Abenomics and Japan's Future

Viara Bojkova

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Global Policy Institute, London Metropolitan University,
Electra House, 84 Moorgate, London EC2M 6SQ

ABSTRACT[1]

The Japanese policy package known as “Abenomics” began in early 2013 with three major components – monetary, fiscal and structural reforms. This paper focuses on all three components, showing the measures undertaken by different authorities and exploring to what extent the whole package contributes to stimulating the economy; discussing existing current issues and difficulties that may hinder the progress of the policy package, particularly, the third arrow that proves to be very weak. The paper shows that Abenomics in its early two-year-period has had positive effects on inflation expectations, actual inflation as well as financial markets, and to a certain level on the GDP growth[2].

[1] We thank Neil Cantwell at the Japan Foundation, Junko Watanabe of Kyoto University and Chris Dixon of the Global Policy Institute, London, where the authors are senior research fellows.
[2] I am grateful to Prof C. Dixon and Prof S. Whimster for their extremely valuable comments and suggestions.

1. Introduction

The Japanese Prime minister, Shinzo Abe, reaffirmed his political position in the recent snap election and returned to power on 24th December 2014. His immediate priority was countering the 2014 downturn in the economy that followed the 2014 rise in the sales tax through a series of new fiscal measures partly financed by a supplementary budget of 3.5 trillion yen. The government expects this stimulus package to boost the GDP by 0.7%[3] in 2015. However, the new measures and their likely outcome have to be understood in the context of the continuation of the economic programme that since early 2013 has been the hallmark of Mr Abe's premiership.

The programme, which has been labelled Abenomics, is a mixture of monetary expansion, fiscal stimulus and structural reforms of the highly regulated economy. These policies, which have become known as the "***Three Arrows***" of Abenomics, are aimed at countering Japan's long-term problems of persistent deflation and low growth. For some Abenomics pushes at the boundaries of expansionary activity and even represents a monetary regime change that takes the BOJ use of unconventional monetary policy during 2001-06 and 2010, to a different level[4]. At base monetary policies under Abe, like the earlier programmes, are aimed at supporting aggregate economic activity through asset purchases when the traditional instrument of monetary policy was not available due to the zero bound constraint. Such asset purchases operate directly on different segments of the yield curve, reducing rates at different maturities while the short-term rate is at zero. However, as the IMF's economist David Lipton explains the quantitative and qualitative easing (QQE) under Abe differs from what had been tried before in that it is a bigger and bolder commitment, and is complemented by fiscal and structural reforms in order to lift growth and inflationary expectations and support price momentum[5]. As such Japan's current policies have attracted a great deal of interest, not least amongst Western policy makers.

While the interest grows around the world, domestic opposition may jeopardise the development of Abe's policies, and further bolder actions may be urgently needed to guarantee the success of his programme. For any progress is conditional not only on national political willingness and policy shaping, but also on domestic market agents' responsiveness to policy shifts, external shocks and a global inflationary environment.

With the above in mind, this paper explores the extent to which Abenomics is contributing to the economic growth of Japan, particularly through monetary and fiscal expansion, for the structural reforms are still at a too early stage for any meaningful evaluation to be made, though, as is discussed below (Section IV), there are serious concerns that they may prove a major stumbling block.

[3] FT, Japan cabinet approves ¥3.5 trillion stimulus spending, 27th Dec. 2014

[4] Bojkova V., "Current results of Japan's QQE", GPI Opinion, January 2014; Romer C., "It takes a regime shift: recent developments in Japanese Monetary Policy through the lens of the Great Depression", University of California, Berkeley 2013

[5] Lipton D., "From deflation to reflation: Japan's new monetary policy framework, effectiveness, and broad lessons" at BOJ-IMES Conference "Monetary Policy in a post-financial crisis era", 28-29th May 2014, Tokyo

2. The First Arrow – Monetary Policy

The Bank of Japan's monetary policy framework under the Abe administration was introduced in early 2013, aiming to achieve price stability. As a result, the Bank replaced the long-time used "price stability goal" with the "price stability target". More specifically, in April 2013 the newly appointed Governor of the Bank of Japan (BOJ), Haruhiko Kuroda, promised that the 2%-inflation target would be reached within two years via asset purchases and a doubling of the monetary base. The latter involved an annual increase of some 80 trillion yen (10-20 trillion yen more than in the past). For this purpose, the BOJ purchases Japanese Government Bonds (JGBs) so that their amount outstanding increases annually at 80 trillion yen (30 trillion more than in the past). In addition, the average maturity of BOJ's remaining earlier JGBs purchases would be extended to some 7-10 years (an extension of 3 years compared with the past)[6]. These measures were to be accompanied by the BOJ purchase of exchange-traded funds (ETFs) and Japan real-estate investment trusts (J-REITs) so that the amounts outstanding increase at an annual rate of some 3 trillion yen and 90 billion yen, respectively. Thus, as the Japanese economist Ito has noted the BOJ's measures comprise a combination of pure-QE (a large-scale expansion of BOJ's balance sheet) and credit easing (purchases of ETFs, J-REITs and extension of the average remaining maturity of its purchases of JGBs)[7].

The sheer scale of the increase in the monetary base alone (Table 1) does suggest that the BOJ may reasonably be expected to achieve the price stability target of 2%, but given the likelihood of changes in market circumstances due to volatile oil and other commodity prices, the price target stability will take longer to reach than was originally expected. In addition, the monetary expansion has lowered long-term rates (Table 3) and depreciated the yen, which will boost further the growth of export companies and make their investment decisions easier taken.

Table 1: Monetary Base (Amounts outstanding at end of period)

Time period	Monetary Base, 100 million yen
2011/12	1,250,788
2012/12	1,384,747
2013/12	2,018,472
2014/12	2,758,740
2015/01	2,786,054

Source: Bank of Japan, February 2015

[6] Bank of Japan, "Expansion of the Quantitative and Qualitative Monetary Easing", 31st October 2014, Tokyo
[7] Ito T., "We are all QE-sians now" IMES Discussion Paper No. 2014-E-5, Institute for Monetary and Economic Studies, Bank of Japan, 2014

Table 2: Inflation of Japan (CPI, monthly basis)

Before Abenomics		*Under Abenomics Policies*			
Month/2012	*Rate*	*Month/2013*	*Rate*	*Month/2014*	*Rate*
January	0.20%	January	0.00%	January	-0.20%
February	0.20%	February	-0.10%	February	0.00%
March	0.50%	March	0.20%	March	0.30%
April	0.10%	April	0.30%	April	2.08%
May	-0.30%	May	0.10%	May	0.39%
June	-0.50%	June	0.00%	June	-0.10%
July	-0.30%	July	0.20%	July	0.00%
August	0.10%	August	0.30%	August	0.19%
September	0.20%	September	0.30%	September	0.29%
October	0.00%	October	0.10%	October	-0.29%
November	-0.40%	November	0.10%	November	-0.39%
December	0.10%	December	0.10%	December	0.10%

Source: www.inflation.eu, February 2015

Table 3: Japan 10-Year and 30-Year Bond Yields (monthly data)

Month/2013	*30-Y Rate*	*10-Y Rate*	*Month/2014*	*30-Y Rate*	*10-Y Rate*
January	1.866	0.786	January	1.644	0.627
February	1.823	0.665	February	1.650	0.588
March	1.514	0.556	March	1.714	0.647
April	1.610	0.611	April	1.714	0.622
May	1.770	0.867	May	1.688	0.577
June	1.829	0.844	June	1.688	0.569
July	1.816	0.798	July	1.681	0.537
August	1.764	0.720	August	1.627	0.497
September	1.712	0.688	September	1.611	0.526
October	1.634	0.594	October	1.580	0.463
November	1.649	0.612	November	1.393	0.425
December	1.738	0.737	December	1.267	0.330

Source: www.investing.com/rates-bonds

The most immediate and strongest impact of QQE has been on the financial markets, which responded well to the expansion in 2013 with the Nikkei 225 stock market index rising by 57%, and further by 10% in 2014. More significantly, there are, as is discussed below, some encouraging signs that Abenomics is having positive impacts on inflationary expectations, actual inflation and GDP growth.

Table 4: Nikkei 225 (monthly data)

Month/2013	*Adjusted Close*	*Month/2014*	*Adjusted Close*
January	11,138	January	14,914
February	11,559	February	14,841
March	12,397	March	14,827
April	13,860	April	14,304
May	13,774	May	14,632
June	13,677	June	15,162
July	13,668	July	15,620
August	13,388	August	15,424
September	14,455	September	16,173
October	14,327	October	16,413
November	15,661	November	17,459
December	16,291	December	17.808

Note: Adjusted Close - close price adjusted for dividends and splits

Table 5: Japan GDP growth rate (quarterly data)

Quarter	GDP growth rate	Quarter	GDP growth rate
IQ/2012	1.1%	IIIQ/2013	0.6%
IIQ/2012	-0.6%	IVQ/2013	-0.4%
IIIQ/2012	-0.6%	IQ/2014	1.6%
IVQ/2012	-0.3%	IIQ/2014	-1.9%
IQ/2013	1.4%	IIIQ/2014	-0.5%
IIQ/2013	0.8%	IVQ/2014	0.6%

Source: www.tradingeconomics.com

2.1. Impact on Inflationary expectations

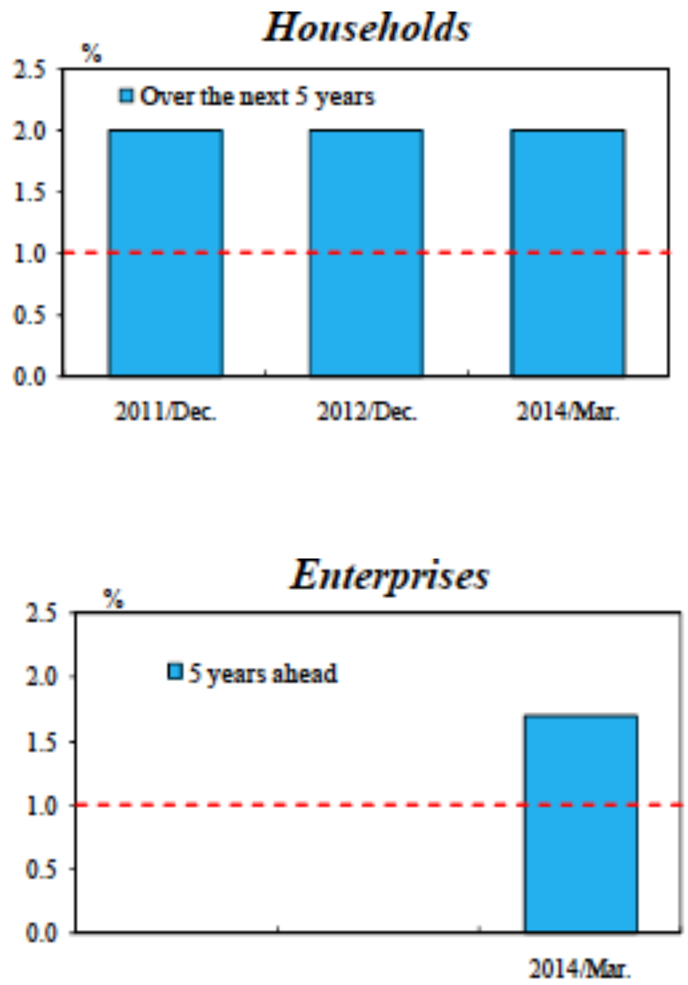
There were during 2014 some encouraging signs of increases in inflationary expectations. These have been variously estimated at between 1.0% and 1.4%, and the actual inflation responded as expected[8]. While in October 2013, the Consensus Economics survey of professional forecasters showed that the 2-year inflation expectations had risen to 1.8% in Japan[9]. More pessimistically, Hausman and Wieland (2014) estimated that Abenomics had raised long-term inflation expectation by only approximately 1-percentage point, a view reiterated by the Bank of Japan[10]. However, the BoJ surveys of the expectations of Japanese households and enterprises (which excluded the effects of the scheduled consumption tax hike) suggested that households expected inflation to reach its targeted 2%-level over the next 5-year

[8] Bank of Japan (The year-on-year actual inflation rate was negative 0.1% in December 2012, rose to 1.6% in December 2013 and 2.38% in December 2014)

[9] Consensus Economics Survey of professional forecasters – it is a leading economic survey organization that provides forecasts and views of economists.

period, while enterprises expected inflation to be around 1.6% (Fig.1). As a result, it is difficult to conclude that the monetary QQE has yet had a credible effect on long-term inflationary expectations, and that the 2%-target will be reached during 2015.

Figure 1: Inflationary Expectations of Households and Enterprises in Japan



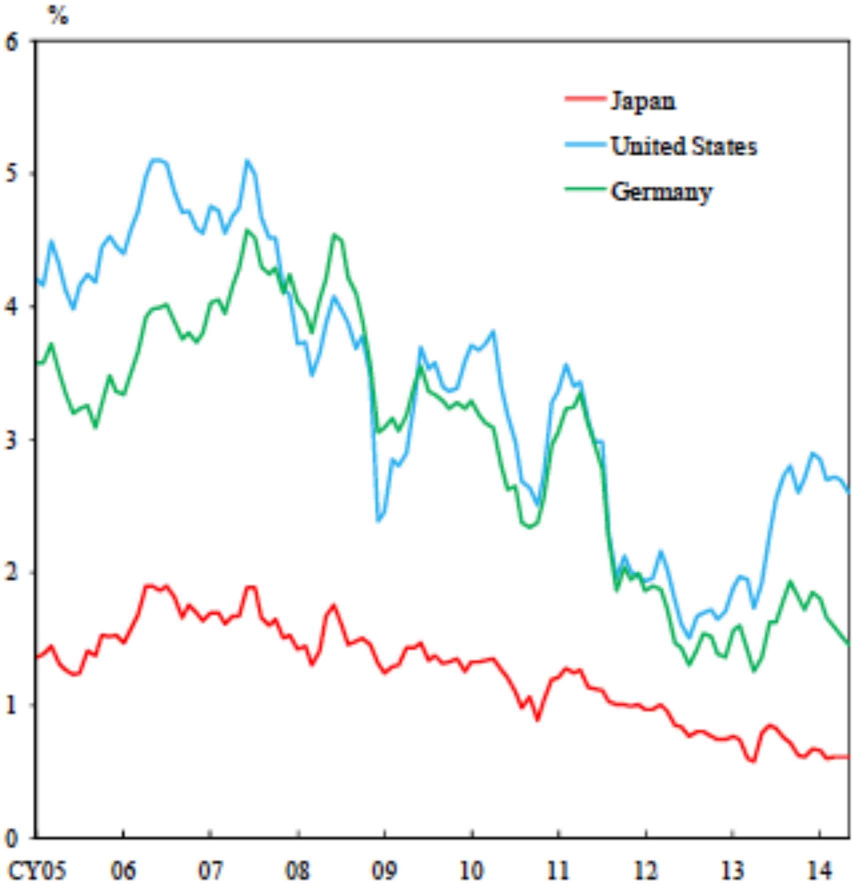
Source: Bank of Japan, QUICK Surveys, April 2014

Moreover, both 10-year and 30-year JGBs yields have been on a downward trend for some time and the monetary QQE put additional pressure on their yields (Table 3).

It is also a source of concern that after two years of QQE, any expectations of inflation induced by the BOJ have not led yet to higher nominal interest rates. In contrast, between 2012 and 2014, the long-term interest rates of the US and Germany began to raise slowly, which indicates that market participants expected an increase in the nominal interest rates in these two countries (Fig.2). Such expectations, even if they exist in Japan, have not been channelled yet to the long-term interest rates.

[10] BOJ, Kuroda H., "Welcome to the '2-percent' Club", Speech at the Meeting of Councillors of Japan Business Federation, 25th December 2014, Tokyo

Figure 2: Long-term interest rates: Japan, US and Germany



Source: Bloomberg

Under such conditions of long-term nominal interest rates fall and increasing inflation expectations, real interest rates decline precipitously. In fact, the real interest rate is negative and this has an impact on Japan's economy. It encourages the private sector to take risk and shift towards riskier assets in their portfolios. As such the asset prices have risen and the Japanese Index Nikkei 225 shows this clearly (Table 4). Japanese households have also increased the purchases of stocks. In contrast, the insurance and pension funds have reduced their purchases of riskier assets and transferred to the low-risk bonds[11]. Overall, these are early signs of a shift in investment behaviour of households and firms.

Higher asset prices are a major channel through which Abenomics may further boost the real economy. Higher stock prices lead to more consumption and investment. And the official statistical data show that the private consumption and public demand have been gradually and consistently rising, while the Japanese business investment has increased only very

[11] Bank of Japan, December 2014

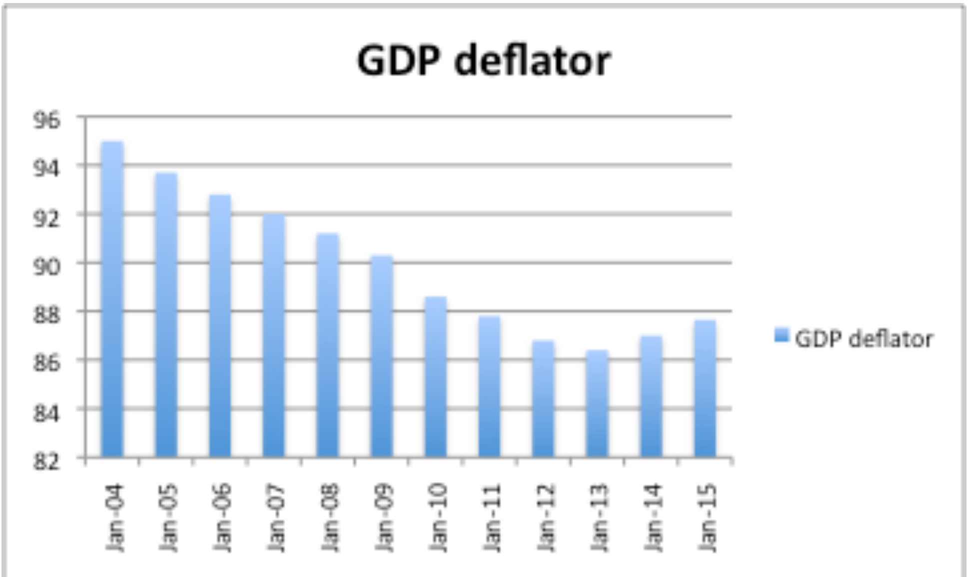
moderately[12]since 2013. Thus, households appear to have more positive views about the future of Japan, while corporate businesses are still cautious with their investment decisions.

2.2. Impact on Inflation

Actual inflation on a year-over-year basis turned to be positive, averaging around 1.25% in 2014 and around 0.33% in 2013. Monthly-based inflation as described in Table 2 showed a certain degree of volatility through 2014, partly accelerated by the introduction of a first-phase-sales tax-increase in April, which led to pre-tax increased consumption demand. This volatility was certainly expected as the previous National Diet voted the consumption tax rise into law.

However, to achieve a stable 2-percent increase on a year-on-year basis, prices will be expected to change moderately upwards, and there is still a long way to reach this moderation. Thus, there is a real concern among economists that the current inflation may not be stable as yet, with temporary effects, as the weaker yen and expensive import goods may have been solely driving it.

Figure 3: Japan's GDP deflator



Source of Data: International Monetary Fund

However, another measure of inflation – the GDP deflator that excludes all imports, Fig.3 demonstrates after years of steady decline, in 2013 for the first time the GDP deflator showed signs of positivity. In 2009, the deflator was 90.3, and in 2015 is expected to be 87.6 according to the IMF data. There are further grounds for assuming that in the long-run Abenomics will have positive effects on the price levels, also explained by persistent domestic factors such as a lack of spare capacity, a tight labour market (not only the weak yen) that play an important role.

[12] Japan's Statistical Office, December 2014

However, to have a consistent positive inflation in Japan, this will require increases in nominal wages. Many firms have agreed to small nominal wage increases, including Bank of Japan where the pay-rise will be about 1.3%[13].

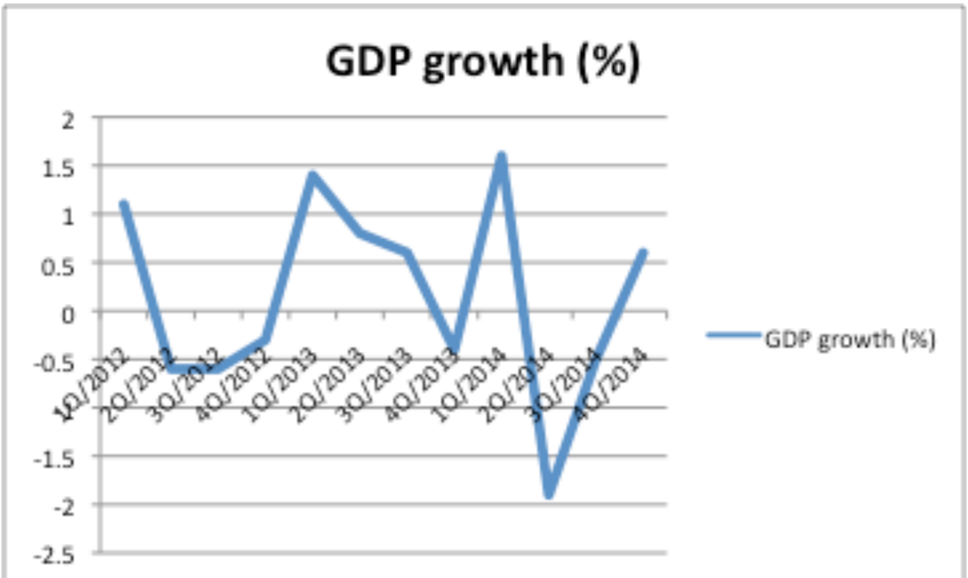
While any nominal wage increases are good news, since as inflation rises, real wages will decline. Nonetheless, the extent to which firms will be decisive to go ahead with any wage increases depends very much on their inflation expectations. As shown in Fig.1, and noted above, enterprises expect inflation to be about 1.6% in the next 5-year period. Both households and enterprises inflation expectations have risen since the QQE began and this change is very promising for achieving a stable 2%-inflation. One can argue that a potential constraint such as low profit margins of enterprises may halt this progress, and thus, it does not translate into continuous rising wages. Such a long-term situation would also suggest, that inflationary expectations may be wavering.

Overall, during the early period of Abenomics, the package has had *positive effects* on the inflation expectations, the actual inflation as well as the financial markets, and to a certain level on GDP growth.

2.3. Impact on GDP growth

The Fig.4 shows quarterly GDP growth at an annual rate since 2012. Japanese performance was notably better in 2013 than in late 2012, but in 2014 the economy went into a technical recession.

Figure 4: GDP growth rate (Quarterly, 2012-2014)



Source: Data provided in Table 5

[13] Bloomberg, "Wages rise in US, UK and Japan, to relief of the central bankers" by Rich Miller and Simon Kennedy, 15th December 2014

For since the first quarter of 2013, growth has declined due to the fall of net export contribution to the real GDP growth and an introduction of the sale tax in 2014. To a large extent the output growth in Japan was accounted for by consumption and government spending in 2013-2014, which explains the contraction after the sales tax rose in April 2014.

The Oct. 2014 IMF report, "Regional Economic Outlook Update: Asia and Pacific" estimates the real GDP at 0.9% in 2014 and 0.8% in 2015[14]. The considerable slow down, in comparison to the 2013-annual growth of 1.5%, is expected to continue in 2015, but be offset by rising private investment. Nevertheless, Hausman and Wieland (2014) notice that under Abenomics 2013 growth per working-age person was 3.1%, compared to 1.6% from 1995 to 2007, and 0.4% from 2008 to 2012. So taking into consideration only the working-age population, the growth under Abenomics looks impressive.

There is a significant debate among Western economists over whether Abenomics will have real effects on the current output gap – the difference between the actual output of an economy and its potential output/production capacity. If all problems of the Japanese economy are a result of changes to the potential output, then the only way forward is through the structural reforms (the third arrow). With this in mind, official estimates of Japan's output gap are small. IMF estimated it to be (-0.9%) in 2013[15], while the OECD estimated it to be positive (1.1%)[16]. In 2014, the IMF projected a real GDP growth of 0.9%, as they believed actual output was still above potential output[17]. IMF has lowered potential output of Japan significantly for the last decade. If this is correct, there is little role for monetary and fiscal expansion.

However, there are views that these official estimates of the Japanese output gap are far too low with alternative estimates ranging from 4.5 to 10%[18]. These mismatching numbers show certainly the difficulty with statistically measuring output gaps. The output gap measures also the degree of inflation pressure in the economy as a link between the real side of any economy and price levels. IMF and OECD use differing models with their strengths and weaknesses, but the underestimation of Japan's gap perhaps is due to a number of factors, one of which is the lower investment[19]. Certainly a smaller capital stock at a given point diminishes the level of output achievable in a future day - whether this can be overturn in a long run is a matter of future research. In the views of those that believe the output gap is larger than 4.5%, the role of monetary and fiscal expansions is essential to raise the actual output. Hence, the first two arrows of Abe's package should be implemented with credibility.

Despite all differences in opinions about the Japanese output gap, it is clear that a combination of all three measures (the three arrows) needs to be implemented to tackle a range of differing economic issues. Thus, the efforts of Bank of Japan and the government are certainly fruitful in terms of targeting the right policies and instruments. Of course, there are difficulties to be overcome that may prove to be stronger than the political will, but that remains to be seen.

[14] These are year-on-year percent changes (Table 1; Asia Real GDP, p. 3)
[15] IMF World Economic Outlook, October 2013
[16] OECD Economic Outlook of Japan, November 2013
[17] IMF World Economic Outlook, October 2014
[18] Estimations of American economists incl. Paul Krugman, Joshua Hausman, Johannes Wieland, and others. For instance, Krugman combines an estimate of Japan's natural rate of unemployment with an estimate of Okun's law coefficient in Japan. He suggested that the output gap in 2013 be roughly 9% (Krugman, 1998, "It's baaack: Japan's slump and the Return of the Liquidity trap", Brookings Papers on Economic Activity)
[19] Jacobson M., F. Occhino "Behind the slowdown of potential GDP", Federal Reserve Bank of Cleveland 2013

In October 2013, IMF estimated in its "World Economic Outlook: Transitions and Tensions" that the entire package of Abe's policies would add 1.3 percentage points to 2013 growth, while a study by Hausman and Wieland suggested a slightly lower contribution of 1%[20]. However it is less clear whether the monetary expansion or the fiscal stimulus has larger effects on the output.

3. The Second Arrow – Fiscal Policy

The Fiscal Policy component of Abenomics was formally announced in January 2013 with a ¥10.3 trillion stimulus package. This was done via the establishment of a supplementary budget and was initially conceived as a one-time programme equal to 2% of GDP[21]. However, further fiscal measures have proved necessary with in October 2013, the Government formulating an "Economic Policy Package" with ¥5 trillion to address any risks of economic downturn that could be caused by the tax rate hike in 2014 and to put the economy on a sustainable growth path.

Some of the measures included in the package are as follows[22]:

1. Tax reduction to promote investment – tax incentives for capital investment, R&D tax credits, tax incentives for business restructuring, and tax incentives to facilitate investment of venture capitals;
2. Trilateral partnership among the government, labour and employers;
3. Formulation of new economic measures to balance any negative impacts from the consumption tax hike.

In response to the tax hike, the government formulated a supplementary budget and implemented measures that included:

1. Lump-sum benefits for the affected – Provision of ¥10,000 to the 24 million of people who are exempt from municipal inhabitant's tax. An additional ¥5,000 will be paid to the people who receive old-age basic pension;
2. Lump-sum payouts for home buyers: Provision of ¥100,000 – 300,000 to home buyers with salary income of approximately ¥5 million or less;
3. A review of automobile taxation;
4. Acceleration of measures for reconstruction, disaster prevention and safety (restoration of areas damaged by disasters);

The fiscal packages are usually well described and targeted with specific measures reaching different groups of the population. However, the Economic Policy Package despite its well

[20] Hausman J.K., J. Wieland, "Abenomics: Preliminary Analysis and Outlook", Brookings Papers on Economic Activity, Brookings Institute, April 2014

[21] American economists estimate that the actual stimulus in 2013 was one percent of GDP much less than the announced number in the headlines -Hausman J.K., J. Wieland, "Abenomics: Preliminary Analysis and Outlook", Brookings Papers on Economic Activity, Brookings Institute, April 2014

[22] Ministry of Finance, Japanese Economy and Policy Measures, Oct. 2013, Tokyo

intentions, it did not prevent the economy from moving into recession in late 2014, which raises doubts about the effectiveness of any new stimulus package. The opposite effects from a consumption tax rise in 2014 by 3 percentage points and an undertaken expenditure increase of about 1% of GDP also add to these doubts.

However, the December 2014 ¥3.5 trillion stimulus package represents a further even more focused targeting of fiscal stimulus with support for the country's lagging regions, small businesses, students[23] and house buyers, through such measures as housing loan subsidies, tuition support and merchandise vouchers. In addition, the second sales tax increase originally scheduled until 2015 was postponed for April 2017[24]. Thus, repeatedly, during the last two years the government has increased their spending to boost the real economy. This trend continues for the fiscal year 2015-16 with a draft budget of ¥96.3 trillion ($813 billion), which is a slight real increase from the previous year's budget[25].

The fact that the monetary expansion and the fiscal stimulus packages have been run simultaneously makes it more difficult to conclude which policy has the larger effects. For instance, in 2012 the IMF forecasted that Japan's cyclically adjusted primary budget-deficit, as a share of potential GDP, would be 7.5%[26]. In 2013, the IMF concluded it would be 8.5%[27]. This implies a fiscal stimulus equal to 1.0% of GDP in 2013. Thus, it is very likely that through the multiplier effects this fiscal package added more than 1% to 2013 GDP. It boosted the public demand growth that exceeded expectations in 2013, but this trend did not continue permanently in 2014.

The monetary policy would also have effects on the consumption behaviour through the lower real interest rate that encourages households to spend today rather than tomorrow. In 2013, on a year-on-year basis, real consumption expenditures rose 0.9% and the value of new loans taken rose 9%. Additionally, the composition of the consumptions spending shifted towards durable purchases and private residential investments. These both components of consumption expenditures are most responsive to changes in the real interest rate. The real residential investment grew 10.4% in 2013, while the spending on durable goods rose 15.7%. This positive trend was interrupted in 2014 by the sale tax increase. Private consumption contracted in the second quarter of 2014 by 19% on an annualised basis, but it recovered slowly by the end of the year.

Summarising, there are reasons to be believed that the monetary expansion certainly contributed to the private consumption growth. Intertemporal substitution is observable. To what extent the monetary effects have been channelled through is difficult to conclude since the monetary and fiscal effects are entangled.[28] And they both play their role via the multiplier and the interest rate, respectively, at the same time. Arguably both arrows of Abenomics contributed to the GDP growth.

[23] Yahoo! "Shinzo Abe returns as Japanese prime minister after snap election" by Kyoko Hasegawa, 24th December 2014
[24] FT, "Japan affirms pledge to raise consumption tax in 2017", Robin Harding, 12th February 2015
[25] Reuters, Yamaguchi T. "Japan readies record $800 billion 2015-16 budget", 11th January 2015
[26] IMF, "Taking stock: A progress report on fiscal adjustment", Fiscal Monitor, Oct. 2012, Washington
[27] IMF, "Taxing Times", Fiscal Monitor, October 2013, Washington
[28] However, Hausman and Wieland (2014) concluded that the effects of Japan's new monetary policy, particularly in 2013, were modest to the output gap. They explained the lack of large effects with the behaviour of net exports.

4. The Third Arrow – Structural Reforms

The structural reform or the third arrow of Abenomics was officially announced with a detailed programme of deregulation in June 2014. The specific measures include the following:

1. Corporate tax reform – this calls for a general reform of the corporate tax system. The proposal is to reduce the tax rate on corporate profits from the current 35.6% to somewhere between 20 – 29%;
2. Boosting employment of young and old workers – the plan suggests more flexible work rules and allowing workers to be paid "based on outcomes rather than hours worked";
3. Female labour force – the government calls this measure "Womenomics", and plans to encourage the share of women in managerial positions, through flexible working hours, changes to the tax law designed to create greater incentives for women to work, and expanded day care for small children;
4. Agricultural reform – the proposal is to consolidate Japan's fragmented system of food production and distribution, which leads to unusually high food prices in the country. Rationalisation of the system will require reducing the political power of farmers in Japan;
5. Boosting private sector participation in public infrastructure projects;
6. Boosting Foreign Direct Investment through liberalising the rules;
7. Creation of Special Economic Zones – in these zones gambling will be legal and the tourism in the country encouraged;
8. Changing the portfolio allocation of the public pension fund – this implies a shift from low-risk government bonds to riskier assets;
9. Improving corporate governance – the plan aims to improve the management of public companies via induction of independent directors in the companies' boards. This will bring the Japanese rules in line with international standards of governance;
10. Energy – the idea is to end monopolies of public utility companies, introduce more competition and import LNG from the US, as well as restart the nuclear power industry;
11. The Trans-Pacific Partnership – most obstacles to trade within the Pacific region involve non-tariff barriers. In order to remove them, some Japanese domestic industries will have to be deregulated before an agreement for free trade can be reached. This agreement is important for boosting the economy further.

The proposed reforms suggest deregulation, liberalisation of economic activities, increasing competition, increasing the risk that private sector take, and privatisation. Many of these measures had been implemented along time ago in the western countries, particularly the UK and US. Some of these reforms by their nature might be deflationary in long-term, unless nominal wages are kept increasing. Moreover, today economists speak about "secular stagnation" in the advanced countries that may persist and keep the prices low for a longer period, which will require a lasting monetary expansion.

In theory the long-run structural reform will bring the necessary changes and success to Abenomics. Monetary and fiscal stimulation could have temporary effects if not supported by a more radical reform of deregulations. This arrow is critical for the successful implementation of Abenomics. Indeed in 2014, the IMF concluded that any delay in implementing the structural reforms could lead to slow growth and overreliance on monetary policy domestically that could hurt regional trade and global prospects.

However, from practical perspective, some of the suggested reforms would appear to be too ambitious, requiring a great deal of debate and understanding from the Japanese society. In the case of creating incentives for women to undertake more work and managerial positions, it means the existing system that dominates in Japanese firms would have to be reformed fundamentally and adapted to rewarding employees based on their results, not process or time spent. The emphasis will have to be more on short-term financial results – such drastic changes would mean that most of existing practices of how Japanese companies operate will have to be ceased[29]. Thus, observers conclude that there are major obstacles to achieving a "gender neutral social system" in Japan, under which women are promoted by corporations and encouraged to take up more responsibilities and executive opportunities as has become the norm in the United States and Europe.

Due to the demographic structure of the Japanese society, more flexible work hours and life-duration packages for younger and older people would be of great benefit to the employment system as well as foreigners contributing to the work force. However, the latter might be particularly challenging, as the anti-foreign sentiment in Japan is stronger today than it was in the past[30]. Thus, while the wage and immigration policy reforms in Japan are of utmost importance, they may lead to the type of general strikes, which paralysed the country during the 1970s[31].

By the same token, since the actual services and labour market deregulations have not begun yet, it is difficult to evaluate what would be their impact on long-term GDP-growth. Nonetheless, it must be stressed that there has been little real progress in any of the planned domestic reforms and there are serious concerns that the vested interest involved are such that this will remain the case.

5. Conclusion

Overall, Abe's policy package appears to be a well-thought out and intelligently structured programme. However, whether it will bring the necessary success to Japan's economy still remains to be seen. There are certainly some hopeful signs. In particular, markets do appear to believe in the effects of Abe's policies. Their response to monetary announcements, for instance, the asset-purchasing programme in 2013, has been impressive, as this paper's analysis of Abenomics' impacts has showed. Furthermore, the technical estimation by Hausman and Wieland (2014) is highly positive that if current long-term inflation expectations reached 2%, the real interest rate would decline further and increase the efficiency of the monetary expansion more than 50%. Whether this 2%-target is sufficient to boost the real economy to a

[29] Fukushima G. S., "The Future of Womenomics" Forbes Japan, December 2014
[30] See Fukushima G., 2014
[31] FT, "Japan wages: Manufacturing consent", Robin Harding and Kana Inagaki, 18th February 2015

stable recovery is a question for further research. In addition, there has been some significant revision upwards of the expected long-term growth levels. Consensus Economics forecasted the Japanese output in 2022 to be 3.1% above the pre-Abenomics output-forecast. They also raised the long-run growth forecast from 0.9% to 1.1%. A combine effect of all three arrows could add more than 3.1%-growth above no-Abenomics level.

However, this all rests on the assumption that the 2%-inflation target will be reached eventually and it must be stressed that this is still uncertain. Notably, because Abe's policies trying to overcome such a persistent deflation and major structural difficulties. For instance, Japan's demography and the structure of their pension system raise barriers to new solutions. Japan's large retired population had benefited from deflation and Japanese population holds over half its financial wealth in bank deposits and currency. Thus, the presence of a large constituency benefiting from deflation makes any inflation target more difficult to achieve.

A further problem is that the Japanese government heavily relies on the assumption that corporations will be persuaded to keep increasing wages every spring. To this end Mr Abe lobbies companies to raise wages, but there are already worrying signs among the squeezed Japanese working–age population that boosting salaries by asking firms will prove to be an unsustainable policy in a long-term[32]. This type of scepticism is combining with popular disbelief, opposition and resistance to halt the progress of the reform.

In addition, there are real concerns that Abe's policy package may be seriously undermined by external and internal shocks, such as low commodity prices, particularly the oil prices; trade liberalisation policies that eliminate barriers and put downward pressure on prices of consumption goods; uncoordinated actions of other central banks to counteract deflationary fears in Europe, Asia and America; and not least, populations' unwillingness to adapt to any structural and behavioural changes in Japan.

Even if long-term inflation expectations raise the slow progress of structural reforms, as described above, will necessitate much longer-term reliance on monetary and fiscal expansion than originally expected. Thus the QQE as an unconventional policy might turn out to be an ongoing necessity. This would undoubtedly damage the credibility of BoJ and other Japanese authorities' policies, which inevitably will discourage markets from believing in Abenomics. There is, of course, a possibility that the structural reforms will not merely be delayed but prove to be totally unachievable, in which case the whole long-term strategy would be at risk.

Thus, there are still serious concerns that Abe's policy package may disappoint the national and global community. It must be stressed, however, that the policies are at a very early stage and may well involve further extremely bold actions, as the stakes are high, both nationally and globally. Given disturbing signs of a gathering trend towards deflation in the international system, a revitalised Japan and the vindication of Abe's strategy could be of overwhelming importance, not least to policy makers in the West. In particular, would signal to the Euro-zone countries what is expected of their governments and the European Central Bank if they wish to avoid long periods of deflation.

[32] FT, "Japan wages: Manufacturing consent", Robin Harding and Kana Inagaki, 18th February 2015

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