“The Role and the Place of Japan in the International Economy”

[Slide1: Title]

1. Introduction

Distinguished Guests,

Ladies and Gentlemen,

Today I am very pleased and honoured to be given this opportunity to speak to you, the students of the prestigious Bucharest University of Economic Studies, about the present condition of the Japanese economy and its challenges.

[Slide2: Japan Basic Information]

First, let me give you some basic figures about my country – Japan’s population is approximately 120 million people, almost 6 times as large as that of Romania. The total land surface is approximately 380,000 square kilometers, 1.5 times as big as that of Romania. Looking at the economy, the GDP is 4.9 trillion USD (nominal, 2013), 25 times as large as that of Romania, while the per capita GNI of Japan is 46,000 USD (World Bank Country Data), approximately 5 times as high as that of Romania.

[Slide3: Japan Basic Information]

2. Japan’s place in the world economy

(1) Now, looking at Japan from the point of view of its economic relations with the world, first of all, based on UN data, 2013, the total value of world trade was 18.45 trillion USD when expressed as total exports. Of that, Japan’s total exports in 2013 amounted to 710 billion USD, or approximately 3.8% of total world exports. (UN data)

Japan’s GDP in 2013 was 4.9 trillion USD, which represents 6.5% of total world GDP. US’s GDP is 22% of world GDP, China’s is 12% and Japan follows in third place. (UN data)

When we take a look back at how things stood 15 years ago, in the year 2000, the US, the world’s largest economy, accounted for 30% of the world GDP, while Japan was in second place with 14%. At that time, China’s GDP was 3.6% of world GDP, while the EU as a whole accounted for 26.4%. (World Bank data)

The population of Japan is approximately 120 million, smaller than the population of the US (310 million people) or that of China (1.35 billion people) (World Bank data), but, until 2010, when it was overtaken by a fast-rising China, Japan had had, for a very long time, the second largest GDP in the world. Japan has now the third biggest GDP in the world, but in 2013, it was still the second largest contributor to the United Nations Regular Budget, having a share of 10% after the United States of America (22%), and being followed by Germany (7.1%), France (5.5%) and the UK (5.1%). These are the top five most important contributors to the UN Regular Budget. (data from the Ministry of Foreign Affairs of Japan)

Next, let's take a look at Japan's position in the world from the point of view of foreign investments. First of all, in 2013, the world foreign direct investments (FDI) were 1.41 trillion USD. USA's foreign investments were worth 338 billion USD, the EU's was 250 billion USD, China's was 100 billion USD (without Hong Kong and Taiwan), while Japan's was 135 billion USD.

Recently, Japan has invested quite a lot overseas, having held the 2nd position in the world, after USA, in foreign direct investments over 2010-2013.

Thus, at the end of 2013, Japan's accumulated foreign direct investments (by assets) went up to 1.1 trillion USD (JETRO data).

[Slide4: History of Economic Development]

(2) Talking a little about the history of Japan's economic development, we can say that Japan had already been a prominent industrialized nation even before World War Two (WWII), but through the Second World War (WWII) the country lost almost all its industrial production capabilities. After the war, if I am to compare the stages of development of Japan's economy to the stages in someone's life, I can say, first of all, that from the 1950s to the 60s Japan experienced its "fast-growing period of infancy", when the country started to rebuild its economy and grow its industrial base at a fast pace, after having its entire industrial base destroyed in the war. In 1964 Japan hosted successfully the first Tokyo Olympic Games and started to operate the Shinkansen bullet train.

Secondly, from the 1970s to the 1980s Japan experienced its period of "bold adolescence", when Japan's exports grew rapidly and the country had a trade surplus every year, causing severe friction between Japan and its trade partners, in particular the US. In 1971, the first appreciation of the Japanese yen against the US dollar was decided and in 1973 the floating exchange rate scheme was finally introduced. That was the period in which the Japanese economy successfully overcame two oil shocks (1973 1nd 1979) and started growing considerably by enhancing energy efficiency and developing energy saving technology. It was also the period in which Japan started to actively make investments abroad with its strengthened yen.

Thirdly, between the 1990s and the 2000s, Japan experienced its period of “stormy youth”, with its ups and downs, represented by the economic and financial bubble and its burst. Good things come to an end, though, as the economy is also a living thing.

Let me explain this way. The trade surplus earned from exports accelerated the appreciation of the Japanese yen against the US dollar. It hit hard the export industry. For this reason the government implemented large scale fiscal as well as monetary relaxation policies, which injected surplus liquidity into the market. As a result banks started to lend money more easily and ultimately caused an “asset bubble” by speculation. The stock market and the real estate market overheated. Inflation occurred. But, even after the domestic asset bubble burst, Japan was left with a strong yen and entered long-term deflation, with falling prices and wages. Due to the strong Japanese yen, domestic companies started to restructure themselves and transfer their production base out of Japan. Thus investments were directed to foreign countries, like US, China, the EU, South East Asian countries, while domestic investments stagnated and consumption shrank, causing a vicious circle.

To look for a similar example of “economic bubble and burst” in Romania’s recent past, maybe we can talk about the moment, after the year 2000, when it became certain that Romania was going to join the European Union (EU). From that moment on there was acceleration in investments as well as consumption in the country, until the Lehman Shock serious financial crisis of 2008, which plunged the world economy into recession, affecting Romania too, whose economy suffered a severe contraction as a result.

After the bubble burst, Japan had to struggle with the double sufferings of deflation and low economic growth for 15-20 years. In December 2012 Mr. Abe took the office of the Prime Minister and started to implement the economic policies called Abenomics, aimed at ending this negative cycle and transforming the Japanese economy into a sustainable and positive one. It is said that Abenomics has changed significantly the Japanese economy as well as the image towards the Japanese economy. Japan has gradually come out of the long recession and is slowly returning to economic growth. Japan is back on the world stage. Perhaps we can say that now, Japan has entered its period of “steady adulthood”.

[Slide5: Japan Trade Relations]

3. Japan’s place in the world trade

(1) Now, let’s take a deeper look into Japan’s trade. Japan’s main trade partner countries in 2014 were China (approximately 20%), USA (approximately 13%), South Korea (approximately 6%), followed by others (data from the Ministry of Finance). Of course, trade with the European Union (EU) is quite significant, representing approximately 10% of the total. The main products that Japan exports to the rest of the world are the so-called high-tech goods

like machine tools, construction machinery, transport vehicles, electronic goods, and it imports mainly natural resources like oil and liquefied natural gas (LNG).

(2) Looking at trade relations between Japan and Romania, based on Japanese data, the value of Japanese exports to Romania in 2014 reached JPY 35.4 billion (or approximately 253 million EUR at an exchange rate of 1 EUR = 140 JPY) and Romanian exports to Japan amounted to JPY 52.4 billion (or approximately 374 million EUR). The main products that Japan exports to Romania are auto parts, auto vehicles, electric circuit parts, pumps and centrifugal machines, synthetic rubber, etc., while Japan imports from Romania mainly lumber, clothing articles, wood for construction, wooden furniture, footwear and such. If we look at statistics, we notice that Japan's commercial exchanges with Romania only account for 0.05% out of Japan's total trade value. As the interdependence of the world economy is on the rise, there is still much more room for an increase in this area.

(3) To give you some information about Japanese companies present in Romania, there are approximately 150 Japanese companies registered in Romania. Of these, 25 are large manufacturing companies, which have 46 production plants in Romania and employ more than 30,000 people here.

(4) Japan is trying to promote trade and investments with countries throughout the world, including Romania, not only through the WTO framework, but also by making active efforts to conclude trade agreements with various countries and regions. In this respect, the negotiations for concluding an Economic Partnership Agreement (EPA) between Japan and the European Union are ongoing, and, hopefully, a broad agreement will be reached in the course of this year. Once this agreement has been signed, trade and investment relations between Japan and Romania are expected to be activated.

Also, as I will explain next, the Abenomics policies aim to not only revitalize the Japanese economy, but also place a great importance on its "integration in the world economy". From this point of view, along with the EPA between Japan and the European Union, the TPP agreement negotiations with countries form the Pacific region, starting with the United States, is also crucially important. At the same time, I am happy to tell you that the Economic Partnership Agreements (EPA) between Japan and Australia was largely agreed on last year.

[Slide6: "Abe-nomics" 3 Arrow Policy]

4. **Abenomics**

Let's get back to the Japanese economy. After the bubble burst in the early 1990s, despite recording some moderate growth, Japan has been suffering from a prolonged period of deflation. What is Abenomics? It is the package of policies that Prime Minister Abe announced in 2012 to tackle the long-term deflation, that is, falling prices and wages, and an over-valued Japanese currency, the yen, so as to revitalize the Japanese economy. It was the international media that named this package “Abenomics”.

(1) The basic framework of Abenomics

The essence of Abenomics is the simultaneous release of “three arrows”: the 1st one, a “bold monetary policy”, aimed at wiping away the deflation mindset by increasing the liquidity in the economy through monetary easing by the central bank, the 2nd one, a “flexible fiscal policy”, which is a temporary initiative of the government to boost demand by making a large budgetary expenditure at just the right time, and the 3rd one, “growth strategy measures that stimulate longer-term private investments”, whose goal is to attain a society in which the true abilities of the individual and of private businesses are allowed to shine through, by implementing further reforms and structural adjustments. The targeted goal is to break away from the economic contraction cycle and to achieve a strong and sustainably growing economy that encourages innovation and the creation of new businesses, more jobs and higher personal incomes.

[Slide7: Recovery Track of Japan’s Economy]

(2)The results of Abenomics

Abenomics is made of these “three arrows”, as explained. Of these, the first two have already been implemented and have shown good results. The stock index, the economic growth rate, company balance sheets, employment levels, etc. have all registered considerable improvements.

In particular, one year after the Abe Government took office, by the end of 2013, the indexes that measure economic growth already started to show considerable signs of improvement, and, comparing with the rest of the world, the pace of economic growth of Japan reached a relatively high level. Nevertheless, suffering a direct hit from the first action of the fiscal reform, that is, the increase in the consumption tax from 5% to 8% on April 1st 2014, the real GDP in the second and third quarters of 2014 recorded a contraction. The economy returned to growth at length in the fourth quarter, however, registering an annual increase in GDP of 1.5%, and is currently moving towards overcoming deflation and a steady recovery.

Abenomics, the initiative of Prime Minister Abe, so far, has been appreciated by the market as well. On April 10th this year, for instance, the Nikkei average of the Japanese Stock Exchange reached 20,000 JPY, the highest level of the past 15 years. Company profits also reached the highest levels in recent history.

On the other hand, as it can be seen from the first and second “arrows”, many of the implemented policies were on the supply side. It is believed that it would be difficult to keep the growth only with them. That is why it is important for demand side policies that stimulate consumer spending, capital investments and exports to be implemented at the same time, in order to create a sustainable synergy effect. Among such measures, efforts have been made recently to increase workers’ wages. In Japan, every year in March “the spring offensive” takes place, when wage increases and bonuses are negotiated between employees and their bosses. Prime Minister Abe appealed repeatedly to companies to increase wages and, in March this year, responding to the expectations of employees, the increase of base salaries at large companies reached a 20-year high.

[Slide8: Growth Strategy to Stimulate Private Investments]

(3) Growth strategy measures that stimulate private investments

Now the Abe Government is committed to shoot, with firm determination, the “third arrow”, aimed at a growth strategy that stimulates private investments. Needless to say, private enterprises are the main players of the market economy.

The growth strategy, based on four main pillars, depicts a road map intended to lead the Japanese economy along the path of sustainable growth, bringing out the true potential of both individuals and private companies, through structural reforms. The four elements of the growth strategy are:

1. “investment promotion” policy measures, such as deregulation and lowering investment taxation, etc.

2. “further integration of the Japanese economy in the world economy”, in other words, encouraging Japanese companies to expand their business abroad as well as welcoming increasingly more foreign direct investments to Japan,

3. “making better use of human resources”, by creating an inclusive, better work environment, in which women, young people as well as the elderly can get more actively involved,

4. “the creation of new markets”, in an attempt to solve issues that the entire world is facing right now, such as low birth rates and longevity.

The reason why the growth strategies of the past governments have not worked well and, therefore, have not materialized in a boost in private investments, lies with the fact that a strong determination of the government to carry them out was lacking. Learning from past experience, the Abe Government is committed to engaging all the policy resources at once, including the budget, regulation reforms, the tax system, etc., in pursuing this growth strategy.

[Slide9: Fiscal Consolidation Targets]

(4) Fiscal Consolidation/Debt Problem

You might already know this, but, looking at the Japanese state budget, Japan has a big deficit in what regards both the fiscal balance and the primary balance. The fiscal deficit refers to the fact that the government revenues are exceeded by the government expenditures, such as investments in the social capital, social security costs, which include health costs and pensions, etc., and the salaries of public sector employees.

The primary balance shows the gap between government revenues and expenditures that exclude the principal plus interest payments on government debt.

When we look at the fiscal 2015 general state budget, only 60% of the government expenditure is covered by current tax collections. The rest of 40% depends on government debt to be transferred to future generations. According to data of the Ministry of Finance of Japan, in 2014 the total accumulated public debt amount reached 230% of GDP.

The situation requires that the government should mobilize quick and flexible measures in the short and medium run but, at the same time, it is crucial that the government makes a strong commitment to implement sustainable fiscal policies in the long run. So, the current government decided to reduce the primary balance deficits at both state and local levels, by half in 2015 compared to 2010 levels. In 2010 the primary deficit was -6.6% of GDP; now, in 2015 this would mean -3.3% primary deficit.

Based on the effectiveness of the fiscal management so far, this fiscal consolidation target seems to be, hopefully, achievable. Moreover, the current government will release by this summer a plan, which will detail how the current primary budget deficit will turn into a surplus by 2020.

Restoring Japan's fiscal health is an important topic not only for the Japanese economy, but for the management of the world economy as a whole. It is one of the "international commitments" that Japan must fulfill. In order to implement sound fiscal management the Japanese government must raise taxes to increase government revenues. However, as I have mentioned before, it is feared that, increasing the consumption tax, which contributes the most to government revenues, will have a cooling effect on the mind of consumers. That is why, the increase by 2 percentage points in consumption tax, from 8% to 10%, the second consecutive increase in a year and a half, which was originally scheduled to take place this year in October, was postponed by one year and a half, and it will be implemented without fail, with some breathing space, from April 2017 instead.

By the way, monetary policy is another important instrument to be used along the path to achieving fiscal health, which aims to combat deflation and to bring the Japanese economy to a suitable and healthy 2% inflation rate. Nowadays, in view of low international oil prices, this inflation target has not been realized yet, but, once reached, it is expected that, combined with economic growth, it will contribute to higher government revenues, in both real and nominal terms.

Looking into the government expenditures, a very big cause for the budget deficit lies in social security, like the public pension and the healthcare insurance that covers the entire population of Japan. In order to restore fiscal health, redesigning a sustainable social security system, while rethinking the balance between the benefits and the contributions of each individual and the burden-sharing among the people, is an urgent task.

5. Conclusions

Finding ways to pull out of the long-term deflation, which Japan has been struggling with, at the same time, looking at how to steadily decrease public debt levels and trying to tackle the challenge of a rapidly aging society and falling birth rates, which lead to an increasingly smaller workforce, all are the challenging issues for Japan. In addition, there is a growing income gap, especially affecting part of the younger generation, whose lifestyle doesn't seem to improve no matter how hard they work. Japan is now working hard to find answers to overcome these problems, while desiring to contribute to the welfare of Japan's future generation as well as to that of the entire world.

[Slide10: Thank you for your attention]