

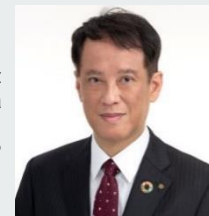
Kishidanomics = Abenomics with beefed up “third arrow”

Must monitor feasibility of stimulating self-sustaining private economy recovery

- Kishidanomics after downgrading coronavirus to “Class 5” is Abenomics with beefed up “third arrow”; stressing growth strategies with long-term view to stimulate private investment even more than Abenomics
- Right prescription for overcoming economic stagnation; major financial market transformation if realized

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Kishidanomics = Abenomics with beefed up “third arrow”

The Cabinet recently approved the 2023 Basic Policy on Economic and Fiscal Management and Reform (referred to as “2023 Basic Policy” hereafter), known as “honebuto no hoshin” (big-boned policy outline). Since downgrading the status of the coronavirus to a “Class 5” common infectious disease (same category for seasonal flu), the characteristics of Prime Minister Fumio Kishida’s economic and fiscal policy (during normal times) have become more clearly defined. From the outside, Kishida’s economic and fiscal policy seems to be Abenomics, but with an enhanced “third arrow” (structural reforms). Specifically, there is a greater emphasis on long-term growth strategies that stimulate private investment even more than Abenomics. This is the right prescription for breaking Japan free from economic stagnation. If realized, we would expect a major transformation of Japan’s financial markets.

The “first arrow” of Abenomics is bold monetary policy. On this front, Kishida selected Kazuo Ueda to replace former BOJ Governor Haruhiko Kuroda. At this juncture, Ueda seems willing to continue monetary easing to a greater extent than the JGB market had expected.

The “third arrow” of Abenomics is growth strategies to stimulate private investment. Former Prime Minister Shinzo Abe first aroused private sector expectations with the word “Abenomics,” a catchphrase that sounds like big changes are coming. Indeed, corporate earnings and employment increased under this new approach. Nevertheless, this was not enough to pull the Japanese economy out of its 20-year period of stagnation. Of course, the impact of the novel coronavirus, which has been raging since 2020, played a role. However, many have pointed out that Abe was better at diplomacy than at domestic politics, and that his “third arrow” (growth strategies) lacked any real punch.

Kishida has presented his “new form of capitalism.” When he first took office, Kishida placed a particular emphasis on “distribution,” which may have reminded some of socialist capitalism with an emphasis on welfare. However, the 2023 Basic Policy clearly states that the government will, “develop policies to promote investment in people and domestic investment.” Using a rich array of measures, we see an attempt to encourage self-sustaining private sector investment in people and equipment.

The “second arrow” of Abenomics is flexible fiscal policy. Abe launched a major economic stimulus package after his second administration took office. Even after leaving office, he was a proponent of aggressive fiscal policy amid the coronavirus outbreak. However, contrary to that, Abe also brought about two consumption tax hikes. There were aspects to his approach that could not be described as either aggressive or disciplined fiscal policy.

During the coronavirus outbreak, Kishida continued to launch major economic measures, partly due to strong requests from those in the ruling party. However, the 2023 Basic Policy suggests a move away from large fiscal stimulus packages, stating that the government will “work to return the expenditure structure to normal and ensure that emergency spending is not prolonged or made permanent more than necessary.” On the other hand, the 2023 Basic Policy also states that the government will “conduct targeted public spending as a catalyst to increase private investment.” The intention to use public funds to spur on self-sustaining investment activities by the private sector is apparent.

20 years of prolonged economic stagnation: Causes & solutions

The Japanese economy has stagnated for more than 20 years since the bursting of the bubble economy. This 20-year period included excessive corporate debt, bad loan problems at banks, excessive depreciation of the yen, the rise of newly industrialized countries, the Asian economic crisis, and the global financial crisis triggered by the collapse of Lehman Brothers, among others. As someone who has lived through this period, the author notes that corporate management shifted to more conservative approaches after each of the numerous crises that hampered their operations. The corporate emphasis on strengthening financial bases by limiting investment in human resources, reducing capital expenditures, and accumulating profits and cash flow is seen as one cause behind this prolonged economic stagnation.

From the viewpoint of overcoming this stagnation, reducing the consumption tax to 0% for a limited period of time or creating a supplementary budget big enough to fill in the supply-demand gap would have little effect. Of course, such measures should be effective in terms of providing short-term support to citizens and businesses impacted by crises. However, this will not arouse the corporate "fighting spirit," specifically the spirit to uncover the seeds for creating long-term businesses and take risks on their own.

As a municipal bond analyst, the author keeps a close eye on local economies and has been surprised by the recent brisk economic activity in Kumamoto Prefecture. Since Taiwanese semiconductor giant TSMC constructed a plant in Kumamoto, there has been no shortage of articles about Japanese semiconductor-related companies moving into Kumamoto and neighboring prefectures. The establishment of TSMC as the nucleus is believed to have produced the buds for creating long-term businesses, while stimulating investment.

We note that TSMC did not decide to enter Kumamoto solely on its own. Although the efforts to attract companies to that prefecture began before the Kishida administration took office, they are the result of efforts by METI.

Kishida administration aims to stimulate private sector's "fighting spirit"

Kishida's recent fiscal policies have drawn attention and criticism for raising taxes and insurance premiums. Still, he is not exactly pursuing "austerity measures." Austerity means increasing taxes while spending remains at the same level or is reduced. Kishida is trying to partly finance increased spending on defense and childcare through taxes and insurance premiums, rather than issuing more JGBs. To be precise, this is "balancing the budget" (as opposed to austerity).

Moreover, when spending is increased for economic and other measures, the customary practice is to respond with a supplementary budget. With a supplementary budget, the size of the budget can be restored later, so the size of expenditures will not constantly expand. However, Kishida's initial budget includes plans to increase spending on defense and child care by trillions of yen. Although the government is trying to avoid issuing more JGBs, the scale of these expenditures alone suggests an unprecedented big-government orientation.

However, this is not the only area that the JGB market should closely watch over the long term. It is also important to note that the government is pump priming (spending in an attempt to stimulate private sector spending) in order to break the economy free from its prolonged stagnation. Indeed, the 2023 Basic Policy states from a medium/long-term perspective of five to ten years that the government will conduct policy management to promote medium/long-term planned investments that ensure the predictability of the private sector, draw out private demand, solve social issues, and ensure wise-spending to guarantee returns on such investments. Furthermore, various concrete approaches for achieving that objective have been determined one after another. These include "expand domestic semiconductor industry sales in 2030 to 15 trillion yen, about three times the current level," "expand the supply of hydrogen to 12 million tons in 2040, six times the current level," "invest 15 trillion yen in the public and private sectors over the next 15 years to achieve this goal," and "increase annual investment in startups to 10 trillion yen by FY27, more than ten times the current level."

If the Japanese economy were to fully emerge from two decades of prolonged deflation, the economy and financial markets would be completely transformed. Such changes are not

imminent. Still, taking a somewhat longer view, we want to focus on the effects of the Kishida administration's growth strategies and how they spread throughout Japan's economy overall.

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