

One Year of Abenomics – an interim report

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After the Nikkei-Index reached its highest point of 38,000 Yen in December 1989, the economic bubble burst. The following stagnation of the Japanese economy is regarded as a serious problem. Some economists hold the theory that the "rate of growth of high-income countries is low and the growth rate of low-income countries is high, thus inevitably they will converge somewhere." Kishore MAHBUBANI (National University of Singapore) writes that the speed of convergence is now accelerating. According to MAHBUBANI there are currently 500 million people that belong to the middle classes, when the Olympic Games take place in Tôkyô 2020 this figure will increase to 1.77 billion people. If we consider that Japan's population will continue to decrease in the future, Japan and Germany should ask themselves how they can use the vitality of these newly industrializing countries for their own growth.

According to Prime Minister ABE, the effects of the 15 years of "deflation are the root of all evil". Consumers first greeted the decrease in prices as something positive, however the decreases in their own income made it more difficult to service mortgages and business loans etc. Economic activities came to a standstill. This is why the ABE government at the beginning of its term in office in December 2012 declared a series of economic policy measures that became known as "Abenomics". The cornerstones are the "three arrows": monetary easing, fiscal stimulus and structural reforms that encourage growth through increased private investment. This introduced drastic reforms to the Japanese economy that included solutions to the problems of deflation.

The theory that a decreasing population is the cause of deflation is difficult to believe. Currently in 24 countries around the world populations are decreasing but only Japan is confronted with deflation. Its cause is more likely to lie in the insufficient money supply. Thus, deflation should be countered with an extreme easing of monetary policy, the first of the "three arrows". KURODA Haruhiko, President of the Bank of Japan since March

2013, announced shortly after taking office that he would double the amount of money in the economy in two years. This awakened hope and the Nikkei increased within a year by 57% (Dow-Jones 30%, DAX 25%). The first arrow fell directly in the black and was awarded an "A".

The second "arrow" (flexible fiscal policy) consists of short and long-term measures. In the short-term, public investment shall increase demand and stimulate the economy. Therefore in the 2013 fiscal year an additional budget of 10 trillion Yen (approximately 70 billion Euro) was implemented. The long-term measures are aimed at restructuring public finances, i.e., by transferring the primary balance into the black again and recovering the financial system. During the creation of KOIZUMI's cabinet in 2001 the deficit of the primary balance was 5% of GDP, by 2006 it had recovered to minus 1% without increasing the value-added tax. The Japanese tax revenue revealed in times of economic recovery a high income flexibility, i.e., when the GDP increases by 1% the revenue increases by 4%. With the growth strategy tax revenues shall also be raised by a larger GDP, at the same time reforms will be carried out to the pension and health systems to counteract the increases in expenditure. The average life expectancy when the pension system was introduced was 66 years in Japan, thus the pension after 65 years was no problem. Today average life expectancy in Japan is 80 years, and the system is no longer able to support this. In April the value added tax will increase from its current 5% to 8%. The additional income will be used to expand social security for the younger generation; this includes childcare and maternity leave to make it easier for woman to play a more active role in society. The short-term measures of the second arrow have been implemented, the long-term measures have been only partly implemented, and this has been awarded a "B".

The third arrow (growth strategy) will create a climate for economic growth in which companies can act freely and compete

constructively. Existing regulations must be decreased here and the burdens for companies must be reduced. Thus, at the end of 2013 the *National Strategic Special Zones* bill was passed. This bill seeks to attract international investment and strengthen the international competitiveness of the domestic economy.

At the global economic forum held in Davos at the end of January Prime Minister ABE described these special zones as a breakthrough and announced "to reform all regulations that until now were regarded as 'written in stone' in the coming two years." Even the Olympic Games and Paralympics Games in Tôkyô will be brought forward by deregulation. In addition to the "hard" effects – such as improvements to infrastructure – the greater exposure of Tôkyô and Japan will have an effect on the soft power, the so called "save face effect". According to research in countries which have hosted the Olympic Games throughout the past 50 years, trade during the games increased by approximately 30%. International attention increases the conviction to get rid of "unique regulations" because they are regarded as "embarrassing". Internal reforms are accelerated, and as result of progressive liberalization trade levels increase. It's too early to make an assessment of this "growth strategy" because we can expect strong resistance to deregulations by other stakeholders. Now, where the *National Strategic Special Zones* have been passed through parliament and have caught a tail wind through the Olympic Games, steadfast efforts are required to implement these measures so they can be awarded with an "A" in the future.

Prime Minister ABE understood 2014 as the decisive year of his "Abenomics"; we can however assume that the "three arrows" of the Japanese economy will continue to fly.



This report is based on a presentation given by the author on the same topic at the JDZB on 27 January 2014.