulfilled; claims for reparations by Malaysia and Singapore remain unsettled. Apart from reparations, Japan has extended relatively little grant aid to the countries of Southeast Asia. Long-term and other credits, though substantial, have been almost entirely on commercial terms. Direct private investment in Southeast Asia is also substantial and accounts for about 20 percent of all Japanese investments overseas. It is particularly important in Indonesia, where Japan has contracted for projects valued at almost \$100 million under "production-sharing" agreements which, coupled with its reparations, have reinforced its very strong trading position.

25. There is likely to be some increase in Japanese aid to Southeast Asia, but any rapid expansion is unlikely. In July 1965, Japan pledged itself to increase its total annual foreign assistance by about 1970 to one percent of national income, or about double the level of Japanese aid committed in 1964. There is, however, no firm timetable or evidence of concrete planning to reach such a goal. This same cautious approach to foreign aid is evident in the cool Japanese reaction to an April 1965 proposal to set up a multilateral program of economic assistance to Southeast Asia in which the US contribution would be as much as \$1 billion. The Japanese view the program as part of the overall US strategy for Vietnam and are reluctant to become involved in it. Yet they have shown great interest in UN ECAFE plans for an Asian Development Bank, whose headquarters they hope to have located in Tokyo, and have indicated willingness to subscribe \$200 million in capital to ensure a major voice in its management. One of the most imaginative Japanese proposals for multilateral aid has been to establish an Asian agricultural development fund to which they would contribute capital and technical assistance. The Japanese probably intend to push this proposal at a conference on Southeast Asian regional economic cooperation which they are sponsoring in early 1966.

26. Japan is not prepared to accept US direction on its economic assistance role in Southeast Asia. An important motive for Sato's current interest in various types of aid activity there is probably a reluctance to see the US completely outdistance the Japanese in a region which they regard as their rightful sphere of economic influence. Sato will almost certainly continue to view Japan's role in Southeast Asia in this light, expanding aid efforts only slowly and in response to clearly defined commercial interests.

27. *The Communist States.* Japan's trade with the Communist states has grown steadily, and since 1960 at a rate higher than that for total Japanese trade.⁴ Though trade with Communist countries still accounts for only about

⁴ See Table 2.

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six percent of Japan's total trade, this performance has stimulated the imagination of Japanese businessmen, many of whom see these countries—particularly Communist China—as a vast untapped market for their manufactures. The Sato administration, like those of Kishi and Ikeda, is experiencing heavy domestic business pressures to encourage expansion of trade with Communist countries beyond the total of \$1 billion expected in 1965.

28. Pressures on Sato from outside the government are supplemented by pressures from within the LDP and the Cabinet. China trade policy is the nearest thing to a divisive issue within the administration and Trade Minister Miki is one of the many LDP proponents of the liberalization of government-backed export credits for Communist countries, a measure that would greatly

TABLE 2

Japanese Trade with Communist Countries (including Cuba), 1960-1965
(in \$US millions)

	COMMUNIST			TOTAL
	USSR	CHINA	OTHER	
1960	147	24	51	222
1961	210	48	98	356
1962	296	84	105	485
1963	320	137	95	552
1964	409	311	198	918
1965 (estimated)	400	450	not available	

assist the growth of Japanese trade with Peking. Sato is also confronted with countervailing diplomatic and economic pressures from the US and other valuable trading partners—Nationalist China, South Korea, and to a minor extent, South Vietnam.

29. Japanese trade with Communist China has increased very rapidly since conclusion in late 1962 of the Liao-Takasaki agreement—a quasi-official trade arrangement nominally made under private Japanese auspices. It is expected to top \$450 million in 1965, exceeding Japanese-Soviet trade for the first time since 1959 and permitting Japan to replace the USSR as Peking's leading trading partner. Barring some unforeseen political decision on the part of Peking, trade will almost certainly continue to grow, though not at the explosive rate of recent years. Its potential is limited by pressures from the US and Nationalist China, and, more important, by the narrow range of Chinese exports acceptable to Japanese firms and Peking's relatively modest purchasing power. The Japanese are also wary, for political reasons, of becoming overly dependent on the Chinese mainland for markets or raw materials. On the whole, therefore, it is unlikely that trade with Communist China, now between two and three percent of Japan's total, will approach five percent within the next two or three years.

30. To compensate for the limitations on Communist China's purchasing power, Peking and the various Japanese proponents of increased bilateral trade will press Sato to remove the ban on government backing of credits for five

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years or more for purchases of capital equipment by Peking. Thus far, the Japanese Government has participated in only one such credit: in August 1963, a five-year, \$20 million credit for a synthetic fiber plant. This action brought strong reprisals from Nationalist China and led to Sato's refusal in early 1965 to provide similar backing for another synthetic fiber plant and a freighter. Japanese concerns quickly offered to provide private credit arrangements to salvage both deals, but Peking cancelled both orders as a means of objecting to Sato and his policy of "separation of politics and economics" (i.e., expanding trade without necessarily accepting closer political relations). Despite this and similar frictions, the two countries continue to exchange numerous business and technical missions, and maintain semi-official trade liaison offices in each other's capital. Trading continues, though in recent months an increasing proportion is being conducted by Peking through so-called "friendly" Japanese firms rather than through the closely supervised Liao-Takasaki channels.

31. Sato is unlikely to be able to hold the present tight line on government-backed credits beyond 1966. Modifications could result from domestic pressures, especially from the larger concerns which would benefit most from sales of capital goods. Indeed, Sato himself, though strongly committed to a tough posture vis-a-vis Peking, may not be inclined to wait until aggressive Western European traders move *en masse* into what he and other Japanese consider Japan's natural market. Sato is cognizant of Taipei's sensitivities on the credit issue and he expected that the \$150 million credit granted to Nationalist China in April 1965 would help mute the latter's protests. He has also conducted an intensive diplomatic campaign to assure Taipei of his political sympathies, meanwhile preparing it for a break in the credit dike. Taipei reaction would also be tempered by its extremely heavy dependence on Japanese markets for its subtropical agriculture produce, but we cannot exclude the possibility of response by the Chinese Nationalists that would break existing economic and even political ties.

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32. A similar but far less critical problem arises in the case of the two Koreas. Japan has few dealings of any sort with North Korea and trade is small and unimportant. Japan is unlikely to jeopardize its much firmer prospects in South Korea by significantly increasing its economic stake in the North in the near future. South Korea is a major trading partner with which Japan consistently runs a large and profitable export balance. With the ratification of the long awaited normalization agreement between the two countries, the way will be open for an \$800 million program of Japanese economic assistance, including \$300 million in grant aid. This will almost certainly lead to Japan's replacing the US as South Korea's principal trading partner and regaining at least a modest degree of political influence in Seoul.

33. Trade with the USSR presents even fewer problems for the Japanese. Although Japan adheres to Free World restrictions on the sale of strategic goods and on the extension of long-term credits, it is one of the USSR's leading non-Communist trading partners; trade for 1965 is expected to be almost the same

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as 1964, approximately \$400 million. Officially backed credit assistance to the USSR will continue to be a problem for the Sato administration. Japan has generally held to a five-year limit with the Soviets, but exceptions have been made and at least one eight-year credit has been granted; the Soviets are now pushing for credits up to ten years. Prospects are good for expansion of trade and other economic relations with the USSR, particularly with respect to fisheries, civil air, and consular matters, but dramatic increases are unlikely unless Japan chooses to enter a credit race with Western European nations or the US lowers the bars on sales of strategic goods to the USSR. In either event, Japan would vigorously compete for Soviet business.

34. Japanese trade with North Vietnam has averaged only \$15 million annually in recent years and any significant expansion is unlikely even under peaceful conditions. Because of objections of the seamen's unions, Japanese shippers have withdrawn their vessels from the North Vietnam trade, but ships of other countries are filling the gap.

IV. MILITARY

35. Sato assumed office with a reputation of being more "defense-minded" than his predecessors. He was believed to favor such measures as elevation of the Defense Agency to a ministry, a substantial increase in defense spending, acceleration in the pace of Japan's peaceful rocket and nuclear programs, and amendment of the "no war" clause in the Constitution. Other than minor increases in the military budget, however, the government has undertaken little action in this field. It probably considers that the strong residual anti-militarism of postwar Japan, augmented currently by fears of possible involvement in the conflict in Vietnam, make increased defense measures politically unwise if not at present unattainable. Also, the lack of a widely recognized and pressing threat makes this government as prone as its predecessors to find refuge under the protective umbrella of the Security Treaty, and to defer increased defense outlays in favor of more popular projects. Current plans approved by Sato call for only modest improvements in the Japanese defense structure over the next two or three years. Within its limited defense budget, however, Japan is responding to the phasing out of US military aid by expanding the domestic production and design of military equipment, including various short-range missiles, and these programs are likely to continue and expand.

36. Popular resistance to a military buildup reflects not only a revulsion from the disasters of World War II but almost equally the absence of a sense of danger. Most Japanese still cannot take seriously the thought of China as a direct threat, although this attitude will probably be modified when Peking approaches the achievement of a credible operational nuclear capability. And, although the Japanese have great respect for the power of the USSR and a historic mistrust of its intentions, the relatively peaceful attitude of Moscow toward Tokyo over the past decade has largely subdued fears of attack from this quarter. This vagueness in defining a military threat has been at the root of Japan's failure

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to establish guidelines necessary to detailed defense planning. In any case, there is a strong tendency to feel that the security treaty with the US provides ample insurance against both Peking and Moscow.

37. The US bases in Japan proper and Okinawa which give meaning to the security treaty also represent a danger to Japan in the minds of some Japanese. They reason that whereas no nation is likely to attack Japan for its own sake, US bases in Japan would make it a prime target if the US were to get into a war with the Communist powers. This fear, continually exploited by the Japanese left, is a major factor in Japanese popular opposition to US policy in Vietnam. Sato has a more sophisticated view of US purposes in Vietnam and quietly supports American policy there. Though Okinawa is not subject to the limitations of the Security Pact, use of its bases for direct bombing attacks on targets in South Vietnam, if publicized, would probably arouse the Japanese public and would cause Sato to protest as he did in July 1965. Similar attacks from Okinawa on North Vietnam would draw a much more adverse Japanese response. On the other hand, Sato is not likely to object to the continued shipment of US troops and materiel to Vietnam via bases in Japan so long as such movements are handled with minimum publicity and create no newsworthy incidents. Japan will continue to oppose the import of US nuclear weapons into the country whether for local storage or for transshipment.

38. The Japanese Government will almost certainly continue to rely upon the US for military protection under the terms of the Security Treaty through 1970 when negotiation for revision becomes possible. The Japanese leaders prefer this arrangement to undertaking the responsibility and expense of establishing and maintaining a Japanese force capable of meeting conventional or deterring nuclear attack. Nevertheless, over the next five years, Sato and his LDP successors will maneuver to gain a stronger voice for Japan in any revision of security arrangements with the US, particularly with respect to US bases in Japan. To this end, they will probably effect certain qualitative improvements in Japan's air and naval arms and engage in some concrete planning for the assumption of a greater share of the defense burden.

39. In striving for a less dependent defense posture, Japanese conservative leaders will at least consider the development of nuclear weapons, though in view of the continuing strong public aversion to the idea, the government is unlikely to press for their development. Indeed, barring a major change in the international situation—e.g., Japanese loss of confidence in the security relationship with the US; blatant Chinese Communist aggression in Korea or Taiwan; or wholesale proliferation of nuclear weapons throughout the world—we believe it unlikely that any Japanese premier in the next four or five years would accept the political risks of openly advocating the production of nuclear armaments.

40. In the unlikely event that Japan decided to become a nuclear power, it is technologically and economically capable of becoming a formidable one. On the basis of its highly advanced nuclear development for peaceful purposes

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and by initiating construction of an indigenous plutonium production reactor facility in 1966, Japan could test its first nuclear device by about 1971 without violating existing safeguard provisions. Thereafter, it could produce an estimated 10 to 30 weapons annually if unsafeguarded uranium were available. By violating safeguards, Japan could advance its initial test of a nuclear device to 1968, but this is unlikely to occur. The test would not lead to any immediately significant production of nuclear weapons; on the contrary, it would jeopardize future shipments of fuels and the acquisition of the technical assistance for further advances in the nuclear field.

41. The Japanese space research program provides an adequate base for the development of missile systems for the delivery of nuclear warheads. During the next few months, Japan will probably try to orbit a small earth satellite and chances of success are good. By applying its rocket technology to the development of an MRBM/IRBM system, Japan could attain an operational capability with such a system early enough to meet the availability of nuclear warheads. We estimate that by 1975 Japan could produce a force of as many as 100 launchers for such missiles together with the necessary nuclear warheads for an incremental cost of about \$1 to 2 billion; annual expenditures would not exceed 0.5 percent of Japan's GNP.

V. FOREIGN POLICY

42. Although Japanese foreign policy has not yet developed a clear sense of mission, certain general lines of action have emerged in recent years. There is a wide consensus that continuation of the close military and economic relationship with the US is the bedrock guarantee of Japanese well-being. At the same time, there is movement toward closer political relationships with the Asian Communist states because they are potentially valuable trading partners but, more important, because they are neighbors with whom normal and peaceful relations must inevitably be established. On the positive side, there is a desire to become politically influential once more in the affairs of those territories lying between the great mainland powers and Japan itself—North and South Korea and Taiwan. Coupled with this is a desire to regain those nearby Japanese islands lost to the Allies in World War II—the Ryukyus (Okinawa), Bonins, and southern Kurils. Beyond the Korea-Japan-Taiwan triangle, Japan's few foreign policy initiatives have been focused on increasing economic ties with Southeast Asia which Japanese continue to view as an important source of industrial raw materials and potentially a great market; in any case, a region where Japanese economic interests have much room for expansion. Japan has done little thus far to indicate any conception of its broader, world role.

43. *Communist China.* Despite differences of emphasis among Japan's conservative leaders, there is general agreement on the desirability of containing Chinese Communist influence in East Asia and providing a Japanese alternative to the region's smaller nations, including Mongolia and North Korea as well as non-Communist nations. Most conservatives are also determined to resist Pe-

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king's efforts to use its expanding trade with Japan as a political weapon. To this end Sato maintains his China policy of "separating politics and economics." When embarrassed by reference to their increasing contacts with Peking, the Japanese rationalize these activities as "building bridges" between China and the West in order to diminish Peking's dangerous isolation from the world.

44. Were it not for sustained US and Nationalist Chinese pressures, Japan would be even further along the path to diplomatic recognition of Peking. The majority of informed Japanese probably feel that it is necessary and most others would not oppose it. Since France granted recognition in 1964, Japanese leaders have been concerned that they might fall behind other Western countries in this regard, thereby incurring domestic complaints and Peking's permanent displeasure. At the UN, Japan has been watchful and nervous on matters pertaining to the admission of Peking; and Japan would probably vote affirmatively if it became apparent that Peking had acquired clearcut majority support. It would prefer to see a "Two Chinas" solution that would permit Taipei to retain its Assembly seat and the other prerogatives of an independent state.

45. Sato will probably be able to cope with domestic pressures for recognition of Peking over the next year or two, as he has in the past, by cautious expansion of economic, cultural, and quasi-official relations. In the event that domestic pressures become unmanageable as a result, for example, of some general international breakthrough on the issue, Sato would probably move to offer diplomatic recognition.

46. Sato's reluctance to recognize Peking is based primarily on concern over US reactions and the fate of Taiwan. Sato is among the many Japanese who are apparently convinced of Taiwan's strategic importance to the defense of Japan and of its situation well within Tokyo's potential sphere of economic and political influence. Nevertheless, he could not afford to maintain an unyielding attitude indefinitely toward Peking's overtures for recognition even if this required, as seems likely, termination of diplomatic relations with Taipei. Though reluctant to abandon their foothold on Taiwan, Sato and the Japanese would probably conclude that with continued US support, Taiwan would not in any case fall into Peking's hands.

47. *The USSR.* A breakthrough on the question of a World War II peace treaty with the USSR is unlikely so long as the USSR continues to refuse to return to Japan the small islands northeast of Hokkaido which Tokyo claims. Neither side, however, appears particularly disturbed by the failure to make a formal peace 20 years after the war; this certainly has been no major obstacle to the expansion of diplomatic and economic relationships over the years. Sato will maintain the firm political posture that he has demonstrated vis-a-vis the Soviets in the face of their frequent protests over the presence of US bases in Japan. Thus far, Japanese responses to these protests have not affected economic relations. Both sides desire to expand their trade and there is much interest in Japanese participation in the development of eastern Siberia. The

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Soviets and the Japanese have a common interest in containing Communist China, and this congruence is likely to find expression in efforts on both sides to intensify their present friendly relations.

48. *Korea.* Sato's attention is presently focused on ratification of an agreement which would normalize political relations between Japan and South Korea. Despite JSP and JCP opposition in the streets and in the Diet, the government will ratify the treaty in December 1965; failure on this issue would have been a severe blow to Sato's prestige. The leftist opposition seems unable to rouse widespread adverse public feeling on the Korea issue. Nor have they succeeded in linking it in the public mind with the vastly more exploitable issue of Vietnam. After ratification and implementation of economic provisions of the agreement, Japanese influence in South Korea is certain to grow despite Korean efforts to keep it in bounds. Until the South Korean enterprise is launched successfully, Japan may feel inhibited from improving its presently meager trade and cultural relations with North Korea.

49. *Okinawa.* There is no easy solution to the problem of Okinawa for the Sato government. It must demonstrate a continued interest in the reversion of the Ryukyu Islands to Japanese administration, a course desired by almost all Japanese of whatever political stripe. At the same time, the government recognizes that the US base structure in Okinawa contributes directly to the security of Japan to an extent that would not be possible were it to come under Tokyo's administration. Faced with the need to maintain some momentum on this issue, Sato will probably concentrate on achieving the maximum possible Japanese economic and political involvement in Okinawan affairs. Though he would probably not want to force a showdown on Okinawa at any time, it is apparent that the island will remain a major irritant in Japanese-US relations. Sato's position would be made much more difficult if there were further dramatic reminders of Okinawa's role in the Vietnamese war.

50. *Vietnam and the US.* Failure to offer more than grudging endorsement of US actions in Vietnam probably reflects Japan's uncertainty as to the chances of US success as well as fears of its own involvement. There is also relatively little concern, even among Japanese conservatives, over the impact of a possible Communist victory in Vietnam on Thailand, Malaysia, and other Southeast Asian states. If US efforts showed signs of reaching a successful conclusion, however, the Japanese Government would probably swing to firmer support of its programs. If the US were patently unsuccessful, Sato would maneuver carefully to dissociate himself and avoid the inevitable political fallout at home. If he did not, he might be forced to resign in favor of another conservative, less identifiable as a defender of US policy in Asia.

51. There is probably little that Sato can do on the diplomatic front at this time beyond occasional cautionary reminders to the US to avoid deeper involvement of Japanese or Okinawan bases in the Vietnamese war. Caught between domestic pressures and the imperatives of Japanese national security, he will

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probably continue to attempt to satisfy both. His consequent ambivalence on Vietnam is likely to be a continuing source of irritation in relations with the US.

52. In addition to Communist China, Okinawa, and Vietnam, there will be other hindrances to fuller Japanese cooperation with the US as Japanese nationalism and self-assurance grow. Inevitably, Japan will develop policy positions on the basis of its own expanding political and economic goals in East Asia, its bargaining power will improve, and conflicts with the US will increasingly require mutual concessions. In short, Japan's position and policies toward the US will come to resemble those of West Germany or other European allies.

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9 October 1963

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NUMBER 41-63

Japan's Problems and Prospects

Submitted by the
DIRECTOR OF CENTRAL INTELLIGENCE
Concurred in by the
UNITED STATES INTELLIGENCE BOARD
As indicated overleaf
9 OCTOBER 1963

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JAPAN'S PROBLEMS AND PROSPECTS

CONCLUSIONS

A. Japan's postwar political institutions, although not yet put to the test of adversity, seem to be taking root, and the outlook for continued political stability appears favorable. Although the leftist political vote has been increasing, to the particular benefit of the Japanese Socialist Party, the conservative Liberal-Democratic Party will probably retain power over the next few years. (*Paras. 5, 7-9*)

B. Japan's economy continues to grow vigorously. It is, however, heavily dependent on foreign trade and is exceptionally vulnerable to threats to its export markets. A substantial expansion of foreign trade will be necessary if it is to meet its 10-year plan goals. Barring a worldwide depression, Japan's foreign trade outlook is favorable. The economy will almost certainly continue to expand, but probably not at the remarkable rate of recent years. (*Paras. 16, 33*)

C. Japan can be expected to move toward a greater involvement in world affairs and a more self-confident and independent posture during the next few years. Relations with the US will be marked by greater insistence on Japan's being consulted as a full partner on matters of concern to it and by great sensitivity to discrimination against it in US markets. In the absence of a material change in circumstances, there is little prospect of a major alteration in Japan's economic or political relations with Communist countries during the next few years. (*Paras. 27, 28, 34-36, 40, 41*)

D. The US-Japan Security Treaty will almost certainly remain the keystone of Japan's defense and military planning under conservative rule. US bases in Japan will be a sensitive subject and the Japanese would be particularly edgy about their use in con-

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nection with hostilities which Japan did not see as an immediate threat to itself. As economic prosperity increases and national self-esteem reasserts itself, Japan may show a greater interest in such issues as national defense and a more impressive military establishment. Strong antimilitary sentiment will, however, continue to prevail among the Japanese for some time to come, and it appears unlikely that professional military opinions will exert a significant influence on governmental policies for many years. (*Paras. 38, 45, 49*)

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I. INTRODUCTION

1. The postwar period has seen profound changes in Japan's political institutions. A number of elements in the prewar scene—the military, the aristocracy, and the special bureaucracy surrounding the Emperor—have been all but eliminated as political forces. The entire legal and institutional framework of government has been fundamentally reorganized and liberalized; the role of political parties has been expanded, and the position of the opposition protected and strengthened; new elements have access to power; labor unions have emerged as a major force; civil rights have been extended; and the size of the electorate has quadrupled.

2. Economic and social transformation have also brought about basic changes in political life. Traditionally, such divisions between left and right as existed in Japanese politics have been rooted firmly in class and functional distinctions; Japan now appears to be approaching a stage in which such distinctions are becoming much less meaningful. There has been a rapid movement of the conservative rural population to urban areas. Industrialization continues to spread into rural areas, breaking down former social, economic, and political identifications. In both city and countryside, there has been a replacement of older, conservative voters by an anti-traditional postwar generation as it came of age. Moreover, in the postwar period, not only the youth, but all elements of Japanese society have been exposed to the teachings and writings of a predominantly leftist intellectual community which was released from past suppression under a tolerant Occupation.

3. These changes have been conducive to the development of leftist political forces. Nevertheless, the left has found it difficult to exploit its opportunities. Prosperity under capitalism, high employment, a better distribution of income, and the growth of confidence in the future have lessened the appeal of the leftist shibboleths of "exploitation" and "oppression" and have, to some extent, satisfied rising expectations. Japan is also currently experiencing a gradual recovery of a sense of national self-esteem which renders it increasingly advantageous for all elements to think in terms of national rather than class goals.

4. In recent years, some reaction to postwar political reforms has occurred: political figures purged during the Occupation are reappearing; the police system is being recentralized on the prewar pattern; there is also a trend toward the national control of education, and a steady diminution of local autonomy. Such revisionist trends as exist, however, seem limited in scope and do not appear to pose any immediate threat to basic advances made to date. A major control over the tempo

and nature of such trends will be the growing dependence of the political leadership on the mass support of an electorate which is slowly but steadily becoming more willing and able to use its ballots and influence in support of other than traditional candidates and programs.

5. Thus, the prospects for continued moderation in Japan's political institutions and policies seem reasonably good. There appears to be little chance that basic postwar reforms will be abrogated. It should be noted, however, that these institutions have developed in a period in which Japan has not had to face political or economic crises of sufficient magnitude as to put them to the test. While we believe that these political institutions are taking root, it does not necessarily follow that their evolution will insure continued compatibility between Western and Japanese interests, or that other factors, primarily economic, could not at some time bring about a radical change in Japan's current Western orientation.

II. POLITICAL PROSPECTS*

6. *Liberal-Democratic Party.* The ruling Liberal-Democratic Party (LDP) carries with it the prestige of success and the advantages of money and power. The LDP, however, is increasingly aware that it cannot rest on its oars. Many of its leaders realize that it must strive to replace the widely held view that the LDP is a party of "old-guard" politicians, steeped in corruption, enervated by factionalism, and responsive to the wishes of big business. These leaders recognize that the LDP must make the transition from a party based primarily on class to one based on broad popular appeal and gain the support of the growing body of independent voters who support whatever party offers the most attractive programs and candidates.

7. The LDP has proven adept at exploiting favorable economic and social conditions in postwar Japan and will probably continue to do so for some time. The party appears to understand what steps it must take to improve its political prospects and, despite continued factionalism, is making some modest progress. The international status of Japan has improved to the point where a judicious amount of nationalism can be made to work for the conservatives, as Prime Minister Ikeda is seeking to do with his theme of Japan as the "third pillar"—along with the US and West Europe—of the Free World. On balance, we believe the LDP will probably be able to maintain itself in power for the rest of this decade.

8. *Japanese Socialist Party.* The Japanese Socialist Party (JSP) will almost certainly continue to be the only major opposition party during this decade. It is supported by Sohyo, the principal trade union federa-

* See Table I for relative electoral strengths of Japanese political parties.

tion, with a membership of some 4 million. There has been a long-term increase in the leftwing vote in Japan, with the JSP as the principal beneficiary. If this trend continues at the present rate, the JSP will present a serious challenge to conservative rule by the end of the decade. However, the JSP may find it difficult to continue to advance at recent rates unless it overcomes certain obstacles to achieving a broad appeal to the whole nation. Many Japanese fear that the JSP would follow radical economic policies which might jeopardize continued economic growth and prosperity. The party will have to attune its presently neutralist foreign policy to the main trends of Japanese nationalism and political life: its anticolonialist theme irritates more than it inspires the Japanese, since it equates Japan with the backward nations of Asia and Africa; and its "American imperialism" theme no longer serves as a convincing explanation for all the world's ills.

9. There has been within the JSP in recent years a demand for "structural reform," in effect a movement away from rigid doctrinaire emphasis on class warfare, and there has been some movement along these lines. The degree to which the Socialists will have moderated by the end of the decade cannot be estimated precisely. Long-term forces undoubtedly favor moderation, and some perceptible changes in JSP orientation are likely to occur over the next several years. However, the Socialists as a party have a capacity to cling tenaciously to anachronistic doctrines, and temporary returns to more radical positions cannot be ruled out. Thus far, there is little sign the JSP is undergoing the same process of moderation which has characterized many Western socialist parties.

10. *Democratic Socialist Party.* The Democratic Socialist Party (DSP) was formed by moderate elements of the JSP which splintered off in 1960. It has the support of the relatively small labor federation Domei Kaigi with some 1 million members. The DSP has experienced a steady decline in popular support and parliamentary influence. Many supporters are returning to the JSP with its superior organization and resources. The DSP may at best have a role as a partner in some coalition.

11. *Japanese Communist Party.* Over the next few years, the Japanese Communist Party (JCP) will probably continue to attract attention disproportionate to its size. When it seems politically profitable, it will act with other leftist groupings in demonstrations, directed primarily against US bases and the introduction of nuclear weapons in Japan and for closer relations with the Communist states. Its proven ability to get out the crowds for demonstrations will encourage the other leftist parties, particularly the JSP, to seek its support and to act in concert with it where popular protest seems advantageous. Given a continuation of the present economic prosperity and moderate political

atmosphere, it seems unlikely that there will be any significant increase in popular support for the JCP or in its parliamentary strength. Its increasing association with Peiping's militant line in the Sino-Soviet split will probably further aggravate internal party dissension and could lead to another defection of party members similar to that in mid-1961 when an important JCP official, Kasuga Shojiro, and a few followers broke away from the JCP and formed the "revisionist" Socialist Reform Movement. Open espousal of the Communist Chinese side would further isolate the JCP from the other leftist forces which, in the main, are unsympathetic to Chinese attitudes on such issues as nuclear testing and coexistence.

12. *Soka Gakkai*. Efforts of both the JCP and the socialist parties to increase their shares of the popular vote will probably be undercut by the Soka Gakkai (Value Creation Society) which is drawing members from the same low-income milieu from which the extreme leftists have traditionally drawn their strength. This partly religious, partly political movement has achieved a considerable measure of influence since 1959, and now has probably several million followers. Its avowed objective is the elimination of corruption through the establishment of its militant Buddhist creed as the state religion, and it pursues this goal by aggressive proselytizing at home and abroad and, to an increasing degree, by political activity. Dissatisfaction with present conditions, personal frustrations, and poverty have played a large part in its growth, but many have joined because they see in the propagation of its creed the salvation of the nation at a time when they believe Japan to be riddled with political corruption and engulfed by alien influences. In spite of its predominantly lower class following, the organization's nationalism and traditionalism leads to some affinity with the LDP.

13. The Soka Gakkai may eventually decline to the status of relative unimportance that has been the fate of numerous postwar quasi-religious movements in Japan. However, its strong and efficient organization, militant recruitment tactics, continued exploitation of antiwar sentiment, opposition to political corruption, and the championing of popular causes point to a probable increase in its growth and political representation over the next few years. Its leaders are young and dynamic, but do not as yet appear to be power-hungry or self-seeking. For the short run, the Soka Gakkai does not appear to pose any major political problem for conservative rule. As yet, its elected representatives have demonstrated neither great political responsibility nor initiative. Greater legislative strength, however, could lead them to develop a more comprehensive political action program. If this should occur, the Soka Gakkai's authoritarian methods and organization, and its nationalistic doctrines, would probably cause it to move to the right; its political philosophy could evolve into a uniquely Japanese form of totalitarianism, which

might eventually pose serious problems for moderate conservative forces in Japan.

14. *Right Extremists.* The number of right extremists is small and they are divided into several hundred groups. There is widespread opposition to the tactics of assassination and terror which some pursue and they are viewed with distrust by the government. They will continue to be a disruptive element on the political scene. However, barring an unlikely coalescence of their forces, they will almost certainly not have a significant influence in government, military, or business circles over the next few years.

iii. ECONOMIC PROSPECTS

15. Since the end of World War II, Japan has enjoyed a higher rate of economic growth than any country of the industrial West; between 1958 and 1961, it exceeded that of any other country in the world.* A number of factors have contributed to these successes. Postwar governments have followed policies which have favored economic development and stability and have taken prompt remedial action to offset periodic downturns in the economy. There has been a high rate of domestic savings and investment. The Japanese still work hard and adapt quickly to scientific and technological advances. US aid and offshore procurement were important boosts to the economy, particularly in the 1950's. Many of these factors will continue to operate and will assist in maintaining the current prosperity.

16. Japan is, however, deficient in nearly all the basic natural resources needed to keep the economy running. Thus, the critical element in Japan's economic viability will continue to be its ability to achieve a volume of export trade adequate to pay for vital and increasing imports of sources of energy, raw materials, and food.

17. Japan's consumption of energy will probably nearly double in the next 10 years. Most of the useable hydroelectric power sources have been developed; Japanese coal, though plentiful, is generally not of high grade and production costs are high. Oil deposits are small, scattered, and difficult to exploit, and Japan will have to continue to import well over 90 percent of its crude oil. The development of the Japanese oil concessions in the Persian Gulf will eventually reduce the foreign exchange costs of oil. The cost of developing these concessions and required royalty payments are now, however, resulting in a net drain on Japanese foreign exchange resources. Japan is pushing ahead in the development of nuclear power as an energy source, but the effort has been hampered to some extent by a lack of funds for both basic and applied scientific research. By 1970, Japan plans to have five nuclear

* See Table II for statistics on Japan's economic growth.

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power stations in operation. Nuclear power, however, will probably account for less than two percent of Japan's primary energy output by 1973.

18. Japan will also remain short of many important industrial raw materials. It imports the bulk of its requirements of iron ore and coking coal. Deposits of nonferrous minerals, with the possible exception of zinc, are insufficient to meet needs. All aluminum ore is imported, and minerals to support the chemical industry are generally inadequate. Japan must turn to outside sources for all its cotton and most of its wool, and faces critical shortages in timber for construction and industrial purposes.

19. Through a highly successful program of intensive cultivation, multiple cropping, and extensive use of chemical fertilizers, Japan has made impressive gains in agricultural output, but it still must import about one-fifth of its requirements of foodstuffs. A uniquely effective birth control program has reduced the annual rate of population growth to about one percent, but the slowly expanding population and higher consumption standard will keep Japan a major food importer.

20. Labor problems will add to Japan's difficulties as the economy continues to expand. The ratio of qualified job-seekers to available jobs has been declining in recent years, and the chief labor difficulty in the near future will be to train enough workers in the proper skills to meet rapidly changing needs. At the same time, rapid modernization and rationalization in industry will create troublesome pockets of unemployment, especially in the coal mining and other older industries.

21. Shortage of skilled workers and pressure from trade unions for parity with West European wage levels will probably continue to force wages up, as has been the case since the end of World War II. Thus far, however, rising labor costs have not impaired Japan's competitive position in world markets, since industries producing for export have generally been able to keep increases in productivity ahead of increases in costs. Consumer prices are also on the rise, in part because of increased support prices for rice and in part because productivity in some industries producing consumer goods primarily for domestic consumption and in the distribution system has not kept pace with rising wage costs. The government has not as yet acted to check these inflationary trends and may be forced to unpopular measures in order to do so.

22. Facts no longer support the popular view of Japan as a low-wage country whose exports have an unfair advantage in other markets. There has been a definite shift in Japan's exports away from labor-intensive towards capital-intensive goods, and Japan's current export industries consist mostly of large firms whose average wage levels are relatively high. The role of traditional Japanese export industries such as textiles, toys, and ceramics in Japan's overall foreign trade is declining and low-wage areas such as Communist China, India, Hong Kong,

Taiwan, and South Korea are now competing with and, in many cases, underselling these traditional Japanese products in the Far East and in other world markets.

23. *Trade with the US.* Japan is acutely aware of its economic and political interdependence with the US and the Free World, and concern for its Western markets will remain the paramount factor in its economic policy for at least this decade. In recent years, the US has accounted for nearly one-third of Japan's foreign trade, with only Canada having greater imports from and exports to the US. Trade between Japan and the US in 1962 reached a new high of \$3.2 billion—exports to the US of \$1.4 billion and imports of \$1.8 billion. Further removal by Japan of restrictions on imports should increase US sales to Japan and Japan will probably continue to be the leading purchaser of US farm products and an important customer for coking coal, iron ore, and capital goods, particularly heavy equipment.

24. A number of crucial problems will plague Japan-US trade relations and may create sensitive political issues as well. Over the past few years, Japan has had serious balance of payments problems, including an important imbalance in its trade with the US. So long as the US faces similar problems of its own, it will be difficult for Japan to increase its exports to the US (visible and invisible) so as to reduce the Japanese import surplus. The suspension of US offshore procurement, the curtailment of US defense expenditures overseas, and the implementation of the Buy-American Act have adversely affected Japan's balance of payments, as well as certain Japanese industries. Also, under the Ship-American policy, the US Government has encouraged preferential treatment for US flag vessels, to the detriment of Japanese shipping earnings. For the short term, Japan's balance of payments will remain a major restraining factor in its economic expansion; as long as this situation obtains, the US will be the chief target of Japanese criticism and Japan will seek means of redressing the balance.

25. *Trade with Communist China.* Trade with mainland China continues to have considerable appeal to the Japanese, who recall the large trade with this area up to World War II. Although developments over the past years on the mainland have weakened the lure of the China market, certain business and government circles in Japan and much of the public look forward to China's eventual economic recovery and the expansion of Peiping's trade with non-Communist countries. The Sino-Japanese trade agreement of November 1962 marked the renewal of quasi-official economic relations between the two countries, broken off by Peiping in 1958 for essentially political reasons.

26. The current pact provides for trade of about \$100 million annually for five years. Actual trade, however, will almost certainly exceed this level, since it is likely that a sizeable volume of business will be con-

ducted for cash or short-term credit at trade fairs or through “friendly firms”—mainly small, leftist-oriented companies and some dummies of large trade concerns. Nevertheless, mainland China’s share of Japanese trade will probably not exceed one to two percent of Japan’s overall foreign trade for several years. A number of factors will limit the growth of this trade: Japan will continue generally wary of dependency on Communist Chinese sources of supply and will be unwilling to jeopardize its US and non-Communist Asian markets. Any large expansion of trade with mainland China during the next few years would require the granting by Japan of extensive medium- and long-term credits which the government would probably be reluctant to do. Japan is also well aware of the political pitfalls in dealing with Peiping and the propensity of the Communist Chinese to inject politics into commercial relations. The present limited arrangement appears useful to the Japanese Government: it serves to offset leftist political pressures for increased trade with Communist China; it offers protection against the political liabilities the government would incur if it failed to meet West European competition for the China trade; and it meets minimum demands among the conservative business community for entry into the China market.

27. In the long run, it is possible that Japan’s trade with mainland China will grow to an extent not now foreseen—whether due to improvements in the Chinese economy, a persuasive softening in Peiping’s policies, a decision by Communist China to look to the Free World for large-scale support for its industrial program, or other factors. Until the end of this decade, however, it seems likely that Japan will move only gradually toward improving its position in the mainland China market, exercising caution and avoiding unacceptable economic or political risks in its relations with the US.

28. *Trade with the USSR.* Barring dramatic changes in Japan’s overall relations with the USSR, the prospects over the next few years for Japan-Soviet trade appear to be only slightly better than in the case of Communist China. Over the next three years, Japan-Soviet trade will take place under an agreement signed in February 1963, replacing one which expired in December 1962. However, since the establishment of normal trade relations with the Soviets in 1957, Japan has built up a large import surplus, which has resulted in a considerable drain on Japan’s foreign exchange reserves. Even if this imbalance were redressed, Japan would face difficulties in absorbing greater quantities of Soviet materials such as coal, iron ore, timber, and oil, because Japan already has stable and advantageous trading relationships in such goods with non-Communist countries. In all these circumstances, it appears unlikely that Soviet-Japanese trade will increase greatly over the present three percent of Japan’s total trade.

29. It is possible that Soviet plans for the development of Siberia could, over time, give a significant boost to Japan-Soviet trade. The Soviets have dangled such perspectives before the Japanese since 1957, but so far have imposed conditions unacceptable to the Japanese. There is still talk of the Japanese participating in the construction of a Siberian oil pipeline, between Irkutsk and Nakhodka on the Pacific coast. However, prospects for this project are stalled over Soviet insistence on favorable credit terms, Japanese unwillingness to accept increased imports of Soviet crude oil in repayment, and Japan's reluctance to breach Western restrictions on selling large-diameter pipe. The recent extension of a five-year credit to Peiping for a vinylon fiber plant, however, may herald a loosening of Japanese credit to Communist countries for certain kinds of industrial development.

30. *Trade with the EEC.* Japan's trade relations with West Europe have improved markedly as a result of Prime Minister Ikeda's talks with various countries in 1962-1963. Great Britain, France, and the Benelux powers have agreed to discontinue discriminatory trade measures against Japanese products. Periodic cabinet-level meetings and Japan's entry into the OECD should stimulate closer economic relations. However, Japanese exports still face a high Common Market tariff wall and increased trade within the market will be at least partly at the expense of trade with other countries including Japan. For the next few years there will probably not be any great increase in Japan's trade with West Europe beyond the present 13 percent of its total trade (six percent with the EEC countries and seven percent with other West European nations).

31. *Trade with Latin America.* A favorable climate exists for an increase in Japan's political and economic relations with South and Central America. These relations have not been hampered by such special factors as the wartime bitterness that affects relations with many Asian states, or the fear of Japanese competition that influences many European countries. Trade with Latin America has increased in the past few years and was six percent of Japan's total trade in 1962. Despite Latin American inflation and shaky economic and political structures, over half of Japan's official loans and guaranteed export credits in recent years have been to Latin America. Japan is also involved in an increasing number of joint ventures in the region. Part of Japanese interest in Latin America is attributable to successful Japanese emigrant colonies there, especially in Brazil. Japan is making greater publicity efforts and Latin American leaders are visiting Japan with greater frequency, and it appears likely that these and other factors should open the way to a steady if not spectacular increase in trade.

32. *Trade with Non-Communist Asia.* Japan's trade with non-Communist Asian nations is as large as its trade with the US (about one-third of total trade). It has, however, shown little recent growth and, with

the exception of a few countries, will probably not rise appreciably during the next few years. Inhibiting factors, particularly in southeast Asia, are unsettled political conditions, low purchasing power, and, generally, a large trade surplus in Japan's favor. Also, a number of Asia's non-Communist nations are developing home industries which are protected and in competition with Japanese products. In its search for markets and raw materials, Japan will continue to interest itself in south and southeast Asia. Its reparations program to various southeast Asian countries is improving Japan's image in the area and facilitating trade. Trade with Australia may show a substantial increase over the next few years. Australia is already an important Japanese source for wool, grains, and coking coal, and may also become one of Japan's chief sources of iron ore. Otherwise, however, prospects for a significant increase in this area's share of Japan's trade do not appear promising.

33. *The Economic Outlook.* Japan's phenomenal recovery and growth and its success in dealing with the business cycle have been based on a more or less steadily expanding market for its exports in the non-Communist world. Foreign trade is the critical element in the Japanese economy. The current 10-year plan (1960-1970) calls for a virtual doubling of Gross National Product (GNP) over the 10-year period, an annual increase of over seven percent. This will require more than a doubling of foreign trade. In the first three years of the plan, Japan surpassed the planned goals, averaging about a 10-percent growth of GNP per annum. As has been pointed out above there are difficulties in the path of continued growth at the planned rate, particularly in the cases of the two most important markets for Japanese exports, the US and non-Communist Asia. If Japan's exports fail to increase at something like the planned rate, the economy will suffer. While the government will probably retain the power to offset periodic economic downturn by monetary and other measures, it could not prevent the difficulties which would result from a serious deterioration in foreign trade. We cannot estimate with any high degree of assurance the course of Japanese trade during the remainder of the plan period. However, we believe that, barring a worldwide depression involving the US, the chances are good that Japan's economic growth will continue at a healthy rate.

IV. INTERNATIONAL RELATIONS

34. In the next few years, Japan will probably move gradually away from its postwar insularity and toward a greater involvement in world affairs. This development will almost certainly take place within the framework of a fairly firm commitment to association with the Free World, particularly the US. At the same time, there will be a trend towards greater independence of posture and less inclination to follow the US lead on outstanding international questions.

35. *Relations with the US.* Japan's dealings with the US in the next several years will be marked by greater insistence on its acceptance as a full and equal partner, and by heightened concern over continued access to the US markets. To Japan, partnership will principally mean prior consultation on contemplated US actions affecting Japan's political and economic interests.

36. Continued major economic problems in Japan-US relations can be expected, springing from Japanese export initiatives and efforts of US producers to protect themselves against Japanese competition. The recent agreement on the allowable levels of Japanese textile exports to the US was reached only with difficulty. Further difficulties are likely to arise over Japanese exports of woolens, metals, and machinery. Any settlement involving real or imagined discrimination against Japanese goods can be expected to produce adverse public reaction in Japan and increase pressures on the Japanese Government and in business circles for countermeasures.

37. Japanese attitudes towards military relations with the US are ambivalent. On the one hand, there is general public acceptance of the need for US military protection to insure Japan's security. Thus, the Japanese can be expected to be sensitive to US moves they might interpret as lessening the US commitment or ability to defend Japan from Communist attack. Steps toward further withdrawals of US forces from Japan or a drastic reduction of US military expenditures in Japan would almost certainly create considerable uneasiness and mistrust in Japan, particularly among government leaders.

38. On the other hand, US bases in Japan and related problems of weapons and forces will continue to involve issues of great sensitivity in Japan-US relations. The government is bound to be responsive to the popular pressures which the left can whip up on these issues. We do not believe that this situation will lead to demands by any conservative government for evacuation of the bases. However, the government will be particularly edgy whenever US bases in Japan are used in connection with combat operations which the Japanese do not see as involving a direct threat to Japan itself. The government will probably not feel able to consent to the storage of US nuclear weapons in Japan, but it may finally take the risk of agreeing to allow US nuclear-powered submarines to make resupply visits to Japan.

39. Continued US administration of Okinawa will probably not become an active political issue in Japan during the next few years. The present government and sophisticated opinion recognize the importance of Okinawa to the defense of Japan and non-Communist Asia. If the Japanese should come to believe that the rights or welfare of the Okinawans were being prejudiced or that the US intended to make the present administrative arrangements permanent, the leftists could

whip up popular resentment, and the question of the return of the islands to Japan could become a major issue.

40. *Relations with Communist China.* The present LDP leadership feels that recognition of Peiping and advocacy of its admission to the UN can be avoided for some time since the minimum demands of both the LDP leftwing and the Socialist opposition have been met by the restoration of limited economic relations with the mainland. Moreover, many conservative leaders see real disadvantages in changing Japan's China policy at this time. In the first place, it would offend the US. Also, Japan would lose the considerable commercial benefits it derives from trade with Taiwan, which might not be easily offset by corresponding benefits in trade with the mainland. On the other hand, popular attitudes will probably continue to reflect a preference for recognition of Communist China, a general feeling that Peiping's exclusion from the UN is unnatural, and a widespread desire to expand trade as much as possible. The government is not now under strong pressure to adopt this view as its own.

41. *Relations with the USSR.* Whereas the Japanese recognize cultural and historical affinities with China and believe they can somehow handle the Communist Chinese, the attitude of Japanese toward the USSR has traditionally been marked by distrust, dislike, and fear. Over the past year or so, the USSR has been seeking in various ways to change its unflattering image and to improve relations with Japan. Although surveys reveal the USSR still to be the country most disliked by the Japanese, these Soviet efforts may not be in vain: there will probably be a greater inclination on the part of the Japanese to favor superficial manifestations of friendship and a greater response to Soviet culture and trade initiatives than in the past. This will be particularly the case if Soviet policy persists in its current effort to seek a general relaxation of East-West tensions.

42. The Japan Foreign Office asserts that the only obstacle to a peace treaty with the USSR is the issue of territories seized by the USSR after World War II. Japan might settle for the return of Shikotan and the Habomai islands but would probably not renounce its claims to the two southernmost Kuriles (Etorofu and Kunashiri) except in return for other concessions. In the present phase of Soviet policy, the USSR may make a move to settle its differences with Japan and achieve a peace treaty.

43. *Relations with Other Countries.* Prime Minister Ikeda has publicly committed himself to attempt a settlement of differences between Japan and the Republic of Korea (ROK). In past years, domestic political difficulties and deep-rooted prejudices and animosities on both sides have made the solution of outstanding issues very difficult. More recently, some progress toward ameliorating relations has been made,

and this movement will probably continue. Japan is informally committed to extend grants and loans to the ROK of around \$600 million as part of an overall settlement. Even if there is no early settlement, Japanese commercial and financial relations with the ROK will probably grow. Japan will probably continue to view good relations with the Republic of China (GRC) to be in its strategic and economic interest. However, a substantial increase in Japanese trade with Communist China would cause severe strains with the GRC and might even face Japan with the alternatives of either reducing such trade or having the GRC break off economic and diplomatic relations with Japan.

44. The Japanese will be concerned to preserve and build up present and potential markets in underdeveloped areas, especially in non-Communist Asia. To this end, Japan will probably take some limited foreign policy initiatives other than those associated with direct commercial advantage. Such Japanese moves are likely in the health, public welfare, and education fields, and the development and gradual expansion of a Japanese technical "Peace Corps" will probably be undertaken by the government. Nevertheless, in these and other projects, Japan's financial contribution will almost certainly be small when compared to the programs of other industrial countries. The Japanese have at various times floated rather vague proposals for regional groupings. The motivation has apparently been to better trade prospects, to emulate the economic groupings in Europe, and to enhance Japan's world position. Similar initiatives may be expected in the future.

V. MILITARY PROSPECTS

45. Barring hostilities directly threatening Japan's security, the next few years will almost certainly see no major changes in Japan's defense policies, military establishment, or assessments of the Soviet and Chinese Communist threats. The US-Japan Security Treaty will almost certainly remain the keystone of Japanese defense and military planning for the rest of this decade. As economic prosperity increases and national self-esteem reasserts itself, it is likely that Japanese concern over such issues as national defense and the desire for a more impressive military establishment will slowly grow. Nevertheless, strong antimilitary sentiment will continue to prevail among the Japanese populace.

46. Japan's current defense outlay is proportionally one of the lowest in the world, and in past years has not kept pace with the growth of either the budget or GNP. There is little prospect for drastic change. Expenditures under the Second Defense Plan (1962-1966) will probably continue to run slightly ahead of scheduled annual increases, but these increases will be partially offset by likely decreases in US military aid before the plan ends in 1966. The annual defense outlay under the draft Third Defense Plan (1966-1971) would come to less than 1.7 percent of the estimated GNP during that period. (European NATO

countries currently devote about five percent of GNP to defense; the US, about 10 percent; Japan's defense outlay in 1963 was under 1.2 percent of GNP.)

47. Within these severe restrictions, public acceptance of growing defense expenditures and the need for improved defense capabilities will probably continue to grow slowly. Leftist forces will not cease their clamor against US bases, but some moderation of opposition to the Self Defense Forces (SDF) seems possible. With a continuing accretion of the good will already gained by the SDF through disaster relief and other civic projects, its public image will probably improve. Within the next few years, for example, the public will probably be receptive to the elevation of the present Defense Agency to a full ministry.

48. Japan's military can also be expected to make steady, if slow, progress in various aspects of advanced weaponry. The Defense Agency will push development of a variety of Japanese missiles. Japan's research and development on sounding rockets has produced excellent results. While no work to adapt these rockets to a military role has apparently been done to date, Japanese efforts to develop an independent missile system in the future are probable. Nuclear weapons and delivery systems are within Japanese industrial and scientific capabilities, though widespread antipathy within the scientific community as well as among the general public will continue to limit research and development in this field. This situation might change after the Communist Chinese acquire nuclear weapons. Japan might then opt for developing its nuclear program to the threshold of a weapons capability, a point which it would take several years to reach, but it would be much more reluctant to cross that threshold than most other countries. The Japanese military will continue to prepare for the possibility of a change in Japan's anti-nuclear policy by continuing to include tactics for an atomic battlefield in SDF training, and by continuing interest in dual-capable weapons systems. Nevertheless, it seems likely that Japan will continue to rely on the US nuclear deterrent and not try to develop its own nuclear weapons at least during this decade.

49. Pressure from military circles for greater independence from civilian control in military planning and policy will probably grow in the future, and leading military officers may become dissatisfied with the scope and tempo of the Japanese military effort. Nevertheless, it appears virtually certain that professional military opinions are not likely to exert a significant influence on defense policy decisions for many years. Through this decade at least, it is almost certain that Japan's military policies will continue to be determined by the civilian government leadership, responsive primarily to what it believes the political traffic will bear.

TABLE I
RESULTS OF LATEST JAPANESE GENERAL ELECTION
House of Representatives, November 1960

PARTY	SEATS GAINED	PERCENT OF POPULAR VOTE
Liberal-Democratic	296	57.5
Socialist	145	27.5
Democratic Socialist	17	8.7
Communist	3	2.9
Minor and Independent	6	3.4
	<u>467</u>	<u>100.0</u>

TABLE II
SELECTED STATISTICS ON JAPAN'S ECONOMIC GROWTH

	1958	1959	1960	1961	1962	TARGET GOALS 1970
Gross National Product (Billion US dollars) 1961 prices	30.7	36.3	41.1	47.2	50.3	81.4
Industrial Production Index	67.0	80.3	100	119.3	128.6	260
Exports F.O.B. (Million US dollars) ...	2877	3456	4055	4236	4916	9320
Imports C.I.F. (Million US dollars)	3033	3599	4491	5810	5637	10150

SOURCES: AID Data Book, Washington, D.C., 1963
Japanese Economic Planning Agency

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NUMBER 41-65

Japan

Submitted by the

W. R. K. Baber

DIRECTOR OF CENTRAL INTELLIGENCE

Concurred in by the

UNITED STATES INTELLIGENCE BOARD

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JAPAN

THE PROBLEM

To estimate the political, economic, and foreign policy prospects for Japan over the next two or three years.

CONCLUSIONS

A. Prime Minister Sato's position is probably secure for the period of this estimate. It is unlikely that his conservative majority will shrink significantly in the next lower house elections, which will probably be held in 1966. The major threat to his position is the current business slowdown, but we believe that his administration's fiscal measures and the basic strengths of the economy will prevent further deterioration and permit a modest recovery within a year or so. (*Paras. 4-18*)

B. Another major problem for Sato is his identification with generally unpopular US policies in Vietnam. If extremists who now lead the opposition Socialist Party succeed in exploiting the issue to mount mass demonstrations on the scale of those in 1960, Sato might be forced to resign in favor of another, less identifiably pro-US conservative leader. On balance, however, we believe that the leftists will not succeed in removing Sato with these tactics under foreseeable circumstances. (*Paras. 4-11*)

C. Economic conflicts between Japan and the US will remain, but none has so far caused or is likely to cause any serious or lasting damage to a generally friendly relationship, or jeopardize the political stability of the Sato administration. The main problems in Japanese relations with the US will continue to be those of Communist China, Vietnam, and Okinawa. Japanese trade with Peking will continue to increase, though at a less spectacular rate than in recent months. In 1966, Sato will probably extend credit guarantees to cover exports to Com-

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munist China. He will seek to avoid diplomatic recognition of Peking as long as possible; but if Peking gained significant further international recognition, he would probably follow suit, hoping that any impairment of Japan's relationship with Taiwan would be temporary. (*Paras. 19-34, 42-51*)

D. Japan will continue to rely on the Security Treaty with the US for military protection. While some qualitative improvement is in prospect, there is little chance that Sato will press for any major increases in Japan's own defense forces over the next two or three years. He will remain sensitive to public concerns on Vietnam and will continue to oppose the use of Okinawan bases for direct bombing attacks, particularly on North Vietnam. We foresee a growth of Japanese nationalism and self-assurance, which will be reflected in a somewhat more independent policy toward the US on these and other issues, and in a more active political role in general in East Asia. (*Paras. 35-41, 52*)

E. Nonetheless, Japan's initiatives in foreign affairs are apt to be cautious and pragmatic, designed to further its efforts to expand trade in as many directions as possible. Willingness to support plans for development of Southeast Asia will be similarly conditioned; Japan is not prepared to accept US direction on its economic assistance role in the area. (*Paras. 24-26*)

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DISCUSSION

I. INTRODUCTION

1. Japan's phenomenal economic growth has thrust it into the ranks of the world's leading industrial and trading nations, and enabled the Japanese people to achieve living standards closely approaching those of Western Europe. Economic success has been accompanied by a remarkable degree of political stability. Yet 20 years after World War II, Japan still does not exert an influence in East Asia commensurate with its assets.

2. There are important reasons for Japanese temporizing on major foreign policy issues. The government has pursued a pragmatic foreign policy, consciously executed to further Japanese commercial interests by taking as few actions as possible that would create enemies in any quarter. At home, despite substantial parliamentary majorities, the ruling conservatives have chosen to operate in accordance with the Japanese tradition of basing decisions wherever possible on a broad popular consensus. Socialists have consistently been ideologically opposed to the US alliance. Of equal importance has been the extraordinarily slow postwar revival of militant nationalism; and there has been widespread opposition to the development of powerful military forces. Finally, Japanese leaders themselves have been ambivalent about what the nation's international role ought to be. On one hand, they are generally sympathetic to US containment of Communist China and reluctant to dilute US efforts in this direction. On the other, they want to assert independence of the US and to restore Japan's Asian identity by improving contacts with neighboring Asian states, both Communist and non-Communist.

3. There are many signs that Japan is moving toward the assumption of somewhat greater international responsibilities: the forthcoming treaty with South Korea and the substantial Japanese economic aid which accompanies it; an aid agreement with Taiwan; favorable responses to certain other Asian developmental needs; attempts to mediate the conflict between Indonesia and Malaysia; participation in several Afro-Asian conferences; and an effort to gain a seat on the UN Security Council. Apart from the Korean treaty, these are all issues where Japan can afford to take initiatives without affecting the basic direction of its foreign policy or arousing serious political opposition at home. Remaining largely unresolved are the critical long-range issues of Japanese foreign policy: relations with Communist China; the future of Okinawa; and the mission of the nation's armed forces. Over the next decade, the Japanese leadership will have to face up to these issues, but in the next two or three years, unless Japan encounters depression or war, it is likely that most of these decisions will again be postponed.

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II. POLITICAL

4. *The Liberal-Democratic Party.* For almost 20 years, conservatives have held between 55 and 65 percent of the seats in the all-powerful lower house of the Japanese Diet; the ruling Liberal-Democratic Party (LDP) now holds 61 percent¹ and seems in no danger of losing its commanding position over the next two or three years.² In November 1964, Eisaku Sato succeeded the ailing Hayato Ikeda as president of the LDP and prime minister of Japan. Though Sato's accession to power was contested within the party through most of 1964, his leadership is now reasonably secure. Serious competition has been virtually eliminated by the deaths over the past year or two of three other party leaders: Ichiro Kono, Bamboku Ono, and Ikeda himself. Other rivals, such as Takeo Miki, the Minister of International Trade and Industry, would require several years to cement a following strong enough to challenge Sato.

TABLE 1

Elections to the House of Representatives (Lower House) of the Japanese Diet, November 1960 and November 1963

PARTY	SEATS		PERCENT OF POPULAR VOTE	
	1960	1963	1960	1963
Liberal-Democratic	296	283	57.5	55.1
Socialist	145	144	27.5	29.0
Democratic Socialist	17	23	8.7	7.3
Communist	3	5	2.9	3.9
Independent and Other	6	12	3.4	4.7
	<u>467</u>	<u>467</u>	<u>100.0</u>	<u>100.0</u>

5. Various developments of the past year have put the party on the defensive and made Sato somewhat more cautious in pressing his programs than was expected when he took office. The Japanese public is generally apprehensive that US actions in Vietnam, particularly the bombings of the North, will lead to the military involvement of Communist China and, ultimately, of Japan. Sato endorses the general line of US policy on Vietnam (though with reservations), and is exposed to heavy domestic pressure on this account. Another major LDP problem is the state of the economy, marked by stagnating production and a wave of bankruptcies, primarily among small businesses. Finally, a succession of political scandals in the LDP, though not involving top party figures, added to Sato's problems. The losses in popular esteem have been reflected to some extent in a lackluster LDP showing in the House of Councillors (upper house) election in July 1965.

6. *The Socialists.* The core of Sato's political opposition is the Socialist Party (JSP) which holds only about one-half the number of seats in the lower house held by the LDP (and about the same proportion in the upper house). The

¹ See Table 1.

² The next lower house election must be held by November 1967; it will probably be held during 1966.

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more moderate Democratic Socialist Party (DSP), which broke off from the JSP in 1959, has had difficulty maintaining its strength and is not now a serious competitor. However, the DSP does provide a political home for significant categories of workers and intellectuals who occasionally support the government, thereby contributing to the "consensus" sought by the LDP on certain major legislation. Behind the JSP stands SOHYO, Japan's major trade union confederation with 4.2 million members. SOHYO provides most of the JSP's funds and street demonstrators, and about one-half of its members and one-third of its Diet representatives.

7. A four-year trend toward moderation in JSP policies was reversed in late 1964 when the leadership of the party was captured by radical elements. Their control was confirmed in May 1965 with the election of Kozo Sasaki as party chairman. Sasaki's leadership is not a reflection of some sudden mass swing to the left of the party rank-and-file, but rather the result of poor convention tactics and overconfidence on the part of his moderate opponents. To some extent, Sasaki was aided by prevailing frustrations over the party's continuing inability to seriously threaten the overwhelming LDP parliamentary majority in a prosperous Japan.

8. Since taking over, Sasaki has attempted to turn the political clock back to the turbulent years 1959-1960; he has resurrected the party's anti-US policy, strengthened ties with Peking, advocated non-cooperation in legislative affairs, and worked to revive JSP cooperation with the Communist Party (JCP) in anti-government activities. He views united front tactics with the well organized Communists as the key to the success in the streets with which he hopes to embarrass the Sato government and attract added popular support.

9. The Sasaki group has seized upon the Vietnam issue as the vehicle to bring the JSP out of the political wilderness. For example, the JSP claims that the South Korean treaty, now in the last stage of ratification, is designed to link Japan more closely with US security arrangements in the Far East. The JSP also injects Vietnam into parliamentary discussions on Okinawa and on US bases in Japan proper. In exploiting the Vietnam issue, the JSP seeks also to lay the groundwork for a campaign to terminate the US-Japanese Security Treaty in 1970, when it first becomes open for suggested revision. Moderate JSP leaders, including many in SOHYO, are opposed to Sasaki's parliamentary obstructionism and, particularly, his new emphasis on a united front with the Communists. The moderates, however, are in political disarray and will probably be unable to do more than slow Sasaki's pace, at least so long as the war in Vietnam remains a major popular concern in Japan.

10. It is unlikely that Sasaki will succeed in his efforts to repeat the JSP's success of 1960 in creating chaos in the streets of Tokyo and forcing the resignation of an LDP prime minister. Sato has already showed signs of greater dexterity than his brother Nobusuke Kishi in handling such tactics; policing of demonstrations has been vastly improved and parliamentary traditions are being

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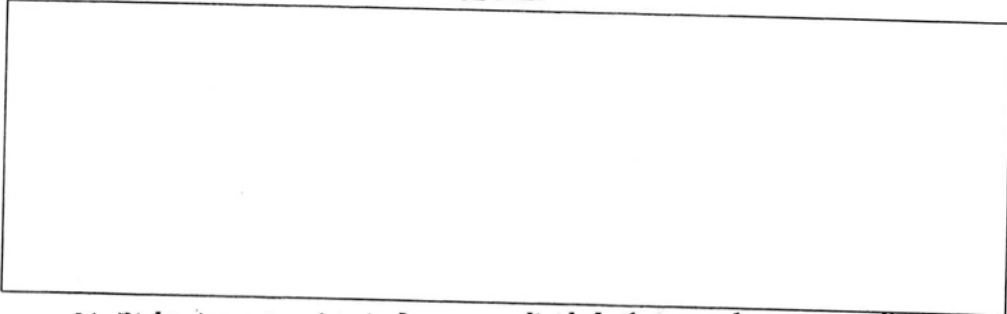
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better observed to avoid provoking public opposition. While not so popular as former Prime Minister Ikeda, Sato has not attracted anything like the hostility that accrued to Kishi and contributed to his downfall. Sato's adroit handling of the issues of Vietnam and Okinawa thus far indicates that he possesses sufficient political sensitivity to weather foreseeable criticism on other foreign policy matters. In any event, the Japanese press and public seem to have matured somewhat since 1960 and apparently want to avoid repeating the excesses of that year. Another favorable element is the absence of zeal for disruptive tactics on the part of the DSP and other minor parties, and among JSP moderates as well. We cannot exclude the possibility that some development in the Vietnamese war—e.g., significant escalation, particularly greatly increased US use of Japanese bases for support or of Okinawan bases for direct air attacks—would create enough public apprehension to support a massive campaign against Sato.

11. *The Communists.* The JCP maintains an uncompromisingly militant line and closely supports Peking in its attitudes toward both the US and the USSR. The party's Chinese bias became more pronounced in 1964 with the expulsion of several ranking members who had Soviet sympathies, including two Diet members who voted in favor of Japanese ratification of the limited nuclear test ban treaty. Communist electoral strength has grown steadily since 1958, due mainly to support from former JSP extremists. Nevertheless, the JCP polled only about seven percent of the vote in the most recent nationwide elections, those of July 1965 for the upper house. In the next lower house election, the Communists could probably not secure more than an additional three to five percent of the vote and this much only if there are wholesale defections from the JSP. The importance of the JCP in Japanese politics, however, rests partly upon its ability to muster agitators and street demonstrators in the major cities and principally upon its function as a transmission belt for ideas, and probably material assistance, from Peking to the radical wing of the JSP.

12. *Soka Gakkai and the Rightists.* The militant Buddhist organization, Soka Gakkai, operating through its political arm, Komeito (Clean Politics Party), is now an important force in Japanese politics. Komeito is the third largest party in the upper house and holds the balance of power between the dominant JSP and the LDP in the Tokyo Metropolitan Assembly. In the next lower house election, the first it will enter, Komeito will probably elect about one-half of the 35 to 40 candidates it is expected to field.

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14. Rightwing extremists in Japan are divided, their numbers are small, and there is widespread public opposition to the violent tactics which they advocate. They could probably gain substantial support from conservative quarters only if the JSP came to power.

III. ECONOMIC

A. The Domestic Economy

15. The Japanese economy has been growing at a phenomenal rate; the growth of GNP averaged 10 percent annually from 1955 to 1964, reaching almost 14 percent in 1964. In the past year or so, however, there has been a marked slowdown in economic growth and the GNP will probably show an increase of only about 4 percent for 1965. The current situation is characterized by the levelling off of industrial production, decline in new orders, excessive inventories, and reluctance among businessmen to make new investments. There have also been serious difficulties in the stock market and among securities companies, an unusually high rate of bankruptcies in small and medium-sized firms, and a sharp profit squeeze for many large corporations caught between declining sales revenues and heavy burdens of debt service. Indeed, most of the recent business failures have resulted from overextended credit positions, a prominent characteristic of Japan's postwar business enterprises whose financing has come largely from banks rather than internal sources of funds.

16. The current slowdown was preceded by an overly rapid expansion of credit during 1963, which spurred the economy into overextension of capacity and producers' inventories, an upsurge in imports, and a consequent balance of payments crisis. In early 1964, the application of the traditional remedy of credit restraints slowed the rate of increase of imports and helped ease the balance of payments problem. However, the reversion to easy money later in the year failed to bring about anticipated increases in industrial investment and production, largely because of earlier satisfaction of the demand for consumer durables and the drag of large producers' inventories of finished goods. A further loosening of credit restrictions in early 1965 did not relieve a growing "recession mood" among Japanese businessmen.

17. The failure to overcome the slowdown through relaxation of credit restrictions has led the Sato government to explore fiscal techniques new to postwar Japan. In order to stimulate the economy, the government plans

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bond issues to finance an anticipated budget deficit; this marks a departure from the postwar policy of balancing the current account of the budget from year to year. The only significant action so far has been an increase of about \$550 million in its loan and investment program which will work its way into the economy in early 1966. The government is also contemplating more investment in long neglected "social overhead"—housing, transportation, water supply, and sanitation. In order to cope with the current economic slowdown and to avoid wide cyclical swings in the economy, Sato is stressing the achievement of a "stable" growth rate rather than a return to the rapid growth and periodic overheating of the economy characteristic of the Ikeda period. His course is favored by a growing recognition among Japanese businessmen that the extremely rapid growth rates of the past decade could not have been maintained indefinitely.

18. By careful manipulation of fiscal measures and business stimulants available to him, Sato will probably manage to prevent any significant worsening of the economic situation. Indeed, there will probably be a modest upturn during 1966 in view of the fact that, despite the slowdown, exports have maintained record levels and unemployment has remained very low. Resolution of such basic problems of the overstretched economy as heavy debt burdens and high interest rates will require additional years of governmental effort. In any event, Japan's economy will continue to be extraordinarily vulnerable to fluctuations in both domestic and foreign demand. Over the next year or two, however, economic problems are unlikely to put Sato's position in serious jeopardy, much less shake the LDP grip on the government.

B. Foreign Economic Relations

19. Japan's foreign trade now totals about \$16 billion annually and is crucial to the economy. Japan's natural resources are severely limited and its industry survives and expands largely by processing foreign raw materials. However, the record of the past decade indicates that Japan can pay for overseas commodities through the export of a wide variety of manufactured goods while steadily improving living standards. A record surplus was achieved in Japan's merchandise trade balance in the first nine months of 1965 and further growth is likely over the next year or so. On the other hand, Japan continues to suffer from a steadily growing deficit in invisible balance of payments items—freight and port expenditures,³ insurance, and credit costs—and, except during the last few months, this has resulted in substantial deficits in the current account of the balance of payments. The Japanese remain generally apprehensive about their balance of payments and view any threat to export growth with alarm.

³ Although Japan led the world in the tonnage of ships launched from 1956 through 1964, Japanese ships currently carry less than one-half the annual volume of the nation's exports. This apparent paradox results from the devastation of Japanese shipping during World War II, the rapid growth of trade since the war, and, particularly, the fact that 63 percent of the tonnage launched in 1956-1964 was sold to foreign shipowners.

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20. *The US.* The US is Japan's leading trading partner by a substantial margin; bilateral trade has reached a level of almost \$4 billion a year and the US customarily takes 25 to 30 percent of Japan's total exports. Because of this heavy dependence on US markets, the Japanese are acutely sensitive to fluctuations in the US economy and react sharply to every manifestation of protectionist sentiment in the US. To anticipate and avoid the development of such sentiment, Japanese businessmen have been persuaded to accept "voluntary" restrictions on certain exports, particularly textiles, and in the case of cotton textiles these have been formalized in bilateral agreements for periodic fixing of quotas for Japanese products destined for the US market. While the steady overall growth of exports to the US has helped minimize complaints from Tokyo, these arrangements have caused resentment among Japanese businessmen.

21. The US also plays an important role in the Japanese economy as a provider of both long-term and short-term capital. Long-term capital inflow from the US has been concentrated on issues of bonds and debentures as a result of the unreceptive Japanese attitude toward foreign equity investment. A US "Interest Equalization Tax" enacted in 1964 and applicable to foreign securities and commercial bank loans of over one year has contributed to a decline in the availability of such funds for Japan. The impact of the tax was softened by the granting in 1965 of a \$100 million annual exemption for US purchases of securities issued or guaranteed by the Japanese Government. Even though the full exemption is unlikely to be used in 1965, the Sato administration remains concerned over the continuing decline in US long-term bank loans and the possibility of further US governmental limitations on bank lending abroad.

22. Other persistent economic problems between Japan and the US concern civil air routes and fishing rights. Japan seeks the right to fly passenger aircraft from the west coast of the US to New York and beyond so as to compete in round-the-world service. The Japanese argue that the existing bilateral civil air agreement is unfair since it was concluded more than a decade ago when Japanese negotiating power was weak. The same argument is made in regard to the Convention which restricts Japanese salmon fishing in the northern Pacific. While prospects are good for a resolution of the civil air dispute, the fishing issue will almost certainly continue to be a source of friction.

23. Thus far, economic problems between Japan and the US have not caused serious or lasting damage to a generally friendly relationship nor jeopardized the political position of the Sato administration. US economic leverage provides a potent restraint against excessive Japanese stubbornness, but commercial irritants of various sorts are bound to arise from time to time, and Sato will probably become somewhat harder to deal with as part of the overall Japanese tendency toward greater independence in foreign affairs. Japan's importance as a market for US exports and as a logistical base gives Japan substantial leverage of its own.

24. *Southeast Asia.* Japan's emergence as a prosperous industrial nation has brought pressure from the US for more liberal economic assistance to less de-

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veloped countries. Japan has moved very cautiously in assuming such responsibility, even in Southeast Asia where it is second only to the US in total trade. Reparations and other war-related payments have so far been the major form of Japan's aid in this region. Its \$1.3 billion program is about half completed, with payments to South Vietnam, Thailand, Laos, and Cambodia almost entirely disbursed, and the much larger commitments to Indonesia, the Philippines, and Burma almost half fulfilled; claims for reparations by Malaysia and Singapore remain unsettled. Apart from reparations, Japan has extended relatively little grant aid to the countries of Southeast Asia. Long-term and other credits, though substantial, have been almost entirely on commercial terms. Direct private investment in Southeast Asia is also substantial and accounts for about 20 percent of all Japanese investments overseas. It is particularly important in Indonesia, where Japan has contracted for projects valued at almost \$100 million under "production-sharing" agreements which, coupled with its reparations, have reinforced its very strong trading position.

25. There is likely to be some increase in Japanese aid to Southeast Asia, but any rapid expansion is unlikely. In July 1965, Japan pledged itself to increase its total annual foreign assistance by about 1970 to one percent of national income, or about double the level of Japanese aid committed in 1964. There is, however, no firm timetable or evidence of concrete planning to reach such a goal. This same cautious approach to foreign aid is evident in the cool Japanese reaction to an April 1965 proposal to set up a multilateral program of economic assistance to Southeast Asia in which the US contribution would be as much as \$1 billion. The Japanese view the program as part of the overall US strategy for Vietnam and are reluctant to become involved in it. Yet they have shown great interest in UN ECAFE plans for an Asian Development Bank, whose headquarters they hope to have located in Tokyo, and have indicated willingness to subscribe \$200 million in capital to ensure a major voice in its management. One of the most imaginative Japanese proposals for multilateral aid has been to establish an Asian agricultural development fund to which they would contribute capital and technical assistance. The Japanese probably intend to push this proposal at a conference on Southeast Asian regional economic cooperation which they are sponsoring in early 1966.

26. Japan is not prepared to accept US direction on its economic assistance role in Southeast Asia. An important motive for Sato's current interest in various types of aid activity there is probably a reluctance to see the US completely outdistance the Japanese in a region which they regard as their rightful sphere of economic influence. Sato will almost certainly continue to view Japan's role in Southeast Asia in this light, expanding aid efforts only slowly and in response to clearly defined commercial interests.

27. *The Communist States.* Japan's trade with the Communist states has grown steadily, and since 1960 at a rate higher than that for total Japanese trade.⁴ Though trade with Communist countries still accounts for only about

⁴ See Table 2.

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six percent of Japan's total trade, this performance has stimulated the imagination of Japanese businessmen, many of whom see these countries—particularly Communist China—as a vast untapped market for their manufactures. The Sato administration, like those of Kishi and Ikeda, is experiencing heavy domestic business pressures to encourage expansion of trade with Communist countries beyond the total of \$1 billion expected in 1965.

28. Pressures on Sato from outside the government are supplemented by pressures from within the LDP and the Cabinet. China trade policy is the nearest thing to a divisive issue within the administration and Trade Minister Miki is one of the many LDP proponents of the liberalization of government-backed export credits for Communist countries, a measure that would greatly

TABLE 2

Japanese Trade with Communist Countries (including Cuba), 1960-1965
(in \$US millions)

	COMMUNIST			TOTAL
	USSR	CHINA	OTHER	
1960	147	24	51	222
1961	210	48	98	356
1962	296	84	105	485
1963	320	137	95	552
1964	409	311	198	918
1965 (estimated)	400	450	not available	

assist the growth of Japanese trade with Peking. Sato is also confronted with countervailing diplomatic and economic pressures from the US and other valuable trading partners—Nationalist China, South Korea, and to a minor extent, South Vietnam.

29. Japanese trade with Communist China has increased very rapidly since conclusion in late 1962 of the Liao-Takasaki agreement—a quasi-official trade arrangement nominally made under private Japanese auspices. It is expected to top \$450 million in 1965, exceeding Japanese-Soviet trade for the first time since 1959 and permitting Japan to replace the USSR as Peking's leading trading partner. Barring some unforeseen political decision on the part of Peking, trade will almost certainly continue to grow, though not at the explosive rate of recent years. Its potential is limited by pressures from the US and Nationalist China, and, more important, by the narrow range of Chinese exports acceptable to Japanese firms and Peking's relatively modest purchasing power. The Japanese are also wary, for political reasons, of becoming overly dependent on the Chinese mainland for markets or raw materials. On the whole, therefore, it is unlikely that trade with Communist China, now between two and three percent of Japan's total, will approach five percent within the next two or three years.

30. To compensate for the limitations on Communist China's purchasing power, Peking and the various Japanese proponents of increased bilateral trade will press Sato to remove the ban on government backing of credits for five

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years or more for purchases of capital equipment by Peking. Thus far, the Japanese Government has participated in only one such credit: in August 1963, a five-year, \$20 million credit for a synthetic fiber plant. This action brought strong reprisals from Nationalist China and led to Sato's refusal in early 1965 to provide similar backing for another synthetic fiber plant and a freighter. Japanese concerns quickly offered to provide private credit arrangements to salvage both deals, but Peking cancelled both orders as a means of objecting to Sato and his policy of "separation of politics and economics" (i.e., expanding trade without necessarily accepting closer political relations). Despite this and similar frictions, the two countries continue to exchange numerous business and technical missions, and maintain semi-official trade liaison offices in each other's capital. Trading continues, though in recent months an increasing proportion is being conducted by Peking through so-called "friendly" Japanese firms rather than through the closely supervised Liao-Takasaki channels.

31. Sato is unlikely to be able to hold the present tight line on government-backed credits beyond 1966. Modifications could result from domestic pressures, especially from the larger concerns which would benefit most from sales of capital goods. Indeed, Sato himself, though strongly committed to a tough posture vis-a-vis Peking, may not be inclined to wait until aggressive Western European traders move *en masse* into what he and other Japanese consider Japan's natural market. Sato is cognizant of Taipei's sensitivities on the credit issue and he expected that the \$150 million credit granted to Nationalist China in April 1965 would help mute the latter's protests. He has also conducted an intensive diplomatic campaign to assure Taipei of his political sympathies, meanwhile preparing it for a break in the credit dike. Taipei reaction would also be tempered by its extremely heavy dependence on Japanese markets for its subtropical agriculture produce, but we cannot exclude the possibility of response by the Chinese Nationalists that would break existing economic and even political ties.

32. A similar but far less critical problem arises in the case of the two Koreas. Japan has few dealings of any sort with North Korea and trade is small and unimportant. Japan is unlikely to jeopardize its much firmer prospects in South Korea by significantly increasing its economic stake in the North in the near future. South Korea is a major trading partner with which Japan consistently runs a large and profitable export balance. With the ratification of the long awaited normalization agreement between the two countries, the way will be open for an \$800 million program of Japanese economic assistance, including \$300 million in grant aid. This will almost certainly lead to Japan's replacing the US as South Korea's principal trading partner and regaining at least a modest degree of political influence in Seoul.

33. Trade with the USSR presents even fewer problems for the Japanese. Although Japan adheres to Free World restrictions on the sale of strategic goods and on the extension of long-term credits, it is one of the USSR's leading non-Communist trading partners; trade for 1965 is expected to be almost the same

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as 1964, approximately \$400 million. Officially backed credit assistance to the USSR will continue to be a problem for the Sato administration. Japan has generally held to a five-year limit with the Soviets, but exceptions have been made and at least one eight-year credit has been granted; the Soviets are now pushing for credits up to ten years. Prospects are good for expansion of trade and other economic relations with the USSR, particularly with respect to fisheries, civil air, and consular matters, but dramatic increases are unlikely unless Japan chooses to enter a credit race with Western European nations or the US lowers the bars on sales of strategic goods to the USSR. In either event, Japan would vigorously compete for Soviet business.

34. Japanese trade with North Vietnam has averaged only \$15 million annually in recent years and any significant expansion is unlikely even under peaceful conditions. Because of objections of the seamen's unions, Japanese shippers have withdrawn their vessels from the North Vietnam trade, but ships of other countries are filling the gap.

IV. MILITARY

35. Sato assumed office with a reputation of being more "defense-minded" than his predecessors. He was believed to favor such measures as elevation of the Defense Agency to a ministry, a substantial increase in defense spending, acceleration in the pace of Japan's peaceful rocket and nuclear programs, and amendment of the "no war" clause in the Constitution. Other than minor increases in the military budget, however, the government has undertaken little action in this field. It probably considers that the strong residual anti-militarism of postwar Japan, augmented currently by fears of possible involvement in the conflict in Vietnam, make increased defense measures politically unwise if not at present unattainable. Also, the lack of a widely recognized and pressing threat makes this government as prone as its predecessors to find refuge under the protective umbrella of the Security Treaty, and to defer increased defense outlays in favor of more popular projects. Current plans approved by Sato call for only modest improvements in the Japanese defense structure over the next two or three years. Within its limited defense budget, however, Japan is responding to the phasing out of US military aid by expanding the domestic production and design of military equipment, including various short-range missiles, and these programs are likely to continue and expand.

36. Popular resistance to a military buildup reflects not only a revulsion from the disasters of World War II but almost equally the absence of a sense of danger. Most Japanese still cannot take seriously the thought of China as a direct threat, although this attitude will probably be modified when Peking approaches the achievement of a credible operational nuclear capability. And, although the Japanese have great respect for the power of the USSR and a historic mistrust of its intentions, the relatively peaceful attitude of Moscow toward Tokyo over the past decade has largely subdued fears of attack from this quarter. This vagueness in defining a military threat has been at the root of Japan's failure

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to establish guidelines necessary to detailed defense planning. In any case, there is a strong tendency to feel that the security treaty with the US provides ample insurance against both Peking and Moscow.

37. The US bases in Japan proper and Okinawa which give meaning to the security treaty also represent a danger to Japan in the minds of some Japanese. They reason that whereas no nation is likely to attack Japan for its own sake, US bases in Japan would make it a prime target if the US were to get into a war with the Communist powers. This fear, continually exploited by the Japanese left, is a major factor in Japanese popular opposition to US policy in Vietnam. Sato has a more sophisticated view of US purposes in Vietnam and quietly supports American policy there. Though Okinawa is not subject to the limitations of the Security Pact, use of its bases for direct bombing attacks on targets in South Vietnam, if publicized, would probably arouse the Japanese public and would cause Sato to protest as he did in July 1965. Similar attacks from Okinawa on North Vietnam would draw a much more adverse Japanese response. On the other hand, Sato is not likely to object to the continued shipment of US troops and materiel to Vietnam via bases in Japan so long as such movements are handled with minimum publicity and create no newsworthy incidents. Japan will continue to oppose the import of US nuclear weapons into the country whether for local storage or for transshipment.

38. The Japanese Government will almost certainly continue to rely upon the US for military protection under the terms of the Security Treaty through 1970 when negotiation for revision becomes possible. The Japanese leaders prefer this arrangement to undertaking the responsibility and expense of establishing and maintaining a Japanese force capable of meeting conventional or deterring nuclear attack. Nevertheless, over the next five years, Sato and his LDP successors will maneuver to gain a stronger voice for Japan in any revision of security arrangements with the US, particularly with respect to US bases in Japan. To this end, they will probably effect certain qualitative improvements in Japan's air and naval arms and engage in some concrete planning for the assumption of a greater share of the defense burden.

39. In striving for a less dependent defense posture, Japanese conservative leaders will at least consider the development of nuclear weapons, though in view of the continuing strong public aversion to the idea, the government is unlikely to press for their development. Indeed, barring a major change in the international situation—e.g., Japanese loss of confidence in the security relationship with the US; blatant Chinese Communist aggression in Korea or Taiwan; or wholesale proliferation of nuclear weapons throughout the world—we believe it unlikely that any Japanese premier in the next four or five years would accept the political risks of openly advocating the production of nuclear armaments.

40. In the unlikely event that Japan decided to become a nuclear power, it is technologically and economically capable of becoming a formidable one. On the basis of its highly advanced nuclear development for peaceful purposes

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and by initiating construction of an indigenous plutonium production reactor facility in 1966, Japan could test its first nuclear device by about 1971 without violating existing safeguard provisions. Thereafter, it could produce an estimated 10 to 30 weapons annually if unsafeguarded uranium were available. By violating safeguards, Japan could advance its initial test of a nuclear device to 1968, but this is unlikely to occur. The test would not lead to any immediately significant production of nuclear weapons; on the contrary, it would jeopardize future shipments of fuels and the acquisition of the technical assistance for further advances in the nuclear field.

41. The Japanese space research program provides an adequate base for the development of missile systems for the delivery of nuclear warheads. During the next few months, Japan will probably try to orbit a small earth satellite and chances of success are good. By applying its rocket technology to the development of an MRBM/IRBM system, Japan could attain an operational capability with such a system early enough to meet the availability of nuclear warheads. We estimate that by 1975 Japan could produce a force of as many as 100 launchers for such missiles together with the necessary nuclear warheads for an incremental cost of about \$1 to 2 billion; annual expenditures would not exceed 0.5 percent of Japan's GNP.

V. FOREIGN POLICY

42. Although Japanese foreign policy has not yet developed a clear sense of mission, certain general lines of action have emerged in recent years. There is a wide consensus that continuation of the close military and economic relationship with the US is the bedrock guarantee of Japanese well-being. At the same time, there is movement toward closer political relationships with the Asian Communist states because they are potentially valuable trading partners but, more important, because they are neighbors with whom normal and peaceful relations must inevitably be established. On the positive side, there is a desire to become politically influential once more in the affairs of those territories lying between the great mainland powers and Japan itself—North and South Korea and Taiwan. Coupled with this is a desire to regain those nearby Japanese islands lost to the Allies in World War II—the Ryukyus (Okinawa), Bonins, and southern Kurils. Beyond the Korea-Japan-Taiwan triangle, Japan's few foreign policy initiatives have been focused on increasing economic ties with Southeast Asia which Japanese continue to view as an important source of industrial raw materials and potentially a great market; in any case, a region where Japanese economic interests have much room for expansion. Japan has done little thus far to indicate any conception of its broader, world role.

43. *Communist China.* Despite differences of emphasis among Japan's conservative leaders, there is general agreement on the desirability of containing Chinese Communist influence in East Asia and providing a Japanese alternative to the region's smaller nations, including Mongolia and North Korea as well as non-Communist nations. Most conservatives are also determined to resist Pe-

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king's efforts to use its expanding trade with Japan as a political weapon. To this end Sato maintains his China policy of "separating politics and economics." When embarrassed by reference to their increasing contacts with Peking, the Japanese rationalize these activities as "building bridges" between China and the West in order to diminish Peking's dangerous isolation from the world.

44. Were it not for sustained US and Nationalist Chinese pressures, Japan would be even further along the path to diplomatic recognition of Peking. The majority of informed Japanese probably feel that it is necessary and most others would not oppose it. Since France granted recognition in 1964, Japanese leaders have been concerned that they might fall behind other Western countries in this regard, thereby incurring domestic complaints and Peking's permanent displeasure. At the UN, Japan has been watchful and nervous on matters pertaining to the admission of Peking; and Japan would probably vote affirmatively if it became apparent that Peking had acquired clearcut majority support. It would prefer to see a "Two Chinas" solution that would permit Taipei to retain its Assembly seat and the other prerogatives of an independent state.

45. Sato will probably be able to cope with domestic pressures for recognition of Peking over the next year or two, as he has in the past, by cautious expansion of economic, cultural, and quasi-official relations. In the event that domestic pressures become unmanageable as a result, for example, of some general international breakthrough on the issue, Sato would probably move to offer diplomatic recognition.

46. Sato's reluctance to recognize Peking is based primarily on concern over US reactions and the fate of Taiwan. Sato is among the many Japanese who are apparently convinced of Taiwan's strategic importance to the defense of Japan and of its situation well within Tokyo's potential sphere of economic and political influence. Nevertheless, he could not afford to maintain an unyielding attitude indefinitely toward Peking's overtures for recognition even if this required, as seems likely, termination of diplomatic relations with Taipei. Though reluctant to abandon their foothold on Taiwan, Sato and the Japanese would probably conclude that with continued US support, Taiwan would not in any case fall into Peking's hands.

47. *The USSR.* A breakthrough on the question of a World War II peace treaty with the USSR is unlikely so long as the USSR continues to refuse to return to Japan the small islands northeast of Hokkaido which Tokyo claims. Neither side, however, appears particularly disturbed by the failure to make a formal peace 20 years after the war; this certainly has been no major obstacle to the expansion of diplomatic and economic relationships over the years. Sato will maintain the firm political posture that he has demonstrated vis-a-vis the Soviets in the face of their frequent protests over the presence of US bases in Japan. Thus far, Japanese responses to these protests have not affected economic relations. Both sides desire to expand their trade and there is much interest in Japanese participation in the development of eastern Siberia. The

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Soviets and the Japanese have a common interest in containing Communist China, and this congruence is likely to find expression in efforts on both sides to intensify their present friendly relations.

48. *Korea.* Sato's attention is presently focused on ratification of an agreement which would normalize political relations between Japan and South Korea. Despite JSP and JCP opposition in the streets and in the Diet, the government will ratify the treaty in December 1965; failure on this issue would have been a severe blow to Sato's prestige. The leftist opposition seems unable to rouse widespread adverse public feeling on the Korea issue. Nor have they succeeded in linking it in the public mind with the vastly more exploitable issue of Vietnam. After ratification and implementation of economic provisions of the agreement, Japanese influence in South Korea is certain to grow despite Korean efforts to keep it in bounds. Until the South Korean enterprise is launched successfully, Japan may feel inhibited from improving its presently meager trade and cultural relations with North Korea.

49. *Okinawa.* There is no easy solution to the problem of Okinawa for the Sato government. It must demonstrate a continued interest in the reversion of the Ryukyu Islands to Japanese administration, a course desired by almost all Japanese of whatever political stripe. At the same time, the government recognizes that the US base structure in Okinawa contributes directly to the security of Japan to an extent that would not be possible were it to come under Tokyo's administration. Faced with the need to maintain some momentum on this issue, Sato will probably concentrate on achieving the maximum possible Japanese economic and political involvement in Okinawan affairs. Though he would probably not want to force a showdown on Okinawa at any time, it is apparent that the island will remain a major irritant in Japanese-US relations. Sato's position would be made much more difficult if there were further dramatic reminders of Okinawa's role in the Vietnamese war.

50. *Vietnam and the US.* Failure to offer more than grudging endorsement of US actions in Vietnam probably reflects Japan's uncertainty as to the chances of US success as well as fears of its own involvement. There is also relatively little concern, even among Japanese conservatives, over the impact of a possible Communist victory in Vietnam on Thailand, Malaysia, and other Southeast Asian states. If US efforts showed signs of reaching a successful conclusion, however, the Japanese Government would probably swing to firmer support of its programs. If the US were patently unsuccessful, Sato would maneuver carefully to dissociate himself and avoid the inevitable political fallout at home. If he did not, he might be forced to resign in favor of another conservative, less identifiable as a defender of US policy in Asia.

51. There is probably little that Sato can do on the diplomatic front at this time beyond occasional cautionary reminders to the US to avoid deeper involvement of Japanese or Okinawan bases in the Vietnamese war. Caught between domestic pressures and the imperatives of Japanese national security, he will

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probably continue to attempt to satisfy both. His consequent ambivalence on Vietnam is likely to be a continuing source of irritation in relations with the US.

52. In addition to Communist China, Okinawa, and Vietnam, there will be other hindrances to fuller Japanese cooperation with the US as Japanese nationalism and self-assurance grow. Inevitably, Japan will develop policy positions on the basis of its own expanding political and economic goals in East Asia, its bargaining power will improve, and conflicts with the US will increasingly require mutual concessions. In short, Japan's position and policies toward the US will come to resemble those of West Germany or other European allies.

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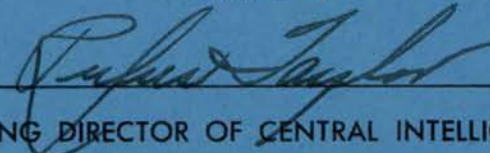
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NATIONAL INTELLIGENCE ESTIMATE
NUMBER 41-68

Main Trends in Japan's External Relations

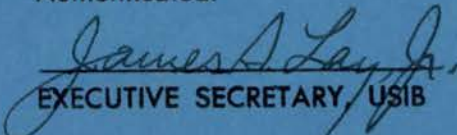
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MAIN TRENDS IN JAPAN'S EXTERNAL RELATIONS

CONCLUSIONS

A. Japan is acquiring an increasingly important position in the international economic community; its remarkable economic growth will soon make it the third most productive nation after the US and the USSR. At the same time, Japan is becoming progressively more assertive in world and regional affairs. The constraints on Japan's willingness to seek international political responsibilities are bound to diminish further over time, nevertheless its acceptance of such responsibilities, and its exercise of influence and power in international affairs generally, will probably not increase to the degree suggested by its powerful economic position within the next 5 to 10 years.¹

B. We believe that Japan will continue to identify its basic interests with those of the US and the Free World over the next 5 to 10 years. In particular, it will probably devote important diplomatic efforts to cementing friendly relationships with its leading trading partners—the US, Canada, and Australia. These economic ties and an increasing similarity of political goals have aroused Japanese interest in the development of an informal grouping of advanced Pacific nations.

C. Japan will continue to rely primarily on the US for its strategic security. In relations with the US, Okinawa is likely to continue as a troublesome problem, but we foresee no effective opposition in Japan to the continued application of the US-Japan Security Treaty past 1970. During the next five years, Japan will probably not decide to develop nuclear weapons but it will keep the option open. It will also improve its conventional military capabilities, particularly its air and sea defense forces.

¹ The Director of Intelligence and Research, Department of State, believes that paragraph A greatly underestimates the probable significance of the political role Japan will play in the next decade.

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D. Japan will probably avoid direct military involvement in efforts to "contain" communism; in certain circumstances, however, the Japanese might be willing to accept a limited measure of responsibility for the defense of lines of communication in the Northeast Asian area.

E. Japan sees Communist China as a long-range competitor for influence in East Asia, but the Japanese will continue to avoid unnecessary provocation of Peking while working, mainly through economic means, to limit its influence. In the Japanese view, security in Asia can best be insured by the development in Peking of a less militant and more realistic view of the outside world; Japan will attempt to foster any such tendencies in China, taking care not to impair its own relationship with the US.

F. Japan will seek to expand its influence in South Korea and Taiwan, and in Southeast Asia, but its interests in the latter region are less compelling. Japan is reluctant to become deeply involved in the region's political turbulence, considers that security there is primarily the responsibility of the US, and is aware that Southeast Asia trade is not critically important to Japan's economy. Japan's most likely course for the next few years will be to continue its present emphasis on economic assistance; its role in the political field will probably grow but it will still move carefully, applying its influence in support of stability and regional cooperation.

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DISCUSSION

I. INTRODUCTION

1. The basic direction of Japan's foreign policy is unlikely to change over the next 5 to 10 years: Japan will continue to rely on the US for military security and to identify its basic interests with those of the US and the Free World in general. This policy is rooted in Japan's self-interest as seen by its ruling conservative leaders and by most moderate political elements, and is supported by a substantial majority of the population. Within this established framework, however, Japan is likely to become progressively more assertive in world and regional affairs, to take more initiatives in developing and protecting its national interests, and to be less restrained than formerly by pacifist and other emotions generated by World War II.

2. This outlook is already evident in the conduct of Japan's external relations. It is partly a result of the passage of time since the war and the rebirth of pride in being Japanese. Of equal importance, perhaps, is Japan's increasingly eminent position in the world economic community.² This has led Japanese leaders to assume growing international responsibilities in matters of trade liberalization, monetary affairs, and assistance to less developed countries. It has provided them with important leverage in the conduct of affairs with larger nations. And, inevitably, it will lead them toward a greater concern with political developments in areas of major interest to Japan.

3. The Japanese Government is opposed to the spread of Communist influence in Asia. As a matter of general policy, however, Japan is likely to avoid heavy involvement in efforts having as their declared purpose the containment of communism. Many Japanese, including some conservative leaders, do not see a direct Communist military threat to Japan at this time. With regard to the USSR, there is suspicion of its ultimate ambition in Northeast Asia but the Japanese, sure of the US umbrella, are relatively confident that the Soviets will not resort to force to achieve their objectives. It is generally believed in Japan that Soviet leaders will maintain their friendly pose in hopes of weaning Japan from the US alliance and preventing a closer Japanese relationship with Peking, as well as to keep open the possibility of developing an expanded Soviet-Japanese economic relationship.

4. Concern about Communist China has been growing recently, but few Japanese leaders expect a Chinese military attack on Japan. There is some appre-

²In terms of purchasing power of gross national product (GNP), Japan now ranks above France and the UK and is on the verge of overtaking West Germany to become the world's third most productive nation (after the US and USSR). In volume of international trade, it will surpass Canada and France and move into fourth place in the early 1970's (after the US, West Germany, and the UK). In the early 1980's, the people of Japan will probably achieve living standards comparable to those of the more advanced Western European countries. (See table and graph at Annex for 1966 Japanese trade statistics.)

hension over the potentialities of China's massive armies, but little respect for its air or sea arms. China's recent progress in the development of nuclear weapons and delivery systems is causing concern among some informed Japanese, and the radicalism of the Chinese cultural revolution has had a disillusioning effect on Japanese generally. To the extent that there is concern in Japan over the Chinese military threat in the near term, it is now chiefly in terms of the possibility of war between China and the US in which Japan, with its US bases, might somehow become involved. This accounts in large part for the sensitivity of the Japanese to US military actions in Southeast Asia or elsewhere which might conceivably provoke Peking to fight. There is also growing concern that once the Chinese amass a nuclear arsenal, they will attempt nuclear blackmail.

5. There are other important reasons for continued reluctance in Japan to participate in military containment efforts in East Asia and elsewhere in the world. Japanese leaders are extremely sensitive over the health of an economy so dependent on foreign trade, and they are unlikely to pursue courses of action which might jeopardize profitable markets and critical sources of supply. Moreover, the Japanese people in general do not yet share their leaders' interest in assuming responsibilities overseas. There are still psychological restraints on political activity in Southeast Asia resulting from the war, but more important today are Japanese popular concerns with domestic needs. Despite Japan's brilliant economic performance, living standards in general are still below those of Western Europe and the populace is well aware of this. The discrepancy is particularly obvious in the public sector of the economy; roads, housing, and sanitation facilities are grossly inadequate, and there is considerable pressure on the government to raise budgetary expenditures to meet these needs. Finally, the very success of Japan's domestic and foreign policies in the past decade make for inertia and a reluctance to entertain very significant shifts of resources to defense or foreign aid.

II. THE ESTIMATE

A. General

6. In the following estimate, we start from the judgment that Japanese foreign policies will evolve in the context of continued conservative political predominance in a generally favorable economic environment, with high rates of economic growth likely through the early 1970's. We believe, in short, that the "mainstream" factions of the Liberal-Democratic Party will maintain their position of dominance for at least the next several years. After that, even if they should lose their commanding majority, power would probably pass to a moderate centrist coalition rather than to a Marxian Socialist government bent on drastic changes in domestic and foreign policy.

7. There are, of course, many external variables which could significantly affect our estimates: major changes in the US defense posture in the western Pacific; strong protectionist trends in US trade policy; worldwide constriction of markets brought on, for example, by a general economic depression; significant

changes in Communist China's attitude toward its neighbors; or increased belligerence on the part of the Soviet Union in the Far East. The implications of such contingencies are considered in this estimate.

B. National Security and the US Alliance

8. Despite the absence of any feeling of an imminent direct threat to their security, the leaders of Japan—as they contemplate the Communist giants on the Asian mainland—are sensible of the need for a powerful military protector. They prefer to see the US take this role. They also see the military alliance as an essential component in the complex of bilateral arrangements—political and economic—which have proven advantageous for almost two decades. Maintenance of these arrangements is strongly favored by the conservative leadership and by most middle-of-the-road political elements in Japan. We foresee no effective opposition, therefore, to the continued application of the US-Japan Security Treaty past 1970.³

9. The most troublesome problem in the security field is the status of Okinawa. National feeling against US occupation of the Ryukyus continues to grow and will in time cause the Japanese Government to press even more strongly for the return of complete administrative control. Prime Minister Sato has virtually committed himself before the electorate to obtaining, within the next few years, at least a timetable for “reversion.” The Japanese may accept reversion under terms which would not bring US bases in the Ryukyus under the same restrictions as those imposed on US bases in the home islands—i.e., no nuclear weapons and prior consultation on major military deployments. Japanese attitudes in this connection will be greatly affected by the overall military environment in the western Pacific; a relatively peaceful situation would probably accelerate demands for reversion without special privileges. In any case, the Okinawa issue will probably be the most difficult problem in US-Japanese relations over the next few years. The US bases in Japan proper are no longer an important political issue, though they are seen by some Japanese as an embarrassing remnant of the Occupation and hence do constitute a residual irritant in bilateral relations.

10. During the next few years, it is probable that considerations of self-respect and national prestige as well as defense needs will lead the Japanese to improve their conventional military capabilities. The emphasis will be upon the development of air and sea defenses for the home islands. Japan will strive to become increasingly self-sufficient in the production of conventional armaments, not only for military and prestige reasons, but to save foreign exchange and establish new export lines.

11. We do not believe that Japan will make a firm decision during the next five years to develop nuclear weapons systems. Japanese nuclear “allergies” are

³The “Treaty of Mutual Cooperation and Security” became effective on 23 June 1960. Its term is indefinite, but after 10 years either party may terminate it after one year's notice.

weakening, but they are still very strong. In addition, Japan could not utilize its existing nuclear facilities for weapons research and production without breaking a series of international agreements, including the projected nuclear non-proliferation treaty. Another obstacle would be the very limited supplies of high-grade uranium deposits in Japan and the difficulty of procuring sufficient unsafeguarded supplies from abroad. In any case, so long as the US alliance remains firm and the US discourages Japanese acquisition of nuclear weapons, it would be difficult for proponents of Japanese nuclear armament to justify publicly the heavy expenditures, although these would be well within Japanese economic capabilities.

12. The Japanese will not, however, foreclose the option to develop nuclear weapons systems. Continuing technological advances in the field of space rocketry will make the production of delivery vehicles progressively easier. The Japanese already have experience in building nuclear reactors for power generation and have an impressive supporting technological base. They have plans to build more power reactors and chemical separation facilities to process the plutonium produced in such reactors. Recent Japanese studies have indicated to them a probable future need for an independent capability to produce enriched uranium fuel. Such facilities, though designed for civilian needs could, of course, produce material for weapons.

13. *Contingencies.* In certain contingencies, Japan might give serious consideration to the development of nuclear weapons. For example, failure to achieve effective nuclear nonproliferation agreements and the acquisition of nuclear weapons by India would probably encourage some Japanese nationalists to demand nuclear weapons. It is unlikely that the Japanese Government would accede to these demands. If it did, any nuclear weapons program undertaken in these circumstances would probably be a relatively limited one, designed more for prestige than to meet overall defense requirements. It would not be intended to supplant Japanese reliance on the US for strategic security.

14. The Japanese might consider the acquisition of a nuclear capability if concern over Communist military strength in East Asia were to become much greater than at present. This situation could result from an unexpectedly rapid and extensive missile deployment by the Chinese, coupled with the adoption of a policy of nuclear blackmail by a self-confident Peking regime. It might also stem from a Sino-Soviet rapprochement (admittedly most unlikely at this stage) which appeared to include renewed cooperation between their military forces.

15. In calculating their course of action under such circumstances, Japanese leaders would be acutely sensitive to any evidence of a weakening in US determination to defend the area. This applies both to the maintenance of US forces in the northern Pacific and to the credibility of US nuclear protection. If such evidence appeared, the Japanese would probably feel compelled to review their entire security position. Neutralist alternatives might be considered. An unarmed neutralism would almost certainly be rejected; the Japanese leadership recognizes the perils, consequently the impracticality, of unarmed neutrality in

the volatile East Asian environment. Neutralism founded on a strong, nuclear-armed, and independent Japanese military establishment would have greater appeal, but we believe that this alternative would only be adopted as a last resort. Japan's leaders would appreciate the severe domestic political and economic problems involved in providing entirely for their own defense: vastly increased military expenditures, crossing of the nuclear weapons threshold, conscription and, possibly, amendment of the "no war" constitution. In overseas relations too, it is recognized that a military buildup of the required proportions would be detrimental to Japan's longer range interests, causing mistrust among the non-Communist nations of East Asia and sharpening the hostility of the Communist states. We believe, therefore, that in the face of an enlarged Soviet or Chinese Communist military threat, Japan would probably seek reaffirmation of US security commitments. Meanwhile, acting with prudence, Japan would accelerate the buildup of its own conventional forces and perhaps initiate a limited or shared nuclear weapons program.

16. Alternatively, should the Chinese Communist threat appear to diminish, Japanese interest in nuclear weapons would probably lag and many might be attracted by the idea of reducing or cutting "unnecessary" defense ties with the US. They might see this as conducive to gaining an influential and profitable role for Japan in China's struggle toward political and economic maturity. In our view, however, such reasoning would probably not prevail in Japanese Government circles. Tokyo would certainly wish to exploit fully any commercial opportunities on the mainland and to improve political relations. If circumstances were favorable, the Japanese would also try to promote a US-Chinese rapprochement. In any event, however, the Japanese would not wish to damage the established and highly advantageous political and economic relationship with the US. This relationship, in which the US consistently accounts for some 30 percent of Japan's trade, may be as compelling as its security requirements in guaranteeing Japan's continued desire to align itself with the US.

17. Certain economic contingencies may be of vital importance in the context of the US-Japanese security relationship. A major return to protectionism in US trade policy would greatly upset the Japanese. While it might not have a critical impact on the Japanese economy, there would be strong resentment against the US which might lead to a loosening in political ties. Simultaneous protectionist trends in Western Europe would further strengthen the arguments of those calling for a reassessment of Japan's Free World alignment. A severe depression in the US or Western Europe could lead to an economic crisis in Japan and, in turn, to increased political strength for extremists of both left and right.

C. Japan in Asia

18. *China* is, of course, the central problem for Japan in Asia. Japan is concerned to contain China's influence within its present limits. But as indicated above, Japan will rely mainly on US military power to give effect to the military aspects of this policy of containment. We do not envision a Japanese contribution of land forces to a conflict which might develop in Northeast Asia within

the next five years or so. However, it is possible that Japanese air and sea units would accept a measure of responsibility for the defense of lines of communication in and around Japan, Okinawa, South Korea, and perhaps Taiwan.

19. In the prevailing Japanese view, prospects for peace in Asia can best be advanced by avoiding provocation of Communist China while promoting trade and other contacts. There are other, more direct Japanese approaches to the China problem. Japan has become, and almost certainly hopes to remain, China's leading trading partner (although China accounts for only about three percent of Japan's total trade). While the profit motive is predominant in Japanese business circles, some Japanese leaders view economic interchange with Communist China as a contribution to the "pacification" of Peking. In time, it is hoped, China will abandon its unmitigated hostility toward the outside world and adopt more realistic attitudes on the pattern of the USSR. And certainly, if Peking should adopt a less militant policy and if there appeared to be prospects for a significant expansion of trade, pressure in Japan for the establishment of full relations with Peking would increase.

20. At the same time, Japan sees China as a probable long-range competitor throughout East Asia and is taking advantage of China's current infirmities to entrench itself in the markets of this region, hoping thereby to diminish China's political as well as its economic prospects. It seems clear that some Japanese leaders view their nation as uniquely qualified to provide the sort of leadership which the underdeveloped nations of East and Southeast Asia require to attain economic and political stability.

21. *South Korea and Taiwan* are strategically and historically of overriding importance to Japan. In each case, Japan has overtaken the US as leading trading partner, and will probably take the lead as a provider of economic assistance in a few years. In the ROK, Japan already exerts some covert influence on behalf of political elements favorable to its commercial interests. In official channels, there are bilateral working arrangements in matters of defense, intelligence, and internal security. These ties will grow, although traditional Korean distrust of the Japanese will compel both governments to move cautiously. In Taiwan, the situation is roughly similar, with close personal relationships helping to smooth the way toward establishment of a special position for the Japanese.

22. Japan's interests in the more distant lands of *Southeast Asia* are less compelling. Trade is important; Japan ranks at or near the top as a trading partner in every country. But this trade amounts to only about 10 percent of Japan's total, and there is widespread awareness in Japan that Southeast Asia is not central to the nation's prosperity. Continued rapid expansion of Japanese trade requires developed markets, and Southeast Asia with its low purchasing power is unlikely to become of great importance to the Japanese economy for many years. Moreover, the raw materials production of Southeast Asia is increasingly inadequate to Japan's industrial needs.

23. Japan's political interest in the area is likely to grow, even if its economic involvements remain relatively moderate. Developments in Southeast Asia will

probably offer broad opportunities to exert political influence, both in regional affairs and within specific countries. Nevertheless, Japan's most likely course for the next few years will be to continue its present emphasis on bilateral and multilateral economic aid, while moving slowly in the political field to apply its influence in support of stability and regional cooperation. Security in the region will still be viewed as primarily the responsibility of the US. There will also be an unwillingness to become deeply involved in the region's political turbulence lest such activity reawaken fears of Japanese domination, prejudice commercial interests in the area, and mar Japan's political prestige on the world scene.

24. Among the countries of Southeast Asia, *Indonesia* may offer the greatest attraction to Japan. It is the largest, most strategically situated, and richest in resources of the countries in the region. It is also actively encouraging foreign investment. In addition, neither the US nor any Western European nation yet holds the inside political and economic track in Djakarta. It remains politically unstable, however, and a long-term petitioner for foreign assistance. Japan will be willing to continue, along with the US, as a major provider of economic assistance to Indonesia. The Japanese are still reluctant to commit themselves to an influential role in Indonesia's internal and external affairs, but this reluctance may diminish in time.

25. *Vietnam* will remain an area of acute Japanese concern at least until the situation there is resolved. Although Japan has no intention of becoming militarily involved, the government should not have difficulty withstanding press and opposition criticism of its support for US policy (so long as the situation there does not change radically for the worse) and will continue to attempt to play a role in promoting negotiations. As an ultimate solution, Japan would probably support neutralization of the Indochina area, coupled with provisions designed to prevent a recurrence of the war. Japan might be willing to participate in truce supervision in a nonmilitary capacity and is prepared to assist in postwar reconstruction both in the South and North.

26. Further afield, in the subcontinent—*India, Pakistan, and Ceylon*—Japanese interests are likely to remain strictly economic. This might change in the event of a greatly heightened Chinese military threat throughout East Asia, which would tend to draw Japan toward some sort of modest cooperation with India. Even in this instance, it is unlikely that the Japanese would seek any close political or security alignment with the Indians, whom they tend to view as relatively impotent militarily, disorganized politically, and economically unpromising. There is, in addition, no important body of thought in Japan which deems the subcontinent relevant to Japan's security position.

D. The "Pacific Community"

27. Japan's most vital economic interests are focused in North America and the western Pacific. The US is overwhelmingly Japan's most important trading partner. Far behind, but in second place, is Australia. Canada is third. In

total, these three countries supply 40 percent of Japan's imports, and purchase only a slightly smaller proportion of its exports. Trade with Australia and New Zealand could increase significantly if Britain enters the European Common Market and Commonwealth nations lose their preferential trade arrangements with the UK. Awareness is also growing in Japan of the untapped raw material potential in Australia, Canada, and, most recently, Alaska. These economic prospects, as well as an increased similarity of political interests, have aroused Japanese interest in the development of a community of advanced Pacific nations—the US, Canada, Australia, New Zealand, and Japan.

28. Though still vague in concept, this grouping of politically stable areas connected by safe lines of communication is viewed by some Japanese as a counterweight to the EEC and other Atlantic Community economic organizations, which Japan fears may ultimately work to its economic disadvantage.⁴ The Japanese also regard this concept as a useful device in countering any isolationist trends that might grow in the US. Moreover, the Japanese policy-makers see the grouping as useful in assuring the participation of the several wealthy Pacific nations in the task of furnishing economic aid to Southeast Asia.

29. The Japanese will probably devote important diplomatic efforts over the next 5 or 10 years to the cementing of friendly relationships with these countries, though they will probably not press, in the short run, for a formal political organization of the community. We also doubt that Japan will seek a formal security pact within this community, as the US-Japan Security Treaty and the ANZUS pact are sufficient from the Japanese viewpoint.

E. Elsewhere in the World

30. Japan has little interest in exerting influence in the political affairs of such relatively remote areas as *Latin America, the Middle East, and Africa*. We do not foresee any real change in this attitude for some time to come. There is an unwillingness to risk antagonizing potential customers and suppliers by taking sides in any dispute not directly affecting Japan's security. These regions together account for only about 18 percent of Japanese trade and are not of critical economic importance, with the notable exception of the Persian Gulf, which supplies some 90 percent of Japan's crude petroleum imports.

31. *Europe* is of increasing economic importance to Japan because of its potential as an export market and source of capital. Relations with Europe are strongly influenced by Japan's desire to be recognized as a full member of the "club" of advanced industrial nations.

⁴The basis of the Pacific community already exists to some degree in prevailing trade and investment patterns. Japan's top three trading partners, as noted above, are the US, Australia, and Canada. Japan ranks as second among US trading partners, third among those of Canada and Australia, and fourth for New Zealand.

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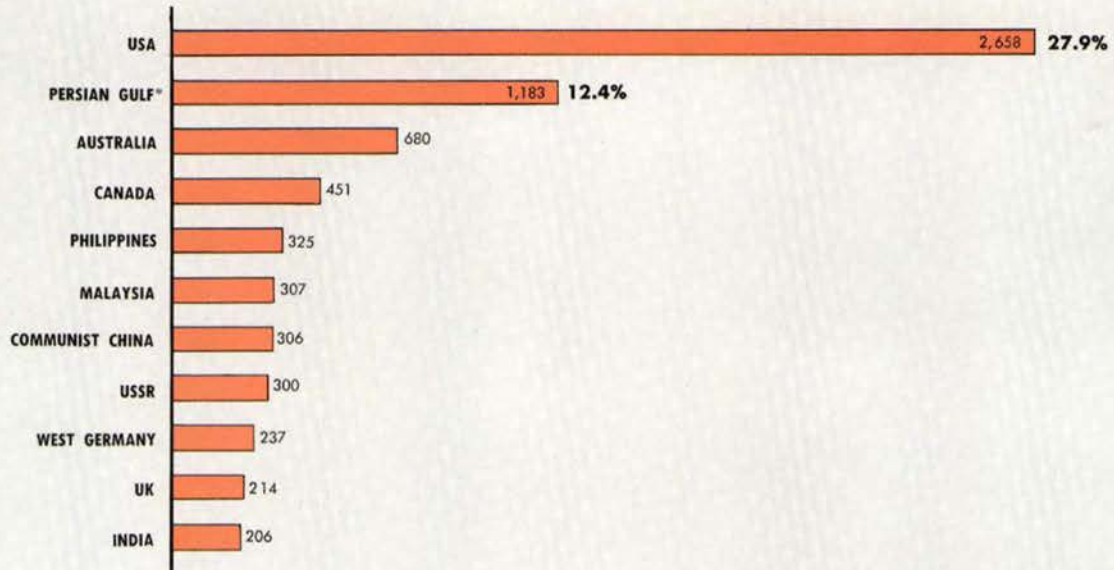
32. *The USSR.* With both sides agreed on the advantages of peaceful relations, the Japanese-Soviet detente seems likely to continue over the next five years. Over the longer run, however, the range of rapprochement is limited on the Japanese side by the conservative Japanese leadership's antipathy toward communism and its continuing mistrust of Soviet intentions in East Asia, and on the Soviet side by opposition to any expansion of Japan's role in Asia which tended to further the Western orientation of nations in the area. Other irritants which will continue to inhibit closer relations are Japanese territorial claims against the Soviet Union, Japanese support for US policy and operations in Southeast Asia, and the continuing Soviet propensity to involve themselves in what the Japanese construe as Japan's internal affairs.

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JAPAN'S MAJOR SUPPLIERS, 1966

(in millions of dollars)

WORLD TOTAL \$9,523 (100.0%)



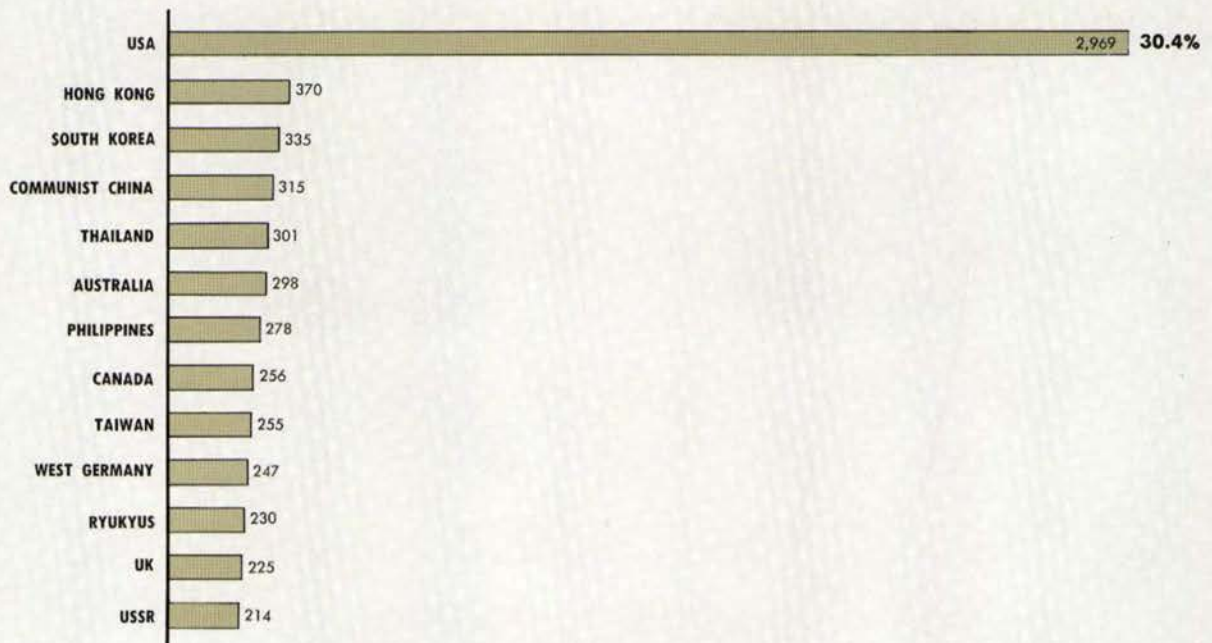
*Includes Iran (362), Kuwait (290), Saudi Arabia-Kuwait Neutral Zone (186), Saudi Arabia (247), Iraq (67), Bahrain (10), Trucial Oman and Qatar (21); imports are almost entirely petroleum.

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JAPAN'S MAJOR MARKETS, 1966

(in millions of dollars)

WORLD TOTAL \$9,776 (100.0%)



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ANNEX

JAPAN'S TRADE, 1966 (In millions of dollars)

COUNTRY OR AREA	EXPORTS (FOB)	IMPORTS (CIF)	TOTAL TRADE	
				Percent
WORLD TOTAL	9,776	9,523	19,299	(100.0)
North America	3,503	3,444	6,947	(36.0)
US	2,969	2,658	5,627	(29.2)
Canada	256	451	707	
Mexico	50	178	228	
Other	228	157	385	
South America	279	446	725	(3.8)
Africa	729	420	1,149	(6.0)
South Africa	127	133	260	
Other	602	287	889	
Europe	1,575	1,216	2,791	(14.4)
USSR	214	300	514	
Other Communist	99	50	149	
West Germany	247	237	484	
UK	225	214	439	
Other Non-Communist	790	415	1,205	
Southwest Asia	332	1,213	1,545	(8.0)
Iran	72	362	434	
Other Persian Gulf	171	821	992	
Other	89	30	119	
South Asia	308	248	556	(2.9)
India	167	206	373	
Pakistan	100	31	131	
Other	41	11	52	
Australasia	399	832	1,231	(6.4)
Australia	298	680	978	
New Zealand	59	113	172	
Pacific Islands	42	39	81	

Footnotes are at end of table.

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JAPAN'S TRADE, 1966 (Continued)
(In millions of dollars)

<u>COUNTRY OR AREA</u>	<u>EXPORTS (FOB)</u>	<u>IMPORTS (CIF)</u>	<u>TOTAL TRADE</u>
			<i>Percent</i>
<u>Southeast Asia</u>	<u>1,139</u>	<u>1,029</u>	<u>2,168 (11.2)</u>
North Vietnam	6	10	16
South Vietnam	138	5	143
Laos	3	"	3
Cambodia	12	7	19
Thailand	301	153	454
Burma	47	15	62
Malaysia	89	307	396
Singapore	143	30	173
Philippines	278	325	603
Indonesia	119	176	295
Other	3	"	3
<u>Northeast Asia</u>	<u>1,510</u>	<u>674</u>	<u>2,184 (11.3)</u>
Ryukyus	230	79	309
South Korea	335	72	407
Taiwan	255	147	402
Hong Kong	370	47	417
Communist China	315	306	621
North Korea	5	23	28
Mongolia	"	"	"

Source: Japan. Ministry of Finance. Customs Bureau.

" Less than \$1 million.

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