1. The Government of Japan has consulted the Fund under Article XIV, Section 4, of the Fund Agreement, concerning the further retention of its transitional arrangements.

2. The rapid cyclical recovery in Japan's economy that began from about the middle of 1958, following the earlier recession, has been completed and Japan is now experiencing a period of prosperity and continued expansion. Output and employment have advanced to new highs. The external payments position has continued strong and foreign exchange reserves have increased substantially. The recovery and the subsequent expansion have, in general, not disturbed monetary stability. The Fund commends the cautious domestic financial policies which have helped to make this improvement possible.

3. Wholesale prices increased by 2 per cent from November 1958 to April 1959; they declined slightly in the following two months but this decline was partly seasonal. Imports have been rising from the beginning of 1959 and are expected to rise further. Exports, which had increased only slightly in 1958, have also been improving, but the increase in exchange reserves may nevertheless slow down in the coming months. Recently there has been some acceleration in the rate of expansion of private credit, and the government budget for the current fiscal year visualizes a substantial cash deficit. The Fund welcomes the assurance of the authorities that they have these developments under close observation and that they will continue to pursue cautious and flexible financial policies so as to maintain domestic and external equilibrium.

4. The Fund welcomes the progress made by Japan in relaxing restrictions and reducing discrimination, including the termination of three of its remaining bilateral payments agreements. Some progress has also been made in reducing the scope of minor restrictive practices such as the retention quota, the linking system, and barter trade. However, the Japanese exchange system, involving a rigid exchange budget, still has a considerable restrictive effect on import demand, discrimination still exists, and the minor restrictive practices have not been removed. The Fund believes that, especially in the light of Japan's improved balance of payments and reserve position and of the action taken by Western European countries in making their currencies externally convertible, further progress in all these respects is possible and desirable.

5. In concluding the 1959 consultations, the Fund has no further comments to make on the transitional arrangements maintained by Japan.