

Effective Strategies for the Implementation of Reforms

“The Future of Structural Reforms in Germany and Japan”

September 8, 2015

Atsushi NAKAJIMA

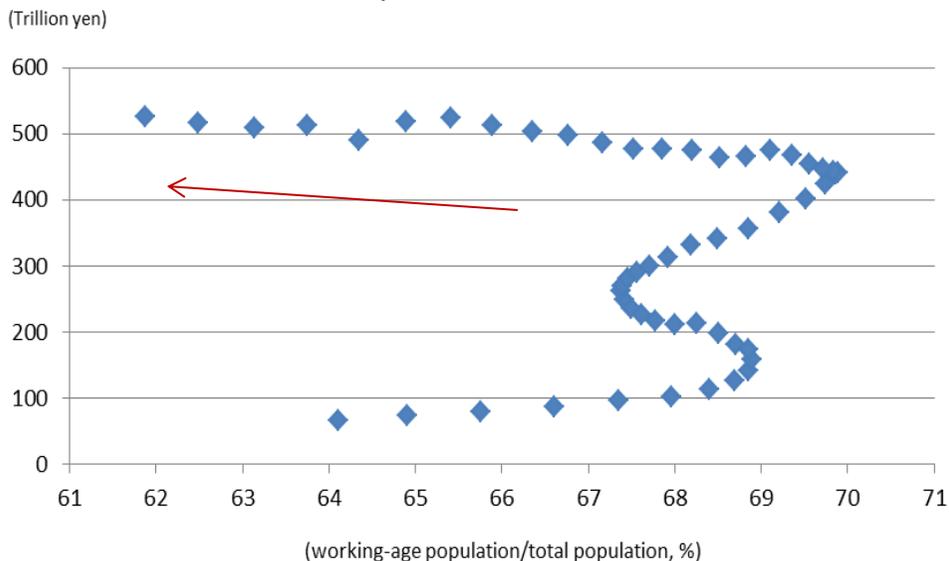
Research Institute of Economy, Trade and Industry (RIETI)

(1) Revitalization of the Japanese Economy

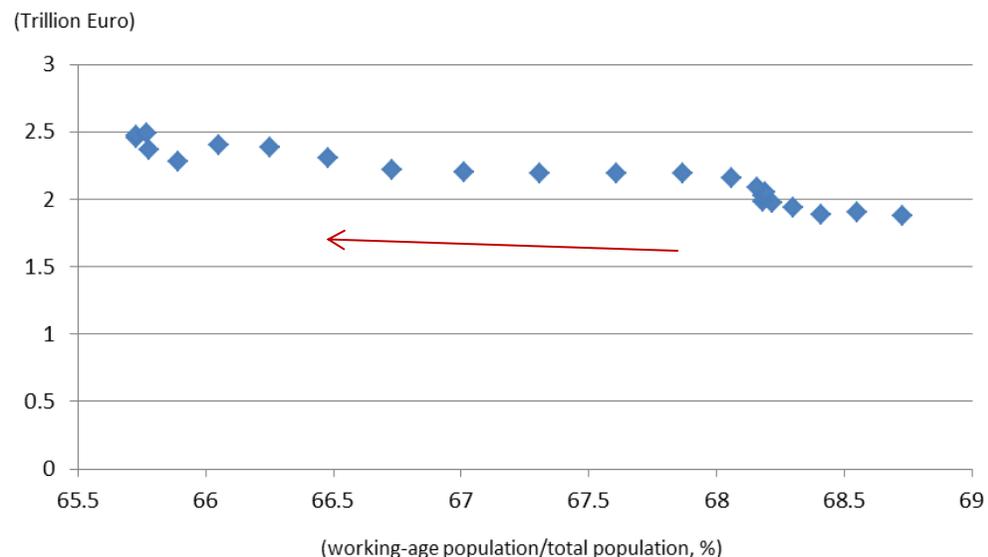
- Japan where the population is rapidly aging, productivity growth and the increase in the working population are critical.
- Japan has to rely on more women's and elderly people's activities and has to further relax labor market regulations (ex. Convergence of treatment between non-regular workers and regular ones) in order to maintain the working population. The use of immigrants is also a big choice for Japan to consider.

Relation between Working-age Population ratio and GDP

【Japan (1960-2013)】

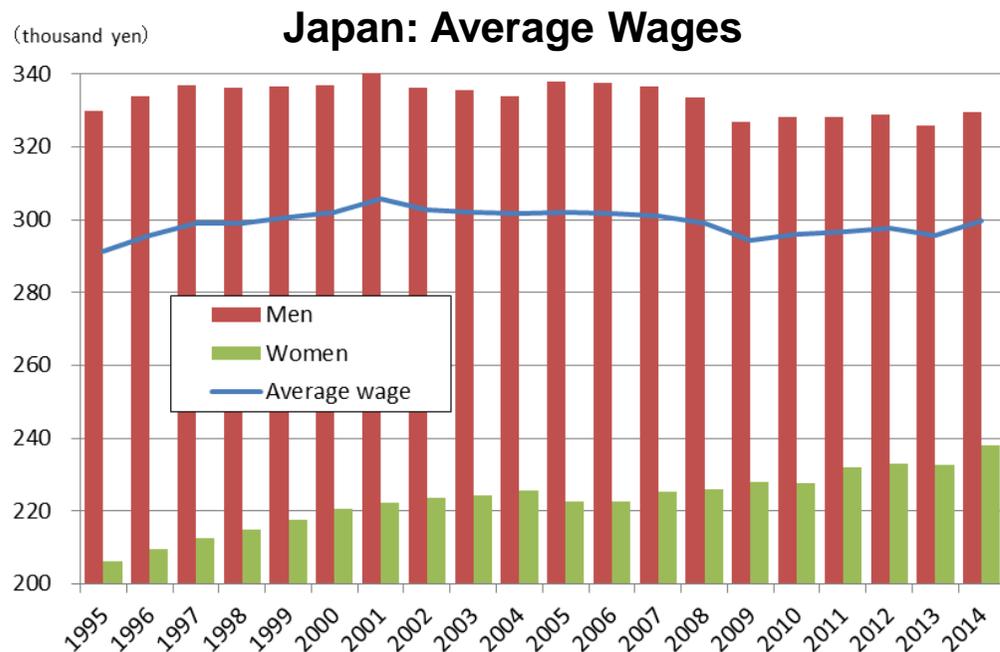


【Germany (1991-2013)】



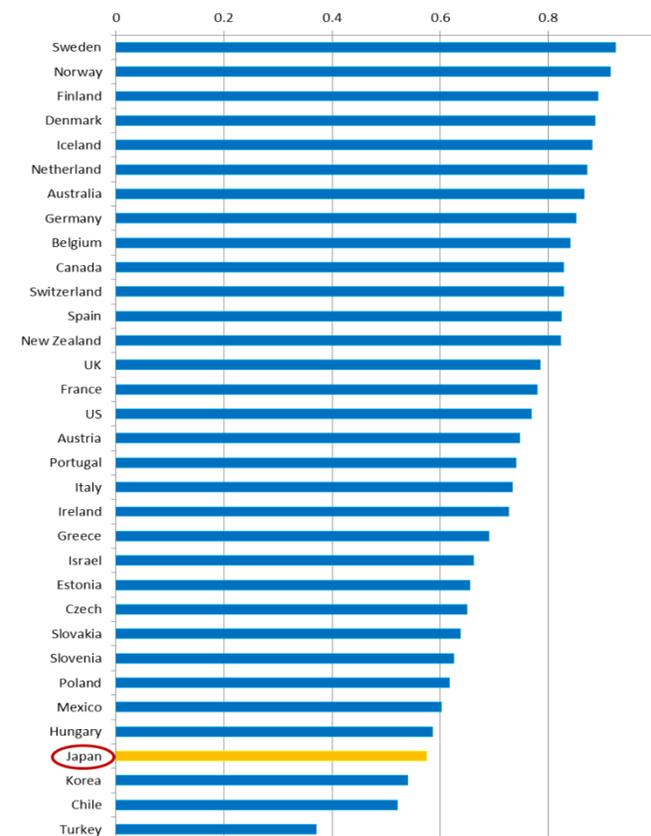
Note: OECD Economic Outlook, World Bank WDI

- Unused potential in Japan is quite significant, especially in the human resources area.
- Japan is one of the least advanced countries within the OECD in terms of using female labor and realizing a diversified society.



Source: Ministry of Health, labor and Welfare

OECD Countries: GEM ranking



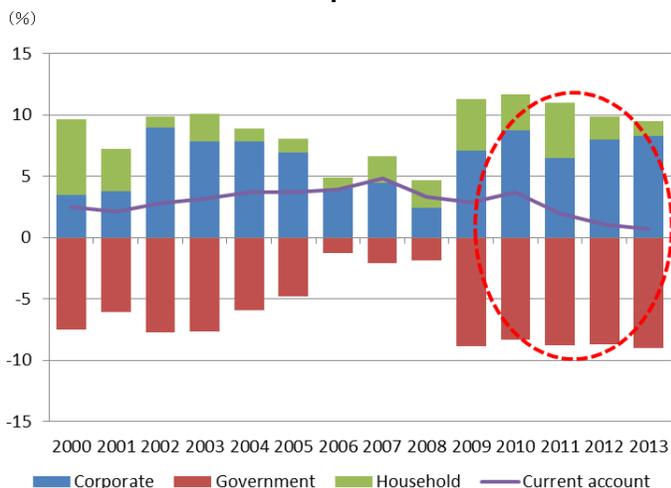
Note: 2006. Gender Empowerment Measure (GEM) is a measure of inequalities between the opportunities of men and women in a country. GEM is composed of 1) political participation and decision making, 2) economic participation and decision making, and 3) power over economic resources.

Source: OECD

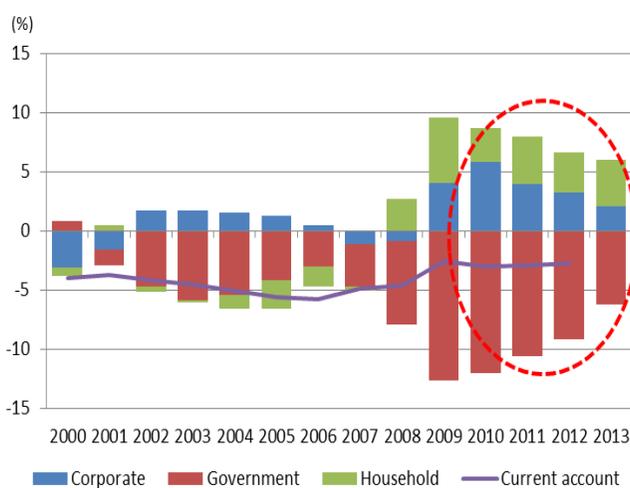
- In addition, one of the reasons for the Japanese economy's low growth and persistent deflation is the lack of vitality in its companies.
- The Japanese corporate sector has a relatively high investment-savings surplus, which provides companies with additional room to enhance investments and raise wages.

Japan-United States-Germany: Investment-Savings Balance

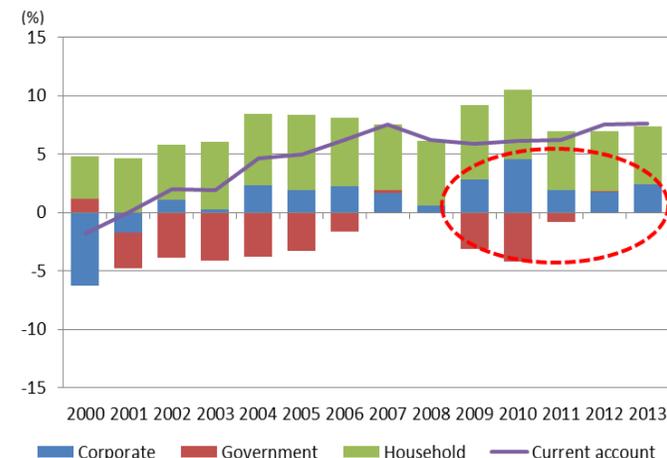
(Japan)



(United States)



(Germany)



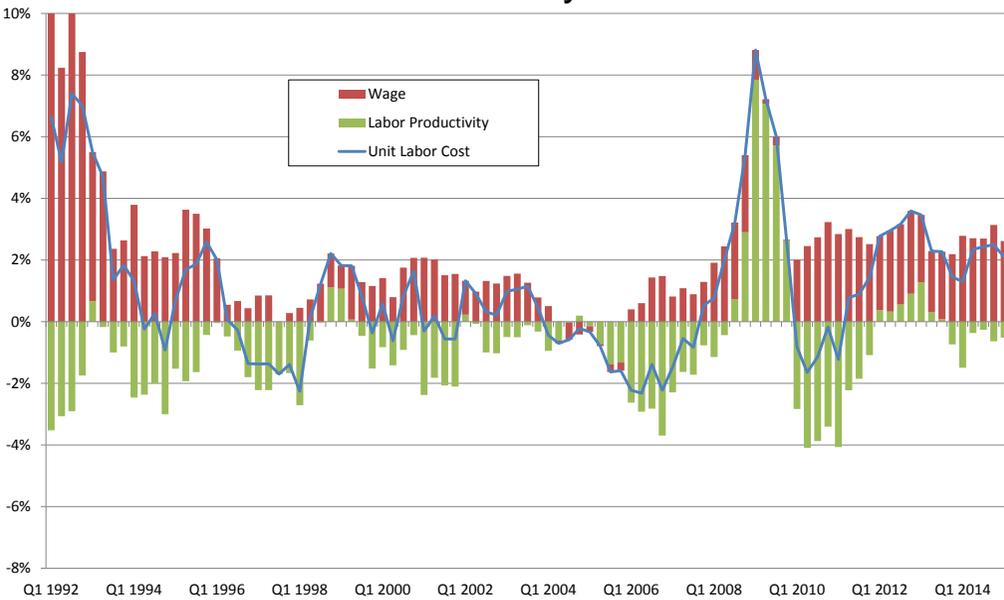
Note: Above 0 means an excess of savings, under 0 means an excess of investments. Both are on a GDP basis.

Source: European Commission AMECO, OECD StatExtracts

- It is clear that the steady productivity growth combined with the wage growth has not been realized in Japan as it is in Germany.
- The success of Abenomics depends on the Japanese economy moving from a vicious cycle to a virtuous cycle, and the revitalization of the corporate sector is the key.

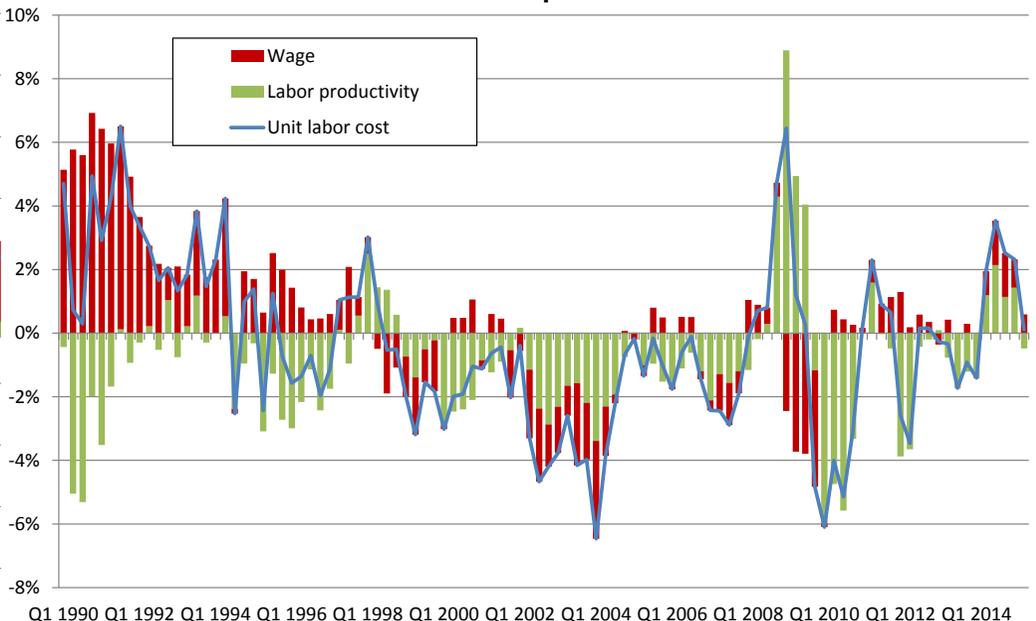
labor Productivity and Wage Growth

(Germany)



Note: Year-on-year basis. Unit labor cost = compensation of employees/real GDP
Source: Eurostat, Federal Statistical Office Germany

(Japan)



Note: Year-on-year basis. Unit labor cost = compensation of employees/real GDP
Source: Cabinet Office, Ministry of Internal Affairs

(2) Quantitative Effects of Various Policies

- Quality improvement of human resources by education, through deregulations of labor market etc. is the most efficient way to raise growth. But, the task is for the long term.
- In short term, the hike of labor participation rate, R&D enhancement and corporate vitalities stimulus through policies are efficient.

Quantitative Effects of Various Policies

	Contribution to GDP Growth (% per year)
5% hike of Women Labor Participation Rate (25-44years old)	+0.08%
5% hike of Senior Labor Participation Rate (over 60 years old)	+0.16%
Doubling the growth of Foreign Labor Forces	+0.02%
10% point cut of Corporate Tax rate	+0.1%~0.2%
1% point increase of R&D/GDP	+0.3%~0.4%
Literary Ability to the Top Level of the World	+0.6%
TFP Growth of Agriculture Industry similar to the U.S.	+0.04%
Inward FDI (Doubling of Foreign Companies Capital Stock)	+0.01%~0.02%
TPP	+0.07%~0.16%
Doubling the Rate of Corporate entry/exit	+0.4%
Increase of Social Security Charges	-0.1%
Negative Integrated effects of Population Decline	-0.1%
Zero Nuclear Power Plant	-0.1%

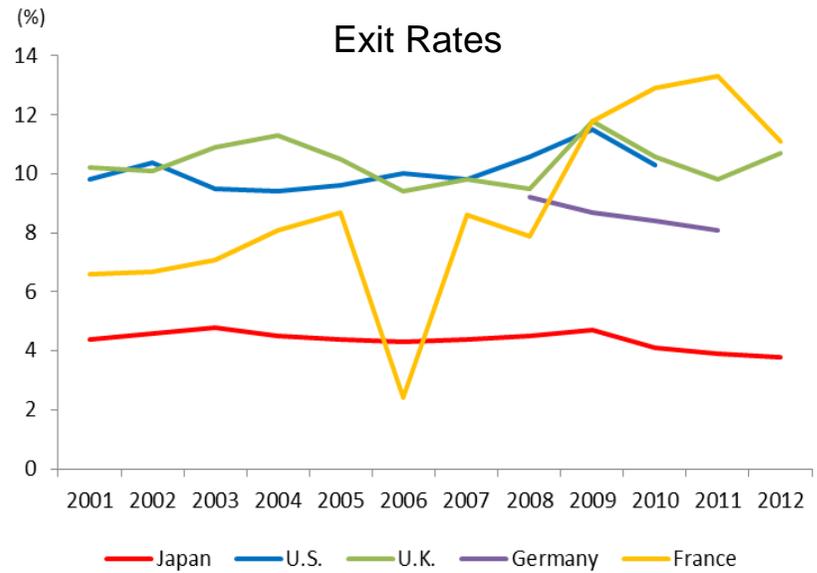
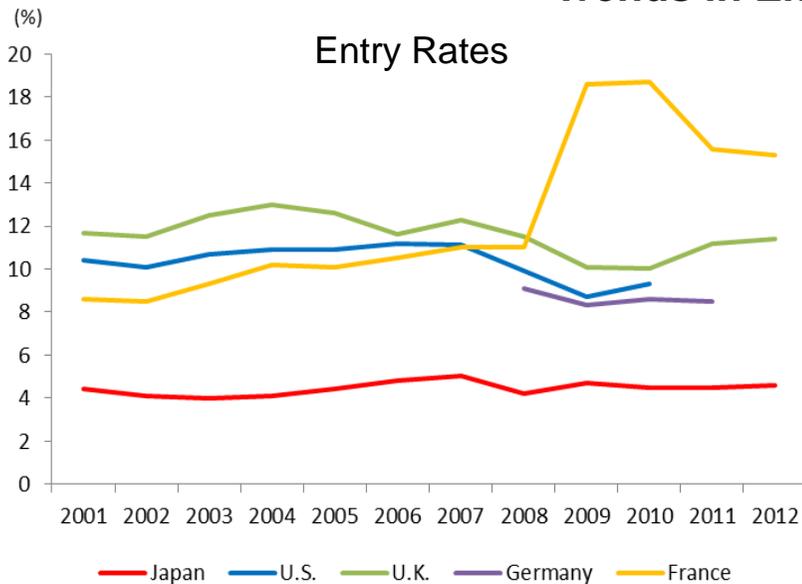
Source: RIETI PDP15-P-001

(3) Some Short-term Effective Policies

- Enhancement of market competition

- Entry rates (start-up ratio) and exit rates (going out of business ratio) of companies are low in Japan. Start-up companies' productivity and employment growth rates are basically higher than that of exiting companies.
- The effect of reshuffling is higher especially in wholesale/retail sectors and other services (business/professional services, personal services, etc.) where the presence of large companies lowers the profit ratio.

Trends in Entry and Exit Rates

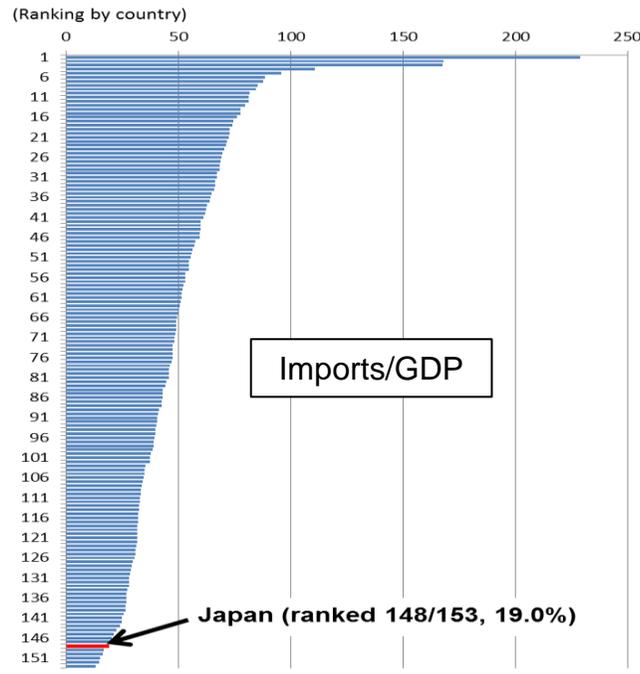
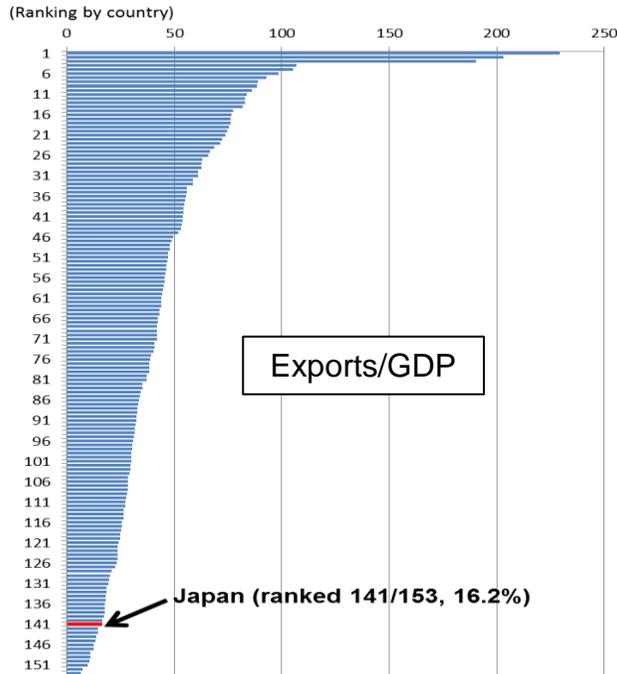


Source: Small and Medium Enterprise Agency "the 2014 White Paper on Small and Medium Enterprises in Japan"

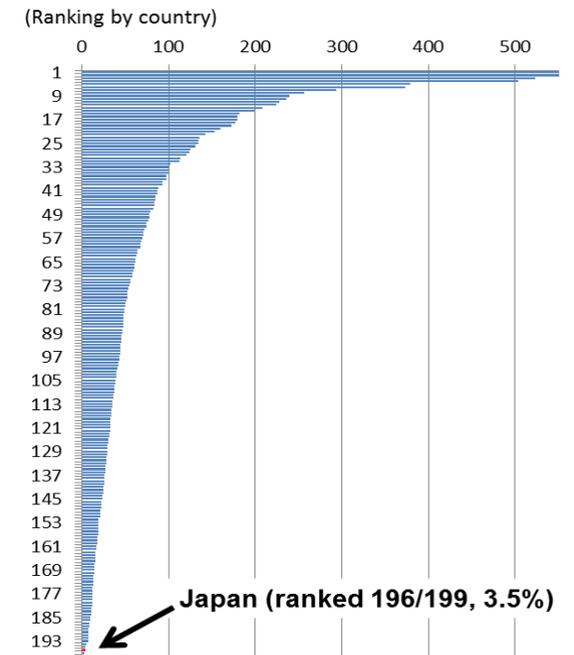
- TPP

- Japan has room for its growth rate to rise through growing external demand. Globalization promotes innovation, and productivity soars by building a global human/supply chain network.
- Japan's exports/import and inward FDI to GDP are one of the smallest in the world. With the stabilization of the currency's fluctuation, the TPP and other FTAs enable Japan to drastically enhance globalization not only by exports growth but also by acceleration of inward FDI.

Exports/Imports to GDP



Inward FDI Outstanding Amount/GDP



Note: Exports/imports are for goods and services. Nominal GDP, 2013 basis.
Source: World Bank

Note: Inward FDI outstanding amount is the total outstanding amount of inward FDI for 1980-2013. Nauru and British Virgin Islands are excluded.
Source: UNCTAD

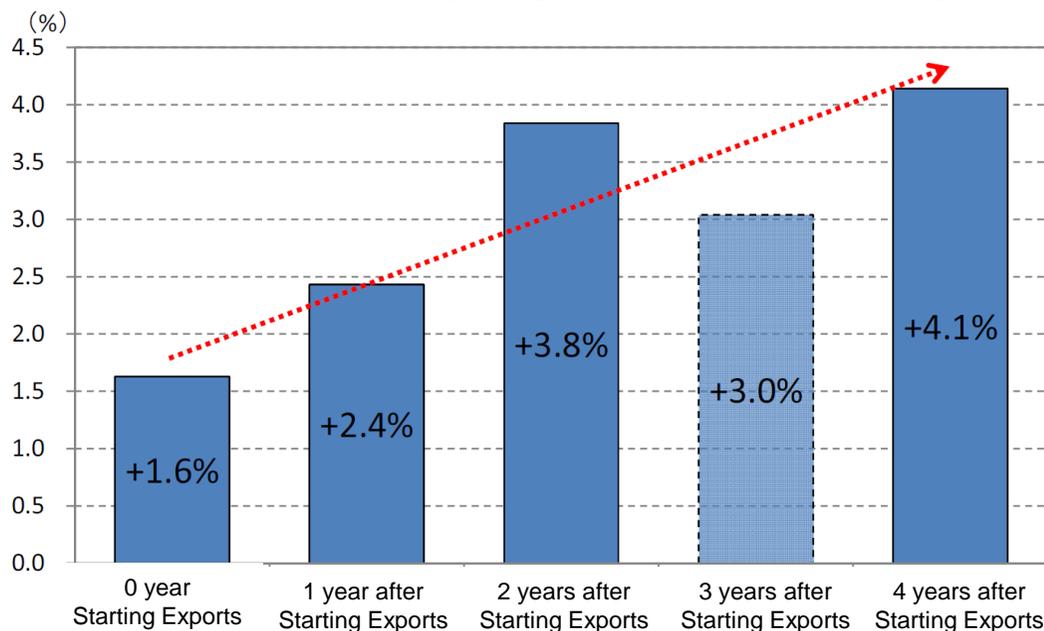
- Further globalization of small and medium-sized enterprises (SMEs) is necessary. Japanese SMEs' exports and FDI are much less than that of their European counterparts.
- The productivity growth rate is higher for companies which have started exports to North America and Europe by learning the effects in highly advanced markets. As the benefits of exports are growing due to the weaker yen, now is a good opportunity for SMEs to globalize further.

Japanese/European SMEs: Ratio of Exporting/Outward FDI Companies

	Japan	Germany	France	Italy	Spain
Share of Exporting companies	2.8%	19.2%	19.0%	27.3%	23.8%
Share of companies with outward FDI	0.3%	17.2%	15.1%	7.0%	12.3%

Source: METI "White Paper on International Economy and Trade 2013"

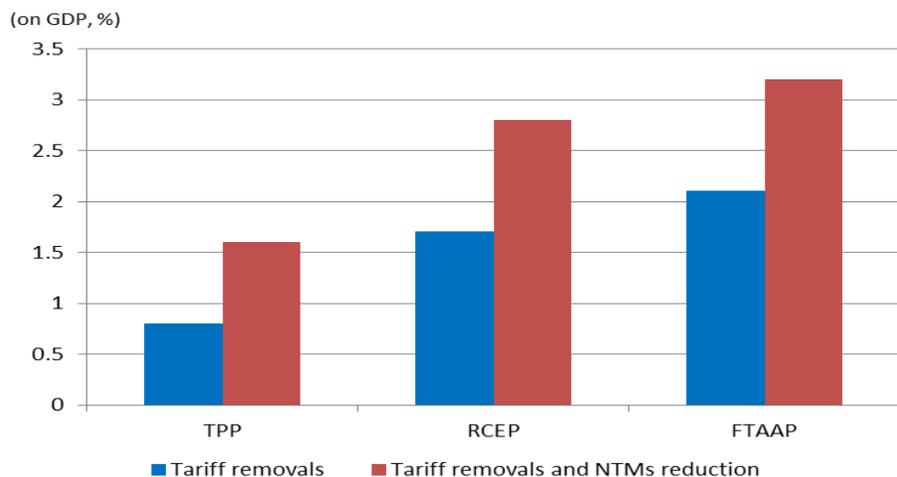
Effects of Starting Exports on Productivity



Note: The value in the 3rd year after starting exports is not statistically significant.
Source: Made by METI according to RIETI DP11-J-066 (June 2011).

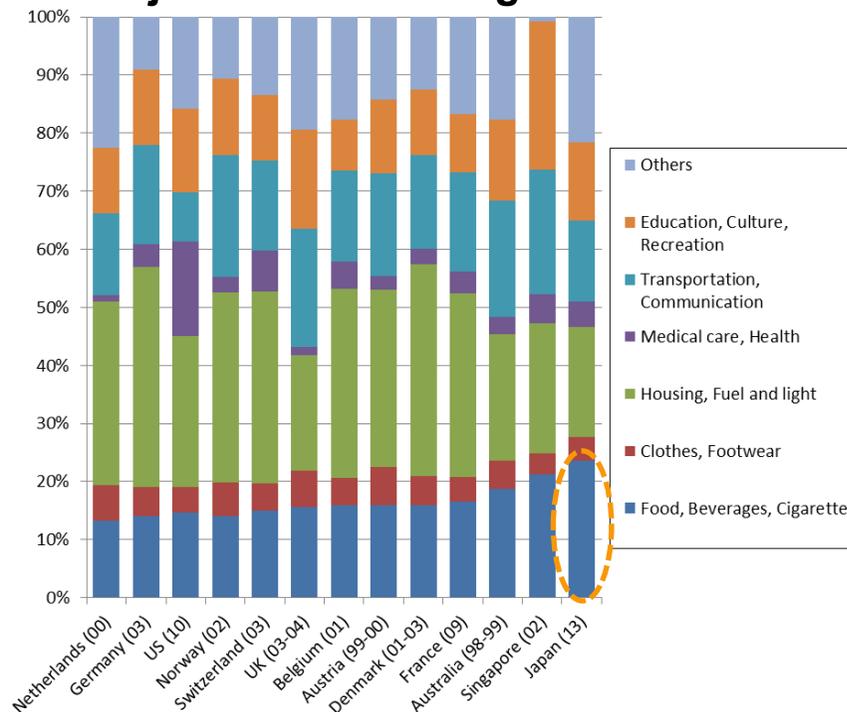
- The TPP will serve to globalize the Japanese economy as well as Japanese companies.
- The TPP's economic effects are larger with tariff removals and non tariff measures reduction than with only tariff removals. Multilateral FTAs are needed increasingly to support companies' supply chains which are becoming more and more globalized.
- Japanese households are the biggest beneficiary of the TPP, ahead of export companies, and a 5%-10% cut in food expenses is possible.

Income Increases Effect of the TPP



Source: "The Relative Significance of EPAs in Asia-Pacific,"
Kenichi Kawasaki (Consulting Fellow) (RIETI DP: 14-E-009)

Major Countries: Engel's Coefficient



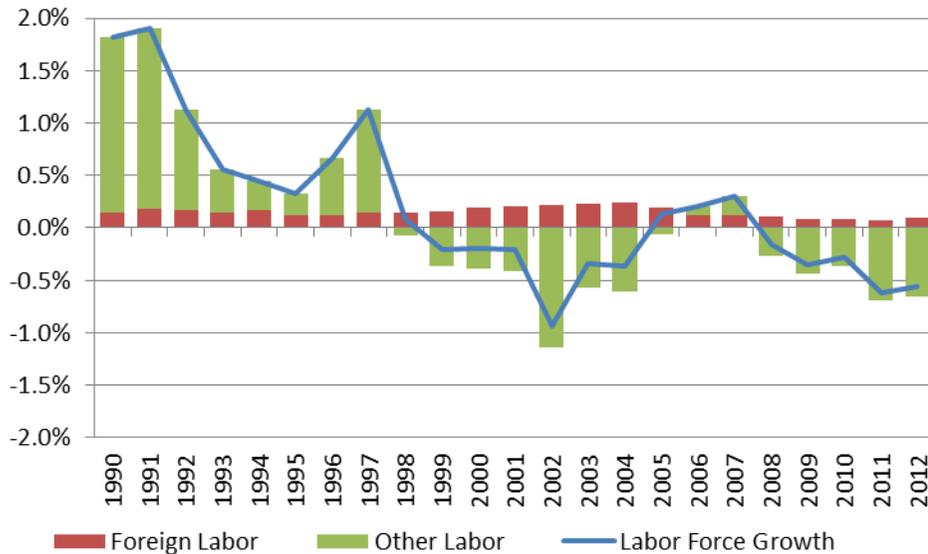
Source: Ministry of Internal Affairs "Statistics of the World",
U.S. Department of Commerce, France INSEE

- Further relaxation of Foreign immigrants related regulations

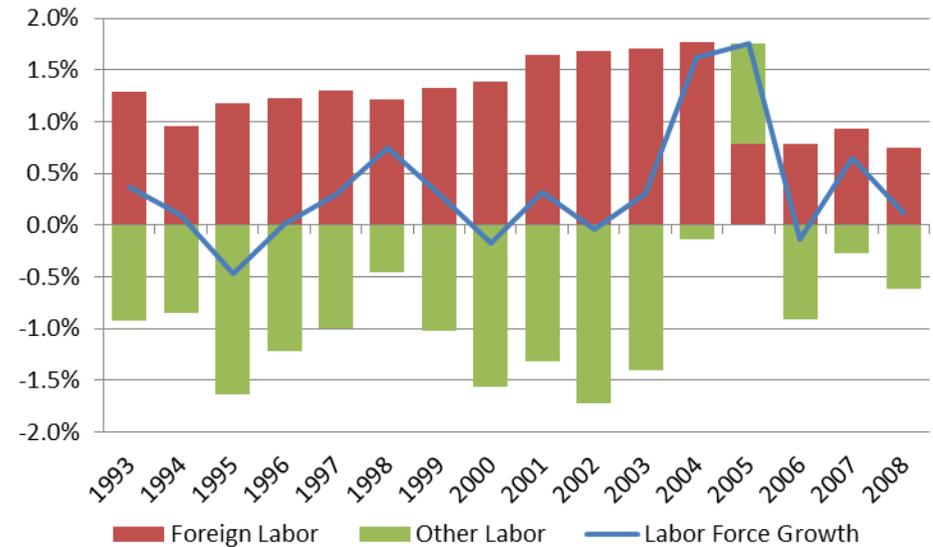
- Also, Japan has a huge room to further introduce foreign labor. For the time being, foreign labor is marginal in Japan and there is a big difference from Germany where foreign labor compensates the decrease of German labor force.

Composition of Labor Force Growth

Japan



Germany



Note: Y-o-y basis.
Source: OECD

