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C O L U M B I A U N I V E R S I T Y I N T H E C I T Y O F N E W Y O R K

Japan's Abenomics: Recovery Leading to Good Growth?

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Abstract

As Japan enters an era of political stability under Prime Minister Shinzo Abe, Japan is poised to recover from the past two decades of mediocre performance toward good, sustained economic growth. Abe, a strong leader who will not be replaced until at least 2016, is giving priority to a much-touted economic program termed Abenomics, comprising three “arrows”: ending deflation and achieving price stability, defined as a 2 percent annual increase in the CPI; achieving stable, long-run, full employment GDP growth over the next decade; and fiscal consolidation bringing an end to enormous government budget deficits and debt. This paper explores these programs, focusing on macroeconomic demand management and the growth strategy. I briefly consider the Trans-Pacific Partnership, and changes in the agricultural, electric power, corporate, and international trade sectors, and identify the key challenges to implementing good economic growth. Despite these challenges, Abe's strong political statements, public support, and the power of the LDP leadership provide hope for long-awaited change in Japan.

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What a dramatic sea change in Japan from late summer 2012 to late summer 2013! More in the politics than in the economy, but even more in the mood, sentiment, expectations, and hopes of consumers and businesses. The selection of Tokyo for the 2020 Olympics is a welcome further boost to Japanese spirits.

With two decades of mediocre economic performance and ineffective government policy, a widespread sense of resignation and malaise had prevailed. After six years of weak governments reflected in annual changes of prime minister and exacerbated by split control of the two houses of the Diet, Japanese were sick and tired of it all. Voters were eager to support a government committed to economic change. Now Shinzo Abe's Liberal Democratic Party (LDP) seems set to govern for at least three more years until the next upper house elections in December 2016, and probably beyond.

For three years and three prime ministers, the Democratic Party of Japan (DPJ) held the government but was struggling and losing support. Rather than hold on, in November 2012 it announced a lower house election for December, sooner than required. Everyone assumed the DPJ would lose, the LDP would win, and Abe would become prime minister. And that happened, but the DPJ still held the upper house. Now, after comfortably winning the July upper house election in coalition with its small Komeito Party ally, Abe and the LDP fully control the Diet.

These solid electoral victories reflect more a disenchantment with the DPJ than a strong endorsement of the LDP. Still, Japan is entering an era of political stability. Attention can now be focused on the challenge of economic revitalization and the further renewal of confidence that is both a condition and a result of revitalization. The substance of economic policy objectives and proposals has not changed in recent years. But now Abe has the political power. And he has strongly stated his political will to achieve three major economic policy objectives.

The first is to end 15 years of small but pernicious deflation. The specific goal is to achieve what the Bank of Japan (BOJ) appropriately terms price stability, defined as a 2 percent annual increase in the CPI. Small CPI increases in July and August suggest deflation is being conquered—July's 0.7% annual rate was the highest since November 2008.

The second is to achieve stable long-run GDP growth over the coming decade of 2 percent in real terms, and 3 percent in current prices.

The third is fiscal consolidation—bringing to an end the enormous government budget deficits and ever-rising amount of government debt as a percentage of GDP, and eventually even reducing that ratio.