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FOR PROFIT OR POWER?
THE STRATEGIC PURPOSE OF ECONOMIC EXCHANGE
IN THE U.S.-JAPAN GREAT POWER RIVALRY

VOLUME I

DISSERTATION

Presented in Partial Fulfillment of the Requirements for
the Degree Doctor of Philosophy in the Graduate
School of The Ohio State University

By

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* * * * *

The Ohio State University
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ABSTRACT

The political and economic motivation for and effects of economic exchange among great powers has received considerable attention in recent scholarship. The question of whether states induce or control this exchange for policy purposes has, however, not been examined sufficiently, nor has the importance of any one type of economic exchange been shown to influence state decision makers in accordance with prevailing theoretical perspectives. This dissertation argues that these shortcomings are due to incomplete specification of economic relations among great powers as well as inadequate attention to the relationship among the actors involved in exchange, state decision makers and the policy making process. Too often, the causal relationship between economic interactions and state policy calculation is normatively assumed instead of demonstrated, or is applied only to cases of great power allies or between a great power and a lesser power. Within much of this analysis, defensive or liberal state policy motivation is ascribed, tested for its validity and found to be insufficient in one or more ways. This dissertation remedies this condition by fully examining exchange in a crucial great power rivalry and reintroduces other, offensive, policy motivations and a means of better identifying the qualities of exchange. A more holistic conception of economic exchange is proffered, one that balances qualitative assessment of trade with investment and other financial relationships, in order to better identify overall benefits and vulnerability from exchange relations.
The U.S.-Japan, 1918-1941, case is compared against contending hypotheses from defensive and offensive realism, liberalism and marxism. In beginning the analysis during WWI, evaluation of the theories is more complete and allows for better interpretations of U.S. policy and its effects on Japan’s domestic and foreign policies. This interpretation of U.S.-Japan economic and strategic interaction improves upon much of the prevailing political science literature, and adds needed and often overlooked explanations for U.S. economic exchange with Japan. Specifically, this dissertation demonstrates that despite often self-serving corporate maneuverings, the U.S. government used exchange with Japan to fulfill its interwar grand strategy and maximize its relative position going into WWII.
To my mother Ann Carey Lehmann
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I wish to thank my advisor, Randall Schweller for his unwavering support, constructive criticism and encouragement over the last few years. His standard of critical inquiry is one that I have aspired to and one that keeps political science scholarship relevant to both historians and policy makers. I would also like to thank Bradley Richardson for introducing me to the complexities of Japanese politics, which helped stimulate my interest in this dissertation’s research. Professor Richardson’s keen sense of concept definition, measurement and significance were also instrumental to this dissertation’s research focus, and more broadly, to confirming my sense of purpose and the value of scholarship. I would also like to thank Raymond Lawton for his time and patience as I completed this project and fulfilled responsibilities at the National Regulatory Research Institute. His collegiality and interest in this work and other projects were instrumental to my capacity to finish this dissertation.

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# TABLE OF CONTENTS

<table>
<thead>
<tr>
<th>Title</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Abstract</td>
<td>ii</td>
</tr>
<tr>
<td>Dedication</td>
<td>iv</td>
</tr>
<tr>
<td>Acknowledgments</td>
<td>v</td>
</tr>
<tr>
<td>Vita</td>
<td>vii</td>
</tr>
<tr>
<td>List of Tables</td>
<td>xi</td>
</tr>
<tr>
<td>List of Figures</td>
<td>xiii</td>
</tr>
<tr>
<td>Chapters:</td>
<td></td>
</tr>
<tr>
<td>1. Introduction and Dissertation Purpose</td>
<td>1</td>
</tr>
<tr>
<td>1.1 Framing the Analysis of economic exchange</td>
<td>4</td>
</tr>
<tr>
<td>1.2 Methodology</td>
<td>12</td>
</tr>
<tr>
<td>1.3 Measurement of Independent and Dependent Variables</td>
<td>16</td>
</tr>
<tr>
<td>1.4 Characteristics of Exchange Instruments</td>
<td>29</td>
</tr>
<tr>
<td>1.5 Comparative Theory Review (defensive and offensive realism, liberalism and marxism)</td>
<td>33</td>
</tr>
<tr>
<td>2. Sovereignty and Exchange</td>
<td>64</td>
</tr>
<tr>
<td>2.1 Chapter Overview</td>
<td>64</td>
</tr>
<tr>
<td>2.2 Capabilities and Autonomy Effects from Foreign Economic Policy</td>
<td>65</td>
</tr>
<tr>
<td>2.3 Limits of Contemporary Exchange Analysis</td>
<td>71</td>
</tr>
<tr>
<td>2.4 Evaluating Exchange Relations (FDI, Trade, Loans, Bonds, Securities and Monetary Assets)</td>
<td>79</td>
</tr>
<tr>
<td>3. U.S.-Japan, 1918-1922</td>
<td>113</td>
</tr>
<tr>
<td>3.1 Case Introduction and Study Summary</td>
<td>113</td>
</tr>
<tr>
<td>3.2 Chapter Overview</td>
<td>120</td>
</tr>
<tr>
<td>3.3 Japanese Expansion during WWI and its Immediate Aftermath</td>
<td>123</td>
</tr>
<tr>
<td>3.4 Versailles Conference and the Russo-Chinese Resource Dimension</td>
<td>130</td>
</tr>
</tbody>
</table>

Reproduced with permission of the copyright owner. Further reproduction prohibited without permission.
3.5 U.S., Britain and the Netherlands: Oil Game and Japan.....................134
3.6 Washington Conference: Naval Arms, Political Order and Oil............147
3.7 U.S.-Japan Economic Exchange, 1918-1922........................................157


4.1 Chapter Overview.....................................................................................164
4.2 Post-Washington Conference: Decreased Threat and Broadened
Exchange.......................................................................................................167
4.3 Post-Washington Conference Widened Competition in Oil...............175
4.4 Failure and Aftermath of the 1927 Geneva Naval Talks: the
Anglo-American-Dutch Oil Peace.................................................................184
4.5 The China Dimension..............................................................................198
4.6 Fallout after Chang Tso-lin Assassination............................................205
4.7 U.S.-Japan Economic Exchange, 1923-1928..........................................209

5. U.S.-Japan, 1929-1933................................................................................216

5.1 Chapter Overview.....................................................................................216
5.2 Shidehara Diplomacy and the London Naval Treaty: Economic
Fealty to the West and Military Autonomy in China and Japan..............221
5.3 Unrest in Japan and Expansion in Manchuria........................................235
5.4 Anglo-American Division over the Manchurian Incident and Domestic
Disarray in Japan..........................................................................................240
5.5 Founding of Manchukuo and dualism in U.S. policy............................255
5.6 U.S.-Japan Economic Exchange, 1929-1932..........................................269
5.7 Summary: from Siberia intervention 1918 to Japan’s Withdrawal
from the League............................................................................................279


6.1 Chapter Overview.....................................................................................285
6.2 The Roosevelt Administration and Anglo-American Buckpassing.........290
6.3 Post-Amaw Statement: Britain and Russia Appease,
Dutch build bridge to America.................................................................301
6.4 Japan’s Movements toward Autonomy and America’s
Response.........................................................................................................310
6.5 The International Situation: Intended and Unintended
Consequences of Economic Alignments and America’s
Economic Policy............................................................................................332
6.6 U.S.-Japan Economic Exchange, 1933-1936..........................................348

7. U.S.-Japan 1937-1941.................................................................................357

7.1 Chapter Overview.....................................................................................357
7.2 Roosevelt Pacification Gambits and Japan’s Assault on China.............364
7.3 Casting About for an American Plan .............................................................377
7.4 The U.S. Position Firms as Japan Expands Against Britain and the Soviet Union .................................................................391
7.5 Japan Tacks South and Britain Bargains for America to Stem its Ebbing Resistance in Asia ..................................................416
7.6 America Squeezes Japan's Resources and Steps Up Japan's Strategic Encirclement ..........................................................433
7.7 Japan Secures its Northern Front, Expands South and Earns a U.S. Embargo .................................................................444
7.8 U.S.-Japanese Economic Exchange, 1937-1941 ..................................................................................................................461

8. Conclusions .................................................................................................................472
8.1 Overview of the Inquiry, Key Findings and Theory Evaluation ..................472
8.2 Relevance to and Implications for Previous Scholarship ...........................489
8.3 Realist Exchange Theory, Application to U.S. Interwar Policy and the Prospects for a Realist Peace ......................................495

Appendix A Causal Model; Exchange Instruments Chart; Theory Hypotheses and Observable Implications Charts ................................503
Appendix B U.S. Office of Naval Intelligence Diagrams ..................................510
Appendix C Selected Exchange Events and Comparative Hypothesis Evaluation ........................................................................513

Bibliography ............................................................................................................................521
LIST OF TABLES

<table>
<thead>
<tr>
<th>Table</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>3.1: Case Period Summary</td>
<td>119</td>
</tr>
<tr>
<td>3.2: Crude and Fuel Oil Exports to Japan, 1918-1922</td>
<td>143</td>
</tr>
<tr>
<td>3.3: Gasoline Exports to Japan, 1918-1922</td>
<td>146</td>
</tr>
<tr>
<td>3.4: Japanese Exports to and Imports from U.S., 1918-1922</td>
<td>159</td>
</tr>
<tr>
<td>3.5: Japan’s Overall and Bilateral Trade Balance, 1918-1922</td>
<td>162</td>
</tr>
<tr>
<td>4.1: U.S. Loans to Japanese entities, 1923-1931</td>
<td>173</td>
</tr>
<tr>
<td>4.2: Crude and Fuel Oil Exports to Japan, 1923-1928</td>
<td>197</td>
</tr>
<tr>
<td>4.3: Gasoline Exports to Japan, 1923-1928</td>
<td>198</td>
</tr>
<tr>
<td>4.4: Japanese Exports to and Imports from U.S., 1923-1928</td>
<td>211</td>
</tr>
<tr>
<td>4.5: Japan’s Overall and Bilateral Trade Balance, 1923-28</td>
<td>213</td>
</tr>
<tr>
<td>5.1: Crude and Fuel Oil Exports to Japan, 1929-1932</td>
<td>262</td>
</tr>
<tr>
<td>5.2: Gasoline Exports to Japan, 1929-1932</td>
<td>263</td>
</tr>
<tr>
<td>5.3: Japanese Exports to and Imports from U.S., 1929-1932</td>
<td>271</td>
</tr>
<tr>
<td>5.4: Japan’s Overall and Bilateral Trade Balance, 1929-32</td>
<td>273</td>
</tr>
<tr>
<td>5.5: Cumulative Value of U.S. Investments by Type, Aggregate Amount end of 1931</td>
<td>276</td>
</tr>
<tr>
<td>6.1: Japanese Imports of Crude and Fuel Oil, 1933-1936</td>
<td>337</td>
</tr>
<tr>
<td>6.2: Japanese Imports of Gasoline, 1933-1936</td>
<td>338</td>
</tr>
</tbody>
</table>
6.3: Cumulative Value of U.S. Investments by Type, Aggregate Amount end of 1935/1936.................................................................350

6.4: Japanese Exports to and Imports from the U.S., 1933-1936.......................353

6.5: Japan’s Overall and Bilateral Trade Balance, 1933-1936...............................356

7.1: U.S. Exports to Japan of Iron and Steel Categories in Thousand Metric Tons.....386

7.2: Exports of Pig Iron to Japan in Thousand Metric Tons..................................389

7.3: Japanese Exports of Gold and Silver, 1930-1940.......................................410

7.4: U.S. Exports of Industrial Machinery to Japan, 1930-1940........................413

7.5: Japanese Imports of Crude and Fuel Oil, 1937-1941.................................428

7.6: Japanese Imports of Gasoline, 1937-1941................................................429

7.7: Japanese Exports to and Imports from the U.S., 1937-1941......................466

7.8: Japan’s Overall and Bilateral Trade Balance, 1937-1941............................470

xii

Reproduced with permission of the copyright owner. Further reproduction prohibited without permission.


LIST OF FIGURES

<table>
<thead>
<tr>
<th>Figures</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.1: Comparison of Japanese Crude and Fuel Oil imports with Total Imports from U.S., 1918-1941</td>
<td>27</td>
</tr>
<tr>
<td>3.1: Exports of Dutch East Indies Crude Oil to Japan, 1920-1941</td>
<td>151</td>
</tr>
</tbody>
</table>
CHAPTER 1

INTRODUCTION AND DISSERTATION PURPOSE

This dissertation will contribute to international relations theory development by evaluating four contending theories' accounts of the purpose and effect of economic exchange between great power rivals. Two primary questions underpin this analysis and divide the theories (i.e., defensive and offensive realism, liberalism and marxism). First, are economic exchange relations a function of state policy serving some national interest? \(^1\) Second, why have rival great powers had extensive economic relations that over time often disproportionately benefit or constrain one of them, increasing one rival's material capabilities and/or vulnerability? This comparative theory evaluation asks whether the actors and instruments involved in exchange fulfill the state's larger policy objectives, which are presumably shaped by varying levels of threat perception (i.e., a state's grand strategy). Or, do corporations achieve their exchange preferences,

maneuvering around often constraining state policies both at home and in the rival?² This dissertation will provide answers to these questions by examining the relative explanatory power of the contending theories in a crucial case of rival great power interaction: U.S.-Japan 1918-1941. This case is crucial because exchange relations were central to the decision for war and have been inadequately addressed in previous scholarship.

A primary unresolved puzzle within the U.S.-Japan case is the importance of the shift in Japan's oil supply from the Dutch East Indies (DEI) to the mainland of the U.S. In the early 1920s Japan received most of its oil supplies from the DEI and few from the U.S., taking between 33-50% of DEI oil exports. By the end of the 1930s the U.S. was supplying over 80% of Japan's oil supplies and the DEI only 10%, representing only approximately 5-8% of DEI oil exports.³ More importantly, after 1928, U.S. oil companies were allowed greater participation in the development of oil concessions in the DEI while Japanese firms were secretly discriminated against.⁴ This dissertation

² Throughout this work the discussion is stated from the principal great power's perspective toward the rival (i.e., the state and the rival), and the term market actors and corporations refer to the same concept and are used interchangeably.
⁴ The importance of DEI oil and Japan's limited access to it is a principal reason Japan chose to attack south instead of north against the Soviet Union in 1941. This fact raises a simple counterfactual question: if the U.S. had assured Japan greater access to DEI oil, might Japan have attacked the Soviet Union instead of the U.S., dramatically altering the outcome of WWII by greatly increasing the likelihood of the Soviet Union's early defeat? The 1928 DEI oil development investments are critical to theory evaluation and prior scholarship because they have been examined narrowly in the past. Stephen Krasner concluded the U.S. acted to obtain greater access to DEI oil primarily out of concern for its own security of supply, and not as I contend due to larger strategic interests related to Japan or concerns of global industry reciprocity and alliance politics with the British and Dutch. See Krasner, Defending the National Interest: Raw Materials Investments and U.S. Foreign Policy, (Princeton, NJ: Princeton University Press, 1978), pp. 110-114.

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evaluates how and why this and other shifts in economic exchange occurred and what their subsequent effects were on U.S.-Japanese political relations and regime change in Japan.5

Previous work has asserted only the inadequacy of defensive realism in explaining the U.S. willingness to supply an increasingly threatening Japan until July 1941,6 while a recent liberal explanation contends war resulted from Japan's negative expectations of future trade.7 This latter account implies that if the trade relations could have remained separate from politics between the U.S. and Japan, war could have been averted. Because these accounts begin their analysis only in 1931, neither explains how Japanese vulnerability was created in the first place or for what possible purpose. This is a common limitation of much work in the interdependence and conflict literature. Untested propositions from offensive realism and marxism would contend that this vulnerability was created by either the state or corporations to control Japanese behavior or markets, leading to conflict when Japan did not comply. International relations theory development requires a fuller evaluation of this case that establishes the roots of Japanese vulnerability and accounts for the observed events, instead of invalidating only one

5. Although not the primary purpose of the dissertation research, the focus on U.S. economic exchange with Japan has yielded several insights into crucial changes in Japanese domestic politics.
theory's hypotheses. This is critical for understanding whether states direct their economic exchange and, more importantly, how exchange contributes to the outcome of war or peace.

The relative explanatory value of the theories in this case will be determined by comparing the theories' hypotheses and observable implications elaborated more fully at the end of this chapter. A simple causal model has been derived from the contending theories and is based on two independent variables: 1) threat perception, and 2) state or corporate determined exchange. The dependent variable is the degree of dependent exchange of the rival, and is measured across three dimensions: breadth of exchange (i.e., how many instruments and how diverse within each instrument); benefits from exchange (i.e., disproportionate, cumulative and transferable gains, strategic goods); and vulnerability due to exchange (i.e., asymmetric vulnerability, alternatives, use provisions). The dependent variable is intended to measure how broad, beneficial and autonomy constraining the exchange is and capture future variation in exchange instruments and values with more precision than other measures.8

1.1 Framing the Analysis of Economic Exchange

Economic exchange is central to the study of international politics because it may lead to changes in material capabilities and patterns of dependence, and may provide the causal basis for intense political conflict, including war. Its effect on political relations is

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8. Throughout this dissertation autonomy means the capacity of a state to determine its domestic and foreign policies independently, free from economic or military pressure by other actors (e.g., domestic corporations or foreign governments).
the subject of much scholarship, yielding contending hypotheses regarding the political effects of extensive economic exchange (i.e., it leads to peace for liberals and conflict for realists). Resolving these contending hypotheses requires answering the logically prior and central question: how and why does extensive economic exchange arise between rivals? For example, does the state influence or direct economic exchange with a rival, affecting the quality of the economic ties between them and thus their likely economic and political effects? By answering this question first, greater specification of economic exchange relations is possible, allowing scholars to better understand when exchange relations are more likely to lead to peace than conflict.9

Scholarship has all too often taken some measure of the degree of exchange (i.e., symmetry of bilateral trade relations, trade/GDP etc) and treated it as an independent variable affecting political behavior in one direction or another (e.g., conflict or cooperation). This dissertation contends that exchange itself should be treated as the dependent variable. It is created by either state or corporate actors and changes in response to their calculations (i.e., based on threat perception changes).10 A growing body of literature has moved from the economic bases of military and overall state power to address the use of economic exchange in implementing foreign policy.11 Many of

9. The degree of dependent exchange is the dependent variable in this dissertation, although it acts as an exogenous, freestanding independent variable for many scholars working on interdependence and conflict. Dale Copeland, for example, found economically dependent states led the "system" into war, but he did not ask where their economic dependence came from. Copeland, "Economic Interdependence and War."

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these works imply that states pursue integrated economic and security policies and that policies change with developments in the strategic environment (e.g., extending trade or aid relations to allies and denying them to adversaries, while modifying these policies when adversaries fade or one's economic autonomy is challenged). Few works, however, contend that rival great powers engage each other purposefully using economic statecraft, and still fewer contend that disproportionate benefits might be extended to a rival for policy purposes (i.e., grand strategy).12

The basic premise of most scholarship is that exchange creates economic gains that can be used to enhance the overall power of the participants to the exchange; therefore state policy accounts, or should account, for these power externalities.13

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13. A typical and succinct account holds: "the source of gains from trade is the increased efficiency with which domestic resources can be employed. This increased efficiency itself frees economic resources for military uses. As a consequence, trade enhances the military power of any country that engages in it."
Because of these externalities, exchange interests are, or should be, considered concomitantly with security interests. Tradeoffs between these interests are a natural part of implementing a state's grand strategy under realism. To date, scholars have examined this tradeoff predominantly in the context of intra-alliance relations, noting that allies trade more extensively with one another than with rivals. For example, during the Cold War the U.S. consistently allowed disproportionate gains from exchange (e.g., trade, aid and monetary instruments) to accrue to its West European and Asian allies because it most valued their security cooperation in overall U.S. policy.

In short, relative gains were extended to allies to fulfill larger U.S. policy objectives driven by the perceived security threat of the Soviet Union. Despite continued relative economic gains for Western Europe, as the allies' threat perceptions of the Soviet Union diverged after 1954, the U.S. was unable to maintain a high level of

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**Notes:**

14. Joanne Gowa held the trade-induced security externalities to be "uncompensated costs or benefits that an agent inflicts or confers on third parties." Gowa, *Allies, Adversaries and International Trade,* p.6, and footnote 8. This definition allows for positive security externalities from trade, but she and all other defensive realists do not consider this possibility in their work. For them, trade always creates a negative security externality due to economic gains from trade, particularly with adversaries.


16. Relative or disproportionate gains are determined through a qualitative assessment of which party's economic and military capabilities are being increased more. For example, equivalent trade balances may miss the fact that one party imports dual-use technology and the other footwear.
European cooperation with its desired export controls vis a vis the Soviet Union.\textsuperscript{17} Similarly, as the relative economic power of U.S. allies increased and challenged the U.S. economic position and its control of the international economy, the U.S. acted to defend its economic autonomy and position in the international economy (e.g., end of the dollar-backed gold standard in 1971 and U.S.-Japanese managed trade in automobiles in the early 1980s). These instances highlight the simple observation that each state identifies the threat other states, even allies, pose to its autonomy, and pursues economic relations accordingly. The fundamental question then is what is the appropriate exchange relationship with another country given a perceived level of threat and can the state establish and manage such relations?

This theme and the methods of policy-induced economic exchange were developed in the classic text on the relationship between economic and security policies. In \textit{National Power and the Structure of Foreign Trade},\textsuperscript{18} Albert Hirschman demonstrated that trade relations can be purposively directed and manipulated toward lesser powers so that a great power may increase its relative power position (i.e., Germany vis a vis Romania, Bulgaria, Argentina, etc). Hirschman delineated the means through which trade could be used to gain control over a target state. A principal tactic in this

\textsuperscript{17} Allied threat perception diverged due to differing assessments of the Soviet Union after Stalin’s death in 1953 and the termination of the Korean war. This divergence increased the bargaining leverage of the allies over the U.S. and they demanded greater disproportionate gains from the U.S. even as they reciprocated with less coordinated policy toward the Soviet Union. See Eckes, \textit{Opening America’s Market}; Mastanduno, “Trade as a Strategic Weapon;” and \textit{Economic Containment}.

manipulated exchange was the extension of asymmetric gains favoring the target (e.g., paying above market prices for a target's exports in order to become its principal trade partner--partner concentration).19

A significant gap in contemporary scholarship exists regarding the policy motivation in economic exchange between great power rivals, not just those between a great power and lesser powers or among allies. If, as Hirschman demonstrated, a great power can use economic exchange to compromise the autonomy of lesser powers, might it use exchange relations with great power rivals for similar purposes? This class of cases deserves greater attention for four reasons. First, extensive and often disproportionate exchange relations between rival great powers recur throughout observed history and demand an adequate and theoretically consistent explanation. Second, these states are presumed by many scholars to be clearly focused on each other's capabilities and motivated to achieve some balance in them (e.g., maintain relative capabilities or increase one's own), requiring oversight if not control of exchange that might upset the balance. Third, great power rivals are important in determining whether major war occurs, affecting all states.20 Fourth, these cases provide a pointed opportunity to view the ability of large corporate actors to affect state policy and exchange relations, as they will likely have significant economic interests in the rival due to its economic size and business


20. The first three reasons conform to realism's emphasis on the centrality of great powers in world politics and the focus they are supposed to have on the relative capabilities balance with rivals, which is challenged by the observation of disproportionate exchange with a rival great power. For more elaboration see Paul Diehl, ed., The Dynamics of Enduring Rivalries, (Chicago, IL: University of Illinois Press, 1998); John Vasquez, "Distinguishing Rivals That Go To War From Those That Do Not: A Quantitative Comparative Case Study of the Two Paths to War," International Studies Quarterly, Vol. 40, No. 4, (December 1996), pp. 531-558.
opportunities. The tension between state concerns for relative capabilities and autonomy (i.e., realism) and corporate interests in profits (i.e., liberalism and marxism) is piqued in these cases, and provides the best setting for comparative theory evaluation and development.

Because most scholarship focuses on cases of exchange between allies or states with significant power disparities, the analysis and conclusions are incomplete. To overcome the possible selection bias in much of this scholarship, crucial cases of economic exchange between great power rivals need to be investigated, particularly those cases where exchange benefits are disproportionate. These cases highlight the key question of the purpose of economic exchange with a great power rival. Toward what end is the state directing its economic exchange and market actors, and does it respond to changes in threat perception by extending particular instruments and not others because of their inherent characteristics (e.g., foreign direct investment (FDI), trade, foreign aid, loans, bonds, currency reserves)? For example, due to its high risk of rival expropriation, is FDI more likely to be promoted by the state only when the rival is perceived as less threatening (e.g., through government insurance or informal persuasion by officials)?

Answering these questions with respect to specific pairs of great power rivals is, of course, more problematic than posing them. Conceptually, these questions must be viewed within a set of two concurrent and interdependent relationships: those between

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21. This reason draws on liberal and marxist emphasis on the power of large corporations to influence if not determine exchange and state policy.
22. Skalnes, "Grand Strategy and Foreign Economic Policy," is a good recent example of this. Grieco, Cooperation Among Nations, Mastanduno, "Do Relative Gains Matter," Gowa, Allies Adversaries and International Trade, and Drezner, "Allies, Adversaries and Economic Coercion," also illustrate this point. In these cases the tension between state and corporate interests are not as pronounced.
states and those between each state and its market actors, including these market actors' foreign operations (i.e., corporations, banks, market exchanges, investors, etc.). Because these relationships must be assessed together, the link between state decision makers, market actors, and the extent of exchange must be made explicit in each theoretical perspective and then tested against the historical record. Too often this linkage goes untested, as normative ascriptions for state decision maker motives, calculations and relations with market actors replace examination of actual state policymaking and the degree of exchange relations. For example, liberals contend that economic exchange between rival states should lead them to pacific political relations because state decision makers will not jeopardize the gains from exchange. This proposition can only be properly evaluated by first determining how and why exchange relations are established (i.e., market or state actor led?), and then investigating whether state decision makers are actually constrained by the value of these relations and their own market actors' preferences. It may be that policymakers purposefully establish

24. These relationships may change over time as market actors, for example, may become more powerful and independent relative to states and this presumably has consequences for state-state relations (e.g., upsetting state relative power relations). See Gregory P. Nowell for a useful analytic framework of the interaction between corporate actors and governments. Nowell, Mercantile States and the World Oil Cartel, 1900-1939. (Ithaca, NY: Cornell University Press, 1994). Also see John Stopford and Susan Strange, Rival States, Rival Firms: Competition for World Market Shares, (New York: Cambridge University Press, 1991).

25. For a good review of this shortcoming see Norrin M. Ripsman and Jean-Marc F. Blanchard, "Commercial Liberalism Under Fire: Evidence from 1914 and 1936," Security Studies, Vol. 6, No. 2. (Winter 1996/97), pp.4-50. Copeland also stresses this point: "If we want to go beyond correlation to causation, we must test the causal mechanism linking variables; that is, we have to see if leaders took their nations into war for the reasons hypothesized." Copeland, "Economic Interdependence and War," p.26. For an example of normative assertion instead of explication see John R. Oneal and Bruce M. Russett, "The Classical Liberals Were Right: Democracy, Interdependence, and Conflict, 1950-1985," International Studies Quarterly, Vol. 41, (1997), pp.267-294.
economic ties with minimal consequences if they are severed (i.e., a core defensive realism hypothesis), and therefore the hypothetical constraint on a conflictual policy is non-existent.

1.2 Methodology

This dissertation will evaluate the relative explanatory power of four distinct theories (i.e., defensive realism, offensive realism, liberalism and marxism) by drawing out and testing several contending hypotheses on rival great power exchange relations. Each theory claims to explain what objective states seek, their behavior with respect to other actors (i.e., market actors and other states), and in particular the economic means employed to achieve such objectives. By selecting a "crucial" case of great power rivalry, a focused comparison of the theories will yield the greatest insight on underlying state motivation, the genesis and degree of economic exchange between rivals, and the effects of exchange on political behavior (e.g., conflict, cooperation, servitude etc). As discussed above, cases of great power rivals are critical because for realists they are "most likely" to demonstrate realism's core proposition that the state controls and directs exchange relations with the rival. For liberals and marxists these cases are less likely to demonstrate their core proposition that large corporate actors affect exchange and

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influence state policy to serve their commercial purposes. For the previously stated reasons, I have selected the U.S.-Japan, 1918-1941 case for comparative theory evaluation.

A causal model with two independent variables is drawn from the contending theories and facilitates testing their hypotheses. The independent variables are: 1) state decision makers' threat perception of the rival, and 2) state decision maker or market actor determination of the economic exchange with the rival (i.e., its instruments, values and actors engaged). The dependent variable is the degree of rival dependence and is measured across three dimensions of breadth, benefits and vulnerability from the exchange (See Causal Model Scheme in Appendix A). Each theory hypothesizes different outcomes on the dependent variable in general, and in response to changes in threat perception and state-market actor exchange preferences. Hypothesis testing is based on two fundamental questions. First, did the state perceive the rival as increasing/decreasing in threat? Second, did the state or market actors establish and/or change economic exchange with the rival by narrowing/broadening it, decreasing/increasing its benefits, or decreasing/increasing the vulnerability of the rival's

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27. Eckstein. "Case Study and Theory Development," pp. 118-19. These cases are less likely to be explicable under liberal and marxist hypotheses because the state, not large corporate actors, is more likely to be centralized in its decision making toward the rival, including directing its corporate actors' operations with the rival. This does not, however, minimize the fact that the market opportunities presented by the rival are likely to entice many corporate interests in exchanging with it and challenging state direction of exchange relations. This raises the likely number of observations of divergent state-corporate preferences in exchange with the rival, increasing the ability to evaluate the contending theories.

28. The bilateral relationship encompasses other countries, as secondary rivalries and exchange relations across third parties/countries will consequently be brought in (e.g., Great Britain and the Netherlands v. Japan in the 1920s). Only one case has been chosen because proper investigation requires review of massive amounts of corporate and state decision maker archival materials. Additionally, this case is divided temporally into four distinct periods, increasing the number of observations on the variables. Other cases that suggest themselves for similar evaluation include: Germany-Russia, 1880-1914; U.S.-China, 1969-1941; U.S.-Russia, 1979-present; Germany-Russia, 1985-present.
autonomy? A process tracing approach is necessary to answer these questions and evaluate whether exchange values are causally determined by changes in these independent variables.  

This methodology has two principal benefits. First, it improves upon much of the extant empirical literature by examining the actual causal process that leads to particular values of exchange between rivals. Only in so doing, can scholars determine state decision maker intent and ability to direct exchange, replacing normative assertions associated with correlational studies. Second, this approach increases the number of observations on all variables, allowing for fuller assessment of the contending theories and, in particular, the link between state decision makers, market actors who implement the exchange and the degree of dependency that results from exchange. By using this method to determine the causes of a particular exchange value, scholars may then be better able to explain why political outcomes such as conflict result from exchange. For example, recent scholarship has demonstrated a significant correlation between trade in "strategic goods" and conflict (i.e., minerals, iron and steel, fuels), in contrast with trade

30. Among others, Copeland noted, "Empirical analyses so far have been primarily correlational studies, finding high trade tends to be associated with lower conflict...these studies, however, provide no documentary evidence that leaders considered trade levels in deciding between war and peace," Copeland, "Economic Interdependence and War," p. 26, footnote 44. Stephen Walt stressed the supporting role of studying covariation between independent and dependent variables in hypothesis testing, and coupled this method with examination of original sources (e.g., participants memoirs) and expert scholar accounts. Stephen Walt, The Origins of Alliances. (Ithaca, NY: Cornell University Press. 1984), pp. 147-148.  
in other goods such as foodstuffs, chemicals and machinery.\textsuperscript{32} This is an important finding, but the direction of causality and explanation of why conflict might be more strongly associated with the trade in minerals and fuels requires tracing the process that first evaluates state officials' decisions for trade in these goods and then links changes in their value to decisions regarding conflict.

The major strength of the process tracing case study method lies precisely in the detailed chronological analysis of the perceived threats, the state-market actor relations and the economic exchange values, which can then compared against the theory hypotheses' observable implications.\textsuperscript{33} A listing of exchange events drawn out from the full temporal domain of the U.S.-Japan case and the method for determining theory validation and invalidation in each event is in Appendix C. Although it would be easier to treat each of these exchange events as equivalent in weight and therefore let the theoretical evaluation flow from a simple counting of each theories' explanatory value, this would not be consistent with comprehensive causal and theoretical analysis. Not all events are equal; some events are more significant, more far-reaching and have a greater effect on a rival's material capabilities, economic vulnerabilities and strategic choices (e.g., importation of autonomy-generating energy technologies versus the trade in toys). Therefore, this dissertation focuses on the crucial economic exchange events over the full period of the case to render an assessment of which theory best explains U.S.-Japanese exchange, instead of relying on a simple frequency event tally to evaluate the relative power of the four theoretical approaches.


1.3 Measurement of Independent and Dependent Variables

The first independent variable is threat perception. Stephen Walt's model of threat perception is a useful starting point for developing a comprehensive list of threat perception factors.\textsuperscript{34} Walt enumerated four threat perception variables: aggregate material power; geographic proximity; offensive capability; and aggressiveness of intentions.\textsuperscript{35} These factors have been restated in recent scholarship.\textsuperscript{36} while Walt's most recent work has stressed elite exaggeration of external threats as a potential source of threat because states may act on their own propaganda.\textsuperscript{37} In this analysis, primary emphasis for threat perception is placed on measures of offensive capabilities and aggressiveness of intentions. This variable will take one of three values: increasing,


\textsuperscript{35} Walt defined offensive capability as "the ability to threaten the sovereignty or territorial integrity of another state." Walt, The Origins of Alliances, p.24. As Walt later states, this definition should also include threats to territories of high interest, but outside of sovereign control (e.g., pre-WWI Britain's interest in Belgian neutrality, extra-territorial properties in interwar China). He held, "offensive power is the state's capacity to threaten the vital interests or sovereignty of others." Ibid., p.165, emphasis added.

\textsuperscript{36} Thomas Christensen has added "historical legacies and national perceptions," while Jonathan Kirshner has reemphasized that high economic growth is an important source of threat. Kirshner's restatement of this factor underscores the question of why a state would threaten itself through exchange by increasing the rival's economic growth. Thomas J. Christensen, "China, the U.S.-Japan Alliance, and the Security Dilemma in East Asia," International Security, Vol. 23, No. 4, (Spring 1999), p.52, footnote 6; and Kirshner, "The Political Economy of Realism," p.24.

\textsuperscript{37} As for example, a rival's elites may vilify the state for internal power consolidation purposes, but these may lead to more concrete actions. These indicators would appear to fall under the aggressiveness of intentions factor. Of course, threats perceived can be purposefully manipulated by offensive-minded statesmen. In Japan this was true as many militarists claimed U.S. discrimination. It was true in the U.S. when the State department leaked important information regarding U.S. assistance to Japan's military capabilities in its war on China in 1938 to stimulate public opinion against Japan. Stephen Walt, Revolution and War, (Ithaca, NY: Cornell University Press, 1996), pp.34,334.
decreasing or static. Increased threat perception is revealed in policymakers' concerns of the rival's territorial and economic expansion, offensive war-planning/exercises and military buildups (e.g., army and navy expenditure and force structure increases, particularly offensive capabilities *vis a vis* one's own territory or vital interests). Other indicators include: military incidents/clashes with rival forces; rival senior political and military elite statements identifying you as enemy (frequency increase or stridency of tone); and advancement of hostile factions in rival over those more aligned with one's policy preferences. Increases in one's own military planning, exercises and alliance activities directed against the rival also indicate increased threat perception.

Decreased threat perception is indicated by policymakers' approval of the rival's restraint or reduction in territorial and economic expansion, war planning/exercises and military buildups. Indicators of this include: arms control agreements; troop and/or force reductions/withdrawals from occupied territories or offensive emplacements; elite statements of cooperation or friendship; and policy alignment with one's preferences. The evidentiary sources drawn on to determine the value of this variable include: primary materials from U.S. State Department and Naval archives and other government publications (e.g., U.S. Defense Department White Papers, Annual Threat Assessment reports); direct evidence from memoirs of participants; and expert scholar accounts.

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38. Base levels of threat perception are assessed similarly from the historical record for the beginning of each case period (e.g., high, moderate). Because the theories are concerned with how changes in threat perception affect an existing state-market actor relationship or an existing exchange value, this is the important variable assessment.

39. Skalnes among others noted that military strategy, war plans and alliance activity are indicators of policymakers' perceptions that "cannot be observed directly." Skalnes, "Grand Strategy and Foreign Economic Policy." pp.583-4.
The second independent variable is whether state decision makers or market actors determine the degree of economic exchange with the rival.\textsuperscript{40} This variable requires identifying state decision makers, market actors and their exchange preferences so that examples of convergence and divergence can be evaluated.\textsuperscript{41} State exchange preferences in the two realist theories are clear and provide opportunities for observing whether divergent corporate preferences shape exchange or not. For example, under offensive realism the state prefers exchange that creates and maintains the rival's dependency; therefore, corporate actors that desire to supply technologies that yield greater autonomy for the rival should not succeed in supplying them (e.g., coal hydrogenation technology that limits dependence on imported oil).\textsuperscript{42} Neither liberalism or marxism provides as explicit a guide to objective state preferences in exchange with the rival; instead, to varying degrees each contends that the largest corporate actors shape state preferences and determine exchange.\textsuperscript{43}

The more important corporate actors include: banks and large investors; large industrial corporations (e.g., oil, manufacturing, transportation, energy systems); producers for export; and companies that import from the rival. Corporations with such diverse business interests with the rival may not prefer similar exchange relations with

\textsuperscript{40}. In this analysis the state is the executive branch authority that regulates and promotes foreign commerce. As in Krasner's analysis, the White House and State Department are the most prominent bodies of the state and the legislature assumes a secondary role in affecting state policy. Krasner, Defending the National Interest, p. 18.

\textsuperscript{41}. The theories hypothesize state and corporate exchange preferences that include preferences for certain counterparties in the rival (e.g., liberalism-private actors, offensive realism-domestic factions that support the state's policy). Assessment of this variable, therefore, requires determining whether corporations or states did in fact prefer one set of actors over another in exchange with the rival.

\textsuperscript{42}. This example drawn from the U.S.-Japan case illustrates that in evaluating state-corporate relations and the degree of exchange what is not traded is often as important as what is. Later in this case (1937) Japan did receive hydrogenation technology, but it was the most inefficient type and was not capable of producing refined products to some military standards.

\textsuperscript{43}. Liberalism's guide is more useful than marxism, as the general objective of wealth maximization through exchange based on comparative advantage provides some basis for evaluation.
the rival (e.g., banks with loans out to rival enterprises and foreign direct investors in the rival are likely to have different preferences than large industrial corporations competing with rival corporations in third markets or at home). And those with close connections to high officials may be more likely to achieve their preferences than others (i.e., an instrumental marxist proposition). The key question is do corporations with clear preferences for some exchange activity achieve their preferences?

Corporations can fulfill their preferences despite state disinclination by: forging ahead without state knowledge or support; provoking state reaction in defense of their property rights or exchange preferences (e.g., threatened transfer of technology to rival); enlisting support from rival actors to pressure the state; or changing state approval of its preferences to more accommodating sites within the state (e.g., different bureaucracies or taking some issue to the legislature). Examples of each of these tactics abound in the U.S.-Japan case and provide opportunities to observe whether states define exchange or allow their corporations to. States have many informal and formal (i.e., public) ways of directing exchange and even reshaping corporate preferences including: requiring pre-approval of exchange (e.g., loans, technology trade etc); promoting or discouraging exchange through changes in tariff and non-tariff barriers, trade and investment insurance programs and other executive branch services; and coordinating exchange toward the rival with other countries. For example, investment promotion/denial can occur through
informal negotiation between government officials and corporate leaders (e.g., U.S. State department assistance in securing corporate property rights in foreign lands or disapproval of proposed loan to rival).\textsuperscript{44}

States may also face divergent corporate interests that seek to limit or end exchange with a rival, not expand it (e.g., corporate desire to embargo a rival, as Standard Oil wanted to do to Japanese oil imports in 1934). In instances such as this, state preferences may converge with some corporate preferences but not others, and lead to state actions supporting only those corporations sharing its preferred exchange (i.e., favor other oil companies supplying Japan).\textsuperscript{45} Observing which actor most affected the resulting exchange will better clarify whether large corporate actors or states define exchange with the rival (i.e., allow for coding state or market led). The evidentiary sources drawn on to evaluate this variable are similar to those for threat perception, and include: primary materials (e.g., corporate histories, U.S. State, Commerce and Defense department documents); direct evidence from participants (e.g., papers and memoirs of businessman, statesmen); and expert scholars.

The dependent variable -- the degree of the rival's dependency on exchange -- is intended to capture variation in exchange instruments to better understand their value and the political and economic vulnerabilities they create (i.e., the potential costs of a disruption to one's autonomy and capabilities). In criticizing the distinction between

\textsuperscript{44} Eugene Staley provides the best analysis of this informal foreign economic policy process. See Staley, War and the Private Investor, (NY: Doubleday, Doran & Company, 1935). Others who have followed his typology or specified their own include: Krasner, Defending the National Interest; Baldwin, Economic Statecraft, particularly pp.40-42.

\textsuperscript{45} Observations like these with divided corporate interests interacting with the state help overcome the difficulties of establishing state or corporate dominance when their interests coincide. On the indeterminacy associated with convergent state-market preferences see Krasner, Defending the National Interest, pp.75-78, 93-97.
sensitivity and vulnerability interdependence, David Baldwin underscored the central measure of exchange -- the costs associated with its cessation.46 Other scholars have sought to maintain a distinction between short-term and longer-term inability to adjust to exchange cessation (i.e., between sensitivity and vulnerability), while providing better measures of the costs of exchange cessation.47 In an effort to better capture changes in exchange values, this dissertation will employ a three dimensional measure of exchange instruments which evaluates the breadth of exchange, its benefits and the vulnerability effects for both the state and the rival, with an emphasis on the rival's bilateral dependency.48 Examining exchange along each of these three dimensions across the temporal domain of the case will allow for better hypothesis testing, as finer changes in exchange should be captured in these dimensions.

The breadth of exchange is established by first counting how many exchange instruments are active in bilateral state-rival exchange (i.e., FDI, trade, loans, bonds,

46. Baldwin noted, "Although scholarly usage during the past decade favors retention of the distinction, the case is less persuasive if one examines scholarly usage during the past two or three centuries. The works surveyed earlier in this chapter suggest that 'vulnerability interdependence' has a superior claim to the mantle of conventionality, at least in international relations, and perhaps even in economics." Baldwin, "Interdependence and Power: A Conceptual Analysis," in Paradoxes of Power. (NY: Basil Blackwell, 1989), pp.194. 212.


48. Contrary to many analyses of exchange relations (e.g., Hirschman), the benefits from exchange do not vary inversely with the costs of cessation, hence vulnerability. Some exchange can increase the benefits to the rival and not increase its vulnerability to cessation. In fact, the opposite may occur (e.g., rival import of technology increasing its energy self-sufficiency reduces its vulnerability to a state that exports oil in large amounts to the rival). This property of exchange requires treating benefits and vulnerability separately, emphasizing vulnerability as a discrete measure of the state's ability to inflict costs onto the rival and compromise its autonomy. The proper focus therefore is on gains that enhance or retard a rival's autonomy, not merely the costs of disrupting existing exchange relations.
securities, aid, monetary assets). Within each active instrument a second determination of breadth is then conducted and monitored for changes over time. For FDI the number of different sectors of FDI investment is assessed (e.g., manufacturing, extractive industries, export/import servicing, banking, transportation and communication etc). The breadth of trade is determined by assessing how many different items are traded. If only one or two items compose over 50% of traded items, then trade is not broad. For loans, bonds, securities and aid the question is whether they are extended to many actors in the rival or only a select few. If, for example, the majority of loans go to only one or two companies then loan breadth is low.

The benefits of exchange are measured to reach a simple bilateral determination of whether one state's material capabilities are increased relatively more than the other's (i.e., relative or disproportionate gains). This entails a qualitative assessment of the content of exchange in addition to basic measurement of which state holds the surplus balance from the exchange. For FDI this means determining which state is investing in

49. Determining the breadth of exchange is useful in aspects of theory comparison as particular instruments are not predicted by some (e.g., no widespread FDI or large loans under defensive realism), and others hypothesize certain effects of threat reduction on the breadth of exchange (e.g., liberalism's contention that threat reductions broaden exchange to capital flows and, more generally, broadened exchange is expected, yielding increased constraints on decision makers).

50. This dimension is relevant to theory evaluation, particularly realism, and is intended to be a simple assessment of who benefits more from the exchange, and not an assessment of the costs or vulnerabilities of exchange ending (i.e., who's relative capabilities are being increased?). Because this case begins with a relatively more capable U.S., the balance of benefits should accrue to the U.S. and not Japan in order to maintain the relative capabilities status quo. See Schweller, "Neorealism's Status Quo Bias," p.106. Other scholars stress the effect of geopolitical variables (e.g., distance, size of economy, growth rate etc) on the distribution of gains from exchange; this analysis ignores them for the sake of simplicity.

51. Ripsman and Blanchard's recent summation of this basic point is exemplary in this regard. Ripsman and Blanchard, "Rethinking Sensitivity Interdependence," pp.12-13. Within this content analysis particular attention should be paid to whether what is imported by the state from the rival are goods that have been imported from other states and not produced at home by the rival for some time (i.e., are the gains from "specialization" real and asymmetric?). The purported efficiency gains from trade would be negligible for the state if it is merely switching supplier countries: and the rival therefore is gaining more from the production and trade (e.g., U.S. imports of toys now come from China as opposed to Mexico or elsewhere.
the other more (i.e., bilateral balance of FDI flows and stocks), and whether one state's investment increases the economic and military capabilities of the other more directly. For example, is FDI in dual-use manufacturing facilities, creating "cumulative gains" (e.g., aircraft, shipbuilding, power or transportation systems), instead of FDI in consumer products with less spillover effects?

The trade balance has two measures. The first is the value of the trade balance (i.e., which state holds the surplus and is that surplus small or large?) Second, the composition of traded items has to be evaluated to see if what is traded is directly increasing one state's relative economic and military capabilities. The balance of trade in "strategic" items matters in this determination, such as machine tools, vital natural resources (e.g., oil, iron ore), energy or power system technologies. The balance in capital markets exchange instruments (i.e., loans, bonds, securities and aid) follows as above with particular attention on whether government, military or civilian actors benefit. Monetary asset exchange does not lead to benefits per se, although money supply and economic growth can be enhanced with inflows of reserves like gold, but this type of exchange is monitored for vulnerability and binding characteristics.

but are adding to China's relative capabilities and not the U.S. because the U.S. has not produced toys for some time).

52. Baldwin's discussion of what goods can be considered "strategic" is compelling, but not strictly observed in this analysis due to the limits on determining the "comparative cost position of the target country" for every item traded. Baldwin stressed that the strategic quality of items does not inhere in their innate military characteristics/utility, but rather in whether they are procured at home inefficiently or not. This position does not address target country exports that may consume its resources and belies the possibility that trade can decrease efficient production. Ripsman and Blanchard hold strategic goods to be those "that if cutoff, would quickly affect a wide spectrum of national activities in a serious manner or that would affect a narrow range of very important defense and/or industrial activities." They stress the determination of what military and industrial activities are potentially affected by trade as the basis for assigning strategic qualities, not efficiency characteristics. Ripsman and Blanchard, "Commercial Liberalism Under Fire," p.42.

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The third and most important exchange dimension measures the extent of the rival's vulnerability held by the state.\(^{53}\) This measure evaluates the importance of the bilateral exchange to both the state's and the rival's economy, military and general government operations as well as alternatives to exchange open to both (e.g., other suppliers/markets, domestic production, substitution, stockpiling). The more important the exchange and fewer the alternatives, the more vulnerable the rival.\(^{54}\) Each instrument is measured against the base of each state's GDP (e.g., exports/GDP) and for partner and commodity concentration characteristics. These measures require calculating the percentage of the rival's total exchange held by the state (e.g., rival exports to state/total rival exports), and determining if a few items stand out in their near total reliance on the state (e.g., 90+% of the rival's export/import of some item go to/come from the state).

The significance of these measures, however, hinges upon the role of these items in the rival's economy, military and government operations, and in the changes that occur in them over time (e.g., concentration of rival's vulnerability held by the state).\(^{55}\)

The ideal measurement of this dimension on FDI means calculating the value of the annual flows and cumulative stock of FDI as follows: the rival's total FDI imports/its

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\(^{53}\) This is in effect an assessment of the state's ability to inflict high costs onto the rival with a disruption/cessation of exchange. This dimension is critical to theory evaluation as a rival's vulnerability is often used to influence its policy or acts as a *causus belli*.

\(^{54}\) Critiquing Hirschman-style analysis of only trade partner and commodity concentration measures. Ripsman and Blanchard noted this point succinctly: "What does it matter, for instance, if a country has all its trade with one state when the total value of that trade is less than .5% of its GDP? Similarly, what does it matter if a developing country's exports consist only of coconuts, but coconut exports represent but a trivial portion of its total production of goods and services?" Ripsman and Blanchard, "Rethinking Sensitivity Interdependence," p.13. Kathleen Barbieri commits the error identified above by not including trade/GDP in a recent model. See Barbieri, "Economic Interdependence: A Path to Peace or a Source of Interstate Conflict?" *Journal of Peace Research*, Vol. 33. No. 1. (1996), p.36.

\(^{55}\) The importance of exchange can only be determined through comparison with domestic bases/sources in the rival. For example, imports of steel or oil may show very high commodity and partner concentration characteristics (e.g., 95% of the imports from one country), but if these are only 5% of total oil usage domestically then vulnerability from exchange is negligible.
GDP and its Gross Fixed Domestic Capital Formation (GFDCF); the state's FDI exports to the rival/the rival's total FDI imports and the state's total FDI exports; the rival's FDI exports to the state/total rival FDI exports and the state's FDI imports. If the rival's FDI imports are significant with respect to its GDP and GFDCF (e.g., above 5% and 25% respectively) and the state's FDI exports to the rival are the largest single source, then the state is greatly contributing to the rival's material capabilities. Because FDI is difficult to retract, assessing whether the rival is vulnerable to the state is more a function of whether the state's FDI is concentrated in particular sectors that can be negatively manipulated (e.g., communications system shutdown). FDI can increase a rival's vulnerability when it is concentrated in production of export products that have no alternative outlets other than the state (i.e., either no ability to absorb in rival’s domestic market or abroad in third countries). If the state's FDI is significant within the rival and more than 50% of it is this kind of export-oriented production, then the rival may be vulnerable to losses from both import cutoffs (e.g., foreign exchange earnings) and production stoppages (e.g., decreased GDP, employment etc).

Measuring this dimension on trade means calculating the same export and import values as with FDI (e.g., rival imports from the state as % of its GDP and its total imports etc). After calculating these general measures, commodity and partner concentration in particular export and import items will reveal possible vulnerability. If there are no or few alternative sources/markets, and these items are significant in overall exports, imports or government operations, then the rival is vulnerable to state cutoff. For example, in 1919, 30% of total Japanese exports were in silk products and 95% of its total silk exports went to the U.S., representing approximately 4% of Japanese GDP.
Although silk was not considered a strategic commodity at this time, its importance in the Japanese economy (e.g., export earnings for government finance and domestic employment) and near total reliance on the U.S. market made it vulnerable to U.S. cutoff. In this instance, unlike its oil supply dependency noted earlier, Japan might have been able to find alternative outlets but the adjustment would have proven very costly. The comparison of Japanese imports from the U.S. with its imports of crude and fuel oil from the U.S. captures the importance of assessing strategic trade vulnerability, and not just overall trade vulnerability (See Figure 1.1). Japan's overall import reliance on the U.S. did not change very much, but its critical oil reliance did, and this demands the full assessment provided in this dissertation.
Figure 1.1: Comparison of Japanese crude and fuel oil imports with total imports from U.S., 1918-1941. Imports from the U.S. as percentage of total Japanese imports compared with crude and fuel oil imports from the U.S. as percentage of total Japanese crude and fuel oil imports. Oil data for 1922-1925 do not include countries other than the U.S. and the Dutch East Indies, and therefore overstate to a small extent the U.S. percentage in Japan's total oil imports.
Measuring vulnerability on loans, bonds, securities and aid means calculating the same measures of importance to GDP, GFDCF and partner concentration. These capital extension instruments flow to the rival's government or corporate actors, and the amount of the capital must be compared to the budget or assets of the recipient in the rival to determine vulnerability (e.g., value of loan is small to the state but large to rival government's asset base or revenue/spending, same calculation for corporations). Monetary asset and currency rate vulnerability is determined first by the composition of the rival's monetary assets (e.g., gold, silver inflows/outflows to the state and holdings of the state's currency as reserve by rival above 50% of its total foreign currencies held); and second, by its ability to defend its currency value and/or attack the state's (e.g., amount of rival's currency outside its government's control/borders as % of total currency in circulation). The rival's monetary vulnerability may be held by the state, but the state may also be vulnerable if the rival's holdings of the state's currency are large enough to permit it to attack its value.

The foregoing measures increase in importance when they interact in ways that increase the state's control of the rival's vulnerability to exchange disruptions (i.e., increase costs to rival across instruments). For example, export earnings from trade are often directly tied to the repayment/servicing of foreign loans by both states and corporations. If the value of the rival's outstanding obligations from capital borrowings

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56. Studying the interaction effects of exchange vulnerabilities is a way of aggregating the measure of overall vulnerability from exchange relations (i.e., do the instruments interact to increase the rival's vulnerability to the state or counteract each other, neutralizing the costs of cessation between the state and rival?).

57. Traded goods can also interact with each other and increase/decrease vulnerability. For example, if the rival imports technology that increases its energy self-sufficiency then it has decreased its vulnerability to energy import disruptions. Conversely, if technology imports impair self-sufficiency they increase vulnerability.
exceed its ability to earn foreign currency to pay or service them, then vulnerability exists (i.e., foreign currency denominated debt/foreign currency earnings through exports). If the state holds a large position in either/both of these it could deny the rival's exports and cause a debt crisis in the rival. Similarly, when the rival uses its reserve assets (i.e., gold, silver or foreign currencies) to finance imports or foreign loans it is potentially vulnerable if these assets decrease relative to the values of imports or debt servicing (e.g., increase in the ratio of value of imports and foreign debt obligations/foreign currency holdings). If the state can decrease the rival's reserve assets (e.g., through depleting its gold or silver balances) it can affect its other exchange activities. Other interaction effects follow from each state's particular setting and underscore the need to examine exchange effects across instruments.

The sources drawn on to evaluate the dependent variable include: original government documents detailing the trade, investment and monetary reserve statistics (e.g., U.S. Department of Commerce, Federal Reserve and Treasury publications, State Department documents and Naval Archives intelligence reports; Japanese government statistics); and expert analyses of exchange values, commodity and partner concentration.

1.4 Characteristics of Exchange Instruments

Exchange is risky because it can result in the state's vulnerability and/or loss of relative capabilities (e.g., transfer of technology or foregone domestic investment with overseas direct investment). But, it can also reward the state with potential influence over a rival. These risks and rewards vary with each instrument due to their differing...
effects on relative capabilities and capacity to be controlled by the state to create influence and vulnerability. Capabilities effects occur directly with supplies of items necessary to economic and military power (e.g., raw materials, technology), or by building up productive assets (e.g., FDI in manufacturing). They occur indirectly by transferring resources to a rival that it can employ at its discretion (e.g., loans, aid, bonds or trade surpluses). Control means among other things the state's ability to direct exchange toward certain actors and not others within the rival (e.g., government factions, core support groups, or private actors), to determine how the gains from exchange develop and can be used, and to easily sever exchange if it so decides. Below are general characteristics of each instrument and examples of how each leads to influence and vulnerability (See Instruments Summary Table in Appendix A).

Foreign direct investment significantly increases the rival's material power, as technology, managerial expertise and foreign exchange earnings may accompany the FDI. FDI increases the rival's economic output and directly affects its military capabilities when the FDI has spillover effects (e.g., dual-use technology and production facilities such as aircraft plants). FDI is the least controllable instrument as the rival always has the option of nationalizing the assets on its territory, and once extended it is not easily retracted. The ties created by FDI are not easily severed and are the least severable of any instrument. FDI can create vulnerability and an influence position when the FDI leads to "intensive specialization" in the target's economy, "inducing a wide discrepancy between the pattern of production for exports and the pattern of production

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58. Other statist reasons for exchange include: establishing a layer of plausible policy deniability using corporations as pawns; probing for intelligence on a target's capabilities and/or intentions; changing the target's social and political structure (e.g., industrialization promotion/denial); creating influence over a target's domestic actors/factions; diluting a target's influence with respect to other states; and acquiring negative control over a target's capabilities. See also Baldwin, Economic Statecraft, pp.41-42.
for home consumption." Vulnerability results when the FDI is predominantly used to create export-oriented industries and these exports become more important to the overall economy (e.g., exports/GDP increases above 10%). Otherwise, FDI only generates mutual vulnerability and risks increasing the relative material capabilities of the target.

Trade affects state capabilities generally by changing the efficiency with which domestic resources can be employed and directly due to the trade's composition (e.g., licensed technology, critical raw materials). In theory, trade relations are easily severed by either party, but this will depend on the importance of the items and actors involved in the trade. Trade can be directed toward particular actors in a rival for influence purposes (i.e., creation of vested interests, "commercial fifth columns"). Trade creates influence by concentrating a rival's production and exports in only a few products with little possibility for substitute markets, and by making these and overall exports more important to the rival's economy and government operations (e.g., intensive specialization of production, critical domestic political actors in the trade, or necessary foreign exchange earnings from the trade). On the import side, influence can be created by becoming a rival's chief supplier of critical imports (e.g., oil).

Loans, bonds/securities and aid extend capital and transfer purchasing power to a target, and once extended they are not easily controlled. Depending on the amount of capital involved, these instruments can significantly affect a rival's capabilities and the state's own vulnerability, without generating a position of leverage for the state. For example, if the value of loans is very high, the threat of default places the state in a

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59. Hirschman, National Power and the Structure of Foreign Trade, p.34.
60. Vulnerability may also result from FDI when the state acquires negative control over a rival's capabilities (e.g., ability to limit or destroy its production or communications).
61. Hirschman, National Power and the Structure of Foreign Trade, p.29.
vulnerable position as it might be forced to guarantee its banks' losses. This situation is
different for market-based bonds and securities offerings, where their value is free to fall
to zero in theory without triggering a response from the state. These instruments create
influence when their value represents a substantial portion of the rival's
expenditures/budget. Influence can also be created through provisions on the use of the
transferred capital. With such provisions, the state can assess the willingness of the rival
to comply with its policy preferences and judge its intentions. These instruments are
particularly useful in this area of state interaction (i.e., intentions assessment), and even
without use provisions their expenditure yields information on the rival's priorities and
intentions.

Monetary reserve assets (e.g., gold, silver, foreign currencies) and currency values
can be used as instruments of state policy to pressure, support or bind a rival. By
buying/selling a rival's currency or changing its reserve assets a rival can be influenced;
however, it is a blunt instrument because domestic groups will be affected differently
(e.g., producers for export, companies holding foreign loans etc). An important way to
generate influence over a rival is through altering the composition of its monetary
reserves. If a rival can be induced to hold more of one's own currency as a reserve asset,
lessening its holdings of standard reserve assets (e.g., gold), then the rival is vulnerable to
changes in one's own currency value and has a direct interest in preserving its value. This
situation binds the rival to oneself (i.e., increasing the costs of severance) and can be
established by allowing the rival to run trade surpluses with oneself or by directly
purchasing the rival's reserve assets, replacing them with one's own currency.

32

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1.5 Comparative Theory Review

The theories drawn out to address the causes and consequences of economic exchange between rivals are: defensive realism; offensive realism; liberalism; and marxism. Each theory addresses state-state and state-market actor relations because of the effect economic exchange can have on the distribution of power, wealth, and policy choices. The theories differ in emphasizing which actor (state or market) most affects state policymaking and which defines the expected degree of economic interaction with other states. They also diverge on the purpose and effects of economic exchange, with some interesting congruencies (e.g., liberal and defensive realist shared contention that trade creates efficiency gains with positive effects on state power). Each theory also begins with a different understanding of state motivation, behavior and the dynamics of international politics that influence and condition such behavior. The hypotheses compared below use those theory hypotheses that apply to economic exchange, as opposed to how the theories might offer different hypotheses on the role of international institutions for example. The principal hypotheses derived from each theory are listed at the beginning of each section, followed by a brief theory review justifying the hypotheses for comparative theory evaluation, and then several observable implications (See Theory Summary Tables in Appendix A). The hypotheses are stated from the principal great power's perspective toward the rival and the term market actors and corporations refer to the same concept and are used interchangeably.

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62. Policy means the state's foreign economic policy toward the rival, and encompasses the state's relations with its corporate actors and other countries to the extent they affect economic exchange with the rival.
Realism

Realists view economic relations as important elements of political and military strategies, providing among other things a means to identify and respond to threats. All realists contend that states are concerned with their relative capabilities, security, and autonomy. States design policy independently of societal interests and in pursuit of some objective "national interest," whether it be security or power. The state's capacity to determine its own fate in international affairs resides in its ability to maintain its relative capabilities, and thus primacy over the agents of its economic bases (i.e., market actors). Michael Mastanduno articulates this central realist tenet: "All realists assume that economic relations are a function of and subordinate to political relations." State authority defines market actors' behavior, but realists are divided over what market actor behaviors are conditioned by the state, particularly with respect to rivals. This division

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64. Hobbes captured the reason for state primacy well: "to assign in what places, and for what commodities, the Subject shall traffe abroad, belongeth to the Sovereign. For if it did belong to private persons to use their own discretion therein, some of them would be drawn for gaine... to furnish the enemy with means to hurt the Commonwealth...therefore it belongeth to the Commonwealth, (that is to the Sovereign only), to approve, or disapprove both of the places and matter of foreign traffique." Thomas Hobbes, Leviathan, (London: Penguin Books, 1651. 1987), Part II, Chap. 24, p.299, emphasis added.

65. Mastanduno, "Preserving the Unipolar Moment," p.73. E.H. Carr is even more explicit: "power is indivisible; and the military and economic weapons are merely different instruments of power...Power, which is an element of all political action, is one and indivisible. It uses military and economic weapons for the same ends." E.H. Carr, The Twenty Years Crisis, 1919-1939, (New York: Harper & Row, 1939), p.132.

66. For example, Waltz contends states "set the terms of the intercourse" and make and remake "the rules by which other actors operate," while Krasner asserts "the behavior of other actors, including multinational
Derives from the contending propositions regarding state motivation (i.e., for power or security) and can be evaluated by testing their economic exchange propositions for rival great powers.

**Defensive Realism**

**Hypotheses**

**H1.** If the state seeks only the minimum of material capabilities necessary to maintain its relative position (i.e., security), then it will direct its market actors behavior toward the rival to not jeopardize its position.

**H2.** If the state and its corporations' interests diverge, then the state will override corporate interests in order to maintain its relative material position vis a vis the rival.

**H3.** If the state seeks only security, then it will not compromise the rival's autonomy.

**H4.** If the state perceives the rival as increasing in threat, then the state will curtail or sever exchange relations with the rival.

**H5.** If the state perceives the rival as decreasing in threat, then the state's imperative of positional maintenance still limits the quality of the exchange relations.

**Theory Review**

Defensive realists contend that states seek to ensure their survival and security, not by maximizing their material capabilities relative to others but rather by maintaining

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Power is defined as material capabilities by defensive realists. Unlike Waltz, however, Grieco defines capabilities in a relational manner as: "economic, military and political resources whose employment permits a state to induce changes it desires in the behavior of other states or to resist what it views as..."
their relative position and not threatening others by pursuing power advantages. The reason a state will not seek more than the minimum of power necessary to maintain its security or position is the ever-present tendency of states to balance power. Increasing one's power beyond the minimum necessary invites (in fact, requires under defensive realism) a balancing response from others that lessens one's overall security. Because of these motivational prescriptions and systemic constraints, defensive realists conclude that states do compete for relative position but "state positionality is more defensive than offensive in nature."
Achieving security through positional maintenance and balancing is predicated on an "optimistic" view of international politics, wherein states are not compelled toward conflict with each other; rather, through restraint and defensive strategies, states can avoid war. Maintaining one's position requires pursuing one's own autonomy in economic and military capabilities and exercising control over market actors and exchange relations that affect these capabilities. This desire for autonomy and positional maintenance conditions states not to allow exchange relations that disproportionately benefit others, increasing others' relative economic and military capabilities, particularly rivals. Therefore, exchange with a rival should not lead to increases in its relative capabilities as the state carefully monitors exchange and its corporations. States must prevent increases in a rival's capabilities because they may be used to increase the rival's military power or otherwise unduly influence the state. This position rules out the use of disproportionately beneficial exchange for intelligence purposes, strengthening particular domestic actors within a rival, or diverting the rival from third parties.

Because the state seeks only the material power necessary to maintain its position, it should not seek to undermine the rival's autonomy (i.e., threaten it), lest it invite

71. Waltz hypothesized: "states seek to control what they depend on or to lessen the extent of their dependency...states do not willingly place themselves in situations of increased dependence." Waltz, Theory of International Politics, pp. 106-7. Grieco echoes this, noting states "are attentive to their capacity for autonomous choice and independent action." Grieco, "Realist International Theory," p.168.

72. Grieco noted, "the fundamental goal of states in any relationship is not to attain the highest individual gain or payoff; instead it is to prevent others from achieving advances in their relative capabilities." Cooperation Among Nations, p.39, emphasis added. Grieco further clarified the objects of this strategy: "states are concerned primarily about their survival and security and that they seek to ensure both not by maximizing power to their advantage but by minimizing gaps in power that are likely to favor rivals or adversaries." "Realist International Theory," p.190, emphasis added.

73. Waltz explained, "one state may use its disproportionate gains to implement a policy intended to damage or destroy the other...the condition of insecurity - at the least, the uncertainty of each about the other's future intentions and actions - works against their cooperation." Waltz, Theory of International Politics, p.105.
counterbalancing efforts and decrease its security (e.g., controlling a rival's vital import needs). Compromising a rival's autonomy through exchange relations is something security-seeking states should not do. Instead, exchange relations are likely to be of minimal importance to both states and be easily severable (i.e., not broad or beneficial). Because states are sensitive to disproportionate gains being used against them, when a rival becomes more threatening a decrease, if not cessation, in exchange relations is expected. The reverse of this hypothesis is, however, not advanced by defensive realists because "gaps in payoffs favoring partners will always detract from a state's utility to some degree." If threat perception decreases, a state will still avoid broadening exchange and extending disproportionate gains to a rival.

**Observable Implications**

The prior hypotheses and foregoing theory review yield several observable implications. First, exchange relations between rivals should be of minimal significance and easily severable (H1). This means that bilateral exchange should not lead to surpluses for the rival nor be significant with respect to state and rival capabilities (e.g., trade/GDP, FDI/GDP with rival not high %). This also means that even if trade values

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75 Grieco noted: "If two states are worried or uncertain about relative achievements of gains, then each will prefer a less durable cooperative arrangement, for each would want to be more readily able to exit from the arrangement if gaps in gains did come to favor the other." *Anarchy and the Limits of Cooperation,* p. 134.
76 Grieco, *Cooperation Among Nations,* p.47.
77 Grieco noted the enduring logic of gains denial, "(the rival) might use that relatively greater power to seek to restrict its independence or to force it to accept a progressively less favorable set of terms in the joint arrangement." *Ibid.* Waltz adds the nuclear balance to this proposition now and declares that any state without a secure 2nd strike capability should be even less likely to receive disproportionate gains because they can be converted into strategic benefit. *Emerging Structure of International Politics,* p.72.
78 Charles Glaser summarized this well: "the standard structural-realist argument predicts that cooperation between adversaries, while not impossible, will be difficult to achieve and, as a result, will be rare and contribute relatively little to states' well-being." *Realists as Optimists: Cooperation as Self-Help,* *International Security*, Vol. 19, No. 3, (Winter 1994/1995), p. 50.
are balanced, the items traded with the rival should not directly contribute to its military capabilities or significantly increase its economic growth and industrialization (e.g., technologies with dual-use military applications like naval or aircraft machine tools, advanced computer systems, etc). More generally, the requirement of easily severed exchange relations precludes high values in particular instruments such as FDI and loans, bonds or securities arrangements, which have the effect of binding states and generating "cumulative gains" more than do simple trade relations. In particular, this would proscribe FDI in defense-related industries in the rival (e.g., naval, aerospace sectors). Overarching these implications is the prohibition on disproportionate gains accruing to the rival.

Second, state decision makers should be observed to direct their market actors' relations with the rival and evaluate the benefits the rival derives from exchange (e.g., compelling corporate reporting on transfers of technology and evaluation of rival's use of exchanged items). In this calculation state decision makers should be observed to decide whether particular exchange items are allowable on the basis of whether they disproportionately benefit the rival (e.g., dual-use technologies, supercomputers etc). Decision makers should be observed to deny, veto or overturn corporate proposals or actions that decision makers conclude benefit the rival in this way (H2). Corporate actions that violate state decision maker preferences or disproportionately benefit the rival should not be observed.

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79. Grieco holds that exchange yielding cumulative or easily convertible gains/payoffs into capabilities (e.g., military or economic resources) should be the most proscribed between rivalrous states. Grieco, Cooperation Among Nations, p.46; Waltz, "Emerging Structure of International Politics." pp.57-8.

39
Third, exchange with the rival should not be concentrated in items with no alternative suppliers or export outlets (H3). The rival should have alternate sources for imports, particularly of necessary strategic goods, and diverse export markets for its goods. The rival's partner and commodity diversification should be a priority for state decision makers and any dependence of the rival upon the state should be avoided by state decision makers. The rival should be allowed to develop alternate sources for strategic goods, particularly if it is pursuing them vigorously (e.g., other suppliers, synthetic fuels instead of oil imports etc), and state policy should seek to bring this about (i.e., no observation of concentration in rival vulnerability).

Fourth, decision makers should be observed to react to threat increase with restrictions if not cessation of exchange (H4) (e.g., trade embargos, quotas, decreased types and values of exchange, informal restrictions placed on corporations etc). The state should pursue alternatives to imports from the rival (e.g., substitution from other suppliers or synthetics, rayon instead of raw silk), and different export markets. Decreases in threat should not be followed by increases in the value and types of exchange, particularly the extension of disproportionate benefits (H5). The state should not be observed to encourage increased exchange by its corporations doing business with the rival.

**Offensive Realism**

**Hypotheses**

H1. If the state seeks the maximum of influence, then it will direct its market actors to increase the vulnerability of the rival and lessen its self-sufficiency (i.e., autonomy).
H2. If the state and its corporations' interests diverge, then the state will override corporate interests to maintain/increase the rival's vulnerability.

H3. If the state seeks maximum influence over the rival's policies, then it will compromise the rival's autonomy by controlling the rival's critical resource needs, creating intensive specialization in its economy through exports, and influencing certain domestic actors.

H4. If the state perceives the rival as increasing in threat, then the state will maximize the rival's dependency, exhaust its resources and capital, foreclose other options for it, build up states hostile to the rival and coordinate the rival's vulnerability with other states.

H5. If the state perceives the rival as decreasing in threat, then the state may broaden exchange to create new types of influence while maintaining any pre-existing vulnerability.

Theory Review

Offensive realists hold that states strive for the maximum of power possible relative to other states, particularly rivals.80 States must seek the maximum of power possible because miscalculation of one's own and others' relative power is endemic to international politics. It is also potentially fatal because war is always possible;81

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80. John Mearsheimer said it best, states "aim to maximize their relative power position over other states...the aim is to acquire more military power at the expense of potential rivals." John Mearsheimer. "The False Promise of International Institutions," pp. 338-9.

therefore, states must "aim" at maximizing their relative power because "no nation can
foresee how large its miscalculations will turn out to be."82 Offensive realists define the
goal of power maximization as "control over the minds and actions of other men."83 For
offensive realists international politics is a competition for relative power and autonomy,
with each great power seeking not only to maintain its own autonomy, or independence
of mind and action, but also to compromise that of others.84 States are therefore
offensive positionalists seeking to maximize their relative autonomy vis a vis rivals, and
economic strategies and interactions will serve --"the end of controlling the policies of
another nation."85

Because states are relative power and autonomy maximizers, they prize their own
independence of action in economic and security affairs and seek to control or influence
others. Economic resources and exchange relations are valued as means to achieve the

83. Morgenthau, Politics Among Nations, p. 28. Classical realists related the imperatives of man's drive for maximum power/control with that of the state, while contemporary offensive realists have subsumed man's drives within the state's. For example, Thucydides held "of men we know, that by a necessary law of their nature they rule as far as their power permits," while Hobbes noted, "man cannot assure the power and means to live well which he hath present, without the acquisition of more." Thucydides, The Peloponnesian War, (New York: Modern Library, 1982), trans. Richard Crawley, Book V. Chapter 105, p. 353; Hobbes, Leviathan, Part I, Chapter 11, p. 161.
end of controlling others' policies, including rivals. Exchange relations are valued as both a lens onto a rival's capabilities and intentions (e.g., monitor its imports, stockpiling efforts, foreign expansion through investment etc), and a lever against its ability to act independently of one's preferences. To these ends, states are willing to "purchase" or pay for exchange relations with a rival that lead to its dependence. States will trade some of their own relative capabilities (i.e., extend disproportionate gains) for an influence position over a rival's security or foreign policy autonomy. Albert Hirschman captured this tradeoff when he emphasized the "conflict between the policy of maximization of national income, on the one hand, and the policy of securing the greatest position of influence with the trading partners."

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86. Robert Gilpin noted, "economic relations constitute power relations and competing groups will seek to maximize their economic power." Gilpin, "No One Loves a Political Realist." Security Studies, Vol. 5, No. 1, (1996), p.8. Samuel Huntington concurs, "economic power is a source of power as well as well-being. It is indeed, probably the most important source of power." Huntington, "Why International Primacy Matters." International Security, Vol. 17, No. 4, (Spring 1993), p.72. Other offensive realist works that stress the importance of controlling economic resources include: Robert Gilpin, War and Change in World Politics, (New York: Cambridge University Press, 1981); Paul Kennedy, The Rise and Fall of Great Powers: Economic Change and Military Conflict from 1500 to 2000, (NY: Random House, 1987); Mearsheimer, "Back to the Future." Christopher Layne, "The Unipolar Illusion: Why New Great Powers Will Rise," International Security, Vol. 17, No.4 (Spring 1993), in Brown, Perils of Anarchy, pp.130-178; Eric Heginbotham and Richard J. Samuels, "Mercantile Realism and Japanese Foreign Policy," International Security, Vol. 22, No. 4, (Spring 1998), pp. 171-203. Statesmen are not motivated to maintain some abstract notion of parity in material capabilities or overly concerned with "security externalities" due to efficiency gains from trade that may or may not be translated into military capabilities; rather, statesmen are driven both to understand and influence their rival's intentions and behavior, and will pay for such avenues as economic exchange to achieve these goals. This does not mean, of course, that influence attempts will be successful; rather that states pursue influence positions. In this sense, binding another as an ally by giving it disproportionate gains is part of an overarching effort to gain and/or maintain control over its policy autonomy. See Paul Schroeder, "Alliances 1815-1945: Weapons of Power and Tools of Management," in Klaus Knorr, ed., Historical Dimensions of National Security Problems, (Lawrence, KS: University Press of Kansas, 1976), pp.227-262. For a recent demonstration of this see Skalnes, "Grand Strategy and Foreign Economic Policy."

87. Hirschman, National Power and the Structure of Foreign Trade, p.26. Michael Mastanduno also stressed the costs of influence creation: "Beginning with little or no bilateral trade, a sanctioning state will need to 'invest' in future leverage by building up its trade relations with the target to the level at which the threat of denial is effective politically." Mastanduno, Economic Containment, p.54.
Hirschman highlighted the counterintuitive short-term logic of offensive realist economic statecraft. A state seeking influence over a rival will extend disproportionate benefits to it in order to make it reliant on economic exchange (e.g., export earnings for government, inward FDI for economic development, necessary imports for production processes). Influence maximization also means the state will direct exchange relations to benefit those domestic actors in the rival that best fulfill the state’s policy preferences (i.e., "vested interests," or "core groups"). Hirschman summarized this well: "Creation of potential adjustment difficulties and of vested interests is thus the twofold result of a commercial policy which aims at an intensive specialization of the trading partner’s economy and which tries to prevent the diversification of the partner’s exports with respect to regions and to products." This is equally applicable to the rival’s imports and other exchange types (e.g., loans, FDI etc), and will be established and maintained by an influence-maximizing state against corporate preferences to the contrary. Accordingly, corporate proposals or actions that allow the rival to become more independent of the state will be vetoed or reversed by the state.

If the state sees the rival as increasing in threat, the state will pursue opportunities to weaken it by further constraining its autonomy and supporting other similarly affected

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90. Mastanduno also summarized this well: "economic cooperation might increase the capabilities of an undecided state, but might also shape its foreign policy intentions in a manner desired by the initiating state." Mastanduno, "Preserving the Unipolar Moment," p.82.
91. Influence maximization entails creating "commercial fifth columns," tying particular groups to the exchange. Hirschman noted, "In the social pattern of each country there exist certain powerful groups the support of which is particularly valuable to a foreign country in its power policy; the foreign country will therefore try to establish commercial relations especially with these groups in order that their voices will be raised in its favor." This also means that unfavored actors in the rival may be specifically denied benefits from exchange, empowering other domestic groups (e.g., military actors v. commercial elites). Hirschman, National Power and the Structure of Foreign Trade, p.29.
92. Ibid. Emphasis added. Intensive specialization means making the rival’s pattern of production diverge widely between serving its domestic market and export markets. Ibid., p.34.
The rival is weakened through narrowing the exchange relations to maximize its
dependence (e.g., ending capital transfers and concentrating on dependent trade of rival) and increasing the capabilities of other states threatened by the rival. The effort to further concentrate the rival’s dependency may yield increased economic exchange between the two states, particularly when coordinating the rival’s vulnerabilities with prospective allies fails, and helps explain how economic interdependence leads to conflict for offensive realists. The state’s effort to establish dependence and the rival’s effort to escape it is a principal conflict mechanism in offensive realism and does not result from a misunderstanding of intent. Instead, the intention of one party to compromise the other’s autonomy is clear. Morgenthau noted, "A does not fight B for economic advantage (autonomy) because he misunderstands the intentions of B: it is rather because he understands them only too well."

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94. Mearsheimer, for example, sees economic relations "as likely to lead to conflict as cooperation, because states will struggle to escape the vulnerability that interdependence creates, in order to bolster their national security." Layne is also leery of economic interdependence because it "has adverse strategic consequences: it contributes to, and accelerates, a redistribution of relative power among states in the international system (allowing rising competitors to catch up to the United States more quickly than they otherwise would)." Both of these realists would benefit from greater emphasis on intentionality in interdependence creation (i.e., states create it for influence purposes and their possible and actual exploitation of it causes conflict). Mearsheimer, "Back to the Future," p.118; Layne. "From Preponderance to Offshore Balancing," p.109.

95. Morgenthau, Politics Among Nations, p.523. This position is echoed by Thucydides’ recounting of the Athenian unwillingness submit to the seemingly “trifle” demand to revoke its economic embargo of Sparta’s ally, the Megarians. Pericles noted the real issue was one of autonomy and honor among equal powers: “For all claims from an equal, urged upon a neighbor as commands...have only one meaning, and that is slavery.” The Peloponnesian War, p.82.
In contrast, decreases in threat perception of the rival create opportunities for the state to broaden exchange relations to include new instruments (e.g., move from trade in only a few items to capital transactions, FDI or trade in more types of goods). The state will, however, use this opportunity to further its influence over the rival, while maintaining any prior dependency of the rival. For example, expansion of exchange may include explicit political provisions, tying preferred policy behavior in the rival to increases in exchange. Different actors in the rival may also be engaged to further marginalize core support groups that oppose the state's preferences.

**Observable Implications**

The hypotheses and theory review generate several observable implications. First, the state should be observed to promote exchange with the rival that encourages its reliance on external markets and suppliers in general, and the state's in particular (e.g., state export/import, capital markets promotion with rival, subsidies, or informal persuasion by state officials leading to increased trade or FDI as a % of GDP in the rival). The state should also be observed to desire control over vital resources (e.g., oil, iron ore) to be able to influence the rival's supply and deny it independent access to such necessary raw materials. The state should become a principal supplier/recipient of the rival's imports and exports, and be willing to pay (i.e., extend disproportionate gains) to become the rival's principal partner in particular exchange items (H1). The state will value its exchange relations for yielding information on the rival's capabilities and intentions. The state gains intelligence on the rival through monitoring corporate interactions with the rival, the rival's supply demands and/or production capabilities (e.g., corporate reports to state officials regarding production in rival or rival officials' intentions).
Second, corporate actions that help the rival limit its vulnerability or increase its autonomy will be blocked or overturned by state officials (H2). For example, corporate actions that allow the rival independent control of necessary raw materials will be blocked (e.g., selling rival oil concessions instead of supplying it with imports). The transfer of technologies that increase the rival's independent capabilities will also be proscribed (e.g., independent air or naval craft manufacturing, energy production from domestic sources). Additionally, corporations that prefer to end exchange with a rival that the state values for influence purposes will be dissuaded from doing so (e.g., sidepayments, coercion etc). Finally, where corporate pressure for undesired exchange relations is great, the state may insulate itself from such pressure by changing the site of the decision within the state bureaucracy or buckpassing responsibility to third states, frustrating corporate preferences.96

Third, using exchange to influence a rival's policy autonomy and specific policies requires the state to control some aspects of the rival's economy (H3). The state will therefore become the rival's single most important supplier of its critical import needs and/or its single most important export outlet for products (i.e., partner and commodity concentration) that make up an important part of domestic production or financing operations (e.g., export earnings for imports, foreign loan financing). The rival's production for export to the state will be increasingly specialized with no alternative outlets, and if possible, in products that do not compete with market actors in the state in order to avoid domestic distribution conflicts in the home state that could jeopardize the maintenance and use of the influence position. The state will direct exchange benefits

96. See Krasner. Defending the National Interest, pp.74-90.
toward rival domestic groups that support the state's preferred policies (e.g., banking/finance community, favorable political parties/factions and related corporations) and away from groups that oppose the state's preferences (e.g., military and related political party and corporate actors), increasing the power of certain domestic groups in the rival to fulfill the state's will. The state may also place explicit conditions on exchange relations with the rival, allowing capital extension, for example, only after obtaining explicit government assurances on its use conforming to the state's preferences.

Increased threat of the rival (H4) will stimulate state actions to substantially limit non-trade instruments (e.g., decreasing the value and volume of loans, bonds, securities, FDI) and to further concentrate the rival's dependency upon the state (e.g., increasing the asymmetry in strategic items the rival imports from the state). The state will force the rival's critical resource needs upon itself by limiting other suppliers of these resources (i.e., coordinated diplomacy to constrain rival) and controlling the flow of important technologies going to the rival, possibly sending the rival inefficient technologies to divert its capital and resources. The state may supply items that force the rival to expend greater amounts of capital and resources to develop products, particularly for military applications (e.g., scrap steel requiring energy-intensive processing before use in naval construction as opposed to finished steel plates ready for use). The state will also begin to constrain the rival's exports to the state by developing alternatives that limit the

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97. Increasing threat may also stimulate changes in the state's relations with its corporations, leading to desired concentration of their operations in and near the rival so state control is simpler (i.e., merger encouragement for greater policy coordination).

98. In contrast to defensive realism, threat increases spur the state to concentrate the rival's dependency upon oneself, leading to the somewhat paradoxical observation of increased economic exchange between the two rivals, as the state maximizes its influence position over the rival. This tendency may be exacerbated by relations with other states similarly threatened by rival, particularly if coordinated exchange against the rival proves untenable.
rival's foreign exchange earnings ability. Finally, the state will develop the economic and military capabilities of other states threatened by the rival (e.g., U.S. loans to China 1928).

As threat decreases, the state will maintain its existing influence position and expand exchange relations to control other aspects of the rival's capabilities or policy autonomy (H5). Exchange should expand to include newer traded items (e.g., different commodities, products), non-trade instruments (e.g., FDI, loans, bonds, securities) and different domestic actors. Expanded exchange will still be guided by the goal of influence maximization and provisions on capital transfers in particular are likely to be tied to aspects of the rival's behavior the state prefers (e.g., loans linked to limitations on rival's foreign expansion or policy toward third parties).

**Liberalism**

**Hypotheses**

**H1.** If state policy is representative of its strongest economic actors' interests in increasing their and the state's overall wealth, then the state will support these actors as they seek material wealth through economic exchange with the rival.

**H2.** If corporations seek to maintain exchange relations with the rival, then they will increase the number of positively affected interest groups in the rival and create incentives for both states not to disrupt the exchange, leading to peaceful relations.

**H3.** If state policy diverges from corporate interests in expanding exchange with the rival, then corporations will seek to achieve their preferences toward the rival despite state policy.
H4. If the state perceives the rival as increasing in threat, then state decision makers will be constrained in limiting exchange by corporate preferences in continuing exchange.

H5. If the state perceives the rival as decreasing in threat, then corporate interests in expanding exchange will drive state policy.

H6. If the state prefers democratic governments because they are more peaceful and responsive to economic interests, then the state will promote exchange with a non-democratic rival to increase its economic growth and industrialization, creating a middle and entrepreneurial class demanding responsive democratic government.

Theory Review

In contrast to realists, liberals hold that the state does not act on an objective national interest, overriding divergent corporate preferences; rather, policy is a resultant of contestation among economic interest groups. Liberals contend the "strongest," "weightiest" or "most effective demand" groups prevail in formulating state policy and maintaining state adherence to their preferences. These actors are interested in

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100. Nordlinger held: "The great debate then turns primarily on the question: Which societal actors constitute the effective demand groups?" Nordlinger, On the Autonomy of the Democratic State, p.44. Liberals do not provide adequate guidance on which economic actors are likely to be the most influential in determining state policy toward the rival, although liberals note the likelihood of distributional conflict among economic actors in the home state. See Moravcsik, "Taking Preferences Seriously," pp.528-530; Ruth Arad and Seev Hirsch, "Peacemaking and Vested Interests: International Economic Transactions,"
increasing their wealth, and by extension the state's wealth, through economic exchange with the rival. Exchange should occur on the basis of freely determined market actor decisions and underlying market forces, such as supply/demand and comparative advantage. The state's role is to facilitate its dominant market actors' preferences in trading and investing with the rival, and respond to their interests in maintaining and expanding exchange.

The primary liberal assumption links state policy to societal interests (i.e., economic actors) by contending states are responsive to their economic actors and the value of their exchange relations. Because corporations want to continue their

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International Studies Quarterly. Vol. 25. (1981), pp.441-45. Because there are likely to be differences among economic actors, those actors' preferences that coincide with state policy outcomes are often determined to have been the most effective or strongest. Typical of this indeterminacy, Moravcsik held states "pursue particular interpretations and combinations of security, welfare, and sovereignty preferred by powerful domestic groups enfranchised by representative institutions and practices." Moravcsik. "Taking Preferences Seriously," pp.519-20.

1 Exchange itself is valued differently by liberals. It is not just a window onto a rival's capabilities and intentions, but more importantly, a vehicle for changing a rival's intentions toward the state and creating incentives for it to act pacifically in its own self-interest in wealth creation.


This requires the rival's state officials to be properly constrained/influenced by the economic actors gaining from the exchange and few or offset domestic consequences from the exchange (i.e., displaced workers, industries etc). John Millar captured this classical liberal proposition, "The voice of the mercantile interest never fails to command the attention of government, and when firm and unanimous, is even able to control and direct the deliberations of the national councils." Millar quoted in Hirschman, The Passions and the Interests, p.91. For recent expositions of this proposition see Paul Papayoanou, "Interdependence, Institutions, and the Balance of Power," International Security. Vol. 20. No. 4, (1996), 51

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exchange activities, they will seek to increase the number of groups benefitting from exchange in order to make both governments value the exchange and respond accordingly. Corporations will therefore seek to expand exchange with the rival, preferring exchange with private corporations over government-related ones and instruments that make both states value the exchange highly (i.e., making it costly to break off exchange). Through these actions the core liberal proposition that exchange leads to peaceful relations between self-interested states becomes operational.\(^{105}\) For classical liberals peace is the "natural effect of trade."\(^{106}\) The causal logic calls for societal actors to influence state decision makers as J.S. Mill noted: "it is commerce which is rapidly rendering war obsolete, by strengthening and multiplying the personal interests which are in natural opposition to it."\(^{107}\)

Corporate interests may not always coincide with those of state decision makers and in these instances (i.e., divergent state-market preferences) liberals predict corporate...

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\(^{106}\) Montesquieu, quoted in Hirschman, National Power and the Structure of Foreign Trade, p.10

\(^{107}\) Mill, Principles of Political Economy, p.582, emphasis added. See also Hirschman's discussion of sovereign constraint by commercial actors domestically and then by logical necessity in their international relations as well. Hirschman, The Passions and the Interests, pp.70-80. Hirschman noted, "It was difficult to maintain that domestically such expansion (commerce) would lead to constraints on the behavior of the rulers while internationally it would cause wars when these were increasingly viewed as motivated by dynastic ambition and folly (as in Candide) rather than by 'true interest'." Ibid., p.80.
actions to change or otherwise subvert state decision makers' preferences and fulfill their own. Corporations may seek to force the state to act on their preferences (e.g., compel government protection of their property or marketing rights in the rival by threatening the rival directly with embargo), change the locus of state decision making to an area where the corporations have more influence, or circumvent the state altogether and fulfill desired exchange with the rival through third party countries and/or corporations. Liberals stress the fragmented structure of state decision making and the ability of large economic actors to influence the state at different structural points (i.e., different executive branch bureaucracies, legislative organs, leaders etc). Opportunities for observing divergent interests and the relative power of differing corporate actors vis a vis the state increase with changes in threat perception of the rival.

When the state perceives the rival as increasing in threat, corporate actors might not share the state's view. This situation can lead to divergent preferences and, as discussed above, corporate actions that may violate state preferences in limiting exchange. In fact, liberals hypothesize that state actions toward an increasingly threatening rival will be constrained by corporate preferences to maintain the exchange relationship. Corporate restraint of state policy does not, however, occur automatically

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108 Herbert Feis held, "Even between rival and inimical powers capital seeks to move, to pass frontiers ringed with bayonets, responding to some clearly perceived banking opportunity, some personal tie, or some need of home industry...A few bankers and statesmen may believe that financial cooperation will create the means of compromising clashing interests and initiate political understanding." Feis, Europe the World's Banker: 1870-1914. (NY: Council on Foreign Relations, 1930. 1964). p.198. Classical liberals (e.g., Montesquieu, Steuart and Smith) held the freedom of capital conditioned state authority to behave responsibly and not jeopardize capital flight through arbitrary authoritarian actions. See Hirschman, The Passions and the Interests, pp.72-78

109 Charles Lipson takes this point the farthest, denying state capacity to direct trade for political purposes: "trade policymaking is an open, fragmented process, especially in America, and is far too cumbersome to plausibly threaten adroit strategic action." Lipson, "International Cooperation in Economic and Security Affairs," p.68. In general, liberals discount the possibility of integrated economic and security policy making by the state, although they posit an integrated effect from trade relations (i.e., they bring peace).
under the liberal framework because corporate actors may be threatened by the rival as well, creating some convergence in state-corporate threat perception and policy preference. Corporate threat perception will occur on a separate basis, however, as rival actions that limit corporations' operations in and with the rival are the basis for their threat perception (e.g., protectionist laws, government monopoly formation, substitution efforts, and other discriminatory practices that limit existing corporate operations and threaten future ones). When there are divergent corporate preferences, the state may be better able to fulfill its own policy preferences toward the rival by aligning with similarly aggrieved corporations against those corporations that do not perceive the rival as threatening.\textsuperscript{110}

This situation, however, would be consonant with liberalism only when those corporations that perceive the threat increase are also the most important economic actors within the state.\textsuperscript{111} Otherwise, liberals predict either stalemate between equally weighted economic actors and no policy change, or predominant weight to economic actors that override the state's interest in changing exchange in response to threat. Threat perception decreases by the state do not provide similar opportunities to view discord among corporate actors and with the state. Instead, liberals predict expanded exchange with decreases in threat, particularly in capital market instruments (e.g., loans, bonds etc) as investors are attracted to less threatening areas.\textsuperscript{112}

\textsuperscript{110} See Nordlinger for a discussion of how the state can align convergent corporate preferences with its own against divergent corporate preferences. Nordlinger, On the Autonomy of the Democratic State, pp.130-133.

\textsuperscript{111} Heretofore liberals have stressed the economic interests' domestic position within the state, not their position internationally.

\textsuperscript{112} See Hirschman, The Passions and the Interests, pp.70-75.
Finally, because liberals believe that democratic government is more responsive to economic actors' interests (e.g., in protecting property rights) and inclined toward cooperative international behavior, a democratic state may use exchange relations to change a non-democratic rival's regime.\textsuperscript{113} Liberals believe exchange and industrialization stimulate economic growth and new patterns of economic development (i.e., middle class emergence, entrepreneurial class with increased power and resources not tied to the rival's government).\textsuperscript{114} This in turn leads to societal demands for changes in political institutions and greater government responsiveness (i.e., democratization), allowing the state to benefit from liberalism's other core contention that democratic states are more peaceful.\textsuperscript{115} If the state were following this policy, it would encourage exchange with the rival, introducing new production patterns and elites not related to the

\textsuperscript{113} Drawing on Kant's insights, Michael Doyle notes the symmetry of purpose in commercial and political liberalism. The character of a rival’s regime can be altered by tying its policy autonomy down through greater economic exchange and more "personal interests" in the rival benefiting from exchange. See Doyle, "Liberalism and World Politics," American Political Science Review, Vol. 80, (1986), pp.1151-1169. Keohane also underscores the tight relationship between economic exchange and political order, but does not draw out liberalism's contention that democratic order best secures economic exchange. See Keohane, "International Liberalism Reconsidered," pp.187-88.

\textsuperscript{114} Liberals contend that although states may encourage increased trade and industrial development believing it increases the power of the state, they ultimately become constrained by the increasing power of "the middle rank of men" (i.e., merchants, businessman) who drive the economic expansion and trade. See Hirschman, The Passions and the Interests, pp.82-93. Adam Smith agreed with this logic: "commerce and manufactures gradually introduced order and good government, and with them, the liberty and security of individuals, among the inhabitants of the country, who had before lived almost in a continual state of war with their neighbours, and a servile dependency upon their superiors." Ibid., p.100.

rival's government. Ideally, these new commercial elites would then reshape their governing structures (e.g., induce industrialization to change domestic interest groups, elites and needs for effective, responsive government).¹¹⁶

**Observable Implications**

Hypotheses one and two yield several observable implications for state decision maker behavior. First, decision makers should be observed to respond to the exchange-related demands of their large corporate actors (e.g., large banks, industrial corporations, traders of goods for import/export). This means corporate lobbying efforts for particular exchanges with the rival should be observed to influence the policy of state officials, particularly where these corporations are substantial actors in the state's political economy. Second, state decision makers should be observed to assist corporate actors in their trade and financial activities with the rival (e.g., export/import promotion, listing rival's corporate bonds on state's market exchange, assisting in commercial loan negotiations with rival, etc). This assistance should not shape or direct the exchange with the rival; instead, corporations should determine the content of the exchange based on market forces (e.g., supply/demand, comparative advantage). This means trade and/or investment should occur in those areas that each country is relatively advantaged in (e.g., technology goods, textiles, natural resources etc). Paradoxically, trade based on comparative advantage may lead to the same outcome as predicted by offensive realists (i.e., specialized trade in only a few goods and high partner concentration).¹¹⁷

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¹¹⁶ Hirschman noted Germany's influence maximization strategy *vis a vis* the lesser states of Central and Eastern Europe prevented their industrialization to maintain control over existing authoritarian elites. Liberals contend industrial promotion can have the opposite effect. Hirschman, *National Power and the Structure of Foreign Trade*, pp.36,54.

¹¹⁷ Liberalism's comparative advantage prescription and offensive realism's intensive specialization prescription can only be differentiated by determining the state's role in managing the exchange. If state
Third, corporations will seek to create interest groups tied to and benefiting from the exchange in the rival. Because liberals believe private or "personal" interests gaining from exchange will influence their government to continue the exchange, corporations should engage as many private, non-government actors in the rival as possible. This will maximize the societal pressure upon the rival's government for continued exchange. Corporations will also prefer exchange instruments that are highly valued and not easily severed for the same reason. Therefore, liberals expect to observe exchange instruments like FDI and large loans in addition to trade relations, and an emphasis on non-government partners in the rival. Truly enlightened corporations would also seek exchange that does not displace a rival's domestic industries or its largest economic interests (e.g., exports to rival displacing its domestic production). Exchange that leads to domestic distributional conflict within the rival would not be in the corporations' interests and would be avoided where possible.

When corporate and state preferences diverge (H3), corporations may be observed to achieve their preferences by changing state preferences to fulfill exchange with the rival (i.e., lobbying, pressure tactics). These efforts might include attempts to force state decision makers to back corporate preferences (e.g., force issue of corporate property rights dispute with rival). Corporations may also try and circumvent state preferences by changing the venue of decision making in the state (e.g., shifting bureaucratic responsibility within the executive branch or appealing to the legislature instead of the executive). Finally, corporations may get around state preferences altogether and fulfill their exchange preferences through third parties (e.g., off-shore companies, third party

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policy establishes and maintains the specialized exchange then it validates offensive realism. In contrast, if corporate actors determine this specialization, independent of the state, then liberalism is validated.

57

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countries etc). In any of these instances liberals expect the largest corporate actors to fulfill their policy preferences and where possible to reshape state policy accordingly.

Increased threat perception by the state (H4) will not lead to changes in exchange relations unless the largest corporate actors are also threatened by the rival (i.e., threats to their business operations). Liberals expect corporations to lobby for continued exchange despite state perception of increased threat, and due to state responsiveness, exchange should be maintained even when state-corporate preferences diverge. Divergent perceptions may also lead to corporate efforts to circumvent or undermine state preferences as noted above (H3) and/or changing them by downplaying the threat posed by the rival. These expected observations are only complicated when the rival also threatens some corporate actors but not others (e.g., industrial corporations but not banks). When corporate perceptions of the rival also diverge, their effect on state policy may be hampered by their contending interests in changing or maintaining state policy. Liberals still expect that the strongest corporate actors will prevail in these situations and have their preferences reflected in state policy. They also discount the ability of the state to align itself with similarly threatened corporations against stronger corporate interests in continued exchange. Decreases in state threat perception (H5) are expected to be followed by expanded exchange relations, particularly in capital markets activity, provided no corporations perceive the rival as threatening their operations.

Finally, exchange with a non-democratic rival is desired by liberals because it is hypothesized to change the rival's political institutions (H6). Liberals expect expanded industrial activity and the introduction of new technologies and business practices to lead to new economic and political elites, an expanded middle and entrepreneurial class and
greater government responsiveness and accountability (i.e., democratization). This proposition requires that the beneficiaries of exchange within the rival be non-government actors. Liberals expect therefore to observe exchange with the rival's non-government or private market actors and the promotion of new industries in the rival through FDI and other instruments. This further requires the observation of state and corporate policy that promotes such exchange and emphasis on private actors within the rival.

Marxism

Hypotheses

H1. If state policy is determined exclusively by the largest banking and corporate actors' interests in maximizing returns on capital, then surplus capital will flow into the rival and will not be subject to state rescission, increasing the rival's relative material capabilities.

H2. If corporate monopolies and/or global cartels control and structure resource and technology allocation across states, then important natural resource distribution and technology transfers should fulfill these actors' interests and not those of either state.

H3. If corporate monopolies or cartels perceive the rival state as increasing in threat (i.e., to their control of resources, capital etc), then the state's coercive institutions (e.g., economic or military pressure) will be used to force the rival's compliance.
Marxists take state responsiveness to market actor interests to a logical endpoint, and assert that states pursue policies that are desired by their large market actors. Within this perspective, market actors determine state foreign economic policy and there is no autonomous state interest in power, security or wealth. The objective of external state relations is to achieve both secure access to necessary production inputs and outlets for capital investment and goods. Because market actors seek to avoid declining returns on their investment and maximum profits, they are likely to invest their "surplus capital" in foreign locations, contributing to the condition or "law" of uneven economic growth. In its more recent formulation, marxists contend that large market actors have unshackled themselves from the nation-state altogether, such that they pit nation-states against each other for the privilege of their investment. Because of this process and the control that market actors have over investment, technology, and trade, their decisions to invest in and maintain exchange relations between states, even rivals, contributes to changes in


119. Marxism in this analysis synthesizes theoretical propositions that emphasize market actor dominance in state policymaking, both domestically and internationally. This corresponds with Krasner's delineation of instrumental marxism in Defending the National Interest, pp.20-26.
relative capabilities. Market actors may act individually in this way or collectively with others in global cartel arrangements (e.g., 1920s oil and rubber cartels), determining states' capabilities by denying technologies that improve autonomous capabilities for example.

Marxists contend that developing a rival's production capabilities, possibly undermining the relative power relationship between the states, is maintained against either objective state interest under realism due to market actors' control of state policy. This hypothesis is derived from marxism's central assertion regarding politics and the political system -- that state decision making follows the leading capitalists' interests. Although Lenin acknowledged intense competition between capitalist nation-states, similar to realism, he drew out the overarching imperative of capital export and its contribution to the uneven growth in capabilities. Lenin stressed the importance of banking and finance actors who control the other types of exchange (e.g., trade and FDI). As evidence of this, Lenin and modern-day marxists note that exchange across state boundaries often serves a single corporation's interests not two independent actors (i.e., more intra-firm investment and trade as opposed to arms length transactions). Lenin held that "finance capital" dominates productive and entrepreneurial forms of capital and is the crucial lens through which state relations should be viewed.

For marxists, corporations control and structure access to critical resources and technologies across the world and not states. Threat perception of the rival therefore occurs on the basis of threats to this corporate control of resources, technology and

120 Lenin's illustration of the tight relationship between capital transactions in the form of loans and resulting trade flows is an example of this aspect of controlled exchange relations across instruments. See Lenin, Imperialism, pp. 119-121.
121 For an excellent summary of how a global corporate cartel can operate see Nowell, Mercantile States and the World Oil Cartel.
finance (e.g., nationalization of corporate assets, monopoly or exclusionist policies etc). If the rival threatens these corporations' operations, the corporations will use the coercive powers of the state to punish the rival and/or force its compliance with corporate preferences (i.e., state-sanctioned economic or military coercion). Because of these concerns, corporations under marxism may prefer authoritarian governments in the rival, which may better guarantee their property from expropriation or domestic challenges to wealth extraction in the rival (e.g., redistribution demands, greater royalty payments requests etc).

**Observable Implications**

Because state policy is synonymous with corporate, particularly banking/finance, interests there should be no observation of divergence in banking and state decision maker preferences for exchange with the rival (H1). The state should not block or otherwise impede financial actors' interests in exchange with the rival and surplus capital should flow freely to the rival, increasing its economic growth. This process leads to relative power change and is further observable in the patterns of FDI and trade (i.e., increasing a rival's economic and military capabilities while not obtaining an influence position for the state over interest groups/factions in the rival), and in the policy making process that sustains such exchange relations. Acting in the financial community's interests, investment in the rival should be observed to be maintained by state decision makers against any domestic pressure groups.

State policy should be observed to assist corporate control of critical resources, technologies or markets (H2). For example, corporations desiring property rights in a rival should receive full backing from state decision makers. Similarly, corporations with
exclusive control of certain natural resources or technologies should be observed to control their diffusion to fulfill their own preferences for market control and profit maximization (e.g., oil import substitution technologies like coal hydrogenation withheld from import dependent states). Corporate desire to control exchange leads to the expected observation of large-scale intra-firm trade and investment between the state and the rival, as corporations ensure their control over the gains from exchange.

Rival actions (i.e., its state or corporations) that challenge corporate control of investment and trade will be resisted by corporations as they enlist the coercive power of the state to change the rival's behavior (H3). These rival actions (e.g., nationalization, import-substitution efforts etc) will be portrayed as threats to the state (i.e., its interests, principles, peace etc) and the coercive power of the state will be wielded at the behest of the corporations to reverse the rival's actions. These measures could include economic sanctions or threats of military intervention, and state decision makers should be observed as readily carrying them out to defend corporate interests.
CHAPTER 2

SOVEREIGNTY AND EXCHANGE

2.1 Chapter Overview

This chapter reviews the vast literature on economic statecraft and the relationship between security and economic interests in exchange among states. In this review the characteristics of economic statecraft are drawn out from the leading works on the subject and the limits of contemporary scholarship are delineated. One of the key questions raised within this review is how do states control economic exchange with other states, particularly when that exchange is carried on by private actors? This review does not attempt to answer decisively this and the other questions raised, but rather to pose them in their starkest light so that empirical, case-based research may be better guided. Additionally, this review covers a broad sweep of history, while raising critical questions regarding contemporary state-market relations that are not addressed in the U.S.-Japan, 1918-1941 case.

The analysis within this chapter is intended to provide a framework for broader studies of economic exchange across more cases than the one investigated at length in this dissertation. The chapter introduces an analytical tool for evaluating the characteristics and importance of the various types of economic exchange, and then
specifies how this analysis is ideally applied to the various exchange instruments, including: foreign direct investment, loans, bonds and securities, trade, and monetary assets and/or currencies. A brief review of each exchange instrument then follows, detailing its characteristics and providing depth for future research.

2.2 Capabilities and Autonomy Effects from Foreign Economic Policy

The importance of economic exchange inheres in its effects on national power, intentions and the dynamic of relative power change. Because of this many scholars have addressed the relationship between state and market actors, seeking to untangle the nature of state-market relations to determine which actor drives state policy and outcomes in international politics. While many works assess which actor is preeminent, often in very narrowly observed cases, few tie their assessment to sovereign state to state relations. Among the many authors addressing the subject of relative power change, Gilpin hypothesized that the mechanism leading to uneven growth occurs "through trade, foreign investment, and the transfer of technology, [as] wealth and economic activities

122. The process of uneven growth in material capabilities is consistently identified by many scholars as underspecified and requiring investigation, as material power changes often drive threat perceptions and state behavior. For a recent statement see Rose. "Neoclassical Realism." pp.170-1. Zakaria contends that increased capabilities lead to expanded interests and perceived threats to these expanded interests; therefore, it is essential to determine where increased capabilities come from. See Zakaria, From Wealth to Power, pp.35,185. This process is analyzed in the power transition literature. A.F.K. Organski and Jacek Kugler. The War Ledger. (Chicago: University of Chicago Press, 1980); Gilpin. War and Change in World Politics; Charles Doran. The Politics of Assimilation - Hegemony and its Aftermath, (Baltimore: Johns Hopkins Press, 1971); Charles Doran & Wes Parsons. "War and the Cycle of Relative Power." American Political Science Review, Vol. 74, (1980), pp.947-965; Kennedy, The Rise and Fall of Great Powers

123. For example, Krasner in Defending the National Interest, asserts that the state (i.e., the White House and State department) does act autonomously vis a vis its own market actors in policy on important natural resource inputs. This analysis does not, however, assess state objectives under realism, such as relative power maintenance/maximization vis a vis other states.
tend to diffuse from the old centers to new centers of economic growth."\textsuperscript{124} Gilpin demonstrated the importance of this diffusion process in changing the distribution of power, as "peripheral" states avoid the costs of developing a given technology or production technique and benefit disproportionately from their use. Financial market instruments (i.e., securities, bonds and other debt/loan instruments) are also important in this regard as access to credit has often proven decisive in relative power relations among rivals.\textsuperscript{125} Gilpin identified how the distribution of state power changes with the diffusion of technology, capital, managerial know-how and other factors of economic production. He claims, however, that states cannot effectively control this process: "efforts to prevent the diffusion of technology to military opponents or economic competitors fail over the long term...at best, states can only slow the diffusion of the technology underlying their military or economic power; they cannot prevent it."\textsuperscript{126}

There appears to be a discontinuity in Gilpin's logic. If uneven growth in economic and military capabilities occurs through exchange relations, why can't states affect these economic relations to forestall rivals' relative power increases or for other policy objectives? If a state understands that through trade, foreign investment or technology transfer it is increasing the material capabilities of others, why does it engage in such practices? It may very well be that states cannot control the diffusion process in

\textsuperscript{124} Gilpin, \textit{War and Change}, p.178; Gilpin, \textit{The Political Economy of International Relations}, (Princeton, NJ: Princeton University Press, 1987), chap. 3. He did qualify this mechanism as being operative where there exists a "world market economy." Presumably if there were no world market economy (i.e., exchange relations) diffusion would not occur as easily. There are, of course, other central mechanisms for the diffusion of capabilities, most notably state competition through economic and military espionage. For recent expositions on this pervasive element in state relations and capabilities development see Fialka, \textit{War by Other Means}; Schweizer, "The Growth of Economic Espionage."


\textsuperscript{126} Gilpin, \textit{War and Change}, p.177.
the long run, due to state competition for technology, hence power, or market actor
preeminence in foreign economic relations. However, it may also be that states willingly
or purposively diffuse capabilities to others, in which case the central question of state
agency and purpose requires investigation. A primary purpose is demonstrating one’s
own positive intentions and evaluating the intentions of others (e.g., are exchange
benefits used by target in accordance with state preferences?).

Gilpin's analysis stands in contrast with Eli Heckscher's account of mercantilism
and the rise of the nation-state system. Heckscher noted that the state system coincided
with and was driven by the practice of mercantilist economic policies (i.e., surplus
seeking in economic exchange and exclusionary domestic arrangements). Heckscher
neatly summarized mercantilism's central state-market analysis: "...what was the object
of mercantilism in using economic forces in the interests of the state? The answer is
primarily that it wanted to make use of them not directly in the interests of the subject but
to strengthen the state authority itself; it concentrated on the power of the state. I refer
primarily to the state's external power, in relation to other states." This primary state
interest required that the state's power had to be secure "internally against particularist
institutions," that might undermine its international position (i.e., domestic market actors
and other authority structures such as religious institutions).

127. Mastanduno claims this willful increase of an "undecided" state's capabilities is intended to move it
toward accepting the status quo. Mastanduno, "Preserving the Unipolar Moment," p.82 and "Economics
128. Heckscher, Mercantilism, Vol 1, p. 24. The only question here is what are the relative power objects of
states? Maximization of material power through mercantilist surplus accumulation may be only one type
(i.e., mercantile realism), while maximizing power, as influence over another state may be another type and
might require exchange deficits to achieve.
129. Ibid., Vol 2, p.15. Thomas Hobbes also noted this, as he deemed corporations to be "many lesser
Commonwealths in the bowels of a greater...animated by false doctrines, perpetually meddling with the

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Albert Hirschman, Charles Tilly and Eugene Staley reach similar conclusions on the rise of the nation-state system and the condition of sovereignty that requires states to maintain, if not increase, their international position and primacy over economic forces. For Hirschman sovereign states with the power to interrupt or otherwise direct trade make "the contest for more national power permeate trade relations." Tilly observed that nation-states exist in competition with each other and, in fact, gain their identities through contrast and conflict with rivals. Tilly explained how the principle and practices of sovereignty were consolidated with the centralization of state administration and control over economic resources beginning in 1700. States moved from reliance on private capitalists for financing state operations, particularly war, to "direct operation of the fiscal apparatus, drastically curtailing the involvement of independent contractors." Nation-states were better able to master or capture the resources of economic actors within their boundaries and wage war more powerfully, thereby consolidating their dominant position vis a vis city-states, empires and other forms of political authority.

Staley's analysis bears directly on the question of whether market actors (i.e., foreign direct investors in his analysis) lead governments into political relations (i.e., conflict) with other states, or the reverse. He found that "international friction over private investments has been a good deal more frequent and dangerous where private investments have been pressed into service as instruments, tools, of a larger political

These classical realist concerns for the primacy of state authority highlight the destabilizing effect that corporations and exchange activities can have on state relations.

132. Ibid., p. 29.
purpose which the investments themselves did not originate." Staley, like Hirschman, held the only solution to sovereign state competition and self-serving manipulation of economic relations was the emergence of an international authority that limited state efforts to achieve economic autonomy and compromise others' autonomy. \footnote{Staley, War and the Private Investor, p.xvi.}

Their insistence on the inherent power competition aspects of sovereign-led economic relations gives rise to an interesting question. If the state does not influence its market actors' foreign operations, and therefore the state's overall foreign economic relations, then can we still conclude that the state is truly sovereign? If states do not exercise the power to interrupt economic exchange relations and do not, or are not capable of, influencing the direction and content of economic relations, then we may conclude that the sovereign state has been seriously compromised. In contrast, if we find that states still exercise significant influence over their market actors' foreign operations, particularly with respect to rivals, then state sovereignty might not be as compromised as many scholars assert. \footnote{E.H. Carr also held that the only way to overcome the competitive aspects of economic interactions in the state system was to "internationalize power." Carr, The Twenty Years Crisis, pp.107-8.}

David Baldwin summarized this proposition well: "As long as states continue to exist, statesmen will make influence attempts." Baldwin also neatly defined what statecraft and foreign economic policy means for state-market actor relations: "Private international trade, however, is carried on within a framework of laws and policies


\footnote{Baldwin, Economic Statecraft, p.27.}
created and maintained by governments of sovereign states. Attempts by statesmen to influence the pattern of international trade through manipulating this legal and political framework can be regarded as acts of economic statecraft."138 Elsewhere Baldwin distinguished between market actor-led trade and statecraft: "Note that it is not the decisions of the private traders themselves that constitute economic statecraft, but rather the statesman's decisions to permit or encourage such trade."139

This framework applies equally to the other exchange instruments, but is, however, somewhat limiting as "private trader" actions cannot be as readily divorced from state strategy as Baldwin implies. Private market actors assess state relations when contemplating economic activities (i.e., political risk assessment) and as a result often act as their home state might intend, internalizing their state's preferences regarding other states.140 The opposite of this may also hold, however, as market actors may act contrary to state preferences. Herbert Feis noted: "Even between rival and inimical powers capital seeks to move, to pass frontiers ringed with bayonets, responding to some clearly perceived banking opportunity, some personal tie, or some need of home industry...A few bankers and statesmen may believe that financial cooperation will create the means of compromising clashing interests and initiate political understanding."141

139. Ibid., p.116, footnote 3, emphasis added. In this sense, acquiescence to market actors' designs is purposeful statecraft. Hirschman emphasized that Germany's influence-maximizing policy was not the result of a "consciously worked out...master plan." and this allows inferences of state motivation based on their economic relations whether stated or not. Hirschman, National Power and the Structure of Foreign Trade, p.35.

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Baldwin's analysis gives scant attention to market actor influence over statesmen's decisions. This is a subject that Krasner discussed in considerable detail, even though he found it to be without merit in particular cases of natural resource acquisition. It remains possible, however, for economic relations between states to be influenced, if not determined, by market actors. This possibility underscores the need to investigate state-market relations (i.e., state permit or encouragement of relations) to determine whose interests are being served in exchange with a rival.

2.3 The Limits of Contemporary Exchange Analysis

Four principal limits in contemporary scholarship can be readily drawn from the most pervasive literature that addresses the relationship between state policy and economic exchange -- the interdependence and conflict literature. First, this literature often overlooks the role that states may have played in fostering economic exchange and their policy purposes in so doing.\(^{142}\) An unstated premise in much of this work is that the volume and value of trade exist independent of conscious political action. Levels of trade are taken as given and then political effects are assessed (e.g., war, openness of trading system, domestic interest group effects, etc.). Additionally, much of this literature does not ask why levels and types of exchange change, particularly changes that occur rapidly. Often, major shifts in trade or investment patterns are attributed to exogenous phenomena or are assumed to have been responses to underlying economic factors (e.g., income of

states, or demand elasticity for traded goods). The essential question of why exchange patterns exist and change and who might be responsible for these patterns (i.e., states or market actors) is often left unaddressed. For example, Dale Copeland holds interdependence affects the likelihood of war through expectations regarding the continuation of trade (i.e., positive or negative). He did not, however, assess how and why interdependent trade relations came into existence in the first place. Presumably, trade occurs within a political vacuum and once established it then has an effect upon state relations. Because Copeland did not first assess the motivations of states and/or market actors in establishing trade, and possibly dependence, he cannot demonstrate an independent effect of existing levels of trade, let alone expectations regarding future levels, on political relations (i.e., war).

The second shortcoming is the lack of specificity in the connections between state decision makers and their exchange relations, both their value and the actors involved. In addition to the oversight of potential state involvement in creating exchange relations, the appropriate response of states to their economic relations is underspecified.143 In Copeland's analysis, it may be that trade was induced by state actors to create political incentives against war or to gain leverage over rivals; and as war grew more likely trade considerations among other variables simply proved incapable of either impeding the decisions for war or actually may have helped provoke the conflict.144 It may also be that trade was conducted largely by private market actors with little connection to and influence on their governments. Therefore, any political check they might have exercised

143. Notable exceptions include Ripsman and Blanchard, "Commercial Liberalism Under Fire" and Skalnes, "Grand Strategy and Foreign Economic Policy."

144. As noted earlier, Mearsheimer makes this point about the effect of interdependent relations, but he too does not establish political intent in setting up the relations. See, "Back to the Future," pp. 118-9.
on the government was absent. In fact, this is a core assertion of many scholars.\textsuperscript{145} In contrast, economic relations engaged in by government actors (e.g., aid or large loans) may have far more political import than trade between private actors. In either case the identity of the actors involved and their relations with state officials needs to be determined.

Other scholars normatively contend that those who trade have pacific orientations and should influence national policy accordingly. Paul Papayoanou addressed state responsiveness to economic exchange in this manner. His analysis of WWI specifies a given level of interdependence and then posits that states pursue aggressive foreign policies based on differences in interest group articulation in state security policy, whether "median preferences of vested (economic) interests" are given representation in state security policy through democratic institutions, or "domestic-oriented economic or other narrow interests" predominate and "shut out internationalist concerns."\textsuperscript{146} In conceiving state policy formation in this manner, Papayoanou effectively eliminates any autonomous role for the state in determining its economic and security policies. Basing his analysis on Snyder's \textit{Myths of Empire}, he renders state policy the product of dominant economic interest groups, whether median, internationalist and therefore presumably pacific, or narrow, domestic and potentially aggressive.\textsuperscript{147} Like many defensive


\textsuperscript{146} Papayoanou, "Interdependence, Institutions, and the Balance of Power," pp. 47-8.

realists/liberals, Papayoanou views the failure of the state to respond properly to its ascribed self-interest as solely a domestic political shortcoming (i.e., faulty institutional setting for policy making).

The third limitation in exchange analysis is the assertion that trade (i.e., exchange in goods and services among states) is the most salient and politically important exchange instrument among states. Within this analysis, trade is assumed to occur at "arms length" between unrelated parties and in finished products. This often unstated assumption allows analysis to proceed assuming that there are two distinct parties to the exchange, each benefiting to some degree and having some theoretically driven political effect (e.g., liberalism's increased interdependence and domestic interest group incentivizing toward peace). This may be valid for earlier historical junctures, but if trade now remains largely within related parts of corporations then this assumption has lost much of its validity. What might be the political ramifications of increased trade conducted on an intra-firm basis? What does this development tell us about state-state and state-market actor relations? Are market actors more influential in state economic policy or is it now easier for states to direct their exchange relations with others (e.g., U.S. government allowing/encouraging the formation of Stanvac in 1933 from Standard Oil N.J. and N.Y.)? This concentration in market power may validate either marxist or classical realist propositions regarding the state's ability to direct its market actors' operations.

148. See for example, Edward Mansfield, Power, Trade and War; Paul Papayoanou, "Interdependence, Institutions, and the Balance of Power;" Liberman, "Trading with the Enemy."
149. Rise in intra-firm trade, up to 40+% of all trade globally is intra-firm. U.S. imports alone were 43% intra-firm in 1993. UN Commission on Trade and Development and U.S. Department of Commerce data. See also Gilpin, "No One Loves a Political Realist," p.21; Susan Strange, States and Markets, (NY: Basil Blackwell, 1988), p.71.
Trade analysis is also incomplete because it often fails to assess the nature or composition of trade. The overall value of trade does not necessarily indicate its importance, as this requires assessing each trading partner's dependence on each item traded and the value of the objects traded to each's economic and military capabilities. In this sense, the value of raw materials, finished manufactured goods, or services traded depends on their importance in the exporter's domestic economy, as well as in the importer's economy. This aspect of the political relevance of trade has gathered attention from scholars; however, most of this analysis has concentrated only on the "security of supply" issue regarding raw materials, particularly oil. Less attention has been paid to the effect that trade in different sectoral areas (e.g., agriculture, manufacturing, capital goods, services etc.) has on political interests and relations. It may be that trade in certain sectoral areas is less interdependence or vulnerability creating, as the economic ties are readily severed with little cost to one or both parties. For example, Papayoanou contends that the underwriting of the pre-WWI German merchant marine by Lloyds of London gave them significant incentive to lobby against war with Germany. If this service sector trade were to really have had the effect posited by Papayoanou, Lloyds would have had to make the payments during wartime, a proposition that seems doubtful and as yet unsubstantiated. Additionally, this type of economic tie might help explain the desire on the part of the victorious allies to assign Germany responsibility for starting the war (e.g., possibly in order to invalidate or limit indemnification liabilities and/or to recoup them in reparations with all of its effects on German politics in the 1920s and 1930s).

150. See Jean-Marc F. Blanchard and Norrin M. Ripsman. "Rethinking Sensitivity Interdependence."
151. Papayoanou, "Interdependence, Institutions, and the Balance of Power" is a good recent example of this failure to disaggregate trade's importance, and instead imply dependence based on overall value.
152. Dale Copeland, "Economic Interdependence."; Mearsheimer. "Back to the Future." and others make this point.

75
The focus on trade obscures other types of economic exchange, which may be both more economically and politically relevant. For example, the value of trade today is eclipsed by the value of sales of foreign-owned affiliates of corporations, which have chosen to serve local markets by direct operations abroad and not through trade. Thus, foreign direct investment may be more important today than trade; and it may, in fact, determine the patterns of trade, as investment is often followed by trade flows between the host and home states. International debt obligations through bonds or loans have been well documented for their political effects. Jacob Viner's classic assessment of pre-WWI financial diplomacy demonstrated how the market for governmental loans affected political relations among the European states and each state's relations with its market actors. For example, the alliance between Russia and France with its impact on European politics and German military strategy (i.e., Schlieffen Plan) can not be fully understood without taking account of the severing of Russian loan flotations in German capital markets in 1887. This was a response to commercial competition (i.e., tariffs) and Russian decrees against foreign, primarily German, ownership of land on Russia's western frontier. This financial action of Bismarck drove a reluctant Russia into closer relations with France. Viner noted, "there was no other country in which it could secure the financial help it needed, and it was soon to find that a Franco-Russian political

understanding was the price of continued access to the Paris money market.\textsuperscript{155} Additionally, these more politically salient instruments may also be more controllable by states, as in this case the states were able to direct their market actors (i.e., banks and market exchanges) to fulfill their ends. Viner summarized: "In all of these transactions the bankers seem to have been passive, and in some cases unwilling, instruments of the diplomats."\textsuperscript{156}

The fourth and perhaps most important limitation is the unidirectional assertion that trade, and economic exchange more generally, creates increased economic efficiencies and growth in their participants' national economies, freeing economic resources for other purposes (e.g., military). Baldwin notes this starkly: "[it is] the fundamental fact that trade enhances the productivity of the economy of the trading country."\textsuperscript{157} Related scholars conclude similarly: "the source of gains from trade is the increased efficiency with which domestic resources can be employed. This increased efficiency itself frees economic resources for military uses. As a consequence, trade enhances the potential military power of any country that engages in it."\textsuperscript{158}

These propositions are accepted as truisms across the field of international political economy, but rest on unproven and dubious assumptions and causal pathways. First, these propositions assume that exchange actually creates freed resources and not their diversion into unproductive, duplicative and inefficient operations (i.e.,

\textsuperscript{155} Viner, "International Finance," p.51.
\textsuperscript{156} Ibid., p. 84. Although the Paris Rothschilds did manage to pressure Russia to end its persecutions of Jews, reacting to the expulsion of Jews from St. Petersburg and Moscow in 1891.
\textsuperscript{157} Baldwin, Economic Statecraft, p.222.
\textsuperscript{158} Gowa and Mansfield, "Power Politics and International Trade," p.408. Copeland notes how this efficiency is generated: "when a state trades, it specializes in and exports goods in which it enjoys a comparative advantage, while forgoing the production of other goods, which it then imports. This process of specialization, however, entails potentially large costs of adjustment if trade is subsequently cut off." Copeland, "Economic Interdependence and War," p.18.
specialization actually occurs). Second, these propositions assume that the administrative state captures the gains from freed resources, not private actors, and then diverts the gains seamlessly to military purposes. This assumption runs counter to the liberal proposition it is drawn from, namely that trade and increased efficient production constrain the capacity of the state to interfere with the actors involved in the trade (e.g., taxation of gains from trade). Mastanduno highlights the critique of these often unstated assumptions well, noting that some trade may be "resource-absorbing," generating economic inefficiency, or at least diversion away from any possible increased resource usage for military purposes (e.g., roadway construction and/or automobile exports).159

In sum, the overwhelming emphasis on trade as both the most politically salient type of economic exchange and one that yields only increases in economic efficiency and overall capabilities has as yet not been borne out. This is primarily because the nature or composition of trade has not been adequately assessed on a relative dependency basis, taking account of the full nature of vulnerability or exposure that inheres in different types of trade and resource utilization. Further, trade itself has not been demonstrated to be the most important type of exchange among states, as other instruments have been documented as having at least as much political import in great-power relations. Analysis should therefore take account of the relative importance of the different types of exchange among states in addition to a more qualitative assessment of trade in goods and services. Finally, the political intentions and potential directedness of exchange relations have not been addressed prior to hypothesizing about the effects that exchange has on state decision making and relations.

2.4 The Nature of Exchange: Evaluating Exchange Relations

The instruments of economic exchange between states include: government aid; loans; bonds and other debt/security instruments; currencies or monetary reserve assets (e.g., gold, silver, foreign currencies); trade (in goods, services, technology, etc.); and foreign direct investment. Each instrument has political and economic effects that vary based on: 1) the severability of the exchange relationship; 2) its relative value and importance to each party and each party's political economy, including whether the gains from exchange are transferable or cumulative in nature; 3) the actors involved in the exchange relationship and the ability to use the instrument with discrimination (i.e., direct exchange onto certain actors and not others); and 4) the long-term ability to control the exchange and affected interests, and at what cost to oneself. The purpose of introducing these four dimensions is to identify when exchange relations have a significant degree of political salience or relevance, and therefore to better understand the effects of exchange on political behavior. In short, we need to assess who is gaining from exchange relations and how those gains might be used before any inferences can be drawn regarding the political importance of exchange. These exchange dimensions are introduced as ideal assessment tools with the full disclosure that they are often in practice difficult to determine.

Severability is the ease with which a given economic tie between great powers can be broken.\textsuperscript{160} Indirectly, the ease of severance indicates the level of political commitment between exchanging parties. Severability depends on the nature of the

\textsuperscript{160} Hirschman identified this aspect as adjustment costs. National Power and the Structure of Foreign Trade, pp.26-29.
exposure created by a given instrument: mutual vulnerability or asymmetric vulnerability. Mutual vulnerability occurs when a given exchange instrument creates roughly equivalent loss potential between the two states. In the event of a breakdown in exchange or political relations, both states would be vulnerable to similar losses. An example of this type of vulnerability would be a large loan from one great power to another. The loan creates mutual obligations and vulnerabilities, as the debtor great power may influence the creditor if it proves unable or unwilling to fulfill its loan obligations. Asymmetric vulnerability occurs when the benefits of a given exchange instrument accrue largely to only one party, and therefore the potential costs of disruption as well. This occurs whenever one great power is more reliant than the other on the gains from exchange between them. For example, asymmetry would typify a trade relationship wherein a substantial amount of one party’s total exports go to the other and the value of these exports to this receiving great power are small compared with its overall imports.

The second dimension concerns the relative importance of an individual instrument to the state’s political economy (i.e., capabilities effects). Each instrument’s importance depends on its value to the government (e.g., tax, budget, military effects) and the economy in general. For example, a state that receives a large percentage of its government budget in the form of loans or bonds underwritten by another is likely to value this instrument highly, possibly more than any other form of exchange. The relative importance of an instrument also inheres in its ability to be used by the recipient state in a manner of its choosing. Assessing whether the gains or resources from the

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161. When a loan is large enough a debtor acquires not just a creditor but a partner. Staley held, "there is strong reason for believing that the borrowing nation has more leverage on the policies of the creditor nation than vice versa." Staley, War and the Private Investor, p.406.

162. This would also be somewhat rational for the government, as state finance may be more important to government officials than trade relations more generally.
exchange can be easily transferred to desired areas by state officials is a necessary aspect of establishing relative importance. This calls for a highly qualitative assessment of the value of an exchange instrument within a state. For example, the importance of trade, particularly imports, cannot be minimized simply if its numerical value is low (e.g., imports as % of GDP is 1-2%). If the imports that comprise this low trade figure are crucial to industrial or military power and are controlled by another state, then their relative importance is high. Similarly, if the items imported are significant technologies that generate cumulative advances in economic and/or military capabilities, then the exchange is also important despite its numerical value. Therefore, each instrument must be evaluated for its importance to the state's political economy, both in its governmental operations and general economic capacity.¹⁶³

Third, each instrument varies based on the actors involved in and affected by its use. These can be government or private actors. Because each instrument has some relationship with governmental authority in the originating state, it is important to define this relationship and its effect on a rival's political economy. Without understanding the actors involved in the exchange activities, the political purposes and effects of the exchange cannot be accurately assessed. Additionally, some instruments may be more useful in affecting distinct actors within a target (i.e., discriminate), as opposed to bluntly affecting all actors within a target's political economy. The use of more discriminate instruments would indicate a higher degree of political relevance or intent in the initiating state. For example, governments often deal directly with each other in certain exchange instruments, such as loans, aid or currency/monetary assets, and can have their own

¹⁶³ Ripsman and Blanchard. "Commercial Liberalism Under Fire." 81
economic agencies such as state trading operations or banks. Other types of actors differ in their degree of affiliation with their home governments. Semi-governmental actors have significant interaction with their governments, either through ownership and governance relationships, or production and finance ties. For example, a company that produces the majority of its output for the government or one that receives most of its financing from the government would fall under this category (e.g., heavy industry, military contractors or development/industrial banks). Private market actors, on the other hand, conduct a majority of their operations and financing independent of the government, and their ownership and governing bodies are least likely to be directly influenced by government officials.

Identifying the domestic significance of actors is also crucial (i.e., are they core support groups, vested interests). Kirshner noted core groups including: "the military, the middle class, agricultural laborers, big business, oligarchic commodity producers, etc. regional and demographic factors can also be influential."164 The distinction of actors involved is important. We would not expect the political and economic effects to be the same if the exchange partners are government actors instead of private ones. Because the effects of exchange differ depending on the actors involved, policy motivation underlying exchange relations can become more evident. For example, if the objective is to create better and lasting political relations with a rival not only will its government be engaged, but also its core support groups and private actors. Assuming state responsiveness to non-state actors' interests, the creation of broader vested interests within the target state that benefit from exchange with oneself would increase the likelihood of better political...

relations (i.e., liberalism's integrative exchange). In short, who you target depends on your policy purpose; government or private actors may or may not be the most useful exchange partners for a given policy.

The final dimension is the ability of a state to control its exchange relations with a target. Control of the economic effects and actors involved will vary by instrument as will the costs incurred in establishing the exchange. The benefits of some instruments are more lasting and cumulative (e.g., technology transfer or FDI), and do not lend themselves to easy manipulation by the initiating state. Therefore, any state extending these instruments should consider the spillover effects from the exchange. The extent to which states seek to control their exchange with others and avoid disadvantaging themselves is readily observable in their use of "tied provisions" (e.g., loans or aid with specified spending provisions). Additionally, the actors involved in the exchange may not remain under the initiating state's control, as the effort to create influence and vested interests in a target may also create them in oneself. Eugene Staley captured this dynamic with FDI well:

This is a rather general characteristic of private investments used as tools of diplomacy. They do not remain merely tools, but having been led into rather large risks in support of government policy, they in turn demand that the government support them, which usually means a pressure that is hard to resist in favor of continuation and intensification of a policy...they add momentum to policy.\textsuperscript{165}

Because of this possibility, exchange relations led by private actors may be less controllable and more likely to generate relative power changes between states. The costs in extending an instrument include foregone domestic opportunities and erosion of

\textsuperscript{165} Staley, \textit{War and the Private Investor}, p.63.
one's own economic bases of power (e.g., purchasing power, financial/investment, industrial production). For example, a state with a large investment and industrial base can draw on it and extend FDI to a target. However, in so doing, the initiating state is foregoing the use of its capital base for domestic development and may weaken its own development due to external overextension.\textsuperscript{166} Identifying the domestic opportunity costs to one's bases of economic power indicates the level of political intent in the initiating state by exposing what base of its own power it is willing to trade for exchange relations with a target.

The general characteristics of each instrument and their characteristics on the above dimensions are summarized below. For each instrument the usefulness in affecting desired targets (i.e., domain) will be assessed as well as any interaction effects among the instruments (e.g., loans with trade import provisions).

\textbf{Foreign Direct Investment}

Foreign direct investments (FDI) are "cross-border expenditures to acquire or expand corporate control of productive assets."\textsuperscript{167} Control of productive assets is established through: "greenfield" FDI (i.e., setting up productive assets from scratch); mergers and acquisitions (i.e., takeover of existing productive assets); or joint ventures with host country corporations. In any modality, FDI is a very tangible foreign economic

\textsuperscript{166} This is Gilpin's argument regarding British FDI at the expense of domestic investment and productivity in the late 19th and early 20th century. Gilpin, \textit{U.S. Power and the Multinational Corporation}. Carr noted that using one's purchasing power in importing a target's goods also costs a state: "Purchasing power had become an international asset; and the fact that price was no longer the dominant factor (Germany made most of her purchases in South-Eastern Europe at rates above world prices) put the purchaser and not the producer in a position to call the tune. A new power has thus been placed in the hands of countries with a large population and a high standard of living. But it is a wasting asset which, if used to excess, tends to destroy itself." Carr, \textit{The Twenty Years Crisis}, p.129.

presence within a target country, compared with bond or securities investments. With FDI comes the possibility of significant transfers of technology, managerial or production know-how, and export and foreign exchange earnings. Because of these possibilities, FDI directly affects the economic capabilities of a target country, improving its manufacturing capabilities for example.168 Depending on the significance of technology or know-how transferred, it may also directly affect the military capability of a recipient state (i.e., dual-use assets and transferable applications).

In his comprehensive review of U.S. and British foreign investment behavior, Gilpin summarized the qualitatively different nature of FDI. He noted: "Direct investments are intended to establish a permanent source of income or supply in the foreign economy; consequently, they create economic and political relationships of a lasting and significant character."169 The significance of direct investment inheres in this longer term commitment of resources and its creation of mutually vulnerable interdependence (i.e., the least severable instrument). Whether intentional or not, the political commitment FDI represents is more significant than other exchange relations precisely because direct investments are vulnerable to target country actions (e.g., nationalization) and they often generate cumulative gains. Because of this property, FDI is more likely to occur between politically friendly states or those seeking better relations

168 FDI also can lead to continued gains for the recipient country (i.e., cumulative gains) and potential spin-off/spillover effects that increase the economic and military capabilities of the recipient. See John C. Matthews, "Current Gains and Future Outcomes: When Cumulative Relative Gains Matter," International Security, Vol. 21. No. 1. (Summer 1996), pp.112-14; Waltz, "Emerging Structure of International Politics," pp.57-8.

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than between unfriendly states. Therefore, FDI should be the instrument most correlated with changed threat perceptions, although government influence on corporate FDI may require more effort than with bankers on loans.

Further variation in the significance of direct investment depends on: the economic sectors invested in; the economic purpose of the investment (i.e., local or export market servicing); the value of FDI within the sector, overall domestic investment and the macroeconomy; and relations to target political authority/oversight, particularly where joint venture partners are involved. Eugene Staley identified five distinct sectoral categories for FDI: commercial, for trading purposes (e.g., export-import servicing); transportation and communication (i.e., infrastructure); extractive industries (e.g., oil, minerals, lumber etc); manufacturing; and banking/finance. Staley found that direct investment in infrastructure areas and extractive industries were the most highly correlated with political conflict. Interestingly, Staley found that investment in manufacturing was the least associated with political conflict, although there were comparably fewer cases of this type of investment. Staley's separation of commercial investment from manufacturing is questionable for contemporary analysis, where FDI in

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170. This is also valid in comparison with other instruments (i.e., trade, loans etc). FDI is politically salient to a different degree than other instruments. Investors also perform more significant political risk assessments with FDI, including comprehensive assessment of the political relations between home and host countries.

171. Staley, War and the Private Investor, pp.373-376. Staley's analysis must be qualified by the fact that most of his cases of great power conflicts occur over disputes in 3rd countries, not over investments between great powers. Updating Staley's classification scheme, we would add aircraft manufacture to the category of manufacturing.

86
manufacturing can also be commercial FDI due to its export-oriented nature. Nonetheless, his findings and analytical framework provide a solid basis for differentiating investment types.

The economic purpose of the investment can create potential adjustment difficulties (i.e., vulnerability) in the employment of the productive assets. A primary distinction can be made between FDI instituted to serve the target's market (e.g., trade-substituting FDI) and FDI that serves export markets (e.g., export processing zone investment or resource extraction). The former motivation for FDI creates political and economic ties between states of a more lasting and mutually vulnerable nature (i.e., ease of severance is low). The latter type can lead to a situation where the target country becomes asymmetrically vulnerable to changes in export markets or the investor's practices. Hirschman noted that influence over a target can be had by "Inducing a wide discrepancy between the pattern of production for exports and the pattern of production for home consumption." A target's vulnerability increases as earnings from its exports become relied upon by domestic actors and the government, and as the variation in production for domestic consumption and export increases (i.e., adjustment costs increase as does asymmetric vulnerability).

The value of FDI within the target's overall economy, domestic investment capacity and sectoral setting determines its importance to the target and its potential vulnerability. FDI may come to represent a significant portion of a state's overall economy (i.e., FDI stock/GDP, foreign-owned output/overall output), allowing foreign


173. Hirschman, National Power and the Structure of Foreign Trade, p. 34.
investors influence over the economic capabilities of a target. Similarly, foreign investment may come to represent a significant portion of overall domestic investment and yield foreign investors influence over a target's growth capacity. Finally, foreign investment may be concentrated in particular sectors, industries or geographically, and derive influence from its position in these sectors. These variables may or may not become politically salient. For example, foreign investment may turn out to be relatively unimportant to the overall economy and domestic investment levels, but it may represent a significant portion of ownership in an important economic sector (e.g., transportation, aircraft manufacturing, banking etc). Therefore, in order to determine an influence position through FDI, qualitative assessment of its placement is necessary.

Qualitative assessment also requires identifying the actors involved in the investment in both home and target countries. From the home country's perspective, FDI can be a discriminate instrument, implemented to affect a target state and/or particular actors in a desired manner. Investment may be directed toward private market actors, particular economic sectors or their creation through greenfield investment, for the purpose of creating vested interests within a target that will then influence their government in a desired direction (i.e., trickle up influence). Investment may also be directed, or required due to a target's foreign ownership laws, toward semi-government actors (e.g., joint ventures with state corporations or similar relationships like co-production). In this case, the relationship between the target's semi-government actor (i.e., one that has been acquired or joint ventured with) and its government requires specification. Is the semi-government actor related to any particular government agency (i.e., ministry of defense, state, economy etc.), or is its directorship composed of
members/leaders of important political groups within the state (i.e., core groups)? In answering these questions, the investment's political importance can be better established.

Because FDI establishes one's market actors in a target state, these market actors may influence the home government in unintended directions. Their potential influence will differ depending on their relationship with their government (i.e., are they private actors or semi-government/large oligopolistic?). Actors with greater ties to the home government are likely to be able to influence it more than private actors, possibly leading the state toward policies that these actors favor, even at the expense of some objective state interest.\footnote{See Staley's quote on intensification of policy by market actors, p.83.} This outcome would depend on the balance of power between market actors and state officials in the home country. FDI could lead the home state to constrain itself with respect to a target, yielding mutual vulnerability between the states as vested interests are created in both states, not just the target. Because of this possibility and the potential transfer of material capabilities, FDI is the least controllable exchange instrument. Additionally, FDI draws on the investment capacity or capital base of the initiating state and is extended at an opportunity cost of investment in one's own state. The extent to which policy-directed FDI undermines one's domestic economy can not be readily stated in advance, but is widely held to contribute to relative power decline.\footnote{Gilpin, U.S. Power and the Multinational Corporation; Kennedy, The Rise and Fall of Great Powers; Lenin, Imperialism.}

The methods through which governments induce direct investment into a target state include: direct participation; subsidies, including tax advantages and sidepayments; investment/profit guarantees; official and unofficial persuasion, drawing on government relations with investors, official information and other resources (e.g., foreign ministry
analyses, embassy commercial and government contacts etc); and public campaigns promoting the target's attractiveness. Direct government participation in foreign investment is not uncommon (e.g., British Petroleum in Iran, Japan's Manchuria Railway Co. and Oriental Development Co. in China), but its intentions and policy objectives then become overt and potentially compromised. Government subsidies and investment guarantees offer more subtle means of directing investment and are pervasively used by governments.\textsuperscript{176} Perhaps as important as government financial inducement is the relationship between finance and government elites. Staley noted:

Personal unions not infrequently unite the precincts of government where decisions on diplomatic support of foreign investments are made with the precincts of business where foreign investments are controlled. That is, some individuals hold positions of influence or authority in both realms at once, or they pass back and forth from one realm to the other, permeating each with the attitudes of the other and shaping the policies of each to accord with the desires of the other.\textsuperscript{177}

Staley illuminated this fusion of private and public foreign investment interests across countries, noting cases involving Andrew Mellon of Gulf Oil and the U.S. Treasury Department, and Gerson von Bleichroder connected to both the Paris and London Rothschilds and Bismarck. Outside of this fusion of state and investor policy, Staley underscored the importance of sidepayments or logrolling in state-directed foreign investment. He noted, "Those who control diplomacy are able to exert pressure upon bankers by intimating that if they accede to official wishes in the present instance their interests elsewhere will be much better looked after...[while] the goodwill of the foreign

\textsuperscript{176} Gilpin describes in great detail the various tax and accounting policy changes that have encouraged American FDI in the postwar period, but he does not tie these inducements to policy toward particular states. See Robert Gilpin, "The Multinational Corporation and the National Interest," Report prepared for U.S. Senate, Committee on Labor and Public Welfare, (October 1973); and Gilpin, \textit{U.S. Power and the Multinational Corporation}, pp. 19, 59-63.

\textsuperscript{177} Staley, \textit{War and the Private Investor}, p.214.
office is often valued by bankers simply for the improved sources of information which it opens to them.\textsuperscript{178} It is important, therefore, when observing changes in the objects (i.e., target states) of these various foreign investment inducements and patterns in foreign investment itself to assess the relationship and interaction between the investors and their government. The central question is: in whose interest was the investment made, the government's or the investor's?

**Trade**

International trade is the most widely discussed type of exchange and the least properly investigated for political and economic effect. International trade concerns the cross-border movement of goods and services. The concepts of goods and services include such items as: wheat; iron ore; oil; machinery; licensed technology; and insurance policies. Specifying the effects of such diverse items can not meaningfully be done in the abstract; rather, the effects of trade vary with each state and in each state's bilateral relationships. The composition of trade (i.e., what goods and services are traded, in what volumes and values?) and the patterns of countries traded with is likely to differ markedly. It is this composition and trading partner pattern that defines the parameters of the political and economic effects of trade, rather than simple calculations of overall import and export values.\textsuperscript{179} The importance of trade depends on the composition of a state's trade compared to its domestic resource base and economic production needs. In short, the more self-sufficient a state is in its domestic economy's necessary inputs (e.g., oil, iron ore, timber, agricultural products etc), the less likely it is to engage in trade as a

\textsuperscript{178} Ibid., p.294.

\textsuperscript{179} See Ripsman and Blanchard, "Rethinking Sensitivity Interdependence."
matter of national necessity.\textsuperscript{180} Under these circumstances, influence over a relatively self-sufficient state must come from other aspects of trade dependency (e.g., export of fewer, luxury items or increasing government reliance on foreign exchange earnings).

The basic economic property of trade is that it creates gains for both parties to the exchange. The extent of these gains, their division among the parties and their possible further application form the fulcrum of debate in the fields of international security and international political economy. Most scholars who contend that trade has a large effect on political behavior hold that trade leads to increased economic efficiency, increased economic and potential military power, and therefore, demands policy oversight on the maintenance and distribution of these gains. Increased efficiency in domestic resource use due to trade occurs because of specialization in domestic production and trade based on comparative advantage.\textsuperscript{181} This ascription of specialization and efficiency gains from trade is questionable on the grounds that much of trade occurs not on a highly specialized, or diversified product basis, but rather in the same items traversing state borders (aka., intra-industry trade in autos, auto parts, capital goods for example).\textsuperscript{182} If each state truly sought to export its comparative advantage then the composition of trade would be more differentiated. It is therefore important to examine the composition of trade and assess whether trade occurs on a specialized basis or not. At a basic level, trade in goods can be divided into two broad categories: trade serving producer markets (e.g., industrial inputs, natural resources etc) and trade that serves consumer markets (finished

\textsuperscript{180} This refers to the "security of supply" effect in trade relations and is operative for most states regarding vital raw materials and industrial inputs (e.g., oil, iron ore, minerals etc).

\textsuperscript{181} The important question is does a state "specialize" in some traded items due to some invisible market forces or due to the trade policies of other states as Hirschman indicates?

and semi-finished products, agricultural products etc). If trade becomes more concentrated in any one market serving or product area then an influence position may result.

A state seeking influence over another through trade will try and force it to produce only a few items without alternative domestic or export markets and make this production important to the overall economy and particular political actors. Hirschman identified many specific policies that lead to an influence position, all of which have the objective of increasing the target's dependence upon oneself and increasing its vulnerability to a cessation of trade. Hirschman's most important insight was the manipulability of a target's domestic politics through trade. He held that trade leads to influence when used to create new "vested interests" and/or tying the interests of existing powerful groups to the trade.

In identifying the role of directed trade in influence creation, Hirschman underscored the discretion with which trade can be employed as an instrument of statecraft. Trade relationships can be created or directed toward particular actors within a target and are therefore the least blunt instruments of potential influence creation. The purpose of an influence position may vary, however, from fostering better political relations to undermining certain actors within the target (e.g., military) by making others more powerful. Because of this potential variance, identifying which actors are involved in and gaining from the trade between states is critical. If only semi-government (e.g., state trading firms) are traded with, the economic and political effects are more direct.

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183 Skalnes also demonstrated this with Britain's effort to tie isolationist American midwestern agricultural interests to the fate of Britain by importing their goods at favorable prices.
184 Hirschman, National Power and the Structure of Foreign Trade, p.34.
185 The transferability of the gains from trade will also necessarily depend upon which actors are acquiring these gains, government or private.
than if private actors are engaged within the target. Similarly, if government actors are the only parties to the exchange (e.g., US-Soviet grain in early 1970s), then the broader economy and society of the target are less influenced. If the actors are private and do not have influence with their government, the effects are likely to be muted and consigned to a form of trickle up pressure, if any. In short, who is advantaged from trade within the target matters.

The ability to direct and control trade is contingent on the relationship between the government and market actors in the initiating state. Some scholars contend that of all exchange instruments trade is the least susceptible to government manipulation. For example, Kirshner believes: "trade is an inefficient instrument of state power. Trade is usually dominated by domestic policy concerns...Trade is also in most cases functionally outside of government management (state trading being the exception) and thus the state's hands are not on the levers of control." Despite this criticism, governments retain many policy tools that can induce or direct trade. These include: tariff rates; non-tariff inducements (e.g., lessened customs oversight on a target's exports or valuation discretion); licensing regulations (e.g., dual-use technology items or particular actors); trade financing (e.g., export-import underwriting); and governmental procurement (e.g., direct purchase by the government or stipulations regarding foreign content in government contracts). With any of these measures a government may induce greater trade with a target through incentives to its market actors. It may also bargain with its market actors in order to get their desired behavior in exchange for favorable treatment elsewhere. These types of government actions should not be dismissed as unimportant.

or worse, non-existent, because they are difficult to investigate. It may remain valid, however, that trade is more difficult to control than other instruments because of the greater number of actors involved, particularly private actors. This does not necessarily allow us to conclude that trade between rivals fits this condition, as government oversight and influence in the initiating state may be high.

The importance of trade and the ease of severance/dependency depends on the concentration of a state’s exports and imports (i.e., commodity and country patterns) and the value of these exports and imports to the domestic economy of the target. If a state exports few products (i.e., commodity concentration) and exports these to only a few countries or a majority to only one country (i.e., partner concentration), then it may be asymmetrically vulnerable to these partners. The degree of vulnerability will depend upon the importance of these exports in the target’s economy (i.e., do they represent a significant portion of GDP, important actors’ interests, necessary foreign exchange earnings etc). Similarly, if a target state imports only a few commodities from a small number of countries or important items from only one country (e.g. oil), then it may be asymmetrically vulnerable. As with exports, the degree of vulnerability will depend on the trade’s importance to the target’s economic and military capabilities (i.e., portion of GDP, necessary inputs in production processes etc). A situation of mutual vulnerability would result when both the target and initiating state rely on the trade between them in roughly equal measure, or where each holds a dominant position in a

187. Hirschman noted the dilemma of export diversification: “but the fact remains that an intelligent power policy must take account of the greater difficulty which is generally experienced in diverting exports.” Hirschman, National Power and the Structure of Foreign Trade, p.33.
188. In both exporting and importing it is not sufficient to assess vulnerability or importance on a strictly state-state bilateral basis, as corporations from one state may serve the target’s markets through third countries. In these instances it will be important to determine whether the home government directs or monitors such trade from third countries as part of its strategy toward a target state.
necessary item for the other with little opportunity for substitution. The transferability or cumulation of gains from trade will also hinge on the composition of traded items. If traded items include advanced technology or dual-use items their cumulative effects and political salience will be high.

Aid

Foreign aid is a longstanding tool of economic statecraft and involves the extension of monies or other assets/goods to a given country without specific provision for repayment or similar obligation.\(^{189}\) This extension of assistance can be implemented by a single country (i.e., bilateral aid) or through an international institution (i.e., multilateral aid). As such, this instrument is largely the province of government actors in the initiating country,\(^ {190}\) although the targets of the aid can be specific actors in the recipient state's government, and not just the government as a whole. For example, aid may be forwarded to particular governmental agencies within a target or directed toward particular project areas favored by certain political groups within a target. In this manner, aid may be extended purposefully to affect political coalitions in a target. Because of this property, aid is a discriminate instrument and can be controlled through specifying how the aid can be spent by the target/recipient. In bilateral great power relations, aid's importance generally comes from its extension to third countries that may affect the rival (e.g., financial aid to rival's current enemy as way of tying it down). In this instances,


\(^{190}\) Leaving aside private aid like that of George Soros that may affect great power politics or seek to.
this aid can become a serious source of tension in the great power rivalry and is therefore often quite controlled by the state and used with circumspection.

However, as a salient instrument in bilateral great power relations, foreign aid is less relevant compared to aid for lesser states, and where it exists, more politically sensitive to impressions of political inferiority or dependence. This sensitivity would vary with the area that aid is extended to or the conditions attached to its use. The more specific the aid, the more sensitive, particularly if it is used in areas of military stabilization or provision of food and shelter. The economic ties created through aid allow for relatively easy severance on the part of the initiating state and can lead to asymmetric dependence of the recipient. The importance of aid to a recipient country determines whether the aid creates dependency in the recipient, hence political import. If the value of the aid is significant to the recipient government's own resources or budget, then asymmetric dependence exists. This assessment may also be applied to aid that is extended on a project or specific governmental agency basis. If foreign aid represents a significant percentage of the budget on a particular project or agency activity, then asymmetric dependence has been created, although the scope of influence would then be correspondingly reduced. Any state using aid as a policy instrument draws on its own financial resource base (i.e., budget), or uses its influence within international bodies to lobby for preferred aid dispensations toward a target.

Foreign aid is most useful in generating influence when directed toward specific actors within the target state and it is financially significant in the target. If these conditions are not met, as is more probable between great powers, aid is not likely to be a

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191. Notable exceptions to this occur where the political significance of the aid outstrips its financial import (e.g., U.S. aid to Israel)
useful instrument in one's policy, whether it is dependency creation or binding a rival. Although this typifies aid as a policy instrument between great powers, aid may play a significant role in signaling political relations between states. Baldwin noted: "the form in which aid is given sends a signal—accurate or deceptive—about the intentions of the donor. The symbolic effects of military aid and disaster relief are quite different even though the actual economic impact may be the same. The forms of aid matter because symbols matter."\textsuperscript{192} In this manner, aid may be most useful in helping cement political ties between states, even where the relative value or importance of the aid is negligible, provided the aid is directed toward politically relevant actors within the target. However, aid may also signal relations of political superiority and indicate intentions of dependency maintenance. For example, U.S. aid to Russia appears to be more concerned with declawing Russia's nuclear weaponry than creating the foundation for stable democracy and market economics. Because aid creates governmental obligations its political import and salience are high, and thus its effect on overall political relations can be significant.

**Loans**

The lending of money, or the extension of credit (i.e., capital), is another longstanding type of economic exchange between states, and like aid it can be initiated by governments bilaterally or through multilateral offices in international institutions. Unlike aid, however, loans are also implemented by private market actors and their relationship to government authority in so doing requires specification. Every state has an authority and oversight relationship with its banking sector wherein the credit

\textsuperscript{192} Baldwin, *Economic Statecraft*, p.305.
activities of banks are evaluated, both in the domestic economy and internationally. A lending state has the option to decide to lend capital directly from its government offices or to permit or encourage lending by its market actors toward a target state, or both. The means by which a government may encourage lending toward a target state include: providing loan guarantees or other insurance instruments to market actors; providing financial and political analysis (which can include proprietary governmental information) to market actors that promote the creditworthiness and benefits of credit extension to the target state; and the manipulation of relations with one's market actors to induce/coerce their actions abroad. The state, therefore, has the option of acting directly through its own offices, international institutions, its market actors, or any combination of these three modalities. Whether the state chooses direct relations with another state or prefers to work through market actors or international institutions indicates its political intent. If the overall loan relationship between the states is dominated by the government then the political salience of the relationship is higher than otherwise.

The political importance of the loan relationship is also determined by the identity of the borrowers in the recipient state. Are the loans issued directly to the central government, particular government agencies or project areas, large semi-government actors, or private actors? If the loans remain predominantly within the central government then the potential influence established is strictly governmental. However,

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193. This would include backscratching/logrolling between the state and its market actors across a variety of issues. See Nordlinger, On the Autonomy of the Democratic State, pp.130-33, for a discussion of mechanisms by which the state can induce behavior from market actors.

194. States may use international institutional lending to further legitimize their individual policies. For example, France and Czechoslovakia worked through the League of Nations in securing large loans for Austria with specific spending and domestic policy provisions that maintained its political independence from Germany. See Abdelal and Kirshner, "Strategy, Economic Relations and the Definition of National Interests," p.134.
loans may be directed toward semi-government or private actors that are pillars of government support or opposition, thus establishing more indirect levers of potential influence for the sending state. The extent of this potential influence depends on the relative value of the loans to the borrowing actor. If the loan value is a significant amount of the capital base of semi-government or private actors, or the operating expenditures for government actors, then potential influence has been created. Whether this influence position establishes asymmetric or mutual vulnerability depends on the value of the loans to the originating actor(s). If the loans are sufficiently large to the originating state, whether issued by the government or its banking actors, then vulnerability may exist in the originating state, yielding a situation of mutual vulnerability between the states.

Loans establish debtor and creditor relations, but the influence a creditor obtains is more distant than that of a direct investor and is contingent on the payment of the debt. A creditor obtains influence when a debtor defaults on its debt obligations and the terms of the credit relationship are rewritten, often including more specific political provisions (e.g., changes in banking practices, export/import regulations, government officers or foreign policy). The creation of substantial loan obligations can facilitate greater influence over a target through increasing the risk or actual occurrence of default. This maximum leverage position is achieved where the loans to the borrower are substantial and their value to the creditor is not. Debtors, of course, are not without influence, and can use the threat of default to gain leverage over their creditors, provided the creditors are sufficiently exposed to their particular debts. Credit influence may be used for
various purposes, from conditioning another state's spending habits and priorities to assisting particular economic interests and domestic coalitions within the target state.\textsuperscript{195}

The risk of default is not as likely between the governments of great powers, but may exist for their semi-government and private actors. Influence attempts may occur more frequently through these actors by indirectly affecting a target's market actors' vulnerabilities. States must first identify which actors are most vulnerable and politically relevant in the target state. In this analysis private and semi-governmental actors with important relations to their government will be engaged. Because the sending state is directing its efforts at non-state actors it is likely to use its own private or semi-government actors in the exchange relationship, unless it is willing to openly involve its government with all the possible repercussions in the target's domestic politics. Loans, like aid, have the possible benefit of being rather fungible assets whose proceeds can be implemented by recipient state actors in manners of their choosing. Only where loans have provisions tying their use to specific ends would this not be the case, and between great powers this may not be as likely.\textsuperscript{196} Therefore, absent tied provisions, the ability to control the loan relationship ceases with the extension of the monies to the target.

**Bonds and other Securities/Debt instruments**

Bonds are market-based debt instruments issued for countries or companies with specific dates of maturity and auctioned for sale to various investors in money markets

\textsuperscript{195} For example, in the early 1900s, France began to tie its loan extensions to Russia to particular military spending programs proceeding in Russia. See Viner, "International Finance and Balance of Power Diplomacy," p. 58.

\textsuperscript{196} E.H. Carr has noted that in pre-WWI Britain, unlike all other European states, loans extended to foreign borrowers were the least likely to have tied provisions specifying where their proceeds could be spent. E.H. Carr, *The Twenty Years Crisis, 1919-1939*, (New York: Harper & Row, 1939), p.127.
(i.e., private banks, government banks, individual investors etc.). When a bond is written it may be auctioned for sale to investors in locations outside the state for whom the money is being raised, creating the opportunity for economic exchange between states. Bonds, often referred to as government securities or government bonds, can be transferred from one investor to another after their issuance and purchase in a particular bond market. Corporations also issue bonds to investors in addition to issuing stock, or securities, in order to raise capital for their activities. We are concerned with these activities when they require or utilize foreign monies, capital markets and actors. Because bonds are underwritten by investment houses or banks and then traded on market exchanges, governments have influence over the process. Governments can affect bond and securities markets by: regulating the listing process on the market exchanges (i.e., whose bonds are allowed issuance); influencing the market actors that operate in the exchanges; and intervening directly in the markets by buying or selling bonds on their own account.

Government bonds raise capital for the issuing government, creating a debt obligation to the bondholding investors. Because governments are the recipients and beneficiaries of the capital raised, their ability to finance state activities is directly affected. The obligation to repay the investors also carries with it political import as the principal investors and/or their government may be able to influence the recipient state through this debt obligation. For example, through this instrument Germany drove Russia from the German capital markets into a closer relationship with France. In 1887

Bismarck de-listed Russian government bonds from the Reichsbank's list of securities eligible for collateral loans and pressured German market actors not to issue new credit to the Russian government or private Russian market actors.\textsuperscript{198} France reacted to the Russian government's position of financial vulnerability by extending substantial financial assistance to Russia coupled with increasingly explicit political conditions. Viner noted Russia's position nicely: "Although the Russian government, because it disliked the republicanism of France and was not inclined to participate in its dangerous revanche foreign policy, did not immediately align herself politically with France, there was no other country in which it could secure the financial help it needed, and it was soon to find that a Franco-Russian political understanding was the price of continued access to the Paris money market."\textsuperscript{199}

The use of this instrument is influenced by market actors in the state where bonds are underwritten and purchased. Because governments must work through their market actors to ensure the purchase of bonds, these market actors (i.e., private banks, large investors etc.) can exercise some influence over both their government and the government of the bond issuer. Market actor influence occurred in the Franco-Russian case as the Paris Rothschilds pressured the Russian government to rescind laws that persecuted Russian Jews, particularly laws expelling Jews from St. Petersburg and Moscow in April 1891. This pressure did play a role in changing Russian policy toward its Jewish population, culminating in the repeal of these laws in 1894. However, debtor or bond issuing states also have influence in their relations with investors and their

\textsuperscript{198} This action was in response to Russian tariff policy and its decrees against foreign land ownership (i.e., German) on the western frontier of Russia. Viner, "International Finance and Balance of Power Diplomacy," p.51.

\textsuperscript{199} Ibid.
governments. Staley recounted how Germany under Hitler and Economics Minister Schacht discounted its debt by threatening non-payment on its bonds: "The creditors charged that the German government had depreciated the market value of its own bonds by protesting that they could not be paid, and then had bought them at a discount with funds that should have gone for interest to the bondholders."200

This instance of repurchasing one's own bonds at a discount highlights the important variable in the use of bond instruments - the bondholding investor. Because bonds are market-based debt instruments they can be transferred or resold among investors, and this property complicates the assessment of state vulnerability. Unlike loans where the identity of the lender and borrower are clear and consistent, and thus the political quality of their relationship, government bonds can be transferred repeatedly in money markets yielding a situation where the bondholders' identity is ambiguous. Knowing who holds one's debt obligation is essential to establishing the political import of the economic relationship. Because of this property, the direct political effects and signal of political commitment of bonds are less than loans. Bonds also minimize government responsibility as investors theoretically hold the liability in case of governmental default, as bonds are allowed to fall in market value. But, like loans the capital raised through government bond issuances allows the issuing state to expend

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200 Staley, War and the Private Investor, p.39. This and other recent findings on Schacht should call into question the repeated declarations that Schacht was a "moderate." For example, Schacht asked allied occupiers to give Germany some African colonies to effect its return as a modern state in the international community. See Richard Overy, Interrogations: The Nazi Elite in Allied Hands, 1945, (New York: Viking, 2001). Skalnes recently held Schacht to be the leading moderate in interwar Germany. See "Grand Strategy and Foreign Economic Policy," p.595

104

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additional resources in manners of its choosing. They are highly fungible exchange instruments which increase the capabilities of governments or corporate actors without necessarily yielding control for the initiating state.

The relative value of bonds depends on the importance of the capital raised to the issuing state's governmental operations. The larger the percentage of government expenditures accounted for by bond issuances the more important they are, and the more vulnerable a state is to changes in the politics of the bond markets where their capital is raised (e.g., Russia's pre-WWI situation). The degree of vulnerability in the capital sending state is contingent on the amount of its market actors' capital used to purchase the target state's bonds. If the bonds it has purchased make up a substantial portion of outstanding invested capital then a situation of mutual vulnerability may obtain.

Corporate bonds or other debt/securities instruments (e.g., stocks, mutual funds etc.) may also be issued in foreign capital markets or come under foreign ownership, yielding many of the same conditions as described for government bonds. The principal difference is that direct government influence is not created by private market actor foreign debt issuance. Nonetheless, these instruments may yield influence for foreign investors provided significant amounts of capital are raised in this manner for the target state's market actors relative to their other capital financing activities. With these instruments governments may influence a target's politically relevant corporate actors, listing their securities or other debt instruments in its capital markets. In so doing, a state may obtain influence over these corporations' economic activities or change their political motivation with respect to oneself and/or their home government (e.g., internationalize their outlook or create vested interests lobbying their home government in intended
In either case, the foreign debt obligations of a target's private actors may reveal patterns of debt obligations with respect to certain states and their investors.

**Currencies and Monetary Reserve Assets**

Every state with a monetized economy (i.e., paper currency backed by the central government and its reserves of gold, silver, or other assets, including foreign currency holdings) and some external economic relations assesses the value of its currency with respect to others and the effect of changes in its value and/or the underlying reserves. Changes in currency values impose costs on the political economy of a state. Blanchard and Ripsman note: "The actual cost imposed by a drop in the value of a state's currency will depend on the increase in inflation that results from the decline in the value of the currency, the amount of debt denominated in foreign currency, the nature of the firms that go bankrupt as a result of declining currency values, the cost of foreign currency expended to defend an exchange rate, and the cost of any interest rate increase geared towards defending the currency."\(^{201}\) Currency value changes also directly affect producers and consumers of traded goods as the value of these goods is altered and the performance and purchasing power of these groups is similarly affected.\(^{202}\) Due to these various effects on a country's political economy, states may seek to influence others by

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\(^{201}\) Blanchard and Ripsman, "Rethinking Sensitivity Interdependence," p.23.

\(^{202}\) Jonathan Kirshner, *Currency and Coercion: The Political Economy of International Monetary Power*, (Princeton: Princeton University Press, 1995), p.9, makes this argument as do most scholars discussing trade and monetary relations. However, they may be missing the effect of managed, or intra-firm, trade on the costs of currency changes to producers of traded goods. If a company controls both ends of trade across countries, it can set the value of the trade to match whatever currency values prevail (i.e., transfer pricing), thereby avoiding losses from currency vulnerabilities.
affecting their currency. These influence attempts principally involve the buying or selling of a target's currency or changing its underlying monetary reserves in order to pressure, support or bind a target state.203

Because governments are the sole issuers of currency and managers of its stability they are intimately bound to its integrity. Jonathan Kirshner noted: "Aside from the direct economic costs and the possible costs associated with defense (of a currency), threats to currency stability are particularly subversive to existing governments. This is due to the unique psychology of this particular sphere of economics, where value depends explicitly on confidence, and because monetary stability is so closely associated with the legitimacy of governance."204 Governments act as guarantors of currencies and therefore pay attention to all of the economic conditions that affect the supply and demand of their currency and the monetary reserves underlying the currency's value and defensibility.205 Kirshner contends that this responsibility provides greater potential for influence attempts than trade, aid or financial exchange instruments.206 Influencing the value of a target's currency can therefore directly challenge or support its legitimacy in addition to its effects upon domestic actors. Unlike other instruments, however, the ability to

206. Kirshner posits, "Given a reasonably integrated international market economy, monetary power, in theory, should be the most potent instrument of economic coercion available to states in a position to exercise it." Currency and Coercion, pp.30-31.
discriminately affect particular actors within a target state (e.g., government or market actors) is less. In this sense, currency manipulation is a blunter instrument whose use affects many economic actors and the target's government. It is also an instrument that can be easily severed in theory, as either state can sell off its holdings of the other's currency. A target’s ease in doing so will depend on the costs to it in no longer holding and using the sending state’s currency (e.g., limiting trade financing).

George Goschen was one of the first theorists to address the determinants of currency values and the functioning of currency market exchanges, and his insights into the fundamental nature of currencies as exchange instruments among states is still valid. He held that currency values and fluctuations are determined by the overall relation of indebtedness between any two states: "It [i.e., mutual indebtedness and currency valuation] will be discovered to result not so much from the exchange of their respective produce as from the relative totals of all the amounts expended by each upon the other, whether in payment of produce and manufactures, or for the purchase of shares and public securities, or for the settlement of profits, commissions, or tribute of any kind, or for the discharge of the expenses incurred in foreign residence or travel: in fact, from the entire payments (or promises to pay) which pass between the respective countries."207 Changes in currency values react to and affect all of the forgoing elements of inter-nation indebtedness, and provide the opportunity for pressuring or supporting governments and other actors in target states.

Because the banking sector acts as an intermediary for much of the currency exchanged between states, its relationship with the central government is critical to the

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Although banks may independently exchange currencies across states, they often must exchange holdings of currencies with their central bank in order to fulfill their obligations. Ideally, through this activity and other oversight responsibilities, central banks assess how much of their currency is held abroad and how much foreign denominated debt is owed by the government and its market actors. This net foreign currency exposure position can then be compared to the central bank's reserve holdings (i.e., its foreign currency, gold, silver and/or other reserve asset holdings). States are potentially vulnerable if their reserves are not sufficient to cover the value of their potential currency liabilities at an existing exchange rate (i.e., currency held abroad and foreign currency obligations from debt instruments). This vulnerability becomes apparent when currency market activity changes the value of a state's currency in an undesired direction.

Government action toward a target state takes three principal forms. First, governments may enter the currency markets with their own reserves, buying/selling a target's currency according to its policy goal. Second, governments may influence market actors in the currency markets to act according to their policy goals and buy/sell a target's currency. This can be accomplished by influencing market sentiment toward a target state and its currency through private statements of approval or disapproval regarding a particular currency value or underlying factors affecting its value (e.g., inflation rate, current account balance, interest rate, debt burden etc.). This method can also be accompanied by smaller scale, yet public or open, government buying/selling of a

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208 Kirshner noted: "The domestic ramifications of manipulation also motivate actors within the target society. Especially important is the relationship of the banking community to the central government (as seen in the Agadir crisis), and particularly the relative political power of these two sectors." Kirshner, Currency and Coercion, p.267.
target currency as a signal to market actors. Third, a government may influence a target by affecting its monetary reserve composition, pressuring, supporting or binding a target state. In any of these modalities, the initiating state will draw on its financial base (i.e., government reserves and foreign currency holdings) and possibly that of its market actors as well. For example, buying a target's monetary reserve assets (e.g., gold, silver) and substituting them with one's own currency binds the target to oneself and limits its autonomy in purchasing goods or financing international activities. Because these are not limitless bases of economic power, the initiating state should monitor the extent of its exposure to a target and its own reserve position.

Pressure on a target state can be brought by forcing the target to use its monetary reserves to defend a currency value, cover its banking actors' foreign debt obligations, or by devaluing the assets/currencies that constitute its governmental reserves. This would then force the target state to acquire fresh reserves to defend the value of its currency or reserves, and possibly stimulate decreased confidence in the currency across the world's currency markets, yielding greater pressure on its reserve position. Support for a target can be pursued by transferring monetary reserve assets (e.g., gold) at better than market rates (e.g., in times of crisis on favorable repayment terms), or by supporting a currency value through market intervention. Binding a target may occur by influencing the composition of a target's reserves. If a target state can be induced to accept a greater proportion of its exchange reserves in one's own currency, then the target is increasingly likely to desire stability in its value and therefore the political relationship with oneself. This development occurs far more subtly than an overt market intervention and has the

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209. The transfer of reserve assets generates cumulative gains for the target as its ability to expand its economy (i.e., increase its money supply) or purchase other international assets increases.

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added benefit of working on a target state by influencing it to act in its own interest in seeking stability in one's own currency value. In this manner, political stability between the target and oneself is the logical corollary to the pursuit of self interest by the target.210

Whether the target state will view its holdings of a rival currency in this positive self-interested light will depend on its perception of the currency's value and importance to its other financial activities (i.e., habituation to using these reserves to pay for foreign goods, as collateral on foreign loans, or recycled into the rival's investment instruments/assets). Vulnerability between the two states will depend on the pervasiveness of the initial state's currency in the target. The target state is vulnerable when its currency holdings are predominantly one's own currency and this value is not significant in its trading across the world markets. A situation of mutual vulnerability arises, however, if the target recycles its currency holdings into the initial state's assets (e.g., government bonds) and comes to hold a significant position such that selling them would hurt the initial state.

These conditions and vulnerabilities are likely to change over time as the size and composition of currency markets and government reserves change. Nonetheless, influence may be created through policies that affect these markets and holdings (e.g., allowing trade surpluses to accrue to a target state so that balances of one's currency come to represent a larger proportion of the target's reserve holdings). The ability to implement this instrument depends on the target's degree of exchange exposure and the importance of international economic relations to it (e.g., important political actors involved in foreign banking or trade operations, or need for foreign currency earnings to

210 Kirshner, Currency and Coercion, p.119.
pay foreign loans). If the government itself is relatively exposed to currency manipulation (e.g., with large foreign-denominated debts or large balances of its currency held abroad), then it is potentially vulnerable. Similarly, if private and semi-government actors (e.g., state banks) have large foreign currency exposure positions they and the target government, as guarantor of the currency and banking system stability, are potentially vulnerable.
CHAPTER 3

U.S.-JAPAN, 1918-1922

3.1 Case Introduction and Summary

This dissertation examines the economic and security relations between the U.S. and Japan beginning in 1918. It evaluates four theoretical perspectives’ expected economic exchange observations against a more comprehensive historical record than in previous political science research, and in so doing, provides a better explanation of this critical interwar great power relationship. Hypotheses and observable implications from the theories have been drawn out to assess how changes in state threat perception and state relations with corporations affect exchange with a rival. The U.S. perceived Japan as a significant threat to its interests and an obstacle to achieving U.S. grand strategy throughout the full temporal domain of the case. U.S. threat perception of Japan was, however, not encased within a strictly bilateral relationship. The role of Britain in U.S.-Japan strategic interaction loomed large throughout the case. Other countries also grew in importance as both objects and material actors affecting the U.S.-Japan economic and security relationship.

U.S. government relations with its corporations doing business in and around Japan were similarly complex as state officials were not always capable of achieving their preferences in exchange relations with Japan. U.S. corporations were also not
always capable of achieving their preferred U.S. government decisions or in their exchange relations with Japan. Although there were many critical aspects of U.S. exchange relations with Japan (e.g., government loans, direct investment in autos etc.), trade and investment decisions related to petroleum products were the most critical across the whole period of the case. Japanese officials understood this, as did American, British and Dutch. The highest ranking Naval officer to be interrogated after the war held:

> the interest in the (southern) national resources area was neither mainly Naval or Army, both were equally interested...after the U.S., G.B. and the Netherlands refused to sell any more oil, our country was seriously threatened by oil shortage. Consequently, every element in Japan was keenly interested in that region. I think one of the large causes of this war was the question of oil.\(^{211}\)

This dissertation examines the roots of this and other Japanese economic vulnerabilities to the U.S., and improves upon the existing historical analysis of U.S.-Japanese interwar relations (e.g., Irvine Anderson). This analysis is more comprehensive because it focuses on the strategic interactions surrounding oil resource control, supply through trade and decisions regarding synthetic alternatives going back to the end of WWI. The key patterns of all later decisions and relationships were first established in the aftermath of WWI and this dissertation draws out their significance. This dissertation also improves on our understanding of the interactions among the companies that battled for sources and markets and the statesmen who affected the outcomes of these interactions. Other than the Presidents of the United States, Stanley Hornbeck emerges as the key official across the entire case, not only because of his Asian policy leadership

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at the State department, but also because of his critical role in U.S. policy regarding the global oil game with the British and the Dutch. By 1923, he assumed the leading role in formulating U.S. oil strategy within overall U.S. grand strategy. He helped arrange the successful insertion of substantive U.S. oil interests into the Dutch East Indies and was the chief official responsible for Anglo-American-Dutch relations regarding Asia and oil issues in Asia.

This dissertation employed extensive sources of original information to analyze the important economic and security developments in the case. Among other original and secondary papers, these sources include documents from the Office of U.S. Naval Intelligence (ONI), U.S. State department archives and the personal papers of Stanley K. Hornbeck and Arthur N. Young, Economic Adviser at the State department and later chief financial adviser to Chiang Kai-shek’s Nationalist government. The use of ONI sources, in particular, was warranted because of their position as the lead intelligence agency gathering information on all economic and security issues in Asia. Their role increased in importance throughout the temporal domain of the case, particularly under President Roosevelt, an old navy hand himself. ONI’s analyses were relied on by State department officials and after April 1938, the Standing Liaison Committee among the War, Navy and State departments harmonized overall U.S. policy toward Japan using ONI analyses.

Every Monday, State, War and Navy officials met in Hornbeck’s office to coordinate action and analyses that were then acted upon by the Secretaries of State, War and Navy. Hornbeck used his position of bureaucratic influence to ensure that American policy did not act precipitously to threatening developments in Japan and across Asia.
He had been playing this role, however, long before the critical days during the late 1930s. Hornbeck helped institute American economic exchange policy toward Japan as part of U.S. grand strategy beginning in 1917, and more importantly, he engineered the critical Anglo-American-Dutch cooperation that was built on Japanese exclusion and dependence on the U.S. Forging the key state and corporate oil relationships was a halting and messy process, one which the companies tried to exploit to their advantage, often at the expense of stable state relations. Throughout the whole period of the case, naval arms competition and political settlements among the U.S., Britain and Japan were intimately bound up with oil resource ownership and supply arrangements.

The subtext of all negotiations on naval arms control and political order from the Washington Conference (1922) forward continued to be Anglo-American cooperation and discord amidst buckpassing of the Japanese threat to each power's interests in Asia. Naval armaments and power projection in general were intimately related to secure control of oil resources, and this relationship grew exponentially more important and evident throughout the period as all naval vessels became fired on fuel oil and the planes for aircraft carriers required more highly refined fuel. National power itself came to rely on control of these resources and the technology developments that affected them. Japan's inability to secure self-sufficiency in oil and the use of its overall economic vulnerability by the U.S. for political purposes set the stage for its later alliance with Germany, and choice between conflict with the Soviet Union, the Anglo-American-Dutch entente or both.

Oil was not the only exchange that mattered between the U.S. and Japan, however, and changes in other exchange areas had critical effects on Japanese economic
vulnerability, dependence and broader U.S.-Japanese relations. State finance and
government loans mattered substantially in U.S.-Japanese exchange and increased
throughout the period after the Washington Conference. To better capture these
variations in exchange, the temporal domain of the case was divided into five periods.
This allows for more detailed assessment of changes in U.S. threat perception, state-
corporate relations and the overall exchange characteristics between the U.S. and Japan.
These case periods also neatly provide smaller case studies within the larger U.S.-Japan
interwar case. Each period displayed some variation in threat perception, state-corporate
leadership in fulfilling exchange preferences, and overall characteristics of Japanese
economic autonomy vis a vis the U.S. (See Table 3.1 at end of this introduction).
Assessment of these variations has led to better theory evaluation, hypothesis refinement
and measurement of economic exchange.

The first period (1918-1922) encompasses the initial, tense period of U.S.-Japan
relations and ends in the Washington Conference settlement. The second period (1923-
1929) begins in the threat-reduced aftermath of the Washington naval arms accords and
ends in mid-1929, when Japan's domestic political system was beginning to show signs
of increased internal stress. This period ends with the return to power of moderate
civilian leaders but a tenuous domestic base of support for their rule built partly on
exchange gains from cooperation with the U.S.. The third period (mid-1929-early 1933),
covers Japan's acute domestic factional competition and the U.S. role in providing a
proximate cause of the downfall of moderate, cooperative leadership in Japan. The
fourth period (1933-1936) covers President Roosevelt's first term and a redirection of
U.S. economic exchange policy toward Japan during a period when U.S. threat
perception of Japan was beginning to be sublimated within its grand strategy covering Europe and Asia. The final period (1937-1941) covers the complex and volatile time when state alignment and exchange relations were changing across the world and U.S. exchange responses to increased threat perception of Japan fulfilled multiple objectives vis a vis Japan and other countries.

Despite the state-centric characterization of the case periods reviewed above, corporate actors were not quiescent subjects of state authority. At multiple points within this analysis state-corporate exchange preferences diverged and contests over appropriate outcomes were clear, allowing for hypothesis testing and validation (See Appendix C for a list of exchange events). There was no overarching pattern to the corporate challenges to state authority, except that they were observed less as Japan's military threat to corporate operations grew after 1938. After this point, there were not as many objections raised to state authority over economic exchange with Japan. This did not mean, however, that the theory evaluation became similarly limited. In contrast, the increasing threat posed by Japan greatly affected U.S. exchange changes with Japan, but often in ways that were not related to strictly bilateral U.S.-Japan relations. The grand strategic environment of U.S.-Japan relations became a more important factor as war approached, leading to increased exchange in some areas that were not predicted by the various theories.
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Table 3.1: Case Period Summary. Values from start of period with changes through end of period. Bilateral exchange values from Japan's perspective.
3.2 Chapter Overview

U.S. threat perception of Japan at the start of this period was high and growing due to Japan’s continued expansionist activities, which in China were particularly offensive to U.S. leaders. U.S. leaders were also alarmed by the facilitation of Japan’s expansion through the Anglo-Japanese alliance and the execution of secret protocols thereunder at the Versailles Conference. At that Conference, Japan was able to gain British backing for recognition of Japanese claims to all former German colonial possessions in Asia, including islands surrounding U.S. possessions and naval outposts in the Pacific and the rich territory of Shantung province in China. U.S. threat perception of Japan would continue to increase across the 1918-20 period for several reasons. First, in late 1918, Japan overstepped its commitment to allied intervention in Siberia, sending an extra 60,000 troops there and causing significant concern in the U.S. regarding the Japanese government’s intentions and ability to control its army.

Second, Japan’s continued operations in the Russian Far East provided it with the pretext to seize the remaining half of Sakhalin island in 1920. This island’s known oil resources would enhance Japan’s potential autonomy in energy resources and naval power, and demonstrated its willingness to use force to acquire these resources. Third, Japan announced a large-scale naval building program in 1920 which, if completed, would not only enshrine Japanese dominance in the Western Pacific, but also possibly challenge the U.S. position across the entire Pacific. Finally, the lack of Anglo-Dutch cooperation with the U.S. on Dutch East Indies (DEI) oil resource sharing, while
guaranteeing DEI oil to Japan under the Anglo-Japanese alliance, and the potentially ominous worst-case scenario of that alliance turned against the U.S., caused U.S. threat perception to increase and focus on both Japan and Britain. To lessen this threat, the U.S. chose to pressure Britain to end the alliance and agree to a set of new treaties to re-order economic, political and military relations among the U.S., Britain and Japan. This was accomplished in the Washington Conference treaties of early 1922, and Japan complied with most of its threat-reducing pledges by the end of the year (e.g., withdrawal of troops from Shantung).

At the end of this period, U.S. threat perception of Japan was beginning to moderate and drift downward from its previously high level because Japan did retrench from its forward positions in Siberia and parts of China. Prior to this, however, the U.S. government acted to affect Japan’s expansion using the existing asymmetric trade relationship in silk and cotton goods. The U.S. suspended cotton exports to and silk imports from Japan in November 1918, causing potentially great economic hardship in Japan. Japan reacted rather swiftly to this and drew down its forces in Siberia, thereby establishing the interaction dynamic of U.S. economic pressure on Japan to circumscribe its international expansion and domestic factional competition (e.g., civilian leaders v. army). This exchange action was more important than any other in the period because it was a direct and purposeful U.S. government action tied to Japanese foreign expansion behavior. This action conforms to offensive realism because it was premeditated, aimed explicitly at changing Japan’s behavior by compromising its economic autonomy, and intended to affect the Japanese army’s position within Japan’s domestic factional competition.
The 1920-21 jockeying for position between Standard Oil and Royal Dutch Shell was also critical during this period and foreshadowed state and corporate interactions in the coming years. Royal Dutch Shell sold U.S. navy fuel oil reserves from California to the Japanese navy and Standard Oil threatened to sell its few assets in the DEI to Japanese interests because it was not gaining any new oil concessions there. These corporate actions upset governmental actors in each country (e.g., U.S. navy) and heightened Japan's concerns regarding the security of its own oil supply as all navies converted to fuel oil from coal. Standard Oil did not, however, act unilaterally. The U.S. State department was given prior notice of its sale offer to Japan and chose to allow this calculated pressure on the Dutch to go forward. For these reasons, this event is consistent with offensive realism, liberalism and marxism, because both the state and companies wanted to pressure the Dutch using its fear of Japan to gain a better position (i.e., convergent state-corporate preferences in offensive action).

The state wanted a better position in the oil arrangements of the British and Dutch, and influence over the future disposition of DEI oil to Japan guaranteed in the Anglo-Japanese alliance. The company wanted more equal access to DEI oil rights and greater U.S. government assistance in achieving those rights. On balance, the U.S. government was predominant over corporate preferences in this period, particularly in the most important instance of trade cessation in 1918. And, the U.S. government used exchange to limit Japan's bid for greater autonomy-enhancing resources in Siberia, Shantung and the DEI. For these reasons, this period was best explained by offensive realism.
The overall bilateral exchange relationship between the U.S. and Japan was narrow, existing only in trade, and concentrated in relatively few items. Japan benefited more than the U.S. did from this trade because it imported steel and machinery, while the U.S. took largely only silk luxury items that did not release any efficiency gains from specialization in the U.S. economy or contribute to U.S. production in a meaningful way. More pointedly, trade with the U.S. represented approximately 9% of Japanese GDP, while the Japanese trade never was worth more than 1% of U.S. GDP. Nonetheless, Japan's vulnerability to the U.S. was lower in this period than in subsequent ones because Japan was not yet dependent on the U.S. for majority supply of any strategic items (e.g., oil imports from U.S. averaged under 25% of total Japanese oil imports). For this reason, Japan's bilateral dependence was moderately high due to its large trade partner concentration on the U.S., but not as high as it would become in the 1930s.

3.3 Japanese Expansion during WWI and its Immediate Aftermath

Before WWI the U.S. and Japan engaged in reciprocal expansion and rivalry for influence in Asia, as each great power extended its interests in China and elsewhere. For Japan, the Kurile Islands (1875), Bonins (1876), Taiwan, the Pescadores and

Ryukyus (1895), South Sakhalin (1905) and Korea (1910) provided opportunities for political, economic and military expansion. The U.S. advanced westward with control and then annexation of Midway and the Aleutians (1867), and Hawaii, Guam, Wake and the Philippines (1898).\textsuperscript{213} In this and later periods, the principal and interlocking foci of American-Japanese rivalry and American threat perception were: Chinese economic and political development; Siberian and Russian territorial issues; the trade in and development of petroleum products; the naval force balance; and the Anglo-Japanese alliance which ensured Japanese gains and Anglo-American discord. These interlocking relationships continued throughout the interwar period and were manifest in the strategic decisions made by the principal states.

As WWI began, Japan dispossessed Germany of its colonies in China and the Pacific Ocean, cloaking its actions in alliance responsibilities with Britain. James Crowley noted, "the limited role envisioned for Japan by the British government was, however, supplanted by a resolution to seize the German possessions in Shantung as well as the German Pacific islands."\textsuperscript{214} Japan's acquisitive behavior alarmed Britain and other European powers, but disturbed the U.S. more because it saw itself as the most important protector of latent Chinese sovereignty and territorial integrity. Japan's challenge to this position was reinforced with Japan's issuance of the Twenty-One Demands onto China and the signing of the Sino-Japanese treaties in May 1915.\textsuperscript{215} Among other items, these

\textsuperscript{213} Akria Iriye noted the interactive nature of U.S. and Japanese expansion, "the net effect of America's Pacific imperialism (Philippines) was to forestall Japanese expansion in the same regions." Iriye, Pacific Estrangement, p.60. See also Thomas H. Buckley, The United States and the Washington Conference, 1921-1922, (Knoxville, TN: University of Tennessee Press, 1970), pp.90-93.


\textsuperscript{215} Burton Beers noted, "Japan's entry into the war. Lansing pointed out, increased prospects for the intensification of the American-Japanese rivalry over China." With Japan's 21 Demands this conflict over
treaties stipulated that former German rights in Shantung were to be "completely left to the free disposal of Japan," while Japan's existing rights in South Manchuria and Liaotung were extended for 99 years.\(^2\)

President Woodrow Wilson and Secretary of State Robert Lansing responded to these unilateral actions by trying to temper Japan's China ambitions and neutralize China's economic and political development. The result of this effort was the Lansing-Ishii Agreement of November 1917. This agreement came at the price of U.S. recognition of Japan's "special interest" in northern China, which the U.S. would subsequently seek to recover at the Washington Conference. In late 1917, Japan accepted the Open Door principle for Chinese trade and development and recognized the goal of independence and territorial integrity for China. In exchange for this recognition and pledge to respect China's sovereignty, the U.S. recognized that Japan had "special interests" in the Chinese territory "to which her possessions are contiguous" (i.e., South Manchuria and Eastern Inner Mongolia contiguous to Shantung).\(^2\)

Lansing, and to a lesser extent the British, wanted to further neutralize China's development by internationalizing the loan policies of the major powers in China, preventing exclusive Chinese reliance on any one foreign government for its financing. This effort was directed at containing Japan's unilateral loan policies which demanded political

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Footnotes:

\(^2\) Burton, Vain Endeavor, pp.20, 36-41. Crowley, Japan's Quest for Autonomy, p.19. Other important Demands included the military and naval demilitarization of Fukien province, opposite Taiwan, and iron ore development rights in Anshan, South Manchuria. See also Barnhart, Japan Prepares for Total War, p.28.

\(^2\) Burton, Vain Endeavor, pp.115-6. American recognition came on the heels of 50,000 Japanese troops landing in South Manchuria between June and August 1917. Japan sought to have its interests in China recognized as being intimately related to its security, justifying exclusion of other actors.
concessions from China with each capital extension. This effort was also inspired by America’s desire to lessen the deleterious effects on China’s development from unilateral Japanese acts accepted by Britain due to the Anglo-Japanese alliance. The negotiations on the China loan consortium began in 1918, but dragged on until October 1920 due to Japan’s desire to retain an exclusive sphere of financial influence in South Manchuria and Eastern Inner Mongolia and have it legitimized by the other parties (i.e., Great Britain, U.S., and France). On October 15, 1920, the first meeting of the parties to the China loan consortium (aka. the Lamont-Kajiwara Agreement) took place under hopeful American observation.

The failure to cooperate in 1918-9 on politically neutralizing the development of China was overshadowed by the conflict surrounding the Allied intervention in Siberia beginning in August 1918. President Wilson acted to moderate Japan’s plans for an

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218. See Beers, Vain Endeavor, pp.142-148; Hogan, Informal Entente, pp.84-96. This practice was most evident in the Nishihara loans of late 1917 and 1918 that yielded Chinese concessions in Manchuria and complicity in Shantung. Fifield, Woodrow Wilson and the Far East, p.98; Beers, Vain Endeavor, pp.117-8.

219. Beers, Vain Endeavor, pp.173-176. Throughout these efforts Western and Japanese bankers served the interests of their home states, acting in "close liaison with their governments." Fifield, Woodrow Wilson and the Far East, p.98. Multilateral management of China’s debt financing set a precedent for inclusive, joint management of important economic development projects in Asia, a standard that the Dutch government was hesitant to see spread to its colonial possessions. For this reason the Consortium was a mixture of state-sponsored financial cartel and liberal-marxist banker preferences.

220. See memorandum from Nelson T. Johnson. American Minister to China, to Secretary of State, “Japanese Government Withdraws Reservations and Accepts Lamont-Kajiwara Agreement,” November 1920, Box 230, Folder: Japan: China Trade, 1921, Stanley K. Hornbeck Papers, Hoover Institution on War, Revolution and Peace, Stanford University, Stanford, California. hereafter cited as “Hornbeck Papers.” Johnson noted the commitment of the allied Bankers in China to “participate on equal terms in undertakings having in view the assistance of China in the establishment of great public utilities...The consortium agreement of October 15, 1920 goes farther than any previous plan in that it provides for international cooperation in railway and other industrial enterprises...a practicable step toward the elimination of the conflict of national interest in competition for Chinese business.” Japan did succeed, however, in restricting consortium activities to not include South Manchurian Railway Co. properties and mines in Manchuria.

extensive and unilateral intervention and to restore order in the Russian Far East. 222

Original troop commitments were to have been moderate and roughly equivalent, with Japan and the U.S. each supplying 7,000 troops. The Japanese amended this quickly claiming a need for 10,000-12,000 troops with any additional troop needs subject to Allied consultation. 223 This pledge was not kept as Japan dispatched approximately 72,000 troops by September 1918 and seized the Chinese Eastern Railway, extending Japanese army forces westward to Lake Baikal. 224 Japan's rapid expansion into Siberia exposed the divisions within Japan's government. The army and its main political support (i.e., the Satsuma-Choshu clique, led by Prince Yamagata, senior of the Genro and General Terauchi, Premier of Japan) was increasingly opposed by powerful political parties and cliques with internationalist Genro leaders favoring less antagonistic relations with the U.S. and Great Britain. 226 The internationalist faction was encouraged by Genro Saionji Kinmochi, who helped establish the principle and practice of party ruled cabinets in Japan, and Admiral Kato Tomosaburo who led the Western-oriented Japanese navy. 227

As the army expanded rapidly across Siberia, the wisdom and ability of the Terauchi-led cabinet to control the intervention was challenged by the leader of the largest political party in the Diet, Hara Kei of the Seiyukai party. 228


225. The Genro were the remaining Meiji Restoration elder statesmen who acted as an advisory group.


228. Diet criticism of Japan's army activities was "severe," and set a precedent for political party competition over foreign policy that continued until the near total militarization of Japan's political system.
Hara mobilized support from his parliamentary base and position on the Gaiko Chosakai (foreign policy deliberative committee) to enlist the support of the Genro in forming a new government.²²⁹ Hara became Premier on September 29, 1918, replacing Terauchi, and sought to regain cabinet control of the army's general staff and operations in Siberia. For the first time Japan was led by a party politician, who "was indebted partly for his prominence to commercial, industrial, and financial elements, and who might be expected to be more responsive to these groups than were his predecessors."²³⁰ Partly because Hara was unable to limit the army's operations in Siberia, in November 1918, the U.S. acted to curtail the expansion through diplomatic and economic pressure.²³¹

In the only published account, the December 1918 Japanese withdrawal of 14,000 troops and near-term commitment to withdraw another 34,000 resulted from President Wilson's order on November 18, 1918, that the U.S. War Trade Board suspend U.S. cotton export licenses to Japan and silk import licenses from Japan.²³² These items were

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²²⁹ Crowley, Japan's Quest for Autonomy, pp.23-24.
²³⁰ Beers, Vain Endeavor, p.139. The Japanese business community was inclined toward cooperative relations with the West and the U.S. in particular as it saw its future development tied more to trade and investment with the U.S. than Britain.
²³² Douglas noted these commodities were chosen due to limited substitutes for Japan, unlike in iron and steel, where British cooperation would be required straining its existing alliance with Japan and implicitly its relations with the U.S.. In fact, silk exports to the U.S. represented 65% of Japanese exports to the U.S., roughly 18% of total Japanese exports, while the value of Japanese cotton imports was less, at roughly 12% of total Japanese imports. See United States Tariff Commission, The Foreign Trade of Japan: A Study of the Trade of Japan with Special Reference to that with the United States. (Washington, DC: Government Printing Office, 1922), pp.198-203. These licenses were restored shortly after Japan began its troop withdrawals in December with little
among the many subject to licensing and review by the War Trade Board; however, the U.S. did not restrict iron or steel exports to Japan for example. Instead, the U.S. chose those items that Japan could not easily substitute and caused the most pain to the Japanese army's political base (i.e., the agrarian sector of Japan). The U.S. also chose those items it could act upon unilaterally because joint sanctions with the British were highly unlikely given Anglo-Japanese alliance considerations. Interestingly, the U.S. tried to use the export licensing requirement to define the end users of American exports in Japan better and requested the Japanese-American Chamber of Commerce in Tokyo to begin these analyses. Licenses had also been delayed previously in order to influence Japan's decision to cooperate on the U.S. railway plan for Russia's Far East under the direction of John F. Stevens.

The selection of cotton and silk products cut at the Japanese army's sociopolitical base of support in Japan (i.e., the agrarian sector and rural economy), and put pressure on Japan's banking sector which relied on the dollar earnings to finance imports and service British pound-denominated debt. Whether U.S. economic pressure or Hara's own desire for better relations with the U.S. and control over army operations contributed
effect on the trade statistics for 1919. See also letter of U.S. Naval Attache, Tokyo, noting importance of Japan's silk exports in its capital financing operations (e.g., servicing British loans): "The large flow of business between Japan and America has a stabilizing influence on the relations between the two countries, and this influence is still increasing...Japan has learned the power of the boycott to her sorrow." Office of Naval Intelligence, Reports, March 31, 1923. File c-10-b. Register 18992, Record Group 38. Records of the Office of Naval Intelligence, National Archives, hereafter cited as "RG 38."

Letter from War Trade Board to R.S. Miller, Bureau of Far Eastern Affairs, State Department, September 9, 1918, file 694.119/242, Record Group 59, General Records of the Department of State, National Archives, Washington, D.C., hereafter cited as "RG 59." At this time the U.S. also decided to use licensing forms identical to those used by Great Britain so as not to confuse the Japanese, and possibly also to imply coordinated U.S.-British policy toward Japan.

Letter from Roland Morris, U.S. Ambassador at Tokyo to Secretary of State, October 31, 1918, file 694.119/245, RG 59.

more to the moderation of Japan's Siberian operations is still indeterminate.\textsuperscript{236} What is clear, however, is that the U.S. planned to use the wartime licensing of the silk and cotton trade as leverage over Japanese policies, and for this reason this decision is consistent with offensive realism.\textsuperscript{237} A memorandum prepared late in WWI by Stanley K. Hornbeck, then serving as Technical Expert, Office of Economic Advisor, U.S. Department of State, contended: “the issuing of the imports licensing order by President Wilson injects a new feature and gives the United States a new weapon...making it appear that this is a special concession (continuing Silk imports) evidencing our friendship and good will...Japan has Silk. The United States is her market for Silk. The United States could do without Silk.”\textsuperscript{238}

3.4 Versailles Conference and the Russo-Chinese Resource Dimension

Japan's troop withdrawals and acquiescence to an inter-allied railway board for Siberia on American terms helped lessen their rivalry as the Paris Peace Conference negotiations began in January 1919. At these negotiations, however, Japan initially demanded recognition of its control over the Shantung possession in China as per its

\textsuperscript{236} The official response of the Japanese government was delivered by ambassador Ishii on December 28 and noted troop withdrawals due to “consideration of the turn in world affairs, the Siberian situation, and the intention of the United States government.” Kamikawa, Japan-American Diplomatic Relations, p. 368, emphasis added. The precedent of the U.S. signaling its intentions to the Japanese government and attempting to influence its decisions through economic pressure was established at this juncture, not later after Manchuria (1931).

\textsuperscript{237} The U.S., however, reconsidered the cotton export suspension almost as soon as it went into effect due to “domestic considerations,” noting that “import restrictions (i.e., Silk) will suffice for our purposes.” This might have become salient if Japan had not complied so quickly. See telegram McCormick, U.S. State department to Morris, Ambassador at Tokyo, November 22, 1918, file 694.119/255a, RG 59 and Telegram from Polk, U.S. State Department, to U.S. Embassy at Tokyo, December 3, 1918, file 694.119/264a, RG 59.

\textsuperscript{238} Hornbeck memo dated 1917-1918, “Concerning Negotiations for Cooperation between the United States and Japan,” in Hornbeck Papers, Box 240, Folder: Japan: How to Coerce. The mere maintenance of existing or normal trade became a positive increase in trade and political relations, without any corresponding increase in the value of trade. It is precisely this political context surrounding trade issues that matters the most, not any transient changes or stasis in the value of the trade.
treaties with China and continued control over the German islands in the Pacific.\textsuperscript{239} Japan was willing to withdraw support for the League of Nations if its core interests in Shantung were not settled to its liking.\textsuperscript{240} Due to President Wilson's overarching interest in the League of Nations, Japan was able to secure recognition of its possession in Shantung "in return for (only) oral assurances that Chinese sovereignty in Shantung would be restored at an unspecified time."\textsuperscript{241} The former German island possessions (i.e., the Marianas, Carolines, and Marshalls) occupied by Japan since late 1914 were of greater strategic significance to the U.S. as they surrounded the American possession of Guam and straddled the access route to the Philippines.\textsuperscript{242} The U.S. was alarmed by Japan's desire for outright control of these islands and was only able to maneuver Japan into accepting continued occupation of these islands under a May 7, 1919 League of Nations mandate with the provision of their non-fortification. Britain's self-interested support of Japanese claims greatly angered the American delegation and set the stage for much of the post-conference Anglo-American wrangling over oil rights and the possible renewal of the Anglo-Japanese alliance.

Competitive relations between Japan and the U.S. continued after the Versailles Treaty was signed in June 1919, as did the U.S. perception of an expansive and

\textsuperscript{240} Ibid., p.173. Japan made this threat explicit immediately after the Italian delegation withdrew from the conference on April 23, 1919, preying on a vulnerable President Wilson.
\textsuperscript{241} Beers, \textit{Vain Endeavor}, p.160. In response to its treatment, China did not sign the Versailles Treaty, although it did sign other treaties and become a League member. U.S. collaboration with the Chinese delegation was significant and China's disaffection was felt by many U.S. supporters, including Hornbeck and other Asian specialists. See Kenneth G. McCarty, "Stanley K. Hornbeck and the Far East, 1931-1941." (Ph.D. diss., Duke University, 1970), pp.15-16.
\textsuperscript{242} Fifield, \textit{Woodrow Wilson and the Far East}, pp.137-139; Buckley, \textit{The United States and the Washington Conference}, pp.90-92. The U.S. was greatly troubled by yet another negative example of the effects of the Anglo-Japanese alliance on the Far East. Japan and Great Britain signed a secret Anglo-Japanese accord (February 1917) dividing the former German islands between them (Japan those North and Great Britain those South of the equator) and pledging to recognize each other's claims in any eventual peace treaty negotiations, as they did at Versailles.
increasingly threatening Japan.\textsuperscript{243} By early 1920, the allied intervention in Siberia was proving to be counterproductive as Bolshevik forces were strengthening and stability in the region was giving way to increased partisan warfare and Japanese intransigence.\textsuperscript{244} The U.S. and other allies withdrew all forces between February and April 1920, leaving Japan a freer hand in a worsening situation. Japan's assistance to Cossack partisans led to reprisals as the allied forces withdrew, culminating in a massacre of over three hundred Japanese prisoners and others at Nikolaevsk in March 1920.\textsuperscript{245} This city was on the Russian mainland directly opposite North Sakhalin Island, and on July 3, 1920, the Japanese army used this incident to justify their long-desired occupation of North Sakhalin.\textsuperscript{246} This territory was significant to Japan's quest for economic self-sufficiency due to its oil reserves, which by 1919 had begun to be developed by the Japanese navy.\textsuperscript{247}

Japan's occupation of N. Sakhalin and decision to build a fleet of sixteen capital warships to retain its dominance over American naval forces in the Western Pacific alarmed American leaders and further stimulated corporate and state competition for oil resources in the region.\textsuperscript{248} The post-WWI shift to petroleum-fueled naval vessels and perceived worldwide shortage in petroleum also stimulated this competition, and forever

\textsuperscript{243} Beers noted the Shantung controversy "deepened suspicions between the two countries." Beers, Vain Endeavor, p.168.
\textsuperscript{245} See Office of Naval Intelligence, File c-10-k, Register 13351, undated report entitled "The Nikolaevsk Affair and the Occupation by the Japanese of Nikolaevsk and Sakhalin," RG 38. See also Kamikawa, Japan-American Diplomatic Relations in the Meiji-Taisho Era, pp.378-9.
\textsuperscript{246} See Report from Lt. F. V. Martinek to Director of Naval Intelligence. Martinek noted Japan's pre-massacre desire to take complete control of all of Sakhalin by occupying N. Sakhalin "because of the recent fuel, metal and mineral discoveries there." Office of Naval Intelligence, Reports, January 4, 1921, File c-d-1, Register 13954, RG 38.
\textsuperscript{247} Barnhart, Japan Prepares for Total War, pp. 28-9; See also ONI report at File e-10-d, Register 13177, RG 38.
\textsuperscript{248} Crowley, Japan's Quest for Autonomy, p.26.

132
bound the issues of naval force levels, oil supplies and territorial expansion. The U.S. State department increased its global analysis of Standard Oil and Royal Dutch Shell relations and the political import of state competition for oil concessions. This analysis noted the British-Dutch alliance in ownership of Royal Dutch Shell and the guarantees of this company’s secure operations by the British navy, and hence the importance of Anglo-American understanding for peace in the oil world and control of this vital element of naval power projection. State department analysis was supplemented by an extensive U.S. Navy intelligence program that used Standard Oil officials among other overseas American corporate officials as sources for Japanese information. This intelligence was used by American officials to understand Japan’s oil dependency, particularly the corporate and state actors that supplied Japan. This information demonstrated the primacy of the British government and the Royal Dutch Shell Co. in supplying Japan, and underscored how the competition for oil sources and markets that


250. See Pictorial Exhibit 1 in Appendix B. March 1915, of Office of Naval Intelligence relations with Standard Oil, Vacuum Oil Company and American Tobacco. See also Memorandum from Fred Rogers to Director of Naval Intelligence, May 29, 1919 detailing corporate commitments and representatives responsible for transmitting information regarding Japan to naval attaches abroad and ONI directly. These representatives included H.E. Cole, Superintendent of the Far Eastern Division of Standard Oil of New York, who instructed Standard officials in Yokohama to cooperate with the U.S. naval attaché at Tokyo, E.H. Watson. National City Bank, US Steel, the Vacuum Oil Co. and General Electric also explicitly identified representatives for intelligence work regarding Japan. Lt. Commander John A. Gade USN later wrote to Director of Naval Intelligence, August 5, 1926, confirming the “essential cooperation of businessmen as cloaks to the transmittal of news as well illustrated by the Japanese situation.” Lieutenant Gade noted the particular help of bankers and the Federal Telegraph Co. in tracking Japanese purchases and plans. For all three documents see Records of the Office of Naval Intelligence, Security-Classified Correspondence Covering Plans for Intelligence Service through American Commercial Firms, 1915-1931, Entry 83, RG 38.

251. See, for example, Office of Naval Intelligence three part report, “Oil Situation of Japan,” January 1921, File o-1-g, Register 14039, RG 38.
the American government and U.S. oil corporations were engaged in would necessarily conflict with Britain and its policy toward Japan.\textsuperscript{252}

3.5 U.S., Britain and the Netherlands: Oil Game and Japan

In the Western Pacific, competition centered on the Dutch East Indies (hereafter DEI), the largest single source of petroleum in Asia. In September 1920, Standard Oil of New Jersey operating through its DEI subsidiary, Netherlands Koloniale Petroleum Co. (hereafter Koloniale), publicly announced in both the Netherlands and the DEI its intention to discuss selling its entire existing oil concessions in the DEI to Japanese interests.\textsuperscript{253} The talks were initially to be held in October 1920 and were a response to the Dutch government's intransigence in allowing expanded foreign oil interests in the DEI.\textsuperscript{254} They were also motivated by Standard's recent loss to Royal Dutch Shell of the disposition of U.S. naval oil reserves in California. Shell subsequently shipped much of this oil to the Japanese navy, inciting outrage in the U.S. navy and calls for U.S. government control of adequate naval stores.\textsuperscript{255} These calls resulted in the creation of the

\textsuperscript{252} See, for example, memorandum from D.McD LeBreton, U.S. Naval Attache at the Hague, Netherlands, to Director of Naval Intelligence, “British Influence in Dutch Affairs: exploitation of oil fields of Dutch East Indies,” April 5, 1923, File o-l-l, Register 12865A, RG 38.

\textsuperscript{253} Letter, John A. Fowler, American Trade Commissioner at Batavia, Java to U.S. Department of Commerce, Foreign Service Division, Bureau of Foreign and Domestic Commerce, October 30, 1920, file 856d.6363/33. RG 59; Peter Mellish Reed, “Standard Oil in Indonesia,” Business History Review, Vol. 32 (Autumn 1958), pp.319-322. Fowler's letter stated that the Koloniale's local DEI manager, Mr. Colter, mentioned his company's frustration with Dutch authorities and desire to sell all properties to the Japanese so that this information would get to U.S. government officials indirectly, yet purposefully, before they announced their intent to sell. This information was dutifully relayed to the State department as Koloniale intended.

\textsuperscript{254} The U.S. government had also engaged in lobbying for American oil companies in 1920, but to no avail. See Gerald D. Nash, United States Oil Policy, 1890-1964, (Pittsburgh, PA: University of Pittsburgh Press, 1968), pp.61-63.

infamous Teapot Dome naval oil reserves in June 1921, with contract authority concentrated in the Department of Interior under Secretary Albert Fall. Standard Oil used the U.S. navy and the California public's rising hostility to Japan to try and bolster its claims in the DEI and helped bring about Japanese fears of U.S. navy cancellation of the fuel oil contracts.

These corporate joustings played on each other's home government antipathy toward Japan and reflected the oil corporations' still ardent desire to defeat one another in the global contest for oil source control and market outlets. Their actions, however, incensed all of the national governments involved. The Dutch legislature was to make the final award of the petroleum rights to the Djambi field area in Sumatra in 1921 and its Minister of Foreign Affairs, J.H. van Karnebeek, declared that foreign corporations were to be excluded unless organized under Dutch control. Although van Karnebeek stated that American corporations were desired as participants in Djambi development, he claimed Japanese desire for concessions and equal treatment precluded him from overtly.

Fleet, captured this well in early planning against Japan. He stated, "our nation is definitely committed to the exclusion of Asiatic coolies as laborers, and this represents a policy we would rally to arms to defend. White labor cannot compete with Asiatic labor without descending to a scale of life wholly incompatible with white ideals and traditions...Japan is restive under this attitude of the United States. It is today the most probable cause of war between the two countries, since it is an issue on which popular support can easily be rallied, or get beyond the control of the Government, in its demand for hostilities." U.S. Navy Captain, H.E. Yarnell, "Strategy of the Pacific," p.5, lecture delivered before the Army General Staff College, September 8, 1919, U.S. Naval General Board Records, Serials and Studies, War Plans, Record Group 80, National Archives, hereafter cited as "RG 80."

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256. See Nash, United States Oil Policy, pp.72-79.
257. See translated Tokyo Asahi article, October 12, 1920, in ONI Report, "Oil Situation of Japan, Part II, Fuel Oil Situation of the Japanese Navy" File o-1-g, Register 14039, RG 38. This article noted possible U.S. navy pressure on Shell Oil of California to stop supplying the Japanese navy, but concluded that this particular contract would likely be fulfilled.
258. At this same time, the U.S. was irate about being partly excluded from the development of Mexican oil resources by British-Dutch concerns and sent U.S. naval cruisers to Tampico, Mexico coupled with a blunt diplomatic message to the British. This gunboat diplomacy was "no idle threat," and did have the effect of stimulating the negotiations on global reciprocity in oil resources among the U.S., Britain and the Netherlands. See Hanighen, The Secret War, p.112.
helping Koloniale or other American corporations.\textsuperscript{259} Koloniale decided to act independently of U.S. State department efforts and directly pressure the Dutch government, playing on its fear of Japanese economic penetration in the DEI by threatening to sell all of its light-producing oil assets there to Japan. The U.S. government was, however, informed prior to Koloniale’s sale offer and did not block this corporate effort. For these reasons this event is consistent with both marxism and offensive realism because Koloniale deliberately preyed on Dutch authorities’ fear of Japan and the U.S. government permitted them to do so. Standard Oil also used U.S. navy fear of Japan in California to attempt to use U.S. government coercive power against Royal Dutch Shell and its sale of U.S. navy fuel oil to Japan.\textsuperscript{260}

Dutch fears of Japanese military advantage from economic penetration were well founded. For example, in 1912 the DEI government granted a “private” Japanese concern a rubber culture and deep sea fishing concession on two small islands near Singapore. This purported Japanese businessman was later identified as a Japanese naval officer at an official naval dinner in Singapore, while Japanese officers were sounding and charting the waters around the rubber and fishing concession with no signs of the approved activity anywhere in evidence.\textsuperscript{261} The Dutch government’s policy of excluding Japanese and American oil corporations at this time rested on England’s

\textsuperscript{259} Sinclair Oil Corporation had also applied for a portion of the concession in September 1920. Reed. "Standard Oil in Indonesia," p.321.

\textsuperscript{260} Liberalism is also indicated in this instance, although somewhat less convincingly because of Koloniale’s playing upon Dutch fears of Japan to try and achieve its preferences. In using the threat posed by Japan and the Japanese themselves in the negotiations, instead of the mutual benefits from joint commercial opportunities, Koloniale acted more as marxism predicts. Similarly, defensive realism is contra-indicated because the U.S. government allowed its corporations to prey on Japan’s vulnerabilities and insecurity related to oil resources, challenging its security and autonomy not respecting it. More pointedly, a sale to Japan would represent an increase in Japanese capabilities and therefore would not be consistent with defensive realism.

assurance of their security through the Royal navy, whose naval force position was increasing with the building of improved bases at Singapore. In fact, longstanding British policy was adamant in excluding any foreign powers from property concessions in the vicinity of Singapore, including both Americans and Japanese.\textsuperscript{262} The sincerity of official Dutch sentiment that expanded American corporate presence was desirable in Sumatra, but not at the expense of a Japanese presence, came under increasing question by American officials. Standard Oil challenged the Dutch position advancing its own direct interests and indirectly those of the U.S. government.

Negotiations between Koloniale and Japan's Nippon and Hoden Oil companies\textsuperscript{263} finally commenced in early January 1921 and quickly broke down over the "purchase price" for Koloniale's DEI concessions.\textsuperscript{264} Koloniale's strong-arm tactics did not bear fruit, even though many Dutch legislative leaders were inclined to dilute the power of Royal Dutch Shell in the DEI by admitting expanded American interests there.\textsuperscript{265} More importantly, Japan's interest in direct access to the DEI was piqued by Koloniale's insincere sales offer, and Japan's fear for secure supplies was increased with all of these

\textsuperscript{262} Vandenbosch describes the 1911 effort of Standard Oil of New York (SONY) to acquire a concession on the island of Poeloe Bintang near Singapore, only to have the Dutch bow to British pressure to exclude SONY under the pretense that the island was needed as a quarantine station. The station was erected to breathe life into the lie, but never used. Vandenbosch, \textit{The Dutch East Indies}, p.329

\textsuperscript{263} These companies merged into Nippon Oil in October 1921 and were operated abroad by the Japanese navy. U.S. Department of Commerce, Bureau of Foreign and Domestic Commerce (herafter cited as D.O.C., B.F.D.C.), \textit{Petroleum in Japan}, (Trade Information Bulletin no. 245), by Albert T. Coumbe. (Washington, D.C., U.S. G.P.O., June 30, 1924), pp.9-10.

\textsuperscript{264} Office of Naval Intelligence. Reports, January 8, 1921, ONI Report #34. File c-10-1, Register 14017, RG 38. A later report also noted failed negotiations because “pressure from outside...was brought to bear on the Dutch government to induce it to discourage the proposed sale.” This outside pressure likely came from the British government. See letter from Edward Bell, Tokyo to Secretary of State, August 12, 1921, file 856d.6363/142, RG 59.

\textsuperscript{265} Van Karnebeek did not consult with or represent many in the Dutch legislature whose desire lay with diluting the power of Royal Dutch Shell by adding greater American presence. Reed, \textit{Standard Oil in Indonesia}, p.317. In 1920, Koloniale produced less than 1% of the crude oil in the DEI, and Royal Dutch-Shell 99%. Royal Dutch Shell, a merger of British and Dutch corporate interests with British capital and influence paramount, operated in the DEI through its main subsidiary, N.V. De Bataafsche Petroleum Maatschappij, hereafter “BPM.”
actions. The U.S. government tacitly permitted Koloniale to threaten the Dutch with the sale offer to Japan by not blocking the negotiations after being given advanced warning. In so doing, the U.S. government deliberately raised the stakes of the settlement with the British and Dutch governments and the British-Dutch company by offending Japan's desire for equal access to the DEI. This position was influenced by the new Harding administration's desire to pressure Britain into more cooperative oil arrangements globally and its willingness to court political conflict with Britain to achieve this. The Djambi concession was formally awarded to BPM by legislative action at The Hague on April 28, 1921, leaving both American and Japanese suitors determined to gain greater direct access to the DEI's petroleum.\(^{266}\)

The U.S. desired greater access for its corporations not only for obvious commercial reasons, but also for greater intelligence gathering capabilities and influence over British oil policy toward Japan.\(^{267}\) The U.S. had been using Standard oil subsidiaries as intelligence sources for some time and was receiving detailed Japanese naval information from American corporate sources in the DEI and Japan at this time. For example, in April 1921, Standard Oil Company of New York officials reported on

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\(^{266}\) This was evident in Japan's high level official visit to the DEI in 1922 and requests for oil concessions on the Celebes island in April 1923. Reed, "Standard Oil in Indonesia," p.329. Japan's navy surveyed the strategic import of Celebes (i.e., Philippines proximity, no proven oil resources) as it procured crude and fuel oil from eastern Borneo. Office of Naval Intelligence. Reports, May 25, 1921. ONI Report Serial No. 482, File No. 502-400, File c-10-1, Register 14017. RG 38. The Dutch government chastised the U.S. for interfering with the concession negotiations and van Karnebeek stated that any further proposals should be made by private companies and not the U.S. government, which had been perceived negatively by many Dutch officials as influencing the internal affairs of the Netherlands. See Memorandum from Norman Armour, U.S. Charge d'Affairs at The Hague, Netherlands, to Secretary of State, July 12, 1921, in Office of Naval Intelligence, reports, File e-1-1, Register 12865, RG 38.

\(^{267}\) U.S. Navy intelligence had been monitoring British oil ties with Japan under the Anglo-Japanese alliance, particularly in British-controlled North Borneo where Japan gained a sub-concession from British Borneo Petroleum Syndicates in 1920. Japan, however, had lost 500,000 British pounds in unsuccessful operations by 1923 and it remains an open question as to whether Britain intended this to maintain its oil leverage over Japan. See ONI report at File e-10-d, Register 13177C. RG 38.

138
Japanese purchases of oil storage tanks from Pittsburgh and Imperial navy construction of reinforced concrete tanks at the Kure, Sasebo and Tokuyama bases, which allowed Japan to “increase their present storage capacity by over 3,000,000 barrels.” This particular report also described the difficulty Royal Dutch subsidiaries were having supplying the Japanese navy with California fuel oil and the desire of Japanese officials to place large orders with Standard Oil. U.S. government guidance of oil contracts for Japan is implied in this report, at least with respect to Standard Oil of New York which was the largest U.S. supplier of petroleum products to Asia. Other naval intelligence officers were monitoring Japanese naval tanker traffic to California facilities of the Royal Dutch, and took note of the Royal Dutch’s actions to avoid the “notoriety” of supplying the Japanese navy. In early 1921, the Royal Dutch made arrangements that no further Japanese navy tankers would arrive in California. Instead, fuel oil would be supplied by British and Dutch tankers from California and sources in Mexico and the DEI. This decision was

268. See letter L.J. Thomas, Standard Oil Company of New York, to Admiral Andrew T. Long U.S. Navy. April 21, 1921, File e-10-d, Register 13177, RG 38. Other reports indicated total tankage capacity of Japan by location and the nascent efforts of the oil-shale project in Fushun, Manchuria.

269. Ibid., Mr. Thomas noted, “There are all kinds of propositions being made at present, but at this writing we can give you no more definite information...It is possible that within the next week or ten days we may receive a definite offer, either directly from the Navy department or through a middleman for a considerable quantity of fuel.” It is not clear whether the significant drop off in U.S. deliveries to Japan of fuel oil and gasoline over the rest of 1921 and into 1922 resulted from U.S. government guidance to Standard Oil. However, it is highly probable that Standard officials discussed the matter with U.S. officials, resulting in less supply to Japan because of U.S. diplomatic desire to pressure both Britain and Japan into negotiations on new arrangements for Asian order at the upcoming Washington Conference. For this reason, Japan’s decreased supplies from the U.S. are consistent with offensive and defensive realism as the U.S. Navy appears to have brought this about and guided the companies on contracts and lessened supplies to an increasingly threatening adversary.
made because of the hostile reaction by the U.S. navy and in California's press, which was causing a negative effect on Royal Dutch's business operations in California and the U.S. more generally.270

In the aftermath of the fractious awarding of the Djambi concession, the U.S. government brought direct pressure onto the Dutch government, while Standard Oil sought to pressure the Royal Dutch in its home market and elsewhere. The U.S. responded in 1922 by invoking a provision of the recently passed 1920 Mineral Leasing Act, declaring the Netherlands a "non-reciprocating" country that denied U.S. corporations access to government controlled lands and could therefore be similarly denied rights on U.S. government lands. The U.S. denied Royal Dutch-Shell and one of its subsidiaries, Roxana Petroleum Company, rights to lease and develop mineral resources on public lands in September 1922 and March 1923.271 Although these acts of retaliation occurred amidst burgeoning cooperation elsewhere, they did maintain U.S. pressure on the Dutch government regarding the future disposition of DEI oil.272 More importantly, these actions reasserted the U.S. government's primacy in resolving any future distribution of oil rights in the DEI with respect to oil corporations and rival governments.

270. See memorandum from Wallace Bertholf, Commandant Twelfth Naval District, to Director of Naval Intelligence, April 21, 1921, in overall report, "Navy Oil Contract 1917-1920 with Shell Oil Co.," dated May 6, 1921, File e-10-d, Register 13177, RG 38. See also therein report on Japanese government's contracts for Mexican oil under Royal Dutch control. These reports were "obtained by a Standard Oil Co. representative in Japan at the request of this office. It required about one month's investigation to collect the data, and is believed to be very reliable and correct to date."


272. Beginning in late 1921 and concomitant with Lord Cadman's oil peace with the U.S. and the opening of the Washington Conference, the American, British and Dutch governments began to settle some smaller outstanding differences regarding oil development for their national corporations in Costa Rica, Venezuela and Persia, replacing exclusive development arrangements with joint ones. See Hogan, Informal Entente, pp. 166-77.
The Japanese were particularly interested in the DEI concession negotiations at this time because of their great reliance on the DEI's petroleum. Japan depended greatly on the DEI and more pointedly on British government- influenced oil companies (e.g., Anglo-Persian, Royal Dutch Shell) who supplied Japan from other source countries including the U.S.. This relationship was not published in official government statistics which excluded the largest purchasers of petroleum products (i.e., Japan's navy and army).273 This understatement is indicated by accurate DEI statistics that show DEI exports to Japan of 82,879,646 gallons of crude and fuel oil in 1921, roughly 33% of total DEI exports of crude and fuel oil,274 compared to official Japanese total imports of only 11,234,000 gallons. Similar understatement of 1920 imports is also indicated as the DEI reported 21,396,671 gallons of crude oil shipped to Japan, compared with official Japanese total imports of only 4,157,000 gallons.275 These discrepancies serve to highlight the degree of importance of Japan in the DEI's petroleum trade and Japan's


275. Fuel oil exports from the DEI to Japan could not be obtained, although it was large due to the Japanese Navy's purchases there. For 1920, Japan's domestic production of fuel oil from crude oil was 8,826,426 gallons set against total imports of 73,282,178 gallons. This indicates how dependent Japan was on imports. Japan's total production of crude oil was 92,964,690 gallons, from which other products were derived such as gasoline, kerosene, lubricating oils, paraffin, and pitch. See Coumbe, "Petroleum in Japan," pp.2,14. Interestingly, Japan's domestic peak crude production was in 1916 at 124,446,000 gallons after which it declined due to "difficulty obtaining American drilling supplies during the World War." Ibid., p.2
reliance on the DEI for the majority of its crude and fuel oil, particularly when compared with U.S. exports to Japan (See Table 3.2). The peak interwar year for DEI reliance on Japanese crude and fuel oil purchases was 1922, when Japan took 46.7% of DEI exports.
Table 3.2: Crude and Fuel Oil Exports to Japan, 1918-1922

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<td>34.3%</td>
<td>13.3%</td>
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<tr>
<td>imports)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>From other sources</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>to Japan in millions</td>
<td>.000084</td>
<td>3.081</td>
<td>26.758</td>
<td>24.863</td>
<td>N/A</td>
</tr>
<tr>
<td>of gallons: British</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Borneo, Mexico, Persia</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>in gallons (% of total</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Japanese imports)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

* Mexican oil shipped to Japan appears to have begun in 1921, while oil from British North Borneo and Persia was flowing throughout the period. In the first 10 months of 1921, 3,981,390 gallons left Mexico for Japan through Anglo-Persian and Shell contracts and this amount was entered for the 1921 data which is therefore somewhat understated. See “The Petroleum Situation with Special Reference to the Far East,” p.32; ONI Report, November 1921, Serial 866, File No. 502-400, File e-10-1. Register 14017. RG 38.

b U.S. figures include fuel and gas oil while DEI statistics only include fuel oil, and therefore U.S. data are somewhat overstated compared with DEI. These data were compiled from Dutch publications, U.S. Naval intelligence reports and U.S. D.O.C. publications, including: Statistiek van Den Handel en de in-en Uitvoerrechten in Nederlandsch-Indie over het Jaar. 1921-1923; U.S. Naval Attaché Report. “Navy Oil Contract 1917-1920 with Shell Oil Co.” dated May 6, 1921, File e-10-d, Register 13177. RG 38; U.S. D.O.C. “Petroleum Products and Trade of the Dutch East Indies,” by Albert T. Coumbe; U.S. D.O.C. “Trade of the United States with the World, 1920-1921,” (Washington, DC: U.S. G.P.O., 1922), p.402; U.S. D.O.C. Foreign Commerce Yearbook, 1923, p.186; Confidential Memoranda, “The Petroleum Situation with Special Reference to the Far East;” and a report on Japanese Petroleum in Engineering and Mining Journal Press, Vol. 120, No. 10, September 5, 1925, pp.371-374. There were of course several discrepancies among the data sources, notably the U.S. Navy intelligence sources showed higher amounts shipped from U.S. to Japan than did U.S. Department of Commerce sources. It is possible that U.S. Navy reserve oil shipped to Japan by the Royal Dutch subsidiary was not accounted for in D.O.C. publications. Japan may also have received petroleum products transshipped through Singapore, which would increase the non-U.S. supply amounts for Japan. These discrepancies are not material to demonstrating the broad dependency trends, which is the only principal feature that can be established from trade data estimates.

143

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Japan's gasoline imports in these years show less overall foreign reliance due to greater domestic refined production, although considerable dependence on both the United States and the DEI, with approximately 68% of Japan's gasoline imports in 1921 from the DEI.\textsuperscript{276} DEI gasoline exports to Japan were important to Japan, but not as important to the DEI as only 4.1% of total DEI gasoline exports went to Japan in 1920 for example.\textsuperscript{277} The United States supplied considerable quantities of gasoline to Japan as well, but shipments dropped off markedly for 1921 most likely due to the U.S. navy pressure in California (See Table 3.3). Standard Oil of New York was the chief U.S. company importing refined oil products into Japan and as noted earlier was in constant communication with U.S. intelligence on Japanese petroleum issues. It is important to note that most of Japan's refineries and techniques followed American methods and Japan purchased most of its equipment and processing technology from the U.S. and not Britain.\textsuperscript{278} This trend would continue throughout the 1920s as more refining technologies were purchased from the U.S., including the purchase and installation of a Dubbs cracking plant in a “big modern refinery” near Yokohama in July 1924.\textsuperscript{279} Japan’s

\textsuperscript{276} In 1921, Japan reported only 5,814,000 gallons imported against domestic production of 6,733,548 gallons of gasoline. Although the officials import numbers are understated compared with U.S. and DEI export data they are roughly equivalent. Japan's refining industry was at an incipient stage but was being heavily pushed by the government, resulting in increased crude imports for domestic refinement in 1921 going forward. Japan also altered its import tariffs in 1920 to promote fuel oil imports to build stores for the navy. See Office of Naval Intelligence, ONI report, Serial No. 866, File No. 502-400, January 9, 1922, File c-10-l, Register 14017, RG 38; U.S. D.O.C., B.F.D.C., “World Trade in Gasoline,” (Trade Promotion Series No. 20) by Homer S. Fox, (Washington, D.C., U.S. G.P.O., 1925), p.58.\textsuperscript{277} DEI statistics for 1920 contained in letter from Henry Starrett, American Consul at Batavia, to Secretary of State, May 27, 1922, File 856d.6363/202, RG 59.\textsuperscript{278} Coumbe, “Petroleum in Japan,” pp.12-13; “The Petroleum Situation with Special Reference to the Far East,” pp.39-40.\textsuperscript{279} Fox, “World Trade in Gasoline,” p.59. The Dubbs cracking technology patent was held by Universal Oil Products Company of Chicago, a company that would figure prominently later in disputes among the U.S. government, Japan and Standard Oil interests.
demand for gasoline was increasing exponentially by the early 1920s as automobile use and road construction accelerated dramatically, both activities being heavily influenced by U.S. exports.\textsuperscript{280}

<table>
<thead>
<tr>
<th></th>
<th>1918</th>
<th>1919</th>
<th>1920</th>
<th>1921</th>
<th>1922&lt;sup&gt;a&lt;/sup&gt;</th>
</tr>
</thead>
<tbody>
<tr>
<td>From DEI to</td>
<td>4,303,981</td>
<td>1,263,561</td>
<td>5,353,295</td>
<td>4,055,126</td>
<td>3,309,353</td>
</tr>
<tr>
<td>Japan in gallons</td>
<td>(93%)</td>
<td>(59.6%)</td>
<td>(47.5%)</td>
<td>(68%)</td>
<td>(37.7%)</td>
</tr>
<tr>
<td>(% of total</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Japanese imports</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>From U.S. to</td>
<td>321,006</td>
<td>855,036</td>
<td>5,918,020</td>
<td>1,941,027</td>
<td>5,467,000</td>
</tr>
<tr>
<td>Japan in gallons</td>
<td>(7%)</td>
<td>(40.4%)</td>
<td>(52.5%)</td>
<td>(32%)</td>
<td>(62.3%)</td>
</tr>
<tr>
<td>(% of total</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Japanese imports</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Table 3.3: Gasoline Exports to Japan, 1918-1922<sup>c</sup>

<sup>a</sup> Officially reported Japanese imports of gasoline for 1922 were 11,836,000 gallons against the above total from the DEI and U.S. of 8,776,353. The difference likely comes from third countries already mentioned including Hong Kong, Singapore and British North Borneo. These would all be British-dominated firms, either Royal Dutch or related subsidiaries such as Anglo-Saxon Petroleum Co., Asiatic Petroleum or Anglo-Persian. Because these data are not reported they were omitted: their inclusion would decrease the U.S. percentage markedly, and would increase the DEI's percentage as gasoline was transshipped through Singapore and other places from DEI sources. See Fox, "World Trade in Gasoline," pp.2-3, 64-66.

<sup>b</sup> As an example of the needling variation in data, this was the officially reported figure in the Dutch publication Statistiek van Den Handel; however both the report in Engineering and Mining Journal Press and Coumbe, "Petroleum in Japan," have the figure at 4,300,000 gallons. Because the differences are slight the official figure from the DEI source is used.

<sup>c</sup> Japan did receive small amounts of gasoline from third countries, but most of this was transshipped DEI and U.S. gasoline through Singapore or Hong Kong, and was not collected systematically by end use and is therefore excluded in the above chart for simplicity. For example, in 1922 Hong Kong shipped 63,888 gallons of gasoline to Japan after receiving most of its gasoline from the U.S. and the DEI. See Fox, "World Trade in Gasoline," p.65. Gasoline import data come from the same sets of sources as the crude and fuel oil import data, including: Statistiek van Den Handel en de in-en Uitvoerrechten in Nederlandsch-Indie over het Jaar, 1921-1923; Coumbe, "Petroleum Products and Trade of the Dutch East Indies;" Coumbe, "Petroleum in Japan;" U.S. D.O.C., "Trade of the United States with the World, 1920-1921, p.402; and report in Engineering and Mining Journal Press. Vol. 120, No. 10. September 5, 1925, pp.371-374.
3.6 Washington Conference: Naval Arms, Political Order and Oil

United States Navy intelligence analysis of Japan’s oil dependency position increased throughout 1921, with particular attention to the importance of British-assured supplies from the Royal Dutch Shell corporations. After carefully observing Japanese naval purchases in the DEI in 1920-1 and actions in N. Sakhalin, the U.S. government sought to delimit further Japanese strides toward oil autonomy by tempering Japan’s expansion into N. Sakhalin. The U.S. declared that it would not recognize any Japanese claims or rights in the acquired N. Sakhalin territory. This non-recognition foreshadowed the U.S. position on China in 1931, and was motivated not only by concern for Japanese efforts toward oil autonomy but also British policy that facilitated Japanese energy security. At bottom, Secretary of State Hughes’ position of non-recognition of Japanese gains from military expansion was an early and principled effort to coordinate policy with Britain and contain Japan. This principled position on the fate of N. Sakhalin oil resources was tested not only by Japan but also by the American company Sinclair Oil. Sinclair sought and attained oil concession rights from the exiled Russian government despite warnings from Secretary of State Hughes not to do so in September.

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281. U.S. Secretary of State Charles Evans Hughes made this point clearly on May 31, 1921, stating the U.S. would "neither now nor hereafter recognize as valid any claims and titles arising out of the present occupation and control." Hughes quoted in, Chester, U.S. Oil Policy and Diplomacy, p.286. See also Iriye, After Imperialism, p.14; Kamikawa, Japan-American Diplomatic Relations in the Meiji-Taisho Era, pp.378-383.
Hughes was trying to avoid unnecessary interactions with the new Soviet state, but more importantly he did not want to create any more conflict areas with Japan on the eve of the Washington Conference negotiations.

The Washington Conference opened on November 12, 1921 and ended on February 6, 1922. It was desired by the main participants, the U.S., Great Britain, and Japan, as a forum for containing their naval armaments competition then underway, and resolving the status of various contentious territorial issues left over from the Versailles Treaty (e.g., Shantung, mandated German islands, Siberia). Through direct negotiations the U.S. hoped to lessen the increasing threat perception of each party and provide a more stable basis for Asian relations. More importantly, the U.S. sought to end British-Japanese bilateral dealings that conflicted with U.S. preferences regarding

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282 Sinclair's negotiations with the exiled Russian government ended in a 36 year concession agreement (signed January 7, 1922) for Sinclair to explore all of N. Sakhalin and develop its oil resources. The U.S. did not, however, lend any assistance to Sinclair in executing the contract or obtaining access to N. Sakhalin while the Japanese occupied it, despite Sinclair's pleas for government assistance and effort to force government protection of its personnel. In fact, Sinclair paid an even higher price for its non-compliance later in its Persian oil concession quandary as the State department backed Standard Oil and not Sinclair in arrangements with the British. See Hogan, Informal Entente, pp. 176-7. Sinclair's fate in N. Sakhalin was ignored when later in 1922 Sinclair was turned away from exploration by Japanese authorities who subsequently settled with the Russian government in 1925, obtaining agreements for over half of all future N. Sakhalin oil. See Chester, U.S. Oil Policy and Diplomacy, p.287. These instances highlight the weakness of both marxist and liberal positions as Harry Sinclair was an intimate of President Harding, and are consistent with realism's emphasis on state primacy over corporate interests.

283 Relations between Japan and the U.S. had strained since the end of WWI and the naval competition (i.e., U.S. Naval program begun in 1916 and Japan's capital ship plan of 1920) led to widespread speculation of imminent conflict between the two states. Buckley, The Washington Conference, pp.75-82.

284 The idea for a naval arms control conference originated with Senator William Borah of Idaho who pushed a joint resolution in the U.S. Senate on December 14, 1920 calling for a 50% reduction in naval construction among the U.S., Britain and Japan over the next 5 years and for the President to hold a conference to accomplish this. See Margot Louria, Triumph and Downfall: America's Pursuit of Peace and Prosperity, 1921-1933, (Westport, CT: Greenwood Press, 2001), p.25.

285 Stability ensured through treaty obligations was desired by the U.S. as the Japanese leadership seemed potentially unsteady. Premier Hara Kei, who accepted the invitation to the Conference and was inclined toward accommodation with the U.S., was fatally wounded on November 4, 1921. Hara desired the Conference as a means to gain greater civilian control over the military in Japan, particularly with the Navy by exploiting the army-navy rivalry. Richard Fanning noted: "Hara hoped that a naval agreement might strengthen his cabinet's ties to the navy while reducing the power of the army to meddle in foreign affairs." Richard Fanning, Peace and Disarmament: Naval Rivalry and Arms Control, 1922-1933, (Lexington, KY: University of Kentucky Press, 1995), p.5.
Asian order and enabled Japan’s military to secure diverse sources of oil supplies. Lurking beneath the U.S. desire to break up the Anglo-Japanese alliance was the still prevalent concern that if the U.S. faced war with one of the two allies it might be strategically disadvantaged by having to fight both of them across two oceans. An October 1921 assessment from the Director of War Plans noted, “should the United States have to face a war with Great Britain and Japan as allies, it would be necessary to withdraw the bulk of our fighting forces into the Atlantic, and in that case the ability of Hawaii, as at present defended, to hold out against Japanese attack is problematical.” The U.S. demanded the end of the alliance precisely to forestall this worst-case possibility. This was not an easy choice for the British to make or the Japanese to accept, but each did so believing cooperation in its bilateral relations with the U.S. would justify the end of the alliance.

The question of Anglo-American cooperation in worldwide oil development, however, cast some suspicion over the possibility of a successful conference, but “the matter was laid to rest when Lord Cadman established the oil peace at the end of 1921. The Nederlandsche-Indische Aardolie Maatschappij, owned jointly by the Royal Dutch and the Netherlands Government, could begin the exploitation of the Djambi deposits

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286. The preparatory memoranda for the U.S. delegation to the Conference noted a “secret understanding” between the British and Dutch governments regarding possible Japanese attack and Japanese supply arrangements pursuant to the Anglo-Japanese alliance, yielding some “informal assurances (to Japan) of a secure oil supply from the Netherlands East Indies and from Persia.” See “The Petroleum Situation with Special Reference to the Far East.” p.13.


288. A representative Tory view of the American demand for alliance termination came from Winston Churchill. He noted, “The United States made it clear to Britain that the continuance of her alliance with Japan, to which the Japanese had punctiliously conformed, would constitute a barrier in Anglo-American relations. Accordingly, this alliance was brought to an end. The annulment caused a profound impression in Japan, and was viewed as the spuming of an Asiatic Power by the Western World. Many links were sundered which might afterwards have proved of decisive value to peace.” See Winston Churchill, The Second World War: The Gathering Storm, (New York: Bantam Books, 1948), p.13.
with the blessings of the State Department in return for a compromise in the Middle East and the promise of subsequent concessions in the East Indies.\textsuperscript{289} By helping Britain to choose entente with the U.S. instead of continued alliance with Japan, the U.S. was able to lead in shaping the emerging Anglo-American bloc.\textsuperscript{290} A core foundation of this entente was the political understanding that global oil development would be a shared Anglo-American enterprise. This shared enterprise would come to entail change in DEI oil supplies to Japan across the rest of the interwar period (See Figure 3.1)


\textsuperscript{290} Writing in Peking, Stanley Hombeck noted the deleterious effects of the alliance and its likely renewal as “victory for spheres of influence.” He held: “The Anglo-Japanese alliance has in the past been detrimental to American interests, it has positively injured China, it has complicated the relations between America and Japan. If it is renewed, it will place a greater strain on relations between America and Japan, it will foster disaffection between America and Great Britain, and it will be a menace to the status quo if not to the Peace of the Far East...British private individuals have said repeatedly that if only Great Britain could count on the United States for friendly cooperation (preferably an alliance), the British government would gladly drop the Japanese alliance.” Hombeck memoranda, “The Anglo-Japanese Alliance: A Way Out,” June 6, 1921, in Hombeck Papers, Box 520, Folder: Miscellany 1920-1928.
Figure 3.1: Exports of Dutch East Indies Crude and Fuel Oil to Japan, 1920-1941

Percentage of total DEI crude and fuel oil exports
The U.S.'s primary military goal at the Washington conference was to stabilize the naval force balance in the Pacific and lessen the drive toward converting island possessions into strong naval bases with offensive power capabilities (i.e., Philippines, Guam, Bonins, Ryukus, Formosa, Hong Kong).\(^{291}\) To this end, Secretary of State Hughes began the conference with a dramatic unilateral declaration that the U.S. would end the building of 15 capital ships already under construction and would scrap an additional 15 older battleships.\(^ {292} \) The U.S. also wanted to supplant the Anglo-Japanese alliance of 1902 with a broader, multilateral great power accord governing the territorial possessions of the major powers and reaffirming the principles of Open Door economic development and independence for the remaining states of Asia. Many in Britain shared this desire because of the now common Anglo-American concern of "the danger that the Japanese would continue to use the alliance to further their interests on the Chinese mainland and in the Pacific. Acquisition of former German possessions during the World War seemed to demonstrate Japanese expansive tendencies that were furthered by the

\(^{291}\) Buckley, *The United States and the Washington Conference*, pp.90-92. Even with fortification the defense of the American Western islands was highly questioned as the Japanese surrounded the Philippines and Guam with their possessions. The agreement not to fortify these possessions led Advisory Commission member Theodore Roosevelt Jr. to conclude American advantage: "we trade certain fortifications which we never would have completed, for fortifications which they would have unquestionably completed." quoted in Buckley, *ibid.*, p.102, footnote 48.

\(^{292}\) Buckley, *The United States and the Washington Conference*, pp.72-3. Hughes went on to specify what reductions the British and Japanese should make to match the U.S. reductions, noting the overall imperative that "competition in armaments must stop." Hogan noted, "By 1921, then, British officials were hoping to replace the Anglo-Japanese alliance with a wider system of political cooperation, one founded on close Anglo-American relations and designed to restrain Japan." Hogan, *Informal Entente*, p.91. See also an unsigned, yet exhaustive official British memorandum that starkly summarized the choice facing Britain and the necessity for entente with the U.S. at Japan's expense if necessary. Confidential Memorandum, "The Anglo-Japanese Alliance and the Future of American-British Relations." March 30, 1921, Hong Kong, in Hornbeck Papers, Box 478, Folder: Writings Anglo-Japanese Alliance 1921.

152
existence of the alliance.\textsuperscript{293} The U.S. sought to demonstrate this new principled ordering of Asia by pressing for resolution on Siberia and redefining outside powers' interests in China on the basis of equal, non-discriminatory access and commitment to the integrity of China's territorial sovereignty. This agenda was made concrete in the demand that Japan return Shantung to China and agree to the Open Door principle for the development of China, reversing the Lansing-Ishii agreement's tacit endorsement of exclusive Japanese rights there.\textsuperscript{294}

The Conference resulted in the interrelated Five, Four and Nine Power Treaties. The Five Power Treaty (U.S., Great Britain, Japan, France and Italy) embodied Secretary of State Hughes' Conference opening call for ending current capital warship construction programs and reducing overall naval forces by scrapping older warships. The Five Power Treaty secured these outcomes by placing the relative tonnage of U.S., British and Japanese capital ships (i.e., battleships and battle cruisers) on a 10:10:6 basis. Despite Japan's initial preference for a 10:7 ratio to the U.S., the agreed ratio was acceptable due to the corollary agreement on non-fortification of certain island possessions.\textsuperscript{295} The U.S. pledged not to build advanced naval bases in the Philippines or Guam, lessening Japan's perception of an advancing offensive U.S. naval capability. In return, Japan agreed not to

\textsuperscript{293} Buckley, \textit{The Washington Conference}, pp.144-5.
\textsuperscript{294} Resolution on the principle of Open Door economic development of China was critical to naval arms reductions. Pre-conference U.S. war plans held "the crux of the Japanese situation is our policy of the "open door" in China. If we do not succeed at the coming conference in obtaining the support of other nations and an agreement on the part of Japan to respect this policy, we must either abandon it or fight to enforce it." See Memorandum, "Questions Concerning the Limitation of Armament," p.2, from Director of War Plans to General Board, October 19, 1921, General Board Records, War Plans 425, RG 80.
\textsuperscript{295} The U.S. was able to bargain Japan down to this ratio and in other areas due to its intelligence on Japan's negotiating positions and deciphering of all Japanese diplomatic cables prior to and during the conference. See James Bamford, \textit{The Puzzle Palace}. (New York: Penguin Books, 1983), pp.25-27.
fortify Okinawa, Formosa, the Bonins, and Pescadores, while the British retained the right to make Singapore an advanced naval base but not Hong Kong.

These arms limitation agreements were closely related to the political understanding embodied in the Four Power Treaty (U.S., Great Britain, Japan and France). This treaty supplanted the Anglo-Japanese alliance with a great power accord for the Pacific in which each state pledged to respect the "insular possessions and insular dominions" of the others and to settle any dispute in the Pacific through diplomacy or conference.296 Japan's possessions were defined to include S. Sakhalin (aka., Karafuto), Formosa, the Pescadore and mandated islands. Resolving the status of the mandated islands required further negotiation as the U.S. was reluctant to unreservedly recognize Japan's control of the islands (i.e., the Carolines, Marshalls, and Marianas).297 Negotiations focused on the island of Yap in the eastern part of the Caroline group due to its importance as a cabling center for Pacific communications traffic. Japan agreed to internationalize control of Yap's communications infrastructure, and more broadly stipulated that bilateral commercial treaties with the U.S. would apply to all mandated islands.298 In exchange, the U.S. recognized Japan's authority over the mandated islands.

The Four Power Treaty's provisions were extended to the Netherlands government's possessions in S.E. Asia (i.e., the NEI) with identical notes sent to the Dutch government by the Four powers, while Chinese economic and political

297 During the immediate post-WWI period of Japanese control, U.S. Naval Intelligence reported numerous instances of exclusionary commercial activities by Japanese authorities and possible building of fortifications. See Naval Intelligence, Reports, "Japanese Activities in Marshall and Caroline Islands after WWI." File c-10-a, Register 4669, RG 38.
298 Buckley, The United States and the Washington Conference, pp.141-143.

154

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development was addressed in the Nine Power Treaty (U.S., Great Britain, Japan, France, Italy, Belgium, Netherlands, Portugal and China). This treaty committed the signatories to respect the sovereignty, independence and territorial integrity of China, and not to develop exclusive spheres of influence in China. Secretary Hughes wanted to make the Nine Power Treaty a "substitute for all prior statements and agreements" concerning China, reversing the acceptance of a special sphere for Japan in Southern Manchuria and elsewhere that Japan interpreted the 1917 Lansing-Ishii Agreement to condone.\textsuperscript{299} In accord with this treaty and U.S. diplomatic offices, Japan negotiated with China the return of Shantung province to Chinese authority and the rescission of many special Japanese economic rights in the province (e.g., Japanese control over the Shantung railway).\textsuperscript{300} Shantung's disposition had been a major source of tension between the U.S. and Japan since the Versailles Treaty which left it under Japanese control without any provision for final settlement.\textsuperscript{301} Similarly, Japan pledged to open development of Manchuria and Eastern Inner Mongolia to the international loan consortium, thereby lessening its monopolistic control over development in these areas.\textsuperscript{302} Subsequently, the

\textsuperscript{299} Secretary of State Hughes, quoted in Iriye, \textit{After Imperialism}, p.18; Buckley, \textit{The United States and the Washington Conference}, p.152. The Lansing-Ishii agreement was formally terminated in April 1923.

\textsuperscript{300} The negotiations resulted in the Treaty between Japan and China for the Settlement of Outstanding Questions Relative to Shantung, signed February 4, 1922. U.S. government pressure reducing the total economic resources under Japan's control is more consistent with offensive realism than defensive realism, because it reduced Japan’s economic autonomy efforts even when Japan was decreasing in threat to U.S. with the naval limitation agreement.


\textsuperscript{302} Iriye, \textit{After Imperialism}, pp.19-20; Crowley, \textit{Japan's Quest for Autonomy}, p.29. This commitment helped overcome deficiencies in the Lamont-Kajiwara accord (October 1920), in which the parties agreed to pool their loan policies in China, except for railway projects in Japan's sphere of influence, and pledged that the consortium would not compromise "the economic life and national defense" of Japan. See Hogan, \textit{Informal Entente}, p.89. The idea of a revived and expanded consortium to tie Japan's hands originated in February 1918 with British and American firms with interests in Chinese railway construction. Beers, \textit{Vain Endeavor}, pp.144-47.
U.S. and Britain, together with their bankers, collaborated to manage capital flows into China so as not to further advantage Japan in creating an exclusive sphere, particularly in Manchuria.  

The United States also obtained Japan's commitment to withdraw its forces from Siberia and N. Sakhalin, pending further negotiations with the Russian government. In the months following the Washington Conference, Japan withdrew its military forces from Shantung and in October 1922 its forces were fully withdrawn from Siberia. By the end of 1922 then, Japanese military expansion had been curtailed and relations between Japan, China and the Western powers had been placed under a broad framework of treaties governing behavior on a multilateral basis. These treaties bound the states to the principle of Chinese sovereignty and cooperative development, and regulated their ability to threaten each other's now recognized possessions through the naval arms limits of the Five Power Treaty. For these reasons, the Washington Conference and related agreements decreased the tension and mutually high threat perception in the U.S.-Japanese relationship that had led many on both sides to conclude that war was imminent.  

The Conference agreements were not, however, without limitations and consequences. First, the naval force balance did not include cruisers, destroyers or

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303. Hogan, Informal Entente, pp.95-6. ONI Reports, “America's Special Interests in Manchuria,” November 26, 1920, and “American Direct Investments in China,” October 19, 1931. File c-10-l. Register 13994, RG 38. This agreement is not evaluated for theory consistency because it did not amount to much in practice whereas Japan did withdraw from Shantung.

304. Japanese troops withdrew from Siberia after post-Conference diplomatic urging from the U.S., but did not withdraw from N. Sakhalin until 1925 after the January 20, 1925 oil concession agreement with the Soviet Union was signed. In this agreement Japan obtained rights to 50% of N. Sakhalin's oil production and equal treatment in the foreign production, if any, of the remaining oil properties. Chester, U.S. Oil Policy and Diplomacy, pp.288-290; Buckley, The United States and the Washington Conference, pp.165-6.

submarines, and aircraft carriers were allowed to be built from foregone battle cruiser platforms and only nominally limited in tonnage. These shortcomings led to a naval arms race in precisely these categories throughout the interwar period despite an early and failed effort to limit them at Geneva in June 1927. Second, the commitment to Chinese sovereignty existed more in rhetoric than reality, as the practice of extraterritorial legal rights and foreign controlled tariff rates was left intact with only a call for a future conference to resolve these questions. Third, due to the ending of the Anglo-Japanese alliance, Japan began to turn to Germany for its naval technology needs throughout the 1920s and the Japanese navy itself became divided between officers that accepted the Treaties and those that opposed them (i.e., the treaty and non-treaty factions within the navy). Despite these shortcomings, the Conference was successful in drawing out Japanese cooperation and providing a new basis for political and economic relations in the middle 1920s by breaking up the previous exclusive bilateral Anglo-Japanese economic and political arrangements.

3.7 U.S.-Japan Economic Exchange, 1918-1922

A brief review of economic relations between the U.S. and Japan through the conclusion of the Washington Conference (1918-1922) shows that the exchange relations were narrow, in that the U.S. and Japan engaged primarily in trade, and not financial or

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investment relations through loans, foreign direct investment or bonds/securities. This trade can be characterized as asymmetric (i.e., Japan relied on the U.S. more) and concentrated, as relatively few items comprised the trade.309 United States imports from and exports to Japan were not significant as a percentage of total U.S. imports and exports. Exports to Japan in this period never averaged above 5% of total U.S. exports, and imports ranged between only 7-10% of total U.S. imports. In contrast, the U.S. was Japan's single largest trading partner. Japan relied on the U.S. market to absorb between 27-44% of its total exports, and between 31-37% of its total imports came from the U.S. (See Table 3.4). Japan's reliance on the U.S. was more concentrated in exports as 60-83% of its exports to the U.S. were in the single commodity of raw silk (i.e., commodity concentration).310 Japan's raw silk exports were further concentrated on the U.S. market because the U.S. took 83-96% of total Japanese raw silk exports in this period (i.e., partner concentration in the most important single commodity).

<table>
<thead>
<tr>
<th></th>
<th>1918</th>
<th>1919</th>
<th>1920</th>
<th>1921</th>
<th>1922</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Total exports of Japan in thousands of Yen (as % of Japanese GDP)</strong></td>
<td>1,962,101 (16.57%)</td>
<td>2,098,873 (13.58%)</td>
<td>1,948,395 (12.26%)</td>
<td>1,252,838 (8.42%)</td>
<td>1,637,452 (10.51%)</td>
</tr>
<tr>
<td><strong>Japanese exports to U.S. in thousands of Yen (as % of total Japanese exports)</strong></td>
<td>530,129 (27.01%)</td>
<td>828,098 (39.45%)</td>
<td>565,018 (29.2%)</td>
<td>496,000 (39.59%)</td>
<td>732,377 (44.73%)</td>
</tr>
<tr>
<td><strong>Japanese raw silk exports to U.S. in thousands of Yen (as % of total exports to U.S.)</strong></td>
<td>318,673 (60.11%)</td>
<td>600,843 (72.56%)</td>
<td>341,599 (60.46%)</td>
<td>394,453 (79.53%)</td>
<td>610,844 (83.41%)</td>
</tr>
<tr>
<td><strong>Japanese exports to U.S. as % of Japanese GDP</strong></td>
<td>4.48%</td>
<td>5.36%</td>
<td>3.6%</td>
<td>3.33%</td>
<td>4.7%</td>
</tr>
<tr>
<td><strong>Total imports of Japan in thousands of Yen (as % of Japanese GDP)</strong></td>
<td>1,668,144 (14.09%)</td>
<td>2,173,460 (14.06%)</td>
<td>2,336,175 (14.7%)</td>
<td>1,614,155 (10.84%)</td>
<td>1,890,308 (12.14%)</td>
</tr>
<tr>
<td><strong>Japanese imports from U.S. in thousands of Yen (as % of total Japanese imports)</strong></td>
<td>626,026 (37.53%)</td>
<td>766,381 (35.25%)</td>
<td>873,177 (37.37%)</td>
<td>574,000 (35.56%)</td>
<td>596,169 (31.54%)</td>
</tr>
<tr>
<td><strong>Japanese imports from U.S. of cotton, iron and steel items, and machinery in thousands of Yen (as a % of total imports from U.S.)</strong></td>
<td>471,561 (75.32%)</td>
<td>512,476 (66.87%)</td>
<td>589,404 (67.5%)</td>
<td>N/A*</td>
<td>N/A</td>
</tr>
<tr>
<td><strong>Japanese imports from U.S. as a % of Japanese GDP</strong></td>
<td>5.3%</td>
<td>5.0%</td>
<td>5.5%</td>
<td>3.9%</td>
<td>3.8%</td>
</tr>
</tbody>
</table>

Table 3.4: Japanese Exports to and Imports from U.S., 1918-1922

* Imports of all iron and steel items not available. Cotton and machinery showed same trends as previously, although cotton imports from all sources decreased in 1921-2.
* U.S. Tariff Commission, Foreign Trade of Japan, pp.201-02; Uyeda, Recent Development of Japanese Foreign Trade, pp.57,70.
Japanese imports from the U.S. were principally raw cotton, iron and steel products and machinery. Cotton imports were the single largest item imported from the U.S. (e.g., 38% of 1920-1 total Japanese imports from U.S.). But, Japan was not exclusively dependent on the U.S. for its supply, as British India supplied roughly equal amounts of cotton to Japan. The U.S. had some vulnerability to Japan in cotton exports, as approximately 11% of U.S. cotton exports went to Japan in 1920-21.\(^{311}\) For all iron and steel products the U.S. was supplying the majority of the total, with Britain a close second. However, in the most important item necessary for shipbuilding (i.e., plate or sheet iron), the U.S. was supplying at least 75% of Japan’s import needs through 1921.\(^{312}\) Japanese imports of machinery (8-12% of total imports from the U.S.) were largely supplied by the U.S. in 1918 (i.e., 80% from U.S., 17% from Great Britain), but by 1922 they were more equalized between the two main suppliers (i.e., U.S. 50% and Great Britain 37%).\(^{313}\) Japan’s balanced sources of supply for the main items imported from the U.S. was an important aspect of this period. This balance affected the earlier trade sanctions effort of the U.S. in 1918 when the U.S. had to rely more on sanctioning

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\(^{312}\) U.S. Tariff Commission, *Foreign Trade of Japan*, pp.163-4. The U.S. government entered into substantial shipbuilding contracts with Japanese firms beginning in May 1918 under the Japan-America Steel Ship Exchange Agreement. This agreement and related contracts called for continued U.S. exports of iron and steel to Japan in exchange for completed merchant vessels inspected and certified by Lloyds of London. Some of this U.S. iron and steel probably directly or indirectly facilitated supplies to the Navy’s building plans. See Ohara, *Japanese Trade and Industry in the Meiji-Taisho Era*, pp.516-518. This fact illustrates the disregard in practice of the theoretical tension between economic and security interests as the U.S. supplied much of the imported plate or sheet iron necessary for Japan’s naval expansion up to the Washington Conference. It also demonstrates the willingness to supply an adversary building against oneself. However, the U.S. may have continued these supplies in order to hold this position as future leverage, preventing Britain or Germany from re-establishing their prewar supply positions. Nonetheless, because the U.S. supplied this steel to Japan while it was perceived as a great threat, realism is contra-indicated, particularly defensive realism, and liberalism is highly indicated as U.S. business interests appear to have desired this greatly.

Japanese exports of silk to the U.S. Not insignificantly, the first Japanese imports of crude petroleum from the U.S. in over a year occurred in December 1922 after Japan’s October withdrawal from Siberia and totaled 2,184,000 gallons.\(^{314}\)

During this period Japan’s overall trade balance was in deficit each year except in 1918 when Japan had a modest surplus of approximately 294 million Yen. This overall negative trade balance would continue for most of the interwar period and require Japan to maintain sufficient credit lines abroad or export reserves such as gold and silver to finance her excess import balances.\(^{315}\) Japan had pledged at the Genoa Conference (1922) that it would return to the gold standard, allowing its accumulated gold reserves to flow more freely to balance trade deficits while maintaining the Yen exchange value.\(^{316}\) This pledge was set back by the earthquake of September 1923, which compelled Japan to borrow from abroad to meet trade and currency value commitments. The bilateral trade balance with the U.S. showed a trade deficit for Japan in 1918 and 1920-21 of amounts ranging from 78 million Yen to 308 million Yen in 1920. Japan’s decade long run of trade surpluses with the U.S. began in 1922 with a bilateral trade surplus of 136 million Yen (See Table 3.5).

\(^{314}\) U.S. Department of the Interior, Mineral Resources of the United States, 1923-Part II. (Washington, DC: U.S. G.P.O., 1924), p.399. With Japan’s withdrawal from Siberia in October 1922, it appears the U.S. government may have released or eased oil exports to Japan. Compliance with the Washington Conference arrangements was undoubtedly significant in this change, although it remains unclear. See “The Petroleum Situation with Special Reference to the Far East,” p.43.

\(^{315}\) The majority of Japan’s overseas gold holdings were held in New York, as most of it moved from Britain in 1915, as a response to the war and security to balance its trade. Japan’s total gold holdings at home and abroad were $925 million dollars in 1922. It is not possible to determine how much was held in New York. It is odd that Japan would maintain more of its overseas gold in New York when most of its foreign debt obligations were in British pounds, although the U.S. was its largest trading partner. See U.S. D.O.C., Foreign Commerce Yearbook, 1922, pp.553-5.

Table 3.5: Japan’s Overall and Bilateral Trade Balance, 1918-1922

<table>
<thead>
<tr>
<th></th>
<th>1918</th>
<th>1919</th>
<th>1920</th>
<th>1921</th>
<th>1922</th>
</tr>
</thead>
<tbody>
<tr>
<td>Overall trade balance of Japan in thousands of Yen (Exports - Imports)</td>
<td>293,957</td>
<td>-74,587</td>
<td>-387,780</td>
<td>-361,317</td>
<td>-252,856</td>
</tr>
<tr>
<td>Bilateral trade balance of Japan with U.S. in thousands of Yen (Japanese Exports to U.S. - Japanese Imports from U.S.)</td>
<td>-95,897</td>
<td>61,717</td>
<td>-308,159</td>
<td>-78,000</td>
<td>136,208</td>
</tr>
<tr>
<td>Total U.S.-Japan trade as % of Japanese GDP(Japanese exports to and imports from U.S. as % of its GDP)</td>
<td>9.78%</td>
<td>10.36%</td>
<td>9.1%</td>
<td>7.23%</td>
<td>8.5%</td>
</tr>
</tbody>
</table>

During this period, Japan’s trade with the U.S. was significant to its overall economy averaging 9% of GDP, whereas U.S. trade with Japan was never more than 1% of U.S. GDP. The importance of the bilateral surpluses going forward was primarily in mitigating extra pressure on Japan’s holdings of gold or need for foreign loans to maintain her trade financing position. Based on the content of the traded items it is easy to conclude that Japan’s material capabilities were being relatively advantaged compared with the U.S. This conclusion flows from the obvious and direct effect that U.S. exported steel plates had on naval construction in Japan and the cumulative gains effect of other items such as machinery. Japanese exports to the U.S. consisted mostly of luxury items (e.g., silk) that did not materially affect U.S. military power and did not generate any release of efficiency gains from specialization away from U.S. silk production with the
trade. For these reasons the exchange relationship during 1918-1922 can be
categorized as narrow due to its trade only character, concentrated in relatively few items,
and far more beneficial to Japan's economic and military capabilities.

317 Silk would later be used in large quantities for parachute manufacturing and would then constitute a
significant item to the U.S.
CHAPTER 4

U.S.-JAPAN, 1922-1929

4.1 Chapter Overview

The successful conclusion of the Washington Conference treaties marked the early part of this period as the U.S. reacted favorably to Japan’s compliance with the treaties and withdrawal from Shantung in particular. U.S. threat perception of Japan at the beginning of 1923 was less than previously, but still moderate due to Japan’s continued occupation of N. Sakhalin and endeavors to exclude other states from economic development in Manchuria and North China. Nonetheless, the decreased threat perception continued through 1925 when Japan’s agreement with Russia regarding the disposition of N. Sakhalin oil raised U.S. concerns regarding Japan’s ability to achieve oil autonomy and affect a rapprochement with Russia allowing it to expand more easily in North China and Manchuria. Despite an assessment by Stanley Hornbeck among other U.S. officials that Japan would pursue a moderate foreign policy in China due to financial considerations and broader economic ties with the U.S., the Japanese field army in Manchuria, the Kwantung army, assassinated the Manchurian leader Chang Tso-lin in early June 1928.

This action and the failure of Premier-General Tanaka’s Japanese government to effectively manage the domestic fallout over the rogue actions of its field army, caused
the U.S. threat perception of Japan to begin to increase gradually. As a result, the U.S. stepped up its economic assistance to China beginning in July 1928 and announced its support for a fully sovereign China under the Nationalists. The period ends with the change in Japanese leadership from General Tanaka to Premier Wakatsuki, a Finance Minister in a previous Japanese cabinet who established a “moderate” pro-Western government. U.S. threat perception of Japan up through this change was linked, however, to its competition for influence with both Britain and Japan over the fate of China, naval arms limitations and the disposition of DEI oil resources. Repeated failure to achieve more coordinated Anglo-American-Dutch oil cooperation in the mid-1920s helped cause the U.S. to take an aggressive naval armaments position leading up to the Geneva naval arms talks in June 1927. This posture against Britain would only ebb after the British and Dutch agreed at the end of 1927 to allow greater U.S. oil company presence in the DEI. In mid-1928, these pressures resulted in fundamental oil cooperation in the DEI among the Dutch, British and Americans, but came at Japan’s expense. Because Japan had sought ownership rights in the DEI as did America, the Dutch feigned cooperation with the Japanese while genuinely incorporating greater American oil company interests there. The Japanese were given oil lands in the DEI at the same time as well. They were “valueless” properties, however, and would only lead to wasted Japanese capital in the future and reinforced dependence on U.S., British and Dutch government-controlled sources.

The U.S. knowingly partook in this exclusion by induction of Japan, thereby maintaining Japanese oil import dependency. The U.S. increased Japan’s crude oil dependency by paradoxically assisting Japan’s crude-based refinery development and
providing the majority of its oil products imports by the end of the period. This set of exchange interactions was the single most important exchange that occurred in the period because it established the predicate for joint Anglo-American-Dutch coordination against Japan's oil autonomy efforts. Its resolution validates offensive realism because U.S. actions and purposeful failures to act combined to ensure Japanese dependency on principally U.S. supply sources going forward and the U.S. policy of supplying Japan over its navy's initial objections. Other U.S. exchange with Japan was even more intrusive although also more beneficial to Japan than in the prior period. U.S. loans to Japan began in 1923, but were directed by the State department and often contained government to government pledges that the proceeds would not be spent in Japan's "sphere of interest" (e.g., Manchuria, South Sea islands). The U.S. also continuously blocked loans to the Japanese army-related South Manchuria Railway Co., showing its hand in attempting to influence Japan's domestic factional competition and foreign policies. More importantly, the U.S. coordinated the grand strategic purposes in the loan extensions without relying on any one banking actor to achieve its overall Asian policy preferences. By coordinating the actions of the different banks in the Japan finance (i.e., J.P. Morgan, National City) and those in the DEI finance (i.e., Guaranty Trust, Dillon Read & Co.), the U.S. government maintained its position of primacy over all of the banks. For these reasons, the U.S. government was dominant in the balance of state-corporate achieved preferences in this period, but did not restrict Japan's increased economic capabilities remotely enough to validate defensive realism.

U.S. direct investment in productive enterprises with potential dual-uses increased (e.g., auto production facilities), as did the accumulation of dollar balances by Japan due
to its bilateral trade surpluses with the U.S.. The composition of traded items continued to yield Japan a relative advantage, as it received large amounts of scrap iron and steel necessary to naval building and its further industrialization, while the U.S. continued to import primarily silk. The trade was still highly asymmetric with Japan relying on its U.S. trade to support over 9% of its economy and the U.S. value of its Japanese trade remained under 1% of GDP. Furthermore, Japan did not reduce its vulnerability to a U.S. silk embargo because the U.S. continued to absorb almost all of Japanese silk exports. Japan’s import dependence on U.S. crude and fuel oil increased over the period, ending 1928 at 73.4%. For these reasons, the exchange in this period was broadening considerably, but paradoxically increasing both Japan’s vulnerability to the U.S. and its dependence on it. Japan’s dependence on the U.S. was, in fact, higher than it had been previously due primarily to the oil dependency and foreclosure of its access to DEI concessions. Because much of these outcomes were the result of U.S. policy, the dominant theory perspective in this period was offensive realism.

4.2 Post-Washington Conference: Decreased Threat and Broadened Exchange

The post-Washington Conference environment of improved relations between the U.S. and Japan provided opportunities for expanded trade and financial relations between the two countries. In fact, Japanese support for the Conference agreements was predicated on increased and non-discriminatory economic exchange with the U.S., and Secretary of State Hughes believed that more exchange benefits for Japan would help it
choose cooperative foreign policies. In the area of foreign loans, however, the U.S. government took steps to ensure its oversight, if not control of the beneficiaries of increased exchange. In early 1922, President Harding met with leading American bankers and instructed them about prior government notification of foreign loan and bond offerings, and this was formally announced by the U.S. State department in March 1922. This notification and approval process had existed informally in the past, but by early 1922 it was formally placed under State department control.

The State Department used its authority to manage capital flows to Japan from 1922 forward, placing use provisions on some loans that were allowed and discouraging other loans altogether. The basis for approving or denying capital extensions to Japan was whether the funds would be used to further Japan's exclusionary and monopolistic practices in Manchuria and northern China (i.e., its "peaceful penetration" and political control). Diplomatic review of these loans demonstrates the desire to control Japan's foreign policy through this economic relationship. For example, in 1922 Japan's government-controlled Oriental Development Company negotiated a $19,900,000 loan from the National City Bank of New York, but was denied approval for the loan by the

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318. Louria, Triumph and Downfall: America's Pursuit of Peace and Prosperity, 1921-1933, p.39. For their part, Japanese industrialists held similar beliefs. For example, Kaneo Nanjo, managing director of the Mitsui zaibatsu hoped the conference would reverse declining U.S.-Japan relations: “with friendly relations once firmly established between America and Japan there opens out for the people of our respective countries such prospects for trade and wealth production as no other countries have ever enjoyed.” Ibid.

319. The State department announcement noted that it "should have the opportunity of saying to the underwriters concerned, should it appear advisable to do so, that there is or is not objection to any particular issue." See Pamphlet No. 52, Diplomatic Protection of American Investments Abroad, (NY: Foreign Policy Association, September 1928), p.10. See also Herbert Feis, The Diplomacy of the Dollar: First Era, 1919-1932, (Baltimore, MD: Johns Hopkins Press, 1950), pp.7-8.

320. U.S. financiers had participated in earlier Japanese bond issues through sharing in issues originating in London. For example, Japanese government bonds totaling 10,000,000 British pounds were issued in May 1904, and New York bankers took equal shares of this issue and resold them to U.S. investors. This occurred again in 1912 when the City of Tokyo issued 9,175,000 British pounds of debt and U.S. bankers picked up 2,000,000 pounds of this. See Paul Dickens, U.S. D.O.C., B.F.D.C., A New Estimate of American Investments Abroad, (Washington, DC: U.S. G.P.O., 1931), p.21.
State and Commerce departments. Only after obtaining Japanese government assurances that the proceeds would not be expended in Manchuria, Mongolia, the South Sea Islands or the Straits Settlement was the loan approved and finalized on March 15, 1923.321 This example is compatible only with offensive realism, as the State department conditioned the terms of the loan’s use in an effort to influence how Japan acted abroad. The U.S. was demonstrating that it would assist Japan economically only where it acted according to U.S. preferences, and attempting to condition Japan to act these ways to receive the benefits of U.S. exchange.

Initial opposition to this first large-scale loan to a Japanese concern was stated directly to American bankers, but to the Japanese "diplomacy demanded, however, that the explanation exclude the blunt mention of political or strategic considerations."322 Instead, objection was couched in the logic of non-discrimination against American firms competing in the Far East.323 National City Bank also sought loans for Japan's South
Manchuria Railway Company in 1923 and again beginning in March 1927. Both times the U.S. State department objected and the loans never materialized. In the Fall of 1927, J.P. Morgan & Co. sought to issue a $30 million dollar loan to the South Manchuria concern and was similarly shepparded into non-issuance. The South Manchuria Railway Company never directly received American funds in the interwar period, despite bankers' interests in providing them, because of its exclusionary colonizing practices and the U.S. government's desire not to directly assist Japan's Manchuria policies. These denials of American capital to the South Manchuria Railway Company were also made necessary by the fierce opposition of Chang Tso-lin, the politico-military leader of Manchuria and North China, who demanded that Washington cancel the proposed loans or bear the consequences of adverse Chinese public opinion. Washington backed Chang’s demand and directed Morgan & Co. to cancel the loan, thereby further tying the U.S. position on Northern China to Chang and against Japan. This position cost the U.S. government any hope of buying off or specification that a given portion or all of the proceeds shall be devoted to purchases in the United States."

See letter from Leland Harrison, Assistant Secretary of State to Milton Ailes, Riggs National Bank, June 14, 1923, in Hornbeck Papers, Box 244, Folder: Japan Oriental Development Company.

This company was formed subsequent to the Russo-Japanese war and was directly controlled by the Japanese government, which used it to increase its economic and political control in South Manchuria and elsewhere. The South Manchuria Company obtained foreign financing from the British in 1923 and thereafter directly from the Japanese government. See Staley, War and the Private Investor, pp.275-7; Wilson, American Business and Foreign Policy, p.214.

President Coolidge stressed the difference between loans to Japan and its South Manchuria company, where assistance to the latter "might carry with it the implication that we endorsed what might be called the Japanese special position (in Manchuria)." President Calvin Coolidge, quoted in, Iriye, After Imperialism, p.185.

National City Bank and Morgan & Co. tried to make these loans more palatable to U.S. officials by guaranteeing that their proceeds would be spent on American goods. Bankers, including Thomas Lamont of National City Bank, insisted Japan was not violating Open Door principles in Manchuria and was instead a force for stability in the region. Lamont found one sympathetic American official, U.S. Ambassador to Japan, Charles Mac Veagh, who openly lobbied for the Morgan loan as well. See Wilson, American Business and Foreign Policy, pp.212,305, footnote 53; Iriye, After Imperialism, pp.187-189.

Feis, The Diplomacy of the Dollar, pp.36-7. American officials were interested in Chang Tso-lin because of his anti-Japanese sentiment and his precarious position in Manchuria, where he used Japanese
positively influencing Japan's army and contributed to the army's willingness to violate American preferences on China policy, exacerbating the long-run incompatibility of U.S.-Japan interests that ended in war.

Other than the Oriental Development Company and government loans, American loans were made exclusively to Japanese electric utility companies (See Table 5).³²⁸ These companies were affiliated with Japan's two main political parties, Minseito and Seiyukai, which were increasingly responsive to public opinion, particularly after universal male suffrage in 1925.³²⁹ It is not clear if the U.S. extended loans to these private companies explicitly to bolster their operations and those of their political party patrons in domestic competition with imperialist factions. However, the capital denials to the army-dominated South Manchuria Railway Co. appear to indicate this, and certainly had that effect whether it was intended by the U.S. or not. Similarly, the total value of non-government, or private corporate loans across the 1923-1931 period when the U.S. made loans to Japan, was $251.2 million dollars. Loans to the Japanese national and local governments in the same period totaled $284.3 million dollars. If anything, this demonstrates U.S. government willingness to authorize financial exchange with and

³²⁸ Some of these loans were, however, diverted by the Japanese government to pay for its unsecured loans in China (i.e., the Nishihara loans) and to colonizing corporations throughout Asia. See Wilson, American Business and Foreign Policy, pp. 212-14.

possible influence upon Japanese government offices directly; instead of allowing loans predominantly to non-state actors, facilitating bottom-up pressure through private actors in Japan (i.e., this is more consistent with offensive realism than liberalism). Nonetheless, some have concluded the overarching purpose of U.S. capital extensions to Japanese concerns was consistent with liberal appeasement. This position was stated well by Herbert Feis: "The American government preferred to allow Japan to grow stronger in the hope that it would grow friendlier—rather than give it another grievance."330

<table>
<thead>
<tr>
<th>Japanese Recipient</th>
<th>Amount of Loan</th>
<th>Date of Issue</th>
<th>Use Provisions/Quid Pro Quos</th>
</tr>
</thead>
<tbody>
<tr>
<td>Oriental Development Co.</td>
<td>$19,900,000</td>
<td>March 1923</td>
<td>no use in Manchuria, Mongolia, South Sea Islands or Straits Settlements</td>
</tr>
<tr>
<td>Japan National Government</td>
<td>$150,000,000</td>
<td>February 1924</td>
<td>most went to conversion of Sterling balance loans and remainder to post-earthquake reconstruction</td>
</tr>
<tr>
<td>Daido Electric Power Co.</td>
<td>$15,000,000</td>
<td>August 1924</td>
<td></td>
</tr>
<tr>
<td>Industrial Bank of Japan</td>
<td>$22,000,000</td>
<td>August 1924</td>
<td></td>
</tr>
<tr>
<td>Toho Electric Power Co.</td>
<td>$15,000,000</td>
<td>March 1925</td>
<td></td>
</tr>
<tr>
<td>Ujigawa Electric Co.</td>
<td>$14,000,000</td>
<td>March 1925</td>
<td></td>
</tr>
<tr>
<td>Daido Electric Power Co.</td>
<td>$13,500,000</td>
<td>July 1925</td>
<td></td>
</tr>
<tr>
<td>Tokyo Electric Light Co.</td>
<td>$24,000,000</td>
<td>August 1925</td>
<td></td>
</tr>
<tr>
<td>Toho Electric Power Co.</td>
<td>$10,000,000</td>
<td>July 1926</td>
<td></td>
</tr>
<tr>
<td>City of Yokohama Reconstruction</td>
<td>$19,740,000</td>
<td>December 1926</td>
<td>city reconstruction</td>
</tr>
<tr>
<td>City of Tokyo Reconstruction</td>
<td>$20,640,000</td>
<td>April 1927</td>
<td>city reconstruction</td>
</tr>
<tr>
<td>Tokyo Electric Light Co.</td>
<td>$7,650,000</td>
<td>December 1927</td>
<td></td>
</tr>
<tr>
<td>Nippon Electric Power Co.</td>
<td>$9,000,000</td>
<td>January 1928</td>
<td></td>
</tr>
<tr>
<td>Tokyo Electric Light Co.</td>
<td>$70,000,000</td>
<td>June 1928</td>
<td></td>
</tr>
<tr>
<td>Oriental Development Co.</td>
<td>$19,900,000</td>
<td>November 1928</td>
<td>no use in Manchuria, only Korea or Japan proper</td>
</tr>
<tr>
<td>Toho Electric Power Co.</td>
<td>$11,450,000</td>
<td>July 1929</td>
<td></td>
</tr>
<tr>
<td>Japan National Government</td>
<td>$71,000,000</td>
<td>May 1930</td>
<td>quid pro quo for signing London Naval Treaty</td>
</tr>
<tr>
<td>Taiwan Electric Power Co.</td>
<td>$22,800,000</td>
<td>June 1931</td>
<td></td>
</tr>
</tbody>
</table>

Table 4.1: U.S. Loans to Japanese entities, 1923-1931


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As will be discussed in greater detail in the next chapter, the most significant loan in the whole period of American loans to Japan was the Japanese government loan in May 1930. The U.S. State department authorized loans to the Japanese government totaling $71 million at that time, but this loan was explicitly tied to consummation of the London Naval Treaty in April 1930. The monies were used to refinance prior British pound-denominated loans and to cushion the deteriorating government budget position due to the world depression. The final loan advanced to Japanese interests occurred in July 1931, when the Taiwan Electric Power Co. obtained $22.8 million in New York, despite the effects of the depression on the U.S. banking community and a possible national interest in keeping capital at home. Because American loans to Japan continued well after the effects of the U.S. banking crisis were felt, the primacy of U.S. government policy is evident. The economic interests of U.S. bankers and disregard for domestic capital retention were made subservient to the policy of propping up the embattled liberal elements in control of Japan’s government. Financial exchange ended with the September 1931 aggression in Manchuria and the U.S. government’s decision to ban loans to Japan in support of the Stimson Doctrine.\textsuperscript{331} The loan ban was upheld despite vigorous protestations by leading American financiers that Japan was acting legitimately in Manchuria and was in fact a force for stability there.\textsuperscript{332}

\textsuperscript{331} Wilson, American Business and Foreign Policy, pp. 232-5.
4.3 Post-Washington Conference Widened Competition in Oil

The post-Washington Conference period also witnessed a halting realignment of political and economic relations among Great Britain, the U.S. and the Netherlands, particularly with respect to oil in Asia. This realignment would eventually have serious consequences for Japanese efforts to achieve some measure of economic autonomy.

Prior to the Washington Conference, commercial and state competition in the oil industry had reached an intensity that would not be seen again in the interwar period. Standard Oil was engaging Royal Dutch Shell in price wars in its home state by reducing the price of gasoline in the Netherlands, directly challenging the Royal Dutch as it perceived the Royal Dutch was doing in the U.S. and elsewhere.3 3 3 This situation was resolved in principle with agreements to cooperate globally with Britain, the Netherlands and their companies, Anglo-Iranian and Royal Dutch Shell, in 1922 and 1923 in the Caribbean and Middle East.3 3 4 However, the U.S. felt that reciprocity was not forthcoming with respect to DEI access for U.S. nationals. In order to influence the decision regarding American participation in DEI oil development, the U.S. practiced mild coercive diplomacy toward the Dutch by sending the flagship of the U.S. Asiatic Fleet with a six destroyer convoy to the DEI’s capital of Batavia in March 1923.3 3 5 Having made its desire clear, diplomatic

333. See letter William Phillips, Ambassador at The Hague Netherlands, to Secretary of State, March 28, 1922, file 856d.6363/189, RG 59; Nash, United States Oil Policy, pp.65-67. Phillips was charged with assessing whether any rapprochement between Standard Oil and the Royal Dutch was occurring (i.e., cooperative development of oil resources and possibly non-competitive pricing in markets).
335. See Reed, “Standard Oil in Indonesia,” p.330; Office of Naval Intelligence, Reports, from D. McD. LeBreton, Naval Attache, The Hague Netherlands to Director of Naval Intelligence, March 28, 1923, File o-1-l, Register 12865A. RG38.
wrangling continued to stumble over the Dutch dilemma of granting Americans oil concessions but not the Japanese, while making it not appear to be discriminatory against Japan.336

Lying underneath this oil concession sophistry was a very clear desire on the part of the Dutch to obtain increased security assurances as part of any oil arrangement.337 The Dutch clearly foresaw the strategic significance of DEI oil, Japan's threat to the DEI and the economic and security competition among Japan, Russia and the emerging U.S.-British nexus. Dutch authorities accurately assessed Japan's need for peace with either Russia or the U.S.-Britain entente, due to its resource needs and desire to avoid a two front war (e.g., N. Sakhalin and N. China, or DEI and mainland U.S. oil supplies).338 The Dutch understood their strategic importance in any Pacific conflict and wanted to absolve themselves of responsibility for oil resource demands and conflicts by having the private companies in the DEI assume this burden. A leading Dutch analyst, Dr. de Bruyn, noted: "Should America or Japan wish to obtain their fuel from India, they must try to come to an understanding with the Royal Dutch with regard to supplies of fuel. But this must be

336. The Japanese were seeking DEI oil concessions on "equal terms with other nations" (i.e., open door principle and joint management/exploitation of resources by Five Power Treaty signatories as in China). Dutch proposals for "legitimately" excluding Japanese interests included restricting concessions to only large oil companies with prior experience in the DEI, or companies with large capital budgets organized under Dutch law as Koloniale was, or having closed bids so that American interests could be rewarded without public discussion.

337. A typical exchange along these lines occurred between Richard M. Tobin, American Minister, The Hague Netherlands, and Jonkheer Sixx, Chief of Mineral Resources of the Netherlands Colonial Office, who spoke on his own and the foreign minister's behalf. Sixx asked whether allowing Standard Oil of New Jersey (i.e., Koloniale, as opposed to Standard Oil of California, Pure Oil Co., or Sinclair who also demonstrated interest) greater involvement would mean American government support for Koloniale and by extension security for the DEI. See Telegram, from Richard Tobin, American Minister, The Hague, Netherlands to Secretary of State, May 8, 1924, file 856d.6363/317, RG 59.

338. See article by Dr. Feuilletau de Bruyn, "Our Petroleum Industry and the International Position of Netherlands India," enclosed in letter from Charles Hoover, American Consul, Batavia to Secretary of State, September 23, 1924, file 856d.6363/445, RG 59. Hoover noted that this review article was "officially inspired," and corresponded to the Netherlands' Fleet Law legislation introduced for the Volksraad session of October 14, 1924.
done without the interference of the Government. As a neutral nation this will be the standpoint which Holland will have to take up." For its part, the U.S. understood that Japanese-Russian cooperation (i.e., Sakhalin and other resource sharing arrangements) might lessen Japan's dependence on any Anglo-American position and might have deleterious consequences for the fate of China.

The United States sought to demonstrate that Dutch neutrality backed by English naval power was not likely to be sufficient to deter Japan, nor placate U.S. interests, particularly if Russo-Japanese concord failed to materialize. The U.S. fleet visit in March 1923 was designed to do just this, as the American Consul in Batavia noted: "I hope that the visit of the fleet here in March will assure them eventually that there is a strong power on the line of communication between Japan and these islands which, in spite of our policy of non-interference in European affairs would undoubtedly have something to say to any attempt to seize the islands, which is what they fear." Dutch authorities favored the English because they held America's non-interference policy to be a hindrance to DEI security, and therefore were not inclined to open up the DEI to a non-politically backed American oil company presence. This Dutch sentiment extended to American loans made to the DEI in January of 1923 and highlight the intransigence of the Dutch to yield oil concessions without significant material or security compensation.

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339. Ibid., p.26. de Bruyn also contended this country's first policy would place liability for seizures of oil tankers squarely on private companies and remove the government from this area of contention.
341. Letter from Charles Hoover, American Consul at Batavia, to Secretary of State, April 26, 1923, RG 59, file 856d.51/48.
342. Anglo-Dutch security cooperation was increasing at this time as the new Dutch submarine base was being built opposite Singapore, flanking the Djambi concession area, and British naval and oil interests were increasingly coordinating with their Dutch counterparts on DEI matters. See letter Louis Sussdorff, U.S. Charge d'Affaires at the Hague, to Secretary of State, April 19, 1923, RG 59, file 856d.6363/237.

177

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The Guaranty Trust Company of New York was negotiating a $30,000,000 loan to the DEI throughout 1922 and requested approval by the U.S. State Department as per its now formal oversight function. The Secretary of State was advised by William Phillips, American Minister at The Hague, not to link the loan negotiations with the DEI oil concession issue as this would likely kill the loan negotiations and further bind the Dutch with London, because London would supply the capital. Despite this admonition a lengthy debate between State department officers in the Netherlands, the DEI and the Office of Economic Adviser ensued regarding the desirability of the loan and whether it should be tied to stymied U.S. oil interests in the DEI. Henry Starrett, American Consul at Batavia, noted "if American interests should have a substantial stake in these territories, the Dutch government might feel that this would tend to lessen the possibility of aggression by Japan in any contingency that might arise." Stanley Hornbeck responded to Messrs. Starrett, Phillips and Harrison that U.S. oil companies had already been given guidance to continue to press their claims with Dutch authorities, but more importantly the Dutch would resent overt pressure using the loan negotiations and British exposure to DEI loans was optimal. He noted:

343. This was the second installment of a $80,000,000 loan to the DEI. See Guaranty Company of New York, The Dutch East Indies: Holland's Colonial Empire. (New York, 1922). The Guaranty Company noted the necessity of lending to a trading partner: "we shall eventually import an increasingly large volume of foreign merchandise, and, against that time, we must acquire foreign investments, the return from which will pay for that merchandise. There is no firmer foundation for an extensive world trade than large foreign investments. Trade follows capital." Ibid., p.31.

344. Letter from William Philipps, American Minister The Hague, Netherlands, to Secretary of State. March 15, 1922, file 856d.6363/188, RG 59.

345. Starrett suggestion in letter from Arthur N. Young, Economic Adviser, State department to Leland Harrison, Assistant Secretary of State and William Phillips, American Minister at the Hague, November 4, 1922, file 856d.51/39, RG 59. Interestingly, the following year Starrett wrote a lengthy letter to Phillips lobbying for the creation of an oil coordinator within the U.S. State department because of the need to match British guile. He recommended Hornbeck for the position because of his commanding expertise on the delicacy of the U.S.-British oil and alliance negotiations. See letter from Henry Starrett to William Phillips, May 12, 1923, file 856d.6363/336, RG 59. Phillips responded "we are making a further effort here to concentrate the oil matters in the hands of Hornbeck." Letter Phillips to Starrett, June 1, 1923, Ibid.
We have already loaned the Dutch a considerable amount. Why not let or encourage some British money to go in?...Is it not better to have the risks which are inherent in the situation there in the N.E.I. distributed among several countries, and shared in particular by the British?^{346}

The loan went forward in January 1923 without being tied to U.S. oil concession negotiations nor the desire to further commingle economic and security exposures in the nascent Anglo-American alliance. The desire to commingle Anglo-American economic and security interests was expressed by Hombeck in August 1923 at the Williamstown Institute of Politics. His address entitled “The Struggle for Petroleum” was well attended by American and British officials and described the critical nature of oil in world politics and the intensity of competition among companies and governmental agencies.^{347} Hornbeck noted that the global competition was largely between the U.S. and Britain, and that the San Remo Agreement of April 1920 between Britain (Cadman) and France (Berthelot) established a troubling principle that their collaboration in the Middle East was to “expand to other countries by mutual consent.” Hornbeck declared the chief difference between American oil companies and their British counterparts to be one of private ownership instead of governmental ownership, wherein “the U.S. government makes no choice among them as they compete with each other both at home and abroad and has no connection with or financial or commercial interest in any of them.” Instead of continued political and commercial stalemate, Hornbeck offered a solution. He stated:

^{346} Stanley Hombeck. State department. Office of Economic Adviser, to Arthur Young, Economic Adviser, November 9, 1922, file 856d.51/42, RG 59. This instance illustrates state primacy and desire not to link loans and oil concessions due to alliance building considerations; it is also inconsistent with marxism-leninism’s contention that finance capital is linked to trade and investment by banking actors and they achieve their preferences over or through states.

regulated competition is an answer, however little has been done this way...suggestions have been made that the great companies themselves should get together and more or less distribute and parcel out the exploration and exploitation of undeveloped regions. That would greatly simplify the problem.348

Managing an understanding among oil companies while assuaging the security concerns of competing governments was to be no small task. It was fortunate that American linkage between its loans to the DEI and its oil company negotiations were kept separate in 1923 because the Dutch did not view the American loans as being extended on favorable terms, either economic or political. Instead they were seen as set at the “highest market price,” and this generated some repurchases of the bonds made from the loans back in the Netherlands in order to escape undue American pressure.349 Dutch desire to remain indebted only to the British continued throughout 1923-4 as they began consideration of opening further oil concessions in Aceh, the northernmost area of Sumatra. The Dutch were willing to allow American company ownership in these concessions, but not Japanese and they made this clear both to American officials and oil corporation executives.350

As with the Djambi concession the Dutch contended “international political considerations of the first magnitude make it impossible to offer the Aceh fields in an unreserved public competition.” This primary strategic consideration was that “possession by Japan of oil reserves adjacent to the proposed Singapore base would

348. Ibid. In this statement is tacit approval for the global oil cartel that finally emerged in 1928 and a realist rationale for it because it makes state policy more easily enacted.
349. Letter from Charles Hoover, American Consul at Batavia, to Secretary of State, April 26, 1923, file 856d.51/48, RG 59.
350. See letter Frederick Asche, Vice President, Standard Oil of New Jersey, to Secretary of State, June 21, 1923, file 856d.6363/264, RG 59. Dutch fears of Japanese penetration in the DEI were constant and evident in their reception of a “visit of study” delegation of Japanese parliamentarians in September 1924, whose real purpose was to obtain petroleum concessions at any price. See letter Charles Hoover, American Consul at Batavia, to Secretary of State, September 3, 1924, file 756d.94/3. RG 59.
constitute a menace both to the Netherlands and to Great Britain. It is of even greater importance to Great Britain than to the Netherlands to exclude Japanese interests from the Aceh oil fields, as these fields are nearer to the proposed British base than to the Dutch.\textsuperscript{351} The Dutch were willing to award these fields to American interests in an undisclosed bid and were interested in determining whether any American oil company carried particular weight with the U.S. government such that its participation in the DEI would help ensure American political involvement in DEI security. The U.S. government listened to these various machinations and responded in a principled manner. Secretary of State Hughes declared that the American government was "seeking equality of opportunity for American companies, not a particular opportunity for one or some American companies...the mere fact that some American interests might under this plan be admitted to participate in petroleum development in the Netherlands East Indies would in no way meet the contention of this government, advanced consistently and persistently that opportunity should be given openly and equally to any American companies which may wish to compete for concessions."\textsuperscript{352}

This lofty position did not extend, however, to Japanese companies who were discriminated against in the first allotment of foreign oil concessions in 1928, nor did it satisfy Dutch authorities' security interests. Instead, in late 1924 the Dutch declared that without explicit or implicit political guarantees from the U.S. government they would

\textsuperscript{351} Letter from Richard Tobin, Minister at The Hague, to Secretary of State, June 1, 1924, file 856d.6363/329, RG 59.

\textsuperscript{352} Telegram, from Secretary of State Hughes to Tobin, May 21, 1924, file 856d.6363/318, RG 59. Both Hughes and Hornbeck received Tobin's missive and were equally "principled" about open door economic policies. Hughes, however, had intimate ties to Standard Oil as an attorney prior to becoming Secretary of State, and after, as legal counsel he assisted Standard Oil of New Jersey in its effort to purchase Russian crude in 1925. See Denny, \textit{We Fight For Oil}, p.182; Hanighen, \textit{The Secret War}, p.110.
“keep the oil resources unexploited for a considerable period.” The Dutch position underscores the primacy of security concerns in economic negotiations and the willingness of states to forego economic production and revenues where adverse security effects would result (i.e., Japanese anger because of U.S. oil presence in the DEI without U.S. alliance commitment). While the possibility of Anglo-American-Dutch government cooperation temporarily faltered in the Far East, competition between the oil companies quickened over Russian oil exports, middle eastern supplies and N. Sakhalin. Understandings between Sinclair Oil and the Russian government about Sinclair’s rights in N. Persia and N. Sakhalin disintegrated as the British and American governments backed Standard Oil of New Jersey in North Persia and Sinclair’s claims fell apart in N. Sakhalin. Russian support for Sinclair was predicated on the close association of Harry Sinclair, Albert Fall and President Harding. After the Teapot Dome scandal and Harding’s death, Russian preference for Sinclair expired as well. Because of this change, Russia decided to foster better relations with China and Japan instead of

353 See Memorandum of Conversation between Tobin, Minister at The Hague and Arthur Young, Economic Adviser, State Department, November 25, 1924, file 856d.6363/367, RG 59.
354 In the mid 1920s, Dutch officials did share with U.S. officials the activities of various Japanese delegations to the DEI, particularly where Japanese officials made contact with Soviet sponsored communists in the DEI or toured oil and naval facilities. See letter C. Porter Kuykendall, American Consul in Charge, Batavia, to Secretary of State, November 6, 1928, file 856d.20/21, RG 59.
355 The capitalist common boycott of Russian oil due to Soviet nationalization fell apart in 1923 as Royal Dutch and Standard Oil contracted with the Soviet government for its oil exports. Their competition for Soviet oil intensified after 1925 as both sought to lockup Soviet oil exports in coming years. This conflict was occasioned by acrimonious charges as for example when Henri Deterding accused Standard Oil of New York in "trafficking in stolen goods," with its purchases of Russian oil in the fight for market share in India in early 1928. These price wars were commonly reported to have spread to China and likely next to the British Isles. See Denny, We Fight For Oil, pp.171-2, 182; New York Times, January 17, 1928.
356 Russia hoped to obtain U.S. diplomatic recognition through Sinclair’s influence and felt his company’s presence in N. Sakhalin would induce Washington to pressure Japan to evacuate the territory. See Denny, We Fight For Oil, pp.177-8. The U.S. State department also received entreaties from Standard Oil of California regarding its N. Sakhalin oil rights and informed them that the government would not back their claims either. Hornbeck had lobbied in vain for a more aggressive U.S. policy backing the oil companies rights and the Russian government’s desire to supplant Japanese occupation with American oil interests. See Chester, U.S. Oil Policy and Diplomacy, p.288.
America. This culminated in the January 1925 agreement with Japan sharing development of N. Sakhalin oil resources on a 50-50 basis, although the Japanese came to purchase most of Russia’s production there as well.

This reversal of Russian-Japanese antipathy and granting of long-term access to Japan of northeast Asia’s most promising oil resource created a new great power alignment possibility. Drawing on Japanese official sentiment, Louis Fischer concluded: “the Sakhalin contract is thus not merely an indication of a spirit of trust and friendship between the two great Far Eastern Powers, but also in a way a guarantee against future trouble...It is without a doubt an important component part of the mortar of the still imperfect Sino-Soviet-Japanese bloc.” Japan subsequently withdrew its military forces from N. Sakhalin and American oil interests there were effectively ended. This example of oil rewards from Japanese military occupation did not comfort Anglo-American-Dutch government or corporate actors. Instead, it stimulated their desire to reach an understanding on DEI oil resources and U.S. government interest in better relations with Russia.

357. Louis Fischer, quoted in Denny, We Fight For Oil, p.180. From 1925 on Russo-Japanese oil trade increased as did the U.S. government’s efforts to stimulate greater U.S. oil corporation activity with Japan. For example, John Nelson of the Department of Commerce’s Petroleum Section wrote to Francis Loomis of Standard Oil of California that Russian oil deals with Japan’s navy were increasing in 1928, possibly threatening his company’s interests in exporting to Japan, and by unstated extension the U.S. government’s interest in holding Japan’s supply lines. See letter from John H. Nelson, Petroleum Section, Minerals Division, Department of Commerce to Francis B. Loomis, Standard Oil of California, April 18, 1928, General Records of the Bureau of Foreign and Domestic Commerce, 1914-1958, Box 1411, Folder: Oils, Mineral-Japan 1926-1940, Record Group 151, National Archives hereafter cited as “RG 151.”

358. The State department under Secretary of State Frank Kellogg began to relax some of its near total restrictions on credit to Russia and began to allow discussion of longer-term loans, provided they or other instruments were not sold as securities to the public. Short-term financing of trade was never restricted. Denny, We Fight For Oil, pp.204-6; Feis, Diplomacy of the Dollar, pp.46-8. See also Richard Tobin, Minister at The Hague to Secretary of State. November 23, 1925, file 756.00/7, RG 59.
4.4 Failure and Aftermath of the 1927 Geneva Naval Talks: the Anglo-American-Dutch Oil Peace

The competition between Royal Dutch Shell and Standard Oil concerns (e.g., Standard of New York, New Jersey, California) intensified throughout the middle 1920s as conflict over Russian oil disposition and price wars in previously coordinated markets accelerated (e.g., England, India, Africa and central Europe). Continued commercial competition over oil was a consequence and symptom of continued Anglo-American discord in naval matters and national strategies in Asia. Sensing the drifting away of Britain, under Shidehara's foreign ministerial stewardship, Japan sought stronger ties with the U.S. The U.S. reciprocated, hoping that broader bilateral economic ties would temper Japanese policies in Asia better than did Britain's alliance with Japan. This was evident in 1925, for example, as Britain moved toward more unilateral policies in China and fortification of Singapore, which caused greater Japanese apprehension for Britain than any time previously.

The post-Washington Conference competition among the three principal naval powers in cruisers, particularly heavy cruisers, continued to cloud construction of Anglo-American strategic accord in Asia. This became evident in the preparatory talks for the Geneva Naval armament conference set to convene in June 1927. The U.S. demanded parity with Britain in overall tonnage in light and heavy cruisers. It also pressed its preferred constraints on gun size and displacement of these cruisers (i.e., building of

359. Denny, We Fight For Oil, pp.186-199. Over-production and ruinous price war competition was accelerating into the late 1920s as was political acrimony, and was cause for the 1928 "As Is" settlement.
360. Premier Wakatsuki voiced what Washington hoped expanded bilateral economic exchange would mean. After noting that the U.S. was Japan's principal export market, Wakatsuki said, "one does not fight one's best customer." Premier Wakatsuki, quoted in Fanning, Peace and Disarmament, p.48.
361. Ibid., p.22.
10,000 ton displacement cruisers) in addition to parity in submarines and destroyers. The British viewed these demands with some concern as to their utility beyond American prestige bolstering. Winston Churchill captured British sentiment of America’s desire for equality in naval power: “it always seems to be assumed that it is our duty to humour the United States and minister to their vanity. They do nothing for us in return, but exact their pound of flesh.” Japan’s desire to resist extension of the 5:3 capital ship ratio to cruisers and destroyers colored its approach to the Geneva talks, but their position did not materially affect the outcome of failure as Anglo-American discord and French intransigence on even attending the talks doomed this arms control effort to failure.

The Geneva conference talks ended in early August 1927 with no agreements in place on cruisers, destroyers or submarines, and only served to highlight the continued rivalry between the U.S. and Britain. During this period the U.S. pressed for greater inclusion of its oil companies in the DEI and began to make this demand more explicitly tied to other relationships with both the British and Dutch. With respect to the Dutch, the U.S. State department signed off on a $25 million dollar loan from Dillon Read & Co. to the Batavia Petroleum Company (BPM) on January 11, 1927, noting that it would allow the loan because the central Dutch government was “favorably disposed” to granting a concession to Standard Oil in the near future. American lending to the principal rival to Standard Oil of New Jersey in the DEI (i.e., SONJ’s subsidiary Koloniale), while

362. Winston Churchill, quoted in, Ibid., p.61. Britain had proposed a 6:5 overall tonnage ratio for cruisers favoring itself, and this was highly distasteful to the U.S..
363. See letter Arthur N. Young, Economic Adviser, State Department to Leland Harrison, Assistant Secretary of State, January 11, 1927, file 856.51B31/1, RG59. The U.S. government was able to remain above particular bankers’ interests in coordinating overall Asian policy by allowing some banks to deal with the DEI and others with Japan (e.g., Dillon Read with the Dutch, but not Japan). In so doing, the U.S. could help construct a Japanese-exclusionary political and economic entente with Britain and the Netherlands using some American banks, while building ties to Japan using other American banks.
Koloniale was still being formally excluded from further participation there, highlights the U.S. government's desire to end the oil competition and political standoff there through more, not less economic integration. The use of direct financial exchange with the Dutch company also reveals America's desire to bring the Netherlands into its fold somewhat and end the exclusive British domination of Dutch foreign and commercial policies. The Dutch government reciprocated and began passing the contract granting Koloniale new oil concessions through its legislative organs in April 1927, thereby creating the foundations for Anglo-American-Dutch cooperative management of this most important source country in Asia.

Cooperative settlement of the DEI issue was a precursor and emblem of the overall cooperative framework establishing an oil peace between American and British-dominated firms. This cooperative framework was pushed by the British government at Achnacarry, Scotland in August 1928 (i.e., the “As Is” agreement), which followed the agreement expanding concessions for Standard’s Koloniale in the DEI. The As Is agreement established the global oil cartel and control of national markets through fixed percentage quotas for the major oil firms in virtually every national market. One of the most important provisions was the agreement to supply national markets from the closest

364. Richard Tobin, American Minister at The Hague noted the U.S. tone in policy toward the Dutch well when he stated “nothing is gained in dealing with the Dutch people by anything that resembles coercion. Like all small nations they are jealous of their independence and even the semblance of compulsion arouses their resentment.” See letter Richard Tobin to Secretary of State, October 29, 1927. file 856d.6363/493, RG 59. Curiously, this same concern would not be advanced toward Japan at the London Naval Conference in 1930.

365. Most analysts of oil politics in the 1930s looked back on American-Dutch relations in 1927 and noted that they signaled the end of competition and the founding of the “oil peace” among the principal countries Britain, the U.S. and the Netherlands. See report by American Trade Commissioner in Batavia, Donald W. Smith, “American Capital in the Netherlands Indian Petroleum Industry,” July 21, 1937. File o-1-1, Register 12865D, RG 38.

supply sources, with each cartel member using a uniform selling price. It was, however, a structure not limited only to the extraction and distribution of petroleum. Coal hydrogenation (i.e., deriving petroleum products from coal through a high-pressure refining process) under the Bergius patented method had been commercially developed by the chemical giant I.G. Farben of Germany. This technology represented a distinct threat to the oil companies' control of national petroleum markets. For this reason, I.G. Farben was brought into the oil company cartel through a series of binding contracts beginning in late 1927, which yielded control of the Bergius coal-hydrogenation method outside of Germany to the oil companies.

The abundance of coal in many then oil import-dependent countries and the technology for processing it into competing products created tremendous fear in the oil cartel, and thus their desire and success in acquiring the worldwide rights to it outside of Germany. This agreement bound the petroleum and chemical industries in a global petrochemical industrial cartel, and also tied the governments of England, the U.S. and Germany together in a petrochemical concert of divided labor and specialization. The base agreement between Standard Oil of New Jersey and I.G. Farben held "neither party

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367. It is this provision that makes subsequent Japanese oil supplies from predominantly the U.S. all the more striking as the DEI is the closest source to the Japanese market.  
368. Japan's efforts at coal hydrogenation using the German technology may have played a part in U.S. government willingness tolerate the cartel arrangements set up with IG Farben and British oil interests. It can not be determined with specificity what role Japan's efforts may have played in stimulating these arrangements. However, reports of Japanese deals for the German technology existed prior to final consummation of the global cartel. See ONI report, "Purchase of Manufacturing Rights for Producing Fuel Oil from Coal," January 18, 1928, File e-10-d. Register 13177D, RG 38.  
369. See Nowell, Mercantile States and the World Oil Cartel, pp.228-246; Denny, We Fight For Oil, pp.236-241; Hearings before the Committee on Patents, S. 2303 and S. 2491, part 7 (31 July, 3-4 August 1942) and part 8 (4, 5, 12 August 1942) 77th Cong. 2d sess. (Washington, D.C.: USGPO, 1942), hereafter cited as "Hydrogenation Patent Hearings."  
370. The intimate bond between Standard's Walter Teagle and I.G. Farben's Carl Bosch is also reported to have been sealed with Bosch's saving of Teagle's dog's life during his 1925 trip to the U.S. in preparation for the patent arrangement. See Bennett Wall and George S. Gibb, Teagle of Jersey Standard, (New Orleans, LA: Hauser Press, 1974), p.300.
has any plan or policy or so far expanding its existing business in the direction of the
other party’s industry as to become a serious competitor of that other part, but each
recognizes that certain overlapping of activities will exist.” This understanding would
later be tested by the question of Japanese coal hydrogenation, but the oil companies’
coordination of the petroleum market in Japan followed the Achnacarry meeting and
reprised past collaboration there. Unfortunately, the As Is understandings regarding
Japan are not well documented, but their relationship to pricing and production decisions
in the DEI is probable. The 1952 Federal Trade Commission investigation noted that
prices in the DEI were considerably higher than in other producing countries due to
agreement between Standard and Shell.

The year 1928 marked the resolution of Anglo-American-Dutch standoff over
DEI oil resource sharing and the beginning of coordinated manipulation of Japanese
interests in the DEI and its energy autonomy more broadly. At this time, Standard Oil of
New Jersey (i.e., Koloniale) was awarded a large, reserve-laden oil concession and
guaranteed a second concession later in the year as proof of continued “non-

371 Agreement between Standard Oil of New Jersey and I.G. Farben, November 9, 1929, Hydrogenation
Patent Hearings, p.2859. Overlapping activities included ancillary development in the chemical or refining
industries, such as the “production of artificial silk.” The agreement stipulated further cooperation in
controlling these products.
372 Denny reports Dutch Shell and Standard agreements to equally divide Japanese market control in 1911,
while the official U.S. Federal Trade Commission report on the oil cartel noted collaboration dating to
1906. See Denny, We Fight For Oil, p.31; Samuels, The Business of the Japanese State, p.170;
International Petroleum Cartel, Staff Report to the Federal Trade Commission, Select Committee on Small
hereafter cited as FTC Report.
373 FTC Report, p.342. This Report also stated, “While it seems evident that cooperation existed among
the oil companies in the market east of Suez, no information is available that would indicate the nature of
the agreements governing this cooperation.” It is probable that prices were higher in the DEI to keep
Japanese demand lower than for California products, Japan’s “natural market” for petroleum products.
discrimination" by the Dutch. Meanwhile, the Japanese had to be contented with a private acquisition (i.e., not a government concession, although the Dutch government prodded the sale) of previously prospected land held by the East Borneo Co. This concession in Kotei had been previously prospected by both the Royal Dutch and New Jersey Standard’s Koloniale and was optioned to the Japanese by Royal Dutch interests at the same time as the public land concessions were granted to Koloniale, highlighting the coordinated yet minimal fulfillment of Japanese interests. A naval intelligence report concluded: “It would appear that they (Japan) are willing to proceed with considerable outlay of money, even though the land bought is considered by the oil world as valueless, in the hopes that later, after this outlay, they may be in a position to assert that having heavily invested in the Dutch East Indies, they should be allowed concessions in the public lands.” This oil concession and type of foreign direct investment became a large sinkhole for Japanese capital and a clear example of how politically purposive economic exchange can absorb resources (i.e., investment capital) and yield negative effects on economic growth and possible military power.

374. The first Koloniale concession was of approximately 600,000 acres and passed the Netherlands’ upper house on February 8, 1928. The official contract was not signed until July 17, 1928 and the second concession of 360,000 hectares was agreed to in December 1928. See Reed, “Standard Oil in Indonesia,” pp.335-336; Memorandum, Arthur N. Young. Economic Adviser. State department to Secretary of State, March 2, 1928, file 856d.6363/513, RG 59.
375. See also Jan O.M . Broek, Economic Development of the Netherlands Indies, (New York: Institute of Pacific Relations, 1942), p.44. The East Borneo Company was a Dutch concern and after ceding land to Mitsui of Japan they gained one directorship on Mitsui’s oil company board.
376. This was practical on the part of Japan because the Dutch colonial government claimed Japanese exclusion from the public lands awarded to Koloniale was due to its status as a company already heavily invested in the DEI. See Office of Naval Intelligence. Reports, June 6, 1929, Memorandum for Director of Naval Intelligence, File o-1-l, Register 12865C. RG38, p.10, hereafter cited as “ONI Report June 1929.” See also letter, Hallett Johnson, Charge d’Affaires, The Hague Netherlands to Secretary of State, October 16, 1929, file 856d.6363/596, RG 59.
377. This stands in stark contrast to the operating assumption of liberal-based exchange theorists such as Gowa and Mansfield. Japan invested at least 3 million Yen initially, and probably more over the course of the interwar period. None of this investment produced oil of any value. See ONI Report, “Japanese Oil Situation-Calendar Year 1929,” August 1931, File e-10-d, Register 13177E. RG 38.
Anglo-American-Dutch cooperation did not occur seamlessly, however, as the Dutch government’s desire to be reclassified as a “reciprocating” country under the U.S. Public Land Leasing Act of 1920 remained unsettled. The Dutch demanded the removal of the non-reciprocating country label as part of the Koloniale concession arrangement and Secretary of State Kellogg withheld it because of his concern that only concessions to New Jersey Standard’s Koloniale would result. The Dutch raised numerous inquiries about the reclassification because of the mixed ownership structures of their oil companies with the British, who remained classified as a non-reciprocating country. It is still not clear if the U.S. was negotiating Dutch classification as a way of dividing the Anglo-Dutch interests and further pressuring Britain to treat the U.S. as a fully equal partner globally.378

Kellogg reclassified the Netherlands as a reciprocating country after the December 1928 concession to Koloniale, but in 1929 President Hoover withdrew all U.S. public lands from oil prospecting and production. This angered the Dutch government but the corporate alliance between New Jersey Standard and Royal Dutch Shell was functioning smoothly.379 In fact, the corporate alliance was functioning too smoothly. Allegations surfaced in April 1929 that Royal Dutch Shell and Standard of New Jersey had a private agreement that only Koloniale would receive future American concessions in the DEI, particularly in the previously contested Atjeh region. The cartel’s discrimination and implicit Dutch government acquiescence was alleged by Francis Loomis of Standard Oil of California, which had sunk $75,000 in exploration costs in

Atjeh and resented the cartel’s forward looking collusive actions. Subsequent to this revelation, the U.S. government doubted the accuracy of Loomis’ Atjeh allegation, but expressed its affirmative desire to both Standard of New Jersey and the Dutch government that more than one American company should acquire future DEI concessions.³⁸⁰

Despite Japan’s direct investment foothold in the DEI, it did not gain control of any substantial DEI oil producing lands prior to WWII. In fact, the tacit cooperation between the U.S., British and Dutch authorities in limiting and controlling Japan’s access in 1928 would grow more explicit and mutually reinforcing as would their naval cooperation.³⁸¹ Because the U.S. knowingly participated in Japan’s deceptive induction into the DEI and its subsequent waste of investment capital there, this is another example of offensive realist economic statecraft wherein economic “cooperation” is really motivated by a desire to dissipate and control a rival’s capabilities.³⁸² The exercising of this U.S. bias in the DEI did not mean, however, that bilateral U.S.-Japanese economic

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³⁸⁰ William R. Castle stated, “we can not consider as fully reciprocal permission for only one American company to get concessions. The Standard of California, for example, has spent about seventy thousand dollars in surveys in the DEI and are very anxious for a concession. The result of their application will be a test of the good faith of the Dutch government. Furthermore, if the Standard of New Jersey, after the Department had for years struggled to get them a concession, entered into any such arrangement as is being suggested, they were not playing the game squarely with the Department.” Memorandum William R. Castle, Assistant Secretary of State to Secretary of State, June 29, 1929, file 856d.6363/584, RG 59. See also correspondence between Tobin, Minister at The Hague, and the Secretary of State regarding Standard Oil of California’s Atjeh interests in Foreign Relations, 1929, Vol. III, pp.540-46.

³⁸¹ The 3rd ranking Dutch naval officer in the DEI, Captain H.M. Manikus, propositioned the U.S. regarding a naval base in the DEI due to the importance of DEI oil in any future conflict with Japan. He received a warm reception by the author of this naval intelligence report, R.R.M. Emmet Commander USN, Naval Attache, The Hague Netherlands, who forwarded said offer and his agreement with its analysis to Captain A.W. Johnson, Director of Naval Intelligence. See Office of Naval Intelligence, Reports, May 27, 1929, ONI Report Serial #50, File #103-100, File c-10-d, Register 18992C, RG 38.

³⁸² The U.S. could have insisted that Japan be included in a meaningful way in DEI oil development, providing an increased sense of security to the Japanese navy and a basis for liberal cooperative arrangements that improved political relations (i.e., a liberal policy of joint resource development). Despite understanding Japan’s intense concern for oil resources, the U.S. never considered this, and therefore liberalism is contra-indicated in this example as is defensive realism’s emphasis on not contributing to a rival’s compromised autonomy.
exchange in the oil sector was similarly limited. In fact, it expanded greatly, including U.S. assistance in building new Japanese refineries that would cut into U.S. exports of refined gasoline and other products. This exchange was, however, carefully monitored. It was also a later contention of Commerce department officials that Japan's use of American refining technology would cause economic inefficiency if the California crude oil it was designed around were substituted for due to a U.S. export embargo. Increased economic inefficiency then would be the result of importing American refining technology based on California crude. This is a facet of the technology trade that is not well appreciated and may explain U.S. willingness to supply Japan with this technology during the 1920s, which seemingly assisted Japan's drive for energy autonomy (i.e., seemingly liberal trade with small offensive realist underpinnings).

The U.S. increased its economic exchange in oil with Japan after beginning the joint management of all non-Russian sources of possible supply to Japan. The U.S. did so in order to continue to portray itself as a principled and non-discriminatory trading partner to Japan, lest Japan secure sources of supply on its own or under some new

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383. See, for example, letter from E.T. Anderson, Assistant District Manager, Chicago, U.S. D.O.C., B.F.D.C. to Minerals Division, Petroleum Section, U.S. D.O.C., B.F.D.C., January 8, 1929, Box 1411, Folder: Oils, Mineral-Japan 1926-1940, RG 151. In this letter, Anderson relays information of Japanese syndicate contract negotiations with Universal Oil Products Co. for sale of refining processes. The Japanese had impressed upon Universal Oil officials the need for secrecy in their negotiations, which was somewhat reluctantly violated by Universal with U.S. government assurances of strict confidentiality. Universal had already transferred licenses for its Dubbs Cracking refining process to Japan, which was monitored by U.S. Commerce department officials in Tokyo and U.S. intelligence services. The Dubbs technology was implemented at the newly built Tsurumi refinery near Yokohama in July 1924, and the crude oil imported for the refinery was done largely under a contract between the Mitsui company and the Associated Oil Co. of California. See Fox, “World Trade in Gasoline,” p.59.

384. The introduction of marginal inefficiencies into an opponent's economy if it trades with any other is a principal reason a rival would trade with another, and this economic effect is at least as important as the purported efficiency gains from trade. James W. Young, Director of D.O.C., B.F.D.C., noted “the Japanese refining industry is built to operate largely on California petroleum, and use of crudes from other sources would probably result in decreased efficiency.” See letter from James W. Young to Harry Hopkins, Secretary to the President, March 14, 1940, Box 1411, Folder: Oils, Mineral-Japan 1926-1940, RG 151.
understanding with the British or Dutch. State Department Economic Adviser Arthur Young best captured this when U.S. navy and Hearst paper objections to California fuel oil sales to Japan surfaced again in 1928. Young noted: “The Japanese navy can buy in the United States all the oil it wishes. We have no export restrictions...Reports that the Navy Department (U.S.) would cancel leases were used in the Dutch Parliament against the Government which was trying to put through the Standard Oil concession.”

This statement clarified overall U.S. policy at the time which sought to develop as much trade with Japan as possible, particularly in items where Japan was also dependent on British-influenced sources. This was the unstated U.S. policy born of competition with Britain, and motivated by the U.S. preference to hold Japan’s oil supply dependency instead of continuing to yield Britain that leverage and influence position. The U.S. was not willing to be seen as an impediment to Japanese energy supplies precisely because Britain still possessed the power to secure for Japan oil concessions in British North Borneo as it had done in 1920 or through its influence in the DEI. More broadly, the U.S. was seeking to supplement its leverage with Japan in silk and cotton trade with the more substantial influence oil relations could bring. During the middle 1920s the U.S. was growing more anxious about Japanese efforts at energy autonomy, and hence power projection, and preferred to forestall Japanese self-sufficiency efforts with cheap imports.

from the U.S.. Export prices of U.S. petroleum products were collapsing throughout the
mid-1920s as overproduction was the norm and exportation expected to relieve part of
the domestic pricing pressure. This domestic condition fit well with U.S. strategy of
becoming a dominant supplier to Japan and making import prices cheaper than other
alternatives to Japan (e.g., broadened ties with Anglo-Dutch or Russian interests,
 petroleum monopoly laws, extensive domestic refineries, synthetics).

The U.S. carefully monitored Japan's efforts and internal debates on oil
autonomy, including its possible turn to petroleum monopoly laws and coal
hydrogenation.386 Japan's internal debate in early 1927 revealed a clear desire to gain
energy autonomy, promoting where possible Japanese naval leaders on par with Lord
Churchill, who the Japanese believed secured the British navy's dominant oil resource
position through the Anglo-Persian Co. and other activities. Interestingly, Japan's
military leaders were skeptical of relying on private Japanese firms for this task,
particularly in oil transport, refining and even shipbuilding. Navy Minister Takarabe
noted that in the past Japanese oil men could have engaged in the business of supplying
the navy with oil, but chose to sell illuminating oil products instead due to the higher
profits to be had. Takarabe also said navy shipbuilding had suffered for similar reasons

386. Japan had first proposed a petroleum monopoly law effectively nationalizing the foreign oil businesses
in Japan and compelling importation to a government monopoly purchaser as early as 1920, and again in
1922. In June 1928, the Japanese Vice Minister of Foreign Affairs verbally assured the U.S. embassy's
Counselor that it was not contemplating a petroleum monopoly. See ONI reports on Japanese Oil at File E-
10-d. Registers 13177C and 13177E, RG 38. These reports also cover Japan's oil shale project in Fushun,
Manchuria and production capabilities in N. Sakhalin. Charles Mac Veagh, U.S. Ambassador to Japan,
noted that Japan's synthetic fuels efforts in Manchuria were leading to its desire to purchase more advanced
distillation refinery technologies from either the U.S. or Germany (i.e., more advanced than current "scotch
process" then used at Fushun). See letter summarizing 1927 Diet Hearings from Charles Mac Veagh to
Secretary of State, March 3, 1927, File 894.6363/27, RG 59.
in the past, and therefore, “to rely entirely on civilians for fuel and such articles which are so closely connected with our national defense had better not be done just yet.”

Takarabe wanted the North Sakhalin Oil Company, founded in the January 1925 agreement with Russia and administered as a private company, to be kept on a tight leash and overseen by the navy. He felt that production in N. Sakhalin was not as high as it could be because of this private management there, but conceded that the requirement that the workforce had to be 75% Russian did not help either. Other members noted that Russian negotiations for more exploration rights were bogging down and the threat of Russia granting American oil concessions in N. Sakhalin was palpable. This competition and insecurity stimulated Japan’s research into energy autonomy through coal and shale hydrogenation. Minister of War Ugaki concurred with Takarabe that the shale oil experiments at Fushun, Manchuria were critical as was the synthetic fuels effort at the navy refinery at Tokuyama. Both men were optimistic about the possibility of solving Japan’s dependency through these efforts and more N. Sakhalin oil. Naito criticized both for being overly optimistic and presciently held, “the time may come when foreign countries will be forced to limit the oil they export to other countries in time of peace and thus put an end to the system of mutual exchange.”

This would not occur for some time, as the U.S. desire to supply Japan is evident in the petroleum trade statistics for Japan after 1922, which demonstrate greater Japanese reliance on the U.S. and the peak supply position of the DEI in 1922 declining as a result of U.S. selling pressure (See Tables 4.2 and 4.3). The 1923 DEI export of 117,881,329

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388. See statement of Mr. Uehara, possibly the former general and army minister in 1912 Yusaku Uehara, in ibid.
gallons represented 34% of total DEI exports of crude and fuel oil. U.S. crude supplies to Japan increased dramatically after resuming in December 1922 due to lower prices and the general price war that was occurring between Royal Dutch and Standard Oil interests, but still were not a large percentage of total U.S. exports. North Sakhalin production also accelerated after 1926 as Japanese efforts there were stepped up. Other nations supplied Japan, but generally in far lesser amounts and could not be estimated across the entire time period. Prices of refined and crude petroleum were plummeting by 1928 in Tokyo as Standard Oil of New York and Royal Dutch battled in the Japanese market up to the Achnacarry accords in August 1928. Concomitant with that agreement, a six way price cartel including Standard, Royal Dutch, Nippon Oil, Ogura, Mitsubishi and Mitsui was formed, but it broke down after one month.

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390. As noted previously, supplies to Japan transshipped through Hong Kong or Singapore are possible, which would make overall DEI exports to Japan higher. There is, however, little accounting for this in the intelligence statistics and none in official publications.

391. The other supplying states include: British Borneo, Mexico and Persia. However, data for them is sketchy at best and excluded because they are small in comparison to supplies from the DEI and U.S.. For example, Mexican oil contracted for with British-controlled Royal Dutch and Anglo-Persian companies in 1921 called for a total of 28 million gallons to be delivered to Japan. It was recorded for 10 months ending in November 1921 that only about 4 million gallons went, so the balance of 24 million Mexican crude gallons was shipped to Japan beginning in 1922. No figures for Mexican exports to Japan appear in 1925 or 1926, so the contract must have concluded prior to 1925. See U.S. D.O.C., B.F.D.C., International Trade in Petroleum and its Products, (Washington, DC: G.P.O., 1929), pp.8-10. From ONI figures, crude and fuel oil to Japan from British North Borneo is also indicated at 9,138,000 gallons in 1927, not small but not overly large. See “The Petroleum Situation with Special Reference to the Far East,” p.32: U.S. Naval Attache Report, “Navy Oil Contract 1917-1920 with Shell Oil Co.,” dated May 6, 1921, File e-10-d, Register 13177, RG 38; ONI Report June 1929, p.1.

392. Samuels, The Business of the Japanese State, p.174. This cartel was resurrected again in 1931, and both prices and quantities marketed in Japan were cartelized. See FTC Report, p.342.
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<th>1923</th>
<th>1924</th>
<th>1925</th>
<th>1926</th>
<th>1927</th>
<th>1928</th>
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<tbody>
<tr>
<td>From DEI to Japan</td>
<td>117.881 (34%)</td>
<td>N/A</td>
<td>75.556 (20.3%)</td>
<td>71.643 (21%)</td>
<td>64.362 (15.3%)</td>
<td>79.470 (15.5%)</td>
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<td>in million of gallons</td>
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<tr>
<td>From U.S. to Japan</td>
<td>93.483 (4.8%)</td>
<td>180.889 (8.2%)</td>
<td>101.672 (N/A)</td>
<td>189.540 (N/A)</td>
<td>253.272 (N/A)</td>
<td>321.832 (12.7%)</td>
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<td>in million of gallons</td>
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<tr>
<td>Minimum known from</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>12.045</td>
<td>20.412</td>
<td>36.748</td>
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<td>other countries in</td>
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<td>(i.e., N. Sakhalin)</td>
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Table 4.2: Crude and Fuel Oil Exports to Japan, 1923-1928.\(^b\)

\(^a\) U.S. exports include the category of fuel and gas oil, not just fuel oil and are therefore somewhat larger than comparable statistics from the DEI. For example, in 1924 the U.S. sent only 35,154.000 gallons of crude to Japan and 145.735.000 gallons of fuel and gas oil. The fuel and gas oil represented 10% of total U.S. exports of fuel and gas oil, while the crude exports to Japan were only 5% of total U.S. crude exports, not significant dependencies on the Japanese market. U.S. dependency on Japan's market would increase over the next few years.

Table 4.3: Gasoline Exports to Japan, 1923-1928

<table>
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<tr>
<th>Year</th>
<th>1923</th>
<th>1924</th>
<th>1925</th>
<th>1926</th>
<th>1927</th>
<th>1928</th>
</tr>
</thead>
<tbody>
<tr>
<td>From DEI in millions of gallons (as % of total DEI gas exports)</td>
<td>8.476 (5.1%)</td>
<td>N/A</td>
<td>N/A</td>
<td>22.849 (N/A)</td>
<td>17.802 (N/A)</td>
<td>34.219 (11.5%)</td>
</tr>
<tr>
<td>From U.S. in millions of gallons (as % of total U.S. gas exports)</td>
<td>8.634 (1%)</td>
<td>10.39</td>
<td>9.855</td>
<td>24.494</td>
<td>24.233</td>
<td>30.984 (1.4%)</td>
</tr>
</tbody>
</table>

*Amounts imported from third countries are reported as slim, and most would represent transshipped DEI gasoline as noted for the earlier period. These data differ markedly from the official Japanese sources. For example, in 1926 Japan reported total gasoline imports of 29,192,000 gallons, with only 143,000 gallons from countries other than the U.S. and DEI. See U.S. D.O.C., B.F.D.C., International Trade in Petroleum and its Products, p.138. Used sources include: Statistiek van Den Handel en de in-en Uitvoerechten in Nederlandsch-Indie over het Jaar, 1923; Coumbe, "Petroleum Products Dutch East Indies:" report in Engineering and Mining Journal Press, Vol. 120, No. 10, September 5, 1925, pp.371-374; Naval Intelligence Reports, "Japanese Oil Situation-Calendar Years 1927-1928." File e-10-d, Register 13177E, RG 38.

4.5 The China Dimension

The cooperative economic arrangements among Anglo-American-Dutch government and business leaders developed simultaneously with decaying cooperation with Japan on China and Manchuria, and increasing Japanese unilateral action there. From 1927 forward, increased coordination of Anglo-American-Dutch diplomacy in the DEI grew in direct response to Japan’s economic and military expansionism in Manchuria and Northern China, and its unwillingness to allow a sovereign China or independent Manchuria to emerge. More poignantly, U.S. hostility to Japan would grow in response to perceived Japanese transgressions in China as would American
consternation with Britain when it did not react to Japanese actions as the U.S. desired.\textsuperscript{393} One early indicator of this dynamic was the postponement of Chinese economic sovereignty. The Washington Conference agreements with Japan stipulated that China would acquire economic sovereignty in the form of tariff autonomy from foreign powers (i.e., the authority to set customs rates on traded goods). Negotiations for Chinese tariff autonomy began in October 1925, but were suspended in January 1926, after civil strife in North China disrupted the ability of the negotiating powers and China to agree on uniform rates. Instead, the parties chose to defer tariff autonomy for China until January 1929, and agreed only on interim rates for the next three years.

As tariff autonomy for China neared, the Japanese increasingly opposed the growing independent authority in Nanking under Chiang Kai-shek, particularly after Nanking abrogated the existing Sino-Japanese Treaty of 1896. Japan opposed negotiating one tariff schedule for China and the multilateral management of Chinese loans that would be repaid through tariff revenues (i.e., subsuming its bilateral financial leverage to a version of the loan consortium and its excuse to punish China). When the Chinese Nationalist government under Chiang was established with the promulgation of the New Organic Law of the National Government of the Republic of China on October 3, 1928, Japan remained recalcitrant in accepting a unified and sovereign China, and did

\textsuperscript{393} British elite opinion was divided on the benefits of cooperation with the U.S. and not Japan in China, as prior joint exploitation with Japan under the Anglo-Japanese alliance had yielded stable benefits and a more or less pliant Chinese population fit for business expansion. Because of division in British opinion and the perception of naive and moralistic U.S. policy toward China, joint Anglo-American actions in China were not as forthcoming as the U.S. wanted. This changed in the middle of 1928. See Chihiro Hosoya, “Britain and the U.S. in Japan’s View, 1919-1937,” in Ian Nish, ed., Anglo-Japanese Alienation, 1919-1952, (London: Cambridge University Press, 1982), pp. 10-14; Ian Nish, Alliance in Decline: A Study in Anglo-Japanese Relations, 1908-1923, (London, 1972), p.390.
not recognize this government until June 3, 1929. Prior to recognition, Japan held out as the only foreign nation not to reach a damages settlement with China for the Nanking uprisings of March 1927. Japan also refused settlement over its military’s clashes with Chiang in Tsinan in early May 1928. Japan was reluctant to make any concessions to bring about accord with Chiang, and because of this reticence, in late 1928, American military intelligence concluded, “the Sino-Japanese deadlock and the operation of the new tariff schedule are interdependent.” This position inspired the Nanking government to press harder for tariff autonomy and with Anglo-American assistance yielded its eventual adoption in March 1930.

Japanese preference for deferred sovereignty for China and separate arrangements on Manchuria was a position made tenable by the divided and contested political authority situation in China. Chiang Kai-shek was attempting to unify China and was pushing northward in his effort to expand his authority while minimizing that of Soviet Russia and Japan. His efforts were hampered by Soviet-sponsored communist resistance in China, uncontrolled nationalist forces and competing warlords in the South and North, most notably Chang Tso-lin. When southern nationalist forces rampaged in Nanking in March 1927, killing Japanese, American and British citizens, Japan’s opposition political party, the Seiyukai, led by General Baron Tanaka Giichi vehemently criticized the governing Minseito party led by Premier Wakatsuki Reijiro and Foreign Minister

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394 See Military Intelligence Division Summary, “Far East, China,” December 21, 1928, File c-9-b, Register #18542-A, RG 38
This criticism centered on allegations of weakness in Japan's foreign policy toward China and came at a time of financial panic in Japan, which experienced runs on several banks and public bailouts of semi-governmental banks, most notably the Bank of Taiwan. Tanaka's harsh criticism of Shidehara and Wakatsuki's China policy did not cause their government to collapse, but because Tanaka made a strong China policy his leitmotif for the Premiership, upon assuming that office on April 17, 1927, he set out to execute his "positive policy" there.

Premier Tanaka's first act was to dispatch Japanese forces to Shantung with the declared purpose of protecting Japanese lives and property, "but with the transparent objective of preventing the army of Chiang Kai-shek from advancing into Manchuria. The Imperial army preferred the certain impotence of a warlord (Chang Tso-lin) in Manchuria to a potentially more independent authority stemming from Nanking." The Japanese position in Shantung and the condemnation of the Western powers for the Nanking rampages quelled Chinese nationalist forces for a time and Japan sought to place its actions in China and Manchuria under a more comprehensive and clear policy. Tanaka convened the Far Eastern Conference in June 1927 to resolve Japan's policy in

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396. Iriye, *After Imperialism*, pp.142-3. Tanaka was War Minister in Hara's cabinet, and supported the Siberian expedition of Japan in 1918 as Vice Chief of the Army General Staff. He was therefore well experienced balancing Russian and Anglo-American pressures as Japan pursued its Asian strategy. In 1918, for example, he tried to establish separatist regimes in Manchuria and Mongolia as Japanese army forces occupied the territory. See Marius B. Jansen, "Introduction: Manchurian Incident," in James W. Morley, ed., *Japan Erupts: Japan's Road to the Pacific War*, (New York: Columbia University Press, 1984), p.125.

397. Industrial and Banking sector rationalization occurred during and after the financial crisis of Spring 1927, with the number of ordinary banks dropping from 1,359 to 1,030. The crisis was preceded by a rising Yen that hampered raw silk exports in 1926 due to Yen speculation that followed large gold exports in Autumn 1925. See G.C. Allen, *A Short Economic History of Modern Japan*, (London: MacMillan Press, 1981), pp.105-6.


399. Japanese presence in Shantung was given high marks at the time by U.S. officials for their discretion in using force.
China and Manchuria and to justify greater Japanese military force in this area. The purpose of Japan’s positive policy was to vigorously promote and defend Japan’s economic interests in China and Manchuria, instead of reacting to Chinese nationalist uprisings and/or placating American Open Door principles. U.S. State department assessments of Tanaka’s policy noted the “vigorous efforts” made through diplomatic and public affairs outlets to shape world opinion to the view that Japan’s actions in Manchuria greatly benefitted the Chinese there and that Japan deserved a “most favored nation” position in Manchuria. In a memorandum prepared by Leo Sturgeon, the State department concluded that Japan would not likely internationalize the development of Manchuria as the U.S. had proposed for the South Manchuria Railway in 1909. Instead, Japan’s position was that “no material advantages already secured (in Manchuria) will be relinquished without a corresponding gain in another direction.”

This position leaves open the question of whether neutralization of Japan’s privileged position through international management in Manchuria could have been achieved if Japan were brought in more equally into the DEI. Japan’s political elites fully understood the dilemma of balancing a moderate policy on China and Manchuria that did not violate Anglo-American preferences against a more unilateral policy there that would likely result in strained and less cooperative relations, with the U.S. in

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400. U.S. State department memorandum, Leo D. Sturgeon, U.S. Consul at Dairen, in 1927, “Economic and Political Developments in Japan,” June 1928, in Hombeck Papers, Box 520, Folder: Miscellany 1920-1928, pp.8-9. This report noted Japan’s desire to annex Manchuria, but before acting it would have to carefully deliberate on many factors, including above all others the Russian response to annexation. Sturgeon noted, “For the future, there seems little question that Japan would welcome the opportunity to annex Manchuria, both economically and politically.” Ibid., p.11.

particular. For their part, American political and military elites understood the centrality of Chinese resources to Japan’s great power aspirations, and the interrelation between Chinese and DEI resources in the economic and military planning of Japan. U.S. officials simply believed that Japan’s commercial ties to the West in general and the U.S. in particular would lead to tempered behavior on its part in China and Asia. This assessment is particularly striking because Stanley Hornbeck advanced it quite effectively.

Hornbeck affirmed the possibility of trading material advantages and used the Sturgeon memorandum in his lengthy presentation to the Naval War College on July 13, 1928. However, in this document Hornbeck did not mention this accurate intelligence on Japan’s intention to annex Manchuria. Instead, he wrote that Japan would likely advance its interests in Manchuria, but Tanaka has “stopped short of what was expected of it (his positive policy) in some quarters. This is doubtless due in part to the state of Japanese public opinion...and in part to pressure of commercial interests.” Hornbeck elaborated that the opposition Minseito party checked possible expansion as did China’s importance in Japan’s export trade in textiles which served “powerful economic groups” in Japan.

402. See Crowley, Japan’s Quest for Autonomy, pp.32-3; Connors, The Emperor’s Adviser, pp.113-115.
403. See Naval Intelligence report, “Japan’s Foreign Policies,” August 29, 1927, File c-9-b, Register 18583, RG 38. This report contains a translated study entitled, “The Strategical Situation in the Pacific,” by Japanese navy officer, Captain M. Hibino, deemed one of the most able Japanese officers and reflecting prevailing naval opinion there. Hibino held, “When we survey the distribution of the world’s resources today, Indian cotton, East Indian oil, Chinese iron and Manchurian grains—all answer our demands...I consider it absolutely necessary for us to safeguard our lines of communication and transportation east of India, and north of the Dutch Indies, as the minimum requirement for preservation of the existence of our nation.” This report garnered attention at both the U.S. embassy in Japan, the Director of Naval Intelligence’s office and the Navy General Board’s planning division.
404. Official U.S. analysis held the large loans between American banks and Japanese industry, particularly in utility development, to be beneficial and binding “influential Americans and Japanese by the ties of common interest. Upon the whole, the recent extensive investment of American money in Japan has had a favorable effect upon the attitude of Japanese business elements toward the United States.” Hornbeck, “The Far East,” p.17.
who would contain possibly aggressive statesmen. He concluded, “For the present, Japan could not risk a war, even with so weak a power as China, without thinking of the burden that would be placed on her already limited financial resources.” 405 This would be Hornbeck’s last homage to liberal-based analysis emphasizing how financial constraints cause peace.

In the same month of Tanaka’s Far Eastern Conference, Japan dutifully attended the Geneva conference on naval arms limitation. After the failed talks, the U.S. Congress passed a U.S. Naval Board proposal to build a fleet of 23 heavy cruisers in response to Britain’s unwillingness to compromise on new governing quotas. This threat of a renewed naval arms race prompted Britain to revive discussions with the U.S., which eventually culminated in the London Naval Conference of 1930. In the interim, Chiang Kai-shek pushed northward in China prompting clashes with Japanese troops, most notably in and around Tsinan on May 3-9, 1928. The Japanese military reaction appeared excessive to U.S. observers and violated Japan’s pledge to respect the return of Shantung province to Chinese authority. 406

Chiang Kai-shek continued to press his forces northward and began an unintended collaboration amidst his conflict with Chang Tso-lin to deny the Japanese their desired building of new railroad lines in Manchuria. 407 Chang hoped that Japanese-Chinese Nationalist conflict would allow him to rule longer in Peking by restraining Chiang’s

406. Japan had held onto occupied German mines and property acquired in 1915, despite formally restoring sovereignty of Shantung to China after the Washington Conference. Japan used excessive force in Tsinan on May 9th in particular with a general bombardment of the city. For excessive force see also Jansen, “Introduction: Manchurian Incident,” p.129. Japanese forces remained in and around Tsinan until January 1929.
northern advance. However, Chang’s tacit alignment with Chiang Kai-shek to frustrate Japanese plans in Manchuria coupled with the threat of Nationalist troop movements into Manchuria prompted Japanese authorities to take a harder line in northern China. Japan was intent on providing a buffer between a unified China under Chiang’s Nationalists and a pliant Manchuria under Chang.

Tanaka ordered troops into Mukden, Manchuria on May 18, 1928. Initially, they were to disarm a retreating Chang’s forces near the border of Manchuria and China at Shanhaikuan, but finally had orders only to provide safe passage for Chang’s army to Manchuria. Many Japanese officers were not pleased with this policy as it left an armed and uncooperative Chang Tso-lin in charge in Manchuria, instead of the Japanese army. This action did not pacify Chang nor the emerging leaders of the Japanese army in Manchuria, the Kwantung army. Colonel Komoto Daisaku, Senior Staff Officer of the Kwantung army, ended Tanaka’s balancing act by taking the more final action of assassinating Chang on June 4, 1928, blowing up his train car en route from Peking.408

4.6 Fallout after Chang Tso-lin Assassination

Tanaka was commanded by the Emperor to investigate and punish the perpetrators of this act, but was frustrated in so doing by the new generation of non-Choshu army leaders in Manchuria, the army’s General Staff in Tokyo and uncooperative

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408. Komoto was a leading member of the army officer society, Issekikai “Evening Society,” who were strongly committed to separating Manchuria from any Chinese sovereignty claims by establishing a puppet state there under Japanese military control, regardless of Western preferences or likely Russian conflict. Issekikai was the fused officer society encompassing graduates of the Military Academy from the 16th through 25th classes. Other members of Issekikai included Tojo Hideki, Ishiwara Kanji and Itagaki Seishiro who figure prominently in the future direction of Japanese foreign policy. See Seki Hiroharu, “The Manchurian Incident, 1931” in Morley, ed., Japan Erupts, pp.146-8.

205
Seiyukai party officials.\textsuperscript{409} This command came after Prince Saionji, leading elder statesman of Japan and backer of Shidehara, pressured Tanaka into explaining to the Emperor what had happened. Saionji saw the resolution of this flagrant act as an opportunity to “purge the Kwantung army of its anti-Shidehara, anti-Genro factions, thereby also refurbishing Japan’s tarnished image in the West and improving her relations with China.”\textsuperscript{410} Instead, Tanaka bowed to army and Seiyukai pressure and suppressed the findings of the Imperially-ordered army report. Komoto was only reassigned to the Chientao region of Manchuria, and the Minseito party took full advantage of Tanaka’s weakness to criticize his China policy vociferously for domestic advantage, with Saionji leading the charge to replace Tanaka.\textsuperscript{411} Chang Tso-lin’s son, Chang Hsueh-liang, succeeded him in Manchuria and not surprisingly was even less interested in cooperating with Tokyo than his father. Chang Hsueh-liang developed closer ties with the Nationalists under Chiang and worked more explicitly to frustrate Japan’s designs in Manchuria, tying Manchuria’s fate more closely to the Nationalists newly won independence and unity for China.\textsuperscript{412}

\textsuperscript{409} Iriye, After Imperialism, pp.245-6. The Seiyukai general-Premier being undermined in his efforts by the army’s General Staff and Kwantung officers underscores the weakening of civilian authority in Japan. Japan’s foray into full participatory democracy began with universal male suffrage in 1925, and bore full fruit in the first elections conducted with maximum participation on February 20, 1928 and again in Fall 1928.

\textsuperscript{410} Connors, The Emperor’s Adviser, p. 114.

\textsuperscript{411} Jansen, “Introduction: Manchurian Incident,” p.135.

\textsuperscript{412} Chang Hsueh-liang formally unified Manchuria with China on December 29, 1928, accepting symbolic sovereignty of Nanking over Manchuria and using this to frustrate Japanese plans for Manchuria by referring their diplomatic overtures to Nanking. Iriye, After Imperialism, pp. 244-5. See also article on Chang Hsueh-liang by Edgar Snow, “Son of the Grand Marshal,” New York Herald Tribune, December 15, 1929. Snow notes Chang’s affirmation that Japan was the sworn enemy of his father and that Chinese immigrants into Manchuria were part of his policy to displace Japanese influence and align Manchuria with Nanking. Chang stated, “Japan’s position in Manchuria is a menace to China...we are developing a system now to break down Japan’s stranglehold on commerce.” This system centered on separate and competing Chinese railroads to Hulatao in direct competition with the Japanese controlled port of Dairen. This action violated Sino-Japanese treaties regarding the exclusive rights of the South Manchurian Railway Co., and were the centerpiece of conflict through 1931.
These actions in northern China demonstrated time and again that dominant forces in Japan were prepared to use violent means to secure Japanese interests there, which increasingly meant forestalling the rising power of Chinese nationalists and relegating Manchuria to a pliable satellite. Tanaka was not successful in pulling Chang Hsueh-liang into Japan's orbit instead of Chiang's Nationalists, and because of this he did not oppose the symbolic political union of Manchuria and China at the end of 1928. Tanaka realized the tenuous position of Japan's unilateral efforts in China, the possible Chinese backlash against Japanese trade and Anglo-American opposition to these recent actions yielding more overt support for Chiang Kai-shek. Tanaka tried to gain Anglo-American support for Japan's position in China and Manchuria and began the reorientation toward these powers' preferences in the aftermath of Chang Tso-lin's assassination. He was, however, rebuffed in his efforts by both Britain and the U.S.. Secretary of State Kellogg contended Chiang's government "appeared to be making every effort to build a stable and ordered government in China," and affirmed the principle that Manchuria was a part of China.\textsuperscript{413} American economic activity in China accelerated after Chang's assassination, particularly with large U.S. loans to and investments in China's power, communications and airline industries.\textsuperscript{414}

America's position on China and Manchuria was based on adherence to the Nine Power Treaty (1922) and to the principle of non-interference in China's effort to become a unitary state with effective central administration. To this end, the U.S. signed a customs agreement with the Nationalist government on July 25, 1928 that recognized the

\textsuperscript{413} Secretary of State Kellogg, quoted in, Iriye, After Imperialism, p.243.

\textsuperscript{414} Ibid., p.231. The U.S. government also sent many technical and economic advisers to China beginning in early 1929. By September 1929 of the approximately 60 foreign advisers to Nanking 32 were American and 15 British, with only 2 Japanese. Ibid., p.329, footnote 9.
sovereignty of that government and the goal of tariff autonomy for China.\textsuperscript{415} These actions and greatly increasing Sino-American economic ties were perceived by Japan as part of a larger strategic rapprochement which raised the stakes for Japan’s subsequent decisions on China.\textsuperscript{416} This was not an inaccurate assessment, as the U.S. pushed for an end to the China arms embargo agreement among the Washington Conference powers and in particular for the export of dual-use aircraft to China beginning in early 1929.\textsuperscript{417} The U.S. efforts to sell weapons to China were in direct competition with increasing British efforts to do the same in both naval and aircraft areas. By late 1929, Anglo-American competition in arms exports to China was increasing friction between them and causing fear in Japan that China’s capabilities would be dramatically increased with this now unrestricted arms sales competition.

Consideration for these consequences of Japanese unilateral action in China led Tanaka to conclude the arrangements settling the Nanking incident and formally recognize the Nanking government on June 3, 1929. Iriye noted, “Japan was pursuing its objectives unilaterally in Manchuria, and its desire for cooperation with Britain and the United States was merely an expression of its fear of isolation. Nevertheless, it is


\textsuperscript{416} The seriousness of U.S. economic assistance was evident in the assignment of Arthur N. Young, former Economic Adviser at the State department, to be the chief economic adviser to the Nationalist government in 1929, a position he held through WWII. This high level assignment clearly indicated the U.S. position of building China as a bulwark in Asia against both Soviet Russia and more importantly a southern encroaching Japan.

\textsuperscript{417} In 1919, the major foreign powers agreed on an informal China Arms Embargo and in March 1922, President Harding proclaimed U.S. policy not to export weapons to China. These non-codified restrictions were dismantled in early 1929 by some officers in the State department, led by Hombeck. They acted under the pretense that aircraft exports to China were desirable even if used for military purposes by the Nationalists because if the U.S. did not supply them someone else would (i.e., Britain). See Guangqiu Xu, “The Eagle and the Dragon’s War Wings: the United States and Chinese Military Aviation, 1929-1940,” (Ph.D. diss., University of Maryland, 1993), pp.30, 45-57.
significant that for the first time after mid-1925 Japan was acutely feeling the need for understanding with the West. This reorientation took place under Tanaka, not Shidehara. Unfortunately for Tanaka, his overtures to the U.S. were not reciprocated and his authority at home was undermined by the army General Staff, Seiyukai officials, and most importantly, Minseito party officials who opportunistically criticized Tanaka’s “positive” policy as being too weak. The domestic polarization in Japan centered on Tanaka, and his chief critic former Premier and Minister of Finance Wakatsuki. Wakatsuki charged Tanaka with financial mismanagement that threatened needed naval building programs, thereby fueling a domestic polarization that linked state finance and the status of Japan’s naval forces. This linkage would come back to haunt Wakatsuki after the London Naval Conference. Because of Tanaka’s failings, Imperial displeasure with his handling of Chang’s assassination, and the contradictory pressures coming from emerging army officers, the General Staff, opposition party leaders, and Western powers, Tanaka resigned on July 1, 1929.

4.7 U.S.-Japan Economic Exchange, 1923-1928

Due to the continued competition with Britain for influence in both China and Japan, U.S. economic relations with Japan continued their post-Washington Conference trajectory of becoming both broader and more beneficial. U.S. trade with Japan


continued to grow in the 1923-1928 period, but still remained largely concentrated in silk and cotton (See Table 4.4). However, the oil trade described above was a significant and expanding aspect of U.S.-Japanese trade and Japan's asymmetric and strategic dependency on the U.S.. As observed earlier, U.S. exports of crude and fuel oil to Japan in 1928 were 12.7% of total U.S. crude and fuel exports, but represented 73.4% of total Japanese imports of this vital commodity in 1928 (i.e., commodity and partner concentration in a vital strategic good). U.S. exports of oil refining technology also materially assisted Japan's relative capabilities in this area. Japan continued to import U.S. iron and steel products, including 379,000 tons of scrap iron and steel in 1928, representing 6.3% of the total value of Japanese imports from the U.S. On Japan's export side, its reliance on the U.S. market to absorb its silk remained high, with the U.S. taking between 98%-99% of total Japanese silk exports across the period. The dramatically increasing volume of loans and increases in U.S. foreign direct investment during this period were even more indicative of the broadening and beneficial exchange relationship in the post-Washington Conference period. The loans, however, were often extended with political conditions that sought to limit gains to only those Japanese domestic actors the U.S. preferred (i.e., not the army-dominated South Manchuria Railway Company). The restrictions on how and where some of these funds could be expended were quite intrusive and demonstrated the U.S. intent to constrain Japanese autonomy through capital extensions.

420 The U.S. supply of machinery and machine parts was still less than 40% of Japan's total importation of machinery from all countries, with Germany and Britain the next largest suppliers. See U.S. D.O.C., Foreign Commerce Yearbook, 1930, p.350; Uyeda, Recent Development of Japanese Trade, p.70.
421 Uyeda, Recent Development of Japanese Trade, p.30

210

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<tr>
<td>Total exports of Japan</td>
<td>1,447,751</td>
<td>1,807,035</td>
<td>2,305,590</td>
<td>2,044,728</td>
<td>1,922,317</td>
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<td>in thousands of Yen (as % of</td>
<td>(9.7%)</td>
<td>(11.6%)</td>
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<td>(12.8%)</td>
<td>(11.8%)</td>
<td>(11.9%)</td>
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<td>Japanese GDP)</td>
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<td>Japanese exports to U.S.</td>
<td>610,431</td>
<td>750,437</td>
<td>1,006,253</td>
<td>860,881</td>
<td>834,000</td>
<td>826,000</td>
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<td>in thousands of Yen (as % of</td>
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<td>(41.5%)</td>
<td>(43.6%)</td>
<td>(42.1%)</td>
<td>(43.4%)</td>
<td>(41.9%)</td>
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<tr>
<td>total Japanese exports)</td>
<td></td>
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<tr>
<td>Japanese raw silk exports to</td>
<td>442,199</td>
<td>622,223</td>
<td>849,486</td>
<td>709,379</td>
<td>698,883</td>
<td>687,464</td>
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<tr>
<td>U.S. in thousands of Yen (as</td>
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<td>(82.9%)</td>
<td>(84.4%)</td>
<td>(82.4%)</td>
<td>(83.8%)</td>
<td>(83.2%)</td>
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<tr>
<td>% of total exports to U.S.)</td>
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<tr>
<td>Japanese exports to U.S.</td>
<td>4.1%</td>
<td>4.8%</td>
<td>6.2%</td>
<td>5.4%</td>
<td>5.1%</td>
<td>5%</td>
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<tr>
<td>Total imports of Japan</td>
<td>1,982,231</td>
<td>2,453,402</td>
<td>2,572,658</td>
<td>2,377,484</td>
<td>2,179,154</td>
<td>2,196,315</td>
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<td>in thousands of Yen (as % of</td>
<td>(13.3%)</td>
<td>(15.8%)</td>
<td>(15.8%)</td>
<td>(14.9%)</td>
<td>(13.4%)</td>
<td>(13.3%)</td>
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<tr>
<td>Japanese GDP)</td>
<td></td>
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<tr>
<td>Japanese imports from U.S.</td>
<td>512,118</td>
<td>671,150</td>
<td>664,992</td>
<td>680,186</td>
<td>674,000</td>
<td>626,000</td>
</tr>
<tr>
<td>in thousands of Yen (as % of</td>
<td>(25.8%)</td>
<td>(27.4%)</td>
<td>(25.8%)</td>
<td>(28.6%)</td>
<td>(30.9%)</td>
<td>(28.5%)</td>
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<tr>
<td>total Japanese imports)</td>
<td></td>
<td></td>
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</tr>
<tr>
<td>Japanese imports from</td>
<td>177,551</td>
<td>204,918</td>
<td>360,167</td>
<td>317,428</td>
<td>343,563</td>
<td>245,926</td>
</tr>
<tr>
<td>U.S. of cotton in thousands</td>
<td>(34.7%)</td>
<td>(30.5%)</td>
<td>(30.5%)</td>
<td>(46.7%)</td>
<td>(51%)</td>
<td>(39.3%)</td>
</tr>
<tr>
<td>of Yen (as a % of total</td>
<td></td>
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<tr>
<td>imports from U.S.)</td>
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</tr>
<tr>
<td>Japanese imports from U.S.</td>
<td>3.4%</td>
<td>4.3%</td>
<td>4.1%</td>
<td>4.3%</td>
<td>4.1%</td>
<td>3.8%</td>
</tr>
<tr>
<td>as a % of Japanese GDP</td>
<td></td>
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**Table 4.4: Japanese Exports to and Imports from U.S., 1923-1928**


211

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As trade between the U.S. and Japan flourished after the Washington Conference agreements, U.S. loans to Japan helped finance increased imports from the U.S. For example, this was evident in machinery and electrical industry related products (e.g., dynamos and transformers). Nonetheless, Japan continued to rely heavily on the U.S. export market to absorb approximately 42% of total Japanese exports across the period, maintaining Japan's increased reliance visible by 1922. Japanese imports from the U.S. were never less than 25.8% of total imports and peaked in 1927 at 30.9%, continuing the downward trend from the import dependency high of 37% in 1918. The U.S. retained its dominant position in Japan's trade while only marginally increasing its exposure to the Japanese market in certain items (e.g., 10% of U.S. cotton exports went to Japan in 1924, but by 1927 Japan took 14% of U.S. cotton exports). In 1928, the peak year of U.S. export dependency on Japan, only 5.6% of total U.S. exports went to Japan; while the Japanese share in total U.S. imports was roughly constant around 9%, with a peak of 9.6% in 1927.

Despite stimulating Japanese purchases in the U.S. with loans to Japan's electric industry among other borrowers, Japan continued to record large bilateral trade surpluses with the U.S. (See Table 4.5). These bilateral trade surpluses helped make Japan's overall trade deficits throughout the period more manageable, allowing it to not have to draw down on gold reserves at home or abroad. Japan's gold reserves did not change much over the period. In 1923, Japan had 1.057 billion Yen in gold reserves and in 1928,

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422. U.S. export of dynamos and transformers increased from effectively zero in 1923 to approximately $2 million dollars in 1928, or 1.6% of U.S. exports to Japan that year. Admittedly, this is a small amount, but it was growing from a base of zero. See U.S. D.O.C., Foreign Commerce Yearbook, 1932, p.552.
it had 1.061 billion Yen in gold reserves, with only 119 million Yen held abroad.\footnote{U.S. D.O.C., Foreign Commerce Yearbook, 1928, pp.406-9.} Japan’s bilateral trade surplus with the U.S. grew to large amounts, with a record 341 million Yen favorable balance in 1925, while Japan’s overall economy relied on trade with the U.S. at high levels. Total U.S.-Japanese trade was approximately 9.2% of Japanese GDP throughout the period, with a peak value of 10.3% in 1925. In contrast, Japanese trade with the U.S. was still less than 1% of U.S. GDP throughout the period.

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</thead>
<tbody>
<tr>
<td><strong>Overall trade balance of Japan in thousands of Yen (Exports -Imports)</strong></td>
<td>-534,480</td>
<td>-646,367</td>
<td>-267,068</td>
<td>-332,756</td>
<td>-256,837</td>
<td>-224,360</td>
</tr>
<tr>
<td><strong>Bilateral trade balance of Japan with U.S. in thousands of Yen (Japanese Exports to U.S.-Japanese Imports from U.S.)</strong></td>
<td>98,313</td>
<td>79,287</td>
<td>341,261</td>
<td>180,695</td>
<td>160,000</td>
<td>200,000</td>
</tr>
<tr>
<td><strong>Total U.S.-Japan trade as % of Japanese GDP (Japanese exports to and imports from U.S. as % of its GDP)</strong></td>
<td>7.5%</td>
<td>9.1%</td>
<td>10.3%</td>
<td>9.7%</td>
<td>9.2%</td>
<td>8.8%</td>
</tr>
</tbody>
</table>

**Table 4.5: Japan’s Overall and Bilateral Trade Balance, 1923-28**

Because Japan’s reliance on the U.S. was growing both in trade and finance while the U.S. reliance on Japan was not, this period can be categorized as asymmetric in both
benefits and strategic vulnerability. This asymmetry of benefits is made more evident when U.S. loans and direct investments are considered. The value of U.S. loans to Japan from 1923 through 1928 was $430.3 million dollars, but this represented only 7.9% of total U.S. loans extended abroad over the same period.\textsuperscript{425} Although not a small U.S. vulnerability to an unlikely total Japanese default, it was still less than 10% of total U.S. loans issued and therefore not a significant potential vulnerability. During this same period, Britain made several loans to Japan totaling 462 million Yen, or approximately $208 million dollars.\textsuperscript{426} Therefore, the U.S. was the dominant lender to Japan, lending approximately 67% to Japan. Similarly, U.S. direct investment in Japan increased markedly in this period. For example, Westinghouse Electric formed a joint partnership with Mitsubishi shipping in 1923, and wholly-owned subsidiaries of Ford and General Motors were established in 1924 and 1925, respectively. Although there were American corporations in Japan prior to WWI (e.g., Singer Manufacturing Co., Standard Oil, General Electric, National City Bank), the value of American foreign direct investment in Japan grew large only after the Washington Conference treaties were arranged.

These investments are covered more thoroughly in the next chapter because comprehensive data for U.S. direct investments began to be collected by the U.S. Department of Commerce only in 1931 (See Table 5.5 in next chapter for complete end of 1931 values). Nonetheless, it is fair to conclude that Japan’s material capabilities were being relatively advantaged compared with the U.S. in their bilateral exchange due predominantly to this foreign investment in productive plant, which transferred some

\textsuperscript{425} Data from Table 4.1 and Cleo Lewis, America’s Stake in International Investments, (Washington, DC: Brookings Institution, 1938), p.630.

\textsuperscript{426} See Moulton, Japan: an Economic and Financial Appraisal, pp.488-90. British loan figures given in Yen and then converted to dollars at $.45=1 Yen, a rough average exchange rate for the 1923-1928 period.

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substantial production capabilities (e.g., auto plants). Japan was also gaining from the bilateral trade surplus and loans. Additionally, it continued to be valid in this period that U.S. imports of silk did not materially affect U.S. capabilities by creating efficiency gains through specialization or release of greater domestic resources due to trade in this luxury item. In contrast, Japan's continued importation of steel, machinery and electrical equipment assisted its capabilities to a much higher degree. For these reasons the exchange relationship during 1923-1928 can be categorized as broad and broadening by the end of the period, encompassing trade, loans and direct investments. These exchanges were more beneficial to Japan's relative capabilities and were increasing its potential to attain autonomous production capabilities. Japan was, however, becoming more dependent overall on the U.S., with increased vulnerability to U.S. oil equipment and products trade cutoffs of paramount importance.

5.1 Chapter Overview

The U.S. viewed the incoming Japanese administration of Hamaguchi and Shidehara in July 1929 with considerably less concern and some relief than the previous government under General Tanaka. The U.S. began to view Japan as an increasing threat, however, due to its army's seemingly uncontrollable pursuit of unilateral policies in Manchuria and its navy's divided position on necessary force ratios in the upcoming naval arms talks. Despite this moderate but increasing U.S. threat perception, the U.S. reviewed how it could lessen its own actions that Japan perceived as threatening. But the U.S. appears to have concluded that steps, such as giving prior notification to Japanese authorities with U.S. navy visits to Dairen and the mandated islands, were not necessary. U.S. hesitancy in concluding that Japan was truly an increasing threat was reinforced with Chinese Nationalist aggression in Manchuria against Russia, and a somewhat fleeting assessment that order “with justice” in Manchuria would require Japanese forces.

Perhaps because of U.S. uncertainty regarding Japan’s moderates’ ability to retain control over the army and navy, the U.S. pushed hard for Japanese reductions in relative naval power at the London Naval arms talks in early 1930. Secretary of State Stimson, head of the U.S. delegation to London, used the threat of an Anglo-American naval
accord concluded without Japan to press for Japanese concessions on force ratios. He also rejected Japanese interest in linking naval arrangements with broader understandings regarding China, as occurred at the Washington Conference. Japanese naval concessions would guarantee U.S. supremacy in the Pacific by freezing Japanese heavy cruiser construction while the U.S. built well past it, and for this reason the negotiations stalled in mid-March 1930 as Japanese naval and civilian elites engaged in a fierce contest. Stimson coerced Japan financially at this time using the threat of non-renewal of large Japanese government loans and demonstrated U.S. resolve to achieve its preferred naval force ratio. The Japanese government complied with the American "virtual ultimatum," and signed the Treaty. However, the ratification process in Japan signified the decline of civilian authority and the growing disaffection for political party rule in both military services and the upper House of Peers.

In response to this domestic environment of increasingly open military challenges to civilian authority, significant elements within Japan's army began planning for the annexation of Manchuria, while some extremists plotted army coups against the civilian government in the Spring 1931. These plans would gather momentum in response to increased Chinese political and economic integration between Chiang Kai-shek, leader of the Nationalist government in central China, and Chang Hsueh-liang, leader of Manchuria after his father's assassination. Japan's Kwantung army decided to act to reverse the growing tide of Chinese nationalism and integration, and in mid-September 1931, they began the Manchurian incident and the forcible annexation of Manchuria. The conflict spread south of Manchuria, however, and in late January 1932, the Japanese navy joined in, attacking Shanghai. This greatly increased U.S. threat perception and
finally stimulated greater British interest in coordinated diplomacy to stem Japan’s now united military services from advancing further against predominant Anglo-American economic interests. These bilateral efforts and those arranged through the League of Nations foundered on the shoals of British self-interest in appeasing Japan and President Hoover’s steadfast and liberal philosophical opposition to economic pressure against Japan.

Stanley Hornbeck and Secretary Stimson were able to exact some economic cost onto Japan by establishing of a loan ban against Japan in January 1932. However, this ban denied benefits to precisely those actors inside Japan who were moderate and attempting to cooperate with U.S. preferences in reigning in the army and navy expansionists (i.e., electric utility companies and their political party patrons, national government led by former Finance Minister Wakatsuki). It appears that the type of exchange that could be controlled by the State department (i.e., informal authority over loans) was used with almost total disregard of its effects on Japan’s domestic competition, because the other types of exchange could not be used due to Presidential veto (i.e., trade sanctions). Most U.S. banks chafed under the ban and stated their support for Japan in Manchuria, labeling their use of force a “stabilizing” action. Nonetheless, the State department under Stimson and Hornbeck attempted to alter the President’s liberal-based appeasement policy by sending military aircraft and air combat experts to train Nationalist Chinese forces, and limiting the export to Japan of necessary aviation gasoline additives. In this and other exchange decisions, state authority was dominant over corporate preferences, including Hoover’s decision not to restrict exchange. The Japanese anticipated some restrictive U.S. economic action and began demanding large
amounts of cotton in late 1931 in order to build up their supplies. U.S. State department officials monitored this increased demand, but were not authorized to limit it and therefore Japanese cotton imports from the U.S. surged across late 1931 and all of 1932.

The most critical economic exchange decisions of this period were the financial coercion at the London Treaty and the loan ban, each decidedly offensive realist in attempting to control the capabilities of Japan. The loan ban also comports with defensive realism’s emphasis on denying gains to an increasingly threatening rival. However, the previous three loans across the period, particularly the one in May 1930, do not comport with defensive realism. The monies from the May 1930 loan actually helped finance supplementary naval expenditures in Japan to rectify what the Japanese navy claimed were serious strategic vulnerabilities caused by the Treaty (i.e., the U.S. was funding the Japanese navy’s budget increases and indirectly rewarding its undermining of civilian authority). Japan gained quite substantially from overall exchange with the U.S. in this period, earning trade surpluses until 1932 and importing substantial amounts of machinery, finished steel sheets and scrap iron and steel, which facilitated its continued advances in industrial and potential military production. U.S. direct investment also continued to relatively advantage Japan’s capabilities during this period, and was particularly evident in the Associated Oil Company’s building of a refinery in Japan and transferring substantial technical know-how in the process in 1931. For these reasons, exchange in this period was broadening up to the Manchurian crisis and highly beneficial to Japan. Additionally, Japan’s strategic vulnerability to the U.S. in crude and fuel oil imports did not increase, but its long-term energy autonomy was made more vulnerable through increased import of American crude and refining technology. Japan’s overall
economic reliance on trade with the U.S. (i.e., trade with the U.S./Japan GDP) actually decreased by the end of the period, yielding a mixed assessment of slightly increasing vulnerability that maintained high Japanese dependence.

Not all U.S. companies contributed to Japan's material capabilities during this period however. National City Bank led all foreign and domestic banks in destabilizing the Yen after Japan returned to the gold standard. When Japan allowed the free exchange of gold to support the Yen-dollar exchange rate beginning in early 1930, National City Bank sold 273 of the total 760 million Yen sold during the crisis. The Mitsui bank, whose leader was later assassinated for his role in this destabilization, sold only 56 of the total 760 million Yen sold. This event and President Hoover's opposition to any economic restrictions because they were tantamount to acts of war lend substantial weight to the liberal perspective as the most powerful explanatory framework across the period. Hoover's pivotal role in preventing substantial economic action against Japan and potentially bringing Britain and the U.S. together in deterring Japanese military advances, overshadows much of what else occurred. Even though he did not act on the basis of dominant corporate interests, his motivation was decidedly liberal in rationale. Offensive realist actions in the financial coercion at the London conference, the loan ban and the air power assistance to China are weighty as well. They had important effects on Japan's domestic political competition and future autonomy due to their assistance to the resisters of Japanese control of resources in Manchuria and North China. For these reasons this period's dominant theory perspective is a mixture of liberalism and offensive realism.
Hamaguchi Osachi (Premier) and Shidehara (Foreign Minister) of the Minseito party succeeded Tanaka, and sought to balance Anglo-American preferences with a China policy that ensured Japanese interests there. These Minseito leaders decided to cooperate with U.S. arms control efforts and China normalization preferences in order to secure continued economic benefits from bilateral relations. They also decided to let go any further inquiry into the Kwantung army’s responsibility for the Chang Tso-lin assassination. They deferred to the wishes of the General Staff in Tokyo not to expose the simmering conflict within the military over appropriate Japanese policy in China and Manchuria in relation to likely conflict with the U.S. or the Soviet Union. The common position, however, of army officers at all levels was that possession of Manchuria was indispensable to Japan’s security and no civilian authority in Tokyo should be allowed to compromise this position in deference to the U.S.. By early 1930, this position led to concrete army planning for the occupation and annexation of Manchuria.

For their part, Hamaguchi and Shidehara believed that Japan’s advancement and increases in relative material capabilities required cooperation with the U.S., and this meant satisfying to some extent American preferences for Japan’s relations with China. To this end, Shidehara concluded the agreements withdrawing Japanese troops from Shantung and negotiated the final arrangements restoring tariff autonomy to China. The

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428 For summaries of General Staff and Kwantung Army planning which described the need for Manchurian and North China resources for war with the U.S. and/or Soviet Union see Seki, “The Manchurian Incident, 1931.” pp.154-7.
Hamaguchi government also tied Japan’s economic fate more closely to the Western powers when it decided to lift the gold embargo in January 1930, restoring the Yen to its pre-WWI dollar parity. This decision was based on the large trading volumes and values with the U.S. during the last boom year of 1929. It was also influenced by Britain’s return to the gold standard in 1925 and new Finance Minister Inouye’s belief that balanced government budgets would result from freely exchanged gold reserves, instead of sole reliance on domestic and foreign loans to balance government budget deficits.\textsuperscript{430} Unfortunately, this decision and the restructuring of Japan’s agricultural and industrial sectors in the aftermath of the 1927 financial crisis combined to cause increased economic hardship on many Japanese just as the U.S. led economic depression began to affect Japan’s trade and income.\textsuperscript{431}

The Minseito leaders were deeply interested in cooperating with the Anglo-American powers in arms limitation in order to secure better footing for Japan’s economy, by both directly lowering expenses on the military and inducing even greater economic exchange with the Western powers. This was particularly evident in these leaders’ desire for improved financial ties with the U.S. and Britain in order to ease government finance pressures that were increasing with the onset of the great depression. The Japanese decision to rejoin the gold standard on the eve of the London Naval arms limitation conference demonstrates the interrelated nature of Japanese international economic and security policy. Beginning in late January 1930, the London Naval Conference was convened by the Western powers in order to prevent a naval arms race in

\textsuperscript{430} See Allen, \textit{A Short Economic History of Modern Japan}, pp. 106-8.

\textsuperscript{431} Prices of Japan’s most important commodity export - raw silk- declined by over 50\% in 1930, yielding only 53\% of the value of 1929’s exports on 82\% of the volume/weight, causing hardship among Japan’s peasant farmers. Cotton products also experienced similar drops affecting textile mill products and the burgeoning working class. See \textit{ibid.}, pp.107-8.
cruisers, submarines and destroyers. This had appeared likely given the failure at Geneva in 1927 and subsequent American building plans. Japan's agenda was slightly more comprehensive than arms limitation:

Believing that cooperation and material support from Western economic and political leaders was indispensable to accomplishing this goal (economic restructuring and advancement), the cabinet was anxious to achieve an agreement at London not simply because the savings in naval expenditures would be useful but also, more importantly, because the good will thus generated would predispose the Westerners to aid in the solution of Japan's fundamental economic problems. For this larger goal the cabinet was willing to override the perhaps justified security concerns of the Navy General Staff and to accept the political risks this entailed.432

As in 1918 (i.e., Siberia) and 1922 (Washington Conference), Japan's liberal leaders hoped that restraint of its military and cooperation with Anglo-American arms limitation preferences would lead to greater economic benefits.433 In fact, their ability to enforce this policy depended precisely on the receipt of economic benefits from the Western powers and the reduction in Western threat perception of and planning against Japan.434 In particular, the Japanese government was seeking assistance in its fiscal policies and return to the gold standard, which would likely require foreign lending to

433. Imperial adviser Prince Saionji noted that Japanese power could not be guaranteed by the pre-conference desired 10:7 overall tonnage ratio. He held, “a nation's military preparedness, its ability to maintain its strength in time, depends first of all upon its financial policies...it would be extremely impolitic for the future of our country if we were to forego the privileges Japan has enjoyed up to the present, of close ties with Britain and America.” Saionji Kinmochi, quoted in Connors, The Emperor's Adviser, p.118.
434. The United States understood this clearly and took steps to reign in its own navy's actions that appeared hostile to the Japanese. From February to April 1929 a debate regarding U.S. Fleet movements by Admiral Bristol into Dairen and proposed visits to the mandated islands took place among Stanley Hornbeck, Nelson T. Johnson, American Minister to China, and the Secretary of State. Admiral Bristol had taken the position that prior notification to Japanese authorities was not necessary when U.S. vessels put into Dairen because it was a Chinese port, not Japanese. Bristol took this position without reference to the State department, and this and possible lengthy stays in the mandated islands were causing “suspicion and resentment on the part of the Japanese.” Hornbeck asked whether the mandates visits were worth the diplomatic drawbacks, while Johnson saw no reason not to proceed as the Japanese were putting into our ports with and without prior notification. See letters and memorandum February 19, 1929 from E.H. Dooman to Stanley Hornbeck and Hornbeck to Secretary of State, April 10, 1929 in Hornbeck Papers, Box 520, Folder: Miscellany 1920-1928.
ease its transition. Hamaguchi's government was helped early on in this Western appeasement endeavor and image shift by the hostile actions of Chinese and Manchurian forces against the Soviet Union in the summer of 1929. Chinese Nationalists under Chiang Kai-shek and Manchurian forces under Chang Hsueh-liang began harassing Russian consular officials in Manchuria and in mid-July took over the Chinese Eastern Railway and telegraphic offices, discharging Russian officials and imprisoning Chinese communists. Russia mobilized its army to the Manchuria-Siberia border and clashes of troops occurred throughout late July and August, with extensive Russian bombing of Manchuli in northwest Manchuria on August 17, 1929. This blatant Chinese nationalist offensive against Russia alienated Western states and provided Japan with some legitimacy for its previous actions against Chinese nationalism in protection of Japanese rights in Manchuria. Russia broke diplomatic relations with Nanking and continued to engage in conflict with Chinese troops until December, at which time Manchurian negotiators signed the Khabarovsk protocol restoring the status quo of early July. Nanking, however, rejected this understanding as having been negotiated without its approval and China did not re-establish diplomatic relations with Russia again until late 1932.

The United States pushed for a negotiated settlement and respect for the recently effective Treaty for the Renunciation of War (i.e., Kellogg-Briand Pact), and tried to align the Washington Conference powers behind this effort. Japan did not actively participate in this effort due to its desire to improve relations with both Nanking and Manchurian leaders at Russia's expense, and the United States was left alone to enunciate
its principled position on the fate of Manchuria. Stanley Hornbeck gave a concise account of the history of America’s position on the railway issues in and around Manchuria and reaffirmed America’s policy that the railways and politics of Manchuria were “born in and of international politics...and) serve not alone the people or the purposes of any one country. They are public carriers in a much broader sense than that which is usually connoted by that expression...the policy and efforts of the United States in reference to Manchuria always have been directed toward the maintenance of peace-with justice.”

At the end of 1929, tension lessened over Manchuria, but was set to begin a larger brewing over the domestic and international ramifications of new naval arms limits for Japan. The London Naval Conference began in mid-January and ended on April 22, 1930, with Japan deferring to the staunch American position that Japan accept a 10:6 ratio in heavy cruisers and parity in submarine tonnage, while allowing expansion for all parties in light cruisers to the 10:7 ratio. The Japanese navy and delegation to London led by Wakatsuki publicly stated its preference for a 10:7 ratio in heavy cruisers, which would preserve Japan’s primacy over American naval forces in Japanese home waters and the Western Pacific more generally. The United States went into the negotiations with a heavy cruiser advantage of 130,000 tons to Japan’s 108,400 tons, and only a budgeted plan to build a larger advantage over Japan and parity with England. Secretary

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435 Shidehara complained that coordinated notes to China and Russia would not serve a practical end and only irritate the parties. Shidehara told the Russian ambassador in Tokyo that Russian invasion of Manchuria would entail serious effects on Japanese-Russian relations. Iriye, After Imperialism, p.267.

436 Address by Stanley Hornbeck, Chief of the Division of Far Eastern Affairs, U.S. Department of State, August 27, 1929 to Williamstown Institute of Politics. Hornbeck Papers, Box 478. Folder: Writings American Policy and the Chinese-Russian Dispute. As with many of Hornbeck’s principled positions, the U.S. position on Manchuria served not only its principles, but also its own interest in attempting to establish a position in Manchuria against both British-dominated Southern and Central China and encroaching Japanese dominion from Korea into North China.
of State Stimson used the building plan to coerce Japan into settling for the 10:6 ratio in heavy cruisers, telling the Japanese unless they "approved the principle of a 10:6 ratio, the American navy would be expanded until this goal was achieved." Stimson also used the threat of a solely bilateral accord with Britain to pressure the Japanese into accepting the arrangement, which American naval experts concluded allowed the U.S. navy a "chance of conducting a successful campaign" against Japan. This fact was apparent to the Japanese naval officials who opposed concessions on heavy cruisers because a 10:6 ratio would compromise Japan's hegemony in and around its home waters, violating this principle established at the Washington Conference in exchange for Japanese political concessions and understandings elsewhere (e.g., Siberian withdrawal, return of Shantung).

Stimson refrained from pressing Wakatsuki in mid-February because of the pending general elections in Japan and the sitting government's need to be seen as not compromising on a prominent national security position prior to the election. U.S. deference to both the niceties of Japanese domestic politics and its navy's consistent position was fleeting, and after the election Stimson pressed the Japanese to accept the 10:6 ratio under threat of an Anglo-American accord against Japan. These intimations alarmed the Japanese causing fear that America planned offensive war, possibly sparked over China. This prodded then U.S. ambassador to Japan, William Castle, to reassure

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437. Stimson made this position clear to the Japanese in mid-December 1929. Implicit in this threat was the budgetary and resource capacity to build to this advantaged position, which Stimson knew Japan could not match without serious financial difficulty. Crowley, Japan's Quest for Autonomy, p.45

438. Ratification testimony of Rear Admiral Pringle, chief of the Naval War College, quoted in ibid., p.46. Anglo-American unity against Japan in the negotiations was explicit and made clear to Japan in mid-February meetings among the three principals (i.e., Stimson, Prime Minister Ramsay MacDonald and Wakatsuki). The seeds of later U.S.-British discord over Asian policy may also be traceable to this explicit U.S.-led joint coercion of Japan.

226
Shidehara that he could "conceive of no circumstance in which America would go to war over China." This personal assurance was repudiated by higher ranking U.S. officials after Shidehara asked for an official assurance from the U.S. government to this effect, and Castle was directed to refrain from any statement that would "bracket" U.S. and Japanese relations vis à vis China. Japanese leaders averse to solely a naval arms accord attempted to link the naval limits negotiations to a joint understanding on China that legitimized Japan's aggressively expanding position and interests there. This effort was dismissed out of hand by the U.S. and may have prodded the international lawyer in Stimson to remain firm in his commitment to bind Japan by legal treaty to stricter naval arms limits. By early March 1930, however, Stimson's own hard line was being challenged by President Hoover and Senators Borah and Swanson, who held even a 10:7 ratio acceptable because "Japan (was not) an immediate potential enemy with trade conditions and fleets as they are."

Stimson reacted to this potential undercutting of his negotiating position by responding to Japan's recent compromise offer to accept the 10:6 ratio in heavy cruisers conditioned upon America deferring until 1935 the construction of the last 3 of its

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439. William Castle to Foreign Minister Shidehara, quoted in Crowley, Japan's Quest for Autonomy, p.50. This would not be the last time Castle would seek to appease Japan against Stimson and Hornbeck's desires.

440. Admiral Kato Kanji, Chief of the Naval Staff and Vice Minister Admiral Kobayashi attempted to make this linkage not unlike that made during the Washington Conference, but were rebuffed by the U.S.. See exchange of telegrams between William Castle and Joseph P. Cotton, Acting Secretary of State, in Foreign Relations, 1930, Volume I, pp.68-9.

441. Senators Borah and Swanson, quoted in Crowley, Japan's Quest for Autonomy, p.53. Trade conditions restraining some Americans' threat perception of Japan, including President Hoover's, were based on Japan's need for exchange with the U.S. to finance its budget and loan exposures in addition to its return to the gold standard. A driving objective of all three principals to the negotiations was budgetary reductions from arms control agreements, and Japan felt this increasing throughout 1930 as income declined with export declines to the U.S. See Tatsuo Kobayashi, "London Naval Treaty," in Morley, ed., Japan Erupts, pp.53-4. Shidehara enforced this primacy of fiscal discipline and decreased budgets on navy preferences and objections to the 10:6 ratio back in Tokyo. See Crowley, Japan's Quest for Autonomy, p.57.
planned total force of 18 cruisers. Stimson modified this constraint on March 8, demanding that deferred construction begin in 1934, so America's bargaining position would be stronger at the next scheduled naval arms conference in 1936. As the Japanese delegation deliberated over this modified "final" proposal from the U.S., Stimson could not restrain himself from using additional pressure to obtain Japanese compliance. On March 29, 1930, Stimson threatened effective foreclosure on a twenty-five year old government loan in an effort to hurry Japan's deliberation and acceptance. As a result, the Japanese agreed and signed off on the London Naval Treaty on April 22, 1930. Because the U.S. government used financial coercion to gain Japan's signature on the Treaty, this event is most consistent with offensive realism and its emphasis on using economic exchange to compromise a rival's capabilities.

The pressured naval limitation agreement became the critical focal point in Japanese domestic politics and would affect the future course of its foreign policy greatly. The import of the Treaty increased with the explanations made to the Japanese public in the press and the reaction of the public to later accusations about the Treaty negotiations. John Burrell Oliver summarized the Japanese press coverage at this juncture well: "From

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442. Stimson wanted to pressure Premier Hamaguchi directly, having both the U.S. and Britain issue "virtual ultimata" to him to agree to the Treaty terms. Joint messages were drawn up and dispatched for the embassies in Tokyo, but on two occasions in mid-March, 1930, the messages were only relayed to Foreign Minister Shidehara, who assumed the responsibility to bring the Japanese government to agreement. See Oliver, "Japan's Role in the Origins of the London Naval Treaty of 1930," pp.461-67; Thomas Francis Mayer-Oakes, "Prince Saionji and the London Naval Conference: Being Part of Volume One of the Memoirs of Harada Kumao, entitled: Prince Saionji and the Political Situation," (Ph.D. diss., University of Chicago, 1955), pp.27-29.
443. This incident of economic coercion is described in Fanning, Peace and Disarmament, p. 193, footnote 80.
444. Stimson reacted dryly to later Japanese press accounts of his sending a threatening note to Prime Minister Hamaguchi noting, "Had this been published several days ago, it might have been disastrous, and would have been deeply resented. It is fortunate that this was not done, and even more so that the action was not attributed to me." This is not a denial of the issuance of the threat, but raises questions about the nature of the economic coercive communication to the Japanese government. See Telegram Stimson to Joseph Cotton, Acting Secretary of State, April 1, 1930, in Foreign Relations, 1930, Volume I, pp.99-100.
about March 25, after it became obvious that the Japanese government was bent on
acceptance, the press turned conciliatory once more. The financial condition of the
country and tax burden were stressed, and the public was reminded that a large foreign
loan was about to come due. Because the Japanese public had been informed of the
link between renewal of foreign loans and the signing of the London Naval Treaty,
opponents who soon criticized the Hamaguchi government’s actions as corrupt and
lacking in “patriotism” were also indirectly criticizing its ties and fealty to U.S. financial
power.

The final heavy cruiser tonnage allotments required Japan to hold its existing
108,400 tons constant while the U.S. built up from 130,000 tons to 180,000 tons by 1936.
David Evans and Mark Peattie summarized the Treaty’s effect on relative power: “the
treaty resulted in not merely an inferior ratio in Japanese naval strength across the board,
but an actual reduction in that strength vis a vis the other two naval powers. At
Washington, the limitation ratios in capital ships essentially reflected the actual relative
strengths of the three major naval powers as they then existed. At London, Japan was
obliged to halt further construction of heavy cruisers—a category in which, during the past
decade, it had labored with effort and skill to obtain a lead—while U.S. construction
cought up in this category.” The political, military and psychological import of this in
Japan was not lost on Stimson or the American delegation. During Treaty ratification
hearings in the U.S. Senate, Stimson expressed respect for the Japanese willingness to
“stop active construction and to accept a position of inferiority to our potential

446 See Robert Scalapino, Democracy and the Party Movement in Prewar Japan, 3rd ed., (Berkeley, CA:
University of California Press, 1975), p.239
447 David Evans and Mark Peattie, Kaigun: Strategy, Tactics, and Technology in the Imperial Japanese
program." After noting the position of the Japanese Navy General Staff as subordinate only to the Emperor, not the party-led cabinet, Stimson held the civilian government’s capitulation in high esteem:

A government that had the courage to go into a treaty tying itself to stand still while another built past it and put itself into a far better position in case the treaty should not be continued after 1936, has a very hard problem, and no amount of argument could minimize that problem. No country is so poor that it cannot be frightened into competitive building. I take my hat off to the Japanese Government in this treaty.

This comment was widely used in Japan by Treaty opponents led by Chief of the Navy General Staff, Kato Kanji, who held that Hamaguchi and Shidehara had compromised Japan’s security. Kato and the growing chorus of Treaty opponents also held that Japan was a victim of Anglo-American pre-conference arrangements against it, and in this assessment they were not entirely inaccurate. Kato’s critique of the Hamaguchi government and direct appeals to the emperor were made public in a series of press conferences by the Vice Chief of the Navy General Staff, Admiral Suetugu.

These actions violated the longstanding sanctions against publicizing “supreme

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448 Stimson, quoted in, Crowley, Japan’s Quest for Autonomy, p.55
449 Secretary of State Stimson Senate testimony of May 13, 1930, quoted in Kobayashi, “London Naval Treaty,” p.55. While Stimson publicly acknowledged no government is too poor to defend itself, privately he coerced Japan under the presumption that it needed American capital to refinance debts and would therefore sign the London Treaty. See Wilson, American Business and Foreign Policy, p.211.
450 Kanji actually tried to invoke the “right of supreme command” and lobby the emperor directly against accepting the 10:6 ratio during conference negotiations, but he was outmaneuvered by Hamaguchi and other Navy General Staff members who agreed with the 10:6 compromise. Crowley, Japan’s Quest for Autonomy, pp.66-7.
451 Oliver noted, “Great Britain and the United States had determined the general level of Japan’s future naval strength during bilateral negotiations before the Conference met...Committed to naval parity at a meaningful level of reduction, these two found that the intricacies of an agreement establishing that parity made it contingent upon Japan’s naval strength. As a prerequisite to their own agreement, therefore, Great Britain and the United States undertook in advance of a formal Conference to limit Japan essentially to her existing fleet.” Oliver, “Japan’s Role in the Origins of the London Naval Treaty,” p.495.
452 This was an extension of the Japanese navy’s great use of the press to publicize and “educate” the public as to the benefits of the navy position supporting a 70% ratio against the U.S. prior to and during the Conference. By at least one account, it had succeeded in swaying public opinion behind the navy position. See Tatsuji Takeuchi, War and Diplomacy in the Japanese Empire, (New York: Doubleday, Doran & Co., Inc., 1935), pp.303-305.
command” appeals to the emperor and critique of the cabinet by naval officials. Between the signing of the Treaty and its ultimate ratification by the Privy Council in Japan on October 1, 1930, Japan underwent dramatic change in institutional authority among the army, navy and cabinet government led by party officials.

In order to reestablish harmony in the Navy General Staff, Kato accepted the Naval Minister, Admiral Takarabe’s proposition that Admirals Suetsugu and Yamanashi, Vice Navy Minister, would jointly resign while Kato would join the Supreme War Council resigning from his position as Chief of the Navy General Staff. This arrangement was hoped to neutralize the conflict over the legitimacy of the navy’s opposition to the Premier’s treaty. Admiral Takarabe was soon to resign as well, but not before a new precedent in Naval General Staff budgetary demands was established in a supplementary naval budget increase. Interestingly, the ability to finance the General Staff’s supplementary budget increases was materially assisted by the $71 million loan organized by J.P. Morgan in May 1930 to the Japanese government. This loan was delayed until after the signing of the Treaty and authorized by the U.S. State department as part of its policy of rewarding Japan’s compliance with U.S. arms control preferences. It was not clear, nor does it appear to have even been considered by U.S. officials, what the effect would be on Japan’s domestic politics in this explicit financial reward for security compromises. Foreign Minister Shidehara vehemently denied that

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453. British capital was also raised for Japan at this same time, as Britain’s investors extended 12.5 million pounds to Japan through J.P. Morgan’s London affiliate Morgan Grenfell. See Nolt, “Business Conflict and the Origins of the Pacific War,” p.328; Moulton, Japan: an Economic and Financial Appraisal, pp.488-9.

454. This is a prime example of unintended consequences in using financial exchange, as the U.S. was now extending fresh capital to Japan, which financed a disgruntled Japanese navy’s expansion. Wilson, American Business and Foreign Policy, p.211, p.304, footnote 50.
Japan had bowed to pressure from abroad, but the die was cast for the political maelstrom during ratification debates in the Diet and budget negotiations with the navy.

Naval budget allocations previously had been determined by negotiations among the Finance Minister, the Naval Minister and the Premier. But during the conflict over the navy’s position on the London Treaty, the new Chief of the Navy General Staff, Admiral Taniguchi, recommended a supplementary budget directly to the Supreme War Council. They accepted it to “offset” the dangers in the London Treaty and Premier Hamaguchi was effectively forced to agree to the increases without Diet or other cabinet officials’ approval. Cabinet government was also undermined by the Supreme War Council’s official reply to the Throne of July 22, 1930. In this reply the power of future cabinet officials to negotiate naval arms limits was circumscribed and the Hamaguchi government accused of “creating deficiencies in our naval position” by ignoring the fundamental policy of naval supremacy in Japanese waters established at the Washington Conference in 1922. This Treaty not only galvanized naval opposition, but also helped bind both the army and navy services in opposition to party politics and cabinet government. Chief of Staff of the Japanese Army, Kanaya Hanzo, opposed the London Treaty because of its effect on army planning and force projection against the Soviet Union, whose five-year plan was causing Japanese army planners great concern.

455 Crowley, Japan’s Quest for Autonomy, p. 77.
He felt that “naval restrictions would directly affect army manpower,” hampering Japan’s ability to re-supply army operations and support movements into China or the Russian Far East.457

As with perceived Premier compromises with the West in the past (i.e., Hara in 1921), Premier Hamaguchi was fatally attacked on November 14, 1930 by a member of the Aikokusha (Patriotic Society) which was allied with Hiranuma Kiichiro, Vice President of the Privy Council.458 From this point forward, civilian government contended with increasingly radical military officers who stepped up their planning to create a subservient and nominally independent Manchuria and a political structure in Japan proper that accurately reflected “the right of supreme command.” These officers, both navy and army, were dissatisfied with budgetary cutbacks that began in 1925 and continued through the London Naval Treaty ratification period. They resented the deference of Japan’s civilian rulers to Western preferences and the role of financial constraints in curtailing their ambitions in China and throughout Asia.

It is still not possible to determine the degree to which the U.S. loan in May 1930, which helped the Japanese government refinance its debt and manage some of its growing domestic production and foreign trade problems, influenced these military officers to begin plotting against their own government. However, it is known that after

457. Seki, “The Manchurian Incident,” p.157. Army-Navy cooperation against civilian authority galvanized around Treaty opposition, but had other roots as well. In particular, Japan’s experiment with coal hydrogenation at Fushun, Manchuria beginning in 1926 was a navy project operated with the army-dominated South Manchuria Railway Co. as its principal partner. Barnhart, Japan Prepares for Total War, p.29. The U.S. was aware of this collaboration, however, learning in particular that in 1927 the Japanese navy purchased “the manufacturing rights in Japan to a German process for producing fuel oil from coal.” This was likely the Bergius process held by IG Farben. See naval intelligence report January 18, 1928, File e-10-d, Register 13177D, RG38. See also references to naval intelligence analysis of the Fushun shale oil industry in Stanley Hornbeck’s papers. Letter from J.K. Caldwell to Captain A. St. Clair Smith, U.S. Navy, January 4, 1928, Hornbeck Papers, Box 308, Folder: Naval Intelligence.

458. Hamaguchi did not die until August 1931, but Wakatsuki assumed formal control of the cabinet government in April 1931 with his appointment to the Premiership.
the first meeting of the army officer dominated Sakurakai (Cherry Blossom Society) in September 1930, the identification of party politicians and large industrial and banking interests with the decline of the Japanese state became widespread and accepted by officers across all levels of authority.\textsuperscript{459} The further identification of parties and cabinet government with compromises of national security due to foreign economic pressure played a large role in the military’s economic security planning for autonomy.\textsuperscript{460} This planning centered on the vital role of Manchurian and North China resources in creating an autonomous Japan that could better resist pressure from the West, the Soviet Union and nationalist China.

The London Treaty served as a “catalyst” forging an alliance of discontented forces in Japan against Meiji parliamentary government and Western cooperation. It was the London Naval Treaty that galvanized the opponents of democracy and cooperative foreign policy, and empowered them to seek drastic and violent changes in Japan’s internal and external situations. Thomas Mayer-Oakes summarized the primary causality in Japan’s descent from civilian rule:

To outside observers Japan’s volte face from the liberal parliamentary decade of the twenties to the warfare and fascist reconstruction of the thirties and forties may be best marked by the Manchurian invasion of 1931...To the Japanese, however, the first steps toward fascism are associated with the reactions to the Hamaguchi government’s apparent success in obtaining ratification of the London Treaty despite the opposition of important elements in the naval establishment and in the Privy Council.\textsuperscript{461}

\textsuperscript{459} Ogata quotes the Sakurakai prospectus which bemoaned civilian rulers as corrupt and materially self-interested. Fearing for its own self interest, the Sakurakai held that after “the London Treaty issue, it is evident that the poisonous sword of the demoralized and covetous party politicians is about to be turned towards military.” Ogata, Defiance in Manchuria, p.30

\textsuperscript{460} Barnhart, Japan Prepares for Total War, pp.31-2.

5.3 Unrest in Japan and Expansion in Manchuria

Japan’s movement toward military authoritarianism began in earnest after ratification of the London Naval Treaty with the assassination attempt on Hamaguchi and army designs against civilian rulers. Plotting for the attempted coup of March 1931 occurred largely within members of the Army General Staff’s intelligence division, which had previously been responsible for “manipulating, assisting, advising, and undermining the various warlord cliques in North China and Manchuria.” These officers came to view Japan’s position in China and Manchuria as inseparable from Japan’s position at home and vis a vis the Western powers and the Soviet Union. They were therefore inclined to use their skills and tactics developed in the Chinese area at home to “renovate” Japan. Interaction with and support of higher officers, including Army Generals Sugiyama, Koiso, Tatekawa and War Minister Ugaki, occurred throughout January and February, although Ugaki avoided directly stating any support for the idea of Imperial army troops being used in Tokyo. Instead, the coup plotters alliance with disaffected labor groups and others dissipated by early March, and on order from Ugaki, Army General Koiso convinced Colonels Komoto and Itagaki, recently returned from Manchuria, to squelch the effort planned for March 20, 1931. Ugaki decided that any appearance of army involvement in a coup would undermine the prestige and policy

462. Crowley, Japan’s Quest for Autonomy, p.96. This might be another form of blowback that requires greater analysis in civil-military relations.
of the army, which appeared to be gaining ground with increasing criticism of Shidehara and growing military connections between Chang Hsueh-liang in Manchuria and Chiang Kai-shek in Nanking.\textsuperscript{464}

It was the assertiveness of Chiang Kai-shek's regime in aligning Manchuria with Nationalist China that finally caused Japan's military to step up and implement its plan to annex Manchuria under pretext of assault on Japanese army forces there. Chiang's Nationalist government had established bureaus in all major Manchurian cities by March 1931, and in April, Foreign Minister C.T. Wang declared that China would reclaim all rights and all concessions in China and Manchuria, including extraterritoriality and railroad rights. To these ends, negotiations were suspended in early June between "China" (i.e., Chang Hsueh-liang and Chiang Kai-shek's representative, General Kao Chi-i) and Japan on the proposed rival railway to Japan's South Manchuria line under construction in Manchuria.\textsuperscript{465} The Minseito cabinet tried to defend its foreign policy in late June 1931 by noting that Tanaka's more aggressive policies had caused Chinese boycotts of Japanese goods and increased fear among other nations both in Asia and the West.

The Japanese army high command and the Kwantung army in the field in Manchuria decided it was time to act. They wanted to forestall what they perceived to be the negative consequences from the combination of partisan bickering, Minseito financial constraints on the military, the long-term threat of the Soviet Union, and rising Chinese nationalism and integration with Manchuria. Army situation estimates described

\textsuperscript{464} In addition to military opposition, the Seiyukai party launched an attack on Shidehara's willingness to defer to China's positions on ending extraterritoriality and foreign concessions. Seki, "The Manchurian Incident," pp.178-9.

\textsuperscript{465} Crowley, Japan's Quest for Autonomy, p.104.
increasing threats from the Soviet Union due to military budget increases and worked well with the army high command, but were debunked by cabinet officials including Finance minister Inouye, Shidehara and Wakatsuki. The army high command under Kanaya, Chief of Staff, and Minami, War Minister, lobbied successfully to have an army division transferred to Korea in preparation for executing the plans crystallizing in the operations division of the Kwantung army under colonels Ishiwara and Itagaki. They failed, however, to convince the navy that Manchuria was significant enough to Japan’s security and long-term power to justify annexation by force of arms, and were particularly cautioned by the navy that the American position should not be ignored.  

By early August Minami was openly criticizing the Wakatsuki cabinet as “indifferent to national defense,” and urging the newest leaders of Japan’s army (e.g., General Honjo Shigeru of the Kwantung army and General Hayashi Senjuro of the Korea army) to counter the “sell out” of Japan’s interests in Manchuria.  

The Wakatsuki cabinet did not respond to these inflammatory public statements in the hope of settling rising tensions with Manchuria over the killing of captain Nakamura of Kwantung army intelligence. The cabinet was not prepared for the near unanimity within the Army General Staff and the Kwantung army for action, and this was particularly accentuated with the annual rotation of officers in August bringing General Tatekawa to the head of the operations division of the General Staff. Tatekawa signed off on Ishiwara and Itagaki’s plans for annexation of Manchuria as did General Honjo of the Kwantung army.  

All that remained was the timing of the incident that would

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467. Ibid., p.185.
468. Crowley, Japan’s Quest for Autonomy, pp.116-7.
justify armed annexation. The timing was determined by the possibility of a diplomatic solution to the Nakamura murder negotiations between Chang Hsueh-liang and the Japanese authorities. The army's representative negotiating with Chang (General Doihara) was recalled to Tokyo in early September 1931 and given new orders to settle the affair that had helped intensify Japanese public and military opposition to Shidehara diplomacy on the mainland. Before he could return to Manchuria, Ishiwara and Itagaki pressed for action and received the signal to go ahead from General Tatekawa who was ordered by his superiors, Minami and Kanaya, to leave for Mukden on September 15 to help calm the situation. Instead, prior to departing Tatekawa sent a message to Kwantung army operations that he would not arrive for 48 hours. This was a signal to act before his arrival and present a fait accompli of military action. General Honjo complied and ordered the incident to begin on September 17 (i.e., explosion on the South Manchuria Railway Co. line near the best Chinese troops within Mukden).\textsuperscript{469}

The conflict spread quickly as did the effort to contain its spread and consolidate support for it in Japan. The Kwantung army's offensive operations in Manchuria were strictly circumscribed so as not to threaten the Soviet Union by moving too far into Northern Manchuria.\textsuperscript{470} A similar concern for Western opinion does not appear to have been exhibited. The army sought to portray the widening conflict to the cabinet as necessary to protect Japanese rights and nationals. Shidehara, Inouye and Wakatsuki countered that the army was jeopardizing "the foreign and fiscal policies of the government," and after curbing War minister Minami's description of events they

\textsuperscript{469} Ibid., pp.118-121.

\textsuperscript{470} Ogata, Defiance in Manchuria, p.74. Ogata stressed the primary import the army assigned to forestalling Soviet action, but also its willingness to press south toward China, courting Anglo-American resistance.
notified the Emperor that the General Staff had agreed to settle the matter peacefully.\textsuperscript{471} The General Staff was not, however, inclined to positively control the Kwantung army along these lines, nor did it disagree with Kwantung army actions in Manchuria. This was evident when the Kwantung army asked for and received troops from General Hayashi’s Korea army shortly after the annexation began. Inouye and Shidehara believed that withholding funds necessary to effect the transfer might provoke the appropriate hesitation. Instead, Minami forced a showdown with the cabinet over the right of supreme command. On September 23, 1931, Minami extracted a compromise from Premier Wakatsuki that he would not contest the General Staff’s right to command (i.e., funding the troop transfer), while accepting only their pledge to control the Kwantung army in Manchuria.\textsuperscript{472}

In these ways the General Staff in Tokyo, the Kwantung army in Manchuria and cabinet officials affected the annexation of Manchuria. Akira Iriye summarized this well:

\begin{quote}
There never was an instance of the Kwantung Army's openly challenging Tokyo’s authority and defying its orders. Staff officers frequently fabricated crises, accumulated faits accomplis without obtaining prior endorsement from Tokyo, and privately complained of the supreme command’s attitude...the Kwantung Army did not plot revolt, and it honored specific orders from Tokyo, no matter how much the staff officers grumbled about them and how confident they were of eventually overcoming Tokyo’s opposition to their plans.\textsuperscript{473}
\end{quote}

Ineffective civilian and cabinet government resulted partly from the operation’s initial popularity among Japanese citizens and the threat of armed uprising by the Japanese

\textsuperscript{471} Crowley, Japan’s Quest for Autonomy, p.123.
\textsuperscript{472} Ibid., p.126.
\textsuperscript{473} Akira Iriye, “Introduction: Extension of Hostilities,” in Morley, ed., Japan Erupts, p.237. Iriye also noted that “there was no clear dichotomy between civilian and military policy; therefore, there was no complete civilian capitulation. The military may, directly or indirectly, have brought about the atrophy of civilian government, but the latter was much more than a passive mouthpiece for the military.” Ibid., p.238.
army. This threat was palpable among civilian officials of the Wakatsuki cabinet and justified by the attempted coup in mid-October. The Imperial army General Staff’s operations division head, General Tatekawa, was disgusted by the Wakatsuki cabinet’s desire to negotiate a compromise to the Manchurian intervention, and instilled in some of his subordinates a desire to end this possibility.

Led by colonels Hashimoto Kingoro and Nemoto Hiroshi, a group of operations division officers openly called for a military coup, even after Tatekawa was censured by the Army high command for violating policy accepted by Generals Minami and Kanaya. Colonel Nemoto communicated his intent to General Araki, Inspector General of Military Education, on October 16 to press on with the planned coup, and alarmed him sufficiently enough for him to inform Vice-War Minister Sugiyama of the continued planning of the colonels. Sugiyama had all the plotters arrested by military police on October 18, disbanded the Sakurakai and eventually transferred the officers out of central headquarters.474

5.4 Anglo-American Division over the Manchurian Incident and Domestic Disarray in Japan

The October coup attempt and the premeditated daylight bombing of Chinchou beginning on October 8, 1931 alarmed U.S. leaders greatly, stimulating analysis of the situation but restraint in action.475 Chinchou in Southern coastal Manchuria was vital to Chang Hsueh-liang’s forces and was very near the rival railhead Chang was building at

474. Crowley, Japan’s Quest for Autonomy, pp.134-5.
Hulutao. The official explanation of the Japanese government for the bombing of Chinchou also alarmed Washington as it blamed anti-Japanese feeling in Manchuria and China proper for necessitating the “self-defense” activities that began on September 18. More troubling still was the language that equated boycotts on Japanese goods in Shanghai with “intimidation and violence,” and the clear call for Chinese to “spontaneously” organize in contravention to Nationalist rule.476

The U.S. moved from its initial studied non-reaction to the incident because it appeared that the Wakatsuki-Shidehara cabinet could not manage its own military. Secretary of State Stimson’s first approach was to defer to Shidehara and not involve the U.S. in an initial British proposal for a group of inquiry consisting of military attaches of neutral powers in China to go to Manchuria and pressure for settlement.477 Stimson contended that Japan was divided into two groups: the moderate Wakatsuki cabinet and the “rampageous army.” He said his job was “to let the Japanese know we are watching them and at the same time to do it in a way that will help Shidehara, who is on the right side, and not play into the hands of any nationalist agitators on the other.”478 Instead, initial American dithering fueled the Kwantung army and General Staff adventurers who attacked Chinchou, and may have increased the distance between Great Britain and the U.S. that grew more pronounced throughout the crisis.479 Japan’s air attack on Chinchou

477. This proposition was made by the British representative at Geneva, Lord Cecil, shortly after the 17th of September. He later recanted this confrontational impulse and conformed to the general British opinion that Japan should end the affair shortly on its own after “her rights were secured and the punitive mission accomplished.” Armin Rappaport, Henry L. Stimson and Japan, 1931-1933, (Chicago, IL: University of Chicago Press, 1963), p.20.
478. Henry Stimson, quoted in Ogata, Defiance in Manchuria, p.72.
479. The British position was influenced by its own large economic interests in China, its conservative, Tory government under Ramsay MacDonald and the economic depression. Much of British opinion was
did impel a stronger U.S. reaction, however. Stimson arranged for the League of Nations to invite American participation in its deliberations on the situation, and helped it set a November 16 deadline for Japanese troop withdrawals in the League's October 24 Resolution.480

The Japanese ignored this deadline and pressed southward with their army, prompting an American review of Japan's domestic politics that concluded, "the army has practically autonomous power in military matters in crisis...direct access to the emperor makes it difficult for adequate control of the military by the Cabinet in such a situation as present."481 Due to the seeming reign of militarists over Japan's policies and the recent increase in Japanese orders of raw cotton from the U.S., the Stimson State department ordered a lengthy review of the desirability and efficacy of economic sanctions.482 These reports prepared by Stanley Hornbeck, drew on prior research noting Japan's dependency on the U.S. and the moderating effect this relationship had on sympathetic to Japan's position that "lawless" Chinese actors threatened vital economic activities and stability. These factors help account for Britain's hesitancy in acting forcefully against Japan throughout the crisis. Ogata, Defiance in Manchuria, pp.71-2; Rappaport, Henry L. Stimson and Japan, 1931-1933, pp.18-20. Leo D. Sturgeon, U.S. Consul at Tokyo, reported similarly on November 7, 1931, noting in particular that U.S. investments in China were one-fifth those of Britain and scattered geographically and by industry. Britain's investments were larger and in more direct competition with those of Japan. The negative effect of the Chinese boycotts on Japanese goods coupled with the drop in the value of the British Pound when it left the gold standard in September 1931 and higher tariffs in India all acted to hurt Japanese interests vis a vis Britain, such that Britain did not want to be seen as further capitalizing on Japan's situation by sanctioning it. See memorandum from Leo D. Sturgeon, U.S. Consul at Tokyo, to Secretary of State, November 7, 1931 in Hornbeck Papers, Box 369, Folder: Sanctions.

480. Ogata, Defiance in Manchuria, p.88; Barnhart, Japan Prepares for Total War, p.53
481. Memorandum prepared by Far East Division, State department for Secretary of State, "The Reported coup d'etat in Tokyo-Control of the Military in Japan by the Cabinet." November 30, 1931, in Hornbeck Papers, Box 251, Folder: Tokyo Coups d' Etat. This report noted the conspirators in the October coup were released "possibly because they could not be punished without the matter becoming public or possibly because the temper of the army at the present would render unwise such a procedure."
482. Large increases in Japanese raw cotton purchases were "interpreted to mean that Japan either expects possibly to use cotton for war purposes or is indulging in "preparedness" against a possible imposition by the powers of economic sanctions." See Memorandum from Stanley Hornbeck to Secretary of State, November 21, 1931, in Hornbeck Papers, Box 369, Folder: Sanctions. Hornbeck noted information drawn from Dr. Herbert Feis of the State department's Economic Adviser office.
Japan’s foreign policy. In the present circumstance, however, Hornbeck concluded that Japan’s military had become dominant in policy making, that they were intent on complete control of Manchuria, that they would not be “deterred by moral suasion,” and finally, they were forcing the other powers of the world to either “put up or shut up.” He recommended non-recognition of any treaties signed between Japan and Chinese signatories (i.e., puppets in Manchuria or coerced Nationalists) and the imposition of date certain enforcement of an “economic boycott” against Japan if it did not pull back.

Action on the economic boycott was to come from the League of Nations, whose Article 16 expressly called for severing trade or financial relations with violators of its charter proscribing war among members. Hornbeck took special care to mention that the impression by League members that the U.S. would not participate in economic sanctions needed to be countered. To this end, he defined an economic boycott for the Secretary of State for his deliberations with President Hoover to achieve this coordinated world sanctions effort. He noted, “an economic boycott is a weapon. It may or may not be regarded as a weapon of force; it is certainly not a weapon of “war.” It is a weapon midway between a weapon of “moral force” and a weapon of “physical force.”

483. See Memorandum, “Japan’s Trade with the U.S. is of vital importance to her.” from Stanley Hornbeck to Secretary of State, June 14, 1930, in Hornbeck Papers, Box 252. Folder: Japan: Trade. In this memo Hornbeck notes that one-sixth of Japan’s population is directly dependent on raw silk exports to the U.S. and any cutoff would result in “paralyzed economic life.” Hornbeck also noted that American cotton was necessary for mixing with Indian and Chinese cotton in Japan’s making of yarns and cloths for export. Hornbeck noted Japanese dependency in iron, petroleum, tin, aluminum and scientific apparatus, but added that Japan learned from WWI to end its weakness on iron and steel. He also stressed Japan’s reliance on trade surpluses with the U.S. to finance international debts.

484. See Memorandum, “Manchuria Situation,” from Stanley Hornbeck to Secretary of State, December 5, 1931, in Hornbeck Papers, Box 369, Folder: Sanctions. Also located at file 793.94/4314, RG59

485. For his part, Hornbeck doubted the willingness of Britain to act forcefully against Japan provided Japan reassured them that their interests in China were not in jeopardy, which Japan did. See McCarty, “Stanley Hornbeck and the Far East,” p.33.

Secretary Stimson needed this distinction because President Hoover was disinclined to use economic sanctions, equating them to acts of war which he was not prepared to engage in.\textsuperscript{487} For their part, the British were not interested in considering economic sanctions under any auspices. Foreign Secretary John Simon summarized British policy: “Policy-conciliatory to Japan. To China-Don’t rely on others: play your own part. Don’t seek to transfer to Art. 16. To Japan-We don’t want to apply sanctions.”\textsuperscript{488}

In his December 6 analysis of sanctions, Hornbeck made several important observations and justifications for sanctions. First, with coordinated League-U.S. pronouncements, the threat of actually implementing sanctions would itself likely bring about Japanese restraint and compliance. Second, Japan’s dependence on silk exports to the U.S. and imports of cotton, oil, rubber and chemicals rendered it highly vulnerable to pressure, particularly over time when its credit position abroad would suffer. Japanese agrarian dependence on the U.S. silk market itself was a powerful bilateral weapon that the U.S. could use without suffering much domestically, as it had in 1918. U.S. insulation was dramatically pointed out by Hornbeck when he noted “a considerable

\textsuperscript{487} In fact, President Hoover opposed economic sanctions early in the deliberations with his staff and the British during discussions in mid-November 1931. He and the British gave several reasons including the world depression which didn’t need any further impulse downward. Hoover also resented the likelihood that sanctions would be uniquely the responsibility of the U.S. to enact due to the greater volume of Japanese trade with the U.S.. See Rappaport, Henry L. Stimson and Japan, pp.91-2. In early December 1931. Hoover said economic sanctions “meant all the penalties of war except the shooting. Sanctions or the threat of them also meant rising emotions, the development of incurable hatreds, and an insensate opposition to any remedial action.” Hoover quoted in Louria, Triumph and Downfall, pp.196-7.

majority of the personnel engaged in this trade (silk) are Japanese. The shipping and trade interests which would be affected first of all are a comparatively small group in the sum total of American economic life."  

Pointing out that Japanese-Americans and alien Japanese citizens in America would bear much of the economic dislocation caused by any U.S. silk import block may have assuaged some administration officials reluctant to impose sanctions. It did not, however, alter President Hoover's steadfast and principled opposition to economic sanctions regardless of Japan's behavior. The final argument for sanctions was the prescient contention that if economic sanctions were not "given serious consideration and if the effort of the Powers fail, the historians will attribute to the United States no small share of the blame for the failure." Hornbeck concluded that this failure and the consequent appeasement of the militarists in Japan would jeopardize peace and stability in Asia. It is likely that these statements were somewhat self-serving as both Hornbeck and Stimson knew Hoover was opposed by principle to sanctions. Nonetheless, they remain important policy reservation markers. They implicitly question why sterner American actions on the order of the November 1918 cotton and silk licensing restrictions were not taken, and they note the consequences of inaction on Asian stability and American culpability.

As the U.S. was debating sanctions, Japan's behavior grew more alarming. In early December, the Kwantung army fabricated attacks on its forces near Tsitsihar and Tientsin, South of the Great Wall, and advanced its positions in these areas, forcing the

489. Hornbeck December 6 memorandum, p.13. This insulation was only countered by U.S. suffering that would result in narrow exports of cedar, douglas fir and hemlock trees, cotton, automobile parts, tin plate and oil. Hornbeck concluded these costs would be minimal to the U.S. given their small exposure to Japan's market.

490. Hornbeck December 6 memorandum, p.3
General Staff in Tokyo and Shidehara to accept their gains and manage the international fallout. Secretary Stimson had several pointed exchanges with Shidehara and Japan’s ambassador to the U.S., Debuchi Katsuji, and could only conclude that the situation in China was “in the hands of virtually mad dogs.” For his part, Shidehara tried to reassert control over the Kwantung army through General Staff assurances that control and restraint would be affected, while placating a wavering League and petulant U.S. with acquiescence to an investigatory commission but not mediation of the conflict (i.e., the Lytton Commission). This delicate balancing act proved unsustainable, as an understanding between China and Japan on Chinese force withdrawals around Chinchou fell apart and War Minister Minami and Chief of the General Staff Kanaya demanded that Shidehara recognize the futility of international conciliation. The Wakatsuki cabinet fell on December 12, 1931, “unable to fuse two strands of Japan’s foreign policy—cooperation with the Western powers, and consolidation and extension of her special position in Manchuria.”

Japan’s Senior Statesman and last remaining Genro, Prince Saionji, engineered a compromise cabinet led by Seiyukai stalwart Inukai Ki, but not the Seiyukai party leader Suzuki Kisaburo. Suzuki was seen as too beholden to the Kwantung army’s vision for Manchuria and likely to destabilize Japan’s relations with the West due to excessive army

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492. Ibid., p.149
493. Saionji’s role in maintaining Japanese democracy and party politics was pivotal according to Hayashi Kentaro; in fact, he contends, “it is owing chiefly to the decision of the genro, Prince Saionji Kimmochi, rather than to the efforts of the parties, that parliamentary rule was established at all.” Hayashi, “Japan and Germany,” in Morley, ed., *Dilemmas of Growth in Prewar Japan*, p.470.
Inukai was not immune from the same army pressures that ended the Wakatsuki cabinet and out of concern for domestic stability he sanctioned the Kwantung army’s moves into Chinchou on December 24, 1931. Similarly deferential to the new nationalist reality, the new Finance minister of the Inukai cabinet, Takahashi Korekiyo, followed Britain’s lead and ended Japan’s short-lived adherence to the gold standard. Takahashi embargoed further gold exports from Japan at the end of December, preserving what was left of Japan’s gold reserves. This defensive action was made necessary by the large volumes of gold exports over the preceding year and losses of value in the British holdings of Japanese banks due to the Pound’s devaluation following its own gold embargo in September 1931. This action would force the issue of financing government budget deficits to the fore in the coming years, but without having the ready access to American loans and trade surpluses as chief means of balancing the budget.

With the Kwantung army’s expansion into Chinchou, Stimson tried to affect joint action with the British condemning this expansion. His entreaties of the British went unanswered, and on January 7, 1932, Stimson decided to declare as U.S. policy the non-recognition of any “situation, treaty, or agreement” which results from violations of the Pact of Paris which both Japan and China had signed and was now being violated in

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494. Again, the Seiyukai party’s base in the agrarian sector (i.e., particularly “rural notables and ex-officials”) where the army was also strong led to this desire to restrain their undue influence. See Hayashi, “Japan and Germany,” p.469.

495. Inukai had been a leading Seiyukai spokesman against the London Naval Treaty’s comprising the “right of supreme command.” However, with the army invoking the same argument in Manchuria, Inukai was more inclined to moderate its demands and bow to Saionji and the Emperor who “viewed with apprehension” army meddling in domestic and foreign policy. Crowley, Japan’s Quest for Autonomy, p.150.

496. Japan’s gold reserves at the end of 1931 were only 470 million Yen, compared with 1,072 million Yen two years earlier. Britain had ended gold payments on September 20,1931 and closed its stock exchange the next day amidst financial panic. Allen, A Short Economic History of Modern Japan, p.109.

247
Manchuria. The British refused to second the pronouncement, rendering Stimson’s non-recognition policy somewhat stillborn. Their inaction stemmed from all of the factors noted above and their willingness to settle on Japan’s assurance that commercial privileges and rights (i.e., the Open Door) in Manchuria would be respected. Other European nations followed Britain’s deference to Japan and left the U.S. alone to joust against Japan’s expansion. This Tory government deference to Japan reminded many Americans of the bad old days of the Anglo-Japanese alliance, and in fact, British Foreign Secretary Sir John Simon actually spoke fondly of Japan’s role as stabilizer of their joint interests in Asia. Winston Churchill summarized the prevailing British position on coordination with the U.S. against Japan nicely:

There was a rueful feeling in some British circles at the loss of the Japanese Alliance and the consequential weakening of the British position with all its long-established interests in the Far East. His Majesty’s Government could hardly be blamed if, in their grave financial and growing European embarrassments, they did not seek a prominent role at the side of the United States in the Far East without any hope of corresponding American support in Europe.

The Stimson doctrine did have a concrete economic component—a bilateral loan ban against Japan by the U.S. and multilaterally under U.S. pressure. This ban was Hornbeck’s idea and built on the State department’s “informal” approval system for foreign loans, and is consistent with both offensive and defensive realist contentions that

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497. Stimson also announced this policy without reviewing it thoroughly with President Hoover, probably in an effort to bind Hoover to more forceful action against Japan.
499. Ibid., p.103. Britain’s abandonment of coordinated action with the U.S. was a very partisan affair in Britain, but the dominant newspapers and conservative government prevailed in isolating America’s policy in Asia. Hornbeck had feared precisely this Anglo-American discord in October 1931 when he noted that Britain would likely oppose strong action against Japan if Japan promised to respect British interests in the Far East. See summaries of Hornbeck memoranda October 16 and 17, 1931 in McCarty, “Stanley Hornbeck and the Far East,” p.33.
exchange should change with increased threat. Hornbeck declared, “no encouragement be given to American financiers to make loans to the Japanese until the development of more satisfactory evidence concerning their intentions in Manchuria.”501 This did not mean, however, that the American banking community accepted the policy without reservation. J.P. Morgan & Co., for example, refinanced a short-term loan to the Yokohama Specie Bank three days after Stimson’s declaration of the non-recognition policy. Although this refinancing was closed out by March 1932, it did highlight the initial unwillingness of many financiers to follow the State department’s policy.502 As with prior governmental guidance away from loans to the South Manchuria Railway Co., Japanese inquiries for American loans were met not with stern linkages to their invasion of Manchuria. Rather, they were informed that Japan’s international credit position appeared doubtful given its ending of gold exports and declining trade surpluses, and therefore obtaining loans during depressed economic activity would be unlikely.

501 Hornbeck, quoted in Wilson. American Business and Foreign Policy. p.234. Hornbeck also cautioned that the U.S. should not get out ahead of the other powers too much, particularly if the U.S. was not prepared to back up its insistence that the peace treaty’s (i.e., Pact of Paris) principles be observed. Hornbeck memorandum, January 12, 1932. cited in Rappaport, Henry L. Stimson and Japan, p.105, footnote 77. Hornbeck termed the loan ban a “fine economic weapon in the diplomatic contest...regarding Japan’s methods in handling the Manchurian problem.” Hornbeck memorandum, January 21, 1932, quoted in ibid., p.120.

502 Initial responses to Japan’s invasion of Manchuria by U.S. bankers were even more bold. Thomas Lamont of J.P. Morgan, head of the American group in the China consortium, blamed the Chinese for the incident because they withheld loan payments to Japan and used the money to instead build rival railways in Manchuria in violation of existing treaties between Japan and China. Lamont noted: “China has conducted the most lawless and aggravating course possible. Yet they have an extraordinary knack of making an effective yell to the public when anything happens.” Lamont helped Japan’s Finance minister Inouye obtain publicity justifying Japan’s self-defense in Manchuria and rejected the proposal for loans to China. National City Bank officials were even more craven in their support of Japan. John Curtis, manager of Japanese and Manchurian branches, lobbied for U.S. recognition of Manchukuo beginning in 1933. See Wilkins, “The Role of U.S. Business,” pp.353-359. American auto companies also appeased Japan by transferring corporate control of their auto subsidiaries in Manchuria from China to Japan. General Motors, for example, removed Manchuria from the jurisdiction of its China subsidiary and placed it under General Motors, Japan Ltd. See William B. Ashbaugh, “The Yardstick of Trade: The Far Eastern Division and American-East Asian Relations.” (Ph.D. diss., Temple University, 2000), p.114.
Anglo-American relations became starker with the Japanese navy’s attack on Shanghai beginning on January 29, 1932. Earlier clashes engineered by Japanese army officials set the predicate for naval action to suppress Chinese boycotts of Japanese goods and threats to Japanese lives and property in Shanghai. Admiral Shiozawa Koichi ordered the air attack on the Chapei district of Shanghai after marine landings in Shanghai encountered resistance. Because of the army’s successes in Manchuria, the navy “was eager for action to gain for itself a reputation equal to that of the Kwantung army.” Unable to squelch Chinese resistance on their own, Navy Minister Osumi Mineo asked for army support and after some inter-service wrangling a large expeditionary force under Imperial sanction was dispatched to Shanghai on February 8, 1932.

The disproportionate use of air power against a largely civilian Shanghai district of Chapei alarmed the U.S. and stimulated a reluctant Britain to inquire about a joint Anglo-American response. The willing initiative of the Japanese navy in the attack greatly alarmed Western officials, who had previously counted on the navy to act “less

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503. For example, on January 18, 1932, Major Tanaka Ryukichi orchestrated an attack on Japanese priests at a company where there were militant anti-Japanese Chinese workers. Tanaka did this as a diversionary maneuver for Japan’s activities in Manchuria. See Shimada, “Extension of Hostilities,” p.307.
505. Public opinion against Japan in both the U.S. and Britain increased more in response to this incident than the invasion of Manchuria. See George McReynolds and Eleanor Tupper, Japan in American Public Opinion. (New York: The Macmillan Co., 1937) and Reginald Bassett, Democracy and Foreign Policy: a Case History of the Sino-Japanese Dispute, 1931-33, (New York: Longman’s Green, 1952), p.65. Only in late May 1932, did Japan withdraw the over 70,000 troops they added to the initial attack on Shanghai, but not before over 35,000 Chinese had died.
nationalist and more moderate, liberal, and internationally minded than the army.\textsuperscript{506}

More alarmingly, U.S. pilots were flying against Japanese naval pilots in defense of Shanghai and were shooting down Japanese planes. One U.S. pilot, Robert Short, an instructor for the Chinese Military Aviation Bureau, was killed after engaging Japanese forces on February 22, 1932. Short was serving the Chinese as a result of U.S. policy facilitated through Arthur Young, the Finance adviser to the Nationalist government.\textsuperscript{507}

Since the end of the China arms embargo, both the U.S. and Britain were competing to sell to and train the nascent Chinese air force, and with Japan’s actions at Shanghai the U.S. sought to end the conflict through a more united Anglo-American demonstration of resolve.

Despite these concerns, British Foreign Secretary Simon was not responsive to Stimson’s request for joint invocation of the Nine Power Treaty, discussion of an economic embargo, or deployment of British naval forces to Shanghai in support of American reinforcements ordered there on January 30.\textsuperscript{508} In their telephone conversation of February 6, 1932, Simon stated that it was “wise to keep away from” public discussion of economic sanctions under Article 16 of the League, while Stimson declared, “What I think I can hardly breathe aloud. I am willing to keep Japan guessing as to what we are going to do but that I don’t discuss, it is a little dangerous over the telephone even.”\textsuperscript{509}

\textsuperscript{506} Rappaport, Henry L. Stimson and Japan, p.113, footnote 20. See also Ogata, Defiance in Manchuria, p.33. The Japanese navy, in fact, opposed the army’s early moves in Manchuria and may only have bandwagoned with them at Shanghai after it appeared no Western repercussions were likely.


\textsuperscript{508} President Hoover signed off on naval reinforcements from the Asiatic Fleet after conferring with William Castle, Undersecretary of State, Hornbeck, Stimson, the army chief of staff, chief of naval operations, and the secretaries of War and Navy. Rappaport, Henry L. Stimson and Japan, p.119.


251

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Stimson believed a common position regarding some future economic action against Japan had been established at this juncture. Instead of movement in this direction, Simon assisted only in getting the League of Nations to endorse the Stimson non-recognition doctrine on February 16, 1932, while publicly renouncing speculation on economic sanctions by declaring in the House of Commons on February 21, 1932, that Britain would under no circumstance participate in an economic boycott or blockade against Japan.\(^{510}\) This further repudiation of Stimson’s designs for Anglo-American accord \textit{vis a vis} Japan led directly to Stimson’s letter of February 23, 1932 to Senator William E. Borah, Chairman of the Committee on Foreign Relations.\(^{511}\) Stimson contacted Simon by telephone on February 24\(^{th}\) to explain the content of his letter to Borah, which highlighted past British cooperation with the U.S. in Asia and on China matters in particular. In the conversation Stimson reiterated his desire and past request for joint notes from the two countries to Japan, and ended by lamenting Anglo-American discord. He said, “I have been rather sorry that the apparently good concert that we had in the beginning does not

\(^{510}\) \textit{Ibid.}, p.140. There is still considerable debate as to whether Simon did indeed fully rebuff Stimson on jointly invoking the Nine Power Treaty. Simon contended that he merely left the joint invocation matter to be determined after the February 16\(^{th}\) League non-recognition statement. See Borg, \textit{The U.S. and the Far Eastern Crisis}, p.14.

seem to be quite as easy now.” 512 Mutual recrimination and tension would fester over this event over the coming years, and color Anglo-American diplomacy toward Japan at critical junctures. 513

The Borah letter made explicit U.S. policy objecting to Japanese “military aggrandizement...at the expense of China,” which was precluded by the Washington Conference treaties. It further noted the interrelated and self-denying nature of the commitments made in the Washington Conference treaties on naval arms, base fortification and respect for Chinese sovereignty. Stimson declared, “No one of these treaties can be disregarded without disturbing the general understanding and equilibrium...by the group of agreements arrived at in their entirety.” Stimson then stated that U.S. renunciation of its naval buildup in 1922 and non-fortification of Guam and the Philippines were predicated on all of these treaties being adhered to. 514

Stimson left open the implication of this statement and Japanese press and officials interpreted it as bellicose, precipitating statements by Japanese officials of likely conflict between Japan and the U.S.. For example, Vice Admiral Nomura declared anti-American feelings in Japan to be rising because of the Borah letter and warned that “a


253
dangerous situation may develop.\textsuperscript{515} U.S. ambassador to Japan, William Cameron Forbes, stated that the Borah letter was impairing relations with Japan, suppressing moderates inside Japan, and most importantly, any “economic boycott as such is suggested in the U.S. by people looked upon here as responsible is openly regarded as tantamount to war.”\textsuperscript{516} Forbes and the other Western ambassadors in Tokyo recommended that the U.S. should ease its stance toward Japan and allow Japanese domestic financial pressure and quiet diplomacy to foster the reassertion of moderate Japanese to influence (i.e., the new Finance minister, Baron Takahashi, Admiral Kato and Count Makino).\textsuperscript{517} Hombeck rejected Forbes’ analysis and policy recommendations, contending instead that “the whole governmental machinery of Japan, including the Diet, is at present under the dominance of the military party backed by an enflamed public opinion.”\textsuperscript{518} This government was attempting to intimidate not only the U.S. and Britain, but also the League, into non-action with threats of war if sanctions were enacted.

Hombeck questioned the ambassadors’ tremulous advice by noting the high stakes of

\textsuperscript{515} The same day of publication of the Borah letter the press reported Senate Naval Affairs Committee approval of a $1 billion ship construction bill. The combination of the two events helped Tokyo to accept the League call for a truce and conference on February 29, 1932. See Memorandum, “The Tokyo Situation,” by R.S. Miller, approved by Hombeck, to Secretary of State, March 2, 1932, in Hombeck Papers, Box 251, Folder: Tokyo Situation; Rappaport, Henry L. Stimson and Japan, p.143.

\textsuperscript{516} William Cameron Forbes, U.S. Ambassador to Japan, to Secretary of State. February 27, 1932, in Hombeck Papers, Box 251, Folder: Tokyo Situation.

\textsuperscript{517} This account differs from Barnhart’s principally because he concludes that the U.S. government “was certain that Manchuria’s seizure had been perpetrated by irrational men and that its absorption was sure to ruin Japanese finances.” Barnhart, Japan Prepares for Total War, p.63. The Far East Division at the State department was well aware of Japan’s “rational” plans to annex Manchuria at least as early as 1928 and Benjamin B. Wallace of the Economic Adviser’s office clearly demonstrated Japan’s willingness and capacity to run the U.S. financial blockade. Although Barnhart notes Hombeck’s consistent and accurate position doubting other U.S. officials, he fails to note that key personnel who disagreed with Hombeck were reassigned out of responsibility (e.g., Ambassador Forbes in March 22, 1932).

\textsuperscript{518} R.S. Miller memorandum, “The Tokyo Situation,” March 2, 1932. Miller and Hombeck accepted Forbes’ assessment that the overwhelming majority obtained by the Seiyukai in the Diet elections of February 20, 1932 led to more aggressive policies abroad and a willingness to conflict with the U.S. (i.e., 301 Seiyukai seats to Minseito’s 147, a gain of 130 seats for the Seiyukai and a loss of 99 seats for the Minseito). And, unlike the constrained approach of former Finance minister Inouye and Shidehara, the Seiyukai were willing to provide the necessary budgets in these directions regardless of deficits.
inaction: "they do not see the effect of no action on the "peace machinery of the world"...no action might wreck the League and with the League the whole peace machinery of the world."^{519}

5.5 Founding of Manchukuo and dualism in U.S. policy

Fittingly, Hornbeck's memorandum of March 1, 1932, was the same date that the Kwantung army created the "independent" state of Manchukuo. Premier Inukai ratified this action on March 12, 1932, in response to the League of Nations' resolution to investigate the Manchurian incident in terms of the non-recognition policy. Inukai desired a period of domestic stability to quell the recent violence that accompanied Japanese military solutions to China policy. Former Finance minister Inouye was assassinated on February 9, 1932 and Baron Dan Takuma, head of the Mitsui zaibatsu and the chief Minseito supporter, was assassinated on February 23, 1932. With Hamaguchi's fatal wounding in November 1930 and these two executions, the vestiges of responsible Minseito internationalist statesmen were systematically being eliminated in Japan. The hatred for these officials by their junior army and navy officer assassins was predicated on their desire for a pure Imperial rule in Japan, which was being wholly corrupted by the zaibatsu, the party politicians, the nobility and their foreign associations.^{520}

The symptomatic example of these actors' assumptions about the interlocking corruption of Japanese government by party politicians and big business was the "dollar-

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^{519}. Hornbeck memorandum to Secretary of State, March 1, 1932, in Hornbeck Papers. Box 251, Folder: Tokyo Situation. Hornbeck did express again his serious reservations about getting out in front of Britain in challenging Japan as this would expose only the U.S. to Japan's feelings of resentment.  
^{520}. Crowley, Japan's Quest for Autonomy, pp.173-177.
buyer" speculation episode. As Japan’s fiscal position deteriorated in 1930 and 1931, it shipped large amounts of gold abroad to finance its trade and defend the Yen’s value, leading speculators to purchase U.S. dollars as a hedge against the reimposition of the gold embargo at a much lower dollar-Yen exchange rate. When the Seiyukai cabinet under Inukai was inaugurated, it reimposed the gold embargo and the Mitsui house in particular profited mightily, while the rest of Japan suffered.521 What is missing from this general and oft-cited account is the overwhelming role of the National City Bank in this episode of Japanese dollar, then gold, flight. Over the course of the crisis from 1930-1931, National City Bank sold 273 million Yen for dollars out of a total 760 million Yen sold to the Yokohama Specie Bank by all banks foreign and domestic. Mitsui, the banking house most blamed, sold 56 million Yen in the same period. Nolt summarized the effect well: “When the covert Big Four and foreign role in speculation against the yen became public knowledge toward the end of 1931, a campaign of vilification was organized."522 Because National City Bank’s speculation against and de-stabilization of the Yen was done on its own accord with no State department role, this event validates liberal and marxist interpretations.

Stimson went to Geneva in late March 1932 to attend the ongoing Disarmament Conference that convened in February. Ostensibly there to represent the U.S. at the talks, Stimson sought to improve relations with the British and focus League attention and pressure on Japan’s transgressions in China, including maintaining the discussion of possible sanctions. Stimson was deliberately injecting American power and prestige into

522 Nolt, "Business Conflict and the Origin of the Pacific War," p.333. National City’s role here may help explain why State department officials disliked it so intensely and also why National City bought the Japanese line in Manchuria, seeking to placate them in their expansion.
the international deliberations at the League of Nations just as he had done when he maneuvered to get American representation at the League meetings in late October 1931. These actions effectively overcame the U.S.'s formal non-member position in the League and placed American credibility and prestige on the line with the League's actions in Asia. Unfortunately, President Hoover had other designs for U.S. policy. In Stimson's absence, William Castle, Acting Secretary of State, made several decisions influenced by President Hoover. First, on March 29, 1932, Castle declared it State department opinion that U.S. aviation training missions to China were “inadvisable.” This message was sent by Castle to U.S. Consul General at Shanghai, Edwin Cunningham, but was not communicated to Arthur Young, financial advisor to the Nationalist government and lead negotiator for them on aviation assistance.523

Castle's initial blanket advisory was sidestepped by the Chinese National government. Through Young they negotiated instead with the U.S. Department of Commerce for aviation assistance. Castle was informed of his undercut position in middle April 1932, and meekly requested that only civilian aviation assistance be rendered to China.524 Despite this request, Young’s plan for U.S. assistance to China explicitly called for “military training of an advanced type,” and U.S. personnel who were “graduates of the United States Army Flying School...but at present on civilian status.” Due to the negative fallout over Captain Short’s demise in combat with the Japanese, U.S. aviators were specifically enjoined not to “participate in any belligerent

523. Xu, “The Eagle and the Dragon’s War Wings,” pp.112-4; Young, China’s Nation-Building Effort, p.352. Young contended that he never knew of State department disapproval.
action in case of declared hostilities." John Jouett was selected to lead the secretive assistance operation with the title, Principal Advisor on Military Aviation to the National Government of the Republic of China. He was selected because of his expertise as the former chief of the U.S. air corps office where he directed all U.S. military air corps training.

Negotiating through the Commerce department on the grounds of export promotion helped mask the strategic import of aviation assistance to China, and it is still not clear how this proceeded without contravention by Castle or the President. This training and airpower transfer to China would prove important to both China's military capabilities and conflict in U.S.-Japanese relations. Because of this and the purposeful direction of this transfer by Hornbeck, this action is consistent with offensive realism's emphasis on building the capabilities of states opposing an increasingly threatening rival and contra-indicates liberalism's propositions regarding corporate authority seeking to change decision sites to obtain their preferences. In this instance, Hornbeck changed the decision site and rationale for strategic trade to build China against Japan.

After the failure to lessen America's assistance to China, President Hoover instructed Castle to deliver a speech in early May 1932 that made clear U.S. policy on the

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525. Quotations from text of Aviation Plan for China, May 19, 1932 in Arthur N. Young Papers, Box 36, Folder: Military Aviation, Hoover Institution on War, Revolution and Peace. Stanford University. Stanford, California, hereafter cited as "Young Papers."
526. See letter from Arthur Young to Colonel, John Jouett, August 16, 1932, Young Papers, Box 36, Folder Military Aviation. Jouett had been implored into this service with statements that the U.S. government was requesting his service. See Xu, "The Eagle and the Dragon's War Wings," p.116.
527. It may be that Hoover allowed the training assistance with the understanding that it would stimulate aircraft exports and was only to be civilian in nature. It may also be that Hoover and Castle were outmaneuvered by Hornbeck, Stimson and Young who sought to build a more powerful counterweight to Japan in China and used the Commerce department as a domestic bypass of the Acting Secretary of State and President (i.e., realist change of decision site to affect relative power through exchange). These varying interpretations have not been resolved to date. Castle remarked in June 1932 that he would have raised objection had he known of the Commerce department-China negotiations, but since they had gone so far he resigned the State department to inaction. Xu, "The Eagle and the Dragon's War Wings," p. 118.
possible imposition of economic sanctions. Castle addressed the American Conference on International Justice on May 4, 1932, and said, "The President is vigorously opposed to the official boycott because he recognizes it for what it is, practically an act of war...a boycott implies a blockade and I know of no measure more certain to lead to war than blockade." Castle did, however, properly appreciate an economic boycott to "mean, of course, cessation of trade and communication for the sake of starving that nation financially and physically into submission to our will."\(^{528}\) His and Hoover's error in logic, of course, is the leap from economic sanction to blockade. It is not necessary to blockade a nation to pressure it through cessation of exports or imports, nor is it necessary to obtain multilateral compliance with a sanctions effort to affect the target. Principlsed obliviousness to these distinctions does not absolve Castle and Hoover of their culpability for yielding a publicly divided American policy toward Japan and resulting incoherence in the international approach to Asia.

Division among and within the Occidental powers did not pacify domestic nationalists in Japan, and with Premier Inukai's assassination on May 15, 1932, the reign of military officials instead of political parties was officially inaugurated.\(^ {529}\) Inukai's assassination and Admiral Saito's ascendance to Prime Minister followed the army's disaffection with the ending of Japan's assault on and occupation of Shanghai. Under the

\(^{528}\) William R. Castle address to General Conference of Methodist Episcopal Church, Atlantic City, NJ, May 4, 1932, in Hornbeck Papers, Box 369, Folder: Sanctions
\(^{529}\) Inukai's assassination was accompanied by other domestic terrorist acts, including the dynamiting of five public buildings by a group of fanatical naval and army officers and the plotting to attack the U.S. embassy and other American organizations. The decline of Japanese democratic practices (i.e., civilian supremacy over the military) was due to both military actors and career bureaucrats disdain for what they perceived as corrupt and self-absorbed rule by party politicians. Robert Spaulding noted: "Genuine democratic activity in prewar Japan was hampered less by bureaucratic elitism than by military terrorism, the shortcomings of all the political parties, and the insuperable constitutional obstacles to responsible government." Robert Spaulding, "The Bureaucracy as a Political Force," in Morley, ed., Dilemmas of Growth in Prewar Japan, p.79; Joseph Grew, Ambassador to Japan, to Secretary of State, November 15, 1933, Foreign Relations, 1933, Vol. III, p.711.
Armistice Agreement of May 1932, Japan pulled out the approximately 70,000 troops it had added to Shanghai after the battles there intensified in February. Saito’s selection represented stalemate between the army and navy in Japanese domestic politics, and also a desire to check “irresponsible” nationalist politicians, predominantly in the Seiyukai and the army, through somewhat more internationalist naval military leadership.530 Admiral Saito was the first naval Prime Minister since Admiral Yamamoto in 1924. His understanding of the politics of Japan’s vulnerabilities based on his naval experience and concern for energy autonomy led him to conclude new arrangements for oil supplies with Soviet Russia and to seek better relations with Britain.531

Japan’s outreach to Russia followed a renewed domestic cartel for refined oil products in Japan among the four dominant Japanese companies, Standard Oil of New York and the Royal Dutch. This effort was sanctioned by the Japanese government in August 1932 under its Important Industries Control Law and administered by the Ministry of Commerce and Industry.532 Nonetheless, Japan’s domestic oil production was still inadequate as it accounted for at most only 22% of crude and fuel oil acquired by Japan in 1932 (i.e., Japan produced 3.535 million barrels of crude and fuel oil and imported 12.281 million barrels).533 This is an increase in overall vulnerability compared

530 Crowley, Japan’s Quest for Autonomy, pp.178-180; Connors, The Emperor’s Adviser, pp.13-137; Scalapino, Democracy and the Prewar Party Movement in Japan, p.379.
531 Recent accounts of Japanese policy at this juncture in late 1932 note Japan’s desire to re-forge the bonds of common interest in China with Britain. As part of this calculated effort to reinvigorate Anglo-Japanese understandings over China, Japan ended the siege of Shanghai and sought to reassure Britain that its considerable economic interests in Shanghai and China proper would be scrupulously honored by Japan. See Kibata, “From the Manchurian Incident to Pearl Harbor,” pp.4-5.
533 See United States Strategic Bombing Survey (U.S.S.B.S.), The Effects of Strategic Bombing on Japan’s War Economy, Appendix A,B,C, (Washington, DC: U.S. G.P.O., December 1946), pp.135,141. 1921 was probably a peak year for Japanese domestic self-reliance as U.S. exports were low and crude production was high; therefore, this percentage represents the least vulnerability Japan could achieve given
with 1921, when Japan produced approximately 44% of total crude and fuel oil acquired that year.\textsuperscript{534} Because of concerns over this growing vulnerability and inadequate domestic production base, the Japanese government also negotiated with Soviet Russia for more oil supplies, primarily refined products of approximately 35,000 tons per year to be delivered from Soviet controlled areas around Baku.\textsuperscript{535} U.S. officials were aware of this effort and Japan publicly stated its desire for more Russian oil in order to reduce its strategic inadequacy due to dependence on American petroleum products.\textsuperscript{536} Japan was continuing its efforts to have secure and diverse oil supply sources and to forestall the effectiveness of any economic sanctions effort led by the U.S.. The previous asymmetric reliance and vulnerability of Japan on the U.S. was giving way by the late 1920s, as the U.S. sent increasing amounts of oil to Japan. By 1932, Japan was becoming a very important export market for the U.S. as it took in 17.3% of U.S. crude and fuel oil exports in 1931 for example, but this vulnerability was hardly reciprocal as Japan relied much more on the U.S. (See Tables 5.1 and 5.2).

\textsuperscript{534} Coumbe, "Petroleum in Japan," pp. 2-14.
\textsuperscript{535} Samuels, The Business of the Japanese State, p. 175; 35,000 tons of refined products is approximately 12,600,000 gallons.
\textsuperscript{536} See Naval Attache report from C. McCauley, Commander USN, Peiping, to Director ONI, September 2, 1932, Serial No. 302, File No. 103-100, File e-10-d, Register 13177F, RG 38.
<table>
<thead>
<tr>
<th></th>
<th>1929</th>
<th>1930</th>
<th>1931</th>
<th>1932</th>
</tr>
</thead>
<tbody>
<tr>
<td>From DEI to Japan in</td>
<td>94.557 (16.2%)</td>
<td>71.738 (11.3%)</td>
<td>71.968 (14.1%)</td>
<td>106.428 (15.9%)</td>
</tr>
<tr>
<td>millions of gallons (% of</td>
<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>total DEI crude and fuel</td>
<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>exports)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>From U.S. to Japan in</td>
<td>321.204 (N/A)</td>
<td>378.662 (N/A)</td>
<td>379.806 (17.3%)</td>
<td>414.246 (N/A)</td>
</tr>
<tr>
<td>millions of gallons (% of</td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>total U.S. crude and fuel</td>
<td></td>
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<td></td>
<td></td>
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<tr>
<td>exports) a</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>From North Sakhalin in</td>
<td>58.905</td>
<td>57.728</td>
<td>82.5</td>
<td>88</td>
</tr>
<tr>
<td>millions of gallons</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Minimum from other</td>
<td>N/A</td>
<td>27.4</td>
<td>27</td>
<td>27</td>
</tr>
<tr>
<td>sources in millions of</td>
<td></td>
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<td></td>
<td></td>
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<tr>
<td>gallons, including British Borneo, Manchukuo oil shale, Mexico and India b</td>
<td></td>
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**Table 5.1: Crude and Fuel Oil Exports to Japan, 1929-1932**

a. Crude oil exports from the U.S. doubled over the period from 104 million gallons in 1929 to 205 million gallons in 1932, while fuel and gas oil stayed roughly the same around 220 million gallons per year.

b. No data are included of exports from Mexico or India, but they are referenced in ONI reports as source countries.

Table 5.2: Gasoline Exports to Japan, 1929-1932

<table>
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<tr>
<th></th>
<th>1929</th>
<th>1930</th>
<th>1931</th>
<th>1932</th>
</tr>
</thead>
<tbody>
<tr>
<td>From DEI in millions of gallons (as % of total DEI gas exports)</td>
<td>0</td>
<td>0</td>
<td>53.608 (12.4%)</td>
<td>15.792 (4%)</td>
</tr>
<tr>
<td>From U.S. in millions of gallons (as % of total U.S. gas exports)</td>
<td>38.272</td>
<td>44.808</td>
<td>52.752 (2.9%)</td>
<td>41.622</td>
</tr>
</tbody>
</table>

The prices of DEI gasoline and crude were higher than other source countries pursuant to the Achnacarry accords of August 1928. Additionally, the output of DEI crude and refined petroleum products was decreased in 1931 due to the global economic slowdown and the decisions of the Achnacarry cartel. Partly because Japanese demand for refined products was further concentrating on the U.S., Japan sought the “red oil” contract with the Russians in August 1932 (i.e., partner diversification effort). This was not, however, Japan’s most significant search for greater energy security (i.e., synthetic fuels), nor was U.S. export to Japan unrestrained and driven by only earnings interests of the oil companies. Beginning at least in early 1932, the U.S. State department gave informal guidance to the Ethyl Gas Corporation of Philadelphia on its exports of ethyl fluid to Japan. The Ethyl Gas Corporation was a joint subsidiary of Standard Oil of New

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Jersey and General Motors and was the lead organization in the research and production of necessary inputs for high-octane aviation gasoline, including ethyl fluid. Japan sought large quantities of ethyl fluid from the corporation and its directors conferred with the Far Eastern Division of the State department for permission and guidance on the sale. Ethyl fluid was the key ingredient in rendering high octane (i.e., antiknocking properties) gasoline for military aircraft.

In March 1933, a director of the Ethyl Gas Corporation, Dr. Francis Patterson, informed the State department that an agent of the Japanese government had placed a large order with the corporation for ethyl fluid (i.e., at least two years worth of civilian and military usage). As it had for the prior year, the State department advised that either no sale should go forward or only “in extremely limited amounts.” This guidance was cleared through Stanley Hornbeck and represents a clear desire of U.S. policy to use trade to both limit and maintain control over Japan’s military capabilities, particularly in air power projection (i.e., prevent stockpiling). By supplying Japan’s minimal needs of an exclusive input to air power projection capabilities, the U.S. maintained a window onto Japanese intentions and prevented Japan from establishing alternatives (e.g., indigenous ethyl fluid production capacity or German licensing of same). The processes surrounding aviation gasoline production and the actual sale of aviation gasoline would become increasingly critical during the 1930s, and broad Standard Oil and Royal Dutch Shell cooperation would be maintained in this field through joint contracts to the U.S. Army air corps among other measures.

539 See memorandum for file, March 1, 1933 in Hornbeck Papers, Box 252, Folder: Japan, Trade.
The trade in ethyl fluid highlights an important facet of economic exchange analysis. No easily obtainable reference recorded how much ethyl fluid was exported to Japan in any of the years under review. However, it is a critical component of trade that affects military power directly and it has just been established that its export was under the direction of the State department and not subject to price, profit or other considerations by either the demanding state or supplying corporation. Additionally, the State department did not wait for Congressional authorization to limit export of important items at this time, nor does it appear to have consulted with President Hoover as to the effect of curtailing Japanese import demands on bilateral political relations. For these reasons, this event is consistent with offensive realism but not defensive realism because the U.S. continued to supply Japan for dependency maintenance purposes. Liberalism and marxism are contra-indicated in this instance, as the company did not attempt to fulfill its own exchange preferences or maximize profit through unlimited sales to Japan.

The overall trade relationship with Japan changed markedly after the Manchurian invasion and Shanghai incident. Japan went from an eight year trade surplus with the U.S. to chronic deficits beginning in 1932. The collapse in silk prices severely undermined Japan's ability to finance U.S. imports, and exposed Japan's underlying financial weakness, which the U.S. began to assess how to exploit in November 1932. In the most important U.S. capital exposure to Japan (i.e., Japanese national government foreign debts), the U.S. held only approximately 22% of Japanese government foreign debts).

540 The importance of the silk trade to the overall Japanese economy can not be overstated. The major trading firms and banks played an integral part in financing the silk industry development cycle and in organizing payment abroad. These funds helped the banks and trading firms expand their operations, and consolidated the position of the Mitsui and Mitsubishi trading companies as they controlled over 80% of the trade in silk. See Ohara, Japanese Trade and Industry, pp.294-298.
debt obligations in 1932. The new Ambassador to Japan, Joseph Grew, felt that the loan ban against all Japanese borrowers initiated in January 1932 was precisely the right tool because "continued financial pressure on Japan from abroad will in time destroy the chauvinistic influences." This bottom up pressure, liberal-based view of the constraining effects of a loan blockade was the subject of much contending analysis in late 1932. This analysis was driven by the pending release of the Lytton report in October 1932. Its findings were known by the U.S. to be damning of Japan, and might subsequently lead the League to call for action against Japan. One side of the U.S. debate led by Grew held that increased sanctions beyond the loan blockade already in force would be counterproductive and that subtle financial pressure over time would demonstrate the fiscal folly of the Manchurian invasion. Financial paralysis in Japan would then lead to the return of more moderate political leaders, inclined to cooperate with U.S. preferences in exchange for renewed financial exchange.

Hombeck led the opposing side and relied on Benjamin Wallace's analysis in the Economic Adviser's office at the State department. Wallace first dismissed Grew's claim that Japan could not finance the Manchurian invasion with the denigrating analogy that it "reminds one of the estimates made by bankers in 1914 that the European war could last

542 It may also have been the easiest tool to employ as the State department could informally execute it (i.e., control it) without much contention from other actors. Joseph Grew, quoted in memorandum from Benjamin Wallace, Economic Adviser State Department to Stanley Hornbeck, November 10, 1932, in Hornbeck Papers, Box 369, Folder: Sanctions.
543 See memorandum by JEJ and VDM, Far Eastern Division State department to Hornbeck, October 14, 1932, in Hornbeck Papers, Box 369, Folder: Sanctions. This memo notes that if Japan is found guilty and rejects League recommendations and negotiation with China, the League will "be compelled to consider sanctions" to get Japan to live up to its treaty commitments.
a maximum of six months." Wallace highlighted the economic difficulties that Japan faced when it began the invasion of Manchuria, noting both that they were likely one cause of the invasion in the first place and that they were much less stark at present (e.g., silk prices had recovered somewhat in summer and fall 1932). Wallace then pointed out that Japan had been given no assurance of renewed credit lines for compliance with U.S. preferences, nor had anyone inquired whether Japan would even prefer that to pursuing its own interests in Manchuria and defaulting on the approximately $60 million in annual payments on its foreign debt. Wallace noted that not strategically purposive tariff increases on some Japanese goods were already underway (e.g., Hawley-Smoot) and impelling Japan to push harder in Manchuria to make up the losses. Only by making these tariffs and other trade restrictions explicitly tied to its Manchurian behavior might Japan retreat. Finally, Wallace held: "history shows some attempts at conquest which were beaten off; I recall no case in which the country with superior armament and organization abandoned a rich territory because it was proving expensive to complete the conquest. Japan will relieve the pressure if necessary by non-payment of foreign obligations, for which there are many precedents." Hombeck concurred with these assessments, but was undermined in planning for coordinated action with the League by President Hoover. In early November 1932, Hoover stated: "I will use full the moral strength of America, but I have made one reservation and that is we will join no movement that proposes to use military or

545. Ibid.
economic force in its attempt to prevent war. For that is a contradiction of method."

Hoover's position would help undermine concerted effort at the League, which reconvened in January 1933, to consider what action to take in response to the Lytton report. Secretary of State Stimson was informed that Britain and France were inclined not to support any strong economic action against Japan and Hornbeck was told by the Japanese ambassador in Washington that they desired America and the League to "close its eyes and turn its back and keep still, and give Japan a chance to work the thing out." In exchange for U.S. acquiescence, Japan promised that the open door principle of economic opportunity would be adhered to in Manchuria, including increased demand for U.S. cotton and machinery. As the League mulled over the language and actions in its final statement in late February 1933, the Japanese prepared to withdraw from the League and begin a new offensive against Jehol province in North China. On February 24, 1933, the League held that no member state would ever recognize the puppet state of Manchukuo and Japan's delegation at Geneva withdrew.

Sensing an opportunity to expose American vacillation on Asia and temper Stimson's blandishments, the British government declared a temporary unilateral arms embargo against both Japan and China on February 27, 1933. The British stipulated that they wished to consult with other nations on instituting a more lasting arms embargo and pointedly asked whether Stimson would join them. Stimson was forced to reply that the President, even if so inclined, did not have any statutory authority to embargo arms to any country. The British withdrew their temporary embargo on March 13, 1933, content

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546. President Hoover November 7, 1932 in Salt Lake City, UT, quoted in telegram from Hornbeck to American Consul at Nanking, November 26, 1932, in Hornbeck Papers, Box 369, Folder: Sanctions.
with demonstrating “conclusively to its domestic critics that other nations were not prepared to cooperate in an embargo and that the whole idea of an embargo was impractical.”548 Thus were ended the fleeting coordination efforts of the U.S. and Britain, ushering in the period of Anglo-American competition for influence in Asia and the continued ascendance of militarism in Japan.

5.6 U.S.-Japan Economic Exchange, 1929-1932

The broadening of trade and investment between the U.S. and Japan came to an end after the Manchurian crisis, and the political decision to lessen trade and investment was a cause of the economic slowdown not a consequence of it. For example, the U.S. allowed a $22.8 million dollar loan arranged by J.P. Morgan to the Taiwan Electric Co. in June 1931, well after the banking and financial crisis had begun but before Japan’s army ran “amuck” in Manchuria. Prior to the loan ban of January 1932, U.S. loans to Japan were large and helped Japan finance increased imports from the U.S. and Japan’s compliance with the London Naval Treaty. In this period, three U.S. loans were made to Japan totaling $105.25 million dollars. This was only 7.9% of total U.S. foreign loans issued during the period 1929-1932, the same percentage as for the earlier 1923-1928 period. This amount did not mean substantial U.S. vulnerability to Japan as less than 10% of U.S. loans went to Japan. Britain made only one loan to Japan during this same period for 12.5 million pounds, approximately $61 million dollars.549 Britain’s loan

548 Ibid., p.25
549 Data from Table 4.2 and Cleona Lewis, America's Stake in International Investments, p.630; Moulton, Japan: an Economic and Financial Appraisal, pp.488-9. British loan figure given in British pounds and
represented its post-London Naval Treaty commitment to Japanese government finance in May 1930. The U.S. share of Japanese foreign loans in this period was roughly 63%, signifying its majority position in Japan's foreign financing.

In trade, the U.S. retained its dominant position in Japan's trade while only marginally increasing its exposure to the Japanese market in certain items (See Table 5.3). For example, 18% of U.S. cotton exports went to Japan in 1931, up from 10% in 1924, while 17.3% of U.S. crude and fuel oil exports went to Japan in 1931, up from 12.7% in 1928.\footnote{550} Japan's export reliance on the U.S. decreased from its interwar peak of 42.5% in 1929 to 31.6% in 1932, while its import reliance on the U.S. increased from 29.5% in 1929 to 35.6% in 1932. In contrast, U.S. reliance on the Japanese trade increased in exports and remained roughly constant in imports. The U.S. sent Japan 4.9% of its total exports in 1929 and 8.4% in 1932, while 9.8% of its total imports came from Japan in 1929 and 10.1% in 1932. Although the importance of Japan in U.S. exports increased largely due to the depression's effects on other U.S. export customers, these overall figures still mask Japan's consistent strategic vulnerability to the U.S. for crude and fuel oil. Across this period, Japan imported between 65-70% of these vital items from the U.S.. As noted earlier, this dependency was reinforced by Japan's artful exclusion from meaningful oil production in the DEI in 1928, which facilitated Japan's wasting of capital investment in addition to maintaining its oil import vulnerability.

<table>
<thead>
<tr>
<th></th>
<th>1929</th>
<th>1930</th>
<th>1931</th>
<th>1932</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Total exports of Japan</strong> in thousands of Yen (as % of Japanese GDP)</td>
<td>2,148,619 (13.2%)</td>
<td>1,469,852 (10.6%)</td>
<td>1,146,981 (9.2%)</td>
<td>1,409,992 (10.8%)</td>
</tr>
<tr>
<td>Japanese exports to U.S. in thousands of Yen (as % of total Japanese exports)</td>
<td>914,000 (42.5%)</td>
<td>506,000 (34.4%)</td>
<td>425,330 (37.1%)</td>
<td>445,000 (31.6%)</td>
</tr>
<tr>
<td>Japanese raw silk exports to U.S. in thousands of Yen (as % of total exports to U.S.)</td>
<td>755,378 (82.6%)</td>
<td>398,715 (78.8%)</td>
<td>342,479 (80.5%)</td>
<td>360,149 (80.9%)</td>
</tr>
<tr>
<td>Japanese exports to U.S. as % of Japanese GDP</td>
<td>5.6%</td>
<td>3.7%</td>
<td>3.4%</td>
<td>3.4%</td>
</tr>
<tr>
<td><strong>Total imports of Japan in thousands of Yen (as % of Japanese GDP)</strong></td>
<td>2,216,240 (13.6%)</td>
<td>1,546,070 (11.2%)</td>
<td>1,235,673 (9.9%)</td>
<td>1,431,461 (11%)</td>
</tr>
<tr>
<td>Japanese imports from U.S. in thousands of Yen (as % of total Japanese imports)</td>
<td>654,000 (29.5%)</td>
<td>443,000 (28.6%)</td>
<td>342,290 (27.7%)</td>
<td>510,000 (35.6%)</td>
</tr>
<tr>
<td>Japanese imports from U.S. of cotton in thousands of Yen (as a % of total imports from U.S.)</td>
<td>276,358 (42.3%)</td>
<td>176,801 (40%)</td>
<td>153,701 (44.9%)</td>
<td>320,752 (62.9%)</td>
</tr>
<tr>
<td>Japanese imports from U.S. as a % of Japanese GDP</td>
<td>4%</td>
<td>3.2%</td>
<td>2.7%</td>
<td>3.9%</td>
</tr>
</tbody>
</table>

**Table 5.3: Japanese Exports to and Imports from U.S., 1929-1932**


271

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U.S. trade was still vital to Japan's overall trade balance primarily because the bilateral trade surpluses Japan enjoyed from 1922-1931 made Japan's overall trade deficits less than they otherwise would have been (See Table 5.4). This in turn lessened Japan's need to export gold to finance its trade or to import more capital through loans for the same need. Japanese exports to the U.S. were still largely concentrated in raw silk with these exports equaling approximately 80% of total exports to the U.S. across the period. Japan developed no alternative export destinations (i.e., approximately 99% of Japan's silk exports went to the U.S.), and this continued to be a source of potential vulnerability. Instead of reacting to this vulnerability through diversification, the Wakatsuki-Shidehara-Inouye government tied itself further to the U.S. by resuming gold exports in January 1930. They did this under the assumption that the record year of 1929 would be a norm, and large and growing bilateral dollar surpluses could be expected to cover Japan's overall trade deficit. Unfortunately, raw silk prices collapsed after 1929, while U.S. quantity demanded stayed constant, thereby distressing Japan's dollar earnings, and absent gold exports, its ability to pay for imports and previously assumed foreign loans. Japan's dollar earnings from silk peaked in 1929 at $356 million and were cut in half by 1931 when Japan earned only $163 million. This decreased dollar exchange would hurt Japan's ability to pay dollar loans and stimulate its post-Manchurian invasion search for new export markets and sources of Western currency.

551 Uyeda, Recent Development of Japanese Trade, p.30
552 A leading expert on Japanese trade and finance noted that the quantity of silk demanded was not related to price, as the price dropped beginning in 1930 but quantity demanded stayed relatively constant. Silk exports to the U.S. were not subject to any tariffs and, as noted earlier, their luxury goods status precludes any efficiency gains to other sectors. Laurence Dowd concluded, "failure of silk purchases to react to lower prices would seem to indicate that demand for that product was income elastic rather than price elastic." Laurence Dowd, "Japanese Foreign Exchange Policy, 1930-1940," (Ph.D. diss., University of Michigan,1953), pp.71, 438..
Table 5.4: Japan’s Overall and Bilateral Trade Balance, 1929-32

<table>
<thead>
<tr>
<th></th>
<th>1929</th>
<th>1930</th>
<th>1931</th>
<th>1932</th>
</tr>
</thead>
<tbody>
<tr>
<td>Overall trade balance of Japan in</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>thousands of Yen (Exports Imports)</td>
<td>-67.621</td>
<td>-76.218</td>
<td>-88.692</td>
<td>-21.469</td>
</tr>
<tr>
<td>Bilateral trade balance of Japan</td>
<td>260.000</td>
<td>63.000</td>
<td>83.040</td>
<td>-65.000</td>
</tr>
<tr>
<td>with U.S. in thousands of Yen</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Japanese Exports to U.S.-</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Japanese Imports from U.S.)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total U.S.-Japan trade as % of</td>
<td>9.6%</td>
<td>6.9%</td>
<td>6.1%</td>
<td>7.3%</td>
</tr>
<tr>
<td>Japanese GDP (Japanese exports</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>to and imports from U.S. as % of</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>its GDP)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

As Table 5.4 demonstrates, Japan’s total economic reliance on trade with the U.S. decreased across the period, as total trade with the U.S. was only 7.3% of Japanese GDP in 1932, down from the interwar peak of 10.3% in 1925. In contrast, the value of the total Japanese trade to the U.S. economy declined from .82% of U.S. GDP in 1929 to .67% of U.S. GDP in 1932. As in the previous periods, Japan’s asymmetric reliance on U.S. trade would mean greater strategic vulnerability for Japan to any cessation of trade with the U.S. U.S. exchange with Japan was broader than trade and loans in this period, however, as U.S. direct investment in Japan increased throughout and reached its interwar peak in 1931. Although there were American corporations in Japan prior to WWI (e.g., Singer Manufacturing Co., Standard Oil, General Electric, National City Bank).
Bank), the value of American foreign direct investment in Japan grew substantially only after the Washington Conference treaties. American direct investments were still not large compared with portfolio investments (i.e., loans and bonds to Japanese entities), but were by 1932 nonetheless substantial and contributing to Japan’s economic and potential military capabilities (See Table 5.5). The total number of American companies that had some type of ownership stake in Japanese companies was approximately 50, with 18 that were “fairly large.” Of the total $61,450,000 in American direct investments, at least $8.1 million was from U.S. oil companies, principally Standard Oil sales affiliates and the Associated Oil Company’s joint refinery with Mitsubishi built in 1931. The total amount of U.S. FDI in Japan was still small compared with total U.S. FDI abroad (i.e., less than 1%), and was not large compared to Japan’s overall economy or domestic capital formation.

General Electric and Westinghouse were large investors as well, operating through ownership stakes in Tokyo Electric Co. and Japan Electric Co., respectively. Many of the electrical company arrangements were concluded through the large zaibatsu Mitsui and Mitsubishi, although Westinghouse did also cede exclusive ownership of Japan Electric Co. to the Sumitomo zaibatsu in 1932. As noted earlier, Ford and General Motors invested in Japan in the mid-1920s and like most of these various American operations in Japan, they were geographically centered around Tokyo and Yokohama. The last new direct investment appears to be that of Otis Elevator Co. in

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555. Ohara, Japanese Trade and Industry, p.434; Lewis, America’s Stake in International Investments, p.188.
1932 when it established the Oriental Otis Elevator Company in conjunction with Mitsui. Although other countries also invested directly in Japan after WWI, "it must be admitted that American capital composed the greater part of foreign investments in this country during that period."557

Unfortunately, all that can be concluded about the types of FDI in Japan is that most of the U.S. investment in Japan was engaged in productive manufacturing, whether Singer sewing machines, automobiles or electrical products manufacturing.558 The next largest category was sales distribution investment, principally of Standard Oil. While increasing Japan's production capacity of refined oil products and transferring technical know-how, Associated Oil's joint venture that began in 1931 was built to operate at peak efficiency on California crude oil imports and therefore also reinforced Japan's crude oil dependency on the U.S..559 Nonetheless, from this assessment it can be concluded that U.S. FDI in Japan did add to Japan's material capabilities because most of it was engaged in production, some of which had substantial spillover effects to Japan's overall economic and military capabilities (e.g., auto production and oil refining technology transfer).

557 Ohara was referring to the entire post-WWI period. British and German firms led the list of countries with the next most numbers of foreign firms in Japan, but it is not known when operations began for these entities. Ibid., pp.419, 445.
558 Ibid.
<table>
<thead>
<tr>
<th>Type of Investment</th>
<th>Aggregate Amount, end of 1931</th>
</tr>
</thead>
<tbody>
<tr>
<td>Direct Investments</td>
<td>$61,450,000</td>
</tr>
<tr>
<td>Missionary and Philanthropic</td>
<td>$8,000,000</td>
</tr>
<tr>
<td>Portfolio, Japanese National Government</td>
<td>$161,935,000</td>
</tr>
<tr>
<td>Portfolio, Japanese Municipal Government</td>
<td>$43,130,000</td>
</tr>
<tr>
<td>Portfolio, Corporate with Government-guarantee (Loans to the Oriental Development Co.)</td>
<td>$35,409,000</td>
</tr>
<tr>
<td>Portfolio, Private Corporate (Loans to electric utility companies)</td>
<td>$142,715,000</td>
</tr>
<tr>
<td>U.S. Total Capital Exposure (TCE) to Japan</td>
<td>$453,639,000</td>
</tr>
<tr>
<td>U.S. TCE/Japanese Gross Domestic Fixed Capital Formation, 1923-1931</td>
<td>4.6%</td>
</tr>
</tbody>
</table>

Table 5.5: Cumulative Value of U.S. Investments by Type, Aggregate Amount end of 1931

As noted earlier, U.S. direct investments were not substantial compared with total U.S. direct investments in the rest of the world (i.e., .8%). Similarly, U.S. loans to Japan were only 7.9% of total U.S. loans, and at best, total U.S. capital exports to Japan between 1923-1931 were no more than 4.6% of total Japanese domestic capital formation. Therefore, while the benefits to Japan were substantial they were not

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560 This measure of U.S. total capital in Japan as a percentage of Japanese domestic fixed capital formation was calculated against the 1923-1931 period because this is when most of the U.S. investments specified above were made. This assessment probably overstates the U.S. amounts because some of the
excessive in terms of overall Japanese investment. To the extent there was any
vulnerability it was asymmetric, with the U.S. retaining its minimal exposure to Japan.
Nonetheless, it can not be denied that U.S. investment and loans assisted Japanese
economic growth and its growth in material capabilities far more than did the still
predominantly silk luxury trade the U.S. enjoyed. This is particularly evident in the
productive investment of the auto companies, which facilitated Japan’s later production
of military vehicles, and in the oil refining investment, which although small did transfer
some substantive capability to Japan.\textsuperscript{561} In the politically critical area of Japanese
national government foreign debts, the U.S. held only approximately 22\% of Japanese
government foreign debt obligations, with Britain retaining most of the remainder of
these historic obligations, some of which still dated back to the Russo-Japanese war
financing done on the European capital markets.\textsuperscript{562} America’s relatively small
percentage of Japanese government foreign debt, despite the fairly large U.S. loans in
1924 and 1930 to Japan’s government, should not obscure the fact that most of the new
debt issued in the period was done in the U.S.. This potential leverage did not, however,
affect Japanese decision makers as some U.S. policy makers assumed it would (e.g.,
Grew), although it did materially assist Japan’s government to finance expanded naval
construction after the London Treaty. Additionally, the majority of U.S. loans, all of

\begin{footnotesize}
\begin{itemize}
\item[562] See U.S. debt leverage calculations of Stanley Hornbeck, “American Investments in Japan,” November
7, 1931, in Hornbeck Papers, Box 252, Folder: Japanese Trade.
\end{itemize}
\end{footnotesize}
which were authorized by the State department, went to Japanese government actors, not private actors. This is inconsistent with liberalism’s emphasis on private capital and actor exchange.

Up to the Manchurian crisis, therefore, the U.S. contributed greatly to Japanese economic and military growth, somewhat supporting liberal propositions regarding investment and trade, and certainly questioning defensive realism’s emphasis on positional maintenance through denial of increased gains to a rival. For these reasons and the above trade analysis, the exchange relationship in this period can be categorized as broad and broadening up to the January 1932 loan ban instituted by the State department under Hornbeck’s recommendation. Beginning in 1932, exchange relations narrowed considerably and permanently in some areas with no further loans and only one more direct investment by Otis Elevator Co.. The gains in this period were large (e.g., trade surpluses) and still asymmetrically favoring Japan. Japan’s overall economy’s reliance on trade with the U.S. decreased, and its overall partner concentration with the U.S. decreased in exports and increased in imports. In this mixed assessment of decreasing overall reliance, Japan’s vulnerability was also growing throughout the period. This was particularly the case in its crude and fuel oil import dependency on the U.S., which the Associated Oil Co. investment and refining technology imports furthered.

563 It is more difficult to assess whether offensive realism and/or marxism apply in the expanded U.S. investment in Japan because one could argue that auto production increased Japan’s dependence on imported gasoline and deprived its military of supplies over the long-term. Similarly, there is no evidence that corporations or banks influenced Hoover’s decision not to use economic sanctions and the statements of support for Japan by U.S. banks do not appear to have resulted in exchange outcomes.
5.7 Summary: From Siberia Intervention 1918 to Japan’s Withdrawal from the League

The prospect of losing the expanded commerce between the U.S. and Japan did not deter Japan’s seizure of Manchuria as it had when coercively employed in 1918 to compel Japan’s retreat from Siberia. Instead, the use and possible use of American economic leverage proved a source of conflict within Japan’s domestic politics and between American businesses and their government. For example, in mid-January 1933 at the height of League debate on the Lytton report, the Singer Sewing Machine Co. was subject to a rioting Japanese workforce of at least 200 in Yokohama. The workers were engaged in a labor-management dispute, but the anti-American sentiment prevalent in Japanese public opinion, stoked by the government on occasion, had yielded a volatile situation that was only calmed after police and diplomatic appeals for calm. This violence mirrored the violence of the army’s young ideologues in Japan, and helped confirm U.S. officials’ desire to maintain the loan ban on Japan and evaluate other means of influencing Japan’s rapidly changing political structure.

The U.S. gained compliance with British and French officials on denying Japan new loans from 1932 forward, but overall relations with Britain were lower than any time since the pre-Washington Conference period. Recrimination over no joint action against Japan simmered in the years to come and would have profound effects on Anglo-American corporate and state relations vis a vis Japan. Governmental buckpassing, including at the League of Nations, on trade sanctions but enforcement of a loan ban on

564. See Staley, War and the Private Investor, pp.391-2. See also letter from Joseph Grew, Ambassador to Japan, to Secretary of State, April 21, 1933, Foreign Relations, 1933, Vol. III, pp.700-702. Grew held that hostility against the U.S., Singer and National City Bank were directed by the army to increase budgetary appropriations, despite the fact that the Soviet Union was their likely foe.
565. Wilson, American Business and Foreign Policy, pp.233-234
Japan illustrate the complex and mixed results from the return of rivalry and discord in Anglo-American relations in Asia. As in the immediate post-WWI period, Anglo-American rivalry centered on the interlocking issues of Chinese development, Japanese expansion, naval force issues, and oil resource control and trade. When the U.S. and Britain did cooperate, it often came at Japan’s expense.

This is not to say, of course, that Britain was America’s chief obstacle to effective sanctioning of Japan similar to that which helped the Hara government restrain the Japanese army in Siberia in 1918. Instead, the chief obstacle was President Hoover, who as a devout Quaker refused to threaten any part of U.S.-Japan trade relations because he deemed the probable consequence to be war (i.e., liberal-based policy). Hoover affirmed:

I have all along been inflexibly opposed to the imposition of any kind of sanctions except purely public opinion. The imposition of any kind of sanction, military or economic, would in the present state of mind of the Japanese people, provoke the spread of the conflagration already in progress and might even involve the United States...the whole doctrine of non-recognition is not alone a method of invoking world opinion but it is equally important in the phase that it avoids precipitant action....(and)relaxes a considerable amount of present tension.566

Hoover rejected the advice of his Secretary of State and chief Asian specialist Hornbeck, and instead stood solely on Stimson’s non-recognition policy and its consequent appeasement of Japan.567 He hoped that this approach would yield the return

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566. Letter from President Herbert Hoover to Secretary of State, Henry Stimson, February 24, 1933, in Hornbeck Papers, Box 369, Folder: Sanctions, Economic, emphasis added. A clearer justification of appeasement and confusing conflation of statecraft tools can only be found in Undersecretary of State Castle’s earlier musings. Hoover’s position did parallel leading U.S. business interests, including the banks and auto companies, who supported Japan’s position on Manchuria. From the above remarks it is clear, however, that Hoover was acting on the basis of his own principles and not those of some American commercial interests.

567. This account differs markedly from recent analyses. For example, after noting Hoover’s opposition to sanctions at one point in the Manchurian crisis, Barnhart declares, “in the end the Hoover administration did nothing. But its inaction was a result more of congressional opposition than of faith in Grew’s natural economic forces.” Barnhart, Japan Prepares for Total War, p.59. This analysis is fundamentally flawed as to who stopped what possible efficacious moves against Japan.
of more moderate leaders to Japan's government, but his administration undermined precisely these people with its loan ban and prior financial coercion during the London Treaty negotiations. Moderate Japanese foreign policy was undercut at home by disaffected agrarian and industrial workers in league with militarists who saw territorial expansion as the answer to Japan's resource constraints. The U.S. helped seal the fate of moderate Japanese foreign policy by denying the benefits of capital exchanges to the government of Japan and the western-oriented businesses that it had been engaging with great vigor since 1923. These groups and the political factions within the parties they influenced were among the most effective counterweights to militarism in Japan. With only trade relations and declining benefits from trade to show for interacting with the U.S., moderate Japanese elites were marginalized and weakened relative to army and, after Shanghai, navy imperialists. Those Japanese who accepted financial influence from abroad and sought to lessen domestic budgets (e.g., Inouye's effort to cut military budgets) in response to international financial constraints were removed from government and often from their earthly existence.

The United States chose to pressure Japanese moderates at the 1930 naval negotiations to enforce a distasteful arms accord on the Japanese navy. The U.S. furthered the appearance of imposing its will on Japan with the rather unseemly payment  

568. In defense of Hoover's appeasement, he may have felt that his administration pushed Japan too hard during the London Treaty negotiations and thus he reacted more passively after Manchuria because he did not want to further undermine Japan's moderates. This does not, however, absolve him then for passing on the loan ban which further undermined precisely these groups. Hoover and Stimson were both well informed of the tremendous civil strife in Japan during the Treaty ratification debates, and there is no record of Hoover asserting this rationale against greater economic pressure. See Oliver, "Japan's Role in the Origins of the London Naval Treaty," p.6.

569. Minseito party fiscal retrenchment and gold hemorrhages caused the further economic strife in Japan, and "those economically and socially dissatisfied" aligned with militarists; "an alliance between these malcontents and the military critics of civilian foreign policy. Perhaps this is the most crucial factor in the history of pre-1931 Japanese militarism." Iriye, After Imperialism, p.284.

281
for the arms accord in the form of the $71 million loan to the Hamaguchi government only after it signed the London Naval Treaty in April 1930. Subtlety in assuaging Japan's domestic politics and understanding, if even for only exploitation purposes, the army-navy rivalry was not demonstrated by the U.S. Instead, Britain, the Netherlands and the U.S. acted in concert to only symbolically include Japan in DEI oil development, while increasing U.S. company ownership through Standard Oil of New Jersey's concessions in 1928. The U.S. knowingly participated in this manipulation of Japan's legitimate quest for oil resource ownership, and chose to maintain, if not increase, Japan's resource vulnerability for future political purposes. A stronger pro-Japanese navy and oil interests position by united Anglo-American governments and corporate actors might have provided a heftier counterweight to the army imperialists who increased their domestic position after Chang Tso-lin's assassination in June 1928.570 This could have been achieved through more collaborative development of DEI oil resources. Instead, the Japanese navy was coerced by a U.S.-led Anglo-American negotiating stance in London. Thereafter, the U.S. placed its faith in ever-weakening civilian elites responsive to financial constraints, while Britain deferred to Japanese expansionism helping to ensure the perception among Japanese that the U.S. was the principal obstacle in its way.571

If the Japanese nation could have been co-opted into a stable Asian and world order, this opportunity receded with the navy's actions at Shanghai in late January.

570. It can be argued, however, that after the Manchurian invasion the lack of significant analysis to threaten limits on oil sales to Japan's navy was a small effort to appease this group. Instead, much of the analysis focused on silk export cutoffs that would undercut the army's base.

571. Joseph Grew noted, "it should be borne in mind that in 1930 the civilian and liberal elements in the Japanese government had reached their zenith, and have since then practically vanished." Letter Joseph Grew to Secretary of State, July 26, 1933, Foreign Relations, 1933, Vol. 1., p.381.
1932. From this point forward, leading U.S. policy makers came to conclude that Japan needed to be economically and militarily contained and efforts to differentiate domestic groups within Japan for strategic purposes lapsed. The economic containment of Japan proceeded with ever-increasing measures after the founding of Manchukuo, and led to the increasing economic dependence of Japan on the U.S. in particular in strategic goods. Because of the cessation of capital transfers to Japan and the gradual ending of U.S. foreign direct investment in Japan, U.S.-Japanese exchange during the 1930s was reduced to trade only, and later conducted on the basis of Japanese payment in gold and silver reserves for needed imports. The chief area of Japanese political and military dependence continued to be its oil dependency, and this would grow after 1932 and become more centrally controlled by the U.S. government. This consolidation did not occur seamlessly, however, as oil corporations and rival governments pursued disparate and often conflicting agendas.

Japanese aggression in China challenged the Washington Conference system, the policy preferences of the U.S. and the authority of the League of Nations. Japan's appeasement undermined the international authority of the League and Anglo-American understandings on Asia with far-reaching consequences. It is important to stress Japan's central role in ending any possible effectiveness for the League and setting back

572. Proponents of a possible U.S.-Japan peace, even as late as the Fall of 1941, contend that Japan could have been coopted if only the U.S. accepted their position in China, and for that matter, the DEI and all of Asia. See, for example, David M. Kennedy, Freedom from Fear: The American People in Depression and War, 1929-1945, (New York: Oxford University Press, 1999), pp.513-5,524-6. Kennedy holds, "Roosevelt's deepest failure, it might be argued, was his inattentiveness to Asian matters and his unwillingness to be seen as "appeasing" Japan, when in fact a little appeasement—another name for diplomacy—might have yielded rich rewards." Ibid., p.525.

573. Changing of the terms of payment was a part of U.S. balance of payments and finance pressure on Japan. It did have an effect on Japan's behavior in China. It stimulated territorial expansion in search of gold and silver to pay for needed imports which had risen in price with the Yen's devaluation, the end of Japan's bilateral trade surplus with the U.S. and export tariffs on cotton among other goods. See M.A. Aziz, Japan's Colonialism and Indonesia, (The Hague, Netherlands: Martinus Nijhoff, 1955), p.41.
coordinated deterrence by the leading democratic states for many years.\textsuperscript{574} The buckpassing behavior of the British and American hesitancy in challenging Japan unilaterally stand out at the end of this period, and differ markedly from America’s willingness to challenge Japanese expansion in 1918 and pressure Britain in Asia. These patterns would continue until Japan’s threat to both British and U.S. political and commercial interests became overwhelming in late 1937, inducing greater corporate and state coordination against Japan. U.S. assistance to China and increasing control of vital Japanese strategic imports became the focal points of the coming conflict whose true wellspring was the diametrically opposed visions of order in Asia. Japan’s desire for political and economic autonomy on the basis of military control of resources was met and possibly stimulated by increasing discrimination by the U.S. and then the coordination of Anglo-Dutch-American oil diplomacy. Once Japan moved south of the Great Wall in July 1937, this competition could not be resolved short of war because Japan refused to negotiate withdrawal from its hard-fought positions in exchange for “peaceful trade” with the U.S.

\textsuperscript{574} Winston Churchill captured it succinctly: “the moral authority of the League was shown to be devoid of any physical support at a time when its activity and strength were most needed.” Churchill, \textit{The Gathering Storm}, p.80.
FOR PROFIT OR POWER?
THE STRATEGIC PURPOSE OF ECONOMIC EXCHANGE
IN THE U.S.-JAPAN GREAT POWER RIVALRY

VOLUME II

DISSERTATION

Presented in Partial Fulfillment of the Requirements for
the Degree Doctor of Philosophy in the Graduate
School of The Ohio State University

By

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* * * * *

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ABSTRACT

The political and economic motivation for and effects of economic exchange among great powers has received considerable attention in recent scholarship. The question of whether states induce or control this exchange for policy purposes has, however, not been examined sufficiently, nor has the importance of any one type of economic exchange been shown to influence state decision makers in accordance with prevailing theoretical perspectives. This dissertation argues that these shortcomings are due to incomplete specification of economic relations among great powers as well as inadequate attention to the relationship among the actors involved in exchange, state decision makers and the policy making process. Too often, the causal relationship between economic interactions and state policy calculation is normatively assumed instead of demonstrated, or is applied only to cases of great power allies or between a great power and a lesser power. Within much of this analysis, defensive or liberal state policy motivation is ascribed, tested for its validity and found to be insufficient in one or more ways. This dissertation remedies this condition by fully examining exchange in a crucial great power rivalry and reintroduces other, offensive, policy motivations and a means of better identifying the qualities of exchange. A more holistic conception of economic exchange is proffered, one that balances qualitative assessment of trade with investment and other financial relationships, in order to better identify overall benefits and vulnerability from exchange relations.
The U.S.-Japan, 1918-1941, case is compared against contending hypotheses from defensive and offensive realism, liberalism and marxism. In beginning the analysis during WWI, evaluation of the theories is more complete and allows for better interpretations of U.S. policy and its effects on Japan’s domestic and foreign policies. This interpretation of U.S.-Japan economic and strategic interaction improves upon much of the prevailing political science literature, and adds needed and often overlooked explanations for U.S. economic exchange with Japan. Specifically, this dissertation demonstrates that despite often self-serving corporate maneuverings, the U.S. government used exchange with Japan to fulfill its interwar grand strategy and maximize its relative position going into WWII.
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<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>6.1</td>
<td>Chapter Overview</td>
<td>285</td>
</tr>
<tr>
<td>6.2</td>
<td>The Roosevelt Administration and Anglo-American Buckpassing</td>
<td>290</td>
</tr>
<tr>
<td>6.3</td>
<td>Post-Amou Statement: Britain and Russia Appease, Dutch build bridge to America</td>
<td>301</td>
</tr>
<tr>
<td>6.4</td>
<td>Japan's Movements toward Autonomy and America's Response</td>
<td>310</td>
</tr>
<tr>
<td>6.5</td>
<td>The International Situation: Intended and Unintended Consequences of Economic Alignments and America's Economic Policy</td>
<td>332</td>
</tr>
<tr>
<td>6.6</td>
<td>U.S.-Japan Economic Exchange, 1933-1936</td>
<td>348</td>
</tr>
<tr>
<td>7.</td>
<td>U.S.-Japan 1937-1941</td>
<td>357</td>
</tr>
<tr>
<td>7.1</td>
<td>Chapter Overview</td>
<td>357</td>
</tr>
<tr>
<td>7.2</td>
<td>Roosevelt Pacification Gambits and Japan's Assault on China</td>
<td>364</td>
</tr>
<tr>
<td>7.3</td>
<td>Casting About for an American Plan</td>
<td>377</td>
</tr>
<tr>
<td>7.4</td>
<td>The U.S. Position Firms as Japan Expands Against Britain and the Soviet Union</td>
<td>391</td>
</tr>
<tr>
<td>7.5</td>
<td>Japan Tacks South and Britain Bargains for America to Stem its Ebbing Resistance in Asia</td>
<td>416</td>
</tr>
<tr>
<td>7.6</td>
<td>America Squeezes Japan's Resources and Steps Up Japan's Strategic Encirclement</td>
<td>433</td>
</tr>
<tr>
<td>7.7</td>
<td>Japan Secures its Northern Front, Expands South and Earns a U.S. Embargo</td>
<td>444</td>
</tr>
<tr>
<td>7.8</td>
<td>U.S.-Japanese Economic Exchange, 1937-1941</td>
<td>461</td>
</tr>
<tr>
<td>8.</td>
<td>Conclusions</td>
<td>472</td>
</tr>
<tr>
<td>8.1</td>
<td>Overview of the Inquiry, Key Findings and Theory Evaluation</td>
<td>472</td>
</tr>
<tr>
<td>8.2</td>
<td>Relevance to and Implications for Previous Scholarship</td>
<td>489</td>
</tr>
<tr>
<td>8.3</td>
<td>Realist Exchange Theory, Application to U.S. Interwar Policy and the Prospects for a Realist Peace</td>
<td>495</td>
</tr>
</tbody>
</table>

Appendix A  Causal Model; Exchange Instruments Chart; Theory Hypotheses and Observable Implications Charts 503
LIST OF TABLES

<table>
<thead>
<tr>
<th>Table</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>6.1: Japanese Imports of Crude and Fuel Oil, 1933-1936</td>
<td>337</td>
</tr>
<tr>
<td>6.2: Japanese Imports of Gasoline, 1933-1936</td>
<td>338</td>
</tr>
<tr>
<td>6.3: Cumulative Value of U.S. Investments by Type, Aggregate Amount end of 1935/1936</td>
<td>350</td>
</tr>
<tr>
<td>6.4: Japanese Exports to and Imports from the U.S., 1933-1936</td>
<td>353</td>
</tr>
<tr>
<td>6.5: Japan’s Overall and Bilateral Trade Balance, 1933-1936</td>
<td>356</td>
</tr>
<tr>
<td>7.1: U.S. Exports to Japan of Iron and Steel Categories in Thousand Metric Tons</td>
<td>386</td>
</tr>
<tr>
<td>7.2: Exports of Pig Iron to Japan in Thousand Metric Tons</td>
<td>389</td>
</tr>
<tr>
<td>7.3: Japanese Exports of Gold and Silver, 1930-1940</td>
<td>410</td>
</tr>
<tr>
<td>7.4: U.S. Exports of Industrial Machinery to Japan, 1930-1940</td>
<td>413</td>
</tr>
<tr>
<td>7.5: Japanese Imports of Crude and Fuel Oil, 1937-1941</td>
<td>428</td>
</tr>
<tr>
<td>7.6: Japanese Imports of Gasoline, 1937-1941</td>
<td>429</td>
</tr>
<tr>
<td>7.7: Japanese Exports to and Imports from the U.S., 1937-1941</td>
<td>466</td>
</tr>
<tr>
<td>7.8: Japan’s Overall and Bilateral Trade Balance, 1937-1941</td>
<td>470</td>
</tr>
</tbody>
</table>
CHAPTER 6

U.S.-JAPAN, 1933-1936

6.1 Chapter Overview

Franklin D. Roosevelt’s inaugural on March 4, 1933, ushered in a new U.S. administration and approach to Asia policy just as Japan was withdrawing from the League of Nations and continuing its more unilateral policies in Asia. With these moves, the United States’ key decision makers began to focus less on internal divisions in Japan and began applying a simple holistic image of Japan as a highly threatening state dominated by a “military” party. In its own way Japan gradually did the same relative to the U.S., but still hoped to split Anglo-American accord. Roosevelt sought to build it by not getting out in front of British policy toward Japan. Instead, Roosevelt’s administration initially sought to aid China in a limited fashion as a counterweight to Japan’s expansion and any possible Anglo-Japanese rapprochement at China’s expense. The President also recognized Soviet Russia for among other reasons as a way to add complexity to Russo-Japanese relations. Roosevelt further understood that to build better relations with Britain a commonality of economic and strategic interests was necessary. He therefore sought to align further American business interests with Britain’s and concurrently with the Dutch in the DEI. Due to Dutch antipathy for Japan, these preferences bore fruit in the DEI with increased American oil corporation ownership.
there in 1934 and Dutch manipulation of Japanese investment designs using American corporations as cover. Despite Roosevelt's preferences for more cooperative Anglo-American policy in Asia, competition continued over the interlocking issues of naval arms limits, equitable economic relations including in oil matters, and, most importantly, China policy.

Japan's policies of increasingly open military and economic expansion in Asia (e.g., Amau Statement April 1934) benefited from Anglo-American discord, but also helped stimulate increased Anglo-American understanding of Japan's threat. This understanding did not stimulate coordinated actions to deter or rollback Japanese advances. Despite perceiving an increased threat from Japan, which grew particularly acute after its renunciation of naval arms limits in December 1934, the U.S. did not overreact and publicly alter its economic exchange with Japan. It did not do this because its "vital interests" in Asia were not yet at risk with Japan's moves against Manchuria, North China and possibly the Soviet Union. As both British and American corporations began to feel the sting of Japanese nationalist economic policies in Manchuria and Japan proper, their entreaties for governmental action were met with purposeful vacillation and buckpassing between the governments of America and Britain.

The most important exchange event regarded oil markets and the question of Japan's energy autonomy. In an effort to force action to protect oil company property and trade rights, Standard Oil and Royal Dutch first threatened to embargo oil shipments to Japan and then later to sell it coal hydrogenation technology, whose international rights to the German-owned patents they controlled. This possible transfer of synthetic fuel capability to Japan would have meant decreasing U.S. leverage over Japan due to its
crude oil import dependency. The U.S. government signaled its disapproval of the sale and soon brought Standard Oil to heel, but not before laying bare U.S. policy of denying Japan energy autonomy. At this juncture, the oil supply trigger for war crystallized in the discussions among U.S. government officials. Overt military considerations played an increasing role in U.S. trade during this period as well. This was most importantly viewed in the military aircraft sales to Nationalist China, which greatly upset Japan.

Japan reacted to this and other perceived affronts to its desires by seeking an entente with Germany, which led to the Anti-Comintern Pact of November 1936. This Japanese realignment had multiple objectives vis a vis Britain, the Soviet Union and China; among these were the acquisition of advanced German synthetic fuel and other chemical technologies. Prior to this strategic shift, the U.S. had limited Japan’s advantages in trade with the U.S. by increasing its import restrictions on Japanese goods, while also increasing the prices of its exports to Japan (e.g., cotton good export restraint agreements, increased tariffs and increased raw cotton taxes). U.S. action in the cotton trade increased Japan’s vulnerability to the U.S. by enlarging its trade deficit, hampering its exports and focusing more of its economic activity on finding alternative cotton goods outlets, thereby diverting its attention from possibly other more important economic considerations. More pointedly, by late 1935, the U.S. directed corporations not to invest any further in Japan, and thereby demonstrated U.S. intent to restrain Japanese capabilities and increase its vulnerability to U.S. actions.

The U.S. began its concerted effort to “ration” Japanese imports into the U.S. and related dollar-earning territories (e.g., Philippines) in 1933. The U.S. did so to reinforce Japan’s adverse trade balance and resulting need to consume its monetary assets to cover
needed U.S. imports. This monetary asset exchange increased in 1935 with the U.S. buying Japanese-acquired silver. The U.S. did export increasing quantities of necessary items to Japan, but it began to send cruder materials not refined ones ready for application even though these would have earned higher profits for the exporters. In this period, the U.S. also began to use formal embargos on critical materials (e.g., tin-plate scrap embargo in April 1936). The tin embargo was directed specifically against Japan, but had the possibly unintended effect of focusing Japan’s demand for this item back onto British concerns in Malaya.

In addition to other factors, the U.S. commitment to build one China paradoxically assisted Japan’s military in determining that attacking China preemptively was preferable to waiting for its economic and military capabilities to coalesce further around Chiang Kai-shek’s Nationalist government. The U.S. commitment to China in the period grew in direct response to further Japanese predations in northern China. Japan would eventually attack all of China in July 1937, finally stimulating both Britain’s desire to more fully align itself with the U.S. against Japan and more aggressive American preparation for the economic and military containment of Japan. As Japan gradually placed its economy on a total war footing, it experienced foreign exchange pressures due to trade restrictions in both the U.S. and Britain and its dominions. These restrictions, Japan’s adverse balance of trade, and its inability to secure foreign financing caused Japan economic hardships, but did not hinder its overall economic expansion during the period. Changes in Japan’s international payments position actually helped fuel its
military expansion and undermining of authorities in North China, as Japan extracted Chinese silver to ship to the U.S. and Britain to balance its bilateral trade deficits with the U.S..

These purchases, and Japanese trade more broadly, served several U.S. purposes even though they destabilized China and gave Japan needed dollar balances. First, they transferred malleable reserves (i.e., silver and later gold) to the U.S., preventing Japan's use of them for other purposes including procuring German technologies. Second, they demonstrated to Japan, the Dutch and Britain, that America could be relied on to supply Japan. This simple assurance would itself forestall any increased likelihood of Japan pressuring the DEI or engaging Britain more aggressively to realign with it on resource supplies and China, and against the U.S.. Third, U.S. supply enabled Japan to test its position in China against either or both Britain and the Soviet Union. The U.S. gained valuable intelligence on Japan's capabilities and intentions in these actions, and paradoxically helped confirm for the British that America was a better partner for protecting and advancing British interests in Asia by assisting Japan's capacity to threaten those interests.

Japan's economy expanded rapidly in this period as the development of Manchuria contributed to markedly better growth. This helped convince Japan that the costs of imperial autarchy (e.g., foreign resentment, pressure) were worth the perceived gains from policies promoting economic autonomy. Japan grew more asymmetrically vulnerable to the U.S. during the period because of the changes in the terms of trade in cotton and increased reliance on U.S. oil. Japan also relied more on the U.S. to advance its material capabilities during this period, but the U.S. government narrowed the breadth
of exchange considerably from its peak in the late 1920s. In the 1933-1936 period, the U.S. allowed Japan to gain more in the narrowed exchange through supply of oil, steel and machinery, even though the U.S. actively managed Japan's adverse trade balance with the U.S. Japan's economy grew rapidly, but its growth was still reliant on the U.S. and others outside the emerging yen bloc. By the end of 1936, for example, Japan was relying on the U.S. to supply 82% of its crude and fuel oil imports. Despite the somewhat unilateral and destabilizing actions of Standard Oil, the state affected exchange with Japan far more than corporations. Instead of severing trade with a threatening rival, the U.S. government used trade to squeeze Japan's finances and divert its economic activity in cotton goods in particular. For this reason, this period is most explicable under offensive realism, although oil company actions materially affected each state's security and threat perception of the other.

6.2 The Roosevelt Administration and Anglo-American Buckpassing

The Roosevelt administration came into office as Japan continued its expansion of army operations in North China, occupying Jehol province just north of the Great Wall in early March 1933. The issue of adhering to the prior Hoover administration's divisive policies on Asia or fashioning a new approach toward Japan was pressing on the new administration, but it was primarily viewed as a problem requiring multilateral coordination with British support paramount. Roosevelt's new Secretary of State, Cordell Hull, was personally inclined to have economic exchange relations used to foster
positive political ties among nations, including with Japan. President Roosevelt, however, was not disabused with basic liberal beliefs, and his primary assumption of Britain was that it always bargained hard and with an eye toward maximizing its own material interests at others' expense if necessary. This consideration fit nicely with the advice that Roosevelt received from Stanley Hornbeck, who had become even more influential in determining overall U.S. policy in Asia with the departure of Hoover and Stimson.

After observing Japan's aggressive persistence extending "Manchukuo" sovereignty to China's Great Wall, Hornbeck held the bilateral Chinese-Japanese truce negotiations in May 1933 to be premature and prejudicial to American interests. Hornbeck felt that the pending Tangku Truce would consolidate Japan's offensive position in North China leading to "either further coercion of China, or conflict with Russia, or conflict with the United States...In the long run our interests would best served by a complete exposure of Japan's program, her strength and/or weakness, and as complete as possible involvement of herself in the situation (in North China)." This statement captured the future set of Japan's strategic choices neatly; war with China, Russia and/or the U.S.. Japan would face this basic set of choices even more starkly in the early 1940s, and ultimately make a "rational" choice for war with the two powers that best suited its grand strategy. Hornbeck also clearly enunciated official U.S. policy

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577. For a recent restatement of this see Ashbaugh, "The Yardstick of Trade." pp.36-7.
578. Hornbeck quoted in Borg, The United States and the Far Eastern Crisis, p.35.
embracing China as a proxy conflict site wherein America could weigh and measure Japan’s capabilities and intentions for its own possible conflict with Japan.579

In order for America not to suffer Japan’s wrath exclusively, Hombeck advised Roosevelt to keep U.S. policy at a low profile, and particularly not to evince any overt public support of China against Japan. After the mutual castigation and posturing between the U.S. and Britain during the Manchurian expansion and Shanghai attacks, Hombeck advised that U.S. policy be strictly controlled so as to allow Britain to shoulder more of the responsibility in addressing Japan’s expansion into China. Underlying Hombeck’s cautious approach, which advocated less unilateral containment or coercive acts against Japan, was his understanding that if the U.S. were to have acted coercively against Japan, with oil embargos for example, this would have allowed the re-forging of Anglo-Japanese bonds of self-interest in China, and possibly elsewhere (e.g., a new Anglo-Japanese DEI oil agreement).580 If the U.S. pushed Japan it would alienate Britain with no commensurate gain for itself in Asia. Unlike America’s successful sanctions against Japan in 1918, Japan could have alternate suppliers of oil and cotton if Britain were coopted anew by Japan. The prospect of this was significantly higher due to Stimson’s heavy-handed and confrontational approach to Japan, which convinced many in Britain that America was recklessly pushing Japan toward conflict and possibly worse acts in China.

Roosevelt understood these possible deleterious effects and fashioned an Asian policy that haltingly followed Hornbeck’s recommendations. Roosevelt would seek to

580. Interestingly, Japan understood this as well and had fairly optimistic assessments of Britain’s willingness to agree to some “imperialistic division of spheres of interest in China.” Kibata, “From the Manchurian Incident to Pearl Harbor,” p.4

292
preclude U.S. actions that facilitated both further Japanese expansion into China and disagreements with Japan that benefitted Britain’s relations with Japan. This nuanced policy of “delay and inaction” sought to make transparent Britain’s own vulnerability to Japan’s expansion while not making the United States the only and constant obstacle to Japan’s desires.\(^5\)\(^8\)\(^1\) The economic exchange strategy fulfilling this policy had the U.S. trade with both Japan and China so that neither would feel discriminated against, and Britain would not have increased leverage to seek rapprochement with Japan at America’s expense throughout Asia.\(^5\)\(^8\)\(^2\) The U.S. did, however, seek to ensure that Japan honored its pledge to uphold “open door” principles in Manchukuo commerce, while beginning the reporting regimens to catalog Japanese violations of this principle.\(^5\)\(^8\)\(^3\) The inherent tension in U.S. policy was quickly put into sharp contrast in the competition with Britain for aircraft sales to China and the debate over a loan to the Nationalist government.

Britain’s support for the regional Canton government in China, and more broadly its primary economic stake in the Yangtze valley of central and southern China, had led its government-assisted companies to make many aircraft sales to the Cantonese government. These aircraft were dual-use, military capable aircraft, and were used by this sometime rival to the Nationalist government in Nanking for its own internal political leverage against Chiang Kai-shek. The U.S. took the position that the Nationalist

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\(^5\)\(^8\)\(^2\). Ashbaugh agrees that the U.S. sought “balanced” trade with both China and Japan in the 1933-1935 period, but he declares the reason to be U.S. commercial self-interest motivated by export needs during the depression, and not due to strategic considerations and competition with Britain. Ashbaugh, “The Yardstick of Trade,” p.214.

\(^5\)\(^8\)\(^3\). For text of Japan’s commitment to the open door in Manchuria see Shimada, “Extension of Hostilities,” p.330. For U.S. officials collecting evidence of open door violations in Manchuria see exchange of letters from Secretary of State to the Ambassador to Japan in Foreign Relations of the United States: Japan, 1931-1941, Vol. I, pp.125-130.
government was the best guarantor against civil war in China, not to mention U.S. export opportunities, and that the British should work with the U.S. to limit aircraft sales to both Canton and Nanking, but particularly to Canton. To this, the British did not reply beyond their blanket offer of an arms embargo against all belligerents in both Japan and China in early February 1933. As noted earlier, this offer was designed to expose America’s lack of capacity to institute a limiting of the arms trade. As America’s aviation assistance under Colonel Jouett to the Nationalists increased, so did its aircraft sales to Chiang’s regime. This commercial competition with the British intensified from early 1932 through 1936, leading to increased sales by both states to their respective regional clients inside China, with the U.S. supplying the lion’s share of China’s air market (i.e., 440/692 of Chinese military aircraft by 1937).584 U.S. support for Nationalist China’s air capabilities was directed by Hornbeck in order to counter Japan’s military, and was therefore, decidedly realist, not a result of commercial liberalism impulses.

The air power assistance rendered Nationalist China by the U.S. caused great consternation and public denunciations in Japan, and would later help provide an opportunity for British officials to attempt a strategic rapprochement with Japan. In the first half of 1933, however, the British were engaged in commercial rivalry and conflict with Japan as a result of Britain terminating British India’s 1911 Treaty of Commerce and Navigation with Japan in April 1933. Following the Ottawa Agreements protecting

584 Xu captured Anglo-American competitive discord well: “Anglo-American cooperation in helping the Chinese government control importation of airplanes to China was difficult because each country had to consider its economic interests in China. The arguments also disclosed and underscored the distrustful and accumulated grievances that existed between those governments during the period of the Sino-Japanese hostilities.” Xu, “The Eagle and the Dragon's War Wings,” p.212. For the U.S. share of the market see ibid., p.236.
British dominion trade in August 1932, Britain placed its economic self-interest and concerns for dominion trade above Anglo-Japanese accord in the May 1933 abrogation of the Anglo-Japanese commercial treaty covering Britain's West African colonies. The Indian act, in particular, sought to defend British cotton interests against an onslaught of Japanese cotton piece goods with higher tariffs and numerical quotas.585 Japan responded in June 1933 with an embargo against imports of Indian cotton, thus stimulating increased demand for U.S. cotton and contributing a great deal to the relaxation of tension with the U.S. that has often been referred to during the middle of 1933.586 Although U.S.-Japanese relations were improving from their very low state under Secretary of State Stimson, the U.S. did not restrict itself to improving those ties at the expense of building a stronger China.

Despite Hornbeck's advice not to support China overtly and Hull's total opposition, in June 1933, President Roosevelt decided to extend a U.S. government loan of $50 million dollars to the Nationalist government in order for it to purchase U.S. wheat and cotton.587 The purpose of the loan has been open to interpretation since its extension, with Roosevelt's own declaration that it was part of supporting domestic farm production and prices remaining the prevailing view. The Chinese declared that they would resell the cotton and wheat extended under the loan provisions and use the proceeds for

587. Roosevelt's own strategic assessment of how to play the Anglo-American-Japanese triangle in China was controlling here. Perhaps Roosevelt saw things more clearly than his advisers; he would remind staff later to, "please remember that I have a background of a little over a century in Chinese affairs." Roosevelt memorandum to Secretary Morgenthau, December 4, 1934, quoted in John M. Blum, From the Morgenthau Diaries: Years of Crisis, 1928-1938, (Boston, MA: Houghton Mifflin, 1959), p.206.
"productive purposes." These productive purposes were dedicated to basic infrastructure, but the Japanese accused the U.S. of assisting China's procurement of U.S. aircraft in this indirect financial assistance to the Nationalist government. Undoubtedly, the loan did assist the Chinese government in financing its total expenditures, including those that went to U.S. aircraft. Arthur Young handled the negotiations on behalf of China and monitored the outlays made under its terms, which amounted to only $17.1 million dollars due to the May 1936 revisions to China's U.S. debts. Additionally, Japanese cotton mills in China, who used 60-70% of American cotton exports to China, were directed not to buy American cotton under this program and thereby help finance China's Nationalist government.

Young concluded that the loan boosted "the morale of China" at a critical juncture, was so intended, and helped cement the strong ties between Nationalist China and the U.S.. Britain objected to the loan on the grounds that it violated the spirit if not the letter of the China Loan Consortium. In this objection the British were joined by Thomas Lamont of J.P. Morgan and other Consortium members, all of whom were opposed because of the negative fallout the loan would have on their business relations with Japan. Because of commercial competition for the China market that the loan helped tilt toward the U.S. at Britain's expense, the British government resented it and would cite it as a cause of increased friction. For these reasons, the loan was "political,"

589. Young, China's Nation Building Effort, 1927-1937, pp.382-386. Interestingly, under the 1936 revised loan China appears to have paid back only $3.4 million dollars of the $17.1 million extended to it during 1933-35, thereby generating a net transfer, or aid, to China in excess of $13 million dollars. And this was not paid until during World War II, rendering any inflation-adjusted value of the transfer to China even higher.
590. Ibid., p.386.
and although it is superficially consistent with liberalism and marxism by tying loans to exports to support domestic producers, it was also realist in supporting a Japanese counterweight when no one else would. Furthermore, because the U.S. government loan did challenge the China Loan Consortium against U.S. bankers’ preferences it also contra-indicates liberalism and marxism.

This friction increased with the failure of the World Economic Conference in London in July 1933, after Roosevelt withdrew his pledge to stabilize the dollar-pound exchange rate and not re-link currency stability negotiations and the outstanding European war debts to the U.S..\textsuperscript{591} Roosevelt followed through on this new unilateralism by removing the U.S. dollar from the gold standard in October 1933 and declaring that the U.S. would seek a new value of the dollar on its own terms through buying more gold domestically and internationally as it suited U.S. interests and exchange rate preferences.\textsuperscript{592} This retreat from Anglo-American monetary and Asian policy cooperation paralleled growing rivalry in Anglo-American naval relations.

Since the London Naval Treaty had only placed a ceiling on the displacement dimensions of cruisers with less than eight-inch guns (i.e., six-inch gun heavy cruisers), the U.S. decided to begin building to the upper limit, partly in response to Japan’s building of two 8,500 ton cruisers in 1931 and likely procurement of two additional 8,500 ton cruisers.\textsuperscript{593} The U.S. authorized the building of four 10,000 ton six-inch gun cruisers in June 1933 and awarded the contracts for them on August 3, 1933. Britain objected

\textsuperscript{591} Dallek, Franklin D. Roosevelt and American Foreign Policy, p.54.
\textsuperscript{592} Ibid., pp.72-4.
\textsuperscript{593} Eight-inch gun heavy cruisers with 10,000 ton displacements were the locus of conflict from Geneva 1927 to the London Treaty in 1930, and were resolved with the agreement that Britain and America would each build out to 18 of these. From at least 1930, the U.S. fully intended to complement these eight-inch cruisers with an increase in six-inch gun cruisers with large displacements.

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vigorously to America’s cruiser building plan, stating “a new expensive type of large cruiser will thus become actually established and the prospects in regard to future naval limitation will be gloomy in the extreme.” Even though the U.S. had only built up to 75% of its overall allotted Treaty strength at this time and with this program would still be 150,000 tons short of its quota by the 1936 renewal date, the British tried to squelch the American building plan. Britain requested postponement of America’s building plan pending Anglo-Japanese-American talks on limiting both American and Japanese plans. The U.S. rejected Britain’s plea and effort to undermine U.S. ascension to naval parity with it.

Britain’s effort to forestall a further degradation of its naval power relative to both the U.S. and Japan was not warmly received in the U.S., and the U.S. stepped up its analysis of Japan’s building programs, strategic motivations and possible moves toward renewed alignment with Britain. Although Hornbeck understood that many in Japan’s navy were “less war minded” than in Japan’s army, he did not share Ambassador Grew’s optimism that “the more responsible officers of the government and navy” understood the “danger” in courting anti-American feeling and would, therefore, act with restraint. Hornbeck’s reticence was validated by the ever-growing power of Japanese navy expansionists as evidenced in the Navy General Staff’s assumption of greater authority over the Naval Minister in October 1933 and the dramatic increases in naval

595. Japanese and American building plans further pressured Britain’s resource allocation decisions, which were becoming linked to European developments, particularly German rearmament efforts. One of the visible products of Asia, America and Europe being linked in British policy was the June 1935 Anglo-German naval agreement.
appropriations beginning in 1932. This is particularly illustrative in light of the army's increased budget demands due to its China operations. In early November 1933, to reduce Japan's threat perception of the U.S., President Roosevelt ordered the "American Scouting Force," which had been in the Pacific for the last three years, to return to the Atlantic in 1934. Naval press statements gave as a reason the Fleet's long absence from family and friends on the American east coast, and stated, "this is returning to the normal operating policy of the Fleet." Despite this overture and having an aged and presumably Western-leaning admiral as Premier, the growing domestic power of naval expansionists caused Japan's position on future naval arms talks to harden around the principle of Japanese parity with the Anglo-American powers. This principle became inviolate by early 1934 even though it represented a radical departure from the prior post-WWI period.

Japan's naval expansion would demand an increase in resources and relative calm in China, both to meet the construction of the fleet and to fuel its operations. To meet these needs, Japan let it be known that it regarded all of Asia as its rightful area of

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598 This decision had been in the works for some time as Hornbeck had taken advice from March 1933 on that returning the Fleet to the Atlantic would "allay Japan's fear." He also advised this move due to growing U.S. navy unilateralism, with Admiral Standley declaring U.S. fleet presence in the Pacific was due to Japan's effort to fortify the mandated islands. The Hearst papers proclaimed this and the navy department issued its own public clarifications without clearing them through the State department. See memorandum from Maxwell Hamilton to Hornbeck, March 10, 1933 and navy press-related documents in Hornbeck papers. Box 308, Folder: Navy, 1931-1938.

599 This hardening in late 1933 was also facilitated by the public sympathy for naval power maximization generated during the November 1933 trials of the May 1932 assassins of Premier Inukai. These naval sub-lieutenant assassins, who had also planned to kill the American Ambassador, convinced the "general public" of the links between London naval limitations and corruption in the political leadership of Japan. As a result, these assassins received only 15 year sentences, instead of the death penalty, for their crimes against civilian rule. See Letter Joseph Grew to Secretary of State, November 15, 1933, Foreign Relations, 1933, Vol. III, p.711.

economic prerogative, and in the famous Amau statement of April 17, 1934, declared that assistance to Nationalist China was “prejudicial to the peace of East Asia.” Japan specifically objected to the military aviation assistance and “political loans” rendered China, without directing its ire at the U.S. by name. Following the Amau statement, Japan’s new Foreign Minister, Hirota Koki, relayed his government’s guidelines to the U.S. Ambassador to China, which supposedly predated Amau’s statement and provided the context for it. Hirota’s instructions to the Ambassador declared that Japan had the responsibility to maintain “peace and order” in Eastern Asia. It further clarified “our guiding principle should be generally to defeat foreign activities in China at present, not only those of a joint nature but those conducted individually, in view of the fact that China is still trying to tie Japan’s hands through the influence of foreign Powers.” This declaration greatly disturbed U.S. officials as did Britain’s unwillingness to join the U.S. in responding to Japan’s position.

Under Hornbeck’s analytical leadership, the State department began to place Japan’s latest policy declarations and overtures for U.S.-Japanese declarations of joint interest into sharp contrast. Hornbeck noted that despite Foreign Minister Hirota’s statements of conciliation toward the U.S. and support for the existing Washington

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602. See Hornbeck’s assessment of Britain’s acquiescence to Japan, which blamed America’s wheat loan in particular for Japan’s attitude. Hornbeck noted, “For reasons of their own, the British do not choose to take or to be associated with any “strong position” in opposition to Japan. We may as well face the fact that whatever position we take will have to be ours and that whatever consequences flow therefrom will have to be taken by us.” Letter and accompanying memo from Hornbeck to William Phillips, Undersecretary of State, and Secretary of State, April 25, 1934, in Hornbeck Papers, Box 243, Folder: Japan: No Trespass, 1934.
Conference Treaties after the Amau Statement, Japan’s War Office spokesman had declared that the Nine Power Treaty respecting China was no longer in effect. Hombeck held:

On the Janus head of Japan’s foreign policy, the face which looks eastward with a smile is much smaller and much more refined in feature than is the face which looks westward (upon China and Russia) with the expression of Attila. What Japan actually does in her external relations in the near future and for a good while to come will be done by decision and direction of the military element in Japan (or adherents of that element abroad) and not upon decision or by direction of the “liberal” elements either in or outside of the Japanese Foreign Office. This, it seems to me, the fact that in dealing with Japan we are dealing with a military and militant state, we need to have in mind every step of our way.603

6.3 Post-Amau Statement: Britain and Russia Appease, Dutch Build Bridge to America

In contrast to principled American non-cooperation with Japan, the British did respond to Japan’s latest expression of its interests, albeit, in furtherance of their own interests. Led by Chancellor of the Exchequer, Neville Chamberlain, they began discussions with Japan on a non-aggression pact in the late spring of 1934. When Hirota suggested that any non-aggression pact needed to be linked to Japan’s desire for naval parity in the upcoming naval talks and a statement respecting each country’s sphere of influence in China, the internal British position for comity with Japan collapsed.604


604. Kibata, “From the Manchurian Incident to Pearl Harbor,” pp.7-9
Thereafter, Britain sought to move forward with Japan by revising its imperial trade preferences, which had changed since the Ottawa Agreement to Japan's detriment particularly in cotton goods exports. Japan had sought a similar joint statement from the U.S. in May 1934, but the U.S. objected to adding revised commitments to those already in force under the Washington Conference Treaties. The U.S. waited in a somewhat detached position from Asia, while analyzing what course of action to take in the event that Japan moved further in North China and Manchuria provoking conflict with the Soviet Union.

After normalizing diplomatic relations with the Soviet Union in November 1933, the U.S. assessed what its course of action should be in the event of another Russo-Japanese conflict. A November 1933, U.S. Army Military Intelligence Division (MID) analysis of Russo-Japanese relations concluded that Japan and Russia would likely come into conflict over the Chinese Eastern Railway, a joint Russo-Chinese line. One of the principal reasons for Japanese expansion into Manchuria was the control of the rail lines there, and Japan was likely to use force to obtain control. This would not occur before 1935, when its army reorganization and re-equipment plans were complete. In response to MID's analysis, U.S. recognition of the Soviet Union and Japan's continued expansion throughout Manchuria, Hornbeck prepared a policy paper for the President and Secretary of State which called for U.S. actions to foster a balance of power in Asia

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among China, Japan and the Soviet Union. Hornbeck felt such a balance “is only likely to be achieved if China grows stronger, Russia remains at peace, and the military spirit and power of Japan are kept in check.”  

Among the more striking conclusions of this analysis was that the U.S. should be prepared to intervene militarily on the side of the Soviet Union against Japan “to see to it that Japan does not emerge the victor.” Hornbeck then noted that because Britain had more interests at stake in the Far East, “we could afford to await the taking of an initiative by the British government, in the event of which we would be in better position to gain acceptance of our views than if the initiative were taken by us.”

Hornbeck’s prescriptions for American economic policy were also interesting. First, he stated that the U.S. should avoid exchange with the Soviet Union that would give “Japanese military leaders ground for representing to the Japanese people that we are encouraging and aiding the Soviet Union in preparation for an attack by that country upon Japan. In case we make a loan or an extension of credit to the Soviet Union, we should make a gesture of willingness to be equally accommodating in our dealings with Japan.” Second, he advised American neutrality at the outset of any conflict and no export embargo on Japan until its most advantageous moment (i.e., that which both maintained Soviet engagement in the war and best supported U.S. victory against a vulnerable Japan). Finally, Hornbeck emphasized: “we should make preparations on a basis of complete governmental control

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606. Hornbeck memo, “Russo-Japanese Conflict: What Should be the Attitude and Course of Action of the United States,” February 2, 1934, p.2, in Hornbeck papers, Box 396, Folder: Soviet Union, Soviet-Japanese Relations. Hornbeck began this memo with a declaration that the U.S. had no vital interests at stake in the Far East. He noted, “we have not yet developed there a large financial investment; our trade with that part of the world, though important, is by no means vital to us – as yet.”

607. Ibid., p.11.

608. Ibid., p.7.

303
of man power (both as regards military service and as regards economic service) and of
capital (including all economic resources). We should speed up the construction of our
Navy and should perfect our technical 'war plans.'

This analysis proved unduly pessimistic of Soviet-Japanese relations, given their
increasing trade relations both bilaterally and in Manchuria, particularly in oil. Although Soviet-Japanese tensions remained high, they were able to consummate the sale
of the Chinese Eastern Railway to Japan's puppet state Manchukuo on March 23,
1935. Other sticking points in their relations would not be solved as easily after this
date due to Japan's budding relationship with Germany. British and Soviet appeasement
of Japan helped allow Japan to concentrate its economic expansion into other areas,
particularly those that would benefit its navy as much as the army. At least since the end
of WWI, the natural focus of these naval designs had been the DEI, and in preparation for
the naval talks to begin in 1935, it was again. Japan's economic position vis a vis the
DEI steadily increased ever since Japan devalued the Yen in 1932, resulting in large
increases in the value and volume of exports to the DEI.

Japan's desire to trade on this commercial position in the DEI and improve its
naval position relative to the U.S. and Britain, led it to take two important steps toward
the DEI in 1933 and 1934. First, Japan and the Netherlands signed a new Treaty of

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609. Ibid., 10. This memorandum was rather bellicose in the sense that it advocated offensive war against Japan when the Soviet Union had sufficiently exhausted some of Japan's military capabilities, allowing the U.S. to strike decisively.
610. See in particular letters from U.S. Consul General at Mukden, Manchuria, Myers, and Ambassador to Japan, Grew, to Secretary of State, July-September, 1933, Foreign Relations, 1933, Vol. III, pp.736-739.
612. Japan's share of DEI imports went from 10% in 1929 to 32% in 1933, and its share of DEI textile imports was 77% in 1934. See Rupert Emerson, The Netherlands Indies and the United States, (Boston, MA: World Peace Foundation, 1942), p.48.
Arbitration on April 19, 1933, which affirmed that any disputes would be arbitrated peacefully even though Japan was no longer a member of the League of Nations. Japan was still the ruler of island mandates in the South Pacific under the Versailles Treaty and had declared that it would not turn them over to any other authority. Second, and more pointedly, Japanese officials intimated that Japan might acquire a southern naval base, after which they would be even more interested in the DEI's oil supplies. Possibly as a result of this overture, the Dutch became increasingly worried about any further Japanese economic penetration of the DEI, and wished instead to see greater comity with the U.S. and increased American corporate and political presence in the DEI. To this end, the Dutch steadily applied themselves in 1934, beginning with negotiations on reciprocal tariffs between the U.S. and Netherlands governments.

These bilateral negotiations were, however, not as important as the increased operations allowed American oil interests in the DEI and the manner in which they were increased. Standard Oil of California began to enter the global oil cartel in 1934 due to its acquisition of rights to a massive oil find in Bahrein. Because of its power to upset

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613. Matsuoka Yosuke, Japan's former chief delegate to the League, took these positions during interviews in The Hague in March 1933. Matsuoka was accompanied by Saito Hiroshi, former Charge d'Affaires at the Japanese Embassy in Washington and later Ambassador there from February 1934 to December 1938. See ONI Report, John H. Magruder, Jr., Commander USN, Naval Attaché The Hague, Serial No. 30, File No. 103-100, March 14, 1933, File c-10-l, Register 13774, RG 38. Japan's statements to these effects might best be viewed as both an expression of southern desires and establishing a bargaining position for the naval talks (i.e., pressuring the Dutch hoping Britain and the U.S. might acquiesce to something more).


615. See letters between U.S. Minister in the Netherlands and Secretary of State, Foreign Relations, 1934, Vol. II, pp.627-635. It is particularly interesting to note the U.S. interest in using the purchasing power of its domestic market to support the DEI's struggling economy. Another example of increasing Dutch-American ties was former Foreign Minister van Karnebeek's son being employed by Koloniale and reporting to U.S. ONI on Japanese activities in the DEI. See ONI Report, Serial No. 43, File No. 103-200, April 20, 1933, File c-10-I, Register 13774, RG 38.

616. The global oil cartel created in 1928 and discussed earlier had undergone consolidation and changed affiliate names by 1934. With regard to Asia, chief among these changes was the consolidation of the operations of Standard Oil of New Jersey and Standard Oil of New York into the Standard-Vacuum Oil Company (aka., Stanvac) in September 1933. These companies still cooperated with Royal Dutch Shell.
cartel production and pricing, a new company was formed in 1934 called the Pacific Oil Company, with one-third ownership each for Royal Dutch Shell, Standard Oil of New Jersey and Standard Oil of California. The Pacific Oil Company was granted oil concessions in Central Sumatra in the DEI in mid-1934 and subsequently the DEI government declared that it would admit no further oil companies into the DEI.617 In principle, this would not have affected possible further Japanese acquisitions because they (e.g., Japanese Borneo Oil Company) were already admitted to the DEI through the dissembling transfer of valueless private concessions in 1928. In practice, however, Dutch and DEI colonial authorities were not willing to allow any expansion of Japanese direct investment into the DEI.

Dutch colonial authorities were partly motivated to expand America's presence due to their concerns about Britain's commitment to DEI defense. Dutch Captain J.T. Furstner, head of the Dutch Naval Staff College, expressed an increasingly widespread and skeptical view of Britain's efforts to bargain with Japan, possibly at the DEI's expense. Despite Anglo-Dutch naval talks on joint action against potential Japanese aggression, Furstner noted "England is increasingly determined to keep her own council." In light of this, Furstner expressed a Dutch government desire to step up its intelligence gathering efforts against Japan and invited the U.S. navy to join in this effort in order to bolster DEI security. This Dutch desire for political and military cooperation with America manifested itself most clearly in the manipulation of direct investments in the

and other British oil companies to control production, prices and alternatives to oil across the world. See FTC Report, pp.114-116: Anderson, The Standard-Vacuum Oil Company, pp.26-36. Corporate mergers were not discouraged at this time, as President Roosevelt encouraged greater control of production and distribution of "basic commodities," while Hornbeck had been urging private coordination of oil supplies since 1923. See Dallek, Franklin D. Roosevelt and American Foreign Policy, pp.46-7.

DEI. For example, subsequent to a Japanese filing for a concession in New Guinea in June 1934, DEI authorities: “Not wishing to speak plainly we hurriedly gave a concession to the Pacific Oil Co. (Royal Dutch Shell, Standard Oil of New Jersey and Standard Oil of California), making them a “5A contract,” giving them the right to prospect for 13 years, after which both our government and the company must make up their minds as to future concessions. We were thus able to inform the Japanese that the Berau peninsula was already in the hands of the Pacific Oil Co. and we could not thus consider their proposal.”

This example demonstrates several important points regarding state and corporate relations and U.S. policy toward Japan’s southern expansion. First, American corporations were inserted into this Japanese-contested area without their prior knowledge and they simply accepted the Dutch government’s authority using them as both shields and pawns vis à vis Japan. Second, from this account of the event it is not clear that the U.S. companies were told of Japan’s prior interest and their role in frustrating that interest. Only the U.S. government through the naval attache in The Hague appears to have been informed of this sleight of hand designed to strengthen U.S.-Dutch ties. Third, similar to the decision surrounding Atjeh concessions in the 1920s, the Dutch government was more than willing to curtail development and production of DEI oil resources due to security concerns. The Dutch commitment to end further oil concessions was adhered to from 1934 forward. Finally, as before in 1928, and despite

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618. Captain Furstner would later become Vice Admiral and Minister of Naval Affairs by the late 1930s. See recounting of this event and Dutch sentiment by Captain J.T. Furstner, Chief of Dutch Naval Staff College, Office of Naval Intelligence, Reports, ONI Report, June 22, 1934, Serial No. 104, File c-10-I, Register 14017, RG 39. Interestingly, a Japanese concession for cotton growing near this area did eventually go through in 1937. At that time, the Royal Dutch Shell Co. had to quickly survey and drill in this area to prevent Japanese occupation and justify the “legitimacy” of their prior exclusion. See ONI Report, March 2, 1937, File c-10-I, Register 14017A, RG 38.

307

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fulfillment of Dutch pledges and American desires for broadened oil company presence in the DEI, this transaction again revealed U.S. policy of opportunistically advancing its oil position against Japan. As in 1928, the U.S. did have the option of not participating in its own oil expansion this time explicitly at Japan’s expense. But, the U.S. did not act to assist Japan’s autonomy; it chose to frustrate it instead.619 This event is most consistent with offensive realism because the companies were used as pawns and the U.S. actively participated in maintaining Japan’s oil resource deficiency, forcing it to rely on U.S. supplies. For this reason, this event partially contra-indicates defensive realism’s emphasis on not actively compromising a rival’s autonomy.

Japan began to pressure the Dutch directly during their first trade negotiations at Batavia beginning in June 1934. DEI authorities had begun to consider various restrictions on imports including quotas, licensing laws and higher tariffs, and Japan objected to these restrictions on its increasing export trade to the DEI.620 The negotiations dragged on through December 1934, but took on greater importance beginning in September when Japan attempted to exert stronger political pressure on the Dutch to grant them more expansive trade and investment rights in the DEI.621 Japan was

619 This is an example of a liberal counterfactual, posited for the earlier 1928 period as well, which should have shown a U.S. policy willing to countenance and possibly bring about a more active Japanese role in DEI resource development. 620 These Dutch restrictions were not limited to the DEI, as they ordered the Dutch West Indies to apply an import quota on Japanese cotton goods in mid-June 1934. See Katada, “The Political Economy of the Japanese Navy,” p.175. 621 See Wolthius, “United States Foreign Policy towards the Netherlands Indies,” pp.42-3: van Mook, The Netherlands Indies and Japan, pp.22-3. For their part, the Dutch were determined to curb Japan’s economic penetration. As soon as the Japanese trade delegation was departed, the Dutch planned on placing “some 50 quota restrictions into effect against Japanese goods entering the East Indies.” See letter from U.S. Charge in the Netherlands, Wilson, to Secretary of State, November 22. 1934, in Foreign Relations, 1934, Vol.1, pp.365-7. Interestingly, after the Japanese delegation left, DEI authorities canceled a Japanese timber concession in east Borneo where its proximity to the rich Tarakan oil fields raised Dutch fears that Japan might strike for oil on its timber concession. The Dutch declared this area “forbidden to foreigners.”
partly emboldened in its negotiations with the Dutch by its perception that the consequences of more self-regarding approaches were not high and British quiescence in its stronger approach to the DEI was at least possible. Japan was planning on abrogating the London Naval Treaty by the end of the year and its cabinet had noted that League of Nations withdrawal had not resulted in economic sanctions. They apparently then suggested that abrogation of the "Washington Pact" would result in similar economic inaction by the Western powers.\textsuperscript{622}

The United States had been preparing for the December 29, 1934, Japanese abrogation of the London Treaty for some time, and had concluded that it was best to leave the onus of responsibility for the Treaty's demise squarely on Japan. In order to establish this "clean break," the U.S. position was that no new negotiations on overall naval arms or political understandings should be opened for some time, and Japan should be burdened with explaining what it foresaw in terms of naval arms and understandings in lieu of the Washington Conference Treaties.\textsuperscript{623} The British were, however, vacillating on such a stance and proposing a middle course by which Japan could be kept in negotiations and not have its "moderates" unduly burdened or ostracized by the perception of a "common front" against them. This difference in Anglo-American opinion would continue through the opening of new naval arms talks in December 1935. At that time, Japan formally withdrew from arms limitation negotiations, insisting on achieving force parity and not merely upward revision in its ratio. Japan did not make

\textsuperscript{622} See ONI Report, by Lt. R.P. Bielka, USN, Serial No. 298-13, File No. 304-100, December 18, 1934, File o-1-I, Register 12865, RG 38.

\textsuperscript{623} See letter from Joseph Grew to Secretary of State, December 13, 1934, in Foreign Relations, 1934. Vol. 1, pp.408-9

\textsuperscript{623} See telegram from Secretary of State to the Chairman of the American Delegation, Norman H. Davis, November 22, 1934, and Memorandum of Conversation in the British Prime Minister's Office, November 23, 1934 in \textit{iibid.}, pp.364-5, 368-374.
this move, however, without first attempting to reach a naval arms and oil understanding. According to an ONI report, Japan offered to renounce its desire for naval parity if Western pressure on the Netherlands could yield the "transfer or rent" of Borneo to Japanese oil interests.624 This offer was not taken up by British, Dutch or American officials, but it illustrated yet again the interlocking nature of naval arms, oil and territorial understandings.

6.4 Japan’s Movements toward Autonomy and America’s Response

The Japanese government began taking steps in early 1932 to control its then rapidly deteriorating financial position and place its economy on a higher production plane through government sponsorship, if not direct ownership. These efforts were led by Finance Minister Takahashi Korekiyo. He sought to preserve Japan’s international position in finance and production, which was deteriorating in many ways including large gold exports throughout 1931 as discussed earlier. In fairly quick succession, Japan passed: the Capital Flight Prevention Law (July 1932); the Foreign Exchange Control Law (May 1933); the Industry Association Law (March 1934); the Gold Purchase Law (April 1934); the Trade Protection Law (May 1934); and the Automobile Industry Law (July 1936). In addition to these overall legal frameworks, the Japanese government began to form majority or wholly government-owned corporations in strategically significant industries. For example, in April 1933, the Japan Iron and Steel

624 See ONI Report, prepared and forwarded by Francis Cogswell, Captain USN, Serial No. 382, File No. 103, July 9, 1937, File c-10-I, Register 14017A, RG 38. This report quotes Admiral J.C. Jager, former Chief of Staff, Netherlands Navy, and his recounting of the event.
Manufacturing Company was legally established and became fully operational by January 1934, with the central government holding 70% of its capital. These laws and industrial promotion actions were designed to build up Japan's autonomous industrial capacity, and they succeeded in so doing. According to many measures, Japan's industrial production actually exceeded that of the U.S. from 1931 forward as did the rate of growth in its GDP.

The future success of these governmental efforts and economic growth were, however, dependent on foreign raw material inputs, large-scale domestic deficit financing and exports of manufactured goods. Raw materials were supplied from imperially-controlled areas (e.g., Korea, Manchuria) in increasing numbers, but these areas could not supply all necessary items. With the dramatic depreciation in the Yen's value beginning in mid-1932 (i.e., Yen went from 1931 average of $.4885 cents to 1932 average of $.2811), Japan's ability to finance its necessary imports would be put under increased strain. However, as a result of its depreciated currency and large increases in industrial production, Japan aggressively promoted exports led by textiles, and in particular, cotton piece goods. Japan surpassed Britain on a quantity basis in 1934 to become the world's leading exporter of cotton textiles (i.e., Japan exported 2,725,109,000 square yards of cotton goods while Britain exported 1,993,458,000 square yards). As a result, many countries were restricting their trade with Japan in textiles (e.g., Britain and its dominions, the DEI and 25 other countries). The U.S. had also begun to raise tariff and

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quota barriers to imported Japanese cotton goods as well as changing the price of domestic and exported cotton through application of a processing tax.627 President Roosevelt took these measures in late May 1933 as part of his effort to bolster farm commodity prices, but they would affect Japan by raising their costs of importing raw cotton.628

The U.S. did not wait for higher tariffs and raw cotton price increases to indirectly effect Japanese exports, particularly in cotton piece goods such as rugs. In June 1934, the State Department negotiated a quota (aka., Gentlemen’s Agreement for voluntary export restraint) on imported Japanese cotton rugs and later reached similar quota arrangements on Japanese textiles to the Philippines beginning in October 1935.629 These voluntary quota arrangements were supplemented by specific tariff increases on Japanese products, including on cotton goods in May 1936. These tariffs were higher than average compared with other countries and indicated the Roosevelt administration’s “desire to minimize the threat of Japanese competition as it (has) appeared in numerous small sectors of American industry.”630 Because the U.S. desired to remain Japan’s most important commercial partner but not allow it to obtain significant export earnings in the U.S., the various actions rationing cotton goods imports and raising the price of raw

630. For example, “dolls of cellulose, having movable parts” were hit with a 129% tariff. For the complete list of individual items and the comparatively high rates see Lockwood, Trade and Trade Rivalry, pp.34-5. See also Osamu Ishii. “Markets and Diplomacy: the Anglo-Japanese Rivalries over Cotton Goods Markets, 1930-1936,” in Nish and Kibata, eds., The History of Anglo-Japanese Relations, pp.69-74.
cotton exports are consistent with both realist perspectives and inconsistent with liberal and marxist ones. Defensive realism is better at accounting for the act of regulating excessive Japanese imports, but not the holistic effort at changing Japan’s terms of trade by raising the price of its imports from the U.S. while simultaneously restricting its ability to export back to the U.S. and the Philippines to earn the dollars for higher priced imports. Liberalism and marxism are contra-indicated because U.S. cotton exporters were not supportive of the cotton taxes which threatened to cut into their substantial exports to Japan. These exports grew nonetheless in importance to an interwar peak in 1936, with Japan taking 28.5% of total U.S. raw cotton exports.631

Interestingly, Japan also began to displace U.S. cotton piece exports to South America, garnering attention from the U.S. commerce community, but State department caution regarding public comment on them. Stanley Hornbeck told the Economic Adviser at State: “I advise against there being given any kind of publicity to the fact that special attention is being given by and on behalf of the American government to the subject of Japanese competition in Latin America.”632 The U.S. desired to manage and monitor trade with Japan to minimize Japan’s hyper-growth in textile production and exports as part of overall U.S. policy. The U.S. did not wish to clamp down “hardly” on Japan’s economy, but rather test its dimensions and vulnerabilities as it grew rapidly,

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632. Memorandum from Hornbeck to Economic Adviser. U.S. State Department, December 4, 1936, in Hornbeck Papers, Box 252, Folder: Japan: Trade. The reasons for keeping this interest secret are open to interpretation. It is probable that U.S. intelligence interests against Japanese commercial, shipping and naval activity south of the U.S. were paramount. ONI tracked Japanese activities in central and south America throughout the 1930s and the U.S. began preclusive buying of strategic goods there that Japan sought (e.g., Peru’s Molybdenum substitute Vanadium). See ONI Reports on Japan’s political and economic penetration of Brazil, Panama, Columbia, Mexico, Venezuela, Chile at File c-10-a, Register 16557; File c-10-e. Register 6762.6726; File c-10-h, Register 2234, File c-10-i, Register 11515: c-10-m. Register 21696; File c-10-m, Register 22520; File o-12-c, Register 13362, RG 38. Barnhart, Japan Prepares for Total War, p.179.
while preserving Japan’s perception that the U.S. was a reliable trade partner. A question of excess Japanese exports of sun goggles arose in early 1935 and in response to Assistant Secretary of State, Francis B. Sayre, Hornbeck clarified U.S. intent:

we should be on guard against getting ourselves into a position of psychological disadvantage (to ourselves) in our work with the Japanese on the rationing of Japanese imports into this country. Thus far, we have been dealing with commodities the trade in which is of comparative unimportance...If we deal hardly with the Japanese on a number of these items in the early stages of making agreements, we may find ourselves some day, when something really important comes along, confronted with the contention on the part of the Japanese that, having been hard on them in various previous cases, we should be generous to them in connection with the case then under discussion and cases to follow. Would it not be better for us to be easy on them in cases...not of importance, with the expectation that we will be more generous to ourselves when cases of importance come along.633

The important case had been percolating throughout 1934 and was coming to a head in 1935. The most significant Japanese legislation created the Manchuria Petroleum Company in February 1934 and the Petroleum Industry Law for Japan proper in March 1934.634 U.S. officials already concerned about trading and investment rights violations in Manchuria, now had to contend with Japan’s latest efforts at increased energy autonomy through the imposition of various controls on the oil business in Japan and Manchuria. The Petroleum Industry Law established the Japanese government’s exclusive right to license importing, refining and marketing operations of all oil companies in Japan, and was insisted upon by the Japanese navy. It had as a principle objective building up Japan’s domestic refining capabilities through greater crude oil

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[634] A comprehensive summary of this law and surrounding events is in Anderson, The Standard-Vacuum Oil Company, pp.49-103.
importation, not continued imports of refined products from the Western companies. This law further empowered the government to change the market quotas of oil companies and to fix prices of all oil products. The allowed sales (i.e., market quotas) of the Royal Dutch and Standard companies were reduced in July 1934 by about 2 percent each. The most onerous and critical provision of the law required companies to maintain supply stocks equal to six months of government determined aggregate demand. The government was further empowered to determine where these stocks would be kept at company expense and to demand improvements in company equipment (e.g., refineries, stock distribution facilities etc.).

These provisions alarmed oil company leaders greatly, but also caused U.S. State and Navy department concern due to the potential increase in reserve supplies afforded Japan through the stockpiling requirement. The two most powerful oil company leaders, Sir Henri Deterding, Director General of the Royal Dutch Petroleum Company, and Walter Teagle, President of Standard Oil of New Jersey, began seeking governmental action against these laws in August 1934. At their first meeting with Hombeck and Under Secretary of State William Phillips on August 22, 1934, Deterding and Teagle requested that the U.S. State department take the lead in confronting Japan on this issue by beginning an official governmental review in the Interior department on the feasibility of restricting U.S. exports to Japan. During their discussion Hombeck established that British-Dutch oil interests had more at stake in Japan than did the U.S. and that as yet neither of those governments had reacted to the Japanese laws. Hornbeck accurately

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635. Ibid., p.77.
636. British-Dutch oil interests sold more refined products into Japan, including sales of products originating from the U.S., and likely had larger investments in Japan as well. Royal Dutch interests held

315
assessed Deterding’s motives when he noted: “Sir Henri Deterding might be engineering a plan to cause the American government to take the lead (and perhaps to act alone) in a measure directed, on behalf of all oil interests in Japan.”\footnote{Memorandum of conversation between Phillips, Hornbeck and Eugene Dooman of the State department, August 23, 1934, p.2, in Hornbeck Papers, Box 340, Folder: Petroleum: Standard Oil Offices, Discussions With 1934-1936.}

Under Secretary of State Phillips set a meeting the next day for the oil chiefs and Secretary of the Interior, Harold Ickes, but Hornbeck held a private meeting with Ickes just prior to the ushering in of the two businessmen. Ickes noted to the oil chiefs that the U.S. had led the discussion of economic moves against Japan in the past under Secretary of State Stimson, and had not received much support from other countries. Hornbeck and the oil chiefs then squabbled over whose interests were most at stake:

Sir Henri and Mr. Teagle demurred at the suggestion that this matter is of greater concern to the British and to the Dutch than to American interests, stating that the greater part of the oil imported into Japan is purchased from American sources. Mr. Hornbeck pointed out, however, that this fact would not appear to be germane, the point being that the British and Dutch interests directly to be affected by the operation of the Japanese law (i.e., in business in Japan) are greater than the American interests to be affected, and that the British and the Dutch interests stand to lose more by its operation of the Japanese regulations than do the American interests. Mr Teagle and Sir Henri assented.\footnote{Memorandum of conversation between Deterding, Teagle, Ickes, Hornbeck and Dooman, August 23, 1934, p.6, in Hornbeck Papers, Box 340, Folder: Petroleum: Standard Oil Offices, Discussions With 1934-1936.}

29% of Japan’s petroleum products market, while Standard interests 19%. Teagle estimated his company’s invested capital in Japan at $12 million dollars, while British-Dutch invested capital was greater. See memorandum from Teagle to Hornbeck, September 21, 1934, attached to memorandum of conversation among Teagle, Chester O. Swain, (S.O.N.J.) and Hornbeck, September 21, 1934, p.6, in Hornbeck Papers, Box 340, Folder: Petroleum: Standard Oil Offices, Discussions With 1934-1936. Accuracy of invested capital is difficult to establish. Compare Teagle’s estimate with investment estimates of the U.S. government in 1940 and assets written off as war losses at $7.7 million dollars in Anderson, The Standard-Vacuum Oil Company, pp.202, 208-9. Even this lower figure, however, was over 10% of U.S. direct investment in Japan.\footnote{Of course, it was germane to the U.S. that most imported Japanese oil came from the U.S. and Hornbeck was merely putting the oil company officers into their proper place, beneath the state. Memorandum of conversation between Deterding, Teagle, Ickes, Hornbeck and Dooman, August 23, 1934, p.6, in Hornbeck Papers, Box 340, Folder: Petroleum: Standard Oil Offices, Discussions With 1934-1936.
As a result of this fact and the prior history of discord in Anglo-American economic policy coordination, the U.S. government took the position that any discussion of governmental action with respect to Japan would have to originate with written communications from the British and Dutch governments. Deterding offered that he could induce the British government to begin communications toward that end, and the first bargaining round ended on the understanding that the U.S. would take no step until the British government communicated with it. Subsequently, the British government inquired only as to the attitude of the U.S. government regarding the situation, and the U.S. responded that the matter was serious and that the U.S. would give sympathetic consideration to suggestions which they might offer for action. The Dutch government expressed its position to the State department in early September 1934, noting that it had instructed its Minister in Tokyo to approach informally Japan's Foreign Minister to lodge their objections to the law. The Dutch had also not heard from the British government as to any concrete action.

Despite incessant pressure from the oil companies for the U.S. to act on its own (i.e., beginning the process of restricting exports from the U.S.), Hombeck and Secretary of State Hull continued to await concrete proposals from the British government. This policy was repeatedly relayed to Teagle of New Jersey Standard. After conferring with Deterding, Teagle would continue to suggest that their understandings of government deliberations led them to assume governmental action was forthcoming, and therefore

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639. For a recent British recounting of this event with slightly different interpretations see John Sharkey, "Economic Diplomacy in Anglo-Japanese Relations, 1931-1941," pp.95-99.
they continued to press for such action.\textsuperscript{640} In a particularly pointed summary, Hornbeck noted:

\begin{quote}
We have made it clear to Mr. Teagle and others concerned that they must not expect action on the part of this Government suggestive of or involving threats toward Japan in connection with this matter; that so far as proposed joint action is concerned we will continue to await the taking of an initiative by the British Government; and that we feel that any plans which might call for or involve use of pressure should be developed and be agreed upon between and among the oil interests themselves and in connection with the commercial weapons which are in their hands before there should be considered seriously any suggestion or proposal by them that the Governments turn to and employ methods of pressure.\textsuperscript{641}
\end{quote}

The U.S. took this position partly because American oil companies were not coordinated as to the desirability of threatening Japan's oil supplies, either to Japan proper or to the Manchurian monopoly company. This was due to the large number of independent oil companies and the particular position of the Associated Oil Company with half ownership of a refinery in Japan. Associated was under long-term contract to supply its joint venture refinery operation from its own supplies of California crude, and State department officials were not convinced Teagle could reign them in from supplying Japan absent U.S. government pressure.\textsuperscript{642} The joint venture with Mitsubishi Oil Company began operating in 1931, but even as late as 1939 contributed only 3.2% to Japanese domestic production.\textsuperscript{643} Other independent companies, including an as yet not

\textsuperscript{640} For example, see memorandum of conversation between Teagle and Hornbeck, September 14, 1934, in Hornbeck Papers, Box 340, Folder: Petroleum: Standard Oil Offices, Discussions With 1934-1936. One of the tactics that the oil chiefs used to foment controversy within the State department was to claim that either the U.S. Ambassador to Japan, Grew, or other embassy officers agreed with their position that concerted U.S. action was needed to protect their businesses in Japan.

\textsuperscript{641} Letter from Hornbeck to Secretary of State, November 9, 1934, pp.2-3, in Hornbeck Papers, Box 339, Folder: Petroleum Standard Vacuum Oil Co.

\textsuperscript{642} Standard of California had a supply contract with Mitsubishi which pre-dated the creation of Manchukuo and required them to supply both Japan and Manchuria at "competitive prices." See memorandum of conversation between Hornbeck and M. Dundas, of Stanvac, March 28, 1935, in Hornbeck Papers, Box 340, Folder: Petroleum: Standard Oil Offices, Discussions With 1934-1936.

\textsuperscript{643} Wilkins, "Contributions of Foreign Enterprises to Japanese Economic Development," p.41.
fully-cooperative cartel member Standard Oil of California, were only partly responsive to Standard Oil of New Jersey and Royal Dutch entreaties. In effect then, the U.S. government was being asked to threaten Japan's oil imports in order to allow the cartel to obtain coordinating power over the independent oil companies. This was not something the U.S. government would do in December 1934, particularly with Japan's decision to withdraw from the London Naval Treaty pending. More importantly, the likelihood of an embargo causing Japan to attack the DEI was high and informally communicated to the U.S. government by Kurusu Saburo, Chief of the Japanese Foreign Office's Commercial Affairs Bureau in July 1934.

When the British government finally proposed to support an entirely private and "watertight" action by the companies, they did so in a restricted way that would have still required predominant American governmental action to bring it about. The British declared that the corporate embargo had to be against both Japan and Manchuria, or neither, and the British government would not take any formal action vis a vis Japan (e.g., "protest statement" to Japan's government). In effect, the British were proposing an entirely secret embargo that could not be fully implemented without the much demanded U.S. government action to reign in independent suppliers. To this, Secretary of State Hull replied, "this government does not for the present feel moved to proceed in the

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644. The incomplete harmonization of Standard Oil of California and the Texas Company was attested to by Teagle in an internal corporate memorandum of August 20, 1934. Teagle noted that the question of Japan's Manchurian monopoly and laws "transcend any question of any immediate profit, but affects preservation of our capital and future of our business." He then summarized his and Deterding's views that cutting off supplies from the DEI to Japan was not worthy of consideration unless full equality were achieved between Standard and Royal Dutch there. Instead, control of California and Bahrein were suggested as a way of pressuring Japan. See memorandum from Walter Teagle to W.S. Farish, Orville Harden and George Walden, August 20, 1934, in Hydrogenation Patent Hearings, pp.3680-1.

645. Anderson, The Standard-Vacuum Oil Company, p.57. The U.S. was, of course, aware of the connection between any Pacific Ocean conflict and Japanese seizure of the DEI in the early 1920s.

646. Ibid., pp.89-90.
direction of such action and it does not look as though the oil companies adversely affected are in a position to take or cause the oil industry to take such cooperative action as might be effective.\textsuperscript{647} This proposal appeared to confirm longstanding U.S. fear of British buckpassing to it, neatly summarized by Hornbeck: “we do not wish to chance being made use of by them (British government) as an agency for pulling their chestnuts out of the fire with the possibility that our own chestnuts will be pushed further into and be left in the fire.”\textsuperscript{648}

After organizing an effective joint company representation toward Japan, Hornbeck took the opportunity to advise Standard Oil of New Jersey before representatives left for direct negotiations with Japanese authorities. Hornbeck told P.W. Parker and Teagle that they should limit any further investments into Japan and not negotiate long-term deals for supply imports.\textsuperscript{649} Hornbeck also advised Teagle and Parker to monitor the Japanese-Dutch trade negotiations then ongoing in Batavia. It is not clear what he meant to suggest by this, perhaps merely to inform the company officials in order to remind them that the U.S. was not the only, or even necessarily the most important, government actor involved.\textsuperscript{650} Throughout this early period, Hornbeck

\textsuperscript{647}. Secretary of State Hull to U.S. Ambassador to Great Britain, Bingham, December 5, 1934, quoted in ibid., p.90.
\textsuperscript{648}. Memorandum of conversation between Hornbeck and Teagle, October 29, 1934, in Hornbeck Papers, Box 340, Folder: Petroleum: Standard Oil Offices, Discussions With 1934-1936.
\textsuperscript{649}. In Hornbeck’s November 9, 1934 letter to the Secretary of State, he said he had advised Parker to “be on guard against becoming too heavily or too deeply (as to investment or time period) committed in relations to delivery of oil.” In his memorandum of conversation with Parker he noted Japan’s desire to develop domestic substitutes for all foreign companies, “hence, foreign companies doing business in Japan would need to think seriously before adding to their investments and expanding their agencies of distribution within the country.” See memorandum of conversation Hornbeck and P.W. Parker, Standard-Vacuum Oil Company, November 10, 1934, p.3, in Hornbeck Papers, Box 340, Folder: Petroleum: Standard Oil Offices, Discussions With 1934-1936.
\textsuperscript{650}. In connection with noting that where Japan’s supplies came from was not “germane” to the business in Japan, perhaps Hornbeck was intimating that the companies should speak with the Dutch about restricting their exports to Japan or take such steps themselves from DEI sources that they controlled. DEI exports to
suggested that the companies could simply not comply with the new stockpiling laws in particular, and this they began to do as early as November 15, 1934, by ignoring compliance reporting requirements under the law. The company negotiators congregated in Shanghai in December, waiting for their diplomats in Japan to negotiate their introduction to the Japanese government.\(^6\)\(^5\)\(^1\) This was finalized at the end of December and corporate-Japanese government negotiations began in January 1935.

These negotiations were initially successful in achieving an increase in the Japanese market quota of the two western oil companies and a reprieve from the stockpiling requirement when the negotiations closed on April 13, 1935.\(^6\)\(^5\)\(^2\) Their success, however, had much to do with the companies declaring in early April, that if forced to hold a six month stock of normal sales quantities in Japan proper, they would reduce sales to the point where existing tank supplies would equal a six months stock of sales. This would mean, of course, drastically reducing overall sales in Japan and affecting the stability of Japan's market. Prior to this threat, Hornbeck had received information from consular officials in Mukden that there was increasing division within Japan peaked in 1935, perhaps because of Dutch fear that a corporate embargo from the U.S. could mean increased Japanese hostility toward the DEI. They may also represent mild appeasement after the trade and investment restrictions the DEI imposed on Japan subsequent to the trade talks noted earlier.

\(^6\)\(^5\)\(^1\). Hombeck insisted that Parker not go to Japan on his own to negotiate and Royal Dutch representatives were originally not going to coordinate their representations with Standard's. Hornbeck summarized the U.S. position, "it would be best for these various representations to meet at Shanghai and, in going to Japan, to go together; that throughout this matter the companies and the governments concerned should present, as far as possible, a united front." Memorandum of conversation between Hornbeck, Teagle, Kersey Coe of Stanvac, and Nelson Johnson, Minister to China, November 14, 1934, in Hornbeck Papers, Box 340, Folder: Petroleum: Standard Oil Offices, Discussions With 1934-1936. Johnson confirmed Hornbeck's suspicions of oil company solidarity absent extensive and overt governmental assistance. Johnson described the difficulties in the oil markets of Canton, China where the companies confronted a similar increasingly nationalist government: "(it was) difficult getting cooperation among the companies themselves and acquiescence by them in governmental measures of control which might be necessary to make this process effective." Nelson Johnson quoted in memorandum of conversation between Teagle and Hornbeck, September 25, 1934, in Hornbeck Papers, Box 340, Folder: Petroleum: Standard Oil Offices, Discussions With 1934-1936.

the Japanese government over the wisdom of the Manchurian oil monopoly due to its possible negative effect on Japan's overall oil situation. On March 28, 1935, Hornbeck advised that "now is the favorable moment for the oil interests to get together and make a common effort to give the proponents of the monopoly a first-class scare that they may find themselves unable to obtain oil." The companies negotiating in Tokyo appear to have used this opportunity and governmental encouragement to make the above threat instead, ignoring Hornbeck's desire to see the principle of government monopoly, and more importantly, Manchurian authority challenged. The Agreement of April 13, 1935, would prove fleeting, primarily because the proponents of the stockpiling requirement were not willing to exempt the foreign companies whose practices supplied current Japanese market demand only.

From April through December 1935, pressure was brought to bear on Japanese officials by the army and navy. The military did not approve of the compromise on the stockpile requirement. As a result, in November 1935, the Japanese government told the oil companies that they had to comply with the stockpile requirement, as the domestic Japanese companies had done, or lose any quota increase in the future. This placed the oil companies back where they had started negotiations in January. After stalled

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654. U.S. naval intelligence accurately assessed the contending Japanese governmental actors in the stockpile debate, and the motivations of the western firms. As early as August 1935, ONI observed: the threat by Royal Dutch's Japan affiliate to embargo oil sales; the insufficiency of Russian or Romanian alternatives; and the infighting between the Finance and Commerce departments with the Navy and War departments over whose budgets should cover the costs or subsidies necessary to increase storage tank capacity. The report concluded, "the ultimate outcome undoubtedly will be that the Government will accede to a certain extent on all points rather than give way completely to all of them. The only alternative would be to prosecute the oil companies for their failure to observe the provisions of the Oil Industry Law which would be most detrimental to the country's interests." See U.S. Naval Attaché Report from Tokyo, August 20, 1935, p.2. Serial No. 200, File No. 407, Report No. 199 at File e-10-d, Register 13177F, RG 38.
negotiations and a curt request for governmental assistance, the companies decided to offer the Japanese licenses to the coal hydrogenation technology as a way of fulfilling the Japanese military's desires for stockpiles. They did this not only to try and affect Japan's petroleum laws, but also to forestall an independent break out by Japan through direct negotiations with the German experts of I.G. Farben or non-cartel companies such as Ruhr Chemie. Japan's top scientist on synthetic fuels, Dr. Abe head of research at the South Manchuria Railway Co., had embarked on a trip to review hydrogenation plants in Germany on December 1, 1935. I.G. Farben in Japan advocated the conclusion of an arrangement with Dr. Abe and had meetings with him to that effect prior to his departure on December 1.

This background is necessary to understand Parker's declaration to Hornbeck on December 9, 1935, that the oil companies wished to offer coal hydrogenation patent licensing to Japan. In their conversation of December 11, Parker agreed that the oil companies no longer desired governmental representation vis a vis Japan, and that “Standard-Vacuum would authorize us (State department) to consult with our Navy and

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656. The companies' position on this point is clear from their internal memorandum at the time. Their strategy was: “Approach the British and American Governments to ascertain if they can be of any further assistance in getting the stockholding regulations modified, prosecuting the idea that the question is not entirely a commercial one. If it develops there is no hope in this direction, then the second step should be to discuss with these governments the proposition of selling hydrogenation rights to the Japanese...Mr. Agnew thought it a good plan to attempt to interest the U.S. military authorities in a modification of the stockholding provisions.” Memorandum of meetings on the Japanese Situation, October 29 and 31, 1935, between Royal Dutch Shell's Agnew and Wilkinson and Stanvac's Walden, Parker, et al., Hydrogenation Patent Hearings, pp.3691-2. Negotiations with the Japanese started earlier than this time, however, and were suspended by the companies due to their own bargaining strategy to withhold offering hydrogenation. During the prior negotiations with Mitsui in 1934, Mitsui did not respond to the hydrogenation license offer. See Frank Howard memorandum, January 17, 1935, ibid., p.2895; letter William Carlisle, general counsel of the cartel's International Association, to Frank Howard, December 20, 1935, ibid., p.3716.

657. See letter from William R. Carlisle to Orville Harden, December 7, 1935, Hydrogenation Patent Hearings, pp.3711-12. This letter was forwarded to Howard and Walden. The companies were motivated to control synthetic fuels technology dispersion around the world, and feared that they had held back selective introductions of their technology too long, allowing rival technologies a chance to win customers, particularly deep-pocketed governments and militaries. See letter from Max Ilgner, I.G. Farben, to Teagle, September 11, 1935, in ibid., p.3711.

323
War departments about the proposed trading of the hydrogenation process." Hombeck refused to assist Parker with diplomatic introductions to Japanese officials regarding the proposed sale, but he did instruct Tokyo embassy officials to "participate in conferences but to take no action vis a vis Japanese authorities." In a statement authorized by Secretary Hull and read to Parker, Hornbeck said:

We are not very happy over a portion of the draft of Standard-Vacuum's proposed cable to Agnew (Sir Andrew of Royal Dutch Shell in London). We perceive no good reason why American representatives of an American company should express "our sympathy with what we think are intended to be the real objectives they (the Japanese) wish to attain; that we are offering our suggestion of hydrogenation assistance with the thought that we would thus be cooperating with them towards attaining such objective...in making their coal supplies readily available for petroleum manufacture" whence "they would always have under their own control during an emergency a substantial source of constant supply." We do not think that sounds well.

Hornbeck specifically relayed the U.S. government position that it "should in no way be associated" with the hydrogenation offer or any position in the negotiations to follow. Hornbeck then pointedly added:

As to the political effect of such an offer and/or transaction, if concluded, we feel that it would strengthen Japan in certain courses of action by Japan of which other governments do not approve. In that connection, we would like, with Standard-Vacuum's authorization, to discuss this feature with our Navy and War departments...we greatly doubt whether the offer, if

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658. See memorandum of conversation between Hornbeck and Parker, December 11, 1935, in Hornbeck papers, Box: 339, Folder: Petroleum Monopoly and Japanese. With this consultation came the implied threat to Stanvac's business with the U.S. navy and army. This business obviously exceeded that with Japan, and if the army and navy disapproved they might decide to react punitively toward the company. However, as noted earlier, the companies apparently felt U.S. Navy pique might help them get what they wanted regarding Japan's stockpile requirement. They assumed Navy pressure on the State department to lessen Japan's oil reserves would work to fulfil their original desires. In this they were, of course, wrong because Hornbeck was the lead and trusted coordinator between State and Navy on oil and exchange in Asia, not a supplicant to the Navy or obvious corporate pressure engineered through it.

659. Ibid. This differs from the prior quota and stockpiling negotiations, in that they were conducted privately between corporate officers and Japanese officials. Therefore, the U.S. government was inserting itself into these negotiations, if only as an observer.

660. Statement approved by Secretary of State Hull and read to Parker of Stanvac by Hornbeck, December 11, 1935, p.3, in Hornbeck papers, Box 339, Folder: Petroleum Monopoly and Japanese.

324
made, will get the results desired. If it so proves, the net result would be to increase the self-confidence of the Japanese and weaken the position of the companies.\textsuperscript{661}

As they had done in 1934, the Mitsui interests did not respond to the hydrogenation offer.\textsuperscript{662} This time, however, the background was the Western companies' threats to embargo Japan's oil supplies and their knowledge that Japan was sending a technical mission to Germany. It appears that Mitsui accurately gauged the insincerity of the oil companies' offer and simply did not want to waste resources in this area. Nonetheless, cooperation with the companies would go forward in some areas. In early 1936, Stanvac was negotiating a unilateral deal with the Japanese government and Mitsui to fulfill the stockpiling requirement.\textsuperscript{663} The British-led interests did not wish to comply

\textsuperscript{661} Ibid., p.2.

\textsuperscript{662} Anderson does not mention this prior offer and misinterprets Hornbeck's role in conditioning the company. Although Hornbeck declared that the State department had "no objection" to the companies negotiating with Mitsui interests, he meant that the department would not advise on negotiation with any particular company in Japan (e.g., the South Manchuria Railway Co.). Hornbeck's use of the term no objection was the standard in the State department informal approval system as identified earlier with respect to loans. The fact that no such statement was uttered regarding the hydrogenation proposal is significant. Instead, many negative statements were relayed, quite pointedly, and can not be construed as having consented to the offer going forward on any basis other than as an "intermediate step" in the quota/stockpile negotiations. Parker assented to this interpretation of Hornbeck. Anderson implies Hornbeck held back from objecting, and therefore the companies were the driving force. Because the matter involved Japanese autonomy and military power directly, Hornbeck could not formally object without placing the U.S. in a disadvantageous position, as they would not do on the oil supply embargo question. As the above statements indicate, he did not lend anything but discouragement to the proposal. More broadly, Anderson misrepresents the point of U.S. "delay and inaction" in responding immediately to corporate pressures. He attributes Hornbeck's "ponderous evasions" to indecision in the face of a dilemma, instead of the clear desire not to confront Japan over non-vital interests (i.e., quota shares of the companies). Hornbeck steered U.S. policy to wait to confront Japan on vital interests when Britain was a full partner, or at a minimum not a buckpassing opportunistic actor using the U.S. to defend its own economic interests in Japan and across Asia. More importantly, delay and continued supply of oil to Japan prevented excess stimulation in Japan to achieve oil autonomy through other means. Commercial reliability then is the hand maiden of dependency maintenance and compromised autonomy. For Anderson's version see The Standard-Vacuum Oil Company, pp.82-3,98.

\textsuperscript{663} Mitsui was only one of the oil companies in Japan, and had at most the fourth largest quota of Japanese marketers in the Japanese market. It was, however, one of the two largest industrial zaibatsu with chemical interests and global distribution networks with whom Stanvac had relied on for years to distribute surplus products within Japan. It did not do much refining either, so the offer of hydrogenation licensing would have necessitated Mitsui re-licensing the process to others. Anderson, The Standard-Vacuum Oil Company p.77; U.S.S.B.S., Oil in Japan's War, Final Report No. 51, Report of the Oil and Chemical Division. (Washington, DC: U.S. G.P.O., February 1946), pp.16-18.
with the stockpiling provisions no matter how artful the requirement could be met through joint stockpiling efforts with Japanese concerns. In this corporate dispute, Hornbeck advised that the best position was to preserve a “united front” among the British and American companies as well as their government interlocutors by simply not complying with the stockpiling provision until forced to by the Japanese government.\textsuperscript{664} If this point were reached, the companies could then threaten to withdraw their operations entirely from Japan or agree to a fixed amount for storage, not a percentage of constantly increasing demand, which would necessitate ever larger stocks.\textsuperscript{665} In February 1936, Hornbeck explained to Stanvac officials that further Anglo-American corporate division was “playing right into the hands of the Japanese Government. (Which) would not, in my opinion, in the long run ensure either property or profits to the American interests.”\textsuperscript{666} Eventually, the companies agreed to cooperate with each other under Hornbeck’s guidance, with Teagle declaring we “must hang together or be hanged separately.”\textsuperscript{667}

This was an apt metaphor for not only the companies narrow sales interests in Japan, but between the companies and their governments. Corporate pressure to research the feasibility of an embargo and then respond to the hydrogenation offer forced the U.S.

\textsuperscript{664} This point was well developed as early as the ONI report from August 1935, and the British government preferred it as well. The U.S. desired a united corporate front because it increased the odds that Britain and the Netherlands would be unable to unilaterally appease Japan by placating its oil interests in British Borneo or the DEI.

\textsuperscript{665} These positions never had to materialize, however, due to changing international circumstances by 1937 and Japan’s desire not to alienate the supplying countries through further agitation of their oil companies. Western governments were also even less enthusiastic about oil pressures due to the failure against Italy and the alignment fallout that resulted from threatened oil sanctions (i.e., German-Italian alliance).

\textsuperscript{666} Memorandum of conversation between Parker and Goold of Stanvac and Hornbeck, February 10, 1936, p. 5, in Hornbeck Papers, Box 340, Folder: Petroleum: Standard Oil Offices, Discussions With 1934-1936.

government to take an informal but negative controlling position vis a vis the oil companies, and then to interject its personnel into the hydrogenation negotiations. These corporate machinations were designed to maintain the more profitable business lines of selling refined products into Japan and in an indirect way to have the U.S. government assist the cartel leaders in obtaining discipline over independent oil companies and Japanese actors interested in oil autonomy through coal hydrogenation (i.e., army, navy and nationalist elites). Stanvac and Royal Dutch did not want to give Japan coal hydrogenation technology that would decrease Japanese demand for the companies' products, instead they wanted to use the threat of this sale to stimulate U.S. governmental action on their behalf. Acting on an even narrower self-interest as primarily crude and refined oil products companies (e.g., gasoline), if necessary, they had planned to license the hydrogenation technology to Japan in order to get it to become less of a competitor in the oil business (e.g., threats to investments in oil source countries like the DEI). Additionally, investing in the hydrogenation facilities was expensive and would "tie(s) up the most capital and tend(s) to put them all together on a noncommercial plane in which their expansion is bound to be limited and in which they are not capable of becoming a disturbing factor outside their own bailiwick." This corporate-planned effect from

669. Frank Howard to Teagle, April 9, 1936, Hydrogenation Patent Hearings, p.3698. This text also cited in Nowell, Mercantile States and the World Oil Cartel, p.246. Howard, Standard Oil's chief official in charge of Hydrogenation-related business operations and future Vice President of Development, was primarily referring to Italian negotiations in this passage, but he did specifically mention that it would be "desirable" for Japan to get over-invested in this technology too. With Italy, the oil giant was seeking to forestall military adventures into the oil rich Middle East, which appeared possible after the invasion of Abyssinia.
exchange is another illustration of how exchange can use up resources, expend and waste capital, and increase economic inefficiency, with the effect of making a country even more dependent.

This corporate logic was offensive to U.S. government interests, precisely because it would grant Japan a measure of autonomous fuel production not tied to imported crude oil. Japan had little supply of crude resources across its nascent empire, and since 1933 had begun to shift its domestic usage and factory production away from fuel oil and back toward coal as much as possible.\(^{670}\) Allowing it to lessen its dependence on distant foreign territories for crude was anathema to the U.S. government, particularly when almost all of the crude it did demand was under the authority of the U.S. and a Dutch East Indies government highly antipathetic toward Japan. Japan’s crude oil and distant territorial dependence was a position the U.S. government did not want to decrease in any way, particularly when the major non-U.S. supply source was a great distance from Japan proper and would force Japan to stretch its naval capabilities to the maximum in any conflict scenario. If war, then interdicting Japanese naval supply convoys would become a paramount objective, and the more necessary the supplies from the DEI the better.\(^{671}\)

Concomitant with this strategic rationale to maintaining Japanese crude oil-based dependency was the U.S. export throughout the interwar period of crude oil refining 670. Since 1932 Japan dramatically increased its coal consumption, registering a 22% increase in 1933 over 1932. An ONI report from the U.S. Naval Attache in Tokyo noted, “some large industries which have within the last three or four years shifted from coal to oil as a fuel are now shifting their plants back to burn coal...plants have received orders from the government to make the shift with the idea of increasing the amount of government oil in storage or at least not reducing the reserves any more that can be avoided.” See ONI Report, Serial No. 2, File No. 408, January 8, 1934, File c-10-b, Register 18992C, RG 38.

671. Since the early 1920s, U.S. Naval intelligence and the General Board had studied the central strategic import of DEI oil to Japan, and tracked Japanese naval officers and planning that emphasized seizure and protection of sea trade between the DEI and Japan.
technology to Japan. This trend accelerated after 1934 with approximately 60% of Japan’s refining capacity constructed between 1934 and 1941. It is not possible to determine the exact percentage of Japanese refining technology and equipment that came from the U.S.. The comprehensive postwar United States Strategic Bombing survey concluded that the vast majority of equipment was either designed or built in the U.S., or produced from copies adapted from U.S. companies. The survey noted: “Japan’s modern refining industry began slowly after the last war and was built almost entirely after American patterns. Most of the equipment was bought outright and Japanese technicians came to the United States to study American methods. The Japanese practice was to acquire the equipment for a plant, then to duplicate the units in Japanese factories.”

Japan’s domestic crude-related refining capacity was in fact overdeveloped, with a 1941 refining capacity of 88,100 barrels of crude oil per day, up from 32,800 barrels per day in 1933. The 1941 capacity was seventeen times larger than indigenous crude production, including the North Sakhalin concessions. This overbuilt capacity demonstrates Japan’s planned for reliance on continued crude imports. Japan accelerated its building of refining capacity and negotiated to acquire different types of refining technologies from the U.S. up through 1940, including for high quality lubricating oils for military aviation. Much of this assistance appears illogical if the U.S. were trying to simplistically limit Japan’s capabilities (i.e., defensive realism). However, if the alternatives as well as the nature of Japan’s dependency on refining facilities from American designs and equipment are considered, this exchange can be better appreciated and understood. Supplying Japan with crude oil refining equipment and related

672. U.S.S.B.S., Oil in Japan’s War, p.23.
673. Ibid., p.16.
technologies ensured two important tendencies. First, Japan would continue to rely predominantly on crude oil in its economic and military consumption and planning, which reinforced its dependence on U.S. and Anglo-Dutch territories and governments. This reliance also would mean domestic capital employed in crude-related projects (e.g., refineries, refining technology licenses etc.) would be both largely expended in the U.S. and detract from alternatives (i.e., coal-based synthetic fuel technologies that might free up Japan’s dependence). Second, reliance on U.S. plans and equipment gave the U.S. capabilities intelligence on Japan, and may have contributed to marked increase in Japanese refining inefficiency shortly before the war and during the war.\(^{674}\) For example, specialty steels and other equipment necessary to efficient refinery operation were in short supply by 1940 and altogether lacking in some key parts, forcing Japan’s engineers to either cobble together solutions that were inefficient and wasteful, or to let the projects lie fallow.

These foregoing reasons and an underlying desire to maximize the United States’ possible influence over Japan’s strategic decision making account for the large and increasing U.S. export to Japan of petroleum, crude-based refining goods and technologies after 1934. To be sure, U.S. officials were not omniscient in understanding all of the effects of the various refining technologies, both crude-based and coal. For

\(^{674}\) For example, in August 1939, a Japanese mission to the U.S. composed of army, navy and civilian oil technicians wanted to buy the design for a thermal cracking unit capable of processing 3,000 barrels of crude per day and distilling another 6,500 barrels. “In order to provide the necessary basis for design, they were obliged to reveal that cooling was to be by river water, the piling was required for foundations and that salt water lay three feet below grade.” *Ibid.* p.24. Information like this was constantly reported in ONI reports and likely relayed to U.S. intelligence by the U.S. firms involved in the negotiations, although specific communications of such between the firms and ONI were not found. This stands in contrast to the early 1920s when such specific communications were evident in ONI reports. Their absence does not indicate, however, that these communications ceased, only that they are still undisclosed. See entire ONI file detailing purchases of U.S. processes and synthetic efforts in Japan for 1936 at File e-10-d, Register 13177G, RG 38.
example, after Standard had withdrawn its sketchy hydrogenation offer to Japan, Hornbeck and Teagle had a long private dinner where they “fully” discussed “the oil situation in general and problems relating thereto in Japan in particular.” During the discussion, German hydrogenation production was brought up and its total amount noted to have increased significantly. But, it was still not even equal to the yearly increase in total consumption of crude and other products in Germany from 1934 to 1935.\textsuperscript{675} It appears that Hornbeck and Teagle concluded that hydrogenation, while technically significant, was not sufficiently developed to even cover yearly increases in total demand, let alone fulfill total demand and replace the crude oil basis of energy consumption and power projection.

Regardless of this early oversight of the technological challenge to come from Germany, Hornbeck and other U.S. strategists were fully aware of Japan’s crude vulnerability. They chose to reinforce that vulnerability by allowing increased amounts of both crude oil and related equipment to go to Japan, while blocking the sale of hydrogenation equipment. They did so with the increasing knowledge that employing that vulnerability for political purposes at any time would entail the near certainty of a Japanese attack on the DEI and probably U.S. and British installations along the way that might defend against such seizure. For these reasons, this intricate period of exchange negotiation is most consistent with offensive realism because the state ensured exchange and non-exchange outcomes that reinforced Japan’s crude oil import vulnerability and strategic dependence on distant territorial resources. Defensive realism is not consistent

\textsuperscript{675} See enclosure from Walter Teagle to Hornbeck detailing total crude and synthetic production, import/export and consumption figures in Germany for 1934 and 1935. See letter from Hornbeck to Teagle, March 24, 1936, in Hornbeck Papers, Box 408, Folder: Teagle, Walter C.
with supplying Japan with the equipment and technical know-how that might and did yield Japan increased production (i.e., relative material capabilities increased).

There is, however, substantial support for the liberal and marxist propositions regarding corporate pressure for state coercive power to fulfill their narrow business agendas. In this instance, that included threatening to greatly increase the autonomy and power of Japan and even declaring sympathy for Japan's desire to achieve such autonomy. In the final analysis, however, the companies' positions were not supported. The independents continued to supply Japan and thwart cartel control because the U.S. never considered complying with the companies' desire to threaten use of the oil embargo weapon against Japan. Furthermore, the oil companies were conditioned for the future by being reminded that the greater part of their future business lay with the U.S. army and navy, not Japan. To maintain this, they were thus guided as well into no further investment in Japan, demonstrating state authority over corporate investment decisions.

6.5 The International Situation: Intended and Unintended Consequences of Economic Alignments and America's Economic Policy

Japan was no longer content to wait for autonomy-enhancing offers of economic and political cooperation from the Anglo-American powers. When her army and Manchurian economic leaders embarked on the aforementioned technical mission to Germany in December 1935, they began to form the economic ties that would bind the two states' mutual self-interest against the Soviet Union and curtail the substantial German military and economic assistance to China that Japan reviled. Dr. Abe led the technical investigations of synthetic fuels in Germany while German members of a trade
mission negotiated with Japan on a new trade agreement covering Japan and Manchukuo that would yield de facto recognition of Manchukuo. These negotiations led to an important overarching economic agreement and a specific agreement with Ruhr Chemie AG to transfer to Mitsui the synthetic fuel technology it possessed-- the Fischer-Tropsch process. The Economic Agreement reached in April 1936 was a significant signal of Germany’s desire to pay extra to begin their entente for two reasons. First, Germany had more significant trade relations with China than it did with Japan at the time (e.g., a 56.2 million Reichsmark surplus in 1936). It was lending large sums of money to China and assisting China’s military directly with army advisers and production of war materials. Germany’s overtures to Japan entailed substantial risk to these economic gains due to likely hostility from Chiang Kai-shek. More importantly, the exchange between them would effectively be based on barter trade between them, specifically Manchurian soybeans for German industrial goods. Second, Germany’s General Staff and the Head of the Military-Economic section in the War Ministry concluded that “Japan’s military-economic base has not been secured. In view of Japan’s dependence on overseas supplies, economic sanctions could seriously damage its conduct of war.”


677 This process, not covered by the oil-hydrogenation cartel arrangement with IG Farben, was thought to be inferior by many in the oil business, but did show signs of German innovation at this time. See memorandum by Heinrich Riedemann, London Council of the International Association, February 11, 1936, Hydrogenation Patent Hearings, pp.3699-3701.

678 Chapman, “The Have-Not’s Go To War: the Economic and Technological Basis of the German Alliance with Japan,” p.29.
Despite their economic self-interest and Japan's relative vulnerability, Germany began to forge the ties with Japan to build its capabilities to some point where it would threaten Soviet interests in the Far East enough to give Germany an easier hand in Europe. Hitler pointedly told Oshima Hiroshi, then Japan's military attaché in Berlin and later Ambassador to Germany, of his intention to "split up the Soviet Union into several small states." Their economic and military exchanges blossomed into the Anti-Comintern Pact signed on November 25, 1936, which had the backing of both Japan's army and navy despite the army's more lusty desire for it. For each party the courtship would have negative repercussions in England, China and the U.S. But, both were willing to court that fallout because each thought the pressure on the Soviet Union would redound to his benefit. Germany thought it might be able to gain with another Russo-Japanese conflict, while Japan believed Hitler might attack East against the Soviet Union first, end Germany's assistance to China and transfer synthetic fuels technologies. These calculations would increase in importance later after the outbreak of the Sino-Japanese war in July 1937.

Each country was also willing to court Anglo-American antipathy because it appeared to both that any Anglo-American concord against them was a fleeting prospect, one best kept in abeyance through strong diplomatic and military measures. Japan was more cautious than Germany in its relations with Britain, hoping still in 1936 not to inadvertently forge Anglo-American harmony. Those Japanese elites who espoused this in particular, however, would see their position unravel with the invasion of China proper

680. Ibid., p.44: Crowley, Japan's Quest for Autonomy, pp.304-6: Frank William Ikle, German-Japanese Relations, 1936-1940. (New York: Bookman, 1956), pp.36-43. Japan's navy appears to have believed that disrupting the European situation would redound to its benefit in Asia, through deal cutting agreements with France and Britain.

334
and the direct threats to British interests in China. Prior to that, the Anglo-American and
League of Nations reaction to the Italian invasion of Ethiopia in early October 1935
helped instill a feeling that economic sanctions can be avoided by purposeful action. As
in the post-Manchurian invasion debates, the League of Nations sought to bring the U.S.
into deliberations and the State department was communicating with Britain on the
feasibility of sanctions. Hornbeck, in particular, seemed desirous of redressing the
failures of the past through joint action with Britain, and by extension sending signals to
Japan in Asia. He believed the Italian aggression provided an “unusual opportunity” to
step forward with Britain “in pursuit of common objectives.” He held, “if we act together
we can determine the direction of events...a great objective of our foreign policy is that
there be cooperation between Great Britain and this country.”

Unfortunately, Britain and France decided to take oil sanctions against a near
totally import dependent Italy off the League’s table in early December 1935 (i.e., the
infamous Hoare-Laval appeasement deal). They did this in order not to push Italy into an
Italian-German alliance, but their dithering while continuing to negotiate the threat in the
League had precisely that effect. The U.S. was not much better, however, as President
Roosevelt and Secretary of State Hull were reduced only to labeling American companies
supplying Italy with strategic goods as acting against the “general spirit” of the recent
neutrality act. Worse still was Hull’s pleading that they should not satisfy Italy’s
increased demand for oil in particular to satisfy their own profits. Meanwhile, Britain

681 Memorandum from Hornbeck to Secretary of State, September 28, 1935, in Hornbeck Papers, Box
369, Folder: Sanctions.
682 Williamson Murray summarized the nature of German-Italian joint strategic opportunism: “on the
brink of the imposition of oil sanctions on Italy, the Germans remilitarized the Rhineland. The resulting
crisis led to a postponement of the oil sanction question....when the dust settled, Abyssinia collapsed and
the German army was in the Rhineland.” Murray, The Change in the European Balance of Power (Princeton,
and France buckpassed to the U.S. on oil sanctions, declaring effective sanctions required stoppage of U.S. supplies to Italy, and blamed the U.S. for not doing what they wouldn’t do either. To be sure, Teagle’s Standard Oil was supplying Italy and in increased amounts in late 1935 and into early 1936, but U.S.-based supplies were not large at approximately 10% of Italian imports (i.e., Standard supplied Italy from non-U.S. sources in the Middle East). Standard was also publicly cowed into relinquishing an oil concession signed with Ethiopia on the eve of Italy’s conquest, thereby removing a source of friction in U.S. policy in the conflict. Ever the defender of business interests and their pacifying effects, Teagle dissembled regarding his company’s scruples and enlightened purpose in supplying Italy in an April 26, 1936, Collier’s magazine article. He declared: “I firmly believe that the best preventive of international conflict is greater freedom for international trade. For trade rests on understanding. It endures so long as buyers and sellers deal with one another in good faith.”

The Italian non-oil sanctions episode established the firm precedent that oil sanctions, or even their threat, will push countries toward reaching out for secure oil positions. For Italy this meant closer ties with Germany and hopeful joint pressure on Romania for supplies. For Japan, the U.S. understood clearly that it would mean southern advance toward the DEI, particularly in light of decreasing oil cooperation with the Soviet Union and decreasing DEI supplies to Japan after the peak year of 1935 (See Tables 6.1 and 6.2). The Soviets were fully aware of Japan’s economic and military

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683 Dallek, Franklin D. Roosevelt and American Foreign Policy, p.118.
684 Walter Teagle. "Oil and War." Collier’s Weekly, April 26, 1936, p.76. Of the concession, Teagle said, “it appear(ed) that the contract might involve the United States in the trouble between Italy and Ethiopia. Although they themselves did not share this apprehension, the Standard-Vacuum officials at once went to Washington, offered to cancel the concession and did so when the State Department accepted the offer.” Ibid. Implicitly, Teagle admitted the superordinate position of State to approve of concessions in this remark, and this case helped confirm the company’s growing subordinate position.
outreach to Germany, and its important oil-substitute basis. The Soviets reacted by
dithering on renewal of N. Sakhalin oil contracts, accepting only a revocable 2 year
extension of the initial 10 year deal from 1925. They further refused to make sales from
their part of N. Sakhalin to Japan in 1936, selling instead to Standard Oil of New York.
This opportunistic form of preclusive buying on the part of Standard Oil of New York
coupled with Soviet intransigence in making sales to Japan further stimulated Japan’s
desires to reach synthetic technology accords and later mutually self-interested military
alignment with Germany.

<table>
<thead>
<tr>
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<th>1933</th>
<th>1934</th>
<th>1935</th>
<th>1936</th>
</tr>
</thead>
<tbody>
<tr>
<td>From DEI to Japan in millions of gallons (% of total DEI crude and fuel exports)</td>
<td>117.4 (8.4%)</td>
<td>114.2 (7.3%)</td>
<td>145.6 (10.3%)</td>
<td>136.3 (8.2%)</td>
</tr>
<tr>
<td>From U.S. to Japan in millions of gallons (% of total U.S. crude and fuel exports)</td>
<td>450 (19.5%)</td>
<td>617 (21.9%)</td>
<td>831.3 (25.5%)</td>
<td>824.8 (24%)</td>
</tr>
<tr>
<td>From North Sakhalin in millions of gallons</td>
<td>90</td>
<td>87.4</td>
<td>67.8</td>
<td>50</td>
</tr>
<tr>
<td>Minimum in millions of gallons from other sources including British Borneo, Persia, Manchukuo and Russia</td>
<td>14</td>
<td>79.4</td>
<td>N/A</td>
<td>N/A</td>
</tr>
</tbody>
</table>

Table 6.1: Japanese Imports of Crude and Fuel Oil, 1933-1936

Japan’s percentage of DEI exports are taken from Anderson because accurate DEI total export statistics
were not available. DEI production amounts were available and indicate for the peak export year of 1935
that only 7.3% of DEI crude production was exported to Japan. This crude figure likely includes the DEI

685. Stalin received accurate information from a correspondent of the Frankfurter Zeitung who was trusted
by Eugen Ott and Friedrich Hack, the German Military attaché in Tokyo and the chief German-Japanese
686. The details of the politics, if any, of this transaction are not reported anywhere. See ONI reports
detailing these events and for copy of Japanese article that explained them as well by Dr. Takeo Mori
titled “Oil in the Orient and South Seas.” ONI Reports, January 9, 1936 and April 16, 1936, File e-10-d,
Register 13177G. RG 38
fuel oil production amounts in it as was customary in DEI statistics, but if it did not the percentage would be even lower. Data from U.S. Department of Interior, Bureau of Mines, Minerals Yearbooks, 1933-1936; Anderson, The Standard-Vacuum Oil Company, pp.223-7; Lindblad, “The Petroleum Industry in Indonesia;” ONI Report, Serial No. 131, File No. 906-400, May 16, 1934, File e-10-d, Register 13177F; Serial No. 222, File No. 906-400, September 17, 1935, File e-10-d, Register 13177G; Serial No. 237, September 2, 1937, File e-10-d, Register 131771, RG 38.

<table>
<thead>
<tr>
<th>From DEI to Japan in millions of gallons (% of total DEI gas exports)</th>
<th>1933</th>
<th>1934</th>
<th>1935</th>
<th>1936</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>78.5</td>
<td>9.6</td>
<td>22.1</td>
<td>1.4</td>
</tr>
<tr>
<td></td>
<td>(17.5%)</td>
<td>(1.8%)</td>
<td>(3.7%)</td>
<td>(0.2%)</td>
</tr>
<tr>
<td>From U.S. to Japan in millions of gallons (% of total U.S. gas exports)</td>
<td>43.3</td>
<td>45.3</td>
<td>29.4</td>
<td>45.4</td>
</tr>
<tr>
<td></td>
<td>(3.7%)</td>
<td>(4.7%)</td>
<td>(2.4%)</td>
<td>(4.4%)</td>
</tr>
<tr>
<td>Minimum in millions of gallons from other sources including Russia, Malaya and Peru</td>
<td>95.3</td>
<td>86.3</td>
<td>N/A</td>
<td>N/A</td>
</tr>
</tbody>
</table>

Table 6.2: Japanese Imports of Gasoline, 1933-1936\(^a\)

President Roosevelt accurately observed these trends in Asia and their interconnection with Europe, noting that another “general war” appeared likely. He summarized the consequences of the ominous trends for Anglo-American comity to his cabinet in late December 1935:
The international situation is very grave indeed...there is an understanding between Germany and Japan which may result in a squeeze play against Russia. Great Britain, concerned as usual for the Empire, and anticipating what a threat this combination would be against British colonies, especially in Asia, [has] decided to come to some sort of an understanding with Hitler.687

As part of Roosevelt’s strategy of binding Britain to the U.S., the two powers reached a new naval arms agreement in early 1936. Despite the failure of an early British effort to include Germany in the discussions with attendant negotiations on Germany’s rearmament and treaty breaches, the U.S. and Britain reached a basic accord allowing each to build what it deemed necessary (e.g., 35,000 ton battleships for the U.S.). They agreed on an advanced building notification system, whereby communication of intent was better instituted and on the basic principle of Anglo-American fleet parity. In fact, the British seemed to desire American naval expansion, provided the U.S. did not use British building as an excuse to the American public to justify its own expansion.688 This was particularly the case after Japan’s withdrawal from the naval treaties and their underlying political understandings convinced increasing numbers of the British delegation that Japanese naval expansion was “even more a menace to the security of the British Empire than to that of the United States.”689 Despite an inclination to appease dissatisfied powers with naval arrangements (e.g., June 1934 Anglo-German naval treaty), Britain stayed with the U.S. position of leaving responsibility for the end of the Washington system on Japan. There was always, however, a U.S. fear that Britain might cut a deal with the Japanese in Asia, leaving America holding the sole responsibility for

687. Dallek, Franklin D. Roosevelt and American Foreign Policy, p.117.
688. See memorandum of conversation on Naval Armament among Hull, Hornbeck, Norman Davis, Chief delegate to the talks, Rear Admiral Pye and Commander Schuirmann USN, March 12, 1937, in Hornbeck Papers Box 308, Folder: Navy, 1931-1938.
balancing Japan and indirectly protecting Britain's Asian empire. To avoid this, the U.S. sought to forge Anglo-American harmony in threat perception of Japan.

In order to best secure the interests and position of the United States, Roosevelt followed the advice of Hombeck from early 1934. Hombeck declared that the United States should first understand that it "has no Far Eastern Policy separate from our foreign policy in general," and that "we should make our tactics those of delay." Although an unlikely outcome, this position sought not to directly confront Japan so as not to give it and Britain any grounds to reach some strategic accord that would give Japan an even freer hand in Asia. The concrete manifestations of this policy included assistance to China in military aircraft and limited financial supports, while continuing to export large quantities of important materials to Japan. Hombeck noted the strategic reality of military bipolarity in the Pacific: "there are however, in and on the Pacific Ocean, facing and faced by each other on that ocean, two great powers, and only two: the United States and Japan." As a result of U.S. policy seeking to use China to test Japan's capabilities without overly harming U.S.-Japan relations, the U.S. should "not go out of our way" in making gestures of "good will" to Japan or to China. Instead, the U.S. should balance its support of both being "neither more cordial or less cordial" to either country.

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692 As an example of concern for this, ONI analysts were tracking Japanese production from the limited oil concessions they did have in British North Borneo and found as of October 1936 they were producing 13,640 barrels per day (i.e., 571,200 gallons). These figures may or may not be accurate, but they highlight the navy-oil-alliance relationship concern. See ONI Report from Naval Attaché in Tokyo, Serial No. 248, File No. 407, File e-10-d, Register 13177G, RG 38.
693 Hombeck strategy memorandums, quoted in Borg, The United States and the Far Eastern Crisis, pp.118-9.

340
balancing for tactical advantage was tested as noted earlier by aircraft and loan supports for the Chinese government, which placed the U.S. and British governments at odds commercially as well as strategically divided vis a vis Japan.

In an effort to avoid Anglo-American division over China and possibly not coincidentally to allow Japan to pressure both China and British interests in China, Roosevelt allowed large U.S. purchases of silver under the Silver Purchase Act of June 1934 to come from China and from China through Japan by way of its army's economic opportunism in North China. Roosevelt was certainly motivated to maintain the silver purchases for domestic reasons (i.e., Western states political support and Senator Key Pittman in particular), which remain the dominant explanation of his policy. However, U.S. passivity toward financial instability in China also occurred at the same time that Chiang Kai-shek had terminated America's military aviation assistance in favor of an Italian government-led package inspired by Chiang's tilt toward Mussolini and continued reliance on German army advisers. The Italian venture organized a sizable export promotion effort and threatened U.S. aircraft exports which declined in 1934, even before the silver crisis took hold. Roosevelt may have been motivated to allow China to suffer somewhat for this, and he and leaders at the State department were adamant about not getting out in front of Britain in solving China's financial crisis which the U.S. had caused.

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694. Dallek, Franklin D. Roosevelt and American Foreign Policy, pp.93-4.
695. Young, China's Nation Building Effort, pp.353-355. Young does not make the link in U.S. policy between the Italian venture and U.S. silver policy, except to note the Italian venture collapsed after 1935, but not before China's U.S.-assisted air power capabilities had been set back.
696. Xu, "The Eagle and the Dragon's War Wings," p.245. China absorbed approximately 20% of U.S. aircraft exports and helped stimulate this strategic industry in the U.S.
697. The British led by Neville Chamberlain and then Sir Frederick Leith-Ross sought to create Anglo-Japanese harmony through various proposals to Japan. For example, they proposed a loan to Manchukuo.
The possibly unintended effect of this policy maintenance was to encourage the Japanese army in Manchuria and North China to continue to advance against China and smuggle silver out for re-export to the U.S. directly and through re-exports from Britain to the U.S.. Japan's advances greatly undermined Chinese authority across all of China, but particularly in North China where Japan formed puppet regimes in late 1935. This Japanese advance against China was partly caused by its changed economic relationship with the U.S.. Japan needed monetary assets (i.e., silver) to pay for its excess import needs from the U.S., and therefore purposefully expanded into North China to acquire these reserves while the U.S. was buying silver. In fact, the threat of U.S. ending its silver purchases probably caused Japan to act more rapidly than it otherwise would have. This interpretation is different than the prevailing one that asserts Japan's economic ties with the U.S. increased only after its needs increased due to expansion in China. It is arguably the case that rationed U.S.-Japan trade furthered Japanese trade imbalances which then helped cause Japan's expansion into China for silver, later destroying any possible cooperation with the British. An even more cynical interpretation would hold that instability and conflict in North China hindered Japan's ability to harness the resources there for its war material mobilization, and therefore ought not be dissuaded from continuing if it begins of its own accord. This

which would then be transferred to China as both compensation for its loss of Manchuria and usable for currency stabilization. These entreaties were rejected by Japan, who "was determined to show that it would not allow Britain to interfere with the spread of Japanese influence in East Asia, where 'Japan alone could act as a stabilizing power.'" Kibata, "From the Manchurian Incident to Pearl Harbor," p.11.

698. Ashbaugh, "The Yardstick of Trade," pp.292-300; Barnhart, Japan Prepares for Total War, pp.39-42. At least 200 million ounces of Chinese silver were smuggled out between 1934-5.

699. This is the position that Snyder, Kupchan and Liberman take, although they tend to make the argument more strongly for the post-July 1937 invasion period.

700. There is not much evidence to support this interpretation so it is advanced with much caution. However, the ONI was tracking Japanese deliberations on China policy highlighting the connection between the mineral needs of Japan and a necessary peace with China to secure them. See for example,
interpretation carried with it the secondary effect of increasing the likelihood that Japan would threaten British interests in China more directly, and therefore better align British policy with the U.S..

Before these cynical assessments of U.S. intentions took root, Roosevelt cooperated with the British-led Leith-Ross negotiations to stave off total financial collapse in China. The U.S. cut down on large foreign purchases of silver from both governmental and non-governmental sources, principally allowing only the Chinese government to use silver in exchange with the U.S. Treasury as part of its currency stabilization. This cut back on Japanese direct exports of silver to the U.S., but did not end their effect because silver was re-exported by Japan through Britain to the U.S., earning the foreign exchange Japan needed.\textsuperscript{701} The U.S.'s bilateral arrangements to stabilize China's finances required China to keep silver balances in New York, while using dollars to help stabilize its domestic economy, in addition to British and Japanese loan and currency arrangements. The U.S. government believed it had successfully led Britain to take an active lead in Chinese affairs in a way that did not focus Japanese resentment on the U.S., and had instead generated a mildly positive cooperative outcome.

\textsuperscript{701} See Henry Douglas, "America Finances Japan's 'New Order'." \textit{Amerasia}, Vol. IV, March 1941, pp.221-224. It is not insignificant that Neville Chamberlain was Chancellor of the Exchequer and facilitated these re-exports that assisted Japan's finances at China's expense.

\textsuperscript{ONI Report on Japan's Budget Committee of House of Peers, February 25, 1935; wherein Baron Iwakura Michimoto held "at such time as we may conclude an entente with China, we must turn our attention to those of China's oilfields such as at Szechwan." ONI Report, August 20, 1935, File e-10-d. Register 13177F, RG 38.}
among the three naval powers. The result of this for Britain was, however, that in November 1936 Japan listed Britain for the first time as a potential enemy in its “Plan for Imperial Defence.”

This instance of direct and indirect monetary asset exchange between Japan and the U.S. is difficult to evaluate in terms of the theories expected observations. The U.S. government was engaged in the exchange and knew of the consequences of its purchases and corporate interests were not involved. Domestic silver interests remain the dominant explanation for the silver policy, but its continuance, “hastening the crisis” in China, was Roosevelt’s purposeful choice. He declared that it would undermine Japan’s position, but it is not clear how he meant this to occur, and therefore is only noted as state dominant and important exchange.

One of the casualties in Japan’s advance through Manchuria and China was National City Bank’s Manchurian operations. They closed their operations there in March 1935. Hornbeck expressed the U.S. government’s general satisfaction in this event, noting their closure was “interesting in the light of propaganda which certain representatives of that bank were conducting a year or two ago to the effect that Japanese...

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702. Kibata, From the Manchurian Incident to Pearl Harbor,” p.12; Borg, United States and the Far Eastern Crisis, pp.136-7. Japanese resentment at efforts to affect Chinese stability was beginning to be directed against Britain. Ian Nish summarized the paradoxical results of British policy: “It was, of course, a strange irony that the Leith-Ross mission - in some ways the brainchild of the Chamberlain-Fisher circle, which might be described as ‘pro-Japanese’ - was widely regarded in Tokyo as an example of confrontation.” Ian Nish, “Anglo-Japanese Alienation Revisited,” in Saki Dockrill, ed., From Pearl Harbor to Hiroshima: The Second World War in Asia and the Pacific, 1941-45, (New York: St. Martin’s Press, 1992), p.18.

703. Roosevelt said, “it is better to hasten the crisis in China-to compel the Chinese people more and more to stand on their own feet without complete dependence on Japan and Europe.” Roosevelt memorandum to Treasury Secretary Morgenthau, December 4, 1934, quoted in Blum, From the Morgenthau Diaries: Years of Crisis, 1928-1938, p.206; Dallek, Franklin D. Roosevelt and American Foreign Policy, pp.93-94.
control in Manchuria was a blessing." Hornbeck established the terms of U.S. support for American businesses abroad, contending that any business that acts in ways that put them into positions where belligerents may injure them would and should properly do so at their own risk, with no expectation of governmental support (i.e., U.S. navy protection, diplomatic representation of grievances etc.). When it came to safeguarding the rights of American businesses threatened by Japanese laws, the U.S. did not always act with equal vigor, however. For example, a comparison of diplomatic support for aggrieved U.S. companies with direct investments in Japan is warranted, and particularly stark between the American auto and oil companies.

Standard-Vacuum Oil Company's direct investments in Japan were estimated at approximately $7.7 million dollars in 1940 and these values represented those in 1936 as well due to the U.S. admonition against further investment. While accurate estimates of Ford and General Motors investments are not available, it is clear from various sources that the combined value of Ford and GM investments probably exceeded those of Stanvac. Ford and GM made initial investments of a combined 12 million Yen in 1924 (GM 8 million and Ford 4 million Yen) when average exchange rates were approximately $.42 per Yen, or approximately $5 million dollars. These investments were added to by both companies throughout the 1920s, who also wholly-owned their subsidiary operations unlike other American companies in Japan. Ford estimated its direct investments in Japan in 1941 at $3.87 million dollars. Because GM's operations were at least as large as Ford's, its investments were likely at least that large, and probably larger.

704 Hornbeck was referring to John Curtis of National City Bank. See memorandum from Hornbeck to William Phillips, Undersecretary of State, and Secretary of State, April 1, 1935, in Hornbeck Papers, Box 90, Folder: China: Open Door Policy.
and combined auto investment was therefore likely above $8 million dollars.\textsuperscript{706} Together these three industrial giants controlled at least one-third of U.S. direct investment in Japan in 1936. This is partly because the value of U.S. direct investment dropped from $61.45 million in 1931 to $46.7 million in 1936 (See Table 6.3).\textsuperscript{707}

As already detailed, the State department managed Stanvac's demands for representation before the Japanese. The department devoted considerable time and energy to this company's demands, while preserving the U.S. government position which maintained Japanese crude oil dependence. Did the State department devote anywhere near the attention to the market problems of GM and Ford, who both sold far more to Japan than other markets in Asia? Given the domestic position emphasis of liberalism and marxism and the fact that GM and Ford were more important to the U.S. domestic political economy than Standard Oil of New Jersey (i.e., in terms of employment, production value etc.), did they receive some rough equivalence in diplomatic representation as the private interest-derived theories would expect?\textsuperscript{708} The short answer is no. The U.S. did little more than lodge its displeasure with the Japanese government and its efforts to displace Ford and GM's entire businesses, which was apparent by 1935.

Even Secretary Hull's emphasis was different. He noted, "the problems created by

\textsuperscript{706} See Mira Wilkins, "Contributions of Foreign Enterprise." p.49.
\textsuperscript{708} Data for 1939 show the motor vehicle industry employed four times as many people as petroleum, and contributed twice as much production value. In 1939, U.S. employment in motor vehicles was 459,000, while petroleum was 101,000. This motor vehicle sector contributed $4.04 billion dollars in production value, while petroleum was $2.461 billion dollars. Data from closest year of 1939. See U.S. D.O.C., Bureau of Census, Census of Manufacturers: 1939, (Washington, DC: U.S. G.P.O., 1940).
Japanese legislation which place onerous burdens upon foreign oil companies and Americans doing business in Japan have had our constant attention as has the question of safeguarding American automobile interests.”

Both auto companies were eager to supply Japan in its war mobilization, but the Japanese government was intent on substituting for them with domestic producers. In fact, the auto companies fully understood Japan’s mobilization for war was afoot, with the increased demand for trucks and other transport goods, and they wished to supply that mobilization. Later efforts to find joint venture partners and even whole purchasers of the auto companies’ assets did not succeed, and the companies were left struggling to remit back to the U.S. some of the profits they had amassed since the mid 1920s. This comparison adds weight to the contention that those industries that matter most to relative military power projection capabilities will receive disproportionate representation and direction by government officials abroad. The relative domestic position of the auto and oil companies does not appear to have been a factor at all (i.e., liberalism not very explanatory). Perhaps liberalism can be amended to stress that it is those contending interests abroad that are most capable of upsetting the state’s relative power position who are the weightiest and most influential in state policy.

It must be admitted, however, that the company willing to threaten the state with greatly assisting the rival’s autonomous capabilities received more attention to its preferences (i.e., the oil companies and their hydrogenation sale offer). The fact that the

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709. Secretary of State Hull’s testimony before the Subcommittee of the House Committee on Appropriations, February 3, 1936, in letter from Hornbeck to Parker, April 3, 1936, in Hornbeck Papers, Box 339, Folder: Petroleum Standard Vacuum Oil Co.
711. Interestingly, the Japanese Finance Ministry effectively forced the companies to buy Japanese “China Incident” war bonds before being allowed to exchange Yen profits for dollars in 1937 and 1938. Ibid., p.55, footnote 94.

347
oil companies had purposefully threatened U.S. relative power in this manner after trying to forcibly invoke the state's coercive power on their behalf, does lend some credence to the marxist hypotheses regarding corporate behavior. Despite their failure to achieve their preferences, their agitations among the various governments did certainly affect the structure of state interaction, particularly between the U.S. and Japan (e.g., diplomatic representation assistance in oil executives meetings with Japanese officials).\textsuperscript{712} This instance was reminiscent of the jockeying among the oil companies in 1920-21 regarding investment rights in the DEI. If GM or Ford had offered to build Japan tanks instead of trucks maybe the State department would have aggressively intervened with them and on their behalf as well.

National City Bank, the largest U.S. bank in Asia, fared worse in terms of U.S. government assistance. In fact, as noted above earlier, their destabilizing role in the dollar-yen selling episode 1930-31, open lobbying for Manchukuo recognition and continued support of Japan against China, earned them little support within the U.S. State department. This became particularly evident by the end of this period, when they were forced to begin closing down branch operations in Manchuria and China as Japan's army and then its banking interests took over. The State department did nothing on National City's behalf, barely deigning to meet with its officials to discuss general issues regarding the Far East.

\textsuperscript{712} The companies also affected U.S.-British government relations, exposing the continued vacillation and buckpassing of Britain.
U.S.-Japanese exchange in this period narrowed considerably from the prior periods due primarily to the loan ban instituted by the State department and the informal guidance offered to companies to make no further investments in Japan (e.g., Stanvac). More importantly, under Hornbeck's guidance, the U.S. began to "ration" Japanese imports, restricting Japanese exports to the U.S. and other dollar-earning areas (e.g., Philippines) in managed trade agreements (e.g., cotton piece goods "Gentlemen's Agreement"). This policy had an intended interactive effect on Japan's capacity to finance its growing trade imbalance with the U.S., which increased Japan's vulnerability to and dependence on the U.S.. By managing continued Japanese trade imbalances, the U.S. was forcing Japan to expend its foreign currency holdings in addition to exporting silver and then gold to sustain its needed imports. As a result of these governmental actions, Japanese gains from exchange with the U.S. were reduced overall from the prior period, despite increases in Japan's imports from the U.S. across the period.

Cumulative U.S. investment in Japan declined during this period, as no new direct investments in or loans to Japan were made by American companies, while some existing U.S. loans were paid off by Japanese borrowers and some U.S. direct investors pulled out of Japan. As a result, total U.S. capital exposure to Japan in 1936 dropped to $370.5 million dollars from the value in 1931 of $453.6 million dollars. Because no new loans or direct investments were forwarded to Japan, the percentage of U.S. capital in

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713. This finding obscures the fact that the Japanese government transferred much of the private industry foreign debt to itself in early 1934. Robert Samuels describes this process, but doesn't demonstrate that this debt was not paid off. Rather it was merely assumed by the Japanese government. Samuels, The Business of the Japanese State, p.142.

349
Japan's total gross fixed domestic capital formation during this period was 0%, indicating that Japan was relying on its own financial resources and domestic debt issuances to fund domestic investment. Of the remaining U.S. direct investments in Japan a little over half were in manufacturing as opposed to sales distribution investments, suggesting Japan continued to receive capabilities enhancement from U.S. direct investment. Japan did receive indirect financial support through the purchases of silver throughout the period (See Table 7.3 in next chapter for full listing). These amounts were not small, particularly the silver exports to Britain, which were largely re-exported to the U.S. Direct U.S. purchases of Japanese silver were approximately $4 million dollars, but the re-exports from Britain would put the indirect financing to Japan at approximately $60 million dollars.

<table>
<thead>
<tr>
<th>Direct Investments</th>
<th>$ 46,694,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Portfolio, Japanese National Government</td>
<td>$146,145,000</td>
</tr>
<tr>
<td>Portfolio, Japanese Municipal Government</td>
<td>$ 34,409,000</td>
</tr>
<tr>
<td>Portfolio, all other</td>
<td>$143,246,000</td>
</tr>
<tr>
<td>U.S. Total Capital Exposure (TCE) to Japan</td>
<td>$370,494,000</td>
</tr>
<tr>
<td>U.S. TCE/Japanese Domestic Capital Formation</td>
<td>0%</td>
</tr>
</tbody>
</table>

Table 6.3: Cumulative Value of U.S. Investments by Type, Aggregate Amount end of 1935/1936

\(^2\) See Lewis, America's Stake in International Investments, pp.653-7: See U.S. D.O.C., B.F.D.C., American Direct Investments in Foreign Countries-1936, p.16.
The U.S. trade relationship with Japan increased in value during this period, largely due to increased economic growth in Japan, and U.S. policy seeking not to use trade to confront Japan directly. The trade in raw cotton and cotton goods provides a useful example of how the U.S. used trade to constrain Japanese financial autonomy efforts, while allowing itself to become somewhat vulnerable to Japan. Although the U.S. imposed quotas and tariff increases on Japanese cotton goods exports, it did so through executive branch fiat not congressional or domestic interest group pressures. The common explanation of these trade restrictions has been that the government reacted because domestic employment and production were threatened by Japan, as they were. But, the U.S. government had a strategic reason to restrict the same trade in ways that didn’t necessarily fully protect only domestic producers’ interests. In raising the price of exported raw cotton through an effective cotton export tariff and limiting the cotton products coming back to dollar-related markets, the U.S. was worsening Japan’s terms of trade and making it harder for Japan to earn the dollars necessary to finance the more expensive raw cotton imports.\footnote{\textsuperscript{714}}

During most of this period, Japan relied on U.S. cotton more than the Indian substitute. They did so not only because of the trade dispute with Britain, but also due to the better quality of U.S. cotton. From 1933 to 1936, the U.S. supplied 47.8\% of Japanese\footnote{\textsuperscript{714}. This cycle served to reinforce Japanese dependency on the U.S., much like the sale of crude oil refining technology maintained, if not increased, Japan’s dependency on U.S. crude.}
raw cotton imports, while India supplied 40.5%.\textsuperscript{715} Higher quality cotton was necessary to make precisely those cotton piece goods that Japan exported in large numbers and relied on increasingly to earn foreign exchange, whether in Dutch guilders, dollars or pounds.\textsuperscript{716} The U.S. relied on Japan to take 28.5\% of its total cotton exports in 1936, 12.8\% of total U.S. cotton production, up from 18\% of U.S. cotton exports in 1931. This U.S. reliance was not, however, symmetrical to Japan's reliance on both the raw cotton imports from the U.S. and export of cotton goods products to the U.S. and other countries. At least 10\% of total Japanese exports to the U.S. in 1936 were in cotton-related goods, with cotton piece goods the third largest single category of exports to the U.S. in that year.\textsuperscript{717} Keishi Ohara captured the point succinctly when he noted for Japan, "the production of cotton textile goods formed a valuable source of income for the entire Japanese economy."\textsuperscript{718}


\textsuperscript{716} Ohara, \textit{Japanese Trade and Industry}, p.392. In late 1935, a frustrated Roosevelt noted that strategic goods commonly did not include basic raw materials: "under ordinary and normal circumstances wheat, cotton and copper ingots are not implements of war. The letter of the law does not say so and the trouble is that the spirit of the law, as shown by the debates during its passage, does not allow me to stretch it that far out - no matter how worthy the cause." Roosevelt, quoted in Dallek, \textit{Franklin D. Roosevelt and American Foreign Policy}, p.113.


\textsuperscript{718} Ohara, \textit{Japanese Trade and Industry}, p.393.
<table>
<thead>
<tr>
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<th>1933</th>
<th>1934</th>
<th>1935</th>
<th>1936</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Total exports of Japan in thousands of Yen (as % of Japanese GDP)</strong></td>
<td>1,861,045 (12.9%)</td>
<td>2,171,924 (13.9%)</td>
<td>2,499,073 (14.9%)</td>
<td>2,692,975 (15.1%)</td>
</tr>
<tr>
<td>Japanese exports to U.S. in thousands of Yen (as % of total Japanese exports)</td>
<td>492,000 (26.4%)</td>
<td>399,000 (18.4%)</td>
<td>536,000 (21.5%)</td>
<td>594,000 (22%)</td>
</tr>
<tr>
<td>Japanese raw silk exports to U.S. in thousands of Yen (as % of total exports to U.S.)</td>
<td>355,841 (72.3%)</td>
<td>244,379 (61.2%)</td>
<td>328,910 (61.4%)</td>
<td>333,949 (56.2%)</td>
</tr>
<tr>
<td>Japanese exports to U.S. as % of Japanese GDP</td>
<td>3.4%</td>
<td>2.5%</td>
<td>3.2%</td>
<td>3.3%</td>
</tr>
<tr>
<td><strong>Total imports of Japan in thousands of Yen (as % of Japanese GDP)</strong></td>
<td>1,917,219 (13.4%)</td>
<td>2,282,601 (14.6%)</td>
<td>2,472,236 (14.8%)</td>
<td>2,763,681 (15.5%)</td>
</tr>
<tr>
<td>Japanese imports from U.S. in thousands of Yen (as % of total Japanese imports)</td>
<td>621,000 (33%)</td>
<td>769,000 (34%)</td>
<td>810,000 (33%)</td>
<td>847,000 (31%)</td>
</tr>
<tr>
<td>Japanese cotton imports from U.S. in thousands of Yen (as % of total imports from U.S.)</td>
<td>381,656 (61.5%)</td>
<td>400,919 (52.1%)</td>
<td>317,952 (39.3%)</td>
<td>372,027 (43.9%)</td>
</tr>
<tr>
<td>Japanese imports from U.S. as % of Japanese GDP</td>
<td>4.3%</td>
<td>4.9%</td>
<td>4.8%</td>
<td>4.8%</td>
</tr>
</tbody>
</table>

**Table 6.4: Japanese Exports to and Imports from the U.S., 1933-1936**

There may have been slight mutual vulnerability in the cotton trade, but this relationship was asymmetric and increasing Japan’s dependence on the U.S. and the costs to it if a cotton export embargo were ever considered, as it had been used in 1918. Similarly, U.S. exports of crude and fuel oil to Japan were 24% of total U.S. exports of crude and fuel in 1936, earning $23.2 million dollars and comprising 17.2% of the value of U.S. exports to Japan in that year.\textsuperscript{719} Although this represented a substantial U.S. reliance on Japan, Japan’s dependence on these imports was even higher as they were 81.6% of total Japanese crude and fuel imports in 1936. As detailed earlier, Japan was made increasingly vulnerable because of coordinated Anglo-American-Dutch denial of its oil ownership desires in the DEI, and despite Japan’s endeavors to free itself from the possible consequences of a future oil embargo, it remained dependent on the U.S. (i.e., synthetic outreach to Germany). The U.S. did begin to embargo trade with Japan during this period, ending tin-plate scrap exports in April 1936 in response to stepped up purchases by Japan.

Japan’s ability to earn dollars from the sale of silk in the U.S. continued to slide in this period, with the price of silk in dollars never coming close to its 1929 high. This and cotton goods restrictions would continue to drag on Japanese dollar earnings. Silk imports represented the only significant strategic vulnerability for the U.S. in its direct trade relations with Japan, as silk was used by this point to make parachutes. But, stockpiling efforts of the army and use of synthetic nylon substitutes would erase any real American vulnerability to Japan in this category. U.S. silk demand remained high, but its

\textsuperscript{719} See Table 17 and Treasury Department Interoffice Communication from Mr. Ullmann to Mr. White, August 5, 1940, in U.S. Congress, Committee on the Judiciary, Morgenthau Diary (China), 89th Cong., 1st Sess., Volume I, Senate Committee Print, (Washington, DC: U.S. G.P.O., 1965), p.186.
use further concentrated into women’s hosiery such that after 1936, 70% and more of imported Japanese silk went exclusively to this purpose. The U.S. would never threaten to end trade in these goods until they were finally ended with all other exchange in late July 1941. In this period up to 1937, it can be hypothesized that the U.S. may have preferred to support Japan’s trade and earnings deficits as a result of continued trade with the U.S. because in silk, for example, Japanese production and employment competed with other domestic efforts in Japan (i.e., heavy industrialization plans, army expansion needing agrarian recruits).

The importance of U.S.-Japan bilateral trade changed slightly in this period in response to U.S. government actions and Japanese strategy for an autonomous Yen trading bloc, with the share of Japanese exports going to the U.S. falling further to 22% in 1936. Japanese imports from the U.S. remained roughly constant averaging 33% of total Japanese imports during this period. In comparison, U.S. exports to Japan averaged 8.9% of total U.S. exports over the period with a peak value of 9.9% in 1934. As would be expected given U.S. restrictions, Japan’s share in total U.S. imports declined from 8.8% in 1933 to 7.1% in 1936. The importance of the bilateral trade to each country’s economy remained highly asymmetric during this period with Japan’s total trade with the U.S. accounting for roughly 8% of its GDP throughout the period, while for the U.S. the total trade with Japan declined from .64% of U.S. GDP in 1933 to .58% of U.S. GDP in 1936 (See Table 6.5).

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Table 6.5: Japan’s Overall and Bilateral Trade Balance, 1933-1936

<table>
<thead>
<tr>
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<th>1933</th>
<th>1934</th>
<th>1935</th>
<th>1936</th>
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</thead>
<tbody>
<tr>
<td>Overall trade balance of</td>
<td>-56,174</td>
<td>-110,677</td>
<td>+26,837</td>
<td>-70,706</td>
</tr>
<tr>
<td>Japan in thousands of Yen</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Exports-Imports)</td>
<td></td>
<td></td>
<td></td>
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</tr>
<tr>
<td>Bilateral trade balance</td>
<td>-129,000</td>
<td>-370,000</td>
<td>-264,000</td>
<td>-253,000</td>
</tr>
<tr>
<td>of Japan with U.S. in</td>
<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>thousands of Yen (Japanese</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Exports to U.S. - Japanese</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Imports from U.S.)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total U.S.-Japan trade</td>
<td>7.8%</td>
<td>7.5%</td>
<td>8.0%</td>
<td>8.1%</td>
</tr>
<tr>
<td>as % of Japanese GDP</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Japanese exports to and</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>imports from U.S. as % of</td>
<td></td>
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<td></td>
</tr>
<tr>
<td>its GDP)</td>
<td></td>
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</tr>
</tbody>
</table>

Japan’s overall trade and finance position somewhat improved during this period, with Japan enjoying a small overall trade surplus in 1935. Its bilateral trade balance with the U.S., however, would continue to deteriorate and help stimulate its search for and export of silver and then gold. These negative bilateral trade balances would continue through 1940 and assist in precluding the large Japanese gold exports beginning in 1937 from being used for different purposes, principally paying for increased German technical cooperation. The pattern emerged in this period and accelerated in 1937, wherein America bought Japanese silver and then gold, gave Japan dollars and then received those dollars back for U.S. exports that served U.S. grand strategy of supplying Japan until Britain came around to its views. In this manner, the U.S. was able to maintain and then
later increase its influence position over Japan, while orienting Japan's trade needs
toward the U.S. so much that it couldn't form possibly more beneficial exchange
relations with other states. Interestingly, Britain's trade restrictions against Japan in this
period increased this effect and helped further drive Japanese exports to the U.S.
market.\footnote{Sharkey, "Economic Diplomacy, 1931-1941," p. 100.} For the reasons detailed above, the exchange relationship during 1933-1936
can be categorized as narrow and narrowing toward the end of the period because of the
cessation of loans and direct investment. Japan was still benefiting more than the U.S. in
the trade as imports from the U.S. of industrial machinery, iron and steel and other inputs
necessary for industrialization grew throughout the period, while the U.S. continued to
receive largely only silk in return. Furthermore, despite limited U.S. vulnerability in
some export items to Japan, Japan's vulnerability to U.S. cotton and oil supply
disruptions was increasing during this period, leading to increased Japanese dependence
on the U.S..

\footnote{Sharkey, "Economic Diplomacy, 1931-1941," p. 100.}
CHAPTER 7

U.S.-JAPAN, 1937-1941

7.1 Chapter Overview

At the beginning of 1937, the United States was increasingly wary of how the major states (i.e., Britain, Germany, the Soviet Union and Japan) were likely to interact in the coming years and somewhat resigned to sitting on the fence until the other states had made their strategic choices. Each state was facing two front strategic dilemmas and did not fully resolve those dilemmas until the summer of 1941. Because their choices did not fully materialize until then, the United States, with its advantaged geographical position, did not directly force Japan's hand in Asia through full-scale commercial embargos until then. Facing the same set of strategic options as in 1933, the U.S. chose not to confront Japan directly in Asia, and instead, would wait to see how Japan resolved its strategic dilemma. Japan also faced the same options since 1932: court war with the Soviet Union to protect its nascent empire in China; court war with Britain-American-Netherlands over southeast Asian resources, principally DEI oil; or court war with both. The U.S. understood Japan's strategic options and choices, and preferred to wait for British-American solidarity to emerge from Japan's continued conquest of China before confronting Japan directly.
Japan's wholesale assault on China caused U.S. threat perception to increase markedly, but the Japanese naval air attacks on the U.S.S. Panay in December 1937 confirmed for the U.S. that Japan and the U.S. would war in the future. The U.S. began its serious naval buildup in 1938 and positioned itself for an eventual Anglo-American solidarity under U.S. leadership. Anglo-American bargaining for supremacy continued, however, until the outbreak of the Pacific War. This was largely due to American unease of British strategy under Prime Minister Chamberlain, and then under Winston Churchill, a tactical unwillingness to assume the burdens of defending Britain's empire in Asia without commensurate superiority in joint war planning. Due to this process of halting, yet critical, coordination the United States never took an explicit position on the defense of southeast Asia territories. It did, however, make several statements beginning in 1940 that the status quo in the DEI was vital to U.S. interests. The German-Soviet non-aggression pact in August 1939 helped solve the Soviet Union's strategic dilemma, but this came at Japan's expense as it experienced a decisive defeat by Soviet forces ending a four month long border conflict in a September 15, 1939 cease fire (i.e., the Nomonhan Incident). That conflict cost Japan over 50,000 soldiers and weakened its position in China. More importantly, it helped Japan to reign in its multi-front expansion and make a rational strategic choice for war against the West and not the West and the Soviet Union. This then led Japan to conclude its neutrality pact with the Soviets in April 1941. This agreement also restored some security to Russian supplies of oil from N. Sakhalin that were diminished in the fallout of Japan's dalliance with Germany.

When Germany attacked the Soviet Union in June 1941, Japan's strategic dilemma was stark. It chose not to follow Germany's treacherous path again and violate
its agreement with the Russians. This choice was not irrational, nor was it altogether unlike any other great power’s decision facing a two front strategic dilemma. Instead, Japan logically chose to attack south to secure the needed supplies that were being systematically denied to it. Furthermore, the actual economic benefits of cooperation with Germany were fleeting at best, and after 1939, almost non-existent (i.e., end of German technical assistance that floundered on insufficient parts and financing). The United States government received tremendous domestic criticism, some of it self-directed, regarding its continued allowance of strategic goods exports to Japan while Japan sought to conquer China. This criticism was even more pointed when the vast Japanese gold purchases by the U.S. are taken into account. These allowed Japan to both finance its trade deficit with the U.S. and in fact build significant stores of U.S. dollars in banks across the Western hemisphere. Why did the U.S. continue to supply Japan and how did this exchange affect Japan’s military and overall capabilities?

First, the U.S. would not confront Japan, using the oil weapon in particular, and decisively cause its military advance to the south until it was in the grand strategic interest of the U.S. to do so. The United States was not prepared for war and its strategic bargaining with Britain did not fully blossom until after Britain’s position had fallen due to war in Europe and Japan’s advance in China. More importantly, Japan’s military conflict with the Soviet Union was fully resolved in the spring of 1941, and did not reverse course despite Germany’s attack on the Soviet Union in June. The pivotal time came in summer 1941, and not before. Second, U.S. supplies to Japan largely displaced supplies from other countries; in oil from the DEI and in steel-related products from the Soviet Union, Australia, Malaya and the Philippines. Once Japan’s military threat to
these sources was clear, the U.S. acted to end Japan’s ability to increase exorbitantly its stockpiles of necessary items (e.g., scrap iron and steel embargo of September 1940). In particular, supplying oil in the interim helped shield the DEI from the increasing Japanese pressure on it, buying time for the U.S. to build up its own capabilities and coordinate the future denial of DEI assets to Japan (e.g., destruction of refineries, crude wells etc.). U.S. commercial reliability also may have preserved some elements within Japan lobbying for non-war with the U.S. and lessened the intensity and success of Japan’s drive for autonomy. Maintenance of strategic vulnerability through tactical supply comes at a cost, and that is supplying the enemy until that last moment. The U.S. supplied Japan increasing amounts of material, but much of this was expended by Japan in operations on the Asian landmass against both the Chinese and Russians. The key measure was not the amount supplied, but the amount Japan could store in excess of its consumption (i.e., autonomy enhancing or only consumption sustaining). When this amount appeared to be increasing to excessive levels, the U.S. ended exchange.

Third, there was a shift in types of supplies to Japan which increased Japan’s resource diversion, energy consumption and strategic vulnerability. For example, the U.S. sent steel scrap instead of steel plate ready for application in shipbuilding. This shift from finished goods to raw materials did increase Japan’s resource use, even if only marginally and somewhat in line with Japan’s own drive for indigenous production capabilities. More importantly, the U.S. allowed Japan to import technology and equipment to build excess crude oil refining capacity, which reinforced Japan’s vulnerability to distant crude oil supply sources (e.g., the DEI, U.S., Persia). This Japanese investment and trade focus caused Japanese dependence to increase across the
period and limited its autonomy (i.e., in contrast to a full effort at coal-based synthetic oil). Japan’s ability to overcome its dependence was decreased after U.S. and British trade embargos and removal of their ships from the trade with Japan. Japan was not prepared to replace the Western transport of oil and iron ore that was supplied by U.S. companies in the prior trade. This deficiency and oversight was a product of Japan’s prior reliance and a subtle way U.S. trade had increased the adjustment costs to Japan without Japan fully realizing it until too late.

Finally, the State department and President Roosevelt acted on estimates of these crucial measures and changes in Japanese demand, which were made possible due to Japan’s demand being largely fulfilled in the U.S. and by finally wholly-subservient U.S. corporations (e.g., Stanvac in the DEI). Were this not the case, Japan could have achieved advances in capabilities and stockpiles unbeknownst to the U.S., with worse consequences on relative U.S. power in wartime. This was also true of the gold-dollar exchange that gave Japan dollar assets. The U.S. Treasury monitored Japan’s use of these dollars to purchase supplies across the Americas, and could therefore more easily frustrate the purchases and freeze the funds. This particular exchange fueled itself and diverted Japanese resources as Japan bought U.S. gold mining equipment with the U.S. dollars it earned from selling the U.S. its gold, furthering the exclusivity in the transactions and resource diversion (e.g., Japan couldn’t use this mining equipment to drill for oil in North China).

For these reasons, the U.S. continued to supply Japan even to Japan’s advantage in generating increased material capabilities, violating defensive realism’s basic precept of denying material gains to a rival. It did not do so, however, in ways that it perceived
would increase Japanese wartime capabilities vis a vis the United States’ own war strategy (i.e., stockpiles that endure beyond a year), or because it was inspired to maximize sales due to domestic or corporate interests. In the maintenance of the oil weapon, in particular, the U.S. continually reinforced Japan’s crude-based dependence and insufficient indigenous aviation gasoline refining capability. This was often blatant and had the effect of yet again demonstrating the U.S. true intent of denying Japan the autonomy it sought through empire and industry. Not surprisingly, U.S. government relations with its corporations in this period showed heightened controls over those items that might increase Japan’s long-term autonomous military capability. This did not prohibit some companies from challenging U.S. policies and preferences, but after Japanese attacks on Stanvac vessels in China they came under total guidance by the State department. Some companies were unwilling to support American policy in China and Japan and were remonstrated, rebuffed or simply left to fend for themselves. The U.S. government preserved for itself the ultimate position of choosing when to cease that economic exchange that would trigger Japan’s decision for war and U.S. ascendance to global hegemony.

The U.S. used this position in July 1941, ending trade with Japan and coordinating the financial and trade embargo against Japan across British, Dutch and Western hemisphere territories. Prior to this, U.S. trade with Japan had narrowed considerably and in response to Japanese advances against U.S. interests. Almost all corporate actors complied with U.S. preferred policies across this period, even with the informal “moral embargos” beginning in late 1938. In the crucial Japanese negotiations in the DEI with Stanvac and Royal Dutch Shell, the U.S. guided the companies to
minimal contracts with Japan, and then engineered the tanker withdrawal. This effectively voided most of the contracted supplies by late spring 1941, and reinforced Japan’s strategic vulnerability and dependence on the U.S.. For these reasons, the state was dominant over corporate interests in this period, and exchange was increasing Japan’s dependence on the U.S. while benefiting Japan’s material capabilities more than the U.S.. Because the U.S. allowed these benefits (e.g., large amounts of aviation gasoline) to accrue to Japan in order to retain for itself the influence position that would determine Japan’s decision for war, this period is most explicable by offensive realism.

7.2 Roosevelt Pacification Gambits and Japan’s Assault on China

President Roosevelt observed the changes in Japan’s political establishment throughout 1936 with apprehension, noting in particular that its overtures to Germany and ending of naval arms limitations were ominous signs for the future. Japan had experienced another round of domestic tumult in February 1936 and key assassinations, including the successful Finance Minister, Takahashi, and then Lord Keeper of the Privy Seal and former Premier Admiral Saito. Prince Saionji narrowly escaped targeted execution as did the current Premier Admiral Okada, whose brother was assassinated in a case of mistaken identity. Takahashi’s assassination, in particular, indicated that even mild financial constraints placed on army and navy budgets and influence would be violently resisted. Despite increased U.S. threat perception, President Roosevelt took the opportunity at this time to study a mild peace offensive in the Pacific.
Beginning in November 1936, Roosevelt proposed to his cabinet and then debated with the State department the feasibility of "neutralizing" all of the Pacific islands, thereby preventing their fortification. The Washington Naval Treaty (i.e., the Five Power Treaty) had expired in December 1936, and the U.S. had already rejected a British proposal to negotiate a renewal of only the base fortification article under the rubric of the Five Power Treaty. As he was wont to do, Roosevelt wanted to do something grander in symbolism that might better stabilize relations in the Pacific. His effort to lessen both U.S. threat perception of Japan and Japanese threat perception of the U.S. foundered on State department intransigence in the spring of 1937.\footnote{Kaufman, "The United States and Naval Limitation," pp.429-30; James C. Thomson, "The Role of the State Department." in Borg, ed., Pearl Harbor as History, pp.97-8.} Roosevelt was willing to ignore the evidence that had accumulated on Japanese fortification measures in the mandated islands and building programs far above prior limits (i.e., 16-inch gun battleships with 50,000 ton displacements, not 35,000). He did so in order to reduce Japan’s tilt toward Germany and against U.S.-British-Dutch interests.\footnote{Conferring with Hornbeck, top U.S. naval officials held it “possible” that secret Anti-Comintern pact protocols covered the disposition of the Philippines and the DEI. See letter Admiral Yarnell, Commander in Chief, USN Asiatic Forces, to William Leahy, USN, Chief of Naval Operations, March 27, 1937, in Hornbeck Papers, Box 308, Folder: Naval Intelligence. This certainly was the case later with the Tripartite pact, but it is as yet unknown if understandings existed in the 1936 deal.} Nonetheless, many of his advisers were not convinced that the moment was ripe for an overture of this magnitude and tried to dissuade him from taking it public. Roosevelt lambasted the chief State department analyst who prepared the rebuttal to his plan, Maxwell Hamilton, calling his assessment an “argument of defeatism."\footnote{Thomson, "The Role of the State Department," p.98. Roosevelt also labeled himself a realist in his remarks, not an idealist believing agreement with Japan would mean the provisions would be faithfully observed (i.e., unlike the Nine Power Treaty, etc.). This statement confirms the tactical delay nature of the neutralization plan in Roosevelt’s calculus and quite possibly a way of forestalling German-Japanese concord that would prod Japan south. Borg, The United States and the Far Eastern Crisis, p.252.}
After this internal exercise, a very useful review of America's naval and grand strategy occurred in March 1937 among key U.S. naval and policy strategists. Hornbeck and Norman Davis contended that Japan's post-naval limitation policies were in flux and the current Foreign Minister, Sato Naotake, was inclined to reach accord on not breaking out into qualitative and quantitative naval arms races with the Anglo-American powers. However, "the question was whether Sato would last." Hornbeck contended: "For the moment the Japanese were inclined to take stock of the obstacles in the way of a realization of their program. The most effective obstacle was a show of military force." Hornbeck held it to be "impossible to predict" the likely naval plans of Japan despite the fact that there were Japanese who "did not wish the 16" gun and would advocate staying with us and the British." From this he and the other participants agreed that America's naval building program needed to be stepped up considerably and aligned with British building. Norman Davis noted, "it was a great thing for the two leading democracies, Great Britain and the United States, to build along together. If the time ever came for a further naval conference and the United States had not built, we would be caught with our trousers down." Admiral Pye concurred, relating the joint buildups to Japan: "if we should fail to build along with the British, the Japanese would know that we were not sincere and would be more inclined to go ahead their own way." 

President Roosevelt chose to delay the naval building proposals of his advisers and undercut the base fortification plans put forward by the Congress and some army and navy circles. He ended the public debate over fortification of Guam and the Philippines

725. Like many "moderates" Sato did not last, he was replaced on May 31, 1937 by Hirota.
726. See memorandum of meeting at State department among Hornbeck, Hull, Davis, Dunn, Pell, Rear Admiral Pye and Commander Schuermann, March 12, 1937, in Hornbeck Papers, Box 308, Folder: Navy 1931-1938.
because he understood that these bases could not be defended against a concerted Japanese attack, and further, that efforts to build such fortifications in early 1937 would reinforce anti-U.S. opinion and elites inside Japan at a time when the moderates’ position appeared tenuous. Therefore, Roosevelt delayed the naval buildup and publicly undercut some of the army, navy and congressional advocates of base fortification through large reductions in the budgets for such proposals. This mild form of tension relaxation might have paid dividends to the U.S. position, particularly given the increased economic assistance that Britain had provided to China since early 1936. Britain’s assistance incurred the wrath of Japan’s army imperialists, despite Britain’s evident desire for better relations with Japan.

Since the aftermath of Anglo-American discord over Manchuria, the U.S. had positioned itself not to play the foil for Britain. This did not change as its new leader, Neville Chamberlain, continued to try and forge Anglo-Japanese understanding. Chamberlain believed the Japanese would take advantage of Germany’s challenge to England by advancing on British possessions in China and throughout Asia, not unlike what it had done through the Anglo-Japanese alliance and WW I against Germany’s Asian possessions. Chamberlain, therefore, proposed Anglo-American unity against Japan, which meant, of course, largely U.S. naval force to confront Japanese

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727 Admiral Yarnell’s letter stated it succinctly and Hornbeck summarized the Philippines fortification results neatly. He declared that “it would be overrun” by the enemy, used as a base against us and was therefore a “military liability.” This did not mean, however, that the U.S. should do anything other than provide support for the U.S. position there (i.e., no statements of withdrawal etc.). See memorandum, “Question of Retention by the U.S. of a Naval Base in the Philippine Island,” January 8, 1937, in Hornbeck Papers, Box 308, Folder: Navy, 1931-1938.

728 Borg, The United States and the Far Eastern Crisis, pp.263-273.

729 Chamberlain was Chancellor of the Exchequer until his assumption of the Prime Ministership on May 28, 1937. Since February it was clear, however, that he would be the next Prime Minister and he was therefore approached by the U.S. in April 1937 to sound out his position.
transgressions that protected predominately British economic interests in China. This
was precisely the entangling commitment Roosevelt had avoided since he assumed
office, and Chamberlain’s recent history seeking bilateral non-aggression pacts with
Japan did nothing but reinforce American suspicions of British intent. When Norman
Davis broached Chamberlain about his German policy, he was told that he would handle
the political appeasement of Germany on his own terms due to Britain’s vital interest and
exposure (i.e., without excessive American involvement). After this slight rebuff,
American attitudes toward joining a British rapprochement with Japan that better
protected British interests by implicit threat of American force were politely rejected by
the U.S..

Japan’s invasion of China beginning with the “Marco Polo Bridge” incident of
July 7, 1937 did not alter this fundamental tendency in Anglo-American buckpassing
against Japanese advances. Instead, Britain immediately requested joint Anglo-American
mediation of the conflict, but no consideration of economic sanctions because they would
lead to a war that America was unwilling to commit to.730 The U.S. wanted effective
Anglo-American cooperation, but held parallel actions on independent lines were more
appropriate for assuaging Japanese sensibilities and possible adverse reactions to a show
of unity through identical protest notes.731 As the military conflict widened and a
Japanese-Chinese negotiated settlement became increasingly unlikely, Britain pressed for
joint statements seeking cessation of troop movements and some form of joint mediation
of the conflict to prevent its widening. The U.S. contended that without “some

implication of a sanction," there would be no point to joint Anglo-American efforts. Neither the U.S. or Britain were willing to have a display of force in the region and Britain was unwilling to go down the path of economic sanctions discussions without some firmer American commitment to the use of force, which Britain asserted would be the Japanese response to any sanctions.⁷³²  Ambassador Grew in Japan, who preferred the non-confrontational strategy at this juncture and most subsequent ones, commented on the reversal in Anglo-American positions:

Humorists might find humor in the complete turning of the tables between 1931 and 1937. Then it was we who stepped out in front and the British who would not follow. Now it is the British who are taking the lead while we are moving slowly and very, very carefully. It has always been thus in Anglo-Japanese relations, but the logic of it is perfectly clear. British material interests were not acutely affected by the Manchurian issue. But the farther south Japanese aggression extends, the more closely are British material interests touched...In the present instance the Administration is playing its cards, or withholding them, with eminent wisdom.⁷³³

The strategic purpose of American dilatory tactics are open to interpretation, but it is clear that the U.S. would not join Britain in any action that would incur excess Japanese wrath toward the U.S. and shield Britain's promotion of its own self-interest in opposing Japan. The U.S. had learned from the Manchurian incident and the oil embargo talk of 1935 not to put itself into the forward position against Japan, and resisted British entreaties to do otherwise. The U.S. did vigorously proclaim its support for the lives and property of American nationals in China and these protestations increased with the rise in indiscriminate killing, particularly in international settlement cities like Shanghai where deaths occurred due to both Japanese and Chinese actions. Chiang Kai-shek resisted

⁷³². Ibid., pp.293-4. Chamberlain's echo of Hoover here is striking.
Japanese aggression by using vulnerable western settlement areas like Shanghai to try and involve the western states in his cause against Japan. Chiang had come through a bizarre kidnapping experience at the hands of Chang Hsueh-liang, the former Manchurian warlord’s exiled son, and was released with the understanding that the Nationalist government would stand up to Japan and not negotiate away further northern territories to Japan. The Chinese population genuinely rallied around Chiang and these propositions throughout early 1937, and this may have helped precipitate what the Japanese considered a “pre-emptive” war to protect their citizens and interests. Japan’s assault had the effect, however, of impelling Chiang to seek a non-aggression pact with the Soviet Union, which was signed on August 21, 1937.734

The Japanese and Russians had engaged in border clashes along the Amur River in June and July, and Chiang felt he needed as much material support as he could muster, particularly when he believed the Anglo-American powers were not assisting him sufficiently. By late August 1937, Chiang’s tactics and Japan’s determination had combined to cause tremendous devastation in Shanghai, Tientsin and Peiping, but still no Anglo-American accord on jointly challenging Japan. A prime example of this occurred when Japan declared it would enforce a “pacific blockade” of China’s coastline, and despite no formal declaration of war, aggregated to itself the right to identify all ships coming to China under the unstated threat of blockading any ship carrying weapons to China. This was another example of how Japanese navy actions expanded the war against China.735 The British objected strenuously to this policy and requested American

735. Japan’s navy had insisted on sending forces to Shanghai after the outbreak of fighting and “the navy’s success triggered further advances by the army and finally full-scale war from December 1937 on.” David
joint denunciation of it. Roosevelt declined to join the British and instead, on September 14, 1937, declared that no U.S. government-owned ship would carry weapons to either Japan or China, thereby removing the U.S. from the position of challenging Japan at all on the subject.

Roosevelt held that any private American shipper or other commercial interest that trafficked in weapons to China did so “at its own risk.” This policy clarification was a further sign of the U.S. government position of not confronting Japan to Britain’s benefit. If Chamberlain wanted to pursue a unilateral policy to appease Hitler in Europe, America would not protect its Asian empire against Japanese predations. As noted earlier, Chamberlain sought understanding with Germany to forestall Japanese expansion at its expense, and failing this, American “cooperation” which defended Britain’s position in Asia while it built up against Germany and Italy. Roosevelt was not about to be duped into this position. As a response, U.S.-Japanese economic relations in 1937 supplied Japan, enabling it to continue to threaten predominate British interests in China. Roosevelt’s policy was to force Britain to come to terms with the U.S. by harmonizing its reaction to Japan’s threat under American preferences. The sustainability of this strategy relied upon Japan differentiating between the U.S. and Britain in its advance, and China accepting this situation. To be sure, the U.S. was assisting China’s military through

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736. Lee, Britain and the Sino-Japanese War, p.42. The proximate cause of this declaration was the transport of 19 warplanes to China aboard a U.S. government-owned freighter, the Wichita, which received much negative publicity and demands for Neutrality Act compliance. Roosevelt’s decision, however, was not due to domestic opinion; rather, it was a desire to avoid military aircraft aboard a U.S. ship being boarded or confronted by Japan, causing an unnecessary incident with them. See Jonathan G. Utley, Going to War with Japan, 1937-1941. (Knoxville, TN: University of Tennessee Press, 1985), p.14.
munitions sales, but it was also supplying Japan with large amounts of necessary supplies for its war effort, particularly scrap iron and steel which was going to Japan in record amounts during 1937 (See Table 7.1).

The U.S. stance did not please the Chinese government, nor did Hornbeck's advice that China needed to rely more on "its own capacity without reference to the possibility of assistance from any other country...if any country bases its plans on expectation of assistance from others and then when the time comes the assistance is not forthcoming, it may frequently happen there is not only disappointment and disillusionment but disaster." Unfortunately for China, American corporations seeking to supply China with munitions sometimes sought blanket coverage for their actions from the U.S. government. For example, by August 1937, E.I. DuPont Company had shipped 5,000 bomb casings to China but decided not to ship the TNT necessary to make them functional weapons, because they did not want to be "crucified by publicity." On more than one occasion, the State department informally requested that they complete the sale and transfer of TNT. But, DuPont directors demanded a letter from Secretary of State Hull declaring that "such sales were in the interest of the United States." Hull declined to make such a public declaration and the sale died, frustrating U.S. policy of supplying China on the sly. This event is consistent with liberalism and marxism and inconsistent with realism, because the company forced its preference onto the state and did not fulfill

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377. Hornbeck to C.T. Wang, China's Ambassador to the U.S., August 2, 1937, quoted in McCarty, "Stanley K. Hornbeck and the Far East," p.93. This language and exhortation to China to stand on its own mirrored President Roosevelt's own assessment during the Silver crisis in late 1934. Roosevelt said then, "it is better to hasten the crisis in China-to compel the Chinese people more and more to stand on their own feet without complete dependence on Japan and Europe." Roosevelt memorandum to Treasury Secretary Morgenthau, December 4, 1934, quoted in Blum, From the Morgenthau Diaries: Years of Crisis, 1928-1938, p.206.

the state's preference. The State department would not allow companies to compromise the U.S. government position of unstated support of China even if that meant less assistance to China (i.e., not balancing Japanese threat with ally support).\textsuperscript{739} Despite this corporate-state positional entrapment episode and some corporate retrenchment from the trade, China did receive American munitions, including $7 million dollars worth in late 1937.\textsuperscript{740}

Roosevelt grew discontented with his advisers' neutralized policy toward the conflict in China, which, if continued, might unduly rankle Anglo-American relations due to the forward position Britain was assuming against Japan.\textsuperscript{741} Roosevelt delivered his "Quarantine Speech" in Chicago on October 5, 1937, and in it he commented on the "present reign of terror and international lawlessness." Roosevelt warned that America could not escape the external environment through isolation or neutrality, and recommended "peace-loving" nations make a "concerted effort" to oppose through a quarantine the "epidemic of world lawlessness."\textsuperscript{742} President Roosevelt was careful not to name Japan, Italy or Germany or any specific actions, but his connotation was clear. Roosevelt's call to the peace-loving community resulted in the Brussels Conference from November 3-24, 1937. It was originally convened under the auspices of the Nine Power Treaty, but Japan made it clear it would not attend and the delegates were expanded to include League of Nations members as well. In the period before the conference,

\textsuperscript{739} It could be argued, however, that decreased U.S. assistance punished Chiang for this tactics around the international settlements and forced Britain forward against Japan, both statist justifications for American inaction and Roosevelt placing all the risk of corporate actions upon the corporations themselves.

\textsuperscript{740} This munitions-related trade to China from July to December 1937 was much higher than that to Japan in the same period, which was only $1.8 million dollars. In 1938, however, the export to both countries was roughly equivalent due largely to U.S. fulfillment of prior airplane contracts with Japan that Secretary Hull would not cancel. Divine, \textit{The Illusion of Neutrality}, pp. 209, 218.

\textsuperscript{741} Roosevelt's discontent was likely with Secretary of State Hull.

\textsuperscript{742} For these text items see Dallek, \textit{Franklin D. Roosevelt and American Foreign Policy}, p. 148.
Roosevelt stated that he was not simply calling for debate on punishment and sanctions against Japan, but rather some “positive” approach that would unite the majority of countries in the world while giving the disgruntled countries some stake in cooperation. Accordingly, Hombeck drafted a “constructive” proposal that recommended that the conference should assure Japan that force would not be used against it and that its “access to raw materials” would be made more secure through some future conference establishing these arrangements within an overall political understanding similar to those reached at the Washington Conference. These positive assurances were to be conditioned on the cessation of hostilities in China and are the first evidence of U.S. policy makers struggling to undo the vulnerability they knowingly helped create.

Hombeck, now Political Adviser at the State department, advocated offering Japan greater assurance of “access” to the vital raw materials whose deficiency he admitted helped impel Japan’s expansion, while Maxwell Hamilton, new chief of the Far Eastern Division, advocated a “principle of equality of treatment in the control, development, and export of raw materials.” The distinction centered on the potential ownership of oil sources in the DEI and iron ore deposits in Australia, Malaya and the Philippines, instead of only more secured trade in those resources. Neither of these subjects were actually negotiated with Dutch and British authorities. At the Conference, these states and France tried to secure commitments from America to defend their possessions in Asia. France, then pressured by Japan not to supply war materials to China through Indochina, demanded that the U.S. agree to defend Indochina from

743. Utley, Going to War with Japan, pp.18-9; Borg, The United States and the Far Eastern Crisis, pp.402-4.
Japanese attack in order to reach any accord at Brussels.\(^{745}\) The U.S. refused these invitations to confront Japan. The U.S. also downplayed Britain’s equation that any sanctions employment would mean war and therefore a clear American commitment to use force was a necessary precondition to any discussion of economic pressures, let alone new arrangements for sharing previously exclusive resources. Prior to the conference, Hornbeck had developed a list of economic pressures that might be employed against Japan, including refusing to purchase Japanese gold, its general exports or to receive its shipping.\(^{746}\) At the Conference, these positions weren’t acceptable to the British, and as a result of the common desire not to air these conflicts publicly, the delegations did not openly advocate sanctions against Japan. They agreed not to embarrass each other into displaying each’s unwillingness to actually employ or even discuss economic pressure against Japan. Hornbeck and Davis did press Britain to agree to financial pressure on Japan in the form of joint denial of any loans to Japanese concerns in the conquered parts of China. They were undercut even in this by Hull in Washington, who declared U.S. policy to go no further than moral condemnation of Japanese actions.

British desire for a joint Anglo-American mediation of the war in China was motivated partly by the possibility that Germany would perform such a mediation and reduce Britain’s influence throughout Asia.\(^{747}\) As noted earlier, Germany was a significant supplier of arms and army training to China and had offered its services as mediator to the conflict, despite Japanese unwillingness to accept any outside influence.

\(^{745}\) Dallek, Franklin D. Roosevelt and American Foreign Policy, p.150.
\(^{747}\) Lee described how the British cabinet “briefly” discussed Anglo-German mediation of the China conflict which might salutarily improve their relations. He also noted, “The hope that a basis for cooperation between London and Berlin could be found in East Asia was to recur in 1938 and 1939.” Lee, Britain and the Sino-Japanese War, p.76.

375
The U.S. rejected the British proposition, not wanting to inject itself into a situation where Japanese policy appeared resolute. Despite U.S. forbearance, Foreign Minister Hirota berated Ambassador Grew for allegedly leading the Brussels conferees into discussing economic coercion, thus losing Japan's fleeting view of the U.S. as impartial. Hirota mentioned that previously the Japanese people had blamed Britain for trying to unite a front against Japan, but now they began to view the U.S. similarly. Despite the overall subdued U.S. policy, Japan was voicing displeasure and Anglo-American inaction contributed to China's fairly swift territorial losses, including Beijing and Nanking by the end of December 1937.

China appeared to be collapsing and Germany ascending in influence in the Sino-Japanese conflict when Japanese naval aviators attacked the U.S.S. Panay, three Stanvac tankers and a British naval vessel, the H.M.S. Ladybird, on December 12, 1937. As in the Shanghai attack of January 1932, the Japanese navy's attacks, this time on U.S. government personnel and private property, confirmed the view of Hombeck and others in Washington that Japan was a non-differentiable entity dominated by militarists with whom little accommodation could be sought nor should be. It did not matter that some moderates existed in Japan, they held no power and were intimidated by army and navy assassins. Hombeck consistently held the domestic military faction needed to be defeated in their military expansionism in order to be discredited in Tokyo policy making, allowing for the return of moderate Japanese political leaders. The attack also represented a missed opportunity for Japanese force employment to divide the Anglo-American position (e.g., only attacking U.S. assets). This increased threat perception and

confirmation affected President Roosevelt as well as the U.S. navy, which had vigorously defended the rights of American nationals to exist in Japanese-controlled China. It also bound the oil companies’ perception of Japan’s threat more tightly to the U.S. government, and helped place them under the direction of the U.S. government through the remainder of the period (i.e., the most important corporate actor now fully aligned with the state). President Roosevelt sent an outraged missive to the Japanese government demanding that the Emperor be personally informed of the U.S. reaction and began to search for new ways of containing Japan’s advances, which were now taking as well as directly threatening American lives and property.

7.3 Casting About for an American Plan

Roosevelt pressed beyond Hull’s continued insistence on inaction, and began to promulgate ideas for a naval blockade of Japan and stepped up financial pressure against it. Roosevelt viewed the Japanese undeclared war on China as befitting an appropriate response, “a technique of fighting without declaring war...there is such a thing as using economic sanctions without declaring war and I want to get that technique.”

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Roosevelt had his Treasury Secretary, Henry Morgenthau, contact the British about joint restrictions on Japanese foreign exchange. He also declared U.S. desire for a joint naval blockade after Japan’s next outrage in China. The British had preferred a joint display of naval force to the region, not the instituting of a naval blockade and cutoff of raw materials to Japan. They were somewhat alarmed by Roosevelt’s bellicosity and unwillingness to

749. President Roosevelt to his cabinet, December 18, 1937, quoted in Dallek, Franklin D. Roosevelt and American Foreign Policy, p.154.

377

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admit that if enacted his proposals would likely bring war. Britain’s Ambassador to the
U.S., Sir Ronald Lindsay, summarized Britain’s view of Roosevelt and his blockade
proposal, declaring them “the utterances of a hare-brained statesman or an amateur
strategist.” The President was not intrigued by Britain’s suggestions either, although
the exchange between them did result in Roosevelt’s commitment to send a cruiser force
to Singapore and begin secret naval staff talks in January 1938.

The proposed joint foreign exchange restrictions did stimulate the British
Treasury to review the utility of economic pressure on Japan. They ultimately discarded
Morgenthau’s proposal because Sir John Simon, Treasury Chancellor, held “we shall find
ourselves left in the lurch sooner or later by the U.S.A. (who incidentally have no very
special stakes in Asia) & Japan ... we then add the fatal folly of going to war with Japan &
so committing suicide in Europe.” Because of this prevailing sentiment, Roosevelt
was left to pursue initial joint naval planning through the Roy Ingersoll mission to Britain
in January 1938, the beginning of moral embargoes on U.S. exports to Japan and a
concerted U.S. naval buildup. Roosevelt’s skepticism of British action under
Chamberlain was confirmed by the Anglo-Italian Agreement of April 1938, which
undermined the principle of non-recognition of territorial gains acquired through brute
force. In this agreement, Chamberlain gave de jure recognition to Italy’s conquest of
Ethiopia. This agreement followed Chamberlain’s request that Roosevelt refrain from
pursuing a comprehensive peace initiative through an international conference that would
have linked negotiations on arms reductions with more equal access to raw materials.

750. Ambassador Lindsay quoted in Lee, Britain and the Sino-Japanese War, p.91.
751. Simon quoted in ibid., p.92.
Chamberlain declined Roosevelt’s initiative in January 1938, and declared that it would “cut across (his) efforts to negotiate on immediate issues with the dictators.” Partly because these negotiations ended in appeasement of Italy, Roosevelt submitted his naval buildup plan to Congress and became “discouraged from trying to arrest the fascist advance toward war.” Although this may have been true with respect to Europe; in Asia, Roosevelt began confronting Japan through domestic and indirect foreign efforts, leaving behind many of his advisers’ earlier pleas for prior coordination with Britain.

Roosevelt began to accelerate plans for America’s eventual entry into the coming war during 1938 with three important modifications of overall U.S. policy and relations with Japan. First, on May 17, 1938, he signed the Second Vinson Act. This law dramatically increased the size and number of U.S. naval vessels above past treaty limits and expanded air power capabilities (e.g., air fleet and station buildups). The naval buildup is remarkable for the attention Roosevelt gave to individual ship decisions and their subsequent import in the conduct of the war. For example, Roosevelt pushed the development of fast tankers. The navy was currently building only three for Standard Oil, but Roosevelt wanted many more as part of his vision of superior organizational fueling for the fleet and rapidity of movement. The naval buildup was certainly instigated by both Japan’s military advances in Asia and Britain’s need for support there.

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754. Dallek, Franklin D. Roosevelt and American Foreign Policy, p.156. Leutze summarized Anglo-American distance at this point: “After years of competition and suspicion the collective peril was insufficient to enforce trust. The British were not content to let Roosevelt go forward step by step as he felt able; the Americans, conversely, resented evidence of British mistrust, especially when it followed on the heels of what, to Roosevelt, must have appeared a courageous action.” Leutze. Bargaining for Supremacy, p.28.
756. Ibid., p.469.
even though it pursued appeasement of the rising states. The larger navy was not to be considered only as a prelude to the use of force to defend corporate interests abroad, however. Hornbeck noted: "We do not intend to use armed force anywhere on behalf merely of investments or of trade." Hornbeck summarized the other important reasons for the buildup:

The world knows that the United States could outbuild any other country, but the world has not seen that this country is willing to do that. It might be worth while for this country to demonstrate both its capacity and its intention in that regard. It might be well for the world to see in process of building or built a superior and constantly more superior American Navy. For Japan, in particular, such a visible demonstration of our capacity might be very salutary. The Japanese still cherish the idea of naval parity. It might happen that, once they are definitely shown that there is no hope of their possessing a Navy on a parity with the Navy of the United States, they would give sober thought to the question of naval limitation on the basis of a ratio which would tend to provide parity of security.

Second, the U.S. reformulated its war plans against Japan (i.e., War Plan Orange) to end the emphasis on a short offensive campaign of victory through battle fleet actions, and instead planned for protracted war against Japan within the framework of a global two front war. The basis of victory would be to draw out Japan’s naval communication and supply lines, then attack them and wear Japan down through a naval blockade. Movement toward this strategy was not universally accepted within the naval establishment, but in this and other procurement areas Roosevelt helped ensure maximum

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759. Roskill, Naval Policy Between the Wars, pp.365-6; Kaufman, "The United States and Naval Limitation," pp.440-442; Morton, The War in the Pacific, p.41. Interestingly, U.S. army and navy planners differed over strategy, yielding bargains that gave each service something they wanted, but left army-staffed island outposts undefended by the navy. This was not unlike Snyder’s alleged "self-defeating" Japanese army-navy logrolling in strategic planning, because U.S. navy planners withheld much of the operational planning from the army. Leutze, Bargaining for Supremacy, pp. 29-30, 41.
military power projection capability for the U.S. and operational plans that would not squander these resources prematurely.\textsuperscript{760} This planning shift meant that America would not necessarily have to constrain Japan’s prewar supplies inordinately because it assumed Japan would use up considerable amounts in the initial stages of a drawn-out conflict (e.g., fuel oil reserves). This assumption would be further strengthened if alternative sources of oil in the DEI were rendered useless for some period of time, forcing Japan to draw down its reserves indefinitely. Changes in America’s war strategy, therefore, allowed for changes in its economic policies toward Japan despite increased threat perception of Japan.

Finally, Roosevelt began curtailing U.S. military exports to Japan and instilling in the American public a sense of obligation not to assist Japan’s offensive military capabilities. In July 1938, Roosevelt had the State department send letters to 148 persons and companies informing them that the department “would with great regret issue any licenses authorizing exportation, direct or indirect, of any aircraft, aircraft armament, aircraft engines, aircraft parts...to countries the armed forces of which are making use of airplanes for attack upon civilian populations.”\textsuperscript{761} This moral embargo was not grounded on any domestic congressional authority, but it was strategic economic policy toward Japan informally enforced by the State department. Some further pressure was brought to bear on airplane manufacturers in December 1938, and because “many of these firms relied heavily on government contracts, they yielded to pressure and made the

\textsuperscript{760} Roskili noted that because of Roosevelt’s critical proddings, the U.S. navy “was lucky to have him at the helm.” \textit{Ibid.}, p.415.

\textsuperscript{761} State department letter to airplane manufacturers. July 1, 1938, quoted from McCarty, “Stanley K. Hornbeck and the Far East,” p.179. It’s interesting to note how opposed Secretary Hull was to this plan until the press had graphically recounted the devastation from Japan’s aerial assault on Hankow in May 1938, and forced him to confront his own rhetoric condemning aerial assaults on civilians. Perhaps only liberals respond to liberal pressures. Utley, \textit{Going to War with Japan}, p.36.

381

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“moral embargo” a success.” The increasing power of the federal government as purchaser of first resort may help explain some corporate willingness to support these calls for private action against Japan. For this reason, this event is consistent with realism and inconsistent with liberalism and marxism because state economic power was used to coerce corporate behavior restricting exchange with Japan.

Throughout 1938, Hombeck and other officers at the State department (e.g., Herbert Feis, Economic Adviser and Francis Sayre, Assistant Secretary of State) were working on better ways to constrain Japan. By this time, the U.S. was willing to take steps against Japan without first prodding Britain to take a position. This change of heart was partly due to Britain’s appeasement of Hitler at Munich in September 1938, and the lurking possibility that Chamberlain would do the same with Japan. Hombeck typified new U.S. resolve:

I consider it highly desirable that a plan be made at this time for a comprehensive and thoroughgoing program of measures of material pressure...objective is to prevent a collapse of Chinese resistance to Japan and the concomitant of an early military victory by the Japanese which would place them for the time being in unopposed military occupation of the whole of China. Sharing the view that “close and thoroughgoing European cooperation” cannot be secured, I nevertheless do not believe that such cooperation is necessary – provided the United States would take and would make clear that it had taken and would continue in a determined position of refusal either to assent to or to acquiesce in disregard of its rights and destruction of its interests in China.

762. McCarty, “Stanley K. Hombeck and the Far East,” p.179. Hombeck was opposed to the use of moral embargos and overt public pressure on companies to comply. He took a principled position that the U.S. was a county of laws and legal authority to embargo Japan was the better course, although these sentiments never affected his informal and private guidance of companies previously (e.g., Ethyl Gas Corporation 1932).

763. On the fear of an Asian Munich agreement see Utley, Going to War with Japan, p.43. Other troubling signs from Britain included Anthony Eden’s resignation as Foreign Secretary over the Anglo-Italian agreement. Eden was fairly staunch in supporting Anglo-American cooperation generally and in Asia in particular, and his resignation “ended discussion at the highest level on Pacific cooperation.” Leutze, Bargaining for Supremacy, p.28.

764. Hombeck memorandum to Francis Sayre, Assistant Secretary of State. December 22, 1938, in Hombeck Papers, Box 369, Folder: Sanctions.
Hombeck’s desire to firm up the position of the U.S. regarding China was sorely tested by Secretary Hull’s repeated refusal to allow any State department sanction for loans to China throughout 1938. Hombeck’s basic reason for financial support of China was clear. He declared: “Better to have Chinese soldiers continue to fight Japan and to take now the small risk of an attack by the Japanese upon ourselves, than to take the risk of a stronger Japan, a Japan dominated and using the resources (including manpower) of China in support of her onward march of conquest.” As he had in June 1933, President Roosevelt weighed in on financial support for China and signed a $25 million dollar loan to China to be secured by future Chinese exports of tung oil on December 14, 1938. This government loan to support China is consistent with realism because of its intended effect of building an ally against an increasing threat. Roosevelt was not pleased with Hull’s unsupportive approach toward China, and he used his appointee under Hull at the State department, Under Secretary of State Sumner Welles, to stir up the research on a variety of more direct economic pressures against Japan (e.g., ending gold purchases, discriminatory duties on Japanese ships, forbidding short-term credit sales etc.).

Roosevelt himself was not yet ready to act against Japan, but Hombeck felt compelled to ensure that the public pressure that Hull responded to existed in favor of his preferred policies. Hombeck did not want to repeat the performance of President Hoover; although he knew Roosevelt was no Hoover, he could not be sure Hull wasn’t and wouldn’t sway Roosevelt unduly. Hombeck began a public “education” campaign, inviting in leading journalists and giving them vast amounts of properly constructed

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766. Borg, The United States and the Far Eastern Crisis, p.514; Dallek, Franklin D. Roosevelt and American Foreign Policy, p.193; Utley, Going to War with Japan, p.47.
information regarding how beneficial U.S. exports to Japan were in Japan’s war production. One such journalist, Eliot Janeway, wrote two important articles in 1938 describing how much assistance Japan received from the U.S..767 One of these articles appeared in Harper’s magazine and received considerable attention and generated support for limiting exports to Japan. This public sentiment mobilization did lead to economic exchange changes, including small-scale private embargos that began as early as Roosevelt’s Quarantine Speech. For example, an iron ore exporter wrote to Roosevelt to declare his support for a cessation of his business with Japan shortly after the speech.768 This sort of voluntary compliance with an as yet non-formalized system of economic pressure was not rare, only exceedingly difficult to aggregate in effect. The export of iron ore, finished steel and scrap steel products would rank high in official and public debates, but obscure somewhat the strategically vital trade in oil products. It is nonetheless warranted to review briefly the extent and significance of U.S. exports of iron and steel products to Japan.

During the first half of 1937, the U.S. sent Japan 1.3 million metric tons of scrap iron and steel out of a year end total of 1.9 metric tons. This represented a huge increase over all previous years, and as with prior large increases in Japanese demand, it was being monitored at the State department for indications of Japanese intent (See Table


768 McCarty recounts this instance where Arthur Christensen voluntarily gave up his business and urged an embargo on iron and other goods to Japan on October 14, 1937. McCarty, “Stanley K. Hornbeck and the Far East,” pp.139-40.
Japan’s attack on China in July confirmed the worst case assumption of Japanese intent and set off an internal debate at the State department about how little legal authority they had to control the export of steel products to Japan that were being and would continue to be used in China. The important general relationship in the steel products area is between finished steel product (e.g., plates, sheets and specialty metals with ferro-alloys like tungsten added for armoring purposes or in aircraft engine manufacturing), and its inputs: iron ore and coking coal; pig iron; or scrap iron and steel.

In general, to produce finished steel, scrap iron and steel can be mixed with small amounts of pig iron and with additional smelting processes yield finished products. Or, a lengthier process can be used, taking base iron ore and coking coal burning it in a blast furnace to produce pig iron, which can then be made into finished steel products. In either case Japan would need large supplies of scrap or large supplies of iron ore and coking coal. This choice would place Japan in one vulnerable situation or another: on the U.S. for scrap, or on North China, Manchuria and southeast Asia for iron ore and coking coal. Japan chose to draw on and build its strategy around the resources from its controlled territories, and risk the sea transport of the massive amounts of coking coal and iron ore necessary to make it work. This might have worked if Japan could have found all the iron ore it needed in North China. But, Japan’s invasion of China cost it iron ore supplies there from July 1937 until late 1938, and Australian supplies of iron ore were cut off in July 1938. With Malaya and the Philippines as the next largest sources

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769 Feis, The Road to Pearl Harbor, p.11. For example, cotton imports had surged in the post-Manchurian invasion period.
770 Schumpeter, The Industrialization of Japan and Manchukuo, pp.442-3.

385
outside the area under its control, Japan would remain vulnerable in its steel strategy even after it had occupied these territories during the war. These two territories supplied large amounts of iron ore to Japan through 1939, but by 1941 had reduced their shipments to zero. Drawing on the postwar Strategic Bombing Survey, Cohen noted:

Ironically, the effort in one direction only resulted in even greater dependence on water-borne transportation. To free herself from dependence on scrap imports, Japan had to increase her imports of iron ore. To produce the equivalent in pig iron of one ton of imported scrap required from two to three tons of iron ore and coking coal imports.\(^{771}\)

<table>
<thead>
<tr>
<th>Year</th>
<th>Iron and Steel Scrap</th>
<th>Pig Iron</th>
<th>Steel Sheets, black</th>
<th>Iron and Steel Sheets</th>
</tr>
</thead>
<tbody>
<tr>
<td>1929</td>
<td>208</td>
<td>28.474</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1932</td>
<td>164</td>
<td>888</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1935</td>
<td>1,082</td>
<td>1,668</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1936</td>
<td>1,058</td>
<td>2</td>
<td>n/a</td>
<td></td>
</tr>
<tr>
<td>1937</td>
<td>1,912</td>
<td>409</td>
<td>15,483</td>
<td>113,429</td>
</tr>
<tr>
<td>1938</td>
<td>1,382</td>
<td>316</td>
<td>1,696</td>
<td>13,523</td>
</tr>
<tr>
<td>1939</td>
<td>2,027</td>
<td>10</td>
<td>1,572</td>
<td>.806</td>
</tr>
<tr>
<td>1940</td>
<td>963</td>
<td>6</td>
<td>10,573</td>
<td>5,658</td>
</tr>
</tbody>
</table>

Table 7.1. U.S. Exports to Japan of Iron and Steel Categories in Thousand Metric Tons\(^a\)


\(^{771}\) Cohen, *Japan’s Economy in War and Reconstruction*, p.115. The Strategic Bombing Survey noted, “The significant feature of the "new" Japanese steel industry was that, in eradicating dependence on one kind of import, it had become vastly more dependent on water-borne transportation itself and on the availability of much greater amounts of iron ore and coal within Japan’s sphere of influence. The planners had been unable to escape from their dilemma.” United States Strategic Bombing Survey, *Basic Materials Division, Coals and Metals in Japan’s War Economy*, (Washington, DC: U.S. G.P.O., April 1947), p.68.
In one sense the data in Table 7.1 indicate a shift to raw materials from finished steel, which might have been treated with the ferro-alloys that allowed its direct application into shipbuilding or aircraft manufacture. This shift meant that Japanese steel companies would have to add their vital energy and investment resources into the production of finished steel, whether from U.S. scrap or fully developed from iron ore, and they would have to find their own source for ferro-alloys to make specialty steel products. This shift is noteworthy because finished steel products generally cost more and have higher profit margins, and presumably, would have been supplied to Japan in greater amounts than the raw materials. Because there is no clear evidence of direct U.S. government intervention to bring about these changes before the full embargo of September 23, 1940, we are left to conclude that steel companies willingly passed over higher profits in order to ship raw materials not finished goods. Although it may be true that the moral embargo on aircraft affected the decline in steel sheets and plates that previously had gone into Japanese airplane construction, the only evidence of steel-related companies complying was the aforementioned iron ore shipper who bowed out of the business in late 1937.

Japan was willing to make significant outlays of energy and investment to build indigenous steel capacity and passed the Iron and Steel Industry Control Law in July 1937 to help bring about greater self-sufficiency in steel production. Nonetheless, it can be argued that Japan’s importation of U.S. scrap iron and steel contributed to less thorough efforts on Japan’s part to fully develop stable supplies of steel products within

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772. This lack of information stands in contrast to the early 1920s period when steel and oil companies conferred with ONI regarding their sales to Japan of steel storage tanks and other items.
its sphere of control. Much like U.S. exports of crude oil and crude oil-refining equipment, scrap exports, to the extent they were relied on by Japan, helped reinforce Japan’s deficiency in steel production from iron ore deposits under its control (e.g., North China and Manchukuo). Japan’s war in China actually cut off supply of pig iron for a time as noted above, while most of its imported scrap came from the U.S. (e.g., 2027/2555 metric tons in the peak year 1939). Although large, this amount was a decreasing percentage of Japanese consumption of scrap steel, from 31% of Japanese consumption in 1936 to only 20% by 1940.

United States supply of pig iron to Japan is interesting because it largely displaced pig iron exports from the Soviet Union to Japan (See Table 7.2). As a result, the U.S. was not increasing Japan’s capabilities in its trade with Japan, rather it was merely replacing the source of Japan’s existing capabilities in this area. The significance of this replacement was entirely political, as the Soviet Union cut back on much of its commerce with Japan and U.S. suppliers merely picked up much of the slack. The large reduction in 1939 reinforced Japan’s reliance on scrap imports from the U.S. and its iron ore deficiencies.

773. Cohen, Japan’s Economy in War and Reconstruction, p.118.

388
<table>
<thead>
<tr>
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<th>1936</th>
<th>1937</th>
<th>1938</th>
<th>1939</th>
<th>1940</th>
</tr>
</thead>
<tbody>
<tr>
<td>U.S.</td>
<td>2</td>
<td>409</td>
<td>316</td>
<td>10</td>
<td>6</td>
</tr>
<tr>
<td>Soviet Union</td>
<td>322</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>N/A</td>
</tr>
<tr>
<td>Manchukuo</td>
<td>273</td>
<td>230</td>
<td>50</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>British India</td>
<td>311</td>
<td>317</td>
<td>335</td>
<td>N/A</td>
<td>N/A</td>
</tr>
</tbody>
</table>

Table 7.2. Exports of Pig Iron to Japan in Thousand Metric Tons


By the beginning of 1939, the U.S. embarked on a more unilateral and forward course in its Asia policy. Part of the reason the U.S. did this was to shore up the declining Anglo-American position of assisting China in its struggle with Japan. The British under Chamberlain only reluctantly gave any assistance to Chiang Kai-shek in 1938, and had intimated in early November 1938, that Britain might financially assist Japan in the development of a conquered China. Chiang Kai-shek responded by threatening that before that could happen he would surrender to the Japanese in a way that permanently excluded Britain from China. This Sino-British acrimony did not redound to Britain’s benefit in its relations with Japan, as instead, Japan pressed Britain to recognize its “unique position” in China after the Munich Agreement. The British

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775 Prime Minister Chamberlain said he was “quite certain that when the war is over and the reconstruction of China begins, she cannot be reconstructed without some help from this country.” Neville Chamberlain, November 2, 1938, in the House of Commons, quoted in Lee, Britain and the Sino-Japanese War, p.153

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rejected this and noted that even considering it would alienate the U.S. too much.\textsuperscript{776} With this uncertainty in Asia and overall stressed British position, the U.S. continued its halting efforts to aid China and constrain its own direct assistance to Japan’s military capabilities.

The U.S. did not directly confront Japan with economic pressure, however. It chose instead to assist China and allow the expansion of its commercial ties with the DEI and other Southeast Asian states. The Dutch were particularly interested in trading more with the U.S. from the DEI and had professed a desire “to get as much capital invested as possible in order that the United States would have a stake to rescue in the event of a Dutch war with Japan.”\textsuperscript{777} The investment stake of the U.S. in the DEI continued to be concentrated in the oil companies, but the trade stake accelerated from 1938 forward as the U.S. began buying massive amounts of DEI resources that were willingly sold to the U.S. instead of other countries, including the Netherlands itself.\textsuperscript{778} Chief among these U.S. imports were rubber and tin, and the U.S. began taking ever larger proportions of DEI production and export in these items. By 1940, the U.S. took 333,050 metric tons of the total 454,512 metric tons of rubber produced in the DEI.\textsuperscript{779} These trade ties increased as the Dutch felt more threatened by Japan and sought to bolster U.S. economic self-interest in protection of the DEI.\textsuperscript{780} These developments indicated a U.S. willingness to

\textsuperscript{776} Ibid., p.158; Reynolds, The Creation of the Anglo-American Alliance, pp.59-60. Many prominent British officials did support recognition of Japan’s gains and appeasement. Sir Robert Craigie, British Ambassador to Tokyo, was one through the end of 1938.

\textsuperscript{777} Statement of A.H. Elliot Managing Director of the Koloniale in the DEI to Donald Smith, American Trade Commissioner, Batavia, quoted in ONI report Serial No. 555-22, File No. 602-1000, February 26, 1937, File o-1-I, Register 12865D, RG 38.


\textsuperscript{779} Wolthus, “United States Foreign Policy Toward the Netherlands Indies,” p.17.

\textsuperscript{780} Jonathan Marshall argues that the economic self-interest of the U.S. was at stake in the DEI and was the product of real U.S. material needs. This is true but the Dutch desire to embroil the U.S. in its defense
assume a greater position in the trade in Southeast Asia precisely when Japan was seeking to expand rapidly there as well. Not unlike its aid position with China, by the late 1930s, the U.S. was gradually assuming a predominate stake in Asia directly in Japan's path.

7.4 The U.S. Position Firms as Japan Expands Against Britain and the Soviet Union

The increased position of the U.S. in the DEI's trade did not go unnoticed in Tokyo. Japan sought to increase its military presence in Southeast Asia as a means to improve its access and hopeful ownership of needed materials from the region. Japan's interest in advancing south was as strong as its interest in securing North China's resources for economic development. By the end of 1938, both Japan's army and navy were united in clamoring for a southern advance to secure economic resources and forward military bases. The symbiosis in Japan's two services' need for resources in southeast Asia helped feed an aggressive diplomatic campaign by Japan's political leaders. This was exemplified by Prime Minister Konoe Fumimaro in his promotion of "The New Order in East Asia" in November 1938. Although this proclamation spoke only of economic coordination between Japan, Manchukuo and China, many observers believed that Japan's resource needs would ultimately impel it southward. These concerns were borne out by events in early 1939.

since the middle 1920s was also important to the creation of this U.S. material interest. See Jonathan Marshall, To Have and Have Not: Southeast Asian Raw Materials and the Origins of the Pacific War, (Berkeley, CA: University of California Press, 1995).

In its bid for autarchy in steel production, one of the places Japan turned to for increased iron ore supplies was Hainan Island off the coast of southern China. This island was claimed by France and strategically situated next to northern French Indochina. The Japanese occupied the island in February 1939 and proceeded much further south in March 1939, claiming the Spratly island chain in the middle of the South China Sea. In occupying Hainan and the Spratly chain, Japan placed its navy squarely above Britain's base at Singapore. After a period of fortification, Japan would thus be able to threaten U.S. positions in the Philippines, but be a much greater threat to the commerce of Malaya and the DEI in addition to Britain's navy. This move satisfied both Japan's army and navy in establishing a position that both threatened any southern supply routes to Nationalist China and provided a forward base for future military and intelligence operations into Southeast Asia. These reasons were more accentuated by each service's direct interests, with the army more supportive due to its desire to close off Chiang's supplies. This did not obscure both services' understanding that DEI oil was crucial to their future operational capabilities.

These moves were pre-emptive predations against a declining France, but they increased the threat perception of both Britain and the U.S., although Britain was the most exposed. The U.S. reacted to these southern incursions but chose to evade British and French requests for economic pressure against Japan. As a signal of its position not to aid Japanese development of China, the State department blocked a loan from the Reconstruction Finance Corporation to an American company in occupied China and

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allowed China to use credits to purchase airplanes.\(^7\)\(^8\)\(^4\) Both instances are consistent with realism, but these were tentative measures of a U.S. still waiting for other states to determine their paths. One could argue that the U.S. was playing chicken with its smaller interests in Southeast Asia and the colonial empires of Britain and France, allowing Japan to threaten all of them to see which country would come under the fold of U.S. policy due to their need for U.S. naval protection in Asia. French and British navies were reconcentrating in the European and Mediterranean theaters as war loomed larger there, increasing the importance of the U.S. Asiatic Fleet. The U.S. did assist Britain in spring 1939, by moving the U.S. Fleet from the Atlantic to the Pacific in order to lessen Britain’s need to transfer more of its fleet from the Mediterranean to Singapore.\(^7\)\(^8\)\(^5\)

As the U.S. waited, it prepared the next measures of economic coercion it would employ against Japan. U.S. planning took into account the favorable manipulation of domestic American opinion, which had moved decisively in favor of confronting Japan through economic sanctions. Hornbeck responded to the early formulations of a scrap iron and steel embargo by pointing out that more attention was needed to the “psychological and internal political and diplomatic angles of the subject.” He held that after the successful airplane embargo, the American people had responded to the idea of a scrap embargo and this proposal should be evaluated not just on its economic effect in Japan but also its effect on Americans and third countries. At the time Hornbeck wrote

\(^7\)\(^4\) Utley, Going to War with Japan, p. 56. Roosevelt did begin to formulate the plans for financial pressure on Japan. In January 1939, he said: “I think we should start to lay the foundation for holding Japan accountable in dollars for the acts of her soldiers...it is a fact that there is a vast amount of Japanese owned property in the United States and that we have excellent precedent in the Alien Property Custodian Act for holding this property in escrow. Enough said!” Roosevelt to Hull, quoted in Norman Graebner, “Hoover, Roosevelt, and the Japanese,” in Borg and Okamoto, eds., Pearl Harbor as History, p. 41.

\(^8\)\(^5\) Many British officials worried that Japan’s moves south were timed to distract from Germany’s moves in Europe, perhaps even to lead British forces away from Europe in preparation for a German attack. Lee, Britain and the Sino-Japanese War, pp. 176-7.
this, Japanese imports of scrap iron and steel were reaching their peak, and Hornbeck was advocating not just an eventual embargo, but one well timed to coincide with increased American public opinion for one, possibly after outrage at the amounts exported in 1939 had been well voiced in public.\(^\text{786}\)

During spring and early summer 1939, Japan’s army continued to press against British interests in China and Soviet territories in outer Mongolia, while its navy consolidated its new positions in Southeast Asia. Japanese pressure in China against the British culminated in a humiliating capitulation by the British to Japan’s demands regarding the western concession-laden city of Tientsin in North China. The Japanese accused the British of shielding Chinese “terrorists” and not turning over Chinese silver in the British-controlled Tientsin banks as per Japan’s desire to end rival paper currencies in China backed by silver. Japan blockaded the city in mid-June and threatened military force against the British and French concessions in Tientsin. Britain feared this crisis would divert military resources away from Europe and sought a settlement on Japan’s terms. In the resulting Craigie-Arita agreement of July 24, 1939, Britain recognized that Japan had “special requirements” for safeguarding its own security and maintaining public order in China, not just Tientsin, and that Britain would not act in any way “prejudicial to the attainment” of Japan’s special requirements. Britain also pulled back on a 3 million pound loan to China from December 1938, refusing to extend the remaining 2.8 million pounds to Chiang Kai-shek.\(^\text{787}\)

\(^{786}\) See Hornbeck memorandum to Secretary of State, March 27, 1939, in Hornbeck Papers, Box 369, Folder: Sanctions.

The U.S. objected to Britain’s retreat from the principle of not recognizing a “special” position for Japan in China, and Roosevelt gave notice on July 26, 1939, that the U.S. would end the 1911 Japanese-American Treaty of Commerce and Navigation. Just two days after Britain’s capitulation of principle, the U.S. jolted Japan with this news which would take effect six months hence and allow the U.S. to restrict exports and imports at its discretion with no need for arbitration proceedings. Roosevelt acted without informing Britain to shore up Anglo-American resistance to Japan’s advances. Dallek noted: “Abrogation of the treaty achieved everything the administration could have wished. It encouraged London to be firmer with Tokyo, raised Chinese morale, and received widespread approval in the United States.”

It is important to note that during Britain’s crisis with Japan, the U.S. assisted Britain by transferring its fleet to the Pacific. Roosevelt ordered this, but not before he intimated that if Britain were to lose its Far East possessions it could always recover them. This minor point from mid-April 1939, illustrates the strategic commitment Roosevelt had already formed regarding Southeast Asia (i.e., it was expendable in the early stages of war).

At the same time that Japan was achieving coerced concessions from the British, its army was encountering an escalating conflict with the Soviets at the border of Mongolia and Manchukuo. The Soviets had been supplying Chiang Kai-shek with large amounts of military assistance, including fighter bombers and 250 Russian aviators. In fact, the Soviet Union was the single greatest military supplier to China after 1937, and

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788. Dallek, Franklin D. Roosevelt and American Foreign Policy, p.195. Support for abrogating the treaty had been building for some time, and Hornebeck had forcefully recommended it in December 1938.
the Japanese army probed the border with the Soviet Union to try and limit this trade. The Kwantung army had engaged the Soviets in border incidents during 1937 and 1938, with the Soviets withdrawing on repeated occasions. Japanese commanders in this forward region had inopportuneely concluded that the Soviet Union was weak and retreating due to disarray from Stalin’s purges. Local commanders of the Kwantung army launched air offensives against Soviet troops inside outer Mongolia and expected to advance without serious resistance. They moved against Soviet positions in spite of orders from central military authorities in Tokyo and Kwantung army headquarters at Hsinching not to do so. By August 1939, the clashes were intensifying and forcing the Soviets to transfer troops from their European operations area to the Far East.

This transfer of forces against Japan was one of the reasons Stalin bargained with Hitler toward the Nazi-Soviet Non-Aggression Pact of August 23, 1939. Just prior to the signing of this agreement on August 20, 1939, Marshal Georgi Zhukov attacked Japanese forces in and around Nomonhan and began to deal them a crushing defeat. Three days into the conflict, Japan learned of Germany’s agreement with the Soviet Union and its ensuing defeat at the Soviet Union’s hands took on widening domestic and international dimensions. The Kwantung army’s advances had often been riddled with entrepreneurial activities by local commanders, and in this instance, those activities had helped contribute to a stunning defeat in a first-class mechanized engagement. Imperial army headquarters dealt decisively with the local commanders and staff, transferring out all those officers responsible for the instigation of the conflict and utter defeat in battle.

791. Haslam, “Soviet Aid to China and Japan’s Place in Moscow’s Foreign Policy,” p.49
On September 15, 1939, Japan and the Soviet Union signed a cease-fire agreement that effectively restored stable border relations between them across the region. The damage to Japan's vision of the future of the Anti-Comintern pact was, however, far more significant as the Nazi-Soviet deal caused Baron Hiranuma's cabinet to fall to one led by General Abe on August 28, 1939.

Germany's swift revision of its arrangement with Japan regarding the Soviet Union caused a much needed retrenchment in Japanese planning. This retrenchment was not to benefit the Western powers in Asia or Japan itself. Hata Ikuhiko summarized Japan's plight well: "the Japanese in the end did accept the Soviet Union's demands, and opinion began to grow in military and diplomatic circles that Japan ought to give more attention itself to concluding a nonaggression pact with Russia in order to strengthen its position vis a vis Britain."793 Doubtless, many in Japan realized that Germany had used them to gain pressured concessions from the Soviet Union. Once these concessions were gained and consummated in the Nazi-Soviet pact, they allowed the Soviet Union to turn full force on Japan and administer a lesson in the penalties of overexpansion and lack of military discipline.794 This re-assessment brought down the Hiranuma government with its German alliance advocates, and restored some power to the Anglo-American leaning advocates in Japan. Premier General Abe appointed Admiral Nomura Kichisaburo as his Foreign Minister on September 25, 1939. Under Abe and Nomura the Japanese

794. This position was strengthened by the fact that only in February 1938 did Germany withdraw its military advisers and supplies from Nationalist China and in May 1938 recognize Manchukuo. Germany made these revisions in its relations between China and Japan only after Hitler reacted to intense Japanese lobbying and cleared out conservative military officers and their support of China in early 1938. See Boyd, The Extraordinary Envoy, pp.63-4; Chapman, "The Economic and Technological Basis of the German Alliance with Japan," p.32.
government sought to re-build ties to the U.S., but also appeared willing to court
Germany's counsel that Japanese rapprochement with the Soviet Union would allow
Japan and Germany to profitably exploit British weakness together.\textsuperscript{795} Japan's strategy
was thus a not so tactful effort to pressure Britain and placate the U.S. in an effort to keep
the U.S. neutral while Japan continued to advance against predominately British and
French interests in Asia.

Japan's overtures to the U.S. in the fall of 1939 were met with optimism by
Joseph Grew, but restraint and pessimism by Hornbeck and Roosevelt. The Abe-Nomura
desire for better relations centered on possibly renewing the commercial treaty with the
U.S. and extending a pledge not to apply "unnecessary pressure" on American economic
activities and nationals in China.\textsuperscript{796} As a testament to their revised attitude toward U.S.
interests, the Japanese offered to open the Yangzi river to general navigation as far north
as Nanking "in about two months."\textsuperscript{797} This fledgling offer was rebuffed in Washington.
Even though Japan did decrease its harassment of Americans in China, its recent behavior
driving Britain to the brink and blockading Shanghai were too much for U.S. policy
makers to overlook now that Europe was at war. Japan was obviously only looking to re-
balance its own over-extended position after Soviet victory and German "betrayal."
Hornbeck captured U.S. sentiment well:

We have many indications of an intention on the part of the Japanese to
cultivate better relations with the United States. They obviously intend to
try to improve the situation as regards petty harassing and abusing of
American business and American nationals. There is no indication as yet
of any thought or intention on their part of reorienting their policy in
regard to major matters...We need to be on guard lest, while changing their

\textsuperscript{796} Ibid., p.195.
\textsuperscript{797} Ibid., p.195.
\textsuperscript{797} Utley, Going to War with Japan, p.70.
tactics regarding things and persons, the Japanese, without altering their major strategy, create a popular impression that they are no longer doing damage to or menacing our interests.\textsuperscript{798}

Hornbeck's reasoning held sway even with Secretary Hull at this time, as Hull emphasized America's trampled rights and principles in China to his Japanese counterparts. For Hull, Japan's behavior was objectionable because it was rejecting the basic precepts of his belief system (i.e., liberal commercial exchange raises everyone's standard of living and causes peace). Japan was embarked on a relentless program of economic exclusion, forcing American and Western businesses out of Manchukuo, North China and Japan proper. Ambassador Grew labored mightily to convince U.S. policy makers that efforts to negotiate a new trade agreement were worthwhile and Japan's Yangzi offer was a legitimate and substantive concession from the tenuously situated Japanese moderates worthy of a show of U.S. support. Hornbeck helped dissuade Hull from accepting this view, reminding Hull that Stimson's restraint in late 1931 did not reinforce moderate Shidehara diplomacy in Japan, rather it helped undermine it by convincing the Japanese navy that there were no Western penalties with Japanese expansion.\textsuperscript{799} The decision to end the trade talks was ultimately made by Roosevelt himself in December 1939, and he reset the trade relationship with Japan to the condition where only 24 hour notice was required to alter or end exchange. Thus, by this point

\textsuperscript{798} Hornbeck memorandum to Secretary of State, September 2, 1939, in Hornbeck Papers, Box 425. Folder: Policy of the United States: Far East. Hornbeck dismissed Grew's pleas for a cooperative U.S. stance with Abe and Nomura: “The embassy apparently assumes that the Japanese military element can be caused by influences from within the Japanese state to bring the policies and action of Japan within limits which would satisfy the United States. In my opinion, adoption as a major premise of the thought that the ‘civilian’ element in the Japanese nation may gain ascendancy over the ‘military’ element and, having done so, would alter the objectives of Japanese policy can lead to nothing but confusion and error in reasoning with regard to the possible course of events in the Far East.” Hornbeck memorandum, December 19, 1939, quoted in McCarty, “Stanley K. Hornbeck and the Far East,” p.204.

\textsuperscript{799} McCarty, “Stanley K. Hornbeck and the Far East,” p.204; Utley, Going to War with Japan, p.71.
even a Japanese-led effort at reducing its threat perception in the U.S. resulted in further restrictions on economic exchange with the U.S. This suggests that U.S. planning against Japan was no longer responding to what it perceived as temporary Japanese overtures instead of real efforts at overall threat reduction.

American grand strategy debates at this critical juncture in December 1939 were undergoing an assessment as to how the U.S. should confront both Japan and Germany in a worldwide struggle without also driving the Soviet Union into their camp. Significant numbers of State department advisers and Presidential aides were arguing a Europe first position in which confronting both Germany and Japan simultaneously was unsound grand strategy. Hombeck, Hull and Soviet expert, Mr. “X,” debated these points, with Mr. X advocating “a sound policy [is] to engage in conflict on but one front at a time.” Mr X argued, “it is often best to abandon one bastion and concentrate on defense of another bastion.” Hombeck replied that he wasn’t aware that the U.S. was already in a defensive war, and more importantly, that he perceived no reason to abandon any part of the U.S. position. He held: “An ‘abandonment’ of our Far Eastern ‘bastion’ would in no way strengthen us for defense of our European ‘bastion.’”800 This debate was resolved by Roosevelt in favor of hardening the U.S. position against both Japan and Germany in support of Britain, while mildly appeasing the Soviet Union so that it would not join with Germany against all of Europe.801

As a result of this policy, the U.S. began to take ever stricter economic measures against Japan in December 1939. The U.S. stepped up its constraint of Japan’s war

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800. Memorandum of conversation between Hull, Hornbeck and Mr. “X,” December 11, 1939, in Hornbeck Papers, Box 396, Folder: Soviet Union-Soviet-Japanese Relations. Mr. X was possibly George F. Kennan, then serving as Second Secretary at the U.S. Embassy in Berlin. In any event, his positions represented much opinion in the State department (e.g., Sumner Welles, J. Pierrepont Moffat)

801. Dallek, Franklin D. Roosevelt and American Foreign Policy, pp.208-210, 214-5.
economy with the knowledge that Japan was increasingly vulnerable to U.S. pressure because of the cessation of assistance from Germany. Since the European war began, Germany had ended most exports of specialty equipment to Japan necessary for the development of its chemical and synthetic fuels industries. An ONI report from early December 1939 held:

German plant equipment deliveries for chemical production expansion in Manchuria and elsewhere have been shelved due to European hostilities. The Japanese government now realizes it is impossible to go ahead with the plans for the coal liquefaction industry because the country can no longer barter soya beans for German chemical equipment and processes. The government of the country possesses little gold reserves for the foreign exchange required for American equipment...Likewise the nation's gold production program, which plays such an important part in Japan's ability to meet her excess import balance, was held up due to the reluctance of the Finance department to issue the necessary permits for the remission of foreign currency for the mining machinery so urgently required...The success of the plan for the expansion of the chemical industry and other heavy industries depends entirely on the availability of equipment and materials from the United States.802

It is important to emphasize that Japan's economic dependence re-concentrated on the U.S. not simply because of its war in China, but rather because German technology and equipment alternatives became less available as had earlier Russian pig iron and oil supplies.803 Armed with the knowledge that Japan's economic dependence was re-concentrating upon the U.S., American officials took several decisions that increased Japan's vulnerability. The U.S. began to clamp down on Japanese capabilities

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802. See ONI Report from the Naval Attache at Tokyo, Serial No. 259, File No. 409-200, December 7, 1939, File o-l-g, Register 12417A, RG 38. Germany's decision not to supply Japan was based primarily on its own need for the machine tools and equipment, but Abe's desire not to affiliate too closely with Berlin played a role in this. See Murray, The Change in the European Balance of Power, pp.256-259.

803. Kuperan and Snyder have asserted the blanket opinion that Japan's economic vulnerability on the U.S. increased due to their China expansion, and not to the closure of many alternative suppliers for other reasons. More pointedly, the value of U.S. exports to Japan after 1937 never again equaled the 1937 value, illustrating the lack of increase in Japan's overall trade relations with the U.S. after the Sino-Japanese war broke out.

401
at this time precisely because alternative suppliers became unavailable and the prior U.S. strategy of supplying Japan to appear a reliable and credible economic partner was no longer necessary to pull Japan away from other states' influence and possible capabilities enhancement. The specific American actions following this December 1939 intelligence assessment and Presidential decision are detailed under the following four points. All of these actions are more consistent with realism rather than liberalism and marxism due to their purposeful application to restrict Japanese capabilities over divergent corporate preferences. Some actions are also more consistent with offensive realism over defensive realism because exchange with Japan was increased yielding increased production in Japan, not decreased production and assistance. The key distinction was that Japan's gains were entirely contingent on continued U.S. supply of critical components (e.g., synthetic industry parts).

First, the U.S. expanded the moral embargos to limit Japan's capability to produce weaponry, particularly the specialty steels needed for aircraft. Roosevelt had already ordered restraint in U.S. exports of tin, rubber, quinine, manganese and chrome ore in September 1939. By early December 1939, President Roosevelt ordered the embargos expanded to aluminum, molybdenum, and molybdenum's chief substitutes tungsten, nickel and vanadium. Aluminum was critical to the manufacture of aircraft and molybdenum was a necessary ferro-alloy for the hardening of airframes as well as machine tools. Secretary of the Treasury Morgenthau and Arthur Purvis, head of Britain's Allied Purchasing Mission in the U.S., combined to purchase most of the output of vanadium from Peru, the largest producing state, and coordinated the ending of

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804. McCarty, "Stanley K. Hornbeck and the Far East." p.210. Interestingly, substitutes for these items could be found almost exclusively only in the DEI.

402

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Canadian exports of nickel. Morgenthau gained the cooperation for the molybdenum efforts through the two mining companies who controlled domestic U.S. and global production of molybdenum, Climax Molybdenum Co. and Kennecott Copper. Both companies willingly complied with Morgenthau on December 8, 1940, overriding Secretary Hull's preference for unimpeded trade in these items.805 The aluminum action was effective as aluminum exports dropped considerably in 1940, but may have come too late on molybdenum because Japan possessed enough molybdenum to send some along to Germany in spring 1940.806 Almost regardless of their economic effects on Japan, the U.S.-British purchasing actions were important as the first steps in joint economic warfare against Japan, and foreshadowed the more critical cooperative actions on Japan's oil trade.807

Second, the U.S. acted against independent American oil companies in December 1939, restricting their plans to transfer the equipment and patented technologies necessary to manufacture aviation gasoline in Japan. Three companies, Phillips Petroleum, Badger and Universal Oil, had agreed to supply Japanese firms with rights to aviation gas production techniques. Universal had already begun building a "cracking" plant in Japan that would enable Japan to produce the necessary catalytic agents to refine crude oil into high-octane aviation gasoline. On December 20, 1939, the State department extended its moral embargo to "include plans, plants, manufacturing rights or


806. Aluminum plates and slabs exports went from 10 million pounds in 1939 to only 1.1 million pounds in 1940. Japanese molybdenum exports to Germany were arranged by the Japanese navy and received by the German air force beginning in April 1940, after the embargos were in effect. See Chapman, "The Economic and Technological Basis of the German Alliance with Japan," p.43.

807. These actions are well detailed in Barnhart, Japan Prepares for Total War, pp.179-180. See also McCarty, "Stanley K. Hombeck and the Far East," pp.210-11.
technical information required for the production of high quality aviation gasoline.\textsuperscript{808} Moral appeal, however, had to be backed by State department persuasion to gain adherence by the companies. After communications with the State department, Universal withdrew all of its engineering personnel from Japan and abandoned its originally-planned investment of $2 million dollars at the end of December 1939, declaring it had done so “in the interest of national policy.”\textsuperscript{809}

E. A. Badger, President of Badger Oil, had initially opposed canceling his arrangement because he deemed that Standard Oil was behind the State department’s efforts to end his trade with Japan and squeeze his independent business. Mr. Badger was correct in asserting that the U.S. government had learned of his business plans with the Japanese from Standard Oil of New Jersey officials. Frank Howard, the chief of Standard’s worldwide hydrogenation operations, notified the War and Navy departments about these dealings. Mr. Howard and Standard had earlier threatened to sell Japan hydrogenation and advanced refining technology to get U.S. State department pressure on Japan to reverse its stockpiling requirements and on U.S. independent oil companies through an embargo review. This time, the State department acted against Badger and the others to rescind deals that were already in the making, and Standard Oil was a contributor to the U.S. government’s effort to limit Japan’s energy capabilities. In 1934-35, when the independents were merely supplying crude and refined products to Japan and upsetting Standard’s market position, the State department purposefully did not act to limit the independents’ supplies for Standard’s benefit because their actions maintained


Japan's crude-based vulnerability and U.S. commercial reliability. But, in late 1939, these independent companies were squeezed to fulfill state policy because they were assisting Japanese autonomy efforts, which had the salutary effect of increasing Standard's future position against such independent companies. In both instances the U.S. acted to limit Japan's autonomous oil capability and pressured the companies to fulfill this policy vis a vis Japan.

The purposeful intent of this action was not lost on the Japanese. Their Ambassador protested to Hull who uncharacteristically informed him that the aviation gas deals were now as "obsolete" as Japan's declaration regarding the Nine Power Treaty.810 The U.S. would continue to export aviation gasoline to Japan, even in increasing amounts, but Japan's desire for an independent capability was undermined in these actions and would continue to be by American policy. Japan would accumulate stockpiles of U.S. aviation gasoline, but it would not accumulate enough American or German technical know-how to produce large amounts of the high-octane gasoline that would fuel advanced fighters by war's end. Because the U.S. supplied aviation gasoline to Japan, aiding its capabilities, but acted decisively to limit Japan's autonomous production capability, this event is most consistent with offensive realism. It also partially contra-indicates defensive realism which should have expected cessation of the air power enhancing supply of aviation gasoline.

These overt U.S. actions to constrain a key aspect of Japan's power projection (i.e., air power) were made possible by the European war and Germany's preoccupation with its own defense needs. However, Japan's decisions after the Nazi-Soviet pact to

810. Barnhart, Japan Prepares for Total War, p. 182.
pursue an "independent" foreign policy, distancing itself from Germany, contributed to Germany's decision to curtail technological and heavy industry assistance to Japan. Symptomatic of this was Japan's refusal to ratify an already negotiated trade treaty with Germany in October 1939. Because of these actions and U.S. adamancy, Japan lost assistance to its long-term economic and military capabilities from both Germany and the U.S. at this critical juncture. This cessation of technological exchange with Germany and the U.S. undermined Japanese oil production and left it with considerable invested capital in facilities that was unrecoverable and a large drag on Japan's overall capabilities.

For example, the cracking plant that Universal began building in Japan never became operational because "furnace tubes and hot oil pumps could not be obtained." Compatible vital component parts could only be obtained in the U.S. and they were not sent to Japan after the U.S. government-ordered pull out of Universal in December 1939. Similar inefficiencies occurred throughout Japan's synthetic fuels program. Japan's steel industry was incapable of producing necessary high-pressure steel vessels for the hydrogenation process, and instead Japan had to rely on imported German and American specialty equipment which fell off after 1939. Although Japan received synthetic fuels assistance from Germany's Ruhrchemie, they did not gain any material cooperation from IG Farben until January 1945. IG Farben viewed Japan as a predatory rival in its efforts at coal hydrogenation and did not cooperate in any way that might undermine its control of the Bergius method of coal hydrogenation. In general, German technical assistance foundered on both corporate and government mistrust of Japan. This was only haltingly

811 Chapman, "The Economic and Technological Basis of the German Alliance with Japan," p.43.
812 U.S.S.B.S., Oil in Japan's War, p.25

406

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overridden when Germany began losing ground in its war with the Soviet Union and decided a more capable Japan would help tie down U.S. efforts in the Pacific and delay American entry into Europe. Thus, only in the Spring of 1944 did Germany and Japan sign a Technical Exchange Agreement that promised German patent transfers of military and industrial processes, including synthetic fuels.814

As a result of this incomplete program, Japan’s synthetic fuels efforts contributed to its increased dependence on crude and refined products available largely only in the U.S. and the DEI. In contrast to Germany’s synthetic fuels program, Japan’s was a dramatic failure that consumed much needed capital and other resources.815 The postwar Strategic Bombing Survey summarized the effects of Japan’s synthetic program best: “Strategically, the contribution of Japan’s synthetic oil industry to the war may be regarded as negative. The manpower and materials expended on it certainly impeded the national war effort more than the synthetic oil production aided it.”816 This assessment demonstrates the negative effect on overall capabilities that can result from seemingly beneficial technological exchange, particularly where the exchange is incomplete with vital components remaining in the supplying state (e.g., U.S. furnace tubes). It is clear that the U.S. never intended Japan receive fully functional synthetic or aviation gasoline capabilities, but it remains unclear to what extent policy allowed partial exchange with Japan that contributed to its over-invested and unproductive programs. Nonetheless, when naval intelligence confirmed that Germany’s assistance to Japan was faltering, U.S.

815. Germany’s program led the world with synthetic fuel production accounting for 60% of Germany’s consumption of liquid fuels, and supplying 95% of Germany’s base aviation fuel needs during the war. See Raymond Stokes, “The Oil Industry in Nazi Germany, 1936-1945,” Business History Review, Vol. 59, No. 2. (Summer 1985), pp.254-77.
816. U.S.S.B.S., Oil in Japan’s War, p.42.
restrictions were stepped up against Japan's fledgling oil autonomy efforts, reinforcing Japan's crude and refined products dependency on the U.S. and the DEI.

Third, the U.S. impaired Japan's independent capabilities through the purchase of Japanese gold. Through these gold purchases during the latter half of the 1930s, the U.S. was paradoxically raising Japan's U.S. dollar purchasing capacity while restricting Japan's access to U.S. and Western hemispheric goods priced in U.S. dollars (e.g., Peruvian Vanadium). Beginning in 1937, the U.S. purchased almost all of Japan's gold exports and transferred dollars to Japan that covered Japan's trade deficit with the U.S. (See Table 7.3). Despite limited yet pointed domestic critique of this trade enabling financial assistance to Japan, the U.S. appears to have purchased Japanese gold for two principal reasons. First, the U.S. was intent on importing as much of the world's gold as possible in order to become the primary player in any future monetary system, and therefore Japanese gold was desired as was Dutch or most other countries' gold.

Second, U.S. purchases reoriented Japan's financial and trade relations toward the U.S. and away from Britain. In the initial years after all three states abandoned the gold standard, Japan had re-linked its currency to the British pound as it expected much of its future trade to be with pound-denominated countries (e.g., India, Australia, DEI). By purchasing Japanese gold and supplying U.S. dollars, the U.S. Treasury helped pull Japan

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817. There are no direct discussions or explanations of Japanese gold buying from U.S. officials (e.g., in Treasury Secretary Morgenthau's diaries or John Blum's otherwise excellent books). Henry Douglas wrote an excellent critique of this monetary exchange that enabled Japan to finance its war materials imports and maintain a surplus dollar balance in the immediate prewar years. Douglas' analyses were given wide circulation among the highest U.S. officials, including the President. See Henry Douglas, "America Finances Japan's "New Order"," Amerasia, Vol. IV. March 1940-February 1941, pp.221-224; Thomson, "The Role of the Department of State," p.100; Utley, Going to War with Japan, p.108.

818. The U.S. even demanded gold transfers instead of dollar payments from prospective allies like the Dutch in 1940 for military exports to the DEI. The U.S. was also intent on taking as much British gold as it could and forcing the British to sell their dollar-denominated assets to finance war purchases. See Wolthus, "United States Foreign Policy Toward the Netherlands Indies," p.21; Blum, From the Morgenthau Diaries: Years of Urgency, 1938-1941, pp.169-171.
away from financial condominium with Britain and limited the economic enticement in any possible Anglo-Japanese political rapprochement. For these reasons, the gold exchange in this period is consistent with offensive realism because the U.S. was maximizing its influence position and possible control over Japan, preventing it from using its gold to forge relationships with other states (i.e., binding Japan to the U.S.). This exchange contra-indicates defensive realism because it did increase Japan’s capabilities to conduct its trade and finance activities across the Western hemisphere. Because the exchange was done by the U.S. government exclusively for its own purposes, it is also somewhat inconsistent with liberalism and marxism.

819 U.S. gold purchases also prohibited German-Japanese exchange of Japanese gold for German technology at a time when German gold reserves were negligible and Germany’s annexation of Austria was partly driven by the desire to acquire Austrian gold reserves to assist German trade needs. See Murray, The Change in the European Balance of Power, pp. 256-7.
<table>
<thead>
<tr>
<th>Year</th>
<th>Total Exports and To U.S./G.B.</th>
<th>Gold (in millions of specified unit: Yen or Dollars)</th>
<th>Silver (in millions of specified unit)</th>
<th>Yen-Dollar Average Exchange Rate (1 Yen = x Dollars)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1930</td>
<td>Total</td>
<td>Y 308.6</td>
<td>Y 2.4</td>
<td>$.4939</td>
</tr>
<tr>
<td></td>
<td>To U.S.</td>
<td>$ 157</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1931</td>
<td>Total</td>
<td>Y 419.9</td>
<td>Y 1.6</td>
<td>$.4885</td>
</tr>
<tr>
<td></td>
<td>To U.S.</td>
<td>$ 199</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1932</td>
<td>Total</td>
<td>Y 112.7</td>
<td>Y 8.7</td>
<td>$.2811</td>
</tr>
<tr>
<td></td>
<td>To U.S.</td>
<td>$ 43</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1933</td>
<td>Total</td>
<td>Y 20.9</td>
<td>Y 7.7</td>
<td>$.2511</td>
</tr>
<tr>
<td>1934</td>
<td>Total</td>
<td>Y .6</td>
<td>Y 14</td>
<td>$.2972</td>
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<td>1935</td>
<td>Total</td>
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<td>Y 227.3</td>
<td>$.2871</td>
</tr>
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<td></td>
<td>To U.S.</td>
<td></td>
<td>Y 3.73</td>
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</tr>
<tr>
<td></td>
<td>To G.B.</td>
<td></td>
<td>Y 223.57</td>
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</tr>
<tr>
<td>1936</td>
<td>Total</td>
<td>0</td>
<td>Y 38.2</td>
<td>$.2902</td>
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<tr>
<td></td>
<td>To U.S.</td>
<td></td>
<td>Y 4.7 ($2.144)</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To G.B.</td>
<td></td>
<td>Y 33.5</td>
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</tr>
<tr>
<td>1937</td>
<td>Total</td>
<td>Y 866.9</td>
<td>Y 11.1</td>
<td>$.2879</td>
</tr>
<tr>
<td></td>
<td>To U.S.</td>
<td>$ 265.2</td>
<td>Y 2.2 ($1.271)</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To G.B.</td>
<td></td>
<td>Y 8.9</td>
<td></td>
</tr>
<tr>
<td>1938</td>
<td>Total</td>
<td>Y 660.6</td>
<td>Y 15.6</td>
<td>$.2845</td>
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<tr>
<td></td>
<td>To U.S.</td>
<td>$ 144.2 ($2.93)</td>
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<td></td>
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<tr>
<td>1939</td>
<td>Total</td>
<td>Y 663.8</td>
<td>Y 23</td>
<td>$.2596</td>
</tr>
<tr>
<td></td>
<td>To U.S.</td>
<td>$ 202 ($4.234)</td>
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<tr>
<td>1940</td>
<td>Total</td>
<td>Y 320.1</td>
<td>Y 30.9</td>
<td>$.2344</td>
</tr>
<tr>
<td></td>
<td></td>
<td>$ 108</td>
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</table>

**Table 7.3: Japanese Exports of Gold and Silver, 1930-1940**

The dollar values of U.S. silver and gold purchases from Japan do not equal the Yen value reported in Japanese statistics when converted at average exchange rates. This may be due to preferential prices paid by the U.S. to Japan as Henry Douglas noted. British purchases of Japanese Silver were reportedly fully re-exported to the U.S. and data for every year by importing country was not available. The U.S. did buy some Japanese gold in early 1941, but the amounts were noted as considerably smaller than previous years and ended in June 1941. See Blum, *From the Morgenthau Diaries: Years of Crisis, 1928-1938*, pp.205-410.
Beginning in October 1938, Japan converted its pound balances in London to U.S. dollars. After the outbreak of war in Europe, Japan dropped its pound-related transactions entirely and linked the Yen to the U.S. dollar.\(^{820}\) Japan’s decision to re-link the Yen to the dollar stemmed from Britain’s decline as a reliable trading partner and Japan’s U.S. import requirements and financing ties to the New York market.\(^{821}\) This conscious choice on Japan’s part came at the end of a period of trade and financial centralization by the Japanese government, which by August 1938 had yielded the government complete control over all foreign exchange and trade.\(^{822}\) As the December Office of Naval Intelligence report noted, Japan’s government had aggregated to itself control over all trade and finance and had not done so in a way that yielded efficient resource allocation or purchasing outcomes, particularly when it came to the payment for importations of machinery (e.g., mining equipment and machine tools).

As a result of the Japanese government’s concentration of authority over machinery purchases and the cessation of the German machinery trade, the fourth U.S.


\(^{822}\) Dowd, “Japanese Foreign Exchange Policy,” pp.82-85,105-110. The Japanese government accomplished this centralization through revisions to the Foreign Exchange Control Law in July 1937 and August 1938, and the July 1, 1938, expansion of the Foreign Trade Control Law to cover all imports and exports.
policy adaptation drastically limited Japan’s access to machinery necessary for both gold mining and war materials production. Subsequent to its Gold Production Law of 1937, Japan was purchasing vast amounts of gold mining equipment from the U.S. in order to produce the gold it needed for export to the U.S. to finance its bilateral trade deficit with the U.S. This circular production, trade and finance relationship diverted Japanese mining and production efforts from other ventures that might have yielded more critical strategic benefits (e.g., oil drilling in North China). This relationship bound Japan’s efforts to achieve industrial autonomy ever closer to America’s willingness to supply the necessary machinery for production in Japan and Manchuria. The value of American machinery exports, including mining equipment, increased dramatically from 1930, but did not yield Japan the autonomy in industrial and military production it desired (See Table 7.4). These U.S. machinery exports were valuable to the U.S. as well, but by the late 1930s, there were many more palatable alternatives (e.g., Britain, France, domestic production). For example, in 1940 machinery exports to Japan represented 12.9% of total U.S. exports to Japan, a significant increase in importance from the early 1930s.823

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<table>
<thead>
<tr>
<th>Year</th>
<th>Value of U.S. Exports of Industrial Machinery</th>
</tr>
</thead>
<tbody>
<tr>
<td>1930</td>
<td>$6,452,000</td>
</tr>
<tr>
<td>1931</td>
<td>$3,431,000</td>
</tr>
<tr>
<td>1932</td>
<td>$2,393,000</td>
</tr>
<tr>
<td>1933</td>
<td>$2,971,000</td>
</tr>
<tr>
<td>1934</td>
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<td>1935</td>
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<td>1936</td>
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<tr>
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<tr>
<td>1938</td>
<td>$26,317,000</td>
</tr>
<tr>
<td>1939</td>
<td>$27,667,000</td>
</tr>
<tr>
<td>1940</td>
<td>$29,232,000</td>
</tr>
</tbody>
</table>

Table 7.4: U.S. Exports of Industrial Machinery to Japan, 1930-1940

Industrial machinery exports include mining equipment and machine tools with no discreet values for the substantial component of gold mining equipment broken out. Table data adapted from U.S. Department of Commerce, Commerce Yearbooks, 1930-1940, and reproduced in Dowd, “Japanese Foreign Exchange Policy,” p.342.

Japan's bureaucratically impaired acquisition and distribution of machinery led to inefficient production readily apparent as early as 1939. This was particularly evident in Manchuria where by 1941 much imported machinery lay idle due to insufficient spare parts and lubricating oils. Echoing the December ONI assessment, Lawrence Dowd noted that “serious domestic maladjustment of production” was occurring in Japan as payments for imported gold mining equipment competed against payments for machine...

tools necessary for military industrialization in Japan proper and Manchuria. Japan’s effort to catch up in production of machine tools was facilitated by its passage of the Machine Tool Industry Act in March 1938. However, Japan’s machine tool products were “not of high quality by American standards,” and suffered from a lack of mass production know-how and reliance on specialty materials from the U.S. (e.g., Norton grinding wheels, Bethlehem steel and high-speed small tools). Furthermore, Japan’s reliance on American machine tools carried with it a reliance on American steel inputs (e.g., scrap iron) and lubricating oils. Eliot Janeway captured the mutually reinforcing nature of Japan’s dependence on these various inputs and the underlying American strategic purpose in this trade (i.e., embedding dependency, inefficiency and large adjustment costs into Japan’s production processes):

Japan is making her gears with American machine tools. The steel and the tools are useless if they are not used together, the steel because an old-fashioned tool cannot cut it, the tools because they will destroy a less strongly finished steel...All of the complicated and expensive machinery Japan imports is fitted with oil pumps, designed to force just the right grade and kind of lubricating oil between metal surfaces at just the right speed, and thus, by preventing friction, to lengthen the life of the tool or the engine. And so Japan must acknowledge the hold over her economy of yet another unique American product, which hardly shows up as a significant item in her list of imported goods and yet without which an integrated modern economy would be out of the question. The steel takes the tools, and the tools take the oils, and Japan must come to the United States for all three.

827 Janeway, “Japan’s New Need,” pp.339-340, emphasis added. Japan’s reliance on American lubricating oils would pose a significant substitution dilemma from 1941 forward. The oils Japan did obtain in the DEI “were entirely different from the oils formerly obtained from America and Canada,” and this adjustment led to considerable wartime operating inefficiencies. See U.S.S.B.S., The Japanese Machine Building Industry, p.8.
Janeway was fed this information and analytical emphasis by Stanley Hornbeck, whose intent appears to have been to educate the American public, Secretary of State Hull and the Japanese regarding the critical nature of Japan’s vulnerability to the U.S. and the influence position that this relationship implied.\textsuperscript{828} Janeway ended his article with an important observation on the fundamental basis of economic exchange between the U.S. and Japan. He noted, “what Japan is necessarily and inevitably involving herself in is an economy integrated toward continued imports from one country, interdependent indeed, but far from independent of that country’s good will.”\textsuperscript{829} By January 1940, the U.S. was not interested in trading its good will in machine tool exports for limited gestures of Japanese cooperation in China and elsewhere. As part of President Roosevelt’s desire to dramatically increase American aircraft production both for itself and allied air forces (i.e., Britain and France), he directed Treasury Secretary Morgenthau to cancel all Russian and Japanese machine tool orders related to aircraft engine production. On January 30, 1940, Morgenthau obtained the compliance of the major machine tool producers through their National Machine Tool Builders Association, and the rationing of machinery to Japan began in earnest.\textsuperscript{830}

Machinery export restrictions against Japan would accelerate throughout the spring and summer of 1940, under the careful watch of President Roosevelt, Secretary Morgenthau and a growing contingent of economic warfare advocates in the State department (e.g., Stanley Hornbeck, Herbert Feis, Dean Acheson, Joseph Green, Colonel

\textsuperscript{830} Blum, From the Morgenthau Diaries: Years of Urgency, 1938-1941, p.116; Barnhart, Japan Prepares for Total War, pp.185-6.
Russell Maxwell and Charles Yost).\textsuperscript{831} In May 1940, President Roosevelt removed bureaucratic control over machine tool exports from the economic appeasement-oriented Secretary of State Hull, and placed the key decisions in the hands of Morgenthau and the economic warfare advocates by transferring nominal authority to the National Defense Advisory Commission (NDAC) headed by GM president William Knudsen. Roosevelt noted, "the only thing that now remains outside the Commission...is the coordination of the foreign government purchases in this country, which has, primarily, a financial aspect and that will remain in the general coordinating field of the Treasury Department, of course."\textsuperscript{832} This reservation meant that Secretary Morgenthau would retain bureaucratic authority over actual foreign purchases of machine tools, and Hull reluctantly gave in to this exclusionary move.\textsuperscript{833} President Roosevelt established this precedent of using financial administration (i.e., the Treasury) to control exports, limiting Hull's trade authority at the State department. This process would be replayed under more important auspices in late July 1941 when Japanese funds were blocked from purchasing oil that was technically not restricted for export to Japan.

7.5 Japan Tacks South and Britain Bargains for America to Stem its Ebbing Resistance in Asia

Japan's limited effort to improve relations with the U.S. under the Abe cabinet earned meager results as the U.S. expanded its informal embargos, particularly against

\textsuperscript{831} Utley, Going to War with Japan, pp.120-121; Feis, The Road to Pearl Harbor, p.74.
\textsuperscript{832} President Roosevelt, quoted in, Blum, From the Morgenthau Diaries: Years of Urgency, 1938-1941, p.148.
\textsuperscript{833} Hull generally assented to export denials to Japan when a domestic justification for the materials was made the primary argument. Again, liberals appear to require liberal justifications for realist exchange practices. For a favorable reading of Hull's principled myopia see Utley, Going to War with Japan, pp.119,121. Utley contends that Roosevelt "invariably supported" Hull in most important Japanese exchange decisions, which is a gross overstatement, particularly in light of Roosevelt's backing of other officials to aid China for example against the heated opposition of Hull.
Japan's raw materials and aviation production needs. Throughout the winter of 1939-1940, U.S. officials were direct in their dismissals of Japanese confrontation reducing overtures and in their actions to curtail Japan's ability to acquire needed raw materials. This directness can be explained by U.S. officials' general desire to confront Japan vigorously to shore up Anglo-French resistance and divert Japan from easily exploiting European weakness by making it concentrate on U.S. policy changes. As noted earlier, this tactic was evident in the U.S. termination of the bilateral commercial treaty in July 1939. America's hard line and the failure to reach some new bilateral commercial furthered the collapse of the Abe government in January 1940. Premier Admiral Yonai and Hirota on his second tour as Foreign Minister were then ushered in as Japan's leaders on January 16, 1940. Under this navy-inspired leadership, Japan began a more active diplomatic campaign for southern expansion and Chinese isolation, despite the initial hope of some U.S. officials for even greater cooperative ventures from Yonai (e.g., Ambassador Grew).

Under Foreign Minster Hirota, the Yonai cabinet began to increase its pressure on vulnerable European colonies in Asia and established the Chinese puppet regime at Nanking under Wang Ching-wei. In preparation for increased diplomatic and military pressure against the DEI, on January 12, 1940, Japan terminated its Treaty of Judicial

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835. Feis, The Road to Pearl Harbor, p.46. Admiral Yonai has been considered by many scholars as part of the moderate navy elite (i.e., the Treaty Faction), which sought to avoid military confrontation with the Anglo-American powers. This assessment does not, however, alter the fact that under Yonai Japan began to exert much greater pressure against European southeast Asian colonial possessions and issued a war warning regarding the effect of a general American trade embargo in March 1940. See Michael Barnhart, "Japanese Intelligence before the Second World War: "Best Case" Analysis," in Ernest May, ed., Knowing One's Enemies: Intelligence Assessment Before the Two World Wars, (Princeton, NJ: Princeton University Press, 1984), pp.450-1; Feis, The Road to Pearl Harbor, p.51.
Settlement, Arbitration, and Conciliation with the Netherlands.\textsuperscript{836} This action removed any formal barrier to resolving disputes by other than peaceful means and signaled the potentially imminent movement of Japanese forces southward. The southern advance strategy, dominant among Japan's naval elites appeared to be in full swing under Yonai and Hirota, and was poised to threaten America's single greatest foreign investment position in Asia (i.e., Stanvac's holdings in the DEI).\textsuperscript{837} The U.S. observed these diplomatic moves of Japan and the increasing discomfit of Dutch officials, who contended that Japan's oil demands on them were a direct result of Japanese fears of a U.S. oil embargo. U.S. officials concluded that Japan would likely press for increased economic benefits from the DEI by offering a non-aggression pact to the Netherlands.\textsuperscript{838} Japan's graduated approach at securing greater economic benefits from the DEI might have continued had Germany not begun its western offensive in early April 1940, invading Denmark and Norway on April 9.

Japan took advantage of the imminent danger to the Netherlands government by issuing a stark claim to DEI resources on April 15, 1940. Foreign Minister Arita said:

\begin{quote}
With the South Seas regions, especially the Netherlands East Indies, Japan is economically bound by an intimate relationship of mutuality in ministering to one another's needs...contributing to the prosperity of East Asia through mutual aid and interdependence. Should hostilities in Europe be extended to the Netherlands and produce repercussions in the Netherlands East Indies, it would not only interfere with the maintenance
\end{quote}

\textsuperscript{836} Feis, The Road to Pearl Harbor, p.52.
\textsuperscript{838} See memorandum from Erle R. Dickover, American Consul General at Batavia, to Secretary of State, February 20, 1940, in Naval Intelligence Reports. "Political Conditions in the Dutch East Indies," File c-9-b. Register 18451B, RG 38. Interestingly, Dickover concluded the Dutch would reject Japanese demands "on the grounds of the long-established Netherlands policy of the open door and equal opportunity for all in the Indies." The exclusion of Japan while invoking the principle of equal treatment continued even at this late date.
and furtherance of the above-mentioned relations of economic interdependence and of co-existence and co-prosperity, but would also give rise to an undesirable situation from the standpoint of the peace and stability of East Asia. In view of these considerations, the Japanese Government can not but be deeply concerned over any development accompanying an aggravation of the war in Europe that may affect the status quo of the Netherlands Indies.  

The United States reacted more sternly to this declaration than did the Dutch government, which was generally “relieved” that Japan did not make more explicit demands. Nonetheless the Dutch were still interested in securing some statement from the United States to counter Japan’s diplomatic advances. Secretary Hull issued a clear declaration on April 17, which read in part:

Any change in the status of the Netherlands Indies would directly affect the interests of many countries...many countries, including the United States, depend substantially upon them for some of these commodities (rubber, tin, quinine, copra et cetera). Intervention in the domestic affairs of the Netherlands Indies or any alteration of their status quo by other than peaceful processes would be prejudicial to the cause of stability, peace and security not only in the region of the Netherlands Indies but in the entire Pacific area.

President Roosevelt reiterated Hull’s sentiments in a press conference the next day, solidifying U.S. DEI deterrent policy toward Japan. By linking any forceful change of the DEI’s status to the broader question of peace in the Pacific, the U.S. was acknowledging and communicating to Japan that conflict over the DEI would carry the risk of conflict with the U.S.

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840. Ibid., p.56
842. For their part, the Japanese had also reached this conclusion in naval mapping exercises in mid-May 1940. See Tsunoda, “The Navy’s Role in the Southern Strategy,” pp.244-6.
increased U.S. threat perception of Japan due to the possible loss of vital DEI exports to the U.S., which was still growing at this time (e.g., rubber, tin). The dual nature of increased American threat perception of Japan (i.e., both military and economic) meant that U.S. power would need to be used to delay a war in the Pacific as long as possible in order to ensure the maximum of DEI supplies to the U.S.. U.S. deterrence of a Japanese move against the DEI required further efforts after Germany began its full-scale western offensive with attacks against the Netherlands and Belgium on May 10, 1940. President Roosevelt coordinated the effective neutralization of the DEI by having Britain and the Netherlands issue statements that no foreign occupation of the DEI was desirable or would occur, despite the dramatic collapse of the Netherlands government and the potential security vacuum it created in Southeast Asia. Under new Prime Minister Winston Churchill, Britain complied with this request, issuing a statement to the Japanese calling for maintaining the status quo of the DEI and declaring that no British intervention would occur there. Dutch authorities in the DEI, Japan and later in London issued statements declaring that they sought no outside intervention to secure the DEI, and the U.S. made certain that these statements were communicated to the Japanese repeatedly in mid-May 1940.

Roosevelt's success in coordinating a joint deterrent effort with Churchill rested on the U.S. assuming the role of reliable oil supplier to Japan in order to limit Japan's need to strike south to obtain DEI oil resources. This did not mean, however, that the U.S. would supply Japan in unlimited quantities or meet Japan's full demands on American oil exporters. Under Hornbeck's tutelage, American oil company exports

843. Winston Churchill was officially inaugurated as Prime Minister on May 10, 1940.
fulfilled Japan's basic demands without overly increasing their stockpiles, providing assurance of American supply in the near term in order to alleviate the growing pressure on the DEI. For example, Hornbeck coordinated American oil company responses to increased Japanese demand for aviation gasoline. E.J. Sadler, director of foreign production for Standard Oil of New Jersey, had forwarded to Captain Schuirmann, U.S.N., Japanese bids for 150,000 drums of aviation gasoline. Hornbeck advised Schuirmann to order the company to stall on the bid and to see to it that no more than 2,000 of these transferable and autonomy-enhancing drums would be sold to Japan. Hornbeck also informed Captain Schuirmann that stalling was the best tactic while awaiting the imminent passage of Congressional authority for Presidential embargos on war-related materials.\textsuperscript{845}

During late May and early June 1940, Churchill tried to inveigle the U.S. to take an even greater economic and security burden in Asia by requesting that the U.S. Fleet visit Singapore and assume a more direct and visible role in defending Britain's key naval base. Roosevelt would not accede to this request nor the implication of defending Britain's Asian empire while not achieving his preferred role of American supremacy in any joint operational planning.\textsuperscript{846} Instead, Roosevelt ordered the Pacific Fleet only to remain at Pearl Harbor as a milder deterrent to a Japanese naval movement southward. Even this order was strongly resisted by Admiral Richardson, Commander U.S. Pacific Fleet, who wished the Fleet to return to the American west coast because of its unclear

\textsuperscript{845} See Hornbeck memorandums, June 7 and June 8, 1940, in Hornbeck Papers, Box 308, Folder: Navy 1938-1944.

\textsuperscript{846} Leutze, Bargaining for Supremacy, pp.130-135.
mission in the event of a Japanese move south. American reticence to make a greater commitment to British and Dutch possessions remained unchanged despite the increasing incentives Japan was receiving to pressure European colonial possessions in Asia. On May 22, 1940, Germany made it clear to Japan that despite its defeating the Netherlands it would make no claim on the DEI, preferring instead that Japan vigorously press its own claims against the Dutch and British. The failure of the Yonai cabinet to act aggressively upon this opportunity caused dissension within Japan’s army-navy elites, leading to the replacement of the Yonai cabinet on July 22, 1940. The army had begun its own operational planning for advance against French Indochina, Singapore and the DEI, forcing the navy to assume an even more aggressive posture against the United States and Britain to maintain its position within Japan’s power structure.

Germany’s clear signal to Japan to move aggressively against Anglo-Dutch positions caused Churchill to seek greater clarity in American naval commitments. Churchill chose to portray Britain’s position in the Far East as exceedingly tenuous, necessitating either increased American military and economic pressure on Japan, including imposing a full trade embargo, or a negotiated settlement with Japan that better

847 Wolthus, “United States Foreign Policy Toward the Netherlands Indies.” p.97. A part of the U.S. Fleet was first transferred to Pearl Harbor in April 1939 to deter Japan from further advances south after it had occupied Hainan Island. This part of the U.S. Fleet was renamed the Pacific Fleet. Richardson was convinced that “Dr. Hornbeck was exercising a greater influence over the disposition of the Fleet than I was.” Richardson statement during Pearl Harbor Attack Hearings, quoted in, ibid., p.93.


849 The dissatisfaction with the Yonai cabinet on this point led some extremists to attempt the assassination of Yonai and other cabinet officials on July 5, 1940. See Ikle, German-Japanese Relations, pp.157-8; Hosoya, “The Tripartite Pact, 1939-1940,” pp.211-214.

850 Tsunoda, “The Navy’s Role in the Southern Strategy,” pp.252-54. As a way of strengthening its internal and external position, Japan’s navy also pushed for acceptance of Germany’s offer to mediate Russo-Japanese relations. The navy sought German good offices to secure Japan’s northern front by helping direct Soviet endeavors toward the Middle East and India, in addition to strengthening its technical cooperation with Germany’s armed forces. See Chapman, “The Economic and Technological Basis of the German Alliance with Japan,” p.41; Hosoya, “The Japanese-Soviet Neutrality Pact,” pp.40-48.
guaranteed Japan's finance and trade needs. This British proposal of June 27, 1940, was dismissed by Roosevelt and Hull, but had an eerily similar ring to Roosevelt's proposal to Prime Minister Chamberlain for an economic blockade of Japan in winter 1937-1938. The U.S. rejected this stark dichotomous choice set. More pointedly, the U.S. would not accept a supporting role in defending the British empire and "acquiescing in British grand strategy." Instead, while continuing negotiations with Britain on destroyer transfers and joint planning, Roosevelt accelerated the overhaul of American military power and the reorganization of his administration for the coming war.

President Roosevelt achieved this reorganization of American power and purpose through several actions from May through early July 1940. First, on June 19, Roosevelt added two pre-eminent Republicans to his cabinet, former Secretary of State Henry Stimson as Secretary of War and Frank Knox as Secretary of the Navy. Stimson's record with respect to Japan was clear and his appointment in itself signaled the likely future course of U.S. policy toward Japan. Second, Roosevelt began the massive rearmament effort asking Congress on May 16, 1940, for dramatic increases in defense spending, exemplified in his call for airplane production capacity of 50,000 per year. More importantly, Roosevelt requested an additional $5 billion in defense expenditures on July 10 to rectify the strategically unseemly necessity of moving the U.S. Fleet between the Atlantic and the Pacific oceans to achieve desired naval power projection. Among other things, these appropriations, signed into law on July 20, 1940, were intended to build an

851. See Aide-Memoire, from British Embassy to U.S. Department of State, June 27, 1940, in Foreign Relations, 1940, Vol. IV, pp.365-66. In this appeal, Britain emphasized its solitary status opposing Germany and Italy: "it is now impossible for us to offer opposition in aggression both in Europe and the Far East...there appear to be only two courses open. The first is that the United States should increase their pressure on Japan in order to maintain the status quo either by imposing a full embargo or by the despatch of ships to Singapore."

852. Adolf Berle, President Roosevelt's trusted adviser, quoted in Leutze, Bargaining for Supremacy, p.175.
American two-ocean navy second to none on either ocean. Finally, Roosevelt received Congressional authority under the National Defense Act signed July 2, 1940, to prohibit the export of any item he deemed a war material. He had intimated that scrap iron would likely be embargoed upon passage of the Act, but did not include scrap iron or oil in his first order under the Act on July 2.

Under Churchill, Britain was not content to let America’s buildup and sporadic movements to bolster her flagging position continue without provocation, and Japan would help Britain so provoke the U.S.. As the Yonai cabinet was disintegrating, it attempted to increase its credibility with Japan’s militant expansionists by pressing Britain to close off its support of Chiang Kai-shek. Prodded by the Japanese army, on June 24, 1940, Japan demanded Britain close the Burma Road, the last non-Soviet overland supply line to Chiang’s forces in central China. After receiving no American support for its June 27 proposal for a joint embargo, Britain decided to acquiesce to Japan’s demands in early July, eventually signing the Burma Road Agreement on July 17, 1940. This Anglo-Japanese bargain served two important British objectives. First, because the U.S. would not engage with it in jointly defending its interests in Asia, Britain needed to placate Japan as a more aggressive government under Premier Prince Konoe Fumimaro and Foreign Minister Matsuoka was coming to power. Second, in agreeing to close the Burma Road for three months, Britain was knowingly provoking the U.S. by challenging its policy of supporting Chiang in resisting Japan’s forces on the

854 Feis, The Road to Pearl Harbor, p.74.
mainland. In buckpassing support for Chiang’s resistance to Japan in China, Churchill was goading Roosevelt into action by deliberately raising American leaders’ threat perception of Japan (i.e., a less capable China means a more powerful Japan).

Roosevelt did interpret the Burma Road closing as a non-cooperative British action and on July 17, 1940, Roosevelt used financial pressure to register his displeasure. He suggested to Sir Frederick Phillips, Britain’s ranking Treasury official in the U.S., that England be prepared to liquidate its dollar securities and investments in both Latin America and the U.S. to pay for needed U.S. imports. The next night at dinner, Secretary of War Stimson chided British Ambassador Lord Lothian for closing the Burma Road, and Lothian retorted that America’s continued shipment of aviation gasoline to Japan was no less a form of appeasement. Treasury Secretary Morgenthau also attended this dinner and latched on to the suggestion that a complete oil embargo against Japan coupled with the pre-emptive destruction of DEI oil wells and refineries suggested by Lothian would compel Japan to cease its predation of China and expansion southward, while also simultaneously bolstering the confidence of Britain and Australia.

Despite the somewhat discursive nature of this dinnertime grand strategy session, Morgenthau pressed this proposal with Roosevelt and Harold Ickes over the next few

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856. Closure of this supply route at this time was not, however, as dire as implied by the jockeying statesmen. This period coincided with the rainy season in the region and little supplies would get through anyway. See Reynolds, The Creation of the Anglo-American Alliance, pp.133-135; Peter Lowe, “Great Britain’s Assessment of Japan Before the Outbreak of the Pacific War,” in May, ed., Knowing One’s Enemies, pp.465-66; Pritchard, “Churchill, the Military and Imperial Defence,” pp.36-38; Utley, Going to War with Japan, pp.92-3; Thomson, “The Role of the Department of State,” p.100.

857. Blum, From the Morgenthau Diaries: Years of Urgency, 1938-1941, pp.170-171. In this meeting, President Roosevelt suggested that even the Queen of the Netherlands should borrow money against her properties in Washington, instead of receiving direct U.S. governmental assistance.

days, and succeeded in convincing both that this was a viable and worthwhile proposal. Consideration of a complete oil embargo against Japan was spurred in part by the tremendous increase in Japanese demand for aviation gasoline from the U.S. As noted earlier, increased Japanese demand was reported in early June, but by July 24, 1940, Japanese orders for aviation gasoline were ominously large. Secretary Stimson was alarmed by reports that the Japanese were attempting to contract for all aviation gasoline deliveries for the rest of 1940, without any concern for supplies in 1941.859 This demand resembled other periods of increased Japanese orders which occurred immediately prior to aggressive military action (e.g., late 1931 cotton imports, early 1937 scrap iron and steel imports), and touched off a rancorous debate within the administration. This parallel created enough concern regarding Japanese intentions that President Roosevelt decided to use his embargo authority on July 26, 1940. In a revised order of that day, Roosevelt curbed only the export of aviation gasoline, related lubricants and high-grade scrap iron.860

Roosevelt did not accede to the recommendations of the total economic war advocates (i.e., Morgenthau, Stimson, Ickes) and cut off all oil exports to Japan. He stepped back from this precipitant action precisely because he understood it would very likely impel Japan to attack the DEI and bring about war with the U.S. This was unacceptable timing because the U.S. was just beginning to gear up domestic production


860. Aviation grade gasoline with an octane level of 87 or higher and its additives were the specific categories embargoed. This left considerable room for export of 86 octane level gasoline and other products which Japan exploited and could modify into higher-grade fuel by adding tetraethyl lead. Additionally, the “No. 1 heavy melting iron and scrap steel” embargoed was only 15% of recent Japanese scrap iron and steel purchases from the U.S.. Feis, The Road to Pearl Harbor, p.93.
for a global two ocean war.\footnote{See Dallek, Franklin D. Roosevelt and American Foreign Policy, pp.241-3; Feis, The Road to Pearl Harbor, pp.93-4; Marshall, To Have and Have Not, pp.129-30. What is more striking about Roosevelt's restraint is the dominant public opinion in favor of ending exports to Japan. In a large Gallup poll from February 1940, for example, 75% of Americans supported an economic embargo against Japan. See Wolthus, “United States Foreign Policy Toward the Netherlands Indies,” p.101, footnote 1.} Roosevelt summarized his position in later remarks to his son Elliott: “We are, in essence and in fact...appeasing Japan. It's an ugly word, and don’t think I like it. But it’s what we’re doing. We’re appeasing Japan in order to gain the time we have to have to build a first rate navy, a first rate army.”\footnote{President Roosevelt’s conversation with his son Elliott, September 19, 1940, quoted in Wolthus, “United States Foreign Policy Toward the Netherlands Indies,” p.119.} Despite Roosevelt’s clear understanding of the purpose of U.S. actions, he allowed his key administrators to wage a pitched bureaucratic war over this issue, as he often did, in order to test the strength of contending policies while retaining ultimate decision authority. He ended their divisive debate by ensuring that oil supplies to Japan would continue despite the high-end category restrictions and the licensing system established in his July 26 order. While most scholars have noted the inadequacy of these curbs on Japan’s ability to produce aviation gasoline from U.S. supplies, few have noted the contemporaneous reduction in U.S. crude oil exports to Japan.\footnote{U.S. crude exports peaked in 1938 at 21.2 million 42-gallon barrels and declined precipitously thereafter, with 16.1 million barrels in 1939, 11.5 million barrels in 1940 and only 5.2 million in 1941. This decline is not as visible in Table 7.5 due to the necessary inclusion of fuel oil exports data which did not decline as precipitously. Assessing crude and fuel oil together is necessary to capture usable oil for Japan’s navy. For critical assessments of the temerity in U.S. export limits see Utley, Going to War with Japan, p.100; Feis, The Road to Pearl Harbor, pp.88, footnote 1.} The reductions in U.S. crude were much larger than the increases in gasoline and render a comprehensive assessment that, in fact, the U.S. was reducing Japan’s overall imports of U.S. oil products despite the large and continued increases in gasoline imports throughout the second half of 1940 and early 1941 (See Table 7.5 and 7.6).\footnote{This shift from crude to refined products also likely had a salutary effect on America’s ability to earn back the U.S. dollars supplied to Japan through gold purchases. This is the case because refined gasoline is}
Table 7.5: Japanese Imports of Crude and Fuel Oil, 1937-1941\(^a\)

<table>
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<tr>
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<th>1937</th>
<th>1938</th>
<th>1939</th>
<th>1940</th>
<th>1941</th>
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</thead>
<tbody>
<tr>
<td>From DEI to Japan in</td>
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<td>97.5</td>
<td>89.1</td>
<td>131</td>
<td>82.5</td>
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<tr>
<td>millions of gallons (% of total DEI exports)</td>
<td>(8.6%)</td>
<td>(6.4%)</td>
<td>(4.8%)</td>
<td>(7.2%)</td>
<td>(8.3%)</td>
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<tr>
<td>From U.S. to Japan in</td>
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<td>1.243.9</td>
<td>1.091.8</td>
<td>788.6</td>
<td>378</td>
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<tr>
<td>millions of gallons (% of total U.S. exports)</td>
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<td>(23.7%)</td>
<td>(21.4%)</td>
<td>(21.6%)</td>
<td>(18.8%)</td>
</tr>
<tr>
<td>From North Sakhalin in</td>
<td>70.2</td>
<td>46.3</td>
<td>42</td>
<td>42</td>
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<tr>
<td>millions of gallons</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Minimum from other</td>
<td>154.1</td>
<td>96.8</td>
<td>20.8</td>
<td>209.8</td>
<td>N/A</td>
</tr>
<tr>
<td>sources in millions of</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>gallons, including</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>British Borneo,</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Manchukuo oil shale,</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ecuador, Mexico, Persia,</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bahrain and Saudi Arabia</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

\(^a\) Japan's percentage of DEI exports are taken from Anderson because accurate DEI export statistics were not available. DEI production amounts were available and indicate for the peak export year of 1937 that only 6.2% of DEI crude production was exported to Japan. This crude figure likely includes the DEI fuel oil production amounts as was customary in DEI statistics, but if it did not the percentage would be even lower. Sakhalin island exports to Japan were fused with Japan's domestic production after 1937, but Anderson's statistic for 1939 showed 42 million gallons. Data for 1941 are from January to end of July 1941, when all shipments to Japan ceased. It is interesting to note that U.S. Naval intelligence data break out Japanese navy crude and fuel oil imports by source, either the U.S. or DEI. The DEI never supplied more than 10% of total Japanese navy imports. Data from U.S. Department of Interior, Bureau of Mines, Minerals Yearbooks, 1936-1941; Anderson, The Standard-Vacuum Oil Company, pp.223-7; Lindblad, "The Petroleum Industry in Indonesia;" ONI Reports, August 26, 1938; No. 194-39 of September 1939, File e-10-d. Register 131771, RG 38; British memorandum, "Total Imports-Japan and Manchuria," attached to Hornbeck memorandum, March 21, 1941, in Hornbeck Papers, Box 338. Folder: Petroleum.

more expensive per barrel than is crude oil, thereby exhausting more Japanese dollar holdings than if more crude were sold.
Table 7.6: Japanese Imports of Gasoline, 1937-1941

<table>
<thead>
<tr>
<th></th>
<th>1937</th>
<th>1938</th>
<th>1939</th>
<th>1940</th>
<th>1941</th>
</tr>
</thead>
<tbody>
<tr>
<td>From DEI to Japan in</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>millions of gallons</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(% of total DEI</td>
<td>10.9</td>
<td>19.9</td>
<td>5</td>
<td>10.2</td>
<td>10</td>
</tr>
<tr>
<td>exports)</td>
<td>(1.5%)</td>
<td>(2.7%)</td>
<td>(.6%)</td>
<td>(N/A)</td>
<td>(N/A)</td>
</tr>
<tr>
<td>From U.S. to Japan in</td>
<td>60.2</td>
<td>62.1</td>
<td>58</td>
<td>136</td>
<td>93.4</td>
</tr>
<tr>
<td>millions of gallons</td>
<td>(3.7%)</td>
<td>(3%)</td>
<td>(3.1%)</td>
<td>(12.9%)</td>
<td>(13.9%)</td>
</tr>
<tr>
<td>(% of total U.S.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>exports)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>From other sources,</td>
<td>29.9</td>
<td>79.7</td>
<td>71.1</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>including Romania,</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Malaya, Russia and</td>
<td></td>
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<tr>
<td>Persia</td>
<td></td>
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</tr>
</tbody>
</table>

Despite the intense domestic wrangling over unilateral American export decisions, Japanese oil demands on the DEI were even larger and, if fulfilled, they would negate the effect of any American restrictions. Because of its unsettled position among the British, Americans and Japanese, on July 26, 1940, the Dutch government assured Japan that it would “stimulate and facilitate exports to Japan with all the means at its disposal—bearing in mind Japan’s minimum demands.” In order to force greater U.S. governmental assistance, Dutch officials informed Stanvac corporate officers that they would be responsible for fulfilling 75% of Japan’s total demand from the DEI with the

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865. In response to the American restrictions of late July, the Japanese doubled their oil demands on the Dutch.
866. Dutch note to the Japanese Foreign Office, July 26, 1940, quoted in Wolthius, “United States Foreign Policy Toward the Netherlands Indies,” p.108.
remaining 25% to be supplied by Royal Dutch facilities.\textsuperscript{867} This burden shifting to the American company was even more glaring considering that Stanvac production in the DEI was no more than 30% of total DEI production.\textsuperscript{868} Somewhat fortuitously, the Dutch government informed Japan that it did not itself control the oil exports from the DEI. As a result, Japan would have to negotiate directly with the oil companies for increased supplies.\textsuperscript{869} The Dutch would honor their commitment only to “stimulate and facilitate” increased oil flows to Japan by hosting the negotiations among the companies and a Japanese delegation. The Dutch government’s generalized commitment to help Japan increase its oil supplies coupled with its buckpassing of responsibility for the actual supplies helped cement the need for a coordinated Anglo-American-Dutch oil supply strategy \textit{vis a vis} Japan.\textsuperscript{870} This task would be undertaken by Hornbeck beginning in mid-August 1940.

Roosevelt’s administration had several important considerations that conditioned the decision to remain the chief supplier of oil products to Japan, while overseeing a shift in the makeup and source countries of those products. First, Roosevelt continued these supplies because official British and Dutch reaction to the possibility of a U.S. cutoff was not favorable.\textsuperscript{871} Ambassador Lothian’s dinner stratagem did not appeal to the Foreign

\textsuperscript{867} Ibid., p.109-110.
\textsuperscript{868} Lindblad, “The Petroleum Industry in Indonesia Before the Second World War,” p.56.
\textsuperscript{869} Van Mook, \textit{The Netherlands Indies and Japan}, p.44. This was of course the Dutch strategy they had planned to invoke at least as early as 1924. See article by Dr. Feuillateau de Bruyn, “Our Petroleum Industry and the International Position of Netherlands India,” enclosed in letter from Charles Hoover, American Consul, Batavia to Secretary of State, September 23, 1924, file 856d.6363/445, RG 59.
\textsuperscript{870} The U.S. was fully aware of the pressure that was being put on the Dutch by the Japanese. Japan explained clearly to the Dutch that due to their desire to be free of U.S. supplies, either they would receive increased supplies from the DEI or they would occupy the DEI. In February 1939, the Japanese ambassador in London explained this to Lord Bearsted, a director of Royal Dutch Shell, and began the Japanese demands for a long-term supply agreement with the DEI. See ONI Report Serial No. R-37, File No. 602-1000, February 6, 1939, File e-10-d, Register 131771, RG 38.
Office or Churchill as preparations were afoot for the Battle for Britain which began on August 8, 1940. Despite his earlier suggestion of a joint embargo, Churchill did not wish to have the U.S. unnecessarily cause Japan to attack its possessions in Asia while it simultaneously fought Germany over its own soil. Second, there was a keen U.S. self-interest in continuing U.S.-DEI trade. Because a critical part of the U.S. war production effort required continued imports from the DEI (e.g., rubber exports for the 50,000 airplanes’ tires), Roosevelt was not willing to sacrifice this trade and the larger American buildup prematurely to an American-induced Japanese occupation of the DEI. Finally, the pressured position of the DEI required a more subtle approach to constraining Japan’s demands on both the U.S. and the DEI. The U.S. did not want to overly influence Japan into a full-scale southern war strategy when Japan might still decide to expand northward against the Soviet Union. This factor was predominant given the absence of any firm Anglo-Dutch-American security understanding and the pending negotiations regarding renewal of the Burma Road agreement and DEI oil supplies for Japan.

By late August 1940, Hornbeck had begun the working relationship with the British to coordinate the oil companies’ negotiations with Japan which commenced in Batavia on September 12, 1940. This cooperative step was a product of better relations

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872. By 1940 the U.S. was taking 33% of total DEI exports, up from 20% in 1939. In tin the U.S. took 64% of DEI exports, and in rubber as noted earlier the U.S. was buying the largest portion (e.g., for the first 10 months of 1941 the U.S. took 339,062 of the total 531,064 metric tons produced). See Wolthius, “United States Foreign Policy towards the Netherlands Indies,” p. 17, footnote 8. Without citing Wolthius, Marshall’s recent book re-clarifies this compelling reason to delay the Pacific war as long as possible. See Marshall, To Have and Have Not.

873. Even at this point, Britain had not made any formal commitment to the defense of the DEI, nor had Anglo-American negotiations led to any understandings in broad principles or operational responsibilities in the Pacific. This stands in some contrast with Roosevelt’s willingness to begin aggressive “neutrality patrols” in the Atlantic to support Britain. See Leutze, Bargaining for Supremacy, pp.263-265; Reynolds, The Creation of the Anglo-American Alliance, pp.136-144; Prichard, “Churchill, the Military and Imperial Defence,” pp. 37-38; Wolthius, “United States Foreign Policy towards the Netherlands Indies,” pp.113-121,150-152.
emerging between Churchill and Roosevelt, whose joint commitment was to see to it that the Burma Road re-opened and was made acceptable to the Japanese by delaying the successful conclusion of the DEI talks as long as possible (i.e., holding out the carrot of DEI resources to keep Japan from using its stick over continued China assistance). With this understanding, the link between Chinese resistance and Japanese expansion southward was made an explicit part of Anglo-American efforts to placate and restrain Japan. Through delayed fulfillment of Japan’s desires, the U.S. sought to buy time for its own re-armament and extension of tangible and psychological support for Britain and China. Toward this latter end, on September 2, 1940, the U.S. signed the agreement with Britain exchanging 50 U.S. destroyers for rights to British bases in the Western hemisphere. Eleven days later, the U.S. extended $25 million dollars to Chiang’s regime through the U.S. Export-Import Bank, enabling his forces to continue their arms purchases. However, neither of these developments nor the promise of greater DEI oil could stem Japan’s opportunistic military advance against French Indochina or its consummation of the Tripartite Pact with Germany and Italy on September 27, 1940.

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875. Blum, From the Morgenthau Diaries: Years of Urgency, pp.356-7. By December 1940, the U.S. was increasing its shipments to China and contemplated the diversion of 500 new Flying Fortress bombers to Chiang’s forces if he would commit to attack Japanese cities. President Roosevelt enthusiastically supported this idea, calling it “wonderful,” but it foundered on Britain’s needs. Still, some 100 fighter aircraft were sent to China under a new $100 million dollar loan of November 30, 1940, and the Flying Tiger program under Colonel Claire Chennault was begun in April 1941. See Xu, “The Eagle and the Dragon’s War Wings.” pp.282-90; Michael Schaller, “American Air Strategy in China, 1939-1941: the Origins of Clandestine Air Warfare,” American Quarterly, Vol. 28, (1976), pp.8-11; Dallek, Franklin D. Roosevelt and American Foreign Policy, pp.269-71.
In response to Japan’s quick victory over French forces in northern French Indochina and its formalizing the alliance with Germany against the U.S. and Britain, the U.S. expanded its scrap iron and steel embargo on Japan making it total on September 26, 1940.\textsuperscript{876} The U.S. accurately perceived the alliance as being aimed partly at it, increasing America’s threat perception of Japan and uncertainty regarding the pace of its likely expansion.\textsuperscript{877} As a result of this alliance of opportunistic predators, the U.S. sought both to negate the advantages of the Pact and create increased economic difficulties for Japan. On this latter point, Herbert Feis contends the complete iron and steel embargo caused great diversion of resources in Japan, exacerbated the inefficiencies referred to earlier in Japan’s steel-making industry and yielded Japan one-fifth less steel-making capacity during 1941. A significant part of this resource diversion and inefficiency can be attributed to Japan’s reliance on the prior supply relationship with the U.S. Japan’s failure to build larger more efficient blast furnaces, for example, was acceptable when U.S. exports flowed unimpeded. But, when these ended the shortages caused greater than anticipated production inefficiencies and cascading production slow downs. This effect is a direct consequence of Japan’s prior trade dependency and may help explain why the U.S. was willing to continue it up to this point. It was more important, however, for the U.S. to supply Japan’s scrap iron needs because other source countries in southeast Asia

\textsuperscript{876} Feis and Barnhart have contended the purpose and effect of the total embargo were great, while Utley holds it was largely a domestic measure taken at an internationally opportune time. See Feis, The Road to Pearl Harbor, pp. 107-109; Barnhart, Japan Prepares for Total War, p. 196; Utley, Going to War with Japan, pp. 106-107.

were decreasing their supplies to Japan. Australia's iron ore and scrap exports to Japan and toleration of a Japanese firm in Australia conducting operations ended in May 1938 with a total embargo and suspension of the firm's business. This increased the importance of U.S.-controlled supplies in the Philippines and the mainland of the U.S..

Japan sought the Tripartite Pact to improve its relations with the Soviet Union, in part to be able to achieve restored trade in iron and oil benefits comparable to what Germany had received in the Nazi-Soviet deal. Japan believed the continuous stream of German entreaties regarding its ability to effect such an improvement, which might also lessen Russian support for Chiang's forces. In response, Secretaries Morgenthau and Stimson attempted to improve relations with the Soviets in the aftermath of the Pact, but these efforts were generally rejected by Secretary Hull despite their clear potential to disrupt further Japanese ventures south. In contrast, Britain desired even greater U.S. shows of support in Asia, as Churchill yet again requested U.S. naval forces to visit Singapore and accelerated joint planning talks. Roosevelt continued to resist these overtures in October despite Churchill's argument that a show of U.S. naval power there would ensure Japanese compliance with the re-opening of the Burma Road in late October 1940. Unable to achieve increased third country pressure against Japan and unwilling to go as far as Britain wanted, the U.S., under Hornbeck's guidance, ensured that Japan's negotiations in the DEI would prove a success on paper but shallow on the sea.

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878. See Frei, Japan's Southward Advance and Australia, pp.153-4.
880. Blum, From the Morgenthau Diaries: Years of Urgency, pp.359-62. Hornbeck had advised this course of action in June 1940 and probably communicated his rationale for doing so to Stimson, his long-time correspondent. See memorandum from Hornbeck to Undersecretary of State Welles, June 21, 1940, in Hornbeck Papers, Box 396, Folder: Soviet Union: Soviet-American Relations.
Hombeck's role in achieving a hollow outcome in Japan's DEI negotiations began prior to the arrival of the Japanese delegation there on September 12, 1940. Before the negotiations, the Dutch government had attempted to place the onus of supply fulfillment on the American companies in the DEI, and both British government and Royal Dutch company officials declared that Japan's increasing demands would have to be fulfilled, including Japan's ever larger aviation gasoline demands. Hombeck remonstrated the British government officials and business executives, refocusing them by stating: "that there was no need and no advantage to be gained by assuming a defeatist attitude...if the negotiators go into the negotiations in such a frame of mind they will be in a hopeless position, as the Japanese would of course take the fullest advantage of that situation." Hombeck then set the terms of the negotiations by directing the company officials to approach the talks as "business" negotiations, bargaining hard with the Japanese at every opportunity as to contract duration and amounts to be sent to Japan. Both Britain's key petroleum industry representative, Sir Andrew Agnew of Royal Dutch Shell, and Ambassador Lothian agreed with this approach aligning official British policy behind Hornbeck's suggestions.

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881. Stanley Hornbeck, quoted in Shinjiro Nagaoka, "Economic Demands on the Dutch East Indies." in Morley, ed., Fateful Choice, p.142. Following one British participant's assessment, Anderson takes the position that Hornbeck reacted "violently" to these totally compliant initial corporate and British positions, and thereafter cut himself out of the decision making in large part. This assessment is contradicted in his own analysis, which demonstrates Hornbeck's centrality in managing the negotiations and passing along the daily communications to Hull and Far East Division Chief, Maxwell Hamilton. Compare Anderson, The Standard-Vacuum Oil Company, pp.147-8 with p.149.

882. Nagaoka, "Economic Demands on the Dutch East Indies," pp.142-3; Anderson, The Standard-Vacuum Oil Company, p.151. To delay Japanese action, Hombeck did distance the U.S. government from the direct negotiations. He went so far as to claim "at no stage did it (the U.S. government) express approval or disapproval, nor did it in any way interpose" in the actual negotiations. This may be true, but the pre-negotiation remonstration had that effect, as did the post negotiation "suggestion" that tankers not be supplied to fulfill the deal's terms. As with prior corporate guidance, Hombeck did not want the U.S. government directly tied to the outcome because Japan would have greater cause for direct grievance to it.
The united Anglo-American position assured Dutch officials that they need not fear Japanese aggression due to lengthy and potentially unsatisfying talks, and allowed them to neatly sidestep direct involvement in the negotiations with Japan. Instead of direct Dutch government involvement, the colonial government of the NEI refused to negotiate with the Japanese on behalf of Stanvac and Royal Dutch Shell, forcing the Japanese to bargain directly with these two companies. However, the U.S. government controlled these negotiations as Herbert Feis neatly summarized: "Secretly guided, the companies dallied with the unwelcome customer. They offered about half of what was asked; and in that half there was to be very little aviation gasoline...Washington had tutored the oil companies."883 The negotiations were drawn out over an extended period of time as the U.S., Britain and the Dutch desired, and were finally completed on November 12, 1940. Although Japan had achieved commitments to receive increased oil products, actual receipt of these and U.S. products was made problematic through joint Anglo-American efforts to remove tankers from all of Japan's oil trade (i.e., from the DEI, U.S., Mexican, and Middle Eastern trade).

With great foresight and following Hornbeck's instructions to bargain hard, the corporate negotiators had made the terms of their contract such that Japan would have to provide its own tankers to take actual receipt of DEI oil products. In much of the previous trade, the oil companies made the deliveries to Japan in their own tankers. In early January 1941, the British renewed their proposal from November 1940, to have

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883 Feis, *The Road to Pearl Harbor*, p.130.

436
foreign tankers withdraw from the Japanese trade. The U.S. now readily accepted this idea and, by early February 1941, ordered all American-owned tankers withdrawn from the trade, with the effect that “by late spring there were almost no non-Japanese tankers left in the trade.” Similarly alarmed by Japan’s acquisition of storage tanks and portable drums of gasoline, the U.S. placed an embargo on these items in February 1941. These measures were accomplished through informal communication with the companies involved, thus avoiding the negative political consequences that might have accompanied them had Japan been fully aware of the government deception causing Japan to receive roughly only half of its contracted oil products.

884 Previously Hornbeck had proposed a more devious method of perverting Japan’s aviation gasoline autonomy efforts. Hornbeck suggested that the embargo on aviation gasoline refinery construction in Japan be lifted. Instead, the U.S. should allow the building of the expensive plants, but withhold “the catalytic agents which go into the production of aviation gasoline and thus render the plants practically valueless to the Japanese.” He recommended this approach because it feigned cooperation, forestalling Japanese aggression southward, and would earn back large amounts of Japan’s dollar holdings without actually letting it acquire aviation gas that they were presently purchasing and stockpiling. See Hornbeck memorandum, December 28, 1940, in Hornbeck Papers, Box 338, Folder: Petroleum.

885 Anderson, The Standard-Vacuum Oil Company, p.163; Feis, The Road to Pearl Harbor, pp.158-9. Prior to the introduction of the tanker shortage, Japanese officials expressed satisfaction with the Batavia Agreement. In January 1941, Foreign Minister Matsuoka exclaimed Japan “had obtained more oil than we had expected.” This assessment bears repeating because it came from the key foreign policy official pushing the formal inclusion of the DEI in the Greater East Asia Co-prosperity Sphere. This statement also contradicts Copeland’s contention that negative expectations of future trade cause conflict as Japan stepped up its planning against the U.S. and threats of DEI conquest precisely when its future expectations were positive. See Nagaoka, “Economic Demands on the Dutch East Indies,” pp.146.

886 From the contract date of November 1, 1940 through the October 31, 1941 end of the contract term, only 430,613 long tons of crude oil was delivered against the agreed amount of 660,000 long tons (65%). For refined products 237,430 long tons were delivered against an agreed amount of 646,500 long tons (37%). The total contract amount of 1,306,500 long tons of oil products was sharply lower than Japan’s peak negotiating demand of 3,750,000 long tons, suggesting a successful “business” negotiation circumscribed by Hornbeck. Interesting but possibly not surprisingly, Stanvac withheld more of its allotted deliveries of crude than did Royal Dutch Shell. It is odd in retrospect that Japan did not plan better to secure the tanker traffic between the DEI and Japan, as this Anglo-American tanker gap should have helped incent. For a related observation see Evans and Peattie, Kaigun, pp.408-9. For DEI delivery limitations see Batavia Agreement summary table, in Hornbeck Papers, Box 339, Folder: Japan and Netherlands East Indies; Wolthus, “United States Foreign Policy towards the Netherlands Indies,” p.150. These figures differ only marginally from Anderson’s which do not mention each company’s fulfillment and add lubrication crude with the crude and fuel oil category. See Anderson, The Standard-Vacuum Oil Company, p.156.
The tanker shortage and storage embargos were intended to curb Japan’s accumulation of large and portable oil stockpiles. These autonomy-enhancing capabilities and their relation to Japan’s wartime operational capacity came under increasing Anglo-American review in early 1941. Both countries were concerned about supplying Japan in excess of its consumption and thereby lengthening its operational range in the event of a political decision to end the oil trade from the DEI and the U.S.. Intelligence assessment of Japanese oil reserves, consumption and trade demands that affected net stockpiles became the focus of Anglo-American debate in March and April, 1941. U.S. estimates of Japanese reserves at this juncture held that Japan was beginning to rebuild its overall reserves which had been roughly stagnant due to increased consumption from 1937 forward. The best U.S. estimate from the Office of Naval Intelligence held total Japanese oil products stocks (i.e., crude, fuel oil, gasoline, lubricants etc.) on January 1, 1941 to be 10 million long tons, or between 70-75 million 42-gallon barrels.

U.S. intelligence deduced from this that Japan could sustain military operations for approximately 18 months drawing exclusively on its own stocks with no trade. British estimates were less than U.S. estimates, conjecturing that Japan had accumulated 39.5 million 42-gallon barrels, enough stocks to sustain 9 months of military

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887. For example, U.S. Naval Intelligence held that Japanese navy crude, fuel oil and gasoline in storage did not increase at all from 1937 to 1938, as operations in China accelerated consumption. See ONI Report No. 194-39, September 1939, File e-10-d, Register 131771, RG 38. However, by late by March 1941, ONI estimates concluded that Japan’s stocks were “already dangerously high.” See memorandum possibly prepared by Charles Yost, Division of Controls, U.S. State department, “Control of Japanese Supplies of Petroleum and Petroleum Products,” p.15, in Hornbeck Papers, Box 338, Folder: Petroleum, hereafter cited as “Control Memorandum.”

888. Control Memorandum, pp. 15,18; Feis, The Road to Pearl Harbor, pp.159, footnote 14.
operations.\textsuperscript{889} In contrast, actual Japanese stocks were 48.9 million 42-gallon barrels, representing a decline from peak stocks in 1939 of 51.4 million 42-gallon barrels.\textsuperscript{890} The decline in navy fuel oil stockpiles was more dramatic, from 29.6 million barrels in 1937 to 22.7 million barrels in July 1941. But, the navy built up its aviation gasoline stockpiles adding: 104,000 tons in 1936; 99,000 tons in 1937; 97,000 tons in 1938; 150,000 tons in 1940; and 371,000 tons in 1941.\textsuperscript{891} Although it can not be evaluated for intent, it can be argued that decreased crude and fuel oil exports from the U.S. would have restricted Japan's fleet and aircraft carriers from full operational capacity over the course of the war even though the aircraft aboard had more than enough gasoline.

Both British and American estimates held that Japan's total stockpiles were increasing in early 1941 and the exchange of these intelligence assessments led to a harmonization of some key assumptions that would condition trade and diplomatic strategies going forward.\textsuperscript{892} First, accepting Japanese reserves to likely provide them a minimum of one year's full-scale military operations absent trade, Hombeck and the

\textsuperscript{890}. Ibid., p.230. Anderson's statistics are drawn from the postwar U.S. Strategic Bombing Survey, which used Japan's Joint Army-Navy Oil Committee statistics. These statistics have been called into serious question in recent scholarship. Evans and Peattie hold "no definitive figures on stockpiles, consumption and so forth are available because of government secrecy, interservice rivalry and the wholesale destruction of documents at the end of the Pacific War." See Evans and Peattie, \textit{Kairiun}, p.593, footnote 40.
\textsuperscript{891}. According to the postwar strategic bombing survey, aviation gasoline stocks were accumulated through domestic production and imports in roughly equal amounts. Japan's stocks of aviation gasoline increased from 842,000 barrels in April 1939 to 4,254,000 barrels on the eve of Pearl Harbor. See U.S.S.B.S., \textit{Oil in Japan's War, Appendix}, pp.19,25. One ton of aviation fuel equals 360 gallons or approximately 8.6 of the 42-gallon barrels. See U.S.S.B.S., \textit{The Effects of Strategic Bombing on Japan's War Economy}, p.139: Evans and Peattie, \textit{Kairiun}, p.594, footnote 44.
\textsuperscript{892}. It is odd, however, that Britain's own assessment of Japanese supplies showed that total Japanese oil imports were largest in 1938 at 43.7 million barrels. For 1940, British intelligence held Japanese imports to be 37 million barrels. If imports were declining and operations still taking larger amounts of oil, how could they conclude stocks were increasing? British estimates of Japanese consumption were larger than U.S. ONI estimates, and this raises serious questions regarding British intent in advising that Japan was improving its oil autonomy position. See Control Memorandum, p.21; British memorandum, "Total Imports-Japan and Manchuria," attached to Hornbeck memorandum, March 21, 1941, in Hornbeck Papers, Box 338, Folder: Petroleum.
British, who were prodding for increased restrictions if not a total embargo, formalized their planning to destroy the oil production, refining and transportation equipment of the DEI. Hornbeck assumed that these measures would “make it impossible for Japan to obtain oil from the Netherlands East Indies for at least a year after their occupation.” This assumption made U.S. war planning for delayed action in the Pacific all the more palatable. If Japan would use up its stocks in the first year of the war and have no alternatives due to DEI destruction, U.S. plans to “abandon” the Pacific during this period were rational for American planners. To the British, however, this delay and abandonment would mean the loss of their colonies and future influence in Southeast Asia. Nonetheless, both Britain and the U.S. were intent on supplying Japan only to fulfill current consumption.

Second, both countries now saw that oil supplies from other countries were no longer merely a diversionary feature of containing Japan’s quest for oil. Japanese oil demands through Thailand and from Mexico, Peru and the Middle East provided opportunities for joint Anglo-American oil containment of Japan. Britain, in particular, was suffering from Mexican government expropriation of its assets there in 1938 and lobbied the U.S. for increased pressure against Mexico, citing Mexican oil exports to Germany and Japan as reason for action. U.S. intelligence had followed

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893. See Hornbeck memorandum to Secretary of State, January 11, 1941, p.5, in Hornbeck Papers, Box 338, Folder: Petroleum.
894. Hornbeck memorandum to Secretary of State, “Observations on Relation Between Restrictions on Japanese Trade and Japan’s Southward Advance,” April 1, 1941, p.12, in Hornbeck Papers, Box 249, Folder: Japan: Restrictions on Trade Of.
895. ONI compared U.S. and British estimates, and determined “the amount of United States exports which can be permitted without exceeding Japanese average consumption.” They figured this to be 12,773,000 barrels of crude and refined products. See Control Memorandum, pp.15-16,21.
896. See British memorandum recommending stoppage of U.S. and DEI oil to Thailand and memorandum of conversation regarding oil contracts for Thailand between Alger Hiss, Hornbeck’s assistant, and James Moffett, Chairman of the Texas Oil Company, February 21, 1941, in Hornbeck Papers, Box 339, Folder: Japan and Netherlands East India.
Japan's efforts to obtain greater amounts of Mexican oil, including an effort to clandestinely build a pipeline to Mazatlan, and stepped in to arrange a settlement which concluded in late 1941. On the subject of oil from Persia, Britain offered to risk its relations with the Shah in order to end the exports from there to Japan which were only less than contracted for at present due to the tanker shortage. Britain claimed that the Shah's greed was being "fully exploited by the Japanese," forcing Britain to make large royalty payments in advance to the Shah to retain the concession.

All of these efforts led to Japan's increased reliance on American oil resources but did not yield a resolution to the internal U.S. debate as to when and with what effect an oil embargo should be applied. Hornbeck advocated early application of the oil embargo weapon, noting that Japan's decision to go or not go southward depended only upon: "the amount of armed opposition or penalty which she fears or does not fear that she will encounter if she so does. Japan will not be pushed into such adventuring by embargoes—provided the embargoes are skillfully and not too drastically applied."

Hornbeck stressed that the most important policy outcome was the continued resistance of Chiang's forces which tied down Japan's army and naval air forces that might otherwise be used in the southward advance. He held a Japanese attack southward was preferable to an all out offensive against China because moving south prior to conquering China would "embroil [Japan] with new East Asiatic populations and (at least in economic warfare) with new Western sovereignties (perhaps with the United States) and

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she might lose both her present position in China and the objectives of her new effort."

Hombeck summarized U.S. supply of Japan tersely:

we do this in the hope that so long as we do it Japan will not move southward and in the fear that if we do not do it Japan will move southward. The hope is tenuous. The fear is a fear of the less of two possible evils in forgetfulness of or disregard of the greater of those possible evils. The fact, as distinguished from hopes and fears, is that Japan is getting and is piling up reserves of aviation gasoline which she does not need unless she is going further southward or is going westward more intensively or is going to fight the United States. I submit that although there would be risks in imposing embargoes, there are also risks in not imposing them, and that the latter risks are greater so far as the interests of the United States are concerned.899

Hombeck challenged the logic of supply appeasement by noting that “the more the stock piles are increased the less will be the influence—toward restraint—of these material considerations.”900 This argument was welcomed by the British who were trying to bring the U.S. into the war and particularly to seeing the wisdom of defending the Singapore base and thus the surrounding areas’ supplies to both Britain and the U.S.. Hornbeck felt compelled to couch the argument for assisting Britain in southeast Asia in terms the State department’s Europe-first proponents would accept. Therefore, the U.S. should help defend southeast Asia in order to support Britain’s ability to defeat Germany, rather than as a purely U.S. strategy of confronting and deterring Japan from a southward advance. This was also necessary to deflect criticism which cited Japan’s warning to the U.S. that a U.S. force presence defending Britain’s base at Singapore might be construed

899. All quotes from Hornbeck memorandum to Secretary of State, January 23, 1941, in Hombeck Papers, Box 338, Folder: Petroleum.
900. Hornbeck memorandum to Secretary of State, “Observations on Relation Between Restrictions on Japanese Trade and Japan’s Southward Advance,” April 1, 1941, p.17, in Hornbeck Papers, Box 249, Folder: Japan: Restrictions on Trade Of.
as a *causus belli* in the Pacific.\(^901\) Because of these domestic and foreign niceties, Roosevelt ensured the strictest secrecy during the American-British-Canadian (ABC) talks from January 29 to March 29, 1941.

During the negotiations leading up to the ABC-1 agreement, the U.S. declared that it would not acquiesce to British grand strategy and accept Britain’s preference for the bulk of the U.S. Fleet to remain in the Pacific to deter and if necessary defend southeast Asia from Japanese attack. Instead, the U.S. bargained hard for a predominant role in operations in the Atlantic under the first priority of the strategic partnership to defeat Germany. British negotiators did not approve of this American willingness to “give up the entire Far East in the early stages of the war, confident that it could be retaken later.”\(^902\) Nonetheless, Churchill directed his negotiators to accept the American commitments such as they were because he believed “once war is declared events will draw them [U.S.] naturally into a forward policy for which we should not now press unduely.”\(^903\) America’s Lend-Lease Act had just passed the U.S. Senate on March 8, 1941, and Churchill accurately gauged that the timing of America’s decision to enter the war would not be positively affected by British pressure or complaints.

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\(^{901}\) Wolthus, “United States Foreign Policy towards the Netherlands Indies,” p.149.

\(^{902}\) Leutze, *Bargaining for Supremacy*, p.231. The sacrifice of the Philippines was explicitly accepted as unavoidable by U.S. negotiators. Roosevelt himself recognized the indefensible position of the Philippines in 1923. He wrote, “if our naval experts a decade ago doubted whether we could hold the Philippines with a fleet more than as powerful as that of Japan, what would they say today, when we have a fleet rated as only five to three with that of Japan?” Franklin D. Roosevelt, “Shall We Trust Japan,” *ASIA*, Vol. 23, (July 1923), p.528. By the middle of 1941 the fleet balance was at least one to one, with Japan likely holding the advantage with one-fifth of the U.S. Fleet withdrawn to the Atlantic as per ABC-1.

7.7 Japan Secures its Northern Front, Expands South and Earns a U.S. Embargo

Throughout the fall of 1940 and spring of 1941 Japan cast an uneasy eye on the growing Anglo-American coordination, particularly when this cooperation came at Japan’s expense (e.g., re-opening the Burma Road and increasing Chiang’s material aid). Japan’s constant fear of strategic encirclement was increasing, and this was a principle reason for concluding the Tripartite Pact with Germany and Italy. The prospect of improved Soviet-Japanese relations were pivotal to Japan’s leaders agreeing to this Pact and the offer of German offices to affect such an improvement made the Pact acceptable to Japan’s leaders. Since the failure at Nomonhan in September 1939, Japan’s leaders had been seeking a way out of their strategic encirclement dilemma by potential and actually hostile forces in the Soviet Union, China, Britain and the U.S.. Rapprochement with the Soviet Union and its neutralization offered a two part solution to Japan’s resource and military over-extension dilemma.

First, Japan wanted to improve its position in the war against China and as noted earlier Soviet assistance to China was considerable (e.g., military aircraft). Therefore, Japan sought a commitment that the Soviets would stop assistance to Chiang. Early in the negotiations, they received such a tentative commitment from Foreign Minister Molotov declaring that the Soviet Union “had no weapons to spare for other countries.” According to Molotov, the only counterweight to greater Soviet commitments not to hinder Japan’s China war was stimulating a negative reaction from

904 Feis details this nicely. See Feis, The Road to Pearl Harbor, p.128.

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the U.S.. Although the Soviet Union welcomed the prospect of a Japanese-American war, they could not appear to be too greatly facilitating it by giving Japan complete security in the north and a freer hand against China.⁹⁰⁷ Thus, a “neutrality” pact held great appeal for the Soviets.

Second, Japan hoped to improve its waning oil relationship with the Soviet Union, thereby giving it increased supplies from a more proximate location. This was increasing in importance as other supply sources and transport were becoming unavailable and were only likely to become even less available in the future (e.g., Persian, Mexican oil). In March 1941, Japan was failing in its efforts to obtain ownership of DEI oil resources, not just trade rights that would fail to materialize, and was therefore desirous of improving its deteriorating oil supply relations.⁹⁰⁸ Direct oil exports from Soviet territory had ceased by 1938 and the amounts Japan was getting out of N. Sakhalin had steadily decreased through early 1941. In 1937, Japan received 89.7 million gallons of crude oil from the Soviet Union including Sakhalin, but in 1940 only 42 million gallons were received by Japan.⁹⁰⁹ These were small amounts in general but could be better ensured and possibly increased in the future. More importantly, they could form a local pillar in Japan’s wartime supply planning and were therefore of primary interest in Japan’s negotiating position with the Soviet Union.

⁹⁰⁷ A telegram dated June 22, 1940 from the People’s Commissariat for Foreign Affairs in Moscow to Soviet Ambassadors in Japan and China held: “we want to avoid treaties that would give the United States the impression that we are entering into close political cooperation with Japan. On the other hand, we must take positive measures to give Japan a feeling of security in the north and so stimulate their determination to advance in the south...we have already reached an agreement with the American government regarding our policies vis a vis Japan.” Ibid., pp.310-11, footnote 65.


Stalin bargained hard with Foreign Minister Matsuoka declaring that the oil and coal concessions in North Sakhalin would have to be "liquidated," and he first offered to buy South Sakhalin from the Japanese. On his return train trip from Germany in early April 1941, Matsuoka finalized the agreement with Molotov and Stalin. In it, Japan obtained only a pledge to conclude a commercial agreement and negotiate a new accord governing Sakhalin oil resources over the next few months. Despite these shortcomings, Matsuoka signed the Japanese-Soviet Neutrality Pact on April 13, 1941. Upon his return to Japan, Matsuoka did his best to undermine Premier Konoe's unofficial overtures to the U.S. for a pan-Pacific settlement and prodded the army-navy decision makers in the Liaison conferences of April 22 to move on their plans for the southern advance.

Partly in response to the Japanese efforts to secure their northern front in preparation for southern advancement, the U.S. held the first Anglo-American-Dutch joint operational planning talks beginning on April 21, 1941, and announced another loan to Chiang for $50 million dollars on April 25. Although no formal defense commitments were made in the final ABD-I joint document of April 27, the talks did facilitate joint operational planning and affirmed the importance of the Singapore base to the budding military allies.

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910. This was stronger position than Foreign Minister Molotov took initially when he declared that "the Soviet government is prepared to supply Japan with oil from northern Sakhalin, for a five-year period." Hosoya, "The Japanese-Soviet Neutrality Pact," p.45.
912. This was, of course, a concession to British interests which was immediately challenged by General Marshall and Admiral Stark. Leutze, Bargaining for Supremacy, pp.264-6; Hosoya, "The Japanese-Soviet Neutrality Pact," p.85.
The Japanese assumed that these talks bore more joint war planning fruit than they in fact did, and Matsuoka began to issue more bellicose statements about American naval convoys in the Atlantic and America’s responsibility to help Japan acquire control of production of vital materials in southeast Asia. The U.S. resisted these demands as did the Dutch who were engaged in still more direct negotiations with Japan. In early June 1941, the Dutch issued a formal denial of Japanese demands ending their negotiations and the U.S. began its fateful reinforcement of army forces in the Philippines and curtailment of oil exports from the East Coast and Gulf of Mexico. The ceasing of Atlantic area oil shipments to Japan was publicly announced on June 20, 1941, and was the subject of much bureaucratic wrangling with Harold Ickes, now domestic Petroleum Coordinator, arguing for a full oil embargo on Japan. Roosevelt lectured Ickes on June 18, that oil shipments to Japan were not merely domestic economic matters; rather, they were the province of foreign policy and grand strategy under the control of only the President and the Secretary of State. He framed the issue for Ickes by noting that a premature full oil embargo would “tip the delicate scales” and force Japan to attack either the Soviet Union or the DEI. In this as in all prior decisions regarding oil to Japan (e.g., aviation gas embargo of July 1940), Roosevelt demonstrated his complete understanding of the consequences of a full U.S. oil embargo.

914 Wolthius, “United States Foreign Policy towards the Netherlands Indies,” pp.167-9, 187, 206-7; Morton, The War in the Pacific, pp.98-100. By December 1941, 8,563 more U.S. soldiers had been added to the Philippines forces, bringing American forces there to 31,095. Given U.S. strategy of sacrificing the Philippines and implicitly much of southeast Asia in the early stages of any conflict, this U.S. army-placating decision to add to the Philippines is an example of sub-optimal U.S. strategic decision making due to army-navy logrolling. This is particularly evident with the U.S. transfer of approximately one-fifth of the Fleet from the Pacific to the Atlantic on May 6, 1940.
915 President Roosevelt to Harold Ickes, June 18, 1941, quoted in Dallek, Franklin D. Roosevelt and American Foreign Policy, p.273.
At this same time, Japan was also hardening its diplomatic and military strategies, with the army and navy agreeing only to renegotiate better oil terms under neutrality with the Soviets in the event of any German-Russian war. They decided not to reverse the southern advance strategy whose next operation would be to secure the air and naval bases of southern Indochina. These plans were thrown into sharp debate with the surprise German attack on the Soviet Union beginning June 22, 1941. Germany’s attack and formal request that Japan intervene against the Soviet Union forced Japan’s leaders to re-evaluate their strategies. Foreign Minister Matsuoka represented those Japanese leaders, predominantly army officers, opposed to the Soviet Union but who had pushed for southern advance in recent years. He reversed course and called for Japan to attack the Soviet Union, noting that if it also would mean war with the U.S. and Britain that would have to be accepted. He also made this appeal directly to the emperor, but was rebuffed in his efforts to re-orient Japan’s expansion in repeated Liaison Conferences beginning on June 25, 1941. In the first of these conferences, Navy Minister Oikawa told Matsuoka: “The Navy is confident about a war against the United States and Britain, but not confident about a war against the United States, Britain, and the Soviet Union...don’t tell us to strike at Soviet Russia and also tell us to go south. The Navy doesn’t want the Soviet Union stirred up.”


917. Navy Minister Oikawa, a former staunch supporter of the Tripartite Pact, at the June 25, 1941 Liaison Conference, quoted in Nobutaka Ike, Japan’s Decision for War: Records of the 1941 Policy Conferences, (Stanford, CA: Stanford University Press, 1967), p.59. This conference was convened to consider Japan’s response to both the German attack and the U.S. Atlantic coast oil embargo. See Wolthius, “United States Foreign Policy towards the Netherlands Indies,” p.207, footnote 19.
Matsuoka and his faction were defeated in their policy recommendations at the key Imperial Conference of July 2, 1941. Instead of joining their erstwhile German ally in yet another of its strategic reversals, Japan’s leaders chose to proceed south to occupy southern Indochina. For the first time, they openly acknowledged that this course of action risked war with the U.S. and Britain, but declared that the “southern area” resources were necessary to the empire’s “self-preservation and self-defense.” In order to secure these resource needs, “the Empire will not hesitate to engage in war with the United States and Britain.”918 This decision to occupy southern Indochina was also driven by the desire to close the Burma Road through greater pressure from Thailand and Indochina. It also would position Japanese forces for increased leverage over the DEI in any future contingency (i.e., renewed negotiations or invasion). These motivations and the contending positions in the internal debate were clear to the U.S. Most importantly, President Roosevelt was anxiously awaiting the outcome of this internal Japanese debate as he confided to Harold Ickes on July 1, 1941: “The Japs are having a real drag-down and knock-out fight among themselves...trying to decide which way they are going to jump—attack Russia, attack the South Seas (thus throwing in their lot definitely with Germany), or whether they will sit on the fence and be more friendly with us.”920

918. Among the vital resources in southern Indochina were tin and rubber. Text from the second article of “Outline of National Policies in View of the Changing Situation,” Imperial Conference, July 2, quoted in Nagaoka, “The Drive into Southern Indochina and Thailand,” p.236. Oddly, Ike’s translation of the same article says “our Empire will not be deterred by the possibility of being involved in a war with Great Britain and the United States.” See Ike, Japan’s Decision for War, p.78.
919. The U.S. was reading the diplomatic traffic from Tokyo to Washington and Berlin, which summarized the debate and policies chosen.
920. Letter from President Roosevelt to Harold Ickes, July 1, 1941, quoted in Dallek, Franklin D. Roosevelt and American Foreign Policy, p.273.
It became clear to the U.S. shortly after July 2, that Japan would occupy southern Indochina, presenting the U.S. with a dilemma of how to respond. Hornbeck assessed Japan's leaders to have "already discounted the probability that the United States will resort to some economic measures against them and they have discounted and are ready to accept the probable effects, adverse to them, of such measures." For this reason on July 16, 1941, Hornbeck recommended that after Japan had made its "overt" move against southern Indochina, the U.S. should take "extensive" measures against Japan including: freezing Japanese funds; ending silk imports; increasing all aid to China; displaying naval force in the region; and preparing to act in concert with the British to end iron ore and oil shipments to Japan from all source countries (i.e., U.S., DEI, Philippines, Malaya). Hornbeck did not advocate complete embargos on oil and iron ore until Japan had further disclosed its intentions to seize more than Indochina (i.e., clear intent to move south). He did, however, recommend full preparation for that event, so that when it became clear that Japan would not go north against the Soviet Union, the aggressive path most in the U.S. "national interest," the U.S. could act quickly. To this end, the British were informed on July 10, that if Japan moved south the U.S. would institute economic and financial embargos. To be sure, many other administration officials were advocating these same measures for many months, but they were only now put into operation.

On July 18, 1941, President Roosevelt directed his confidant at the State department, Undersecretary Welles, to prepare to use the established joint State-Treasury

921. See Hornbeck memorandum, July 16, 1941, in Hornbeck Papers, Box 253, Folder: Japan, U.S. General.
department vehicle to freeze all Japanese funds. Welles directed Hornbeck to draw up the freezing and trade restriction paperwork. The detailed guidelines for precisely what trade license applications were to be approved by Treasury for Japanese funds release was devolved to Assistant Secretary of State Dean Acheson, who oversaw the Foreign Funds Control Interdepartmental Committee between State and Treasury. The frozen funds would control all future Japanese trade through an unpublished two step process. First, trade license applications would have to be submitted to the State department and reviewed under as yet unestablished allowable oil export criteria (e.g., only 67 octane or less gasoline at the average amount from 1935-36). After State approval, another application would have to be made to the Treasury department for frozen exchange funds release to pay for the authorized shipments. The policy of freezing Japanese funds but technically allowing trade to continue was publicly declared by President Roosevelt on July 24, 1941, three days after Japanese forces began their occupation of southern Indochina.

President Roosevelt chose to vest ultimate authority over this process in Morgenthau’s Treasury department, not Hull’s State department. Although Roosevelt made a point of declaring his intention to allow some oil shipments to Japan, he vested authority in Morgenthau knowing his proclivity for embargoing Japan. On the same day the financial freeze was announced, Roosevelt met with Japanese Ambassador

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923. Acheson was the State department official Secretary Morgenthau felt he could be most “candid” with and who shared Morgenthau’s views on economic policy. See Blum, From the Morgenthau Diaries: Years of Urgency, p.332; Wolthus, “United States Foreign Policy towards the Netherlands Indies,” p.209; Utley, Going to War with Japan, p.153; Anderson, The Standard-Vacuum Oil Company, pp.175-6.

924. Anderson describes this bureaucratic wormhole best, but concludes that the President did not intend for an embargo to emerge. See Anderson, The Standard-Vacuum Oil Company, p.178.

925. Blum, From the Morgenthau Diaries: Years of Urgency, p.379. Utley blames Dean Acheson for the bringing about of the full embargo by early August. See Utley, Going to War with Japan, pp.155-6.
Admiral Nomura and warned him that if Japan invaded the DEI it would certainly mean war with Britain and the Netherlands. He then added, “in view of our own policy of assisting Great Britain, an exceedingly serious situation would immediately result.” To avoid the implication of this, Roosevelt suggested the neutralization of Indochina after the withdrawal of Japanese forces from all of Indochina. The U.S. received no immediate reply to this from Ambassador Nomura or the new Foreign Minister Vice Admiral Toyoda. President Roosevelt then summarized for the Japanese and American publics why the U.S. had continued its trade with Japan in the past. In a meeting with a group of civilian defense volunteers attended by the press, Roosevelt declared: “if we cut the oil off, they probably would have gone down to the Dutch East Indies a year ago, and you would have had war. Therefore, there was—you might call—a method in letting this oil go to Japan, with the hope—and it has worked for two years—of keeping war out of the South Pacific for our own good, for the good of the defense of Great Britain, and the freedom of the seas.”

The President’s public declaration of the strategic purpose of supplying Japan in the recent years is most consistent with offensive realism. He knowingly supplied Japan with resources that increased its capabilities, but he did so to maintain the U.S. ability to influence when that war might begin. Delay served the U.S. strategic plan for a two ocean and global war and allowed the U.S. to better prepare for that war. At least as significantly, suppling Japan shielded prospective allies in Southeast Asia (i.e., the

926. Wolthius, “United States Foreign Policy towards the Netherlands Indies,” p.213.
927. President Roosevelt Informal Remarks to Volunteer Participation Committee, July 24, 1941, in Peace and War, pp.703-4; Dallek. Franklin D. Roosevelt and American Foreign Policy, pp.274-5.

452

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Netherlands and Britain) from undue Japanese pressure. In supplying an increasingly threat-#ing Japan, his actions do not support defensive realism's core hypothesis of denying capabilities increases to a threatening rival. This tactical supply also is not supported by either liberalism and marxism because the companies involved were not necessarily desirous of continuing the trade. It is interesting to note that after the cessation of oil exports, oil industry officials made public statements proclaiming that their prior supplies to Japan were directed by U.S. policy and they did not therefore deserve the public vitriol that was directed against them in continuing the supplies up to July 1941. The policy purpose in the full embargo that emerged, however, is still a matter of debate as is the bureaucratic mechanism by which it was affected.

The freeze on Japanese funds was instituted quickly and comprehensively across not just the U.S., but also indirectly in south America and directly in the British empire and the Netherlands. Japan reciprocated, freezing American, British and Dutch yen accounts and by the end of July, trade and finance had been drastically re-oriented. Before leaving Washington on August 3, 1941, for the first Atlantic Conference with Prime Minister Churchill, Roosevelt ordered Welles to revoke all existing licenses for oil exports to Japan, forcing any oil trade aspirant to re-apply under the new framework, which was opaque, staffed by economic warfare advocates and directed by Welles not to

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928 Hornbeck noted that U.S. oil strategy proclaimed by Roosevelt was not "materially different as regards the considerations upon which it was based" from that followed on scrap iron. Hornbeck was likely referring to the fact that U.S. scrap exports shielded Malaya and the Philippines from Japanese pressure as did the oil supplies. See Hornbeck memorandum February 18, 1942, in Hornbeck Papers, Box 425, Folder: Policy of the United States: Far East.


act on any Japanese applications for "a week or so." This delay in early August was turned into a permanent bureaucratic briar patch, and no oil exports or any other traded items left the U.S. or the DEI for Japan after August 5, 1941. The oil companies were used by the U.S. government over the next two months to aid in the bureaucratic muddling of Japan's oil desires by having the companies communicate to the Japanese that their applications for oil licenses and granted licenses appeared to be in process at Treasury for release of funds. Treasury never released any Japanese funds for payment on granted oil trade licenses, and withheld approval due to "the inability of Japan to arrange satisfactory methods of payment."

Whether Roosevelt intended this full cessation or not is still an open question. However, he accepted it in early September on the grounds that re-starting the oil trade would be seen as weak and emboldening to Japan's militarists. If Roosevelt truly intended to avoid conflict with Japan, he would have re-started some oil shipments to Japan while Konoe and Toyoda were still its leaders reaching out to the U.S., albeit in more demanding ways. Roosevelt and his key officials fully understood the consequences of an oil embargo on Japan, and his decision not to alter the embargo can only mean that he was willing to court war with Japan. Most charitably, this may have been part of a strategy to shock Japan into a more quiescent posture in Asia and bring them to better negotiating terms on Indochina and China. The decision certainly did not,

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931. Wolthius, "United States Foreign Policy towards the Netherlands Indies," p.219; Utley, Going to War with Japan, pp.217-8, footnote 42.
932. See memorandum from Dean Acheson to Secretary of State, September 22, 1941, pp.3-4, in Hornbeck Papers, Box 338, Folder: Petroleum; Anderson, The Standard-Vacuum Oil Company, pp.186-8.
933. Dallek, Franklin D. Roosevelt and American Foreign Policy, pp.275. Sagan concludes Roosevelt didn't want to appear as an appeaser to domestic U.S. opinion. He held, "It is possible that similar fears overcame Roosevelt's earlier concerns about provocation in the waning days of the summer of 1941."

Whatever one may say of Roosevelt, he was not a fearful individual, particularly with respect to domestic public opinion. Sagan, "Origins of the Pacific War," p.336.
however, cause Japan to re-evaluate its decision to go south instead of north against the
Soviet Union. With each day of no oil trade, Japan would draw down on its oil reserves
impelling it to seek their replenishment in the DEI. Equally offensive to the Japanese
was the fact that U.S.-Asian oil trade did not end with these financial and trade actions
against Japan.

In late August 1941, the U.S. sent oil tankers carrying gasoline to the Soviet port
of Vladivostok as part of the effort to aid the Russian resistance of Germany. The
Japanese objected strenuously to a particular shipment passing near Japan, declaring that
these “cargoes of petroleum products should be coming to us.” Hornbeck had to beat
back the suggestion from Ambassador Grew that this tanker should be recalled pending
the outcome of a Japanese proposal to hold a U.S.-Japanese heads of state conference to
settle outstanding issues. He did so by noting that the American government’s credibility
as material aid supplier to those countries resisting Germany and Japan would be
damaged if it backed down due to Japanese pressure. His argument carried the day,
even with Secretary Hull, who by this time had accepted the U.S. position of challenging

934. The U.S. also sought to assure the Russians of oil supplies in the event they followed through with the
U.S. desire to see them destroy the oil fields of the Caucasus which Hitler was striving for. See telegram
from U.S. Secretary of State to U.S. Embassy Moscow, September 30, 1941, File 861.6363/413, RG 59.
Digest of this and related memorandums, “Notes and Abstracts of the Papers in the DCR Files Relating to
Demolitions in the Caucasus and the Netherlands East Indies,” in Hombeck Papers, Box 338, Folder:
Petroleum. See also Joel Hayward, “Hitler’s Quest for Oil: the Impact of Economic Considerations on

935. See Hombeck memorandum, August 27, 1941, p.1, in Hornbeck Papers, Box 396. Folder: Soviet
Union: Soviet-American Relations. See also Foreign Minister Toyoda’s summary of the offense at the
Imperial Conference of September 6, 1941, in Ike, Japan’s Decision for War, p.146.

936. An unstated reason to prod this U.S.-Soviet exchange, was the dissension in Japanese war calculations
it might cause giving those advocates of a northern attack some further justification for their position. This
trade appears to have had this effect, judging by the Imperial Conference summary materials. See Ike,
Japan’s Decision for War, pp.153-55. In mid-October, Hombeck noted, “Worse things can and may
happen than an attack by Japan upon the Russian position in east Asia...While we, of course, would not
wish to view with gratification a move by Japan against Russia, there is, in my opinion, no good reason
why we should, in anticipation, view with alarm the possibility of such a move.” See Hombeck
memorandum, October 15, 1941, in Hornbeck Papers, Box 338, Folder: Petroleum.
Japan's diplomatic overtures and demands. After reading various MAGIC decrypts
detailing Japan's southern advance plans despite their diplomatic overtures, Hull stated "I
just don't want us to take for granted a single word they (Japan) say, but to appear to do
so to what ever extent it may satisfy our purpose to delay further action by them."937

An equally plausible assessment of the Roosevelt administration’s embrace of the
embargo would contend that the U.S. was seeking only to delay Japan’s reaction to a full
oil and trade embargo. Delay was imperative and strategically necessary in order to draw
down Japanese oil reserves as much as possible and build up the inadequate defenses in
the Philippines before the outbreak of actual hostilities.938 Every month of delay would
mean less war-fighting capability for Japan in the coming conflict that both sides viewed
as one likely to be long and determined by material resources.939 If this were the policy,
U.S. officials’ statements like that of Hull’s were driven by the logic of delaying Japan’s
requests for as long as possible while appearing willing to negotiate. After their meeting
in early August, Churchill summarized the “President’s idea...to [continue to]
negotiate...and thus procure a moratorium of, say, thirty days in which we may improve

937. Hull to Welles, August 4, 1941, quoted in Blum, From the Morgenthau Diaries: Years of Urgency,
p.380.
938. It must be recalled that U.S. assessments were that the DEI oil facilities would be valueless for a year
and Japan’s reserves up to the stoppage of the oil trade would likely only sustain 18 months of operations at
best. Therefore, any delay that added up to this time period only worked to the U.S. advantage, particularly
if the U.S. war strategy was still defensive action and delay in the Pacific.
939. Hornbeck noted “the war is in all probability going to be a long war: a war that will be won by
machines and resources.” See Hornbeck memorandum, “Better to Give Aid on two Fronts and Fight on
One than to Withhold Aid on One and Have to Fight on Both,” February 22, 1941, p. 16, in Hornbeck
Papers, Box 425, Folder: U.S. Policy-Assistance on Two Fronts 1941.
our position...He will also maintain in full force the economic measures directed against Japan. These negotiations show little chance of succeeding, but President considers that a month gained will be valuable."\(^\text{940}\)

The U.S.-Japanese negotiations from early August through early December did not succeed, nor could they have given both Japanese demands and the U.S. response. Beginning on August 6, 1941, Japan demanded not only a resumption of U.S. exports, but also U.S. government cooperation "with the Japanese Government in the production and procurement of natural resources as are required by Japan in the Southwestern Pacific areas, especially in the Netherlands East Indies."\(^\text{941}\) Japan also demanded that the U.S. recognize Japan's "special status" in Indochina even after an agreement on withdrawal of Japanese troops could be affected. The U.S. would not accept these terms nor the explicit call to obtain for Japan control of DEI oil resources. The U.S. response took refuge in demanding Japanese adherence to the four principles on which a settlement could be based. These were: 1) respect for the sovereignty and territorially integrity of all states; 2) non-interference in the internal affairs of other states; 3) the principle of equality including equality of commercial opportunity; and 4) non-disturbance of the status quo in the Pacific, except by peaceful means. In rejecting the meeting with Premier Konoe, President Roosevelt declared that the American

\(^{940}\) Churchill to Foreign Secretary Anthony Eden on August 11, 1941, quoted in Anderson, *The Standard-Vacuum Oil Company*, p.190.

\(^{941}\) Japanese Government proposal delivered to Secretary of State, August 6, 1941, in *Peace and War*, p.707

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government “could not enter into any agreement which would not be in harmony with the principles which the American people—in fact all nations that prefer peaceful methods to methods of force—believe.”

These principles allowed the U.S. to deflect the Japanese demand that the U.S. help it secure DEI oil territories, because that would mean interfering in the internal affairs of the Netherlands. The non-committal responses of the U.S. and periodic rejection of proposed agreement language, due to Japan’s not renouncing the Tripartite Pact for example, led to stalemate in the negotiations and intense pressure within Japan for a decision. Robert Wolthius noted that each side issued incompatible demands such that “after October 2 meaningful discussions between the two powers ended. Talks continued, but they were a form of shadow boxing while final preparations for war were made.” In this environment, Konoe’s desire to reach some sort of negotiation with the U.S. became untenable within Japan’s domestic struggle for power. Paul Schroeder summarized this well: “The decisive rift in the Konoe cabinet, an extension of the historic opposition within the Japanese government of the bureaucrats and the Army, was over a completely different issue—the question of whether Japan should fight or retreat in the face of the American embargo.”

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942. President Roosevelt to Premier Konoe, September 3, 1941, in Peace and War, pp.729-731. Interestingly, the U.S. closed the Panama Canal to all Japanese traffic by early August 1941, raising the question again of what principles the U.S. was adhering to itself. The Japanese merchant cruiser “Asaka Maru” was hassled so much on its return transit request through the Canal that it decided to sail around the Cape of Good Hope instead in June 1941. See memorandum from Miller, Far Eastern Division, State department to Dean Acheson, September 20, 1941, in Hornbeck Papers, Box 338. Folder: Petroleum: Chapman, “The Economic and Technological Basis of the German Alliance with Japan,” pp.65-6, footnote 60. See also Wolthius’ analysis that the four principles were invoked to gain time for defense preparation and this was “general knowledge” in U.S. policy circles. See Wolthius, “The United States Foreign Policy towards the Netherlands Indies,” p.245, footnote 38.

943. See Wolthius, “The United States Foreign Policy towards the Netherlands Indies,” p.249.

Schroeder overlooks the Japanese navy’s willingness to support war with the U.S. precisely to achieve the oil that had been denied it by the Anglo-American-Dutch powers. Konoe was replaced by Premier Tojo Hideki on October 16, 1941, because Tojo would answer the above question by fully embracing the need for war and for that war to start soon. Japan’s need to make a decision for war was based on its calculation that it could not afford to lose more of its relative naval power capability to the U.S. through oil depletion and time granted to the U.S. to increase its global capabilities under the June 1940 two-ocean building plan. Navy Chief of Staff Nagano summed it up well on October 23, 1941:

The United States will probably try to prevent Japan from getting into the war until the end of 1942, when the United States will be sufficiently prepared to fight on two oceans...we were to have reached a decision in October, and yet here we are...the Navy is consuming 400 tons of oil an hour. The situation is urgent. We want it decided one way or the other quickly. 945

Japan’s decision for war came after a last failed demand for U.S. assistance to supply it oil on November 20, 1941.946 In this “Plan B” submission to Secretary of State Hull, Japan demanded that “the Government of the United States shall supply Japan a required quantity of oil...the Governments of Japan and the United States shall cooperate with a view to securing the acquisition of those goods and commodities which the two countries need in the Netherlands East Indies.”947 In exchange, Japan would agree to

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945. Japanese Navy Chief of Staff Osami Nagano, at the Liaison Conference, October 23, 1941, quoted in Ike, Japan’s Decision for War, p.186.
946. Prior to this last effort, Hornbeck took note of Japan’s labels of its recent proposals. On November 18, 1941, he wrote “We have had on occasion to note mention by the Japanese of their “last proposal,” “final proposal,” and “last final proposal;” now, we note mention of an “absolutely final proposal.” See Hornbeck note, November 18, 1941, in Hornbeck Papers, Box 533, Folder: Intercepted Japanese Telegrams and Notes.
947. See Plan B text in Morley, ed., The Final Confrontation, p.370; Akira Iriye, Pearl Harbor and the Coming of the Pacific War. (Boston, MA: Bedford/St. Martin’s, 1999), p.40.
withdraw forces from southern Indochina immediately and from all of Indochina after the war with China were settled. After consulting Churchill, who was disinclined to compromise even temporarily because of negative ramifications in China, President Roosevelt sanctioned Secretary of State Hull’s counter-note of November 26. In this note, Hull called for Japan to effectively pull back to the pre-Manchurian invasion boundaries and made no mention of Japan’s consistent and specific demands for oil, but did oddly specify that raw silk could be placed on a duty free list.948

This note was interpreted as an ultimatum in Japan, regardless of the U.S. intent in its proposition for Japanese withdrawal from China. President Roosevelt ordered the issuance of the infamous war warning message the next day on November 27, 1941. Secretary of War Stimson directed General Marshall to distribute it; and it read in part: “Negotiations with Japan appear to be terminated to all practical purposes with only the barest possibilities that the Japanese government might come back and offer to continue. Japanese future action unpredictable but hostile action possible at any moment. If hostilities cannot repeat cannot be avoided the United States desires that Japan commit the first overt act.”949 Hornbeck neatly summarized the onus of decision placed upon the Japanese:

Japan has been at war in eastern Asia and the Western Pacific for several years past. Japan has threatened to make war on each and every one of her near neighbors and even on the United States. No price that we might have paid to Japan would buy or produce a peace in the Pacific or security

948. Section 2, Article 3 of the note stated, “The Government of Japan will withdraw all military, naval, air and police forces from China and from Indochina.” See text of cables between Churchill and Roosevelt and Hull note in Iriye, Pearl Harbor and the Coming of the Pacific War, pp.69-77.
for the United States (and/or Great Britain and/or China and/or Russia) in the Pacific. The question of more war or less war in the Pacific rests at this moment in the control of minds and hearts in Tokyo, not in the control of minds and hearts in Washington.950

7.8 U.S.-Japanese Economic Exchange, 1937-1941

Japan’s decision for war came only a few days later on December 1, 1941, as “Japan made the acquisition of Netherlands Indies oil its first foreign policy objective and the ultimate cause of war in the Pacific.”951 Japan’s vital dependence on U.S. crude and fuel oil drove this decision. Prior to the cessation of trade in July, Japan was receiving almost all of these oil products from the U.S. with fewer and fewer alternatives. The U.S. and Britain ensured that Japan’s third country sources were removed from the trade in early 1941 through the tanker shortage, and this reinforced and accelerated Japan’s dependence on the U.S. and the frustration of Japan. Prior to the creation of the tanker shortage, Japan had reached out to several third countries for oil, including: Persia, Mexico and Saudi Arabia. These suppliers and the U.S. policy of not pulling the oil plug until it was prepared to do so, helped Japan in 1940 to decrease its crude and fuel oil dependency on the U.S. to 67.3%.

This was a fleeting moment of only slightly lessened dependence that evaporated quickly with the removal of the tanker transports. In fact, Japan’s reliance on Western tankers during this period caused it to be strategically handicapped once those tankers were removed from the trade, and this deficiency crippled Japan throughout the war (i.e.,

950. Hornbeck memorandum, November 27, 1941, in Hornbeck Papers, Box 255, Folder: Japan: U.S. War with Japan.

461
trade caused strategic complacency due to inadequate Japanese tanker production). This forced Japan to import two to three times as much iron ore and coking coal to replace the scrap from the U.S., and Japan's shipping capacity was therefore doubly stretched with U.S. trade cessation.

Although absolutely critical to Japan's decision for war and the conduct and outcome of the war, the tanker gap was not the only economic relationship increasing Japan's vulnerability and inefficiency, or showing signs of deterioration and the strain of increasing political conflict throughout the 1937-1941 period. Both trade and investment exchange decreased during the period, with trade only decreasing after the peak year of 1937. Accurate data on U.S. loans to Japan for the end of the period are not available, however, there is evidence that the amount of U.S. loans outstanding in Japan decreased quite substantially from the peak value in 1931-32 and from that recorded in 1935-1936. Again, no new loans were issued to Japan in the period and therefore the U.S. share in Japan's domestic fixed capital formation was zero. By the end of 1939, it was estimated that only $112 million dollars of the existing portfolio loans from the U.S. to Japan remained in place. This was down from the 1935-1936 value of portfolio loans outstanding of $323.8 million dollars detailed in Table 6.3.

952. As noted earlier, Japan's own tanker fleet was insufficient to the task of transporting the large amounts of oil from the DEI to Japan proper and Japan did not develop this capability prior to or during the war. See Evans and Peattie, Kaigun, pp.409-10; H.P. Wilmott, Empires in the Balance: Japanese and Allied Pacific Strategies to April 1942, (Annapolis, MD: Naval Institute Press, 1982), p.68.

953. The postwar survey noted, "the tonnage of shipping required for any given level of steel production had greatly increased as a result of the conversion from a high scrap process to a pig iron process. To produce the equivalent in pig iron of one ton of imported scrap would require from two to three tons of iron ore and coking coal imports." See U.S.S.B.S., Coals and Metals in Japan's War Economy, p.68.

954. See Federal Reserve Bank of New York, Office Correspondence from W.H. Rozell to Knoke, February 3, 1941, p.3. Box 147, File: Japan Trade, 1920-1954, RG 82. Interestingly, this correspondence notes Japanese direct investment in the U.S. at the end of June 1937 to be $41 million dollars. No further
U.S. direct investments in Japan declined further during the period, ending 1940 at $37,671 million dollars. This represented a substantial decline from the peak of $61.45 million dollars in 1931 and highlights both the nationalization efforts of Japan's government and U.S. companies' desire to vacate a hazardous environment.\textsuperscript{955}

Approximately 64\% of the remaining U.S. direct investment was in manufacturing, principally electrical and telephone equipment and the auto company stakes. It is important to note that U.S. direct investment in Japan was less than U.S. investment in China, the DEI, India and the Philippines and had been so since 1931. As was noted earlier, the single largest U.S. investment stake in Asia was Stanvac's holdings in the DEI. This was estimated at $74.405 million dollars in 1941, nearly twice as large as total U.S. direct investment in Japan at that time.\textsuperscript{956}

There was substantial selling of Japanese dollar-denominated assets in the U.S. (e.g., Treasury bills, and a few stocks) up to the freezing of Japanese funds in late July 1941. These released dollars were carefully scrutinized by the Federal Reserve Bank of New York and the Treasury department, who took note of the transfers of dollar balances to Brazil and other destinations.\textsuperscript{957} These funds were blocked as well after the freezing of funds in the U.S., leaving Japan with little capacity to use its accumulated dollars.

The most interesting aspect of U.S.-Japan finance in this period is the large U.S. gold purchases from Japan beginning in 1937. U.S. gold purchases allowed Japan to


accumulate dollar balances and pay for imports from the U.S., while indirectly reinforcing Japan's economic vulnerability to the U.S. by circumscribing its potential dealings with other countries and allowing the U.S. government to track Japan's movement of dollars around the Western hemisphere. The U.S. was also buying and demanding gold from other countries, building its reserves to maximize its position in any future monetary system. There is no discussion of the purpose of the U.S. Treasury buying Japanese gold, beyond a few U.S. press indictments of this exchange (i.e., Treasury Secretary Morgenthau does not mention it in his diary, nor does John Blum in his otherwise excellent reviews of Morgenthau's Treasury in the Roosevelt administration). Therefore, only with great circumspection is the speculation above advanced as to the U.S. policy purpose. This exchange did have the effect of increasing Japan's reliance on the U.S. and yielded the observation that as war approached, Japan's monetary asset exchange with the U.S. increased dramatically. The magnitude of the purchases is illuminated by the fact that between 1937-1939 the value of Japanese gold exports to the U.S. exceeded the value of its export of goods and services to the U.S..

As noted earlier, U.S. exports to Japan in 1937 were unusually large due to increased Japanese demand that preceded the wholesale invasion of China beginning in July 1937 (e.g., scrap iron and steel). U.S. exports went up again in 1940 in support of U.S. policy to supply Japan to delay its move southward against British, Dutch and French possessions (See Table 7.7). Nonetheless, U.S. exports to Japan declined in importance to the U.S. over this final period, falling from 8.6% of total U.S. exports in 1937 to 5.7% in 1940, and then only 1.2% in the embargo year of 1941. U.S. imports from Japan were roughly constant averaging 6.5% until they began to fall off in late 1940.
and reduced to only 2.3% of total U.S. imports in 1941. Japanese reliance on the U.S. as an export market continued to decline, as exports to the U.S. were less than 20% of total Japanese exports after 1937. However, Japanese imports from the U.S. remained large averaging above 34% of total imports until 1941. These data demonstrate again that U.S.-Japanese trade was asymmetric, with Japan more reliant on trade with the U.S.. This asymmetry was reduced in particular items in comparison with other periods, but increased in oil as noted above, which was far more critical.
<table>
<thead>
<tr>
<th></th>
<th>1937</th>
<th>1938</th>
<th>1939</th>
<th>1940</th>
<th>1941</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Total exports of Japan in thousands of Yen (as % of Japanese GDP)</strong></td>
<td>3,175,418 (13.6%)</td>
<td>2,689,677 (10%)</td>
<td>3,576,352 (10.8%)</td>
<td>3,655,849 (9.3%)</td>
<td>2,650,865 (5.9%)</td>
</tr>
<tr>
<td><strong>Japanese exports to U.S. in thousands of Yen (as % of total Japanese exports)</strong></td>
<td>639,000 (20.1%)</td>
<td>425,000 (15.8%)</td>
<td>642,000 (17.9%)</td>
<td>569,000 (15.6%)</td>
<td>278,000 (10.5%)</td>
</tr>
<tr>
<td><strong>Japanese raw silk exports to U.S. in thousands of Yen (as % of total exports to U.S.)</strong></td>
<td>325,225 (50.9%)</td>
<td>297,882 (70.1%)</td>
<td>437,611 (68.2%)</td>
<td>382,493 (67.2%)</td>
<td>184,009 (66.2%)</td>
</tr>
<tr>
<td><strong>Japanese exports to U.S. as % of Japanese GDP</strong></td>
<td>2.7%</td>
<td>1.6%</td>
<td>1.9%</td>
<td>1.4%</td>
<td>.6%</td>
</tr>
<tr>
<td><strong>Total imports of Japan in thousands of Yen (as % of Japanese GDP)</strong></td>
<td>3,783,177 (16.1%)</td>
<td>2,663,440 (9.9%)</td>
<td>2,917,640 (8.8%)</td>
<td>3,452,724 (8.8%)</td>
<td>2,898,565 (6.5%)</td>
</tr>
<tr>
<td><strong>Japanese imports from U.S. in thousands of Yen (as % of total Japanese imports)</strong></td>
<td>1,270,000 (34%)</td>
<td>915,000 (34%)</td>
<td>1,002,000 (34%)</td>
<td>1,241,000 (36%)</td>
<td>572,000 (19.7%)</td>
</tr>
<tr>
<td><strong>Japanese cotton imports from U.S. in thousands of Yen (as % of total imports from U.S.)</strong></td>
<td>306,265 (24.1%)</td>
<td>166,195 (18.2%)</td>
<td>146,561 (14.6%)</td>
<td>161,500 (13%)</td>
<td>62,605 (10.9%)</td>
</tr>
<tr>
<td><strong>Japanese imports from U.S. as % of Japanese GDP</strong></td>
<td>5.4%</td>
<td>3.4%</td>
<td>3%</td>
<td>3.2%</td>
<td>1.3%</td>
</tr>
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Table 7.7: Japanese Exports to and Imports from the U.S., 1937-1941

Japanese silk exports continued to occupy an important part in Japan's export trade and trade with the U.S., but as a percentage of Japan's overall economy and total exports their importance had declined from earlier periods (e.g., 1929 silk exports were 4.8% of Japanese GDP, but in 1940 only 1.1% of GDP). Japanese silk exports were the largest single category of exports in 1939 and 1940, but their percentage of total Japanese exports had fallen from the 1929 high of 35.2% to only 11.3% of total Japanese exports in 1940. Japan still relied on the U.S. market to absorb the bulk of its silk exports, with the U.S. taking roughly 86% of Japanese silk exports in 1939 and 1940, up from only receiving 79.9% in 1937. As noted earlier, silk exports were the one U.S. import from Japan that was a strategic commodity, necessary for the manufacture of parachutes. The U.S. continued to import Japanese silk up to the cessation of trade in late July 1941, but had prepared itself for the cessation of imports, thereby removing any U.S. strategic vulnerability in severing trade relations with Japan.

The domestic U.S. silk industry was extensively analyzed by the U.S. government and nylon and rayon substitutes were stimulated by government purchases and investments in production by the DuPont Company in particular. Du Pont began large-scale nylon production in December 1939, and was to benefit from the large government expenditures in the war effort. The U.S. Tariff Commission concluded: "Although a complete stoppage of imports of silk would not have an important effect either on the defense program of the United States or the economy of the country as a whole, the impact would be serious, at least temporarily, for certain groups." These effects would

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959. The U.S. government had undisclosed silk stockpiles for parachute production and civilian stockpiles, under government licensing control after July 1941, were sufficient for producing at least 500,000
fall largely on the women’s hosiery industry concentrated in Charlotte, NC and Berks County, PA. The U.S. Tariff Commission noted that each of these areas had expanding defense production operations and the employment effect would therefore likely be negligible. Well before the trade embargo, the domestic silk industry had prepared for the transition to synthetic fabrics and alternatives, and “their efforts were directed toward (U.S.) government cooperation in a shift to substitute materials, rather than toward a restoration of trade with Japan.”

Japanese imports from the U.S. during this period peaked in 1937, fell thereafter and then rose again in 1940 to near their peak of 1937. Because the trade for 1941 only covers January through July, it appears Japan’s imports in the first seven months of 1941 were averaging approximately what it had imported during this period (i.e., roughly 1.1 billion Yen on an annual basis). The composition of its imports from the U.S. changed, with cotton becoming less a factor and machinery and oil products more of a factor in Japan’s imports from the U.S.. Japanese cotton imports from the U.S., which had been a large percentage of its total imports from the U.S., continued to decline and represented only 13% of total imports from the U.S. in 1940. This was due in large measure to Japan’s efforts to achieve self-sufficiency in cotton production in its occupied territories, including China and the South Seas islands. As a result, the formerly increasing position of Japan in the U.S. cotton trade also decreased, reducing this partial U.S. vulnerability to Japan. In 1940, for example, U.S. raw cotton exports to Japan were 14.1% of total U.S. raw cotton exports, down from 28.5% in 1936.


\textsuperscript{961} Cohen, Japan’s Economy in War and Reconstruction, p.391.
U.S. oil products and machinery exports were, however, increasing in importance. As noted earlier, exports of machinery to Japan increased up through the embargo on them in 1940. In that year, machinery exports to Japan totaled $29.232 million dollars, or 12.9% of total U.S. exports to Japan that year. Unfortunately, it is not possible to extract out how much of this machinery went to Manchuria where much of it lay idle due to insufficient parts and greases, or how much was specific to gold mining operations which contributed to the circular exchange with the U.S. and resource diversion described earlier in the chapter. Nonetheless, it is significant that some U.S. machinery did have these effects and did, if only marginally, contribute to Japanese resource diversion and economic inefficiency. U.S. crude and fuel oil exports to Japan remained substantial and comprised 21% of total U.S. crude and fuel exports in 1941, although the amount of crude within this decreased as opposed to the fuel oil amount. U.S. gasoline exports also increased dramatically in 1940 and 1941, comprising 13.9% of total U.S. gas exports in 1941. The export of all classes of oil products to Japan were roughly 20% of total U.S. exports to Japan, and continued to be this important through the end of July 1941 due to U.S. policy of supplying Japan to delay the conflict.

Although these supplies did materially contribute to Japan’s capabilities and its stockpiles, other aspects of U.S. exchange with Japan instantiated inefficiencies in Japan’s production efforts, increasing its vulnerability, inefficient production and waste of capital. As noted earlier, Japan’s synthetic fuels effort relied on U.S. parts and supplies after Germany went to war in Europe. When U.S. fuel pumps and specialty steel furnace tubes could not be purchased, Japan’s facilities with large capital investments were rendered either useless or of dramatically reduced capacity. It is worth noting again
the postwar strategic survey conclusion: "Strategically, the contribution of Japan's synthetic oil industry to the war may be regarded as negative. The manpower and materials expended on it certainly impeded the national war effort more than the synthetic oil production aided it."\(^{962}\) Inefficient use of manpower and materials was aided by U.S. assistance in building these facilities, up to the point of not supplying some of the more vital components.\(^{963}\) More importantly, the supply of crude oil refinery equipment reinforced both Japan's vulnerability to U.S. supply pressure and Japan's logistical difficulties integrating distant DEI crude oil with its refineries in Japan proper. Japan's inability to make this work cost it its empire.

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<th>1937</th>
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<th>1939</th>
<th>1940</th>
<th>1941</th>
</tr>
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<tbody>
<tr>
<td>Overall trade balance of Japan in thousands of Yen (Exports-Imports)</td>
<td>-607,759</td>
<td>26,237</td>
<td>658,712</td>
<td>203,125</td>
<td>-247,700</td>
</tr>
<tr>
<td>Bilateral trade balance of Japan with U.S. in thousands of Yen (Japanese Exports to U.S. - Japanese Imports from U.S.)</td>
<td>-631,000</td>
<td>-490,000</td>
<td>-360,000</td>
<td>-672,000</td>
<td>-294,000</td>
</tr>
<tr>
<td>Total U.S.-Japan trade as % of Japanese GDP (Japanese exports to and imports from U.S. as % of its GDP)</td>
<td>8.1%</td>
<td>5%</td>
<td>4.9%</td>
<td>4.6%</td>
<td>1.9%</td>
</tr>
</tbody>
</table>

Table 7.8: Japan's Overall and Bilateral Trade Balance, 1937-1941

\(^{962}\) U.S.S.B.S., Oil in Japan's War, p.42.

\(^{963}\) More narrowly, Japanese refineries were built to operate best on California crude, and after July 1941, when different crudes were employed the operating efficiency of the refineries decreased. This is another example of inefficiency through imports of technical processes and equipment built to operate on the characteristics of the source country.
Japan’s overall economic reliance on trade with the U.S. declined after 1937, and is important to note given the claims by many scholars that its basic economic dependence on the U.S. increased after the China war began (See Table 7.8). The importance of the Japan trade to the U.S. declined as well from .7% of U.S. GDP in 1937 to .49% in 1940, before falling off totally with the cessation of trade in July 1941. For these reasons, the exchange relationship during the 1937-1941 period can be categorized as narrow due to the predominance of trade only, but slightly broader than the previous period due to the large increases in the monetary asset trade in gold. While strictly beneficial to Japan, this gold trade was increasing Japan’s vulnerability to the U.S. by foreclosing future exchange partner options to Japan (e.g., Brazil, Mexico). Direct investment and loans declined markedly as well, contributing to the categorization of the period as narrow and narrowing by the end. Nonetheless, Japan still benefited far more than the U.S. in the bilateral trade, particularly through the oil supplies that were allowed to continue until 1941. While it is true that Japan reduced its vulnerability to U.S. cotton embargo, Japan became increasingly vulnerable to the U.S. after the introduction of the tanker shortage in early 1941. This alone caused Japan’s dependence to increase to the point where the embargo triggered Japan’s lunge south for the autonomy-enhancing oil resources needed to defend its expanding empire by force of arms.
CHAPTER 8

CONCLUSIONS

8.1 Overview of the Inquiry, Key Findings and Theory Evaluation

This dissertation began with a simple question. In the late 1930s, why did Japan rely on the distant shores of the U.S. for approximately 85% of its vital oil supplies when the vast supplies of the much closer Dutch East Indies contributed only 5-10% to Japanese needs? This basic question became more interesting when the comparison with Japanese supplies from the DEI in the early 1920s was considered. Then, Japan received most of its oil needs from the DEI and took up to 47% of total DEI oil exports. Even more troubling still was explaining this supply shift to the U.S. given the founding principle of the oil company cartel of 1928. In their global arrangements, the companies agreed that import markets/countries should be supplied from their closest source of supply. The Japanese market simply did not fit this operating principle.

By taking the necessarily longer historical view of U.S.-Japan economic and security relations and a critical process tracing methodological approach, this dissertation has answered that question. Sometimes to advance theory and understanding, one has to step back. Japan became dependent on the U.S. for its vital oil supplies because of Anglo-American-Dutch coordinated control of oil resources in the DEI that began in the...
mid-1920s. U.S. supply of Japan from the early 1920s forward was the price of obtaining that coordination, and doing so served U.S. national interests in maximizing its direct influence over Japan and indirectly its ability to influence Britain as well. Stanley Hornbeck was the architect who oversaw the construction of this coordinated position in the 1920s, and his orchestration of entente with British oil interests and his sensitivity to Dutch predilections was a masterful display of statesmanship. Throughout the 1930s, he reinforced both the oil and overall economic vulnerability of Japan to the U.S., and then assisted President Roosevelt in using it to further U.S. national interests as the global war approached.

This dissertation has added to our understanding of causal processes in international relations by improving the historical record of some key events in the interwar period missing in most other works in the field. This dissertation has produced original historical interpretations from new source documents, and has materially improved upon prior international relations theory by examining a fuller range of economic exchange. The exchange analysis improves upon prior work by including a fuller range of instruments (e.g., direct investment, loans), and more importantly, by assessing the relationships established with third countries (e.g., alternate suppliers). By broadening the scope of analysis this dissertation has demonstrated that bilateral economic exchange assessments are insufficient in determining the strategic purpose of exchange, whether from the state’s perspective or even corporations. Bilateral exchange occurs within grand strategic environments. Assessing the dependence of one state on another is complex and this dissertation provides an analytic framework that yields better methods for theory evaluation and knowledge accumulation.
This dissertation sought to answer central questions regarding the purpose and effect of economic exchange between rival great powers by examining one of the more crucial rivalries during a period that has not received significant attention in recent historical scholarship. The U.S.-Japan rivalry deserves significant attention because it was Japan who first challenged the world's "peace machinery," and demonstrated that its gears were locked on Anglo-American discord. This discord rendered aggression a viable path to securing a state's strategic self-interest. Japan's militant expansion into China in fall 1931 cannot be fully understood without reviewing economic and security relations between the U.S. and Japan that resulted in Japan's exclusion from the DEI and loss of prestige and relative military power in the London Naval Treaty of 1930. The inquiry into this complex subject was directed by two fundamental questions central to the study of international relations and the evaluation of the central theoretical paradigms of realism, liberalism and marxism.

First, are exchange relations a function of state policy or the province of market actors? Second, why do rival great powers exchange with each other, particularly when their exchange appears to benefit one of them more extensively than the other? Outside of direct government exchange, these questions are interlocked and observable in state-corporate relations with respect to exchange with the rival. They are further observable in assessing whether exchange changes in response to changes in state threat perception and/or corporate preferences for exchange with the rival. At one level, the analysis reduces to a simple assessment of whether the state or its corporate actors achieved their

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4. Michael Hogan analyzed the bias toward Cold War history, which has resulted in a dearth of original work on the interwar period. He noted that only 10% of submitted articles to the seminal American foreign policy journal were related to this period, while most had the Cold War as their subject matter. See Michael Hogan, "Annual Report of the Editor," Diplomatic History, Vol. 16, (Spring 1992), p.354.
desired exchange with the rival. At a more complex level, this analysis requires determining the extent to which exchange with the rival compromises or enhances its autonomy, and whether it was so intended by either the state or corporations, or both.

This latter analysis requires a balanced evaluation of the rival’s economic and strategic vulnerability in its exchange relations with the state. This dissertation advanced a process for assessing the breadth, gains and vulnerability from exchange, which allows for a crude determination of whether the rival is becoming more dependent or autonomous in its exchange with the state. This evaluation process is itself broader than most work in the field because it examines the range of exchange that occurs among states (e.g., trade, direct investment, loans and bonds, and aid). Measurements of the importance of overall trade and finance between the state and rival were evaluated in addition to specific analyses of the largest and most critical items to the rival’s economy and military capability. From this review, a determination was made regarding the rival’s bilateral dependence on or autonomy from the state. A meaningful determination can not be made, however, by studying bilateral exchange relations alone, or by accepting even a static measure of vulnerability in one critical item as proof of non-increasing dependence (e.g., Japanese imports of oil from U.S. are flat at 80% of total across a given period).

Evaluating dependence requires assessment of decisions that surround and reinforce a given vulnerability, including actions by the state or its corporations with respect to alternative partner countries for the rival and exchange in items that affect the vulnerability of other items. Assessing these interaction effects is critical to understanding changes in a rival’s dependence and, in the final analysis, on the political
relations between the state and rival. For example, from 1936-1941, the U.S. exported crude oil and related refining equipment, but not synthetic oil technology to Japan. This reinforced Japan's domestic production base's dependence on crude oil through its import across two exchanged items and one non-exchanged item. Japan's oil import reliance on the U.S. in 1936 was roughly the same as in 1941 (i.e., 81.6% in 1936 and 82.1% in 1941), and therefore it alone would not capture this increase in Japanese vulnerability and dependence. Even if quantitative approaches assessed critical trade items like oil, they would still miss the political importance of related trade and non-traded items to changes in a country's dependence. This is, of course, starker when the necessary analysis of third country effects on exchange are taken into consideration.$^{965}$

Comprehensive assessment of all these matters is not simple, but it does lead to improved understandings about the purpose and effects of economic exchange. This dissertation was in part an effort to help the field better refine its concepts and measures of economic exchange. The most important conceptual clarification this dissertation has developed is the basic realization that exchange-related increases in the capabilities of a rival do not mean that the rival is subject to equivalent decreases in its capabilities with a

$^{965}$ Most quantitative methodologists in international political economy don't attempt related trade analysis, and instead rely on overall estimates of reliance or partner concentration, which render fairly useless findings (e.g., Gowa and Mansfield, "Power Politics and International Trade."). To be sure, some quantitative methodologists are attempting to rectify this problem, but they too do not assess the politics surrounding third country coordination of dependency. See Reuveny and Kang, "Bilateral Trade and Political Conflict/Cooperation." At least these efforts may bear fruit, whereas the methods of Mansfield can not. It's interesting to note that Mansfield and others conclude that interwar trade with rivals occurred because states simply were too confused about who their enemies were likely to be (i.e., multipolarity caused trade partner confusion). This is hardly accurate, nor is the contention of Copeland that because states under multipolarity don't know their likely enemies they trade with all other states to increase their power (i.e., liberal-realist fused need for trade due to its efficiency releasing properties from specialization). This dissertation demonstrates that U.S. trade with Japan was driven by its full knowledge that Japan was its likely enemy, and trade was maintained partly to shield allies, not because of structurally-induced myopia about who was the enemy. This finding likely applies to other interwar dyads and contemporary exchange as well. See Liberman for a related and inaccurate assessment of multipolarity, "Trading With the Enemy," pp.152-55.
cessation in exchange (i.e., Hirschman). Some exchange is not only cumulative in its effects on capabilities, but more importantly autonomy-enhancing (e.g., synthetic fuels, rubber). It is this exchange and its opposite (i.e., dependency-enhancing exchange), that properly frame the analysis of state and corporate preferences in exchange and the economic effects of exchange. In essence, exchange carries with it potential opportunity costs to one's autonomy and while a state may increase its capabilities, these are dependent gains.

Better qualitative analysis and conceptual definitions allow for sharper theoretical comparison and the results of this are evident in the U.S.-Japan, 1918-1941 case. It is unmistakably true that Japan was an economically vulnerable country due to its limited geography and natural resource base, even when its territories of Korea and South Sakhalin are taken into consideration at the beginning of the case. What mattered throughout this case was not that Japan was vulnerable, but rather who held this vulnerability--the U.S. or Britain. Bilateral political and economic relations exist within grand strategic environments encompassing many players, and the U.S.-Japan case was no exception. Japanese exchange was embedded within U.S. grand strategy, which partly conditioned the exchange in ways that are largely inexplicable by defensive realism (e.g., allowed material capabilities to accrue to Japan in the 1920s and late 1930s).

Because U.S.-Japanese exchange existed within overall U.S. grand strategy, increased Japanese threat perception did not always lead to reductions in exchange across the five case periods. It did generate, however, concern for exchange with Japan that achieved U.S. positional maximization as Japan made its strategic choice for war against the Soviet Union, China and/or the West. Exchange benefits were extended to Japan to
influence Japan’s choices and keep it from breaking out of its vulnerability to the U.S., and this necessitated increased gains to Japan as other countries ceased their exchange with Japan (e.g., Soviet pig iron and oil embargos in 1936, Australia iron ore embargo 1938). As a result of this larger strategic environment, the U.S. was concerned with controlling key resources throughout the region and in building effective counterweights to both Britain and Japan in Asia. Throughout all five periods of this case the U.S. acted: to increase its influence over Japan; to build a sovereign China friendly to the U.S., maximizing U.S. influence on the mainland against both Britain and Japan; and to obtain equal ownership rights to DEI oil resources and exclude Japan from owning those same resources.

What holds together the most crucial events during this case is the continual U.S. effort to increase its influence over Japan through economic exchange. U.S. economic leverage over Japan at the beginning of this case was very narrow consisting largely in the silk and cotton trade. But, in the years to follow the U.S. would use its broadening exchange with Japan to exercise direct influence over Japan’s domestic and foreign policies, while also maximizing its latent control over Japan by developing its vital oil vulnerability instead of allowing Britain to continue to hold that position. In fact, oil was the substantive link among the three foremost naval powers and the control of it was the subtext during all of the period’s naval arms negotiations. The U.S. was particularly motivated to break up the Anglo-Japanese alliance in the first period of the case, and in part, because Japan was benefitting from Britain’s control of DEI oil and the U.S. was not.

966. The most crucial events are also listed in Appendix C, but as noted there, they outweigh all other events in terms of evaluating the theories’ explanatory power.
The United States did not approve of the consequences of the Anglo-Japanese alliance. The political sundering of China, Japan's seizure and British recognition of Japanese claims to Pacific islands surrounding U.S. positions and U.S. exclusion from DEI oil development all rankled American leaders. As a result, U.S. threat perception of Japan was high in 1918 as was its concern for Japanese actions against China, Russia and even possibly the U.S. In response to the Japanese army's excessive expansion in Siberia, the U.S. acted upon Stanley Hornbeck's analysis from 1917 regarding Japan's vulnerability to a U.S. silk import embargo, and suspended cotton and silk trade licenses in November 1918. President Wilson waited two months before using the U.S. economic weapon of the day because Japan had just established its first civilian party politician as Prime Minister, Hara Kei. Wilson wanted to give Hara an opportunity to control his own army, but when this proved to take too long, Wilson acted decisively on the U.S.'s existing leverage over Japan to affect control over the Japanese army. When Hara re-established army control, Wilson immediately restored the trade licenses, thereby establishing the relationship between U.S. exchange benefits for what it deemed appropriate Japanese foreign behavior and rule by non-army elites in Japan.

This action is best explained by offensive realism precisely because of the intended effect of conditioning and then rewarding Japan's civilian government for its foreign policy behavior with U.S. exchange benefits. The contest for oil rights across the 1920s was also crucial to Japanese autonomy. The unsuccessful effort of Standard Oil to get more DEI oil concessions by using the threat of Japanese entry significantly affected the U.S.-Japan relationship in two important ways. First, because Royal Dutch Shell also used the fear of Japan to cause unrest in the U.S. by selling U.S. naval reserve oil to
Japan’s navy, the U.S. government fully understood the need to appear a reliable commercial partner to Japan. U.S. commercial reliability would make both Japan and the Dutch not worry about the consequences of decreased U.S. supplies of oil to Japan (i.e., greater Japanese demand on DEI oil). The British and Dutch simply would not grant the U.S. significant oil ownership in the DEI without the U.S. assuming the role of reliable supplier to Japan (i.e., no U.S. governmental supply shocks to Japan). This wrangling overlapped with the naval rivalry between the U.S. and Britain as the U.S. forced Britain to accept American parity with it in the aftermath of the failed 1927 Geneva talks.

Second, to prevent Anglo-American naval competition that would also cause Japan to increase its navy, Standard Oil was given increased oil concessions in the DEI in 1928. During the passage of the law enabling this action, Japan’s ability to obtain oil from California was called into question by the U.S. navy and in the press as it had been in 1920-1921. The State department oversaw the silencing of the U.S. navy because it jeopardized Standard Oil’s entry into the DEI. Arthur Young, Economic Adviser at the State department, noted that U.S. reliability in oil supplies for Japan was critical to its gaining entry into the DEI, and was therefore not to be compromised by any temporary concern regarding Japan’s oil trade with the U.S.. The U.S. was building its controlling influence position over all Asian oil matters in this action and establishing the precedent of coordinated action with the British and Dutch on oil. Anglo-American-Dutch cooperation in the DEI came at Japan’s expense through the cynical admittance of Japanese oil interests into the DEI at the same time the U.S. gained greater entry. The Japanese were given twice-prospected and worthless oil lands in a faint gesture of cooperation that only superficially masked Japan’s exclusion from ownership of

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productive DEI oil assets. More importantly, the relationship between the U.S., Britain and the Dutch was enshrined at this juncture for jointly managing Japan’s exclusion and dependence, and this rested on American oil supplies to Japan. Because U.S. trade in oil with Japan supported the exclusion of Japanese ownership of oil, U.S. commercial reliability was the handmaiden of Japan’s bilateral dependency maximization.

Anglo-American cooperation at the expense of Japanese relative capabilities was most pivotally displayed at the London Naval Conference in late March 1930. The U.S. financially coerced a divided Japanese government into signing the arms accord, which codified a higher level of American naval power and a Japanese freeze in its heavy cruiser force. The threat of non-renewal of Japanese government loans helped stimulate the financial moderates then in control of Japan into signing and submitting to a relative military capabilities decrease vis à vis the U.S. The loan was dutifully rewarded to the Japanese government in May 1930 and typified this part of broadened U.S. exchange with Japan in the post-Washington Conference period. The U.S. made large loans to Japan after 1923, but each one was reviewed by the State department for approval and many were rejected. The U.S. government repeatedly denied U.S. banks’ loan submissions for the Japanese army-related South Manchuria Railway Co. from 1923-1928. The U.S. also negotiated with the Japanese government, restricting the use of U.S. loans to the semi-governmental Oriental Development Company. The monies were agreed not to be used in Manchuria, Mongolia and the South Seas Islands. This demonstrated U.S. government policy to use exchange to influence Japan’s expansion, if not control it, and attempt to undermine the military within Japan’s domestic politics.
The U.S. managed loans into Japan to affect Japan's domestic factional competition, rewarding those actors affiliated with Japan's civilian rulers (i.e., the electric companies), denying gains to those affiliated with its imperial expansion and conditioning the government in the process to accept U.S. preferences regarding Japan's economic development and policies abroad. The majority of the loans that were made went to Japanese governments directly (i.e., national and prefectural government loans), and not to private economic actors, even those that accepted use restrictions. Because of this, this area of exchange is inconsistent with liberalism and marxism. In sum, the policy governing U.S. loans to Japan clearly demonstrates offensive realism because the U.S. used expanded exchange with Japan to attempt to gain greater influence and control over its policies and, in the London Treaty, its actual military capabilities. The fact that loans were extended at all contra-indicates defensive realism's prescription against allowing a rival to build up its material capabilities in a potentially mutually binding way. To then use the London loan to compromise those capabilities overtly, thereby stimulating Japan's balancing efforts against the U.S., is another more critical contradiction of defensive realism.

Japan would eventually react to the "corruption" of civilian rule and the paucity of gains in controllable resources earned through cooperation with the West by seeking those resources it needed through military action and political intimidation (e.g., Manchurian annexation of 1931-1932). In the quest for DEI oil, in particular, Japan began using more overt pressure in 1934 and the Dutch responded by shifting Japanese-acquired oil concessions to U.S. companies without the companies' knowledge. The U.S. government was aware of the imposition of its national corporations in the path of an
increasingly frustrated Japanese government searching for greater resource security. The U.S. accepted this position because it sought to increase Japanese vulnerability to U.S. oil influence. During the protracted negotiations (1934-1936) among Standard Oil, Royal Dutch Shell, the State department, the British Foreign Office and the Japanese government, the U.S. took the clear and unwavering position of not assisting Japan to acquire oil stockpiles or synthetic oil alternatives based on coal (i.e., allow it to increase its autonomy). The U.S. also rejected the oil companies' efforts to invoke the coercive powers of the state to threaten both Japan and gain control over the independent oil companies in California (i.e., U.S. Interior department embargo review). The British government continued to buckpass to the U.S. on confronting Japan's middling effort at nationalizing the petroleum industry beginning in 1934. For its part, the U.S. continued to force the issue back to the British as the U.S. was also doing in China during the silver crisis caused by U.S. purchases of ill-gotten Chinese silver from Japan and Britain.

Without understanding their role within Anglo-American bargaining for leadership in Asia, the companies grew increasingly frustrated in not achieving their preferences. And in December 1935, Standard Oil decided to threaten the U.S. by offering the Japanese synthetic fuel technology in lieu of complying with Japan's stockpile provision and market quota reductions. The U.S. took great exception to this offer and its accompanying statement supporting Japan's "making their coal supplies readily available for petroleum manufacture" whence "they would always have under their own control during an emergency a substantial source of constant supply." In response, the U.S. implicitly threatened Standard Oil's extensive U.S. army and navy contracts, but allowed them to make the offer to the Japanese to retain the U.S.
government position of not publicly denying Japan the autonomy it sought. The companies had made this offer before to the Mistui interests and were similarly rebuffed this time. Their offer was slighted, however, because the Japanese were no longer interested in seeking oil autonomy assistance from the Anglo-American interests, and instead, they were reaching out to the leading state in the field—Germany. Although synthetic fuels, and industrial and technical exchange more broadly, were not the only foundation of burgeoning German-Japanese relations, they did form a substantial part of it and contributed to the U.S. supplying oil and crude-related equipment to prevent Japan from falling into a full partnership with Germany. By early December 1939, it was clear to the U.S. that Germany would no longer be a potentially reliable partner to Japan’s oil and chemicals autonomy efforts. It was at this point that the U.S. began to take decisive measures to prevent any Japanese autonomous capability from emerging, and in so doing, the U.S. removed the thin veneer of its trade reliability (e.g., recalling Associated Oil’s engineers from Japan, ending all aviation gasoline technical assistance and equipment supplies).

American tactical supply to maintain Japan’s strategic vulnerability to the U.S. is more consistent with offensive realism than all other theoretical perspectives, and was the dominant explanation of all exchange relations from 1937 until their cessation at the end

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967. This account differs markedly from Irvine Anderson’s central work on the same subject. His work has been relied on by most other scholars and is flawed in its overly generous treatment of corporate machinations and failure to properly assess Hornbeck’s pivotal role in preserving U.S. maximum influence over Japan, Britain and the oil companies.

968. This example properly constructs state motivation for exchange under multipolarity. Binding rivals until the state can maximize its influence over their capabilities is the primary motivation and explains far more than do structural-rationalist propositions of multipolar trade for one’s own economic benefit. Liberman held, “the security implications of relative economic gains should be lower in multipolar systems, even among adversaries...policy makers will tend to focus on prosperity or political objectives in formulating trade policy.” Liberman, “Trading with the Enemy,” p.155.
of July 1941. U.S. supply of large amounts of iron and steel scrap and aviation gasoline in 1940 support this interpretation because U.S. exchange raised the costs of adjustment to Japan when trade ceased and maintained U.S. control over when and why conflict would start (i.e., U.S. oil embargo and Japan's decision clock on its stockpiles begins). Australia stopped Japanese firms from mining iron ore and ended all exports to Japan in May 1938, while the Soviet Union ended pig iron shipments in 1936 due to Japan's budding alliance with Germany against it. Malaya and the Philippines similarly restricted iron ore shipments to Japan, and ended them altogether in early 1941. The U.S. observed all of these trends and only allowed U.S. shipments of iron and steel scrap to Japan to reach large volumes from early 1937 forward.

Filling the gap from other suppliers increased Japan's adjustment costs in terms of shipping and resource usage to produce steel when exchange ended. U.S. supply to Japan in these items reinforced its inefficient steel production base and the much more costly adjustment replacing U.S. iron and steel scrap with raw iron ore and coking coal. The U.S. then used this vulnerability to condition Japan's advance in Asia while Britain battled Germany in late summer and fall 1940 (e.g., partial scrap embargo in July and then full iron and steel scrap embargo September 1940). The U.S. maintained its control over the more critical oil supplies to Japan through coordinated denial of its demands in the DEI in the fall of 1940 and through the tanker shortage of early spring 1941. These actions increased Japan's dependence on the U.S. and U.S. control over Japan's supply from all other countries (e.g., Persia, Mexico), such that, by summer 1941, the U.S. had maximized its influence and control position over Japan.

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969. Paradoxically, or perhaps not, the scrap embargo would incent Japan's southern advance just as would the oil embargo because the iron ore was in Malaya and the Philippines.

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The U.S. supplied Japan with aviation gasoline in the immediate period leading up to this concentrated dependence, but supplied less and less crude and fuel oil in an effort to limit Japan's stockpiles to approximately a little over one year's wartime operational usage. The U.S. assumed the destruction of the DEI would render those assets barren for at least a year and its war strategy of delay in the Pacific would neatly coincide with dwindling Japanese fleet fuel reserves, and therefore decreased power and mobility in Japan's military. It can not be overlooked, however, that the U.S. engaged Japan in tactical supply and dissembling negotiation regarding possible increases in that supply primarily to buy time for its own build up. Its large-scale re-armament program fully began only in summer 1940, and President Roosevelt was not in a hurry to enter the war while Germany, the Soviet Union and Japan were still preparing their advances.

U.S. grand strategy preparing for entry into the global war caused it to direct its bilateral exchange with Japan to maximize the U.S. position when it entered the war; first by delaying the war until U.S. capabilities were increased and, second, by minimizing Japan's wartime capabilities through the same process of delay and minimal supply that only sustained its current consumption. The U.S. publicly declared that it continued supplies to July 1941 to prevent conflict from spreading to Southeast Asia, where most of these resources lay and Japan's full advance was finally decided upon in early July 1941. This declaration was undoubtedly true, but the U.S. also ensured that it controlled the final decision on when Japan's supplies would be cut and the conduct of negotiations drawing out Japan's calculated lunge for DEI oil and autonomy through the attack on the U.S. at Pearl Harbor. The U.S. held this position because it forced its way into the DEI in the 1920s and forged Anglo-American strategic coordination under American plans (e.g.,
non-defense in the Pacific and partial U.S. Fleet transfer to Atlantic under ABC-1). By reviewing U.S.-Japanese economic and strategic relations over a longer time period than most works, this dissertation has better specified the economic and security nexus among the U.S., British and Dutch over ownership of the coveted DEI oil, and thus the political authority over its use as a weapon against Japan.

The U.S. bargained hard against the British and Dutch to build this position and the consequent ability to determine when to use it to affect Japan's decision for war. This relationship was clear to decision makers by the early 1920s, and absent technological or other oil territory breakthroughs, holding it allowed the U.S. to execute its grand strategy and not be forced to follow Britain's strategy of defending southeast Asia. U.S. war plans called for the abandonment of southeast Asia in the early stages of the war, and only changed in summer 1941 with an inadequate military bolstering of the Asiatic Fleet and the Philippines due to U.S. army and navy logrolling.\(^70\) It is still not known why the President sanctioned a half-hearted defensive build up in the Philippines that he knew as early as 1923 could not be defended given a U.S. Fleet advantage then of 5:3, let alone the parity or partial Japanese advantage that existed at the start of the Pacific war.\(^71\)

It is clear, however, that the U.S. did not defend its most substantial investment stake in Asia, Stanvac's direct investments in the DEI. The marxist and liberal propositions regarding government policy defending capital stakes abroad are simply not tenable in this case.\(^72\) Similarly, the roughly equivalent investment stakes of the oil and


\(^{71}\) Evans and Peattie, Kaigun, pp.351-55.

\(^{72}\) Even marxist analysts of this case agree that the U.S. government's behavior can not be explained under their perspective. See Andrew Rollings, “The State, Capital, and the Structure of the World System: 487
auto companies in Japan did not generate equivalent State department intervention on their behalf. The auto companies were actually under greater Japanese government threat of losing their entire businesses unlike Standard’s threatened reduction in market quota. Because the U.S. government did not intervene nearly as aggressively for the auto companies, liberalism’s contention that the more important domestic interest group determines state policy was not evident in this case.

It is certainly valid, however, that corporate actors were not supplicants to U.S. interests, because they did materially affect state relations in pursuit of their own objectives. The oil companies in particular used their control of resources and technology to push their agendas vis a vis all states involved. As early as 1920-1921, the oil companies deliberately played on the threat perception of the states involved, and rendered the eventual settlements that discriminated against Japan a source of tension that persisted to the war. Japan’s access to DEI and U.S. oil may have appeared stable, but its control or ownership of oil producing lands never was allowed to materialize. The companies laid this government preference bare for the Japanese to see, despite DEI authorities’ attempts to legitimize U.S. entry and Japanese exclusion. National City Bank materially affected Japan’s economic stability during the Yen-dollar crisis of 1930-1931, and its actions as a panicky financial institution require further analysis of the role of

corporations within a rival's economy. It may very well be that they do not promote or achieve the stabilizing and mutually beneficial self-interested role often ascribed to them by liberals.\footnote{In fact, it may be that corporate agitation occurs precisely when state competition is also increasing, and therefore exacerbates that state competition. Perhaps corporate fear for lost business due to political tensions causes them to act more rashly to try and secure those business interests. It does appear to correlate temporally, and therefore should be reviewed more critically elsewhere (e.g., Taiwanese business within U.S., Japan and China competitive vortex).}

8.2 Relevance to and Implications for Previous Scholarship

Most scholarship in political science investigating Japanese economic vulnerability and its effects on Japan's strategic choices fails to first determine who Japan was vulnerable to and why. This is true of the major works by Charles Kupchan and Jack Snyder, and the lesser works by Peter Liberman and Dale Copeland.\footnote{More unfortunately, most of these works begin their analyses after 1930, and therefore, miss the creation of the underlying structure of Japan's vulnerability. See Charles Kupchan, The Vulnerability of Empire, (Ithaca, NY: Cornell University Press, 1994), pp.342-343; Snyder, Myths of Empire, pp.116-120; Peter Liberman,"The Offense-Defense Balance, Interdependence, and War," in Mansfield, et al., Power and the Purse," pp.82-86; Peter Liberman, Does Conquest Pay? The Exploitation of Occupied Industrial Societies, (Princeton, NJ: Princeton University Press, 1995), pp.99-100; Copeland, “Economic Interdependence and War,” p.170, footnote 42.}

As noted earlier, the most important part of Japan's economic vulnerability shifted from Britain to the U.S. as a direct result of America's entry into the DEI in 1928 and growing Dutch realization that U.S. power mattered more to its security than British (e.g., in naval force protection and ability to force Japan south with U.S. oil embargo against Japan). Because reliable supplies of U.S. oil to Japan were part of the entry price with the Dutch, the U.S. assumed this position, and in fact, preferred holding Japan's majority oil supply as an expanded avenue of influence over all the states involved. The U.S. preferred to hold Japan's vulnerability because the consequences of the British holding it were Chinese.
depredation and U.S. exclusion from the most important source of oil in Asia, not to mention British sanctioning of Japan's strategic advance against the U.S. (e.g., mandated islands recognition 1919).

Because the U.S. viewed the Anglo-Japanese alliance as anathema, it broke it up by forcing the British to recognize that U.S. power was more important to the security of its long-term interests. U.S. competition with Britain for influence over both Japan and China continued across the entirety of the case (e.g., Churchill's closing the Burma Road). As a result, the U.S. became more committed to building a sovereign China against both Britain and Japan. U.S. support did not come at the expense of U.S. grand strategic interest, however. For example, the U.S. did not support Chinese stability when it served U.S. interests to foment Japanese advance against British interests in China (e.g., silver crisis 1934-1935, no support of British entreaties for joint notes or military shows of force after July 1937). These purposeful non-actions and manipulation of all three countries ended any possible restoration of substantive Anglo-Japanese accord, and thereby maximized U.S. influence vis a vis all of them. Nonetheless, U.S. support for a stronger China began in full measure in 1928 and accelerated after the Manchurian invasion (i.e., Arthur Young's appointment to China in 1928, warplane and pilot assistance in 1932). U.S. aircraft assistance, in particular, was the focus of much of Japan's ire in the Amau declaration of April 1934, in which Japan declared all of Asia its rightful economic domain and its policy to be the "defeat of the foreign" presence in China. For these reasons, to exclude as these scholars do, U.S. policy in China and its
effect on Japan's decisions for annexation of Manchuria and full war in 1937 is a gross oversight in their causal analyses of both Japan's domestic and foreign policy.

More generally, Kupchan, and to a lesser extent Snyder, discount the role of external actors in affecting Japanese economic vulnerability, domestic factional competition and strategic decisions for war or peace.975 For example, Snyder claims, "only after 1937 did the costs of the strategy of autarkic empire outweigh the benefits, owing to the military quagmire in China and the cannibalizing of the light industrial, export-oriented sector of the economy."976 Japan's light industrial, export-oriented sector was its cotton piece goods sector, and it was rendered less than fully effective and worthy of cannibalization because of U.S. and other countries' restrictions on that trade (i.e., U.S. "rationing" of Japanese cotton goods imports to Philippines and the U.S. proper, while raising the price of Japanese raw cotton imports). Snyder notes this factor generally, and dismisses it, contending instead: "Japan's economic problems in the late 1930s were almost entirely caused by the conscious shift from a trading-state strategy to a strategy of autarky and imperialism."977 Why did Japan make this conscious choice for empire by force of arms?

This dissertation has demonstrated that the benefits to Japan from cooperation with the U.S. after the Washington Conference were not increasing Japanese autonomy even though they increased its material production. In fact, increased exchange with the

975. Kupchan states, "the policies of continental expansion and military buildup that elites pursued during the early 1930s were the result primarily of these domestic changes, not of shifts in the external threats facing Japan...the resurgence of Japanese imperialism that occurred during the first half of the 1930s was more the product of opportunity and domestic political developments than a response to increasing international threats." Kupchan, Vulnerability of Empire, pp.301,304.
976. Snyder, Myths of Empire, p.115. More pointedly, Japan's economy grew at an even faster rate after 1937. See Cohen, Japan's Economy in War and Reconstruction, p.6.
977. Snyder, Myths of Empire, p.119.
U.S. led to further erosions of Japanese autonomy. This was evident in the political loans from the U.S. to Japan and the loss of any possible ownership of real oil production in the DEI to an expanding U.S. in 1928. These exclusionary and politically intrusive actions by the U.S. culminated in the London Naval Treaty financial coercion and forced naval reductions on Japan, which were purposefully orchestrated by the U.S. and very different from the comprehensive understandings reached at the Washington Conference (e.g., understandings on China). This action galvanized large sections of the Japanese navy and helped bring about the end of civilian rule in Japan. It was the Japanese navy's attacks on Shanghai in January 1932, that eventually confirmed for the U.S. that Japan's military as a whole was bent on expansion, not just the army. Japan's navy continued its plans for armaments expansion and territorial advance to the south over the rest of the period, and the U.S. reacted to these moves with tactical supply of scrap iron and steel and oil up through July 1941. The U.S. certainly did this to shield allies; but more importantly, it maximized U.S. power and influence over the coming war (e.g., the U.S. waited for Britain to agree to its terms under ABC-1 and the two ocean navy buildup to accelerate).

Snyder's analysis is fundamentally flawed with respect to precisely those external influences that conditioned Japanese domestic factional competition and foreign expansion across the whole interwar period. For example, Snyder held, "only when military ventures, like the occupation of Siberia, had become obvious quagmires was the military-bureaucratic cartel reigned in."978 This supposition is historically inaccurate, because it was the purposeful U.S. cotton and silk license embargo in mid-November

978. Ibid., p.136. Other factual errors include the assertion that loans from Washington dried up in 1937, when they were in fact ended in 1932.
1918 that caused Hara to reign in the army and for the army to abide this outside economic pressure from the U.S.. Thereafter, it was the promise of economic rewards from the Washington Conference that earned their full withdrawal from Siberia and set the rest of the period’s parameter of U.S.-Japanese exchange gains for compliant Japanese foreign policy. Even more critically, the expansion in Siberia and Russian reprisals at Nikolaievsk gave the Japanese army and navy the pretext for seizing the valuable oil and coal deposits of North Sakhalin. Japanese expansion was paying for itself early in the period, not causing a “quagmire.”

Both Snyder and Kupchan contend that a general Japanese economic vulnerability accelerated only after its war on China began in July 1937. Japan’s vulnerability and dependence on the U.S. did expand after the China war began, but did not do so strictly because of increased resource needs due to the China war. It also did not do so in a simply measured or aggregate way, as Japan’s total U.S. trade as a percentage of its GDP decreased after 1937 and its imports from the U.S. did not reach their 1937 value again. Japan’s vulnerability to and dependence on the U.S. increased because the U.S. came to control all of Japan’s oil supplies through a finally effective concert with Britain (i.e., Chamberlain replaced with Churchill, and controlled DEI negotiations and tanker shortage). Furthermore, Japan’s outreach to Germany caused Soviet pig iron, oil and other materials exports to Japan to end in 1936, before the China war began. Australia ended its iron ore shipments to Japan in 1938, and the amounts sent from Malaya and the Philippines were carefully monitored, even though they contributed 57% of Japan’s iron ore imports in 1940. The U.S. merely filled these suppliers’ gaps with scrap iron and
steel exports to Japan and did so to delay war for its own ends, despite its public
pronouncements that it did so to prevent war from spreading south. 979

Perhaps the most troubling assessment from the scholars cited above, is their
universal contention that Japan’s choice for war with the U.S. was “irrational,” and
driven by army-navy logrolling which yielded a strategically deficient selection choice
for war with a vastly more capable U.S.. This assessment of the conflict is flawed. 980 To
be sure, Japan was making deficient strategic choices in 1939, courting war with the
Soviet Union, Britain and the U.S., while fighting China. However, after the stunning
defeat at Nomonhan, Japan reigned in its “irrational overexpansion,” and decided on a
southern advance strategy against only Britain and the U.S.. 981 This was codified in the
Soviet-Japanese Neutrality Pact of April 1941, and Japan kept its bargain with the Soviets
after Germany attacked it. With the U.S. scrap iron and steel embargo of September
1940 and the likely continuance of crude and fuel oil import declines, if not embargo at
any time the U.S. might choose, Japan made a rational choice for war to procure the
resources of southeast Asia (i.e., DEI oil, quinine, and Malayan and Philippines iron ore
etc.).

The fact that Japan made this choice under the realistic assessment that they only
had a slim probability of success in no way renders their choice irrational. Japan’s choice
was made on the basis of material interests and an accurate assessment of its declining

979. This does beg the question of whether the U.S. fully understood that its export cessation of scrap iron
and steel would further impel Japan south. Japan had already taken northern Indochina at this point, but the
scrap embargo furthered their incentive to go south.
980. For related analyses see Christopher Thorne, Allies of a Kind: The United States, Britain and the War
against Japan, 1941-1945, (New York: Oxford University Press, 1978), pp.5-7,52-4,83-5; James Morley,
School of Economics, 1989), pp.4-7
981. Liberman, Does Conquest Pay?, p.100.
relative capabilities vis a vis the U.S., and not on the basis of myths or ideology employed for domestic mobilization purposes.\textsuperscript{982} The stark choice for Japan was either fulfill the will of the United States or act on its own initiative. Japan risked its empire to obtain the autonomy it sought earlier through cooperative action with the U.S.. Japan made the rational choice for peace with the Soviet Union and war with the U.S., because the Soviets gave Japan the assurances it sought for northern security and greater oil from North Sakhalin, while the U.S. continued incremental oil supply embargos to affect Japanese compliance with U.S. preferences in Asia. This was a real competition for control over resources in southeast Asia, the fate of China and the Western Pacific more broadly. U.S.-Japanese competition over these matters began immediately after WWI and not after the Manchurian invasion in 1931, when the possibility of peaceful resolution began to decline. In the end, it was not amenable to negotiation on either side’s terms or settlement by peaceful means.

8.3 Realist Exchange Theory, Application to U.S. Interwar Policy and the Prospects for a Realist Peace

This case and most others do not comport with defensive realism’s central tenets because states are not interested in the mere maintenance of a relative material capabilities balance through narrow exchange (e.g., U.S. extensive trade and investment

\textsuperscript{982} It would be more accurate to argue that the U.S. made strategically deficient decisions in 1941 due to army-navy logrolling and inaccurate and biased assessments of its relative power vis a vis Japan. Inept U.S. bolstering of army forces on the Philippines and somewhat myopic and culturally biased assessments of Japanese military capabilities by U.S. army and navy leaders caused tremendous losses in the Philippines. See Wilmott, Empires in the Balance: Japanese and Allied Pacific Strategies to April 1942, pp.182-191; Wolthus, “The United States Foreign Policy towards the Netherlands Indies,” pp.304-6; Morton, The War in the Pacific, pp.97-101.
benefits in contemporary U.S.-China relationship). States seek the maximum of influence possible over others and use exchange and expanded exchange to achieve that influence and latent control position. What they do once they have a controlling influence position is a different matter. States may abuse their influence position (e.g., Stimson's financial coercion of Japanese moderates at London), or allow it to help fulfill broader grand strategy more subtly, gaining increasing leverage over rivals and binding allies to one's grand strategy. Defensive realism slights these purposes in exchange because it accepts and adopts a liberal view of the effects of exchange without stating so explicitly. Defensive realists call for limited exchange with a rival in general and decreases in exchange if state threat perception increases because they assume exchange has a capabilities enhancing effect.

Defensive realists, like liberals, assume exchange has a unidirectional positive effect on capabilities, and therefore must be limited and decreased with threat increases in order to maintain state position. If we know that the purposes of economic exchange can be as varied as creating or cementing alliances to rendering another state bereft of trade through embargo or principled sanctions, why do we not question whether the effects of exchange might vary as well? It is this dissertation's contention that, of course, exchange effects can vary and exchange can be used to create vulnerability in another country despite its receiving increased material capabilities. This objective may, in fact, require

983. Waltz expanded defensive realism's economic exchange propositions to the nuclear era only recently, contending: "because states with second-strike forces cannot convert economic gain into strategic advantage, an important part of the relative-absolute gains problem is negated." This means, of course, that states without a secure second strike should be doubly circumscribed from receiving exchange gains. See Waltz, "Emerging Structure of International Politics," p.72.

984. Decreased exchange in response to increased threat may be only a symbolic act for offensive realists; registering diplomatic displeasure that is not materially different from recalling an ambassador. Defensive realists assign only one purpose to decreased exchange and therefore betray their underlying assumption of the effects of exchange and state purpose in acting upon them.
the extension of seemingly beneficial exchange to another country in order to build up its reliance, vulnerability and long-term dependence on the state. This proposition builds on Albert Hirschman's seminal work on dependency maximization through trade benefits extension, but seeks to broaden the analysis of state purpose in exchange.\footnote{Hirschman removed purposeful state intent from his analysis by noting that Germany made lesser countries in its periphery dependent, but not as a result of a "consciously worked out...master plan." Economists don't like to assess decision maker intent and motivation, political scientists must. Hirschman, National Power and the Structure of Foreign Trade, p.35.}

A state will exchange with its rival for three principal reasons. First, it will seek to obtain an influence position by increasing the rival's reliance on the state, and this may cost the state some relative capabilities (i.e., the state may pay for a position in the rival). Second, a state will use exchange with a rival to introduce economic inefficiencies and resource diversion in the rival by making it rely on supplies, components or parts available only from the state or other state-controlled territories. For example, sending technologies and equipment to a rival may increase the rival's production for a time, but it may also render that production valueless if key components become unavailable through state cessation of exchange. This was visible in several exchange areas in the U.S.-Japan case (e.g., synthetic oil fuel pumps) as was the resource diversion function in U.S. export of gold mining and California crude-based refinery equipment to Japan.\footnote{This was also evident in the planning by Hornbeck in early 1941 to repeal the aviation gasoline embargo and get Japan over-invested in refineries which the U.S. would negatively control.}

Third, despite threat perception changes, the state will create and then maintain exchange with the rival to gain intelligence on the rival's intentions. It is precisely because the state holds a rival's supply lines in some items that it can learn that the rival...
is planning actions against the state's preferences and anticipating a negative response (e.g., import demands surge prior to and during rival's actions antithetical to state preferences). This was repeated throughout the U.S.-Japan case with cotton import demand surges in 1931, scrap iron and steel in early 1937, and aviation gasoline in 1940. Each time the U.S. observed this demand and assessed its response options, and would not necessarily have had this foreknowledge without the exchange relationship. Although these propositions are inductively verified in the U.S.-Japan case, they are not applicable only to that case and offer an opportunity for theory building and testing that will improve our understanding of the purpose of statecraft and the processes in international exchange.

The core premise of realist exchange theory holds exchange to be necessary to the creation of influence, the garnering of intelligence and possibly the control of a rival's capabilities. Without a basis to exert one's will upon and control over another, there can be no relative power maximization. In order to have power over another, a state must have position within and around its object. Economic exchange can generate this position and provide an avenue for pursuing control over others and one's grand strategic environment. For this reason it should properly form a central aspect of the analysis of state objectives. To date realists have been uncomfortable with this basic proposition.

As detailed earlier in the theory review, Mearsheimer and Layne fret that economic

987. It was precisely because the U.S. did not act publicly on traded goods as it had in 1918 that Japan was falsely led to believe trade with the U.S. could and should continue despite Japanese behavior (e.g., Japanese outrage at U.S. oil shipment to Soviet Union in August 1941). This does not validate, however, Copeland's proposition that negative expectations of future trade caused conflict in late 1940-41. Japan had false expectations of trade continuing and did understand that trade with the U.S. was politically conditioned by the U.S. government and would change in response to their behavior against China and southeast Asia. Trade does not exist independent or a priori of political authority. Copeland's analysis would have been stronger if he had based it on Japan's negative expectations of ownership of vital resources, instead of only the trade in them.
exchange compromises the state’s position.\textsuperscript{988} There is no basis for a realist willingly to reduce the importance of exchange as a lens onto and lever over the intentions and autonomy of others. Other state-centric scholars have missed this as well. Critiquing Morgenthau, Stephen Krasner held: “Power for what is always the puzzling question. The clearest answer is: power to protect the core objectives of the state, its territorial and political integrity.”\textsuperscript{989} Morgenthau clearly stated the purpose of power and its maximal pursuit: the control over the minds, actions and autonomy of others, not the defense of one’s own territory. Because of his narrow assumption of state purpose, Krasner asserts U.S. state preferences are, first for security of its own supply in critical raw materials, and then, competition among private actors for lower prices in these goods.

Stanley Hornbeck clearly negated this preference ordering in the 1920s. After the denial of U.S. company expansion in the DEI in 1920-1921 and the use of the fear of Japan to obtain private commercial advantage by both Standard Oil and Royal Dutch Shell, Hornbeck called for the oil companies to end their competition and manage the markets jointly. Hornbeck pressed for American entry to control Anglo-Japanese supply for more than a concern for U.S. security of supply, which was never in jeopardy given U.S. resources. The competition with Britain to control the world’s oil territory had to do with control over the political power that would flow from manipulating the trade in this resource to other countries, not to oneself. With the pursuit of power comes the pretension of principle to justify its acquisition and employment. Sometimes this is made


\textsuperscript{989} Krasner, \textit{Defending the National Interest}, p.41.
transparent. For example, Anglo-American bargaining led to the Red Line Agreement in the Middle East and Hornbeck's infamous quip:

> from a practical standpoint first-comers must enjoy preference over subsequent applicants. It cannot be expected that equal commercial opportunity can be extended throughout an indefinite period of time.\(^9\)

Hornbeck acted upon this reality when the U.S. was admitted into the DEI in 1928 and Japan was granted the equal commercial opportunity to squander its capital, but not to obtain concrete ownership of oil-producing assets. The relationship established from 1928 forward was not a narrow securing of one's own supply, but rather the coordinated denial of independent supply to Japan based on U.S. supplies going to Japan. This secured Japan's dependence on the U.S. and ultimately U.S. control over Anglo-American policy in Asia. The U.S. did nothing but reinforce Japan's critical oil dependence until Japan began its alliance negotiations with Germany in 1936. Only at that time, did President Roosevelt seek a proposal for granting Japan and Germany assured "access" to necessary materials, but still not ownership or control of them. This internal review was quickly dropped after Japan's buildup for and subsequent attack on China in July 1937.

None of the foregoing analysis of U.S. policy should be construed, however, as concluding that the U.S. acted illegitimately toward Japan after its navy attacked Shanghai in January 1932. After these attacks, America could choose only one path in opposition to Japan's militant expansionism and the rising threat of the totalitarian states. As noted in the summary section for the periods 1918-1933, there may have been an

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9. Stanley Hornbeck, February 1924, quoted in, Hogan, Informal Entente, p.182. This demonstrates the need to follow Hans Morgenthau's advice at least to question, if not generally to reject, statesmen invocations of principles as Hornbeck and Roosevelt were wont to do.
opportunity to forestall Japan’s army-navy bandwagoning in military expansion against China in 1932 and later across Southeast Asia. If the U.S. had sought an affirmative place for Japan in the DEI oil deal of 1928 or shortly thereafter, there might have been a stronger pro-U.S. naval element in Japan to reign in the army and accept the London Treaty. This is a tenuous counterfactual, but frankly the only one this dissertation has uncovered for establishing a possible peace in Asia in the interwar period.\textsuperscript{991}

Some Japanese control of DEI oil instead of merely continued access to it might have provided a substantive basis for cooperative relations that declined precipitously after the London Treaty.

To achieve a realist-based peace, at a minimum, the raw materials foundations of state economic and military power have to be shared with rivals to a significant enough degree to remove them from military contention. This seems an obvious proposition in the post-WWII era (e.g., European Coal and Steel Community for Franco-German iron and steel cooperation), but appears meaningful enough to warrant continued consideration. This is a difficult proposition because states maximize influence precisely through control of these resources as well as through critical technologies and finance, and are therefore reluctant to lessen their influence positions. Additionally, the problem in securing a material basis for peace is that states often don’t or won’t control these resources directly. Instead, they may allow private companies to control these resources and related technologies. States may believe that corporate cover for state policy is expedient and their use of corporations as pawns works to their positional advantage, but

\textsuperscript{991} Of course, it is hard to dismiss President Hoover’s role in not confronting Japan from fall 1931 through the end of his term in early 1933. A demonstration of some economic cost to Japan before January 1932, might have induced caution into the more economically vulnerable Japanese navy, instead of the non-action inducing its opportunistic bandwagoning.
it is an often shaky and transparent foundation. Relying on private corporations means empowering precisely these self-interested and self-serving actors who will serve themselves first. In defending their interests, private corporations are likely to pursue actions that destabilize state relations and mutual threat perception. This was evident with the oil companies' threats throughout the U.S.-Japan case, and in National City Bank's speculation against the Yen. This is equally evident in contemporary international relations (e.g., Loral Space Development Corporation's technical missile assistance to China 1994-95). The state can't rely on private actors creating transnational ties of peace, because they often exploit state fear and exacerbate state conflict in pursuit of their own agendas; or worse, they may actually be so emboldened as to change state relative power by directly assisting the rival. It would be better for a state to seek direct exchange with a rival's government, even its most recalcitrant faction (e.g., the Japanese army), in areas that directly benefit the rival's autonomy and therefore both its perception of its own security and the state's intentions.

The tension between achieving this and the conduct of offensive realist statecraft lies precisely in the reliance on self-serving corporations as exchange intermediaries with a rival. Influence-maximizing statesmen always prefer the plausible deniability that comes with private companies' actions that serve the state's interest in compromising the rival's autonomy. Influence maximization may founder, however, on the shoals of the self-interest of private actors, forcing the state to reveal its true intent of controlling the rival's autonomy.
APPENDIX A

- Causal Model for Theory Evaluation
- Exchange Instrument Characteristics
- Theory Hypotheses and Observable Implications
Causal Model for Theory Evaluation

<table>
<thead>
<tr>
<th>Independent Variable</th>
<th>Independent Variable</th>
<th>Dependent Variable</th>
</tr>
</thead>
<tbody>
<tr>
<td>Threat Perception</td>
<td>+</td>
<td>State-Market Actor Led Exchange</td>
</tr>
<tr>
<td>Key Factors:</td>
<td>+</td>
<td>Key Factors:</td>
</tr>
<tr>
<td>State Policymakers'</td>
<td></td>
<td>Convergence and</td>
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<tr>
<td>Perceptions of</td>
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<td>divergence in state and</td>
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<tr>
<td>Aggressiveness of</td>
<td></td>
<td>corporate exchange</td>
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<tr>
<td>Intensions, and</td>
<td></td>
<td>preference; state and</td>
</tr>
<tr>
<td>Territorial and</td>
<td></td>
<td>corporate methods for</td>
</tr>
<tr>
<td>Economic Expansion.</td>
<td></td>
<td>achieving preferences; actors</td>
</tr>
<tr>
<td>Values: Increasing, Decreasing, Static.</td>
<td></td>
<td>engaged in rival.</td>
</tr>
<tr>
<td>Increasing:</td>
<td></td>
<td>Increasing:</td>
</tr>
<tr>
<td>Rival territorial</td>
<td></td>
<td>Rival restraint or</td>
</tr>
<tr>
<td>expansion; offensive</td>
<td></td>
<td>reduction in territorial expansion,</td>
</tr>
<tr>
<td>war plans/exercises; offensive force</td>
<td></td>
<td>war plans/exercises; arms control agreements;</td>
</tr>
<tr>
<td>buildups; military clashes; elite</td>
<td></td>
<td>military buildups (i.e., troops and</td>
</tr>
<tr>
<td>statements of hostility; hostile</td>
<td></td>
<td>weapons); elite statements of</td>
</tr>
<tr>
<td>factions advancement. State alliance</td>
<td></td>
<td>cooperation/friendship; and policy</td>
</tr>
<tr>
<td>formation/expansion or war</td>
<td></td>
<td>alignment with state preferences.</td>
</tr>
<tr>
<td>plans/exercises vis a vis rival.</td>
<td></td>
<td>State alliance, war plans/exercises</td>
</tr>
<tr>
<td>Decreasing:</td>
<td></td>
<td>Decreasing:</td>
</tr>
<tr>
<td>Rival restraint or</td>
<td></td>
<td>Rival restraint or</td>
</tr>
<tr>
<td>reduction in territorial expansion,</td>
<td></td>
<td>decrease in territorial expansion,</td>
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<tr>
<td>war plans/exercises and force</td>
<td></td>
<td>war plans/exercises and</td>
</tr>
<tr>
<td>buildups; arms control agreements;</td>
<td></td>
<td>force buildups (i.e., troops and</td>
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<tr>
<td>force withdrawals (i.e., troops and</td>
<td></td>
<td>weapons); elite statements of</td>
</tr>
<tr>
<td>weapons); elite statements of</td>
<td></td>
<td>cooperation/friendship; and policy</td>
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<tr>
<td>cooperation/friendship; and policy</td>
<td></td>
<td>alignment with state preferences.</td>
</tr>
<tr>
<td>alignment with state preferences.</td>
<td></td>
<td>State alliance, war plans/exercises</td>
</tr>
<tr>
<td>Static: no discernible movement in either direction.</td>
<td></td>
<td>decrease.</td>
</tr>
</tbody>
</table>

Rival's Bilateral Dependency

- Dependence
  - Autonomy

1 The State means state officials and policy coordinating committees and Market Actors refers to large corporations, particularly Banks and Industrial companies (e.g., manufacturing, energy, communications multinationals).

2 The Rival's dependence on the State from their bilateral exchange.
Exchange Instrument Characteristics: Material Capabilities and Autonomy Effects; Influence Position Utility

Dimensions: relative value (cumulative, transferable gains); actors involved; ease and costs of severance (partner-commodity concentration); and control

<table>
<thead>
<tr>
<th>FDI:</th>
<th>High effect on capabilities, extent depends on sector invested in (e.g., manufacturing v. extractive industries) and technology transfer; gains are cumulative; actor discrimination in target is possible; control is low as is ease of severance.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Influence position when FDI creates intensive specialization in target, high export-orientation and value of production, or when target's major industries are controlled (e.g., communications, computer networks). Least influence when FDI is trade-substituting, serving target consumer market.</td>
</tr>
<tr>
<td>Trade:</td>
<td>Variable effect on capabilities, depends on items traded (e.g., raw materials, technology or textiles); gains can be cumulative (e.g., technology) and transferable with trade surpluses; actor discrimination in target is possible; control is high as is ease of severance.</td>
</tr>
<tr>
<td>Aid:</td>
<td>Little effect on capabilities; gains are not cumulative, but are transferable; actor discrimination in target is possible, remains largely within target government; control is high as is ease of severance.</td>
</tr>
<tr>
<td>Loans:</td>
<td>Variable effect on capabilities, depends on size of loans; gains are transferable and can be cumulative if loans are large; actor discrimination in target is possible (e.g., core supporters or government factions); control is low, absent use provisions; and ease of severance depends on size of loans to the state.</td>
</tr>
<tr>
<td>Bonds/Securities:</td>
<td>Variable effect on capabilities, depends on size of bonds/securities; gains are transferable and can be cumulative if large; actor discrimination in target is possible; control is low, absent use provisions; ease of severance is high as costs are born by investors, not sending government.</td>
</tr>
<tr>
<td>Monetary Assets/Currency Values:</td>
<td>Variable effect on capabilities, depends on transfer of reserve assets and currency value changes; gains can be cumulative if transfer reserve assets (e.g., gold); actor discrimination in target not possible beyond government; control is low, ease of severance is high.</td>
</tr>
<tr>
<td></td>
<td>Influence position when target's currency reserves are largely sending state's currency or when ability to pressure target's currency value, depreciating it.</td>
</tr>
</tbody>
</table>
Defensive Realism

<table>
<thead>
<tr>
<th>Hypotheses</th>
<th>Observable Implications</th>
</tr>
</thead>
<tbody>
<tr>
<td>General form: the state’s purpose in exchange with the rival is not to lose relative position and seek only autonomy for itself, leading to minimal exchange with the rival.</td>
<td>-exchange should be narrow, easily severable and generate no relative gains for rival.</td>
</tr>
<tr>
<td>H1. If the state seeks only the minimum of material capabilities necessary to maintain its relative position (i.e., security), then it will direct its market actors’ behavior toward the rival to not jeopardize its position</td>
<td>-exchange should not be significant to the state or rival (i.e., FDI or trade large relative to GDP; e.g., above 10%), nor should there be surpluses benefiting the rival.</td>
</tr>
<tr>
<td>H2. If the state and its corporations’ interests diverge, then the state will override corporate interests in order to maintain its relative position vis-à-vis the rival.</td>
<td>-the quality of traded goods should not include technologies with dual-use capabilities and/or direct military applications (i.e., satellite, radars, avionics design, jet engine etc).</td>
</tr>
<tr>
<td>H3. If the state seeks only security, then it will not compromise the rival’s autonomy.</td>
<td>-easily severable exchange precludes FDI and large loans with the rival in anything but token amounts, as the state is expected to remain capable of severing exchange quickly and not suffering any losses, or contributing directly and cumulatively to the rival’s capabilities with FDI in defense-related areas (e.g., aerospace) or industrial manufacturing.</td>
</tr>
<tr>
<td>H4. If the state perceives the rival as increasing in threat, then the state will curtail or sever exchange relations.</td>
<td>-the state should be observed to direct its exchange with the rival, conditioning corporate behavior and prohibiting their preferred transactions, particularly those that might generate relative, cumulative gains (e.g., supercomputers).</td>
</tr>
<tr>
<td>H5. If the state perceives the rival as decreasing in threat, then the state’s imperative of positional maintenance still limits the quality of exchange relations.</td>
<td>-corporate actions that violate state preferences should not be observed (e.g., open disputes that are resolved in favor of corporation).</td>
</tr>
</tbody>
</table>

- Exchange should not be concentrated in items with few or no alternative suppliers/outlets. The rival’s partner and commodity concentration should be a priority of the state to see it be diverse, particularly in strategic goods the rival needs (e.g., oil, foodstuffs etc).

- Narrowing in exchange must follow threat increase, as the state seeks to further limit any gains the rival may derive from exchange (e.g., fewer types of exchange, and in trade, for example, reductions in items and values).

- No change is expected when threat reduces, and therefore there should be no broadening of exchange with rival after threat reduction and no extension of relative gains or new instruments.
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Offensive Realism

Hypotheses__________________________________
General form: the state seeks to control the rival’s
capabilities and shape its intentions, using exchange
as tool o f grand strategy (e.g., for intelligence
purposes, ally creation/shielding etc)
H I. If the state seeks the maximum o f influence,
then it will direct its market actors to increase the
vulnerability o f the rival and lessen its selfsufficiency (i.e., autonomy).
H2. If the state and its corporations' interests
diverge, then the state will override corporate
interests to maintain/increase the rival's
vulnerability.
H3. If the state seeks the maximum influence over
the rival's policies, then it will compromise the
rival’s autonomy by controlling the rival’s critical
resource needs, creating intensive specialization in
its economy through exports, and influencing
certain domestic actors.

H4. If the state perceives the rival as increasing in
threat, then the state will maximize the rival’s
dependency, exhaust its resources and capital,
foreclose other options for it, and build up states
hostile to the rival.

HS. If the state perceives the rival as decreasing in
threat, then the state may broaden exchange to
create new types o f influence while maintaining any
pre-existing vulnerability.

Observable Implications
-the state will promote exchange with the rival to increase its external economic activities generally (e.g.,
trade/GDP, FDI/GDP), and to promote the rival's exchange with the state in particular (e.g., subsidies,
insurance, diplomatic assistance, informal persuasion by officials).
-the state will seek to create rival vulnerability on it by increasing its import needs from the state or export
dependency, extending relative gains to the rival in order to become its principal trade partner in some
items (i.e., extend gains to create vulnerability, may include coordinating with other suppliers/recipients
to achieve/maintain)
-state oversight o f corporate actors yields intelligence on rival’s capabilities and intentions, and state
regulates conduct of corporate actors exchanging with rival. When corporate actors prefer exchange that
increases rival autonomy (e.g., sale o f self-sufficiency generating technologies, independent access to
needed resources) the state will block or overturn them. This is also true of instances when corporations
seek to penalize rival on their own terms (e.g., unilateral corporate embargo or withdrawal o f loans); the
state will block these attempts as well.
•the state will seek to specialize the rival's economy (i.e., production o f goods with no outlets other than
the state’s own) through trade, FDI and other instruments, and make this production and associated export
earnings important to state officials (e.g., government financing, loan servicing etc).
-The state will direct these activities and their gains toward favorable domestic groups in the rival, and
away from unfavored ones (i.e., those whose preferred policies conflict with the states, usually military
and related companies, political factions). The state will place conditions on the extension or
continuation o f exchange in this process and test rival beneficiaries willingness to comply with the state’s
preferences (e.g., loan use provisions that are opposed by some factions in rival and acceptable to others).
-threat increases decrease the willingness to further extend fungible gains (e.g., loans, bonds and large
trade surpluses), and instead focus state on directing exchange to increase the rival's vulnerability.
Increased exchange may result, but it will displace other suppliers/outlets, and focus on concentrating
rival's vulnerability to the state (i.e., concentrating partner and commodity dependence o f rival on state,
particularly in strategic goods necessary to rival). This will be observable in coordinated diplomacy with
other states and corporations to achieve rival's increased dependency and weakened self-sufficiency (e.g.,
send inefficient technologies to waste rival's capital and resources, coordinate with third party suppliers
and buildup relative gains for adversaries o f rival)
-threat reductions will lead to broadened exchange, but not a reduction in vulnerability. Any new
instruments will be extended to influence the rival's policies and autonomy, creating new venues o f
influence (e.g., go from trade only to FDI or loans, but with use provisions or high export-orientation with
the FDI).


<table>
<thead>
<tr>
<th>Hypotheses</th>
<th>Observable Implications</th>
</tr>
</thead>
<tbody>
<tr>
<td>General Form: the state is constrained by its largest market actors'</td>
<td>- state decisionmakers should be responsive to corporate interests and their lobbying efforts for exchange with rival (e.g., large banks, industrial corporations preferences should determine state policy, barring conflict with other corporate interests; whereupon the most important ones in the state's domestic political economy win out)</td>
</tr>
<tr>
<td>interests and both seek to maximize material capabilities, without</td>
<td>- state officials should assist corporate actors in exchange with rival, but not seek to shape/direct the exchange (i.e., few examples of denial of exchange); instead corporate actors, responding to comparative cost, relative factor endowment concerns, should determine the content, value and actors involved in exchange with rival. Trade in what each has comparative advantage in or supply/demand predicts (e.g., technology goods, labor-intensive goods, textiles, natural resources etc).</td>
</tr>
<tr>
<td>vulnerability concerns, through exchange based on comparative advantage</td>
<td></td>
</tr>
<tr>
<td>and market forces.</td>
<td></td>
</tr>
<tr>
<td>H1. If state policy is representative of its strongest economic actors'</td>
<td>- corporations will seek to engage private actors in rival who will then pressure their governments for continued exchange. Corporations will also prefer more valuable and mutually vulnerable exchange instruments to maximize societal pressure on governments to maintain exchange (e.g., FDI in large amounts and in trade-substituting facilities that bind interests in both states, large loans, bonds and securities)</td>
</tr>
<tr>
<td>interests in increasing their and the state's overall wealth, then the state</td>
<td></td>
</tr>
<tr>
<td>will support these actors as they seek material wealth through economic</td>
<td>- divergent state officials' preferences will be subverted by large corporations by lobbying/pressuring state officials to change policy, fulfilling preferences unilaterally through third parties, forcing issues through threats of dramatic exchange changes (e.g., embargoing rival, selling rival important resources or military-related technologies).</td>
</tr>
<tr>
<td>exchange with the rival.</td>
<td></td>
</tr>
<tr>
<td>H2. If corporations seek to maintain exchange relations with the rival,</td>
<td>- increased threat will not change exchange if corporations aren't threatened similarly by rival (e.g., rival expropriation of corporate assets, stockpiling requirements, import-substitution efforts etc). Absent convergent state-corporate threat perception, exchange should be maintained by corporate interests.</td>
</tr>
<tr>
<td>then they will increase the number of positively affected interest groups</td>
<td></td>
</tr>
<tr>
<td>in the rival and create incentives for both states not to disrupt the</td>
<td>- threat reductions are expected to lead to increased exchange, particularly in capital markets instruments (i.e., bonds, securities and loans).</td>
</tr>
<tr>
<td>exchange, leading to peaceful relations.</td>
<td></td>
</tr>
<tr>
<td>H3. If state policy diverges from corporate interests in expanding exchange</td>
<td>- democratization through industrialization requires exchange with non-government actors in rival, not government-related ones, and the introduction of new production patterns and advantages/exchange benefits to new elites.</td>
</tr>
<tr>
<td>with the rival, then corporations will seek to achieve their preferences</td>
<td></td>
</tr>
<tr>
<td>toward the rival despite state policy.</td>
<td></td>
</tr>
<tr>
<td>H4. If the state perceives the rival as increasing in threat, then state</td>
<td></td>
</tr>
<tr>
<td>decisionmakers will be constrained in limiting exchange by corporate</td>
<td></td>
</tr>
<tr>
<td>preferences in continuing exchange.</td>
<td></td>
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<tr>
<td>H5. If the state perceives the rival as decreasing in threat, then corporate</td>
<td></td>
</tr>
<tr>
<td>interests in expanding exchange will drive state policy.</td>
<td></td>
</tr>
<tr>
<td>H6. If the state prefers democratic governments because they are more</td>
<td></td>
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<tr>
<td>peaceful and responsive to economic interests, then the state will promote</td>
<td></td>
</tr>
<tr>
<td>exchange with a non-democratic rival to increase its economic growth and</td>
<td></td>
</tr>
<tr>
<td>industrialization, creating a middle and entrepreneurial class</td>
<td></td>
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<tr>
<td>demanding responsive democratic government.</td>
<td></td>
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</tbody>
</table>
### Hypotheses

**General Form:** Large corporations, acting individually or in global cartels, control natural resources, technologies, and state policies across the world, structuring exchange to serve their profit maximization and control interests.

**H1.** If state policy is determined exclusively by the largest banking and corporate actors' interests in maximizing returns on capital, then surplus capital will flow into the rival and will not be subject to state rescission, increasing the rival's relative material capabilities.

**H2.** If corporate monopolies and/or global cartels control and structure resource and technology allocation across states, then important natural resource distribution and technology transfers should fulfill these actors' interests and not those of either state.

**H3.** If corporate monopolies or cartels perceive the rival as increasing in threat (i.e., to their control of resources, capital etc), then the state's coercive institutions (e.g., economic and military pressure) will be used to force the rival's compliance.

### Observable Implications

- Observations of divergent state and corporate preferences in the state should be minimal to non-existent.

- Banking and corporate actors' preference for capital exportation to the rival should occur easily and lead to increased relative material capabilities in the rival (e.g., higher economic growth rate than in state).

- Any divergent state preferences regarding capital export to rival will be overruled by leading capitalists.

- Exchange should be controlled by corporations and remain largely intra-firm, maximizing control over the gains from exchange (e.g., rival exports to state remain within same corporate organization, loans to rival pay for its imports from the state).

- Strategic goods and technologies (e.g., oil, iron ore, energy technologies, industrial processes etc) are controlled by corporate monopolies and/or global cartels and selectively supplied to the rival and/or the state to fulfill corporate preferences for maximum profits and market control.

- Rival threats to corporate controlled-exchange (e.g., nationalization, substitution efforts, stockpiling requirements etc) will be portrayed as threats to state interests/principles, and the coercive power of the state employed to punish rival and force compliance (e.g., sanctions against rival fulfill corporate interests, not objective state interests).
APPENDIX B

- Diagram Illustrating Method of Obtaining Information from Commercial Sources
- Diagram Representing the Method of Transmission of Other Information from Commercial Sources
Diagram Illustrating the method of obtaining Information from Commercial Sources regarding the movements of Enemy Naval Vessels.
Office of Naval Intelligence
March 1918

Diagram
Representing the Method of Transmission
of
Other Information
from
Commercial Sources.

DECLARED
money and "X" by
[Handwritten notes]

[Diagram of flowchart with labeled boxes for Commercial Sources, State Department, and Navy Department]

512

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APPENDIX C

The table below lists the most significant exchange events within each of the five case periods and totals across the entire U.S.-Japan case. The table below and its associated coding scheme does not make a single theoretical validation conclusion for each event, because not all events merit such evaluation and the important assessments are located in the main text of the dissertation accompanied by their theoretical evaluations. The most crucial exchange events are evaluated comprehensively in the text and are also in the list below, including: the oil investment and trade decisions, Japanese government finance, and U.S. trade and embargo decisions on silk, cotton and steel-related products. In the main text, the researcher has attempted to faithfully fulfill the obligations of evidence assessment; in this appendix, the researcher has constructed a simple coding evaluation for assessment of whether any part of the four theories' hypothesized observable implications are present (i.e., validation). This then allows the cumulative weight of simplistic validations to build or not build across the case periods and whole case. As a result, an event may validate more than one theory's observable implications. However, theory implication invalidation is more important to assessment.

992. The researcher concurs with Stephen van Evera regarding large-n studies and events aggregations: "a large-n test of a hypothesis provides little or no new insight into the causal process that comprises the hypothesis' explanation, nor does it generate data that could be used to infer or test explanations of that process. Overall, large-n methods tell us more about whether hypotheses hold than why they hold." Van Evera, Guide to Methods, p.55.
of theory explanatory power and the standard of invalidation is higher.\footnote{For the best statement of this see Karl Popper, The Logic of Scientific Inquiry, 2nd ed., (New York: Harper & Row, 1968).} It requires the negation or observance of the opposite of the implication of a given hypothesis, not merely a congruent observation of a theory implication.\footnote{Van Evera, Guide to Methods, pp.58-9.} This evaluation is not performed here, however, and is done only in the text.

Fortunately, the theories' observable implications often provide for opposing predictions or at least disconfirming implications (e.g., if threat goes up exchange must decrease for defensive realists, therefore any stasis or increase in exchange challenges defensive realism). This does not mean, however, that every event will negate some theory. Some events do not challenge a theory’s implications. For example, the U.S. state department wanted an informal embargo on the export of Molybdenum in December 1939. The companies who controlled the production and export of this item willingly complied with the State department and there were no divergent state-corporate preferences; therefore liberalism and marxism were not challenged. In general, the researcher has tried to include all potentially liberal or marxist events in the analysis, in order not to overly reify realism. In contrast, not all realist actions have been tallied across the whole case and some have been aggregated and not listed as discrete events merely to capture more of them (e.g., U.S. State department loan denials). The coding process is exemplified in the following two examples, one simple the other complex.

1) Simple: In 1927 J.P. Morgan and National City Bank sought to make large loans to the Japanese army-related South Manchuria Railway Company. The U.S. State
department blocked these loans from going forward because it declared that no U.S. loans would be used to further Japan's army's colonial business enterprises in Manchuria. This supports defensive realism's prescriptions against assisting the material capabilities of a rival (i.e., DR hypothesis 1). The State department refused this loan for the additional reason of specifically not aiding the Japanese army in its endeavors at empire in North China, and for that reason it validates offensive realism's hypothesis of influencing domestic factions through exchange and non-exchange with rival (i.e., OR hypothesis 3). The U.S. government did not state this publicly to Japan, however. But, it nonetheless overrode its bankers' clear and repeated preferences. Because the state denied corporate preferences realism is validated and liberalism and marxism invalidated. For marxism it is a starker invalidation, because the largest banks are supposed to control the state apparatus and achieve their exchange preferences (i.e., M hypothesis 1), and both liberalism and marxism were further invalidated after the banks tried to win approval by declaring that the loans would be used to buy U.S. goods, boosting U.S. production and exports at a time when U.S. threat perception of Japan was lower than most other periods (i.e., M hypothesis 2, L hypothesis 5). Therefore this event was coded: OR, DR validated, L, M invalidated.

2) Complex: The most complex event in terms of the theories' observable implications was the June 1933 U.S. government loan to Nationalist China. President Roosevelt directed the loan over Hornbeck and Hull's objections. The $50 million dollar loan was specifically dedicated to the purchase of U.S. wheat and cotton by China. But, the Chinese, advised by Arthur Young, resold the wheat and cotton for cash to purchase
"basic infrastructure" items, and also indirectly to finance U.S. warplanes. The major U.S. banks and the British objected vigorously to the loan, citing its effect on Japanese sensibilities and the middling position of the China Loan Consortium. Because the loan supported domestic U.S. agricultural production and exports, and was stated as doing just that, it validates liberalism’s emphasis on trading in U.S. comparative advantage and supporting agriculture during Roosevelt’s turnaround of the U.S. economy (i.e., L hypothesis 1). It supports marxism similarly and in tying loans to trade. However, it invalidates marxism in not fulfilling U.S. bankers’ preferences not to make the loan and possibly also liberalism because the loan hurt finance and trade with Japan, a much larger export market for the U.S. at the time. And, the banks were more important to the U.S. economy, as agriculture was retrenching under mandated production decreases and financial stability loomed larger domestically requiring the cooperation of major U.S. banks. Both realism’s are supported in building an effective counterweight to an increasingly threatening Japan by this time (i.e., classical balancing behavior). This event was reviewed because it affected Japan’s ability to extract resources from North China and Manchuria and consolidate its economic gains there by emboldening Chiang’s Nationalists to resist and frustrate this when no one else would (i.e., third country effects on Japanese relative autonomy). What this event also demonstrates is Roosevelt’s masterful melding of the domestic and strategic rationales in exchange. This allowed him to deftly evade Japanese charges of supporting Chiang by claiming domestic farm support motivation when any country could have taken the loan for U.S. wheat and cotton exports.

Therefore this event was coded: OR,DR,L,M validated, L,M invalidated.
## Selected Exchange Events and Comparative Hypothesis Evaluation

<table>
<thead>
<tr>
<th>Event Summary</th>
<th>Validates</th>
<th>Invalidates</th>
</tr>
</thead>
<tbody>
<tr>
<td>President Wilson suspends cotton and silk trade licenses to affect Japanese troop withdrawal from Siberia, 1918</td>
<td>OR</td>
<td></td>
</tr>
<tr>
<td>Koloniale's offer to sell DEI assets to Japan</td>
<td>OR,L,M</td>
<td>DR</td>
</tr>
<tr>
<td>Creation of the China Loan Consortium, October 1920</td>
<td>OR,L,M</td>
<td></td>
</tr>
<tr>
<td>Decreased Japanese Navy Fuel Oil from U.S., 1920-21</td>
<td>OR,DR</td>
<td></td>
</tr>
<tr>
<td>Sinclair Oil abandoned in North Sakhalin claims in 1921 despite personal ties to President Harding, 1921</td>
<td>OR,DR</td>
<td>L,M</td>
</tr>
<tr>
<td>U.S. pressures Japan to give up economic rights to Shantung province, China at Washington Conference, 1921</td>
<td>OR</td>
<td>DR</td>
</tr>
<tr>
<td>U.S. iron and steel plates and sheets exports to Japan used in naval construction while Japan a high threat</td>
<td>L</td>
<td>OR,DR</td>
</tr>
</tbody>
</table>

### 1918-1922 Period Summary

<table>
<thead>
<tr>
<th>Event Summary</th>
<th>Validates</th>
<th>Invalidates</th>
</tr>
</thead>
<tbody>
<tr>
<td>Oriental Development Company loan, 1922-23</td>
<td>OR</td>
<td>DR,L,M</td>
</tr>
<tr>
<td>South Manchuria loan denial, 1923</td>
<td>OR,DR</td>
<td>L,M</td>
</tr>
<tr>
<td>South Manchuria loan denials, 1927</td>
<td>OR,DR</td>
<td>L,M</td>
</tr>
<tr>
<td>Guaranty Trust Co. loan to DEI not linked to oil rights issue by State department, 1923</td>
<td>OR</td>
<td>M</td>
</tr>
<tr>
<td>U.S. government secures increased DEI oil rights for Standard Oil while Japan is given worthless DEI land, 1928</td>
<td>OR</td>
<td>DR,L,M</td>
</tr>
<tr>
<td>U.S. export of oil refining technology and oil products to Japan 1924-1928</td>
<td>OR,L</td>
<td>DR</td>
</tr>
<tr>
<td>U.S. economic support for Nationalist China, including preparing to sell dual-use aircraft exports, July 1928</td>
<td>OR,DR</td>
<td>L</td>
</tr>
<tr>
<td>U.S. direct investment in Japan by Ford, GM and Westinghouse</td>
<td>L</td>
<td>OR,DR</td>
</tr>
<tr>
<td>Loans to Japanese Electric Companies</td>
<td>OR,L,M</td>
<td>DR</td>
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### 1923-1929 Period Summary

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<tr>
<td>8OR,3DR,3</td>
<td>1OR,5DR</td>
<td></td>
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<tr>
<td>Event</td>
<td>Source(s)</td>
<td></td>
</tr>
<tr>
<td>----------------------------------------------------------------------</td>
<td>------------</td>
<td></td>
</tr>
<tr>
<td>U.S. threat of non-renewal of Japanese government loan in late March 1930 to gain Japanese compliance with terms of London Naval Treaty</td>
<td>OR DR L M</td>
<td></td>
</tr>
<tr>
<td>National City Bank Yen Speculation 1930-31</td>
<td>L M</td>
<td></td>
</tr>
<tr>
<td>U.S. loan ban against Japan January 1932</td>
<td>OR DR L M</td>
<td></td>
</tr>
<tr>
<td>U.S. transfer of aviation training team to China and decision to export dual-use military aircraft through Commerce department May 1932</td>
<td>OR DR L</td>
<td></td>
</tr>
<tr>
<td>State department limits on Ethyl Gas Corporation exports to Japan 1932-33</td>
<td>OR DR L M</td>
<td></td>
</tr>
<tr>
<td>President Hoover’s refusal to consider economic sanctions against Japan because they were akin to acts of war 1931-32</td>
<td>L OR DR</td>
<td></td>
</tr>
<tr>
<td>U.S. direct investment in Mitsubishi oil refinery and Taiwan Electric Loan July 1931</td>
<td>OR L DR</td>
<td></td>
</tr>
<tr>
<td><strong>1929-1933 Period Summary</strong></td>
<td>5 OR 2 DR 3 L 1 M 4 OR 4 DR 4 L 3 M</td>
<td></td>
</tr>
<tr>
<td>U.S. exports 440 out of China’s total 692 military aircraft up through 1937</td>
<td>OR DR L</td>
<td></td>
</tr>
<tr>
<td>U.S. government loan to China over Bankers’ objections, facilitating U.S. exports to China and Chinese government finance of aircraft purchases, June 1933</td>
<td>OR DR L M</td>
<td></td>
</tr>
<tr>
<td>Pacific Oil Company assumes DEI oil concession from Japanese applicant without knowledge and U.S. government supports 1934</td>
<td>OR DR L M</td>
<td></td>
</tr>
<tr>
<td>U.S. raw cotton export price increase, import quota on Japanese cotton goods in U.S. and Philippines, and increased Japanese cotton import tariffs, 1933-1936</td>
<td>OR DR L M</td>
<td></td>
</tr>
<tr>
<td>U.S. control over oil company negotiations with Japan regarding stockpiles and hydrogenation sale reinforcing Japanese dependence through crude oil refinery equipment exports, 1934-36</td>
<td>OR L M DR</td>
<td></td>
</tr>
<tr>
<td>U.S. purchases of Chinese silver from Japan and Britain</td>
<td>OR DR</td>
<td></td>
</tr>
<tr>
<td>U.S. greater efforts on behalf of oil companies than auto companies, 1934-36</td>
<td>OR L M</td>
<td></td>
</tr>
<tr>
<td>Event Description</td>
<td>Year(s)</td>
<td>Source(s)</td>
</tr>
<tr>
<td>----------------------------------------------------------------------------------</td>
<td>---------------</td>
<td>-----------</td>
</tr>
<tr>
<td>U.S. directs Stanvac to make no further investments in Japan</td>
<td>1935</td>
<td>OR, DR, L, M</td>
</tr>
<tr>
<td>U.S. tin embargo directed against Japan</td>
<td>1936</td>
<td>OR, DR, L</td>
</tr>
<tr>
<td><strong>1933-1936 Period Summary</strong></td>
<td></td>
<td>90R, 6DR, 2L, 2M, 2DR, 7L, 5M, OR, DR, L, M</td>
</tr>
<tr>
<td>DuPont withholds weapons to China seeking State department declaration of support</td>
<td>1937</td>
<td>L, M, OR, DR</td>
</tr>
<tr>
<td>Moral embargo on aircraft exports, reinforced by State department threat of witholding government purchases, July 1937-December 1938</td>
<td></td>
<td>OR, DR, L, M</td>
</tr>
<tr>
<td>U.S. government $25 million dollar loan to China</td>
<td>December 1938</td>
<td>OR, DR, L, M</td>
</tr>
<tr>
<td>U.S. blocks loans for occupied China and furthers Chinese credits to purchase U.S. airplanes</td>
<td>March 1939</td>
<td>OR, DR, L, M</td>
</tr>
<tr>
<td>U.S. embargo on ferro alloy exports to Japan, coordinate non-supply across Western hemisphere with Britain, December 1939</td>
<td></td>
<td>OR, DR, L, M</td>
</tr>
<tr>
<td>U.S. ends technical assistance by companies to Japan for production of aviation gasoline over corporate objections, but supplies Japan increasing amounts of aviation gasoline, December 1939</td>
<td></td>
<td>OR, DR, L, M</td>
</tr>
<tr>
<td>U.S. gold purchases from Japan, 1937-1940</td>
<td></td>
<td>OR, DR, L, M</td>
</tr>
<tr>
<td>U.S. cancels all Japanese machine tools orders, January 1940</td>
<td></td>
<td>OR, DR, L, M</td>
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<tr>
<td>U.S. led negotiations by oil companies in the DEI with Japan Fall 1940 and eventual non-fulfillment of contract with tanker shortage, early 1941</td>
<td></td>
<td>OR, DR, L, M</td>
</tr>
<tr>
<td>U.S. embargos scrap iron and steel exports to Japan</td>
<td>September 1940</td>
<td>OR, DR, L, M</td>
</tr>
<tr>
<td>U.S. supplies Japan with oil products throughout 1940 through July 1941 embargo</td>
<td></td>
<td>OR, DR, L, M</td>
</tr>
<tr>
<td>Full trade embargo through financial freeze administered by U.S. Treasury department, August 1941</td>
<td></td>
<td>OR, DR, L, M</td>
</tr>
<tr>
<td><strong>1937-1941 Period Summary</strong></td>
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<td>110R, 8DR, 1L, 1M, 1OR, 4DR, 4L, 4M</td>
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<table>
<thead>
<tr>
<th></th>
<th>Off. Realism</th>
<th>Def. Realism</th>
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<th>Marxism</th>
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<tr>
<td>Totals: 44 Events</td>
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<td>-9</td>
<td>-13</td>
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</table>
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534


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546
