Can Japan Change?: Abenomics and Its Future

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Two Faces of Abenomics

A. Abenomics as Politics
* Three A’s: Abe, Aso, and Amari
* Abe->the first arrow; reflationary policy
* Aso->the second arrow; “old-fashioned” pork barrel fiscal stimulus
* Amari-> the third arrow; industrial, target policy
* Abe’s reliance on METI

B. Abenomics as Economics
Abe’s Political Strategy

* Cautious, patient, yet resolute
* Fights against the BOJ, avoids fighting against the MOF, seeks help from the METI
* The BOJ front: adoption of inflation targeting, appointment of reflationary governor and deputy governor, Haruhiko Kuroda and Kikuo Iwata.
  * Revision of the BOJ law?
A “Policy Regime Shift” (Romer 2013)

- Contrast with the 2001-06 (original) QE experience
- The Old Regime: accepting deflation
  - Long on excuses, short on action
  - No explicit inflation targeting
  - The BOJ people
- The New Regime: fighting deflation
  - Emphasis on Expected inflation
  - Inflation targeting
  - New people: Kuroda and Iwata
How Abenomics Works

First Arrow

Expected Inflation ↑
Real Interest Rate ↓

Asset Prices ↑
Consumption

Investment

Yen Depreciation
Export

Government Expenditure

Output Gap ↓
Inflation

Demand for Loan
Loan ↑

AD ↑

Demand for Labor
Wage growth
How Kuroda Thinks

- Sense of history (Kuroda 2005)
- A macroeconomic policy interpretation of the Japan’s long stagnation
- Deflation: distinction between Legal responsibility and economic causes (Kuroda 2005, 173-183)
- The role of exchange rate: quite important
- Bubble: Too much expansionary monetary could lead to a bubble (Kuroda 2005, 90), but bursting a bubble was a more serious mistake (Kuroda 2005, 100-102)
- Fiscal consolidation
1. The First Arrow: Could it reach the target?
2. The Second Arrow: What is the Impact of the consumption tax hike?
3. The Third Arrow: Would it even fly?
4. Redistribution, the Missing Fourth Arrow?
5. External Environment: Would the World Economy favors Abenomics?
6. Media: Do they change their mind?
7. Politics as Ultimate Risk: Would Abe Survive?
Right now: they are quite satisfied with their policy
Most likely further action in the case of a drastic fall in expected inflation rate, i.e., change in policy purpose most unlikely
More tools?
  * Increase the purchase of volume of long-term JGBs
  * Purchase of other assets, more likely ETF
  * Purchase of foreign bonds off the table
  * “Forward Guidance”? 
Change in policy target? Less likely now.
  * Targeting nominal GDP, Unemployment Rate
2. The Consumption Tax Hike

* Negative effects expected
* **Permanent** ¥8 trn. Negative impact from FY 2014
* **Temporary** Offsetting Stimulus package ¥5 trn.
* The Repetition of the 1937 US, or 2010 UK?
3. The Growth “Strategy”

* Two different economic policy philosophies
  * A. METI: Old style industrial, export-oriented, target policy with government sponsored funds
  * B. Heizo Takenaka and market-oriented reformers
    * Deregulation, private management of public facilities, corporate reform (outside board member)
    * So far, retreat of market-oriented reformer camp
## Things to come: Next Regime?

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Impacts of Abenomics

- The First Arrow, and TPP are the main pillars.
- With deflation to 2% inflation in 2 years: Phillips curve + Okun’s Law
  - Unemployment: $4.3 + 0.5 = 4.8\%$ (2012) to $2.5\%$ (2014)
  - Okun coefficient: 3
  - Real GDP growth rate: 6.9 % increase in two years
- The Second Arrow: about 0.6% increase in one year
Impacts of Reform?

* TPP:
  * 0.8% increase in growth rate (with all tariffs abolished)
  * 2% (Peter Petri, with all non-tariff barriers abolished)
* Others?
  * Regulatory reforms have positive impact on growth rate (Haidar 2012)
  * Past experiences are not encouraging (Hoshi and Kashyap 2011, 2012)
* But, reasons to be a bit more optimistic: the First arrow matters on the growth front as well
“God grant me the serenity to accept the things I cannot change, the courage to change the things I can, and the wisdom to know the difference” (Reinhold Niebuhr)
References

* Romer, Christina (2013), "It Takes a Regime Shift," [https://emlab.berkeley.edu/~cromer/It%20Takes%20a%20Regime%20Shift%20Written.pdf](https://emlab.berkeley.edu/~cromer/It%20Takes%20a%20Regime%20Shift%20Written.pdf)