

# Lessons from Japan: How Abenomics Can Provide Solutions for Advanced Countries

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# Introduction

- The United States faced financial turmoil from the Lehman Shock in 2008 and Europe also encountered a **financial crisis** in 2011.
- Europe is now on the verge of **deflation**.
- Chinese economy, with a huge current account surplus, is under the continuing pressure of currency appreciation and China will soon face problems with a rapidly growing **aging society**.
- All of these problems are what Japan has already experienced in 1990's.

**“Japan is an advanced country of problems. ”**

# Financial Crisis in Japan

- Japan experienced an unprecedented financial crisis after the collapse of its bubble economy, especially in 1997 and 1998.
- The total number of banks that filed for bankruptcy was 181 from 1991 to 2003.

# Deflation in Japan

- GDP deflator and CPI fell into the negative zone in the 1990's and this situation has continued for 20 years since then.
- The number of regular workers has dropped and wage has also fallen.
- People were gradually losing their animal spirits and the profitability of corporations are kept low.

# Aging Society in Japan

- The speed of aging in Japan is the fastest in the world.
- 30% of population will be over 65 years old in 2025, and 40% in 2050.
- The medical care cost per capita of individuals over 65 years old people is three times that of individuals under 65 years old. Individuals who are over 75 years old is five times that amount.
- As a result, that expenditure has been growing by 10 billion dollars each year.
- The debt GDP ratio is 230% now and this number is still rising.

# Lessons from Japan: Financial Crisis

I. Monetary easing and fiscal stimulus were carried out as macroeconomic measures.

- Adopted the zero target rate in 1999 and monetary easing for the first time in 2001. They were suspended in 2006.
- The volume of fiscal stimulus in 1998 reached nearly 8% of GDP.

II. The Banking Policy

- making strict loan assessments and obliging loan loss reserves
- requiring mergers with sound banks
- protecting all the deposits by using DIC's insurance premium and tax dollars, 10 % of GDP.

# Lessons from Japan: Deflation -1

- What is the reason for this long deflation?
  - “Fallacy of Composition”- Rational actions by each person made deflation worse as a whole.
  - People lost their animal spirits.
  - The shift from regular employment to part-time employment.
- The 1<sup>st</sup> arrow is **ultra-monetary easing**.

It is called Quantitative Qualitative Monetary Easing (QQME). It aims to lift CPI to 2% in 2 years from 2014 (April) by doubling monetary base through the purchase of JGBs, ETFs, etc.
- The 2<sup>nd</sup> arrow is **flexible fiscal policy**.

# Lessons from Japan: Deflation -2

The 3<sup>rd</sup> arrow is **growth policy** i.e. **structural reform**.

Examples include:

- Electricity sector reform
- Agriculture reform
- Enhancement of Corporate Governance
  - Outside directors, Stewardship code
- Corporate tax reform
  - The current corporate income tax rate is 35.64%. The government aims to reduce the percentage level of the corporate tax rate down to the twenties in several years.
  - Broadening the tax base by enhancing the pro-forma standard taxation



# Lessons from Japan: Aging Society

- **GDP Ratio:** 1.1 trillion dollars, 23% of GDP, are used for social security every year. The first step is to not increase this ratio.
- **Consumption Tax:** The ratio of expenditure for public pension to GDP can be around 10 %, its current level, in the future. But the ratio for the cost of medical service and nursing care will keep rising if no reforms are addressed. The last option is to hike consumption tax even more.
- **Remaining Issues “The Causes of Huge Government Debt”**
  - We haven’t collected permanent tax revenue which was enough to sustain the social security system, i.e. adults put these burdens onto their children.
  - Tax revenue dropped because of deflation and tax cut for stimulating the economy. 9

# What is the Core of the Abenomics?

- Creation of inflation expectations by QQME
- Comprehensive policy package
- The last chance to get rid of long-standing deflation

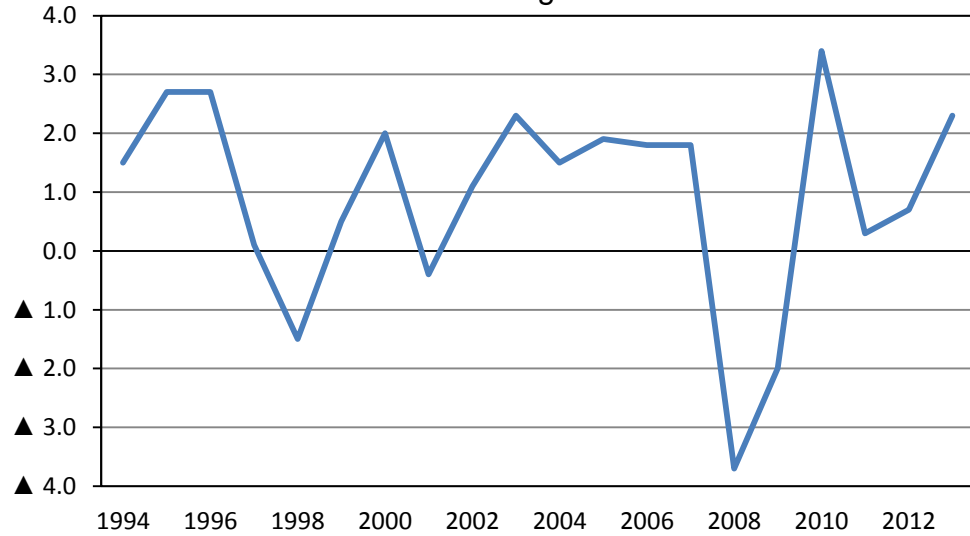
# Conclusions

What is the condition for Abenomics to keep succeeding?

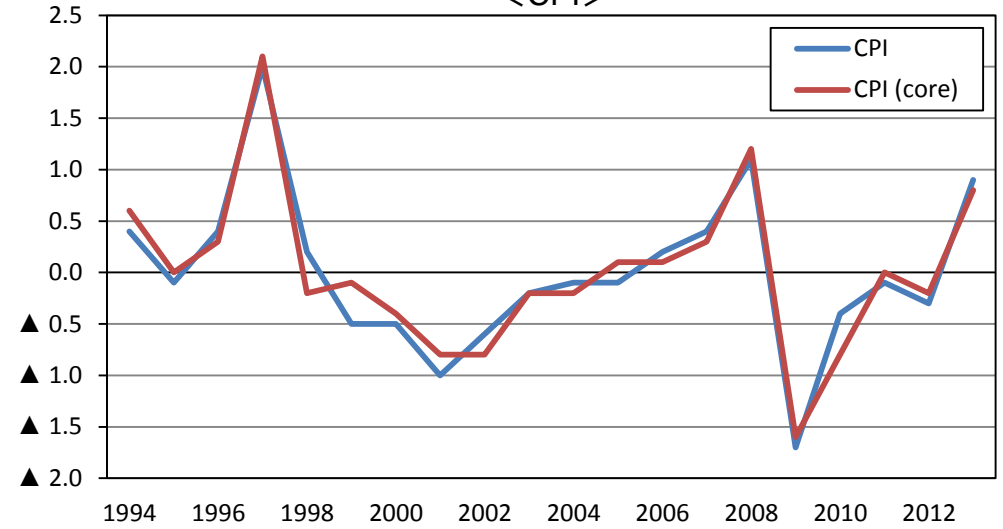
- The stability of government
- The credibility in fiscal consolidation
- The resolution of energy issues

# 1. Current Economics Situation

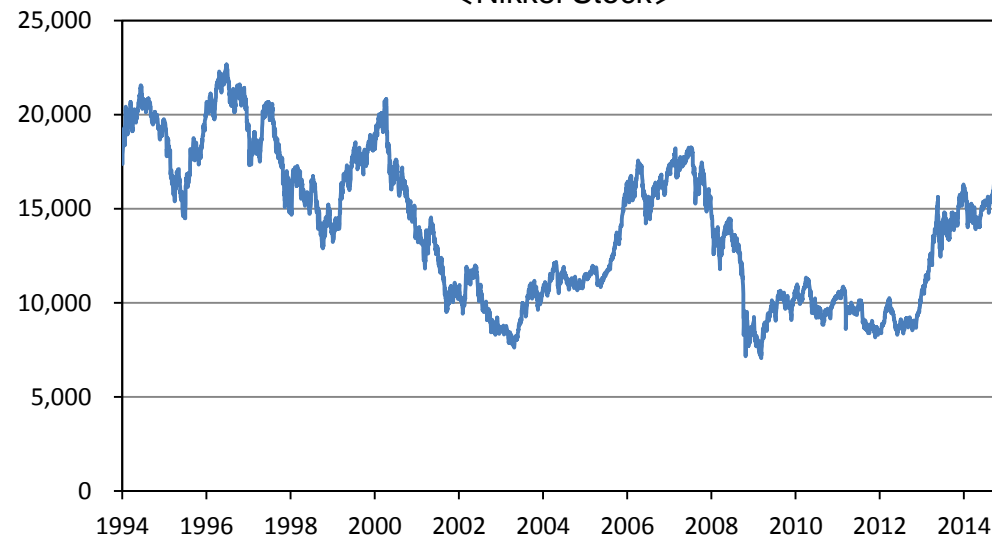
<Real GDP growth rate>



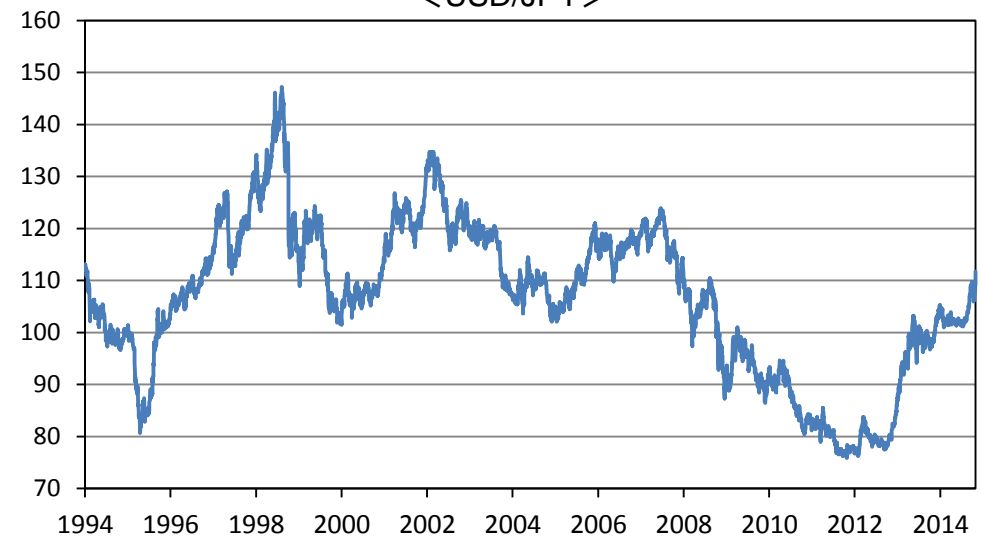
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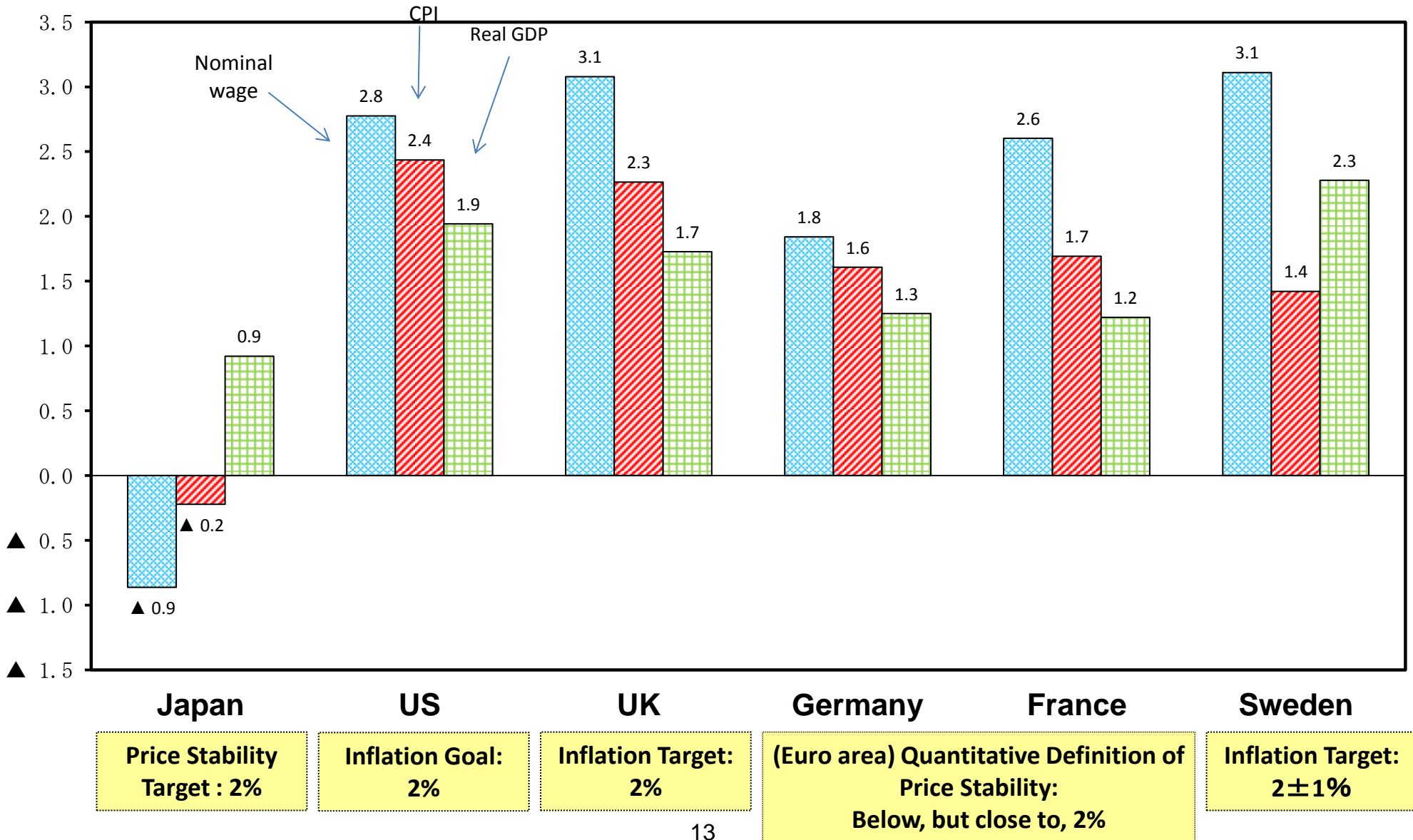


<USD/JPY>

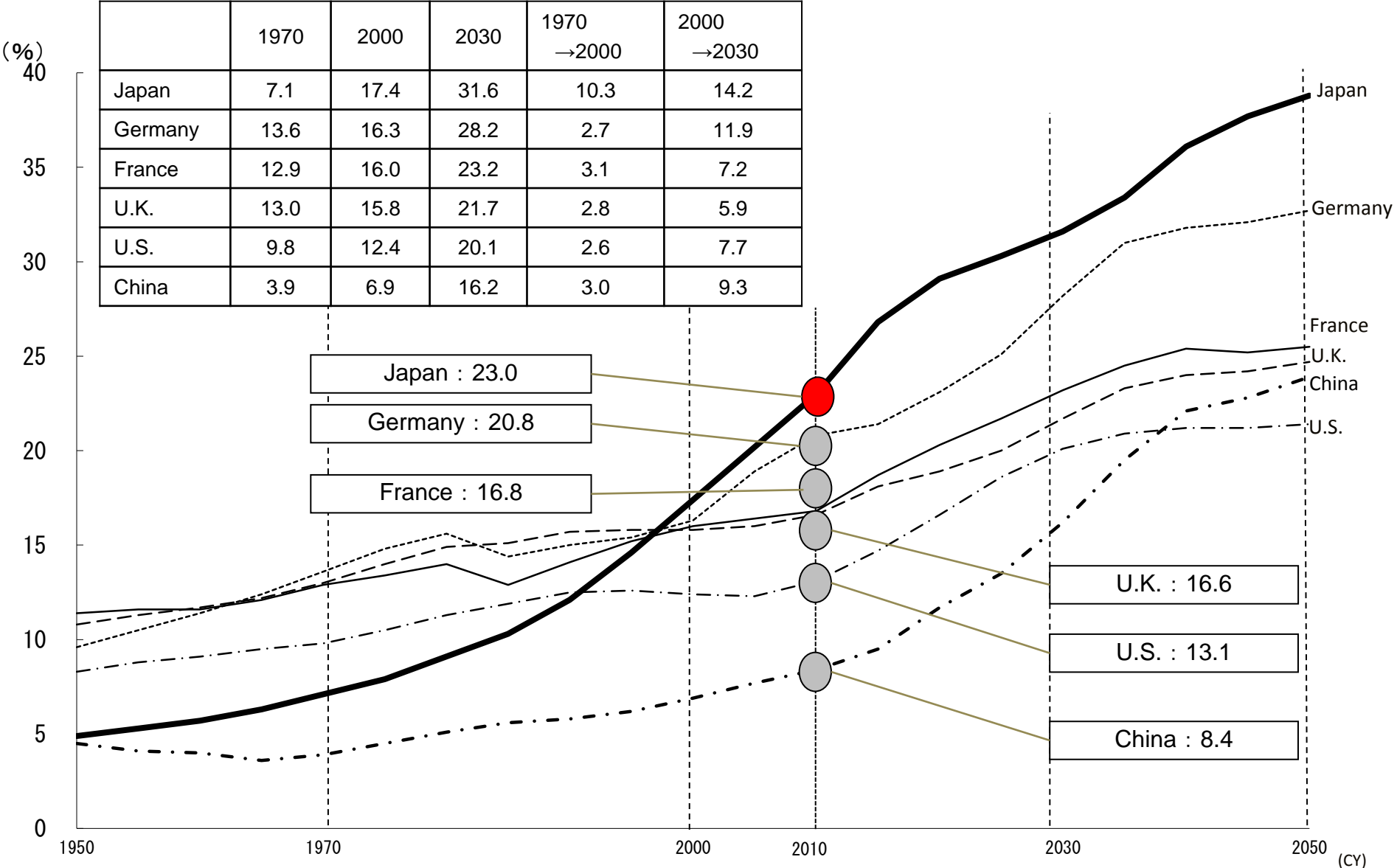


## 2. CPI and Wage

(Average annual growth (increase) rate after 2000, %)

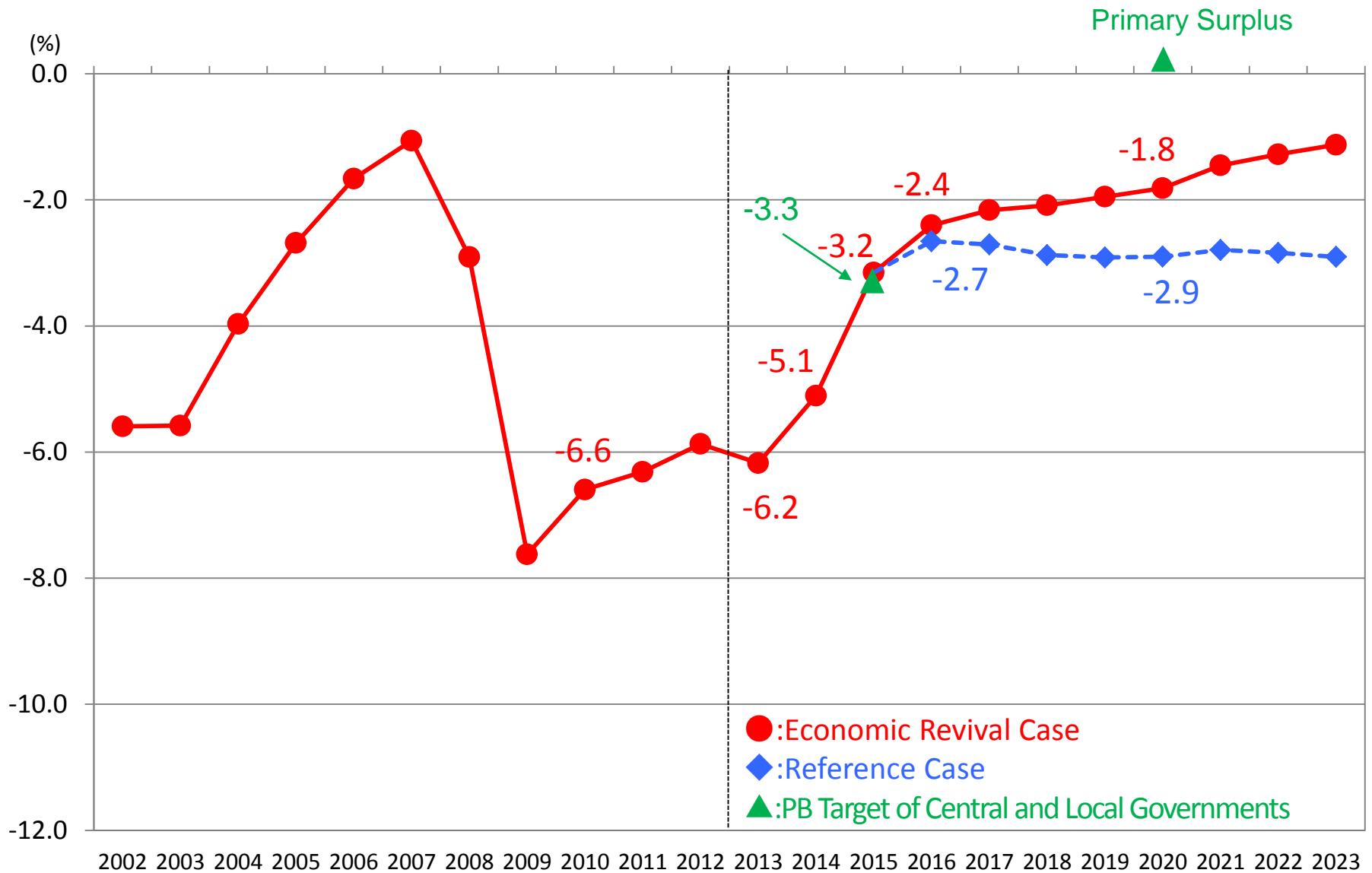


# 3. Ratio of People Older than 65 years to the Total Population



Source: Japan 1950-2010: "National Census" (Ministry of Internal Affairs and Communications)  
 2011-2050: "Japanese Future Demographic Projections" (National Institute of Population and Social Security Research) (January, 2012)  
 Other countries: "World Population Prospects: the 2012 Revision" (United Nations)

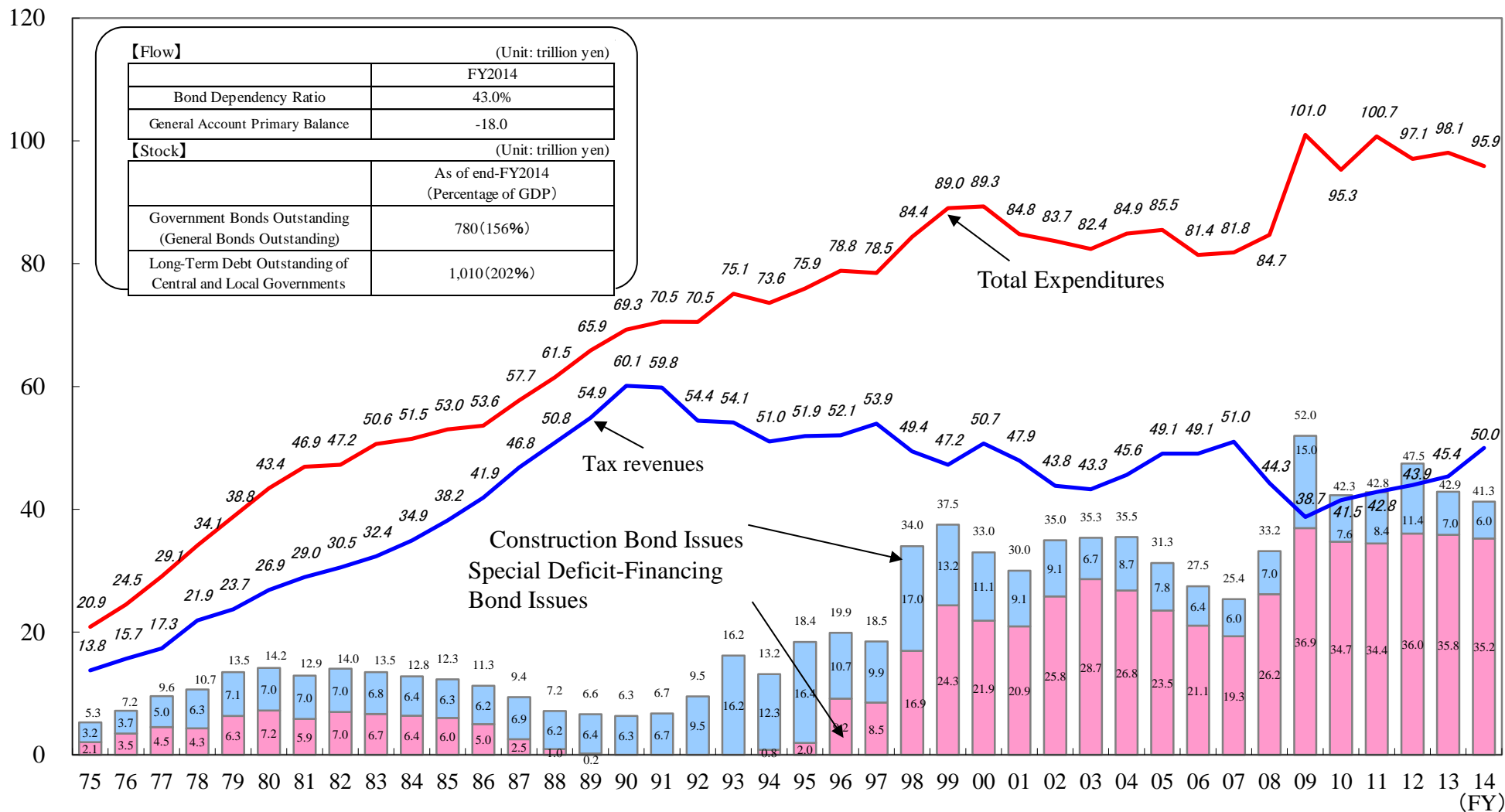
## 4. Fiscal Consolidation Targets



Source: Cabinet Office

# 5. Trend in General Account

(trillion yen)



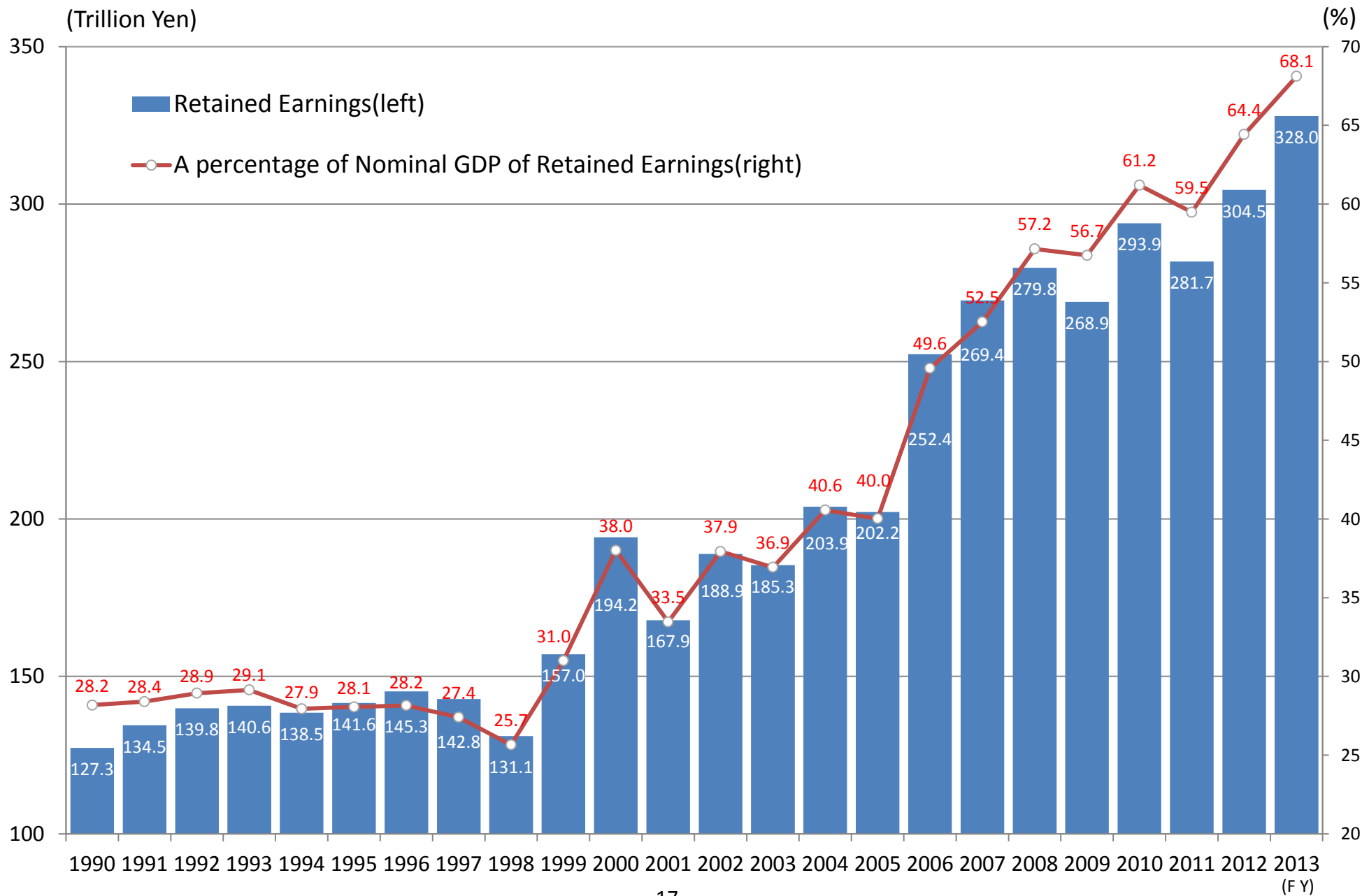
(Note1) FY1975-2012: Settlement, FY2013: Including supplementary budget, FY2014: Initial budget

(Note2) Following various bonds are excluded: Ad-hoc Special Deficit-Financing bonds issued in FY1990 as a source of funds to support peace and reconstruction activities in the Persian Gulf Region, Tax reduction-related Special Deficit-Financing bonds issued in FY1994-1996 to make up for decline in tax revenues due to a series of income tax cuts preceding consumption tax hike from 3% to 5%, Reconstruction bonds issued in FY2011 as a source of funds to implement measures for the Reconstruction from the Great East Japan Earthquake, Pension-related Special Deficit-Financing bonds issued in FY2012,2013 as a source of funds to achieve the targeted national contribution to one-half of basic pension.

(Note3) General Account Primary Balance is calculated by subtracting Primary Expenditures from the sum of Tax Revenues and Other Revenues: It is different from the Central Government Primary Balance on SNA basis.



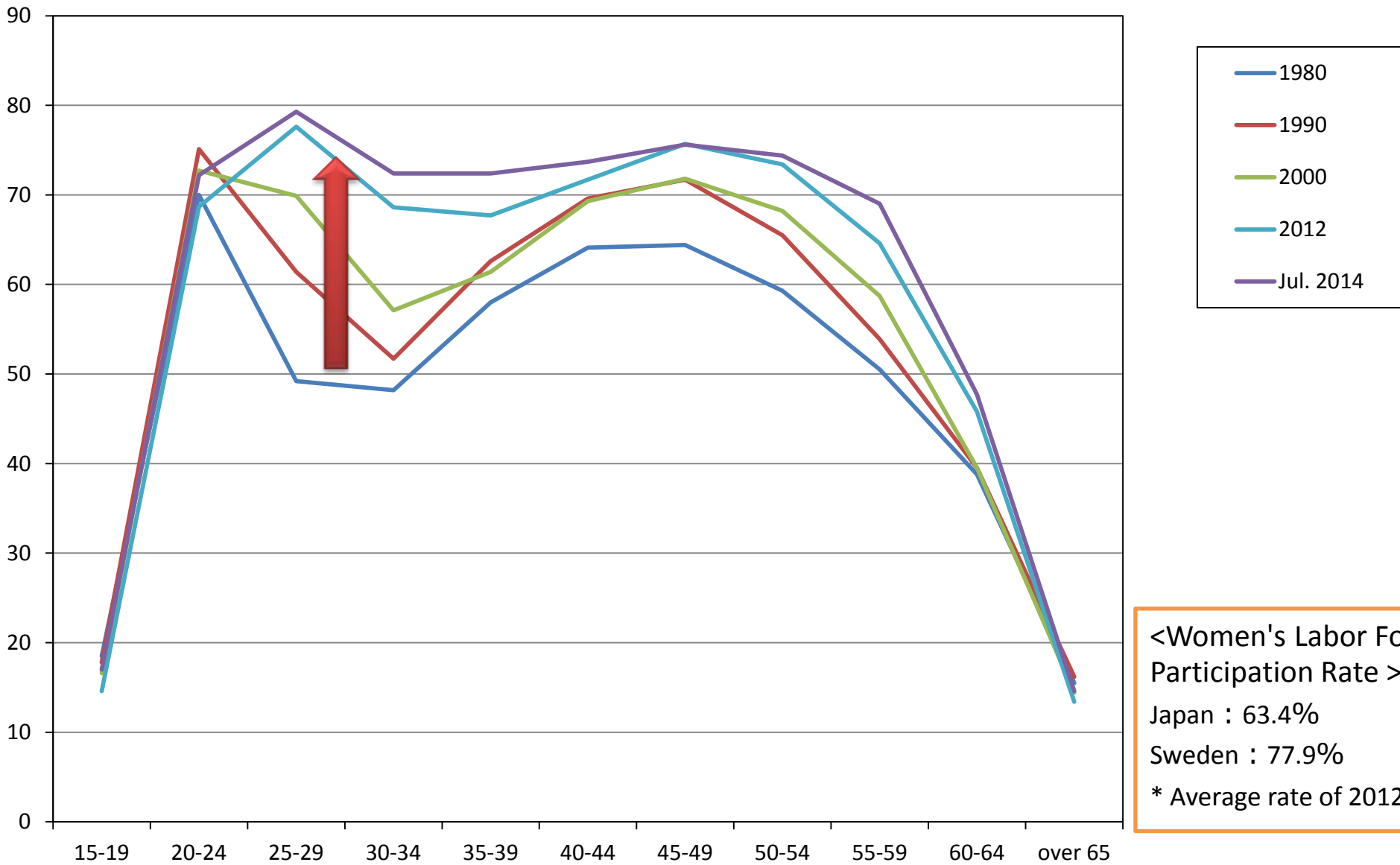
# 6. Retained Earnings



Source: Cabinet office, Ministry of Finance

# 7. Women's Labor Force Participation Rate

(%, rate indicates year average)



<Women's Labor Force Participation Rate >  
Japan : 63.4%  
Sweden : 77.9%  
\* Average rate of 2012

# 8. Japan's External Sustainability

