

## 「My trip to Paris to speak at Japan Euro Dialogue Seminar」

Haruo Shimada

### I. Introduction

This is a brief report of my recent trip to Paris to participate and give a speech at a dialogue seminar which was held by IFRI (French Institute of International Relations) and Japan Ministry of Foreign Affairs as well as JFIR (Japan Forum on International Relations) in the evening of March 9, 2015.

The seminar is planned as a part of a series of international symposiums under the common title “The Future Which is Created by Cooperation of Japan and Europe: in Pursuit of Governance by Law and Prosperity” . On November 21, 2014, the symposium was held in Tokyo by inviting European influential opinion leaders. These opinion leaders are expected to give reports when they returned to their home countries on what they learned by joining such symposium and related activities to various intellectual audiences in Europe so that they can contribute to promote in Europe understanding of Japan and Japanese foreign policies.

One of the invitees, Dr. Claude Meyer, senior advisor, center for Asian studies, IFRI and associate professor of CERI, Sciences Po., who met myself during his visit to Japan last fall strongly demanded to invite myself to a seminar of intellectual and professional audiences in Paris. Responding to his request, Ministry of Foreign Affairs decided to invite me to the seminar mentioned at the beginning.

It was already in February when I first heard from ministry of foreign affairs that they wish me to accept this offer of invitation. Since my time table usually is fully booked by two or three months in advance, so when my secretary checked my schedule she found that it looks practically impossible to accept this offer.

However, she found a slight possibility by canceling a couple of appointments on March 9. She told me that it could be possible for me to participate to this seminar but I could stay only one night in Paris. A round trip of Paris and Tokyo, 12 hour flight plus few hours each way, with only one night stay over in Paris is obviously a very hard plan to travel. I talked this plan to

my wife, she first said to me that she would tolerate me to do so if it was twenty years ago, but she would not let a 72 year old husband to take such a bold attempt. However, a few days later she changed her thought for some reason and tolerated me to accept the offer from the ministry of foreign affairs.

My secretary whispered that this project suits me well as a professor of economics and much interested and involved in international affairs. In fact, she knew well and assisted me to an important extent that I had been preparing a 51 pages long and informative report on Abenomics for my own professional interest much before I was given this offer so that this offer apparently looked to her an ideal opportunity for me to discuss my paper with important intellectual audience.

The staff of ministry of foreign affairs worked well to arrange the best possible trip toward the last minute. They apparently advised ANA (All Nippon Airways) to provide me the best service they could offer for a business class passenger on both ways between Tokyo and Paris.

The schedule turned out to be very tight as imagined. I took off Haneda airport shortly after noon of March 9, arrived in Charles de Gaulle airport shortly after 15:00. The staff of Japan Embassy in Paris took a good care of me to bring me to the hall of IFRI in time for the seminar which is scheduled for 17:00 to 18:30 while letting me check in the hotel on the way.

Since the traffic was smooth I was able to arrive at the hall half an hour earlier so that I had a chance to talk to main players of the panel. Professor Claude Meyer, Dr. Francois Nicholas, senior economist, director of center for Asian studies of IFRI, director of Asian research of IFRI, who is supposed to chair the pane, Ambassador Mr. Yoichi Suzuki of Japan, who represents the sponsor of this project gave a brief speech at the beginning of the seminar. The hall was soon filled with audience.

At the chat before the session, Ms. Nicholas advised that on the three arrows of Abenomics, spend not much time on the first and second arrows, but explain well the content of the third arrow, which is growth strategy. She added that the first two arrows are rather well known in Europe but the content of the third arrow is not as much known, and this is the area that European audience wish to know and understand. This advice was helpful for me to sense the focus

of interest of audience so that I could plan resource allocation within the given 25 minutes appropriately.

The discussion was good which I will introduce in some detail later. In the seminar, professor Clause Meyer gave a well organized introductory speech for 10 minutes which was followed by my speech of 25 minutes. Then the floor was opened for Q and A.

## II. The Back Ground

I was much impressed by the keen interest and breadth and depth of knowledge of French intellectual people on Abenomics.

Aside from general curiosity and intellectual capacity of elitist French people, I suspect that there are due reasons why European people are interested in Abenomics and have been paying keen attention to its development and deployment.

Europe, particularly of Eurozone, has been experiencing a difficult time of dragging stagnation for recent years particularly since the onset of Greek crisis shortly after the Lehman crisis. The problem of Greece has been transmitted to other countries such as Italy, Spain and even to France through the channels of financial institutions and network. European central bank, ad hoc EU committees, and the governments of EU member countries, IMF and other relevant institutions tried to prevent the issue to develop to major financial crisis.

They soon had to face the problems unique to EU itself. That is the very nature of loosely combined multi-country system which makes it much more difficult to determine and conduct remedies speedily and thoroughly.

North and South differentials in terms of productivity and wills of fiscal discipline. This difference is particularly large between Germany and Mediterranean countries such as Greece and Italy. The sharp contrast in the fiscal difference makes the consolidated and unanimous policy decisions much more difficult than otherwise.

Still another fundamental problem unique to EU is that while the currency is unified into EURO across different countries within the EURO zone, fiscal policies are basically not unified and left to the self discipline of each of the member countries which are only bound by uniform criteria such as the maximum annual government debt to GDP.

Imposing the same currency on member countries of different productivity without obliging them to accept autonomous inter-country fiscal adjustment, the country of low productivity tends to lose international competitiveness of its industries and consequently accumulate fiscal deficit while the country of high productivity, in contrast, tends to increase industrial competitiveness and consequently does not suffer from the issue of fiscal deficit.

These structural difficulties unique to EU made it more difficult to conduct for EU swift, uniform and thorough remedies and structural reform on the financial sector and institutions compared to a country like the US. While the reform of financial institutions and fiscal policies has remained insufficient, EU, particularly of EURO zone, began to suffer from deeper stagnation which may well lead EURO zone into chronic deflation.

In order to prevent the economy from falling into deflation, many countries attempted extra-ordinary policy of QE (quantitative easing). Since the interest rate has remained very low in many countries in the wake of the Lehman crisis, central banks supplied huge amount of “base money” by purchasing national bonds and other financial commodities. The Federal Reserve Board of the US has conducted three phases of major QE since the Lehman crisis and consequently supplied abundant liquidity not only to the US but also to the entire world, which helped to encourage economic activities of various countries.

Japan plunged into the group of QE since the spring of 2013 under the slogan of Abenomics. ECB has been increasing the supply of base money side by side with US, UK and other major countries. However, since the threat of falling into deflation has become increasingly serious in recent years, there has been increasingly serious policy debate as to whether ECB should promote a distinctively large scale QE to stimulate the EURO zone economies. Some argue that ECB should do it such as Mr. Mario Draghi, the president of ECB, while others such as financial leaders of Germany and Netherlands oppose against

such a policy choice arguing that such massive QE would weaken the fiscal discipline of deficit prone countries.

After a long and intense debate, ECB finally made a major decision on January 22 that it will start a major QE from March. It was decided that (1) ECB will provide extra-ordinary large amount of base money in order to stimulate the EURO zone economies. The total of 60 billion EURO bonds (of which 45 billion is government bonds of member countries) will be purchased by ECB and central banks of member countries every month. (2) This QE is promoted in pursuit of generating inflation of 2% starting from March 2015 presumably until September 2016.

And on March 9, this operation started. It was an unexpected coincidence that our symposium was held on the same day.

There are arguments both pros and cons about this action of large scale QE. Those who justify this action such as Mr. Mario Draghi and his supporters argue that by providing sufficient amount of liquidity to the market, investment will be encouraged, economic growth will be stimulated, and consequently prices will increase so that EURO Zone economies can avoid trapping by fatal chronic deflation.

Contrary, those who oppose and criticize this QE such as Mr. Jens Weidmann of the Bundes Bank, and Mr. Klaas Knot, he'd of De Nederlandische Bank argue that this action has a danger of weakening or even losing the fiscal discipline in many EURO Zone economies particularly in Southern and Mediterranean areas and thus deteriorates the EURO Zone economies rather than to promote growth. They emphasize that structural reform policies such as labor market reform should be needed rather than macro monetary policy as huge across the board monetary easing policy.

Following the initiation of this voluminous QE, markets have responded in various aspects as early as next day. Prices of government bonds of Northern European countries, where market evaluates relatively good fiscal discipline, went even higher so that financial institutions are obliged to buy bonds with very low or even negative returns. In contrast, bonds of countries which are deemed with low level of fiscal discipline yield high returns and quickly became scarce assets relative to demand. The exchange rate of EURO relative

to other major currencies started to drop rapidly in the wake of QE which gives rise to hope of increasing export of EURO economies.

Given this back ground of economic policy debate, Abenomics provides an interesting case of real experiment. Abenomics aims at salvaging Japanese economy out of sticky chronic deflation which persisted nearly two decades since the mid-1990s. If Abenomics successfully realized good economic growth with decent rate of inflation by the policy mix of three arrows, the experience of Abenomics will be of important reference or model for European policy makers. If it is judged to have failed, then, the case of Abenomics will be of reference to them as the experience not to learn or follow.

European observers seem to know well about the first two arrows: The first arrow is an extra-ordinary policy of supplying large volume of base money to generate inflation and change the mindset of people from deflationary to inflationary expectations. It seems to have succeeded to the extent that stock prices and corporate profits increased and modest inflation started. However, it aggravates the implicit risk of losing fiscal discipline of the government and the public.

The second arrow is an active fiscal policy by supplying fiscal spending whenever necessary. This policy certainly helped maintain the stability of the economy in the process of transformation, but risks the attainment of the ten year fiscal reconstruction plan which Japan committed to achieve.

Although the third arrow was shot twice in June 2014 and June 2015, their effects are less clear and understood not only by foreign observers but also by Japanese public partly because the list of policies are too many, and partly because structural reform policy tends to take long time before policy effects begin to emerge.

Since the onset of Abenomics at the beginning of 2013, economic performance has been mixed or somewhat disappointing for the subsequent two years. Except for good news about stock prices, momentum of inflation seems to have been weakened with unfortunate sharp decline of oil prices, the pace of wage hikes has been slower than price increases so that real wages have been declining for the recent year and a half. Economic growth has been secularly slowing for these two years. Slight increases in economic growth in the most recent quarter seems to indicate some hope for year 2015.

Indicators and economic outcomes seem mixed. It is much too early to judge either the success or failure of Abenomics particularly because the growth strategy, consisting largely of structural reforms, of Abenomics takes time to yield any results. For us to make any meaningful evaluation of Abenomics, we need to understand the components and their progress of growth strategy. It is for this reason, I was invited to contribute to this symposium in Paris.

### III. The Symposium: My presentation and Q&A.

The symposium started punctually at 17:00 in the lecture hall of IFRI. Following the introductory remark of Dr. Francois Nicholas, of IFRI, Ambassador Mr. Yoichi Suzuki gave an opening speech explaining why this symposium was to be organized and emphasizing the importance of mutual understanding between Japan and Europe as well as the importance of this symposium.

Following Ambassador's speech, Dr. Claude Meyer, senior advisor of IFRI spent 10 minutes speaking systematically as to why European people, particularly French, are interested in "Abenomics" explaining comprehensively economic issues which EU and France are faced that have much relevance to what Abenomics attempts to tackle in Japan.

Then the floor was given to me. After thanking the invitation to this symposium, I got on the substance of my speech.

I emphasized first that the primary strategic intent of Abe administration is to get Japanese economy out of the sticky deflation which lasted nearly 2 decades. I heard this directly from Mr. Yoshihide Suga, minister of chamber, when he gave speeches twice in my seminar. The package of economic policy called "Abenomics" was devised as a strategy to salvage Japanese economy from the depth of chronic deflation.

Abenomics is said to consist of three arrows: (1) monetary policy of extra-ordinarily large scale QE (quantitative easing), (2) active fiscal policy, and (3) growth strategy by means of structural reform.

(1) The first arrow: monetary policy. This is to supply distinctively large amount to "base money" to the market so that economic activity is stimulated

and exchange rate of yen gets reduced and through these channels prices will begin to rise to generate inflation. The real intent of this policy is to change the “deflationary expectation” of people to “inflationary expectation.”

In April 2013, Mr. Haruhiko Kuroda, president of Bank of Japan who was just appointed, declared in his first press conference that BoJ will commit to generate inflation of 2% within 2 years, and to double the supply of base money to achieve this goal.

This declaration gave strong impacts to foreign major speculators and investors before it affects the mind set of Japanese public. Expecting a greater supply of yen they plunged to large scale future selling of yen to gain huge profits, and also invested huge amount of fund into Japan’ s stock market anticipating sharp rise of stock prices.

Due largely to such moves, exchange rate of yen dropped sharply as much as 20% in 2 months, and stock prices jumped more than 80% in half a year. Expectations of increased corporate profits and drastically increased stock prices certainly changed the atmosphere of Japanese economy and society.

These developments may certainly be regarded as the merits of the first arrow of Abenomics. However, one must note that this first arrow has a huge implicit risk associated with it. This is because much of the Japanese government bonds provided to the market is purchased by BoJ, which may be interpreted as the government loses fiscal discipline. If the market judges it is indeed the case, then prices of JGB may drop sharply which will have serious consequences to Japan’ s fiscal and economic situation.

(2) The second arrow: active fiscal policy. In the process of transformation from deflationary to inflationary economy, the government is prepared to supply fiscal spending timely to smooth and support the process. In fact the government provided voluminous extra-ordinary budgets a few times in addition to largest annual budgets in history. These active fiscal spending certainly supported the stability of the economy.

However, this active spending made it more difficult to attain the planned fiscal reconstruction. Japan is suffering from a huge government fiscal deficit which amounts to as much as 1200 trillion yen or 2.4times of GDP. The Japan’ s fiscal reconstruction plan proclaims that in ten years from 2010 till



2020, the deficit of primary balance which was 32 trillion yen or 6.7 percent of GDP be eliminated. The plan stipulates that the deficit should be halved by 2015, the mid point of the 10 year plan, namely, 16 trillion yen or 3.2 percent of GDP.

While this figure on the orbit of the plan is barely attained in 2015, it is deemed difficult to stay on the orbit of the plan after 2016. Indeed, the cabinet office of Japanese government predicts that on the better scenario of economic growth, namely, 3 percent nominal and 2 percent real annual growth for 10 years, the primary balance will still have deficit as much as 1.6% of GDP. Judged from the actual performance, the economy will not likely to achieve this good scenario up to 2020, and the deficit will be much larger realistically.

If Japan is judged from experts in the market that it cannot satisfy its fiscal reconstruction plan, it is possible that they judge that the Japanese government cannot maintain fiscal discipline. This could trigger a sharp decline of prices of JGB, which will jerk up interest rates and aggravate already huge government deficit swell like a snowball, namely, the fiscal crisis.

(3) The third arrow: growth strategy. All these risks can be absorbed if Japanese economy grows at a sufficiently high rate for a lengthy period. In order to attain the objective of fiscal reconstruction plan and to enrich the fiscal basis to provide necessary social security services to the aging society, it is desirable that the economy will grow annually more than 3% in real terms and 4% in nominal terms for the coming decade.

Therefore, the growth strategy is the most critical part of the Abenomics. If Japanese economy grows well thanks to Abenomics, then we can say that Abenomics is a successful strategy. If not, Abenomics will be a failure. Prime Minister Shinzo Abe and his team members devised the third arrow in June 2013. This is now called the first version of the growth strategy of Abenomics.

The report of the plan of strategy consists of 94 page papers. It consisted largely of three action plans (1) industry recovery plan which emphasizes renewal of industry and employment structure, (2) creating strategic market in such areas as health, energy and infra-structure, and (3) international

deployment plan of increasing free trade share in the total trade from the current 19% to 70% in five years.

The growth performance of Japanese economy in the wake of announcement of this growth strategy has been rather disappointing. The growth rates (adjusted to annual figure) of four quarters of 2013 were 4.9% and 3.5% in the first and second quarters, but after the announcement, dropped to 1.3% and even down to 0.3% for the third and fourth quarters. Prime Minister Shinzo Abe and his team decided in December 2013 to write the new growth strategy by June 2014 and implement it forcefully to generate growth of Japanese economy. Since this is the topic which French audience and experts wish to know most, let me explain in some detail the second growth strategy in what follows.

#### IV. The Second Growth Strategy of Abenomics

Prime Minister Shinzo Abe emphasized that in the second growth strategy he and his team tackle vigorously to break into the so-called “bed rock” of regulations and vested interests which disturb efficient economic activity. Major areas identified as bed rock include: agriculture, medical services, work rules etc.

The Abenomics team consists largely of four committees, (1) industry competitiveness committee, (2) regulatory reform committee, (3) economic and fiscal policy advisory committee, and (4) national strategic zone committee. In fact these committees have been working vigorously shortly after the disclosure of the first growth strategy on the second growth strategy.

The second growth strategy was disclosed in June 2014. The strategy consists of 3 major reports from the committees mentioned above, which altogether amount to more 300 pages and cover several hundreds of policy items. Financial Times and the Economist described this as “not an arrow but a bundle of one thousand needles” (of acupuncture).

My frank judgement is that the attempts of structural and institutional reform by Prime Minister Shinzo Abe and his team are much more outright, serious, and forceful compared to most of the previous administrations in post war Japan as an effort to change outdated structure and institutions of Japanese economy.

Despite the fact that the second growth strategy includes many policy statements and not easy to read through, it is important for us to understand to judge whether the Abenomics is meaningful and realistic or not. To fill the knowledge and information gap, let me introduce or explain 10 important areas focused by the current growth strategy of Abenomics.

### 1. Renewal of industry and employment

Part of reasons for the sluggishness of Japanese economy is considered as the allocation of industry and labor resources in the outdated sectors. To promote the reallocation of industry and labor resources toward more modern and future oriented sectors, the government enacted “competitiveness reinforcement law” in December 2012. This law authorizes to control subsidies to promote such reallocation of industry resources.

### 2. Corporate governance and capital market

Japanese corporate governance has been viewed as less transparent and more closed and inward oriented than it needs to be. Also, capital resources have been utilized less effectively and efficiently than they should. To counteract such deficiencies, Abe administration promotes such measures as follows:

(1) Revising Corporate Law was enacted by which publicly open corporations, regardless of its size, should appoint at least one independent member of the board, (2) All the publicly listed companies have to determine “governance code” to secure the transparency of management for investors, (3) Major professional investment organizations have to determine and follow “stewardship code,” (4) Change the allocation policy of the fund as much as 130 trillion yen of the Government Pension Investment Fund from low risk low return assets to higher return assets.

### 3. TPP negotiations

TPP or Trans Pacific Partnership is one of the most thorough free trade agreement. Abe administration thinks that joining TPP will help develop Japan’s free trade arrangements with trade partners and secure large free trade market opportunities.

Currently the US and Japan are the two countries which have outstandingly large market shares among those participating to the negotiation. The US joined the group in 2010 and Japan in 2013. Negotiators of participating countries have kept negotiate conditions of trade, investment, intellectual property rights etc. encompassing more than twenty areas earnestly since 2013.

As negotiation proceeded, the focus has been narrowed down on some difficult areas which need political initiatives to reach agreements. Particularly important is fuller liberalization of a few agricultural items for Japan and some conditions of auto trade for the US, and intellectual property rights and government involvement in corporate activities for some Asian countries.

An important issue is whether and when the US congress will allow the president to have TPA or trade promotion authority which can speed up the process of negotiation. Since 2016 will be the year of presidential election in the US, which will paralyze the political and administrative activities in the US other than the election, we hope that the US, Japan and some other countries which have important stakes on the prospect of negotiation will take courageous actions to lead TPP to the general agreement with in 2015.

#### 4. Agricultural reforms

Abe administration wishes to make agriculture a growth leading sector by reforming its structure in which resourceful farmers and agricultural corporations can do their business more freely and actively by means of abolishing non productive regulations and breaking vested rights. Agricultural reform is an important element of Japan' s effort to prepare for joining TPP. Prime Minister Sinzo Abe took a strong initiative to promote reform in the following three areas: (1) abolishing rice acreage reduction policy, (2) reform of national agricultural cooperatives, and (3) reform of land ownership regulations.

(1) Abolishing rice acreage reduction policy implies that by lifting the policy which has been isolating rice farmers from market competition for 40 years letting farmers face up the competitive menace to encourage their effort for productivity increase.

(2) Reform of national agricultural cooperative means by stripping their authorized rights to control uniformly local agricultural cooperatives,

letting the local cooperative find and develop their own ways to improve efficiency of agricultural production.

(3) Reform of land ownership regulations implies by relaxing regulations imposed on farm land ownership, making it easier for productive large-scale farmers and agricultural corporations to own the land to produce high productivity farming.

## 5. Employment Regulatory Reform, Utilization of Female Human Resources, and Introduction of Foreign Workers

(1) Reform of working hour regulation: Work ways of Japanese workers regulated by the law are apparently the factor which disturbs productivity of Japanese workers. Indeed, Japanese labor productivity in recent decades is much lower than counterparts of competitive advanced economies. This is due to Japanese outdated labor law which was enacted shortly after the defeat in World War II imposing the same working hour regulations on both blue and white collar workers in an attempt to abolish status differentiation at the workshop.

Now that service industries provide more than 80% of employment, the fact that the labor law which was designed to regulate production workers 70 years ago not surprisingly disturbs creative service workers from achieving high productivity. Prime Minister Shizo Abe and his team earnestly try to introduce rewards not paid by working hours but rather by performance and also introduce the status of “exempt” for white collar workers. These attempts have been resisted by Japan ministry of labor and trade unions, and have been realized only partially.

(2) Utilization of female human resources. Japanese female workers’ average labor force participation rate itself is more or less comparable of advanced Western nations. However, unique for Japanese female labor is that during the age range of child bearing and rearing, the rate stays very low. This means that the human capital accumulation is terminated during the child rearing period and is not used in the latter part of their career because they can get only casual jobs.

Prime Minister Shinzo Abe earnestly advocates the necessity for Japan to make use of female human resources and try to enrich the public systems to support and assist child dealing, introduce the tax system which is less

discriminatory for working wives, and promote non-discriminatory practices of employment and promotion for females at the workshop. Results of such efforts have not been visible yet but will be realized in the long run.

(3) Utilization of foreign workers. Since Japanese labor force is predicted to shrink sizable in the long-run due to shrinkage of population, it is only natural to introduce foreign human resources to supplement such a decline. Abe administration tries to relax the limits which have been imposed on introduction of foreign workers in an attempt to supplement increasingly scarce workers particularly in construction industry in the face of unfilled demand in North eastern regions devastated by earthquakes and also by increasing demand arising from constructions relating to 2020 Tokyo Olympics.

It is notable, however, that Abe administration is highly careful that their effort not to be interpreted as opening doors generally for foreign workers worrying about the negative attitude of the Japanese against general introduction of foreign human resources. I will touch upon this problems later.

## 6. Shrinking Population and Revitalization of Regions

In May 2014, a well qualified study group disclosed their research result which tells us that if the current inter-regional mobility will be unchanged for the next 40 years, a half of Japanese communities (cities, towns and villages) will begin to disappear after 40 years because female population of child bearing age range (20 to 40 years old) will be halved in those communities. Since the study disclosed actual names of communities which are predicted to disappear within half a century or so, it gave a big and serious repercussion in Japanese society and policy circle.

Since politicians are very sensitive to regional population movement because it relates directly to changes of votes, Abe administration had to be serious to tackle the issues arising from such population changes in regions. The government launched a major campaign and policy efforts under the name of “revitalization of regions.” Under the campaign, the administration plans to provide variety of subsidies to communities particularly of remote regions, and solicit ideas from communities to revitalize themselves. My frank view is that the mega-trends of population would not be easily altered by such subsidies and solicitation of ideas.

## 7. Reduction of corporate tax rate.

Prime Minister Shinzo Abe is taking a strong initiative to reduce corporate income tax rate in order to enhance competitiveness of Japanese corporations and also make Japan a more attractive place for foreign companies to locate themselves in Japan.

The current corporate income tax rate in Japan is 35.6% which is only comparable with that of the US and much higher than many of developing and advanced economies which Japanese businesses have to compete. Prime Minister Shinzo Abe has been advocating to reduce the rate to less than 30% in several years. Toward the end of 2014, reflecting the strong will of the Prime Minister, the government tax panel decided to reduce the tax rate by 2.5% in 2015. Further reductions are necessary to realize the target the Prime Minister proposes.

## 8. Medical reform

Japan has enjoyed half a century ago, a couple of important merits in the world of medicine such as one of the lowest medical costs to GDP and the longest longevity of the population. However, with changes of mega-trends such as aging of population, development of medical technology which jerks up costs of medicine dramatically, and slowing of economic growth which makes increasingly difficult for the population to bear the increasing medical costs.

For the last several decades, the government strengthened the regulations both on prices and quantity of medical services, which resulted in weakening merits of market competition such as innovation. Under such circumstances, the public suffered from heavy burden of medical costs, mal-allocation of medical services in spite of practically bankrupted public medical insurances, deficit ridden hospitals and deterioration of quality of medical services. Japanese medical industry and policies now have a myriad of problems.

Abe administration views that medical industry can be potentially a leading sector of Japan's growth and also international competition. Challenges to realize such goals will need dozens or hundreds of thorough reforms and innovations. For recent few years, Abe administration has been focusing only

on relaxation of one peculiar policy regulation, which prohibits the patient to receive publicly uninsured treatment while receiving insurance benefit on related treatment.

Abe team, particularly of regulatory reform committee, has been working hard to relax this regulation in spite of strong opposition and resistance by ministry of labor and welfare and by the association of medical practitioners. Abe team has attained some progress while it has been dwarfed in the process.

## 9. Social security reform

Social security reform is perhaps the single largest policy issue for Japan to secure sustainability in the long run. Under the mega-trend of rapid aging of population the social cost of aging has been growing dramatically. Currently the ratio of “national burden” or the average burden of tax and social security payments for the public is 40 percent for the society with 25% of population of age 65 and older. In 2050, when the proportion of aged population will be about 40%, the national burden is estimated to rise up to 72 or 73 percent, which means the public can have only a quarter of income as dispensable. This obviously means Japan will lose “sustainability” in the long run.

This is a consequence of absence of major and effective reforms of social security system for more than half a century. Japanese social security system was constructed around 1960 when the population was very young. While the population has been aging dramatically in recent half a century, no major and fundamental reforms have been executed so that the current system is completely outdated and unfitted to the society where population is aging and the age structure is almost opposite relative to half a century ago.

While knowing the importance and the need of comprehensive, fundamental and thorough reforms of social security system, Abe administration so far has not been able to launch such reforms. They tried some reforms toward the end of 2014, which ended up with reforms to impose higher contributions from relatively richer people and larger corporations.

## 10. National strategic zones



Abe administration advocates the policy of designating selected areas in Japan where special deregulations and institutional reforms can be realized, the reforms which cannot be applied to other areas. So far, a dozen or so of areas have been identified as “national strategic zone.” Outcomes from proclaimed deregulations or special policies have not been visible yet.

#### 11. Government’ s request for wage hikes

Prime Minister Shinzo Abe asks strongly industrial circles to raise wages of workers. This is because Abenomics will not succeed without appropriate wage increases which are hopefully higher than the rate of inflation. If not, people will suffer from declines of real wages and lose confidence on Abenomics.

Since mid-2013 when inflationary trend began to be visible, Prime Minister Shinzo Abe earnestly asked leaders of industrial and financial organizations to persuade managers of their member companies to raise wages. In the wage round of 2013, large firms increased wages by 2 percent or so, however, smaller firms were not quite able to raise wages high enough to maintain real wages.

Toward the end of 2014, Prime Minister Shinzo Abe asked the cooperation of industrial leaders even more earnestly to raise wages. The industry leaders agreed to respond the request of the administration for the wage round of 2015. It is expected that real wages will increase somewhat in 2015 partly because of wage increases and partly because of decline of oil prices which slows down the pace of inflation.

#### V. Will Abenomics Succeed?

The contents of Abenomics could be summarized as above. Now the major question to be probed at the Paris conference of IFRI is the question as to whether or not Abenomics will succeed. Let me suggest a few observations in an attempt to think about this question.

First, let me review briefly the economic performance for the recent two years since the outset of Abenomics.

The relationship between prices and wages has been rather disappointing. Prices have been rising reflecting the effects of unprecedented monetary easing particularly by increased import prices pushed up by reduced exchange rate of the yen due to the expectation of drastic increase of base money. In contrast, while wages have been rising but the pace of rising is more modest than prices so that real wages have been declining for year and a half since summer 2013.

Consumer price index has been increasing 0.9% in July–September 2013, 1.4% in October–December, 1.5% in January–March 2014, 3.6% in April–June after raising consumption tax from 5 to 8%, 3.3% in July–September. In contrast, wages increased for the same period, -0.4%, 0.4%, 0.8%, and 1.5%. As a result, real wages have kept declining since summer 2013 until now. This trend may well give rise to dissatisfaction and distrust against Abenomics on the part of the public.

Export performance has also been disappointing. It was expected that export would increase substantively reflecting sharp declines of exchange rate of yen thanks to the unprecedented increase of base money. However, exports have increased only sluggishly, if any, since the beginning of 2013 until recently and did not contribute to enhance the economic growth rate.

Economic growth performance for the same period has also been disappointing. Quarterly growth translated to annual growth rate has been 6.0% in January–March 2013, 3.0% in April–June, 1.6% in July–September, -1.5% in Oct.–December, and 5.8% in Jan.–March 2014 reflecting rush purchases right before the increase of consumption tax rate, -6.7% in April–June, -1.9% in July–September, and 1.5% in October–December.

Aside from these short-run economic performance, it is necessary to assess the performance of Japanese economy in medium to long-run particularly because much of the content of “growth strategy” of Abenomics is structural reform which will take a rather long time to materialize its intended effects.

In view of long term growth, many experts and research organizations have been studying the growth potentials of Japanese economy. According to a summary of the cabinet ministry, the estimated growth potentials are disappointingly low.

For example, IMF estimates 0.8% for the coming decade, Mitsubishi Research Institute 0.6% and 0.5% each for the first 5 years and latter 5 years of coming decade and 0.4% afterwards. Nikkei center estimates 0.6% for the decade. Nissei (life insurance) Institute estimates 1.1 and 1.2% for the first 5 and latter 5 years of the same period, Mitsubishi UFJ (bank) Research Institute estimates 0.7% and 0.6% for the same period. Most optimistic is Daiwa Research Institute estimates 1.3% and 1.3% for the same period.

Economic growth rates attainable under such assessments as above will not be good enough to solve any of the major tasks that Japan needs to tackle to maintain its sustainability. One is the fiscal reconstruction. We have already seen that cabinet ministry of Japanese government discloses their recent estimate of primary balance up to the target year of 2020. According to their estimation, primary balance will still be left with the deficit equivalent to 1.6% of GDP or 11trillion yen in 2020. The above mentioned estimates of growth potential suggest that Japanese economy will not even be able to achieve the good scenario which the government uses for their estimation.

We have examined rather in detail the contents of the second growth strategy of Abenomics. If we scrutinize the contents, we would be left with an impression that it is the policy to change the nature of Japanese economy which has been forged during the period starting from the postwar reform and through the postwar growth. We would be left with the question as to whether this is the “growth” strategy.

The growth strategy which can be most effective for developing economies like China today or Japan during the 1960s and 1970s is public investments to enrich infra-structure such as railways, highways, ports, cities etc. This type of growth strategy could no longer be effective to a matured economy like Japan after 1980s. Japan now suffers seriously from the huge government debt because the public investments conducted voluminously to enhance economic activity since the late 1980s actually did not generate economic growth.

The estimates of growth potential as quoted above are affected heavily by the decline of population and workforce in the near future. They seem to indicate that given the heavy constraint of shrinking population, economic growth as such could not be conceived.

What the growth strategy of Abenomics tackles is the change of the structural and institutional nature of the Japanese economy forged during the 70 years of postwar process of development. I think that this is a fully legitimate strategy because one could not hope to generate economic growth without altering the structural nature of the economy which is hardened by accumulated vested rights of interest groups. However, if the structural reform of Abenomics would be promoted well, would the growth be generated under the heavy constraint of long-term shrinkage of population?

I suggested a conceptual break through to overcome this apparent impasse by referring to several cases of remarkable economic growth attained in the world even under severe constraints of population or other economic resources such as Dubai and Singapore. These are very small countries and may not be useful references for a mid-size country like Japan. I quoted, therefore, the most useful and powerful model which Japan should learn from is “Japan 70 years ago.”

Japan 70 years ago is a completely devastated archipelago because of bombing in the process of defeat in the war. Japan lost all the vested rights in the world, and even lost 3.1 lives of population. Countries suffering from this much of damage, in many cases, could not possibly hope to recover and grow powerfully.

However, Japan grew remarkably and achieved the status of the second largest economy in the world only next to the United States within a quarter of century afterward. Question is why and how Japan made it. My view is that Japan was able to materialize this miracle because Japan denied and abolished completely the prewar system of the country and created an entirely new country where all people are freshly encouraged to work hard and compete.

Reforms of Abenomics are good. I fully appreciate the efforts of Prime Minister Shinzo Abe and his team. But it seems that Abenomics is not strong enough and thorough enough to deny, abolish and change completely the postwar economic system which has been constraining and holding down the potential capability of Japan and Japanese to generate the powerful economic growth required in the new era.

I suggested 9 major reforms and policies which should be pursued to change more thoroughly to liberate the potentials that the Japanese and their country

have to generate fresh growth in the forth coming era. Since I have described such policies in detail in my essay, entitled "Two Year Experience of "Abenomics" and Forthcoming Challenges for Japanese Economy" which was carried as a previous essay in my blog (<http://www.haruishimada.net/blog/2015/02/two-year-experi.html>) , I will not repeat it here.

## VI. Questions and comments from the floor

Following the presentation, many points were raised by questions and comments from the floor. Let me introduce some of them.

On the general performance of Japanese economy, audience expressed fairly positive evaluation. The growth rate has been certainly low, but the economy experience steady mild growth. Stability of the economy is appreciated. I responded that the current growth rate is far less than what is needed to overcome the danger of fiscal crisis and to enrich social security to take care of increasing costs of aging of population.

The huge fiscal debt attracted attention. The government's debt is certainly very large. But it was pointed out that most of the JGB is held by the Japanese so that it may not be sold as easily and quickly as the case of Greece a few years ago. In other words, Japanese economy should be in fact more stable than it looks in the very large amount of government debt. I responded that more than 10 percent of JGB is held by non Japanese and the Japanese investors as well, largely of financial institutions, may well sell the JGB if they judge holding JGB will lose the capital value.

Aging of population and the robustness of the social security also attracted attention. This issue is perhaps the most serious issue that Japan is faced in the medium and long-run.

Reflecting one of my policy recommendation to legislate the immigration law, a question was raised from the floor if Japan really needs to introduce foreign human resource meaning introduction of foreign workforce could not be the solution to counteract the serious issue of shrinking population and workforce which Japan is faced and will be faced more in the future.

I responded to this question emphasizing the need for Japan to make the conditions for accepting foreign immigrants transparent by enacting the immigration law. Japan currently has only immigration control law and refugee recognition law but does not have an immigration law, which is rather rare among advanced countries in the world. Many countries are competing hard to attract and incorporate capable and talented foreign human resources as their nationals. The fact that Japan does not have immigration law which prescribes the conditions to accept foreign people as Japanese nationals is a serious drawback in attracting capable foreign people.

The question was raised as how professor Thomas Piketty was received in Japan. I commented that he was very much welcomed by Japanese media. There is a Piketty fad almost as a fever. His huge book became the best seller. Books to explain the gist of his voluminous book were also sold well.

Japanese media simplified its content that the modern economies have a built in nature of expanding income differentials of people because the rate of return on capital tends to be higher than rate of economic growth. I pointed out that he wrote many other things to describe the modern history of economies. Perhaps the single most important finding is that the process of enlarging differentials were dissolved twice by world wars.

I added that his recommendation in Japan to levy heavy capital gain tax on the rich would not give meaningful effect to mend the problem of growing income differential given the structure of income differential in Japan.

I was impressed particularly by the fact that the audience, mostly French, had a keen attention and good knowledge on Japanese economy and Abenomics. I hope that my presentation is of some use to satisfy their curiosity.

## VII. After the symposium

After the seminar, I was picked up by my old and good friend, Professor Frederic Jenny of ESSEC. We were joined by his wife in a good French restaurant in downtown and enjoyed dinner and talk, which we did not have for a long time.

Next morning, I had an appointment with a person in Paris to arrange a project in the near future. Before lunch, Embassy staff escorted me to Japanese Embassy

in Paris and had a nice talk with Ambassador M. Yoichi Suzuki for about an hour. We discussed much about changes of mega-trends of Japan and the world and about the future. The lunch was planned as a working lunch with a journalist of Le Figaro. His questions were sharp and I explained in some detail the structural reform policies of Abe administration.

The embassy staff drove me directly from the restaurant to the airport. The ANA flight took off shortly afterwards in the evening of March 10, and arrived at Tokyo Narita airport in the morning of March 11, and I resumed my work at my office which was waiting for the last few days.

After the trip, it looked to me almost unbelievable that this much of things were done spending only two days and a half including a round trip flight between Paris and Tokyo. The trip was fruitful not only by having been able to exchange views with European intellectual on Japanese economy, but also particularly personally to have been able to see my good old friends in addition to make new friends. All this was done by being helped by nice people and their good will.