

#### 4. PRIME MINISTER FUKUDA'S SUMMITS, 1977-1978

##### A. The 1977 London Summit

In December 1976, Miki was replaced by Takeo Fukuda due in part to a severe electoral setback suffered by the LDP as a result of the Lockheed scandal. Fukuda soon initiated communications with US President-elect Jimmy Carter and he agreed to take part in the next summit.<sup>83</sup> Two days before these mid-January conversations, Tokyo had held an emergency Cabinet meeting in which the EPA-suggested 6.7% growth target for JFY 1977 had been approved. In responding to US pressure for Japanese cooperation in world economic expansion, Fukuda presented this figure to Carter. It was reaffirmed when Vice President Mondale visited Japan at the end of January. The road leading to the "locomotive theory" that would call on three "engines" -- the US, West Germany and Japan -- to reflate their economies was now paved.

A more complex issue which arose prior to London was also first approached in a bilateral manner. Japan's nuclear energy program was being threatened by Carter's anti-nuclear stance.<sup>84</sup> A majority of Japanese nuclear power plants used American-type reactors whose fuels were mainly purchased from the US. Besides, processing the spent uranium required the approval of the US under the US-Japan Nuclear Power Agreement. The Carter Administration, however, was taking the position of curtailing the growth of fast breeder reactors and nuclear fuel reprocessing abroad for fear of the proliferation of nuclear weapons. If Carter prevailed, the US attitude would be a great impediment to Japan's future energy projects. Specifically, the Japanese government's Tokaimura nuclear power station which had taken 10 years and 30 billion yen to complete would be jeopardized. The nuclear fuel reprocessing plan, with an estimated budget of 2.4 trillion yen over twenty years, would be deadlocked. The Carter-Fukuda bilateral summit in late March took place in the midst of this controversy.

The meeting proved to be a preparation for the May London summit as well as an occasion to discuss pressing bilateral issues.<sup>85</sup> The two leaders reaffirmed their two countries' roles as "locomotive engines", although the 6.7% growth target for Japan was not mentioned in the joint statement. They also renewed their pledge to contribute to the successful conclusion of the GATT Tokyo Round as soon as possible, and welcomed the holding of the upcoming London summit. The nuclear energy issue was not, however, solved. It was shelved. The US consented to pay sufficient attention to Japan's energy needs when formulating its own nuclear energy policy. However, the Japanese strategy of reprocessing plutonium for its reactors was not endorsed by Washington. The American wish to freeze reprocessing of spent nuclear-fuel was underlined by the outcome of the meeting.

Other issues also emerged prior to the London summit. US-Japan trade frictions became increasingly apparent.<sup>86</sup> Japanese exports to the US totaled \$15 billion. This prompted Carter to express his hope of reaching an agreement on import quotas for Japanese colour television sets, implying the Japanese application of VERs. Not only exports to the US but also the Japanese trade and current account surpluses were too large to avoid criticism from such deficit countries as the UK, Italy and France. The Japan-EC trade conflict, which had erupted in the fall of 1976 with bitter accusations made against the visiting Keidanren group, had abated somewhat, but were not yet over. Not surprisingly, Japan had taken some steps to make its policies more congruent with what

would be expected at the London summit. The BOJ had lowered its official discount rate to 5.0% in April -- now lower than the 5.5% of the US, though higher than West Germany's 3.5%. A number of expansionary fiscal policies had been adopted, including a JFY 1977 budget 17.4% higher than the previous year's. Public works spending had been raised 21.4%. A small tax reduction (432 billion Yen) amounting to 2% of the total budget had been introduced. The yen had appreciated from 300 yen to the dollar around the time of Puerto Rico to the 277 yen level by the end of April, partly due to the *laissez-faire* policy of the central government. These measures were largely intended to serve domestic needs. However, the external pressure perceived to be growing against Japan was also a driving force. The summit was seen to be the possible occasion for the concentration of external pressures against "surplus Japan".

Having laid the ground for the summit by consulting with the major government ministries, Fukuda summarized the government's positions.<sup>87</sup> In order to lift the world economy out of its recession, Japan would play the role of "engine" by attaining its real GNP target of 6.7% that year and increasing domestic demand to rectify the external imbalance. It would request deficit countries to make equal efforts to redress the international balance of payments problems. But Fukuda denied the possibility of taking additional steps, on the grounds that the then stimulative measures were enough. Like Miki, he showed enthusiasm for the trade issue; the free trade principles and efforts to conclude the GATT MTN within the year were stressed. The North-South problem and related aid policy were also main concerns. Fukuda hoped to double ODA over the succeeding five years. He also approved of the "Common Fund" idea to help stabilize raw material prices. This was a significant shift from Miki's former disapproval of the proposal. On the nuclear energy issue, Japan would prevent nuclear proliferation and stick to the peaceful use of nuclear resources, especially as it was the only country that had experienced the A-bomb.

After having established its basic stance prior to the summit, there emerged a curious half-hearted turnaround by the government. The Japanese were sensitive to external pressures and responded to media reports issued prior to the summit. These news reports informed the government that the Americans and Germans were swiftly shifting their economic emphasis from expansionist economic policies to anti-inflationary policies. Lest Japan should be greatly out of step with these policy changes, Fukuda directed the EPA to come up with some measures to curtail the rise of consumer prices. The EPA produced a six-point proposal to restrain inflation by strengthened surveillance of the BOJ's money supply, reduction of oil purchases by better energy saving, and a return on the profits created by the yen's appreciation to the consumers. The Fukuda regime seemed to be more susceptible to external pressure in formulating Japanese economic policies than the Miki regime had been. Changed international economic circumstances -- notably the widened economic gap between the strong and the weak among the summit members -- made Tokyo even more alert to the demands made on Japan. Avoidance of all-out criticism of Japan, particularly on its trade policies, was the top priority. The US approval of Japan's plutonium-reprocessing project was earnestly needed to secure the operation of the Tokaimura power station. In light of the upcoming House of Councillor elections, a solution of the energy dispute was more than desirable.

More substantive discussion and a less harmonious but more specific outcome emerged at London than at the previous two summits.<sup>88</sup> The conflicts of interest were more pronounced in these discussions. The case in point for Japan was in the area of trade. Fukuda's warning against rising protectionism took the form of an explicit rejection of

protectionism in the final communiqué. However, there were some positions that Japan lost. French and British trade interests differed from those of Japan. The French insisted on inserting the phrase "organized market" into the communiqué so that the market share of competitive economies in markets sensitive to France would be checked. Although the French phrase was not inserted, France and the other weak economies were successful in inserting the assertion that "...structural changes in the world economy must be taken into account" in making substantive progress in key areas of the GATT Tokyo Round MTN in 1977. Indeed, a de facto concession on the phraseology with regard to the GATT trade talks at Geneva was taken at the expense of Japan. Fukuda's proposal to conclude the agreement on a tariff reduction formula in the Tokyo Round MTN by September 1977 met opposition. Besides, the Japanese attempt to include in the communiqué the OECD trade pledge to "avoid the imposition of new trade barriers," which had been enunciated in the Rambouillet statement and Puerto Rico declaration, was aborted by Franco-British resistance. Although not overly negative, the communiqué was perceived by the Japanese to reflect the strength of the prevalent feeling of the French and British delegates. The responsibility of a surplus country was to create the environment for making free trade viable. In meeting with Fukuda after the summit, British Prime Minister Callaghan requested Japan to do its best to correct the trade surplus by citing the problem of a growing Japanese market share in the British shipbuilding industry.

These divergent economic interests were accentuated by macroeconomic issues.<sup>89</sup> Polarization between the strong economies, represented by the US, Japan and West Germany, and the weak deficit countries, of the UK, Italy and France, was increasingly visible. Japan and West Germany were singled out by the UK as carrying a responsibility created by their surplus country status. Requests for economic expansion led by domestic expansion instead of export drives were made by other nations as well. In response, Fukuda emphasized the importance of international collaboration among the summiteers and the existence of international organizations to help the world economy recover. Explaining the measures taken by his government to attain 6.7% economic growth, he acknowledged the "locomotive strategy" for his country and expressed a willingness to play a responsible role as a surplus country. His citation of personal experiences during the Great Depression impressed Helmut Schmidt. Japan's appreciated yen was unanimously welcomed by all summiteers. Though no specific figures were included in the communiqué, because of German and Japanese objections, Japan's promise to achieve its GNP target of 6.7% was reinforced and made as a multilateral pledge at London. The communiqué committed the summiteers to "stated economic growth targets or to stabilization policies which, taken as a whole, should provide a basis for sustained noninflationary growth" in the summit nations and elsewhere in the world and "for reduction of imbalances in international payments". In the appendix to the communiqué, furthermore, Japan, though not named, was urged to "adopt further policies, if needed to achieve [the] stated target rates and to contribute to the adjustment of payment imbalances". Fukuda's \$700 million deficit projection for JFY 1977 included in his explanation seemed not to have convinced the other governments that no further measures would be needed.<sup>90</sup>

With West German acquiescence, the setting of macroeconomic targets became a great concrete accomplishment at London. The conclusion of the energy issue however, was to prove more turbulent. The gap in perceptions between the Americans, who cautioned against the danger of spreading nuclear technology, and the French and Germans, who depended on nuclear energy development for future energy supplies, was not narrowed. The vocal conflicts between the US participants and the German and French delegates

overshadowed the Japanese position on energy. But the Japanese largely took side with the West Germans in pressing for a change in American inflexibility on the issue. At a bilateral meeting, Fukuda could not obtain an explicit go-ahead from Carter for Japan's nuclear fuel reprocessing scheme. The communiqué admitted "the need to increase nuclear energy" while expressing the summit's consensus of "reducing the risks of nuclear proliferation". The solution of the nuclear energy issue was put off with the formation of a study group assigned to work out an acceptable solution to the problem. The communiqué mirrored a "procedural compromise", and Fukuda judged the outcome as having "neither plus nor minus impact in the Japanese position."<sup>91</sup> The Tokaimura power plant issue was to be settled by negotiations in September.

There was a breakthrough made in the North-South problem at Number 10 Downing Street. The summit indicated its support for "a successful conclusion of the C.I.E.C. (Conference on International Economic Cooperation). "It also endorsed the idea of "the creation of a common fund for individual buffer-stock agreements" with a view to commodity price stabilization. The Japanese change on the "common fund" before the summit made Japan amenable to this suggestion. In retrospect, however, the impetus given at the summit was not enough, even though Japan remained faithful to its pledge.<sup>92</sup> The CIEC on June 30 was stalemated with no tangible results. The endorsement for the "Common Fund" proposal was reaffirmed at Bonn and an agreement to set up the Fund was reached in June 1980. But only Japan and the UK among the Seven ratified the agreement, which was still pending prior to the 1982 Versailles summit.

At the post-summit press conference, Fukuda, like his predecessor Miki, downplayed any disharmony at the summit. He chose instead to focus on the issues which had brought about a consensus.<sup>93</sup> Though he denied any direct condemnation of Japan's export-surplus problem, by the other delegates, he did perceive a critical mood mounting against Japan at London. Accordingly, he warned that Japan should prevent the "torrential export" of some Japanese goods that had happened the previous year. For him, the rejection of protectionism was a sign of cooperation and unity among the summiteers. However, he did not forget to add his pessimistic prediction that the GATT Tokyo Round negotiations would not be concluded by the end of 1977. He also made clear that he did not have to make a promise on ODA as he had originally hoped before London. Japan would constructively tackle the problem of primary products imports from developing countries and accumulated debts. But he stopped short of pledging an ODA increase at the summit.

The Zaikai was relieved to find that the principles of free trade had remained intact at London.<sup>94</sup> Business people lauded the agreements contained in the communiqué despite various arguments put forth during the sessions. They were acutely aware of the prevailing critical views on Japanese trade practices. They also knew that protectionist pressures would deprive Japan of precious markets. The Keidanren chief indicated his willingness to call for self-restraint in excessive exports by using every available opportunity. The 6.7% GNP growth was generally accepted in the business circle as well. Some members, however, noted difficulties in being a "locomotive" designed to pull the world out of its economic stagnation, and placed more emphasis on controlling inflation. Some groups led by Keidanren were expected to call on the government to further lower interest rates.

The opposition parties maintained their overall negative response to summitry, but Komeito and the DSP toned down their criticisms. The JSP, DSP, and Komeito were most

displeased with the vague conclusion. The JSP scoffed at the less assertive Fukuda on the issues of energy and trade. Komeito recognized the significance of the efforts made at the summit to create a new world economic order, but observed that the summit did not come up with specific ways to tackle such pressing issues as the economy, trade and energy. Declaring support for "orderly exports" and enlarged aid to developing countries, it decided to watch closely how the government would translate the summit communiqué into concrete measures. The DSP was unhappy about the unresolved issue of nuclear fuel reprocessing, but called the formation of a study group "an achievement of the meeting". The Communists were furiously against the government as usual. The 6.7% economic growth objective and other promises made by Fukuda would impose a heavy burden on the working Japanese, they warned.

The press response was less supportive of the results of the meeting than it had been of those of the previous two summits.<sup>95</sup> The Mainichi was the most critical of Fukuda's performance at London. It was suspicious of the government's ability to achieve 6.7% real GNP growth without inducing inflation or exacerbating the budget deficit. It felt that Japan should base its long-term macroeconomic strategy on stable growth with energy conservation and anti-inflationary measures as pillars. This strategy should not be subordinated to the economic pledges at the summit, it cautioned. Moreover, it was not satisfied with the meager Japanese economic aid promised to developing countries and urged the government to do more; otherwise the accusation that "Japan earns by exporting but fails to give enough aid" would be directed at Japan. The Asahi took a neutral stand on Tokyo's conduct at the meeting. It stuck to merely reporting the facts of the summit meeting, although it implied its approval of the positive North-South dialogue, as well as the summit's implementation of an international management system of nuclear energy reprocessing.

The Yomiuri was ambivalent. While it recognized that there was no fundamental breakthrough in the issues discussed, it found it meaningful for the leaders to confront the difficulties of solving the issues. Considering that the last summit had made a serious misjudgment in predicting the world economic situation, Yomiuri recognized that this summit had a more "realistic" grasp of the international economic situation and endorsed the communiqué's goal of "creating more jobs while continuing to reduce inflation." Also, any retreat from free trade principles was a pity and should be resisted. However, Japan would be required not to provoke protectionism of the weak economies through its trade. Yomiuri admitted that there was some progress in the field of North-South relations. It also requested the government to honour the 6.7% growth pledge and to take the leadership in conserving energy.

The overall editorial content of the Nihon Keizai was the most plaintive. Now that the 6.7% economic growth became an "international pledge", it observed that the government would have to adjust its fiscal and other policies. Japan would also have to respond wisely to European attitudes toward Japan. The agreement to "make substantive progress" at the Tokyo Round MTNs was a boon to the free trade-oriented Japan, but more sectorally managed trade was gaining ground. Though finding the communiqué significant as a block to the Carter regime's forceful stance on nuclear energy reprocessing, it acknowledged the need for Japan to engage in multilateral negotiations with Europeans and Americans. In the end, the business paper cautioned that the Downing declaration would be nothing but a temporary gimmick unless adjustments in specific areas were followed through.

In hindsight, the London summit became the first summit to attempt a specified

macroeconomic policy coordination among the participating countries.<sup>96</sup> Summitry had also become institutionalized at London. As the discussion at the meeting shifted from general themes for harmony to specific issues aimed at solutions, the contradictory positions of summiters loomed large. For Japan, the summit process *per se* was successful in the sense that it could evade ostensible accusations from other countries. But the outcome did not help Fukuda domestically. Rather the international pledge of 6.7% GNP growth became more difficult as time went by. The pro-expansionist forces in Japan were encouraged and additional external pressure was exerted on Tokyo in the wake of the summit. For example, at the end of May, Keidanren president Doko pressed the government to stick to the fulfillment of 6.7% target even if a supplementary budget was necessary. US Secretary of Treasury Blumenthal asserted that Japan had consented not to resist market forces with regard to the rising value of the yen. The yen's value went up steadily, eroding the profits of Japanese exporters. But Japan's current-account growth was not deterred. Nor was the increasing US-Japan bilateral trade imbalance. By the time of the follow-up meeting in September, it became clear that Japan would be far below its target. As US-Japan trade relations reached an all time low, frustrations across the Pacific grew and the Fukuda regime was confronted with both domestic and international pressure to take drastic measures.

Indeed, the failure to fulfill Fukuda's pledges at London -- a 6.7% growth rate and a reduction of the current account surplus -- might have contributed to the worsening image of an "unfair Japan".<sup>97</sup> In the fall of 1977, the Fukuda regime took some actions to meet these pledges: a further rise in public-works expenditure, reduction of the discount rate and accelerated imports of crude oil, uranium and feed grains. These actions were not successful in stifling the growing criticism against Japan at the IMF annual meeting. Also, pressures to restrict Japanese imports were growing in the US Congress and in Europe. In addition, the Japanese economic growth continued to taper off. By October Japan's current account surplus totalled approximately \$7 billion instead of Fukuda's London estimate of a \$700 million deficit. The Americans exerted tremendous pressure in US-Japan trade talks in November. However, US Ambassador Mansfield felt that these US-Japan economic problems should not be allowed to become "politicized". At an OECD economic policy committee meeting in late November, it was reported that only the US was playing the role of "locomotive engine" among the major economies. Japan was apparently falling behind and its credibility was being doubted.

Japanese domestic actors were divided. The business community, alarmed by a strong yen that hit 250 yen to the dollar at the end of October, and fearful of a loss of export profits, allied with the expansion-oriented MITI and EPA. The stingy MOF saw exchange rate adjustment as better than a loosening of fiscal policy. The bureaucratic in-fighting became intense. Fukuda's reshuffle of his cabinet at the end of November tilted the balance of power toward the expansionist forces. It also gave the original Japanese sherpa, Nobuhiko Ushiba, the post of Minister for External Economic Affairs a newly-created portfolio designed specifically to cope with the urgent economic and trade issues. The results of these developments were Fukuda's promise of a large supplementary budget for the last quarter of JFY 1977 (January - March, 1978) as well as one of the most reflationary budgets for JFY 1978 in the history of fiscal policy in Japan.<sup>98</sup> Besides, the Strauss-Ushiba agreement, reached between the head of the United States Trade Representative Office (USTR) and the former Japanese sherpa for summitry, recorded an official commitment of a 7% GNP growth for Japan in JFY 1978 and settlement of substantive and procedural bilateral trade problems, including Japan's pledge of its renewed efforts to reduce its current account imbalance. The new economic growth target was hailed by the US. It would be reconfirmed at the next