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## Abe's Real Challenge is the Japanese Economy

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**Hiroaki Kuwajima, Chief Financial Officer at Aoyama Shachu Corporation, explains that “The key issue is whether Prime Minister Abe understands the importance of economic recovery as the source of his legitimacy, ahead of his own goals which include constitutional reform.”**

Japan's Liberal Democratic Party (LDP) and its coalition partner, the New Komeito, achieved a landslide victory in late-July elections that finally enabled both parties to control the majority of seats in both the House of Representatives (the Lower House) and the House of Councilors (the Upper House). This election result has serious implications for Japanese politics in that Prime Minister Shinzo Abe and his LDP-led administration now have the means to accelerate their legislative agenda without facing *Nejire*—Japanese political gridlock. Abe successfully persuaded Japanese voters to support his coalition with New Komeito and his policy of “Abenomics” to revive the Japanese economy. He did this by reminding them of the debilitating paralysis within Japanese politics over recent years and the negative impact of this for Japan as a leading global power. Facing multiple domestic problems including a stagnating economy, mushrooming government deficit, a deteriorating social security system, and regional security threats, the Japanese public granted the LDP and New Komeito a mandate to govern.

The July LDP/New Komeito victory was well planned. Since their victory in the Lower House elections in December 2012, the plan was always to win control of the Upper House in order to be able to fully implement their policies without opposition intervention. The coalition government focused their attention on revitalizing the economy by the so-called “three-arrows” policy: a combination of active monetary easing, an aggressive fiscal stimulus package and structural economic reforms. By carefully avoiding or postponing politically controversial issues such as deficit cutting, aggressive deregulation, or revisions to the constitution, Abe was extremely successful in controlling his party and winning the support of the Japanese public. Though opposition parties tried to attack Abe by framing him as a timid reformist or a historical revisionist, economic successes—which included a depreciating yen which is now boosting exports and led to a surge in the stock market—resonated more with Japanese voters. The prime minister also managed to successfully advocate popular public policies not traditionally associated with his party such as child care and female workforce participation. Now that Abe has received a three-year mandate to govern, the question is what will he do? Will he focus upon economic recovery or turn his attention to constitutional reform as in changing Article 9 of the constitution, officially allowing Japan the right to exercise collective self-defense?

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### **Economic Success is Critical for Long-Term Governance**

In thinking through the short-term future of Abe's policies, there are a number of



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important factors to take into consideration. Even with this landslide victory, the LDP and other like-minded parties in favor of revisions to the constitution have not secured the necessary two-thirds majority required in both houses, a prerequisite to move the bill forward before putting it to a national referendum. Secondly, New Komeito, the coalition partner, is stubbornly against constitutional revision pertaining to a reinterpretation of Article 9. These two facts essentially mean Abe is constrained, and he needs first to persuade New Komeito of the merits of his plans. Furthermore, he has to maintain the momentum of the economic recovery, which also includes addressing the difficult issue of fiscal restructuring involving two proposals for consecutive tax increases.

In order to overcome any possible negative economic side-effects of the tax increases, Abe will have to accelerate the implementation of his so-called “third arrow” which comprise of economic structural reforms to protected industries including healthcare, agriculture and services. But once again on this front he will face challenges from those within his own party, especially recently elected members with close ties to specific interest groups. At this stage, it is not clear if Abe will be able to gather the necessary support from stakeholders within his own party to implement these economic reforms. Even with these substantial hurdles in front of him, there is a strong incentive for Abe to focus on economic issues first, since this economic recovery is in the long-run what will empower him to pursue his own agenda including constitutional reform.

### **How Long Will Abe’s Pragmatism Continue?**

Abe understands the reality that without a strong economy he cannot proceed with his own broader agenda. Thus, in this term, while he will focus on the economy, he will also deliberately move to foster a consensus with relevant stakeholders—some of whom are within his own party, along with New Komeito party members and the Japanese public—in preparation for the “next” election to move forward with constitutional reform. Furthermore, as long as the economy is growing, Abe will have more leeway on foreign policy issues. However, at this moment in time, it is the economy that matters.

In the short-term, the biggest risk for Abe is an economic downturn. In the event of the economy slowing down, it is unclear whether he will have the required political capital to continue his reform-centered policies or go back to the LDP’s traditional pork-barrel politics. There is still a degree of uncertainty as to how Abe will choose to hold onto his political legitimacy if he encounters a political and/or economic headwind.

The mid-to-long term concern is yet another delay in addressing other fundamental problems such as social security reform and the issue of an aging and declining population. These difficult issues can only be addressed when the ruling party has the required majority in both houses to pass the required legislation, which Abe currently has. This window of opportunity in Japanese politics is a rare phenomenon and cannot be wasted. As Chief Cabinet Secretary Yoshihide Suga said in an interview, “If Japan as a country misses this opportunity for fundamental reforms, the country will be over.” The question is whether Abe shares that viewpoint.

### **Last Opportunity to Revive Japan?**

The full recovery of Japan’s economy depends upon economic structural reforms, some of which are going to be painful for relevant stakeholders. However, this may be the last chance to fully implement these necessary reforms before it is too late. The key issue is whether Prime Minister Abe understands the importance of economic recovery as the source of his legitimacy, ahead of his own goals which include constitutional reform. The challenges have just started.

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