

Japan's Dilemma:

Why has Japan's economy been struggling with the stagnation since 1990's?

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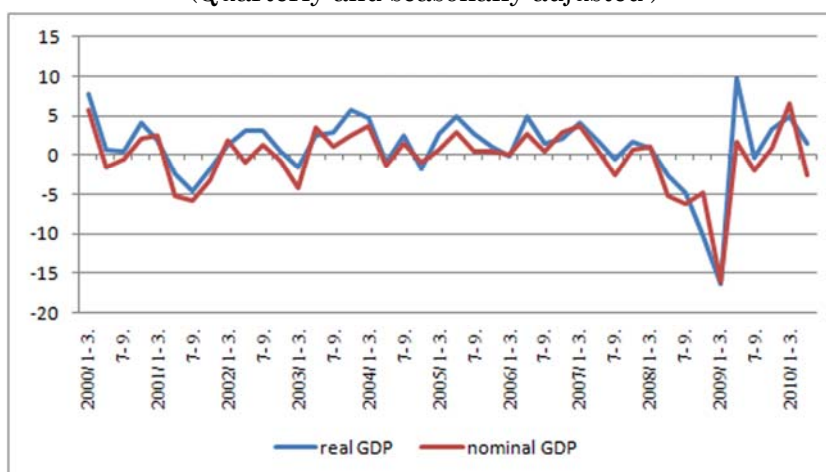
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Introduction: Current Situation of Japan's Economy and Politics

Due to the Lieman Shock which happened in September, 2008, Japan's GDP growth rate showed a big fall and dropped to the negative level. Although it has gradually recovered after the shock, the recovery is the sum of only a part of the big fall and a slight increase of the real GDP caused by the deflation. Thus nobody is able to have the feelings of its actual economic recovery.

This tendency of the economic stagnation in Japan was not caused by the Lieman shock. After the asset bubble which burst in the beginning of 1990's, Japan's economy has been struggling to escape from the stagnation. As shown in Fig. 1, Japan's economy after 2000 is characterized by the low nominal GDP growth rates and the deflation.

Fig. 1 Nominal and Real GDP growth rate after 2000
(Quarterly and seasonally adjusted)



Sources: http://www.esri.cao.go.jp/jp/sna/qe102-2/gdemenu_ja.html

The Political situation in Japan is similar to the economic situations. The DPJ (The Democratic Party of Japan) won the election of the House of Representatives in 2009 under the influence of the Lieman shock and Dr. Hatoyama, the leader of the DPJ,

became the first prime minister from the DPJ. However, the DPJ could not carry out the effective policies and Hatoyama gradually lost the approval of the public. Accordingly, he had given up his post, and Mr. Kan, the then vice prime minister, took up the post. However, Mr. Kan lost the election of the House of Councilors in 2010. Now, though the DPJ hold the majority in the House of Representatives, the nongovernment parties hold the majority in the House of Councilors. This situation is called “the twisted Diet” in Japan. Thus important bills cannot be passed as long as the other parties do not agree with those bills. However, the DPJ’s Administration is not the first to occur such political confusion. In the era of the LDP (Liberal Democratic Party)’s administrations, after Koizumi’s retirement in September 2006, prime ministers resigned one after another (Mr. Abe, Mr. Fukuda and Mr. Aso), and there also existed another “twisted Diet”.

Thus, currently, Japan’s economy is in stagnation and the politics is in confusion. In the latter part of 1980’s, Japan was thought to have the strongest economic system in the world and the secrets of the efficiency of the economic system of Japan were studied by many researchers. The industrial policies by the government in Japan, “Gyosei-Shido,” was considered as one of the ideal industrial policies by any government. But, why is Japan struggling now? In this article, I will consider how Japan fell into this situation and how Japan can get over the difficult situation.

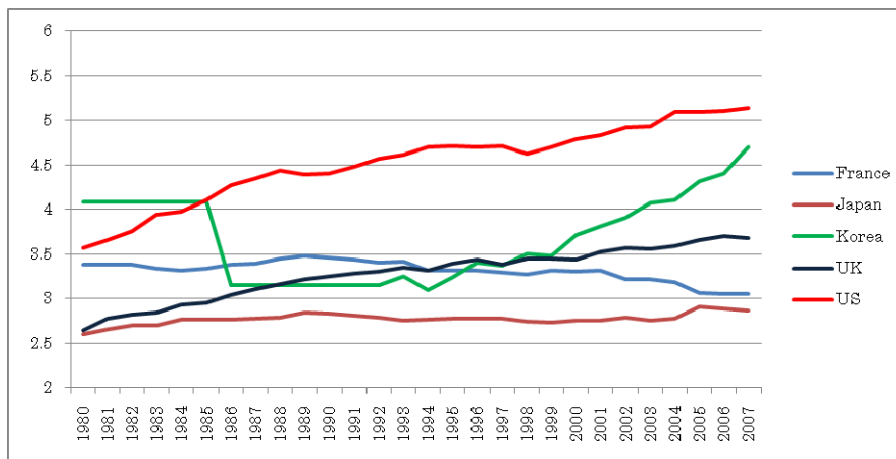
The most important factor of Japan’s economic growth: Japanese Economy as a Socialism

The Japanese management system was presumed to be the foundation of the strength of Japanese economy in 1980’s. It usually is assumed to be composed of the three or four elements including the seniority system, lifetime employment, enterprise unions and the transactions between group companies¹. How did the Japanese management system give their positive effects to the Japan’s economic growth? Fig. 2 shows the ratio of the second highest wage group to the lowest wage group in the selected countries when we divide the wages of the fulltime workers into 10 groups according to the wage level. As we can see from this graph, the disparity of the wages in Japan is relatively small compared with US and Korea. The disparity in Korea increased rapidly after the Asian Economic Crisis in 1997. While the disparity in UK gradually increases, in France it

¹ In this article we only consider the wage systems in Japan. There are many studies which try to explain the efficiency and the rationality of the continuous transactions between the agents by using the differences of the risk attitudes.

decreases. Thus in EU countries, the wage system differs between countries.

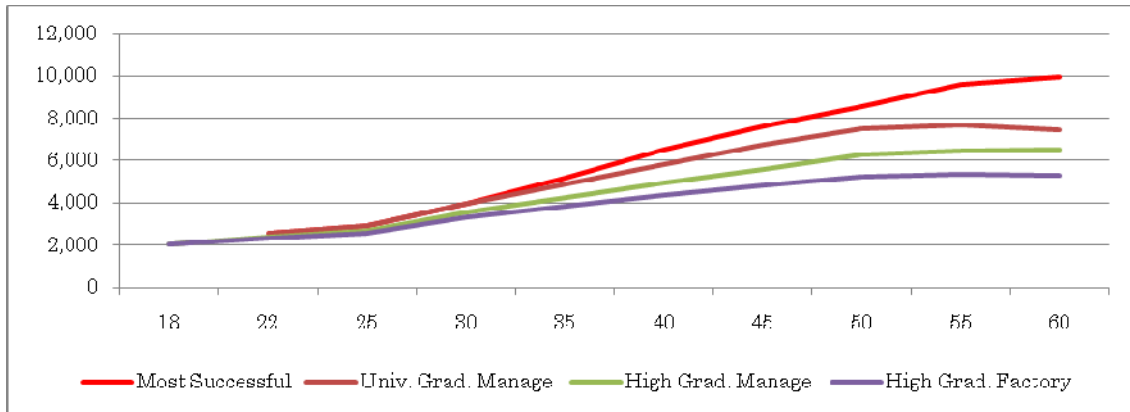
Fig. 2 Wage disparity of Full time Workers



出典 : OECD Statistics, Decile ratios of gross earnings, <http://stats.oecd.org/>

Let us see the details of the wage system in Japan. Fig. 3 shows how the monthly wages of fulltime workers change according to their age in Japanese big companies which are the members of “Keidanren,” an economic group in which Japan’s representative companies including Toyota and Panasonic join. The red line shows the most successful case where a new employee who graduated university at 22 and will be promoted consequently to a subsection chief at 35, a section chief at 40, a vice department chief at 45, a department chief at 50, a member of the board of trustee at 55 and the president at 60. Other lines are the case of the university graduates who assume administrative jobs, high school graduates who assume administrative jobs and the high school graduates who work in factories. The year when the data was collected is 2002. It is clear from this graph that in Japanese big companies, the wage difference between the factory workers who graduated high schools and the elite employees is small. In fact, only until twenty years ago, the income of the presidents of Japanese big companies is only two or three times as much as that of the factory workers. However, recently the annual income of a member of the board of trustee increased under the influences of US companies.

Fig. 3 Wage system of Japanese big companies (monthly wage, US\$)²



Source: Keidanren, *Annual Report on Wage*, June 2002

This is the wage system in Japan. At first glance, this kind of wage system seems to be inefficient as it might harm the incentives of workers for their work. However, in the Japanese social circumstances until 1980's, this wage system had succeeded in causing certain senses among workers to belong strongly to their own companies and the competitiveness of Japanese companies became powerful. Instead of the money incentives, such positions as section chiefs, department chiefs and members of the board of trustee, as well as the evaluations of their capabilities within their companies, became non-money incentives for workers. Even if one cannot win high positions or evaluations, the income disparity is not so big. Furthermore, it is difficult for him or her to move to other companies which have the same income level with their present ones. Thus every employee can make efforts for his or her company. It is true that this wage system only applies to big companies, and the workers in small and medium size companies cannot obtain the same wages as the workers of big companies. But this was the standard system in Japan and this was the wage system for the high-income workers.

This wage system also had the positive influences on the formation of the middle class in Japan after the World War II and the increase of the consumption level of the middle class was the driving force of Japan's economic development. We would like to see the details of this point in the next section.

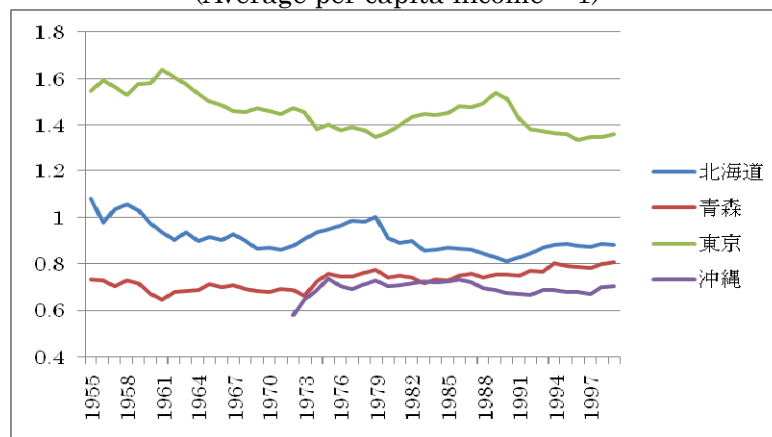
This relatively small disparity in the income distribution also existed in the incomes between urban and rural areas. In 1960's and 1970's, to promote the development of the rural area, the Japanese government implemented policies, such as constructing roads, inviting companies to set up their plants and subsidies to farmers.

² We calculated by setting 1\$=80 JPY.

As a result, the income disparity between Tokyo and the local areas was reduced drastically. Almost all the leaders of the LDP came from the rural areas and they were eager to redistribute the income from the urban to the rural areas. A representative example of such policies may be “The Reorganization Plan of the Japanese Archipelago,” which was proposed by Mr. Kakuei Tanaka (the prime minister, 1972-1974) who was from Niigata Prefecture. He devoted himself to the normalization of the diplomatic relations between Japan and China which was realized in 1972.

Fig. 4 shows the ratio of per capita income level of Tokyo and rural prefectures to the average for the period of 1955 and 1998. The income level of Tokyo ranges from 1.3 to 1.6. On the other hand, Hokkaido, which is situated in the northern end of Japan, Aomori, the northern end of the mainland of Japan, and Okinawa, the south end, are the lowest per capita income prefectures in Japan. But the levels are in the range of 0.6 to 1.0 and the disparity between Tokyo and the rural prefectures had been decreased until the end of 1970’s. Thus Japan used to be a country where the income disparity between the urban and the rural areas was relatively small.

Fig. 4 Per capita income of Tokyo and other prefectures
(Average per capita income = 1)



Source: The Cabinet Office, *Prefecture Economy Calculations*,
<http://www.esri.cao.go.jp/jp/sna/kenmin/h19/main.html>³

Decomposition of Japan’s GDP Growth

There exists a viewpoint that Japan developed its economy by exporting labor-intensive goods to US after the World War II. It is not true. The main factors which have contributed to the economic development of Japan are the consumptions and the investments in private sectors. Fig. 5 shows the contributions of private consumptions C ,

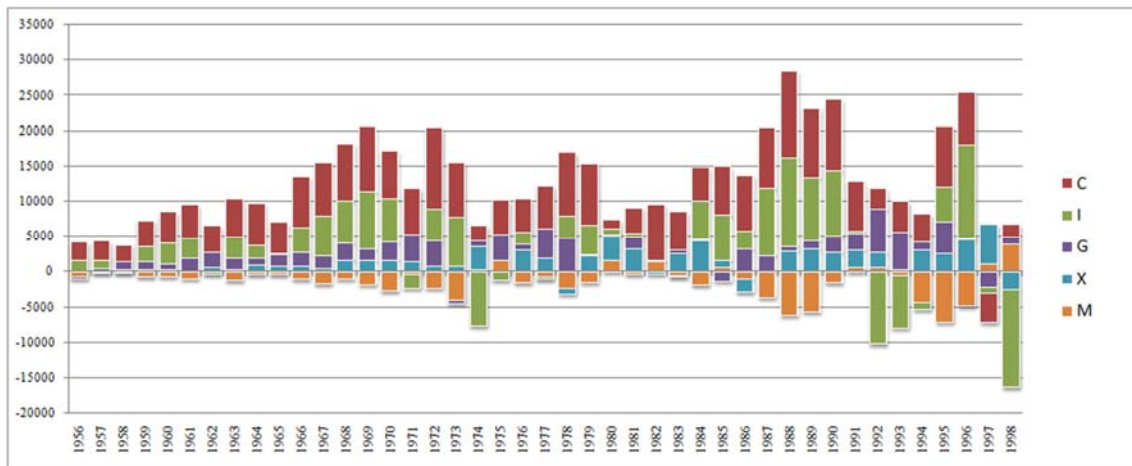
³ Okinawa prefecture was returned to Japan from the occupation of the US in 1971.

private investments I , government expenditures G , exports X and imports M to GDP growth for the period of 1955 and 1998. The increment of GDP ΔY can be decomposed into

$$\Delta Y = \Delta C + \Delta I + \Delta G + \Delta X - \Delta M.$$

It is clear from this graph that the most contributing factors to the GDP growth are the consumptions and the investments in private sectors. Thus Japan developed its economy by expanding the domestic demands.

Fig. 5 Decomposition of Japan's GDP Growth into Factors
(Real GDP growth, Base year is 1990, unit: billion JPY)



Source: *National Economic Accounts* 1998

Let us examine this tendency by using more exact figures. The period from 1955 to 1970 is called “high-rate of economic growth era” in Japan. Tokyo Olympic Games was held in 1964 and Osaka World Exposition was held in 1970, and Japan was recognized by the whole world as a developed country. The GDP growth rates in this era were around 10 %. Each factor's contribution to GDP growth in this period is shown in Table 1. The contribution of the private consumptions is 55.7 % and that of the private investments is 30.8 % and the contribution of the exports is only 7.1 %.

Table 1 contribution of factors to GDP growth (high-rate economic growth era)

ΔC	55.7 %
ΔI	30.8 %
ΔG	15.5 %
ΔX	7.1 %
ΔM	-9.1 %

Source: *National Economic Accounts* 1998

Bubble Economy and Its Burst

An Egalitarian income distribution formatted the middle class and the vital consumption desire of the middle class developed the Japanese economy. Fig. 6 shows the real GDP growth rates from 1956 to 1998. In the “high rate of GDP growth era” the rates are over 10 %.

Fig. 6 Real GDP growth rate of Japan (1956-1998)



Source: *National Economic Accounts 1998*

The Japanese economy experienced such period with the low economic growth rate and the hyper inflation caused by the “Oil Shock” (the crude oil price was raised by the OPEC countries) twice in 1973 and 1979. However, the economy recovered from the oil shock in 1980’s. The trade surplus increased every year and the economic growth became stable again. Thus, in the latter half of 1980’s Japan was thought to have the strongest economic system in the world. Japanese workers worked desperately for the companies they belong to and their income increased as the economy grew.

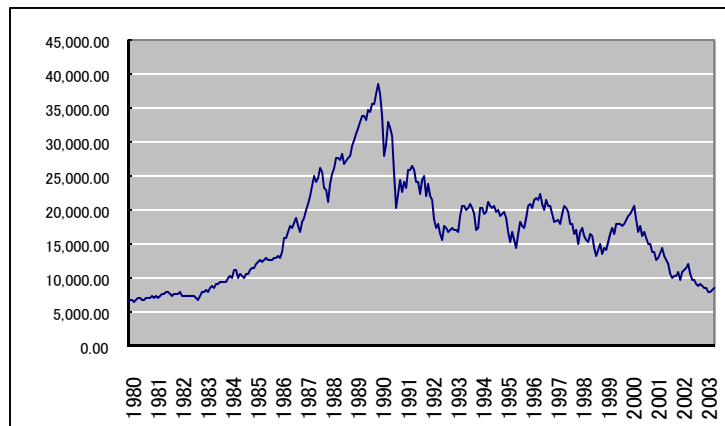
The golden era of the Japanese economy in 1980’s suddenly came to an end at the beginning of 1990’s. The causes of the collapse were the asset bubble which occurred in the end of 1980’s and the burst of the bubble in the beginning of 1990’s. The asset bubble started in 1986. In this period, the Bank of Japan reduced the official discount rate, fearing that a recession might be started by the rising exchange rate of Japanese Yen caused by the Plaza agreement. As a result, the excess money flew into the asset markets. As for the stock price, NIKKEI average stock index which was 12,000 yen in 1985 rose to 38,891 in the end of 1989. Thus the stock price increased more than three times in four years (Fig. 7). As for the land prices, the land prices of Tokyo city center

increased about four times in 1990 comparing to 1985. It was often said, “If you have enough money for buying whole Japan, you can buy four USs” (Fig. 8).

The government and the Bank of Japan implemented the tight-money policy, the regulation of real estate transactions and the tax reforms to control the asset bubble. But the timing was too late and failed.

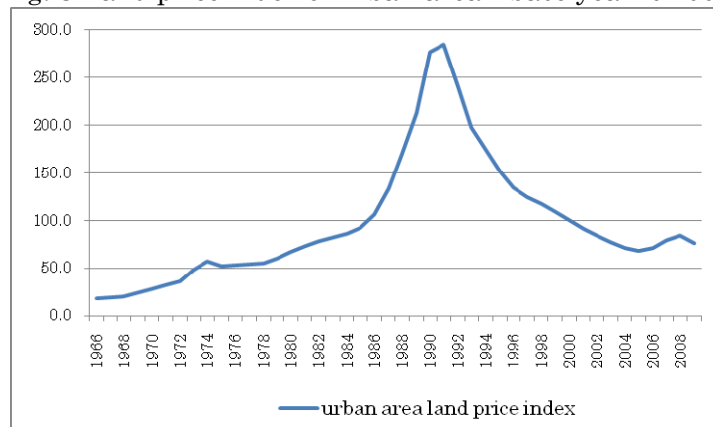
However, the stock price and the land price suddenly started to drop sharply. The NIKKEI average dropped to about 10,000 yen in the fall of 1992. There were some periods when the price rallied but the downward tendency continued until 2005. The land prices also dropped. The publication land values of the business-use areas dropped to a little over one third of what they used to be and those of residential areas dropped to a little under 60 %.

Fig. 7 NIKKEI average index (1980-2003) unit: JPY



Source: NIKKEI newspaper website

Fig. 8 Land price index of urban area base year is 2000



Source: Ministry of Land, Infrastructure and Traffic, Urban Area Land Price Index

In the background of the rapid expansion of the bubble and its collapse, there exists

the homogeneity of Japanese people's minds and the influence of the mass media. Usually Japanese people do not like to invest their money in risky assets. For example, the interest rate in Japan is now almost 0 %, but the percentage of those who are participating in risky investments is only 10 to 15 % in Japan. This is a very low figure, compared to 40 % in the US. However, in the period of the asset bubble, realizing the rapid increase of the stock prices and the land prices, people gradually began to be interested in investing in risky assets, and that made the mental hurdle lower than before. Information about encouraging various investments began to be overwhelmed in every media. Thus the amount of the investments increased and it made the bubble swell. However, once the fear of a sharp fall of the asset prices became evident, people inversely rushed to sell out the assets and it made the bubble burst rapidly. Needless to say, in that situation the mass media played an important role by exaggerating the fear of its sharp drop.

The collapse of the bubble was a fatal blow to the Japanese economy. In Japan banks usually lend money to a company on the security of the land the company owns. As the land prices increased by the asset bubble, the banks increased their loan to the companies. The banks which lent money and the companies which borrowed money both believed that there could be no problem even if the company could not return their money. For, the company can return money by selling the land which increases its value. However, when the land prices drop rapidly, the company cannot return money by selling the land it owns and the loan becomes the nonperforming one that cannot be returned. After ten years of the accumulations of these events, the nonperforming loans increased and the recession became more serious. Having fears of the increase of nonperforming loans, banks became reluctant to lend money and reinforced the debt collecting. The necessary money for the activities of properly producing and selling goods was not financed by banks and it caused the massive bankruptcy of small and medium sized companies and personnel reductions in big companies. Thus the Japanese economy fell into the so-called "deflation spiral" where the rate of unemployment exceeded by over 5 % and the price level continued to decrease.

To the Stagnation and Koizumi's Market Fundamental Reform

To settle the non-performing loans as the aftereffects of collapse of the bubble economy and to stimulate the economy at the same time were the extremely difficult tasks for the LDP government. For, if the government tries to settle the non-performing loans hastily, it may cause the bankruptcy of companies and therefore induce the economic recession.

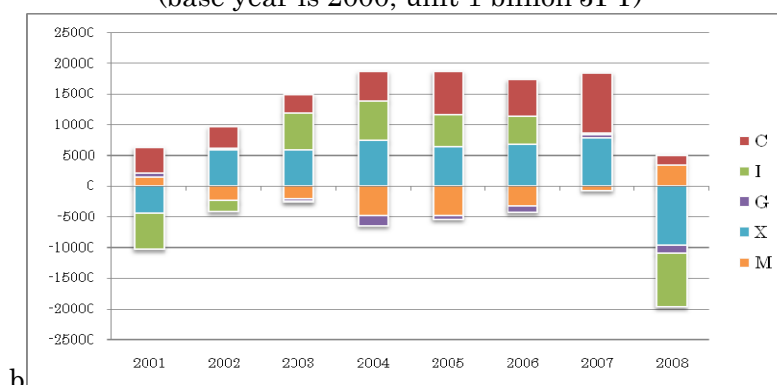
Thus the government should have to carry out soft-landing economic policies; to do the stimulation policies on one hand and the disposal of bad debts on the other.

Another aftereffect of the bubble and the collapse of bubble is the influence on the morality of Japanese people. In the bubble era, real estate prices increased twice or three times within a year and people began to feel that it was absurd to work desperately for their firms every day for the sake of low wages. After the collapse of the bubble, people awoke from their dreams and became pessimistic for the future economic growth and the increase of their income, and the incentive for working decreased. People's desire for consumption declined and it made the recovery of the economy more difficult.

In this blockade situation, the government could not expect the increase of the domestic demands and tried to induce the depreciation of Japanese yen and increase the exports for the economic growth. As a result, a more weight was given to the exports in the contribution to the GDP growth. Fig. 9 shows the contribution of each factor to GDP growth after 2000 in Japan. Comparing Fig. 9 with Fig. 5, it is apparent that the increase of the exports has played an important role since 2000.

However, it is clear that this export-oriented economic growth policy is neither sustainable nor stable in the long run. To increase the competitiveness in the exports markets, Japanese companies requested the deregulation of the employment forms to the government and moved their factories from the rural areas in Japan to the overseas where the wages are relatively low.

Fig. 9 Decomposition of real GDP growth after 2000
(base year is 2000, unit 1 billion JPY)



Source: *National Economy Accounts*

Mr. Koizumi came on stage in the middle of such situation in 2001. The Koizumi administration took monetarist or new-liberalism economic policies, such as the deregulation, a small government and the privatization, and left the economy in the

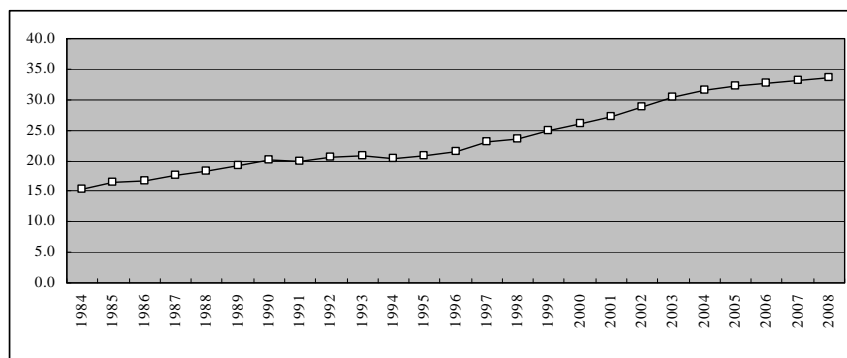
market mechanisms. The LDP administrations before Koizumi also intended to phase these policies. But Koizumi tried to push it forward abruptly and at the same time settle the nonperforming loans drastically. As its inevitable results, the economy was further deteriorating. Koizumi called the situation “a temporary pain”. However, it was not clear how long “the temporary” would continue and those who should suffer “the pain” were the socially weak people.

The policy which has the most serious influences was the deregulation for temporary workers. Dispatching the staff for temporary work (the workers who belong to temporary agencies and work in other companies as temporary employed workers) was legally approved for the first time in 1986. But it was only approved for the special jobs such as the development of computer software. However, it was gradually extended to a wider variety of occupations in 1996 and 1999. And finally in 2004 it was applied to all the manufacturing jobs. The above-mentioned Japanese style wage system is still applied to the full time workers but it is not applied to the temporally employed workers. That means that temporary workers can earn only very low wages even if they do the same jobs as the full time workers do. The ratio of these temporally employed workers has been increasing as shown in Fig. 10. It was 20 % in 1990 and increased to 35 % in 2008.

When dispatching temporary workers was introduced to the Japanese business world, the economy was not in recession and it attracted people’s attention as a new style of life which was not bound by a company. However, the economy gradually fell into the recession and it changed temporary workers just into poor workers whose futures were uncertain. For the 80 % of the temporary employed workers including part time workers and the staff dispatched for temporary work, their annual incomes are below 3 million JPY.

Sending temporary employed workers to the Japanese business system brought a great benefit to individual firms, that is, the total wage reduction. But, on the other hand, it brought negative effects to the whole economy. The middle class has been gradually vanished, whose situation was once described, “everybody belongs to the middle class.” In Japan the newly generated wealthy class did not have the power of leading consumptions like US. Full time workers who work for big companies began to realize the fear of the possibility of being fired and they decided to stop buying things. Thus the stagnation-dominated economy was generated in Japan.

Fig. 10 Rate of the temporary workers (1984-2008, level in February, %)



Source: *Labor Force Examination*, the number of employees by the employment forms

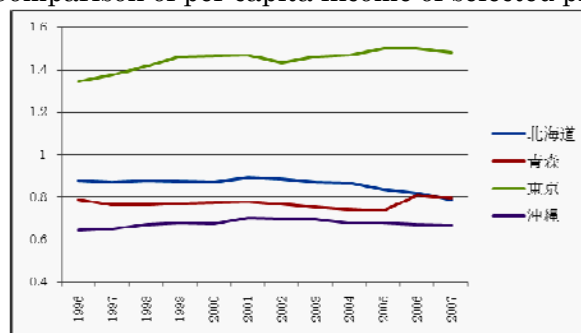
Table 2 Annual income by employment forms

	Ratio		
	Employee	Full time	Temporary
Under 1 million JPY	5.9	1.2	27.5
1~ 1.99 million JPY	10.1	5.7	29.6
2~ 2.99 million JPY	15.9	14.8	20.8
3~ 3.99 million JPY	18.0	19.6	11.1
4~ 4.99 million JPY	15.2	17.4	5.0
5~ 6.99 million JPY	17.8	21.1	3.4
7~ 9.99 million JPY	13.0	15.5	2.1
10~14.99 million JPY	3.5	4.1	0.4
Over 15 million JPY	0.6	0.7	0.2

Source: The Ministry of Health, Labor and Welfare, *Annual Income from Jobs*

For urban and rural areas, the income disparity gradually increased and the local economies went into a decline caused by the recession, the decrease of the subsidized taxes and the reduction of the local public investments (Fig. 11). While the per capita income in Tokyo increased from 1.3 times 1.5 times compared with the average, the per capita income in Hokkaido decreased from 0.9 to 0.8⁴.

Fig. 11 Comparison of per capita income of selected prefectures

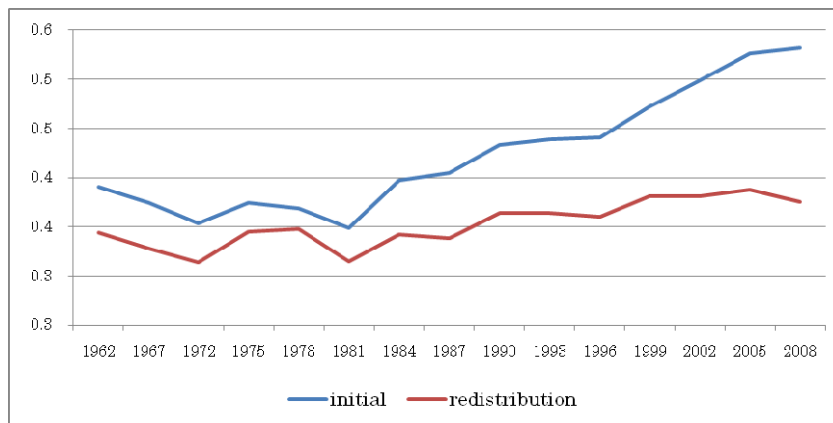


Source: The Cabinet Office, Prefectural Economic Accounts

⁴ The rise of the per capita income of Aomori prefecture is due to the construction of the nuclear fuel reprocessing plant.

The income disparity is thought to increase by the various deregulations and market-oriented economic policies. Fig. 12 shows the changes of gini coefficients of “before the redistribution of income” and “after the redistribution income” in Japan. The gini coefficient before the redistribution of income increases from 1981 and approaches to 0.6, and the coefficient after the redistribution is also in a tendency of increasing. However, there is an argument that the rise of the gini coefficients is due to the aging society. In that argument, as the gini coefficient of the income distribution is high for the elder people, the gini coefficient increases if the rate of the elder people increases. The aging is definitely the major factor of increasing the coefficient. However, the problem here is not the increase of the income disparity in the society but the increase of the poor people. To see this problem, we can directly compare the income distribution of the households.

Fig. 12 Gini Coefficients in Japan

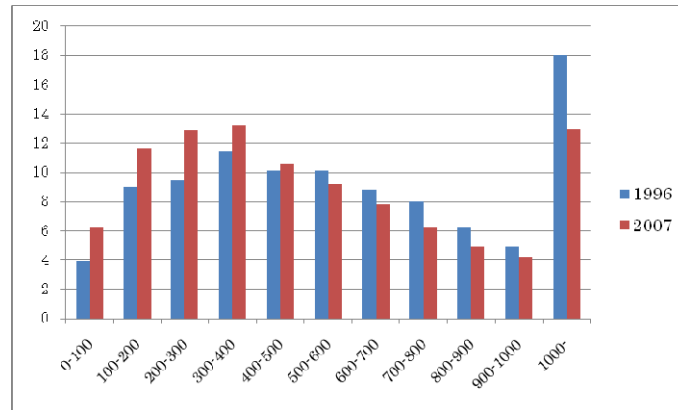


Source: The Ministry of Health, Labor and Welfare, Investigation on the income redistribution

Fig. 13 shows the income distribution of the households between 1996 and 2007. It is apparent from this graph that the households whose annual incomes are below four million JPY increase drastically. These figures are the most reliable “the sense of the income disparity” for the people⁵.

⁵ There could be the possibility that the rate of the low income households increase by the increase of the pensioners who retired.

Fig. 13 Comparison of the households' income distribution (1996 and 2007)



Source: The Ministry of Health, Labor and Welfare, *The examination of people's basic life*.

The poverty rate of Japan (the ratio of the population whose income is below the half of the median of the income distribution to the total population) is shown in Table 3. In the middle of 2000's the poverty rate of Japan's after-income redistribution is 14.9 and this is the second largest number following the 17.1 % of US in OECD countries. The more serious problem is that the poverty rate of Japan before-income redistribution is not so different from that of Sweden. It means that there are serious problems in Japan's social security systems.

Table 3 Comparison of the relative poverty rate (Before and after income redistribution)

	mid-1970		Mid-1980		around 1990		mid-1990		around 2000		mid-2000	
	after	before	after	before	After	before	after	before	After	before	After	Before
Sweden	3.8	22.0	3.3	26.1	3.6	25.9	3.7	29.6	5.3	27.0	5.3	26.7
France			8.3	35.8	7.2	34.3	7.5	34.3	7.2	33.0	7.1	30.7
UK							10.9	29.9	10.2	27.8	8.3	26.3
Germany			6.3	26.9	6.6	24.9	8.5	28.7	9.2	31.1	11.0	33.6
Korea											14.6	17.5
Japan			12.0	12.5			13.7	19.0	15.3	23.9	14.9	26.9
US	15.4	23.0	17.9	25.6	18.1	25.9	16.7	26.4	17.1	25.4	17.1	26.3

Source: OECD Income distribution - Poverty, <http://stats.oecd.org/>

Thus, although there are important factors such as the aging society and a declining birth rate, there is no doubt that the income disparity and the rate of the poor households have increased in Japan. This tendency became the vital factor for depressing the increase of consumption in Japan.

The DPJ administration and the redistribution policy of income

In fact, for the majority of politicians in the LDP whose supporters are small farmers or small-business owners or workers, this situation was quite an unendurable one. However, almost nobody could criticize the Koizumi administration, having fears of his charismatic popularity, and a few who criticized Koizumi were forced to get out of the LDP. It is beyond the range of the normal economic analysis why Koizumi succeeded in getting such a big popularity. Ironically, the people who supported Koizumi enthusiastically were those who suffered most from Koizumi's economic policies. These kinds of phenomena will become more important when we consider the practicability of the economic policies. In Japan and many developed countries, it often happens that the mass media assert opinions which seem to be popular to the public. And the opinions inevitably influence the public opinions which would therefore influence political situations and economic policies. Koizumi used this relationship dexterously and controlled the mass media and the public opinions. Fortunately, it was his personal character that enabled him to win the popularity and it was not established as a method. The prime ministers after Koizumi could not get as great a popularity as Koizumi did and they were made targets of the mass media and were forced to resign as scapegoats.

There are two big political parties in Japan now. These are the DPJ (Democratic Party of Japan) and the LDP (Liberal Democratic Party). Both parties have wide ranging opinions in their respective ones and what kinds of ideologies on which these parties' policies are based are not distinct. However, if we simplify and show schematically, both parties' policies depend on the two big streams of the ideologies, the monetarism and the Keynesian (Table 4). We can explain the differences of the two parties' policies by comparing the weights of these two ideologies. While the LDP represented by the Koizumi administration took the monetarist policies, the DPJ made its Keynesian position clearly in the manifesto of the election of 2009. We can classify that in the US the Republicans are close to the monetarists and the Democrats are close to the Keynesians, and in UK the Conservative Party is close to the monetarists and the Labor Party is close to the Keynesians.

Table 4 Monetarist and Keynesian

	Market	Tax	Economic policies	Ideology
Monetarist	Deregulation Small government Confidence to the market	Reduce taxes to the rich	Fiscal policies: no effects Monetary policies only for inflation	Principle of competition Self-responsibility
Keynesian	Intervention in the market	Subsidy to the poor	Stimulate the economy by public investment Multiplier effect	Human being are influenced by the environment Relief the weak

The DPJ declared in the Manifesto 2009 that it will implement the economic policies such as “child allowance” (pay 312,000 JPY per child to the family), “effectively free public high school tuition”, “individual income support for agriculture” and “ban on the dispatch of temporary workers”⁶. These are the typical Keynesian economic policies of the income redistribution from families with no children to families with children, from urban to rural areas and from the rich to the poor. However at this point of time, it is very difficult to implement these policies.

Why does everything go wrong? What should we do?

What policies should be needed for Japan to escape from the stagnation? As we consider in this article, the burst of the bubble and the subsequent implementations of the economic policies based on the market fundamentalism, especially the deregulation for temporary workers increased the income disparity and the middle class was vanished. These were the causes for depressing the private consumptions in Japan. Thus, to restore the private consumptions by the income redistribution policies from the rich to the poor is no doubt one of the effective policy prescriptions. In fact, the DPJ announced such policies in Manifesto 2009.

However, when the DPJ took office, it was not able to carry out the policies sufficiently due to the lack of financial resources and the frictions with bureaucrats. The mass media also criticized that these policies were “haphazard”. The only person who was thought to be able to implement these policies, Mr. Ichiro Ozawa was ousted from the important posts by the money scandal. The other DPJ politicians were powerless to control bureaucrats and execute their policies by force.

Another reason is the so-called “hysteresis effect” that means that once we lose

⁶ The DPJ, *Manifesto 2009*.

something, it is difficult to regain it. Most important factor may be the people's pessimistic expectations and it is not easy to reverse them.

In any case, it is clear that we should revive the regulations for temporary workers and decrease the income disparity by the income redistribution policies, such as the subsidies to the weak. By means of those, it could be possible to make the private consumptions recover. However, we are made to be pessimistic for the possibility of its realization at this point of time.

The Economic Relationship between Japan and China

In the last part of this article, I would like to make some comments on the Japan-China economic relationships. The economic relationships and the political relations between Japan and China were and are currently in a difficult situation. As everybody knows that there happened a confrontation recently between the governments on the territory problem. In Japanese media and the public opinions, there exists the strong nationalism, especially the antipathy against China and Korea. The reaction of the government who fears the opinions of the mass media, the public, and the right wing politicians who are supported by such opinions made the situation to the worse directions. In every country some kinds of the harmful nationalism exist. But the problem in Japan is the existence of the mass media which agitate the right wing opinions⁷. As we considered above, such opinions of the mass media also is the important factor which make the Japan's politics and its economy feeble.

However, as for the aspect of the economy, the relationship between Japan and China is clearly stable. As Fig 14 shows, overtaking the US, China became the No. 1 trade partner both for the exports and imports of Japan.

Fig. 14 Trade between Japan-US and Japan-China (unit: one billion JPY)
 Japan's Export Japan's Import

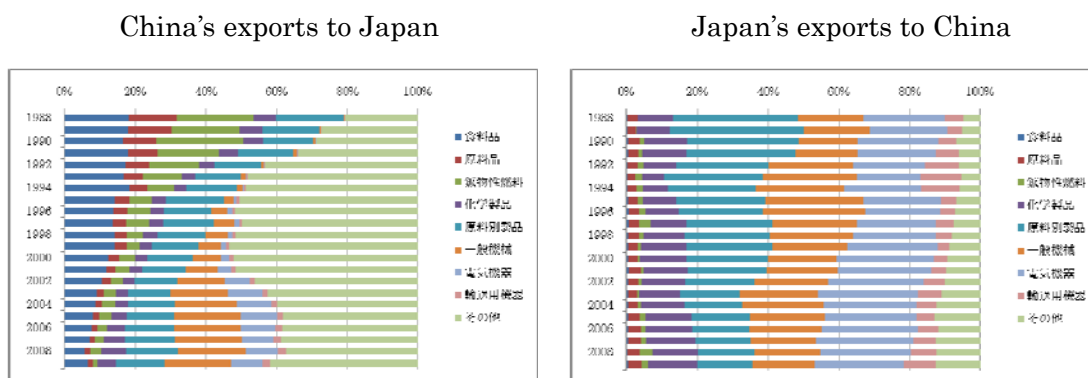


Source: The Finance Ministry: *Trade Statistics*

⁷ These tendencies are also true for the FOX TV and CNN in the US.

For the contents of trade, in China's exports to Japan, the goods that have the high component rates were foods, raw materials and fuels until 1990's. But now the component rates of the general machinery and the electric machinery have increased and the trade becomes the horizontal or inter-industrial where both countries export the goods of the same industries (Fig. 15).

Fig. 15 Trade between Japan and China (money amounts)



Source: The Finance Ministry, Trade Statistics,
<http://www.customs.go.jp/toukei/suii/html/time.htm>

For the foreign direct investment, the FDI to China also relatively increased its weight caused by the economic crisis in US. As is shown in Table 5, the FDI to Asian countries exceeded to that of the US and the EU and the amount of FDI to China is approaching to that of US.

Table 5 FDI of Japan (2005-2009) unit: 100 million JPY

	Asia	China	India	USA	Europe
2005	17,980	7,262	298	13,599	9,015
2006	20,005	7,172	597	10,834	21,423
2007	22,826	7,305	1,782	18,524	24,882
2008	23,790	6,700	5,429	44,617	23,551
2009	19,427	6,492	3,443	9,989	16,680

Source: The Finance Ministry, The Current Situation of the Balance of Payments

There is a possibility of a future expansion of the amounts of trade by the agreements of the FTA or other trade liberalizations. At this point of time, Japan has comparative advantages over China in the fields of technologies, qualities and safety in many industries and China has advantages in cost. Thus the trade between Japan and China is a complementary one and both countries are likely to increase trade and

investment. There is a big opportunity, for example, in the field of environmental business. Trade with China is also important for making Japan escape from the stagnation. The problem here is again that the economic relationships are disturbed by the politics. As we see in this article, the worst factor which makes the politics go to the wrong directions is the opinions of the mass media and the public. How to control them and to make the vanished middle class revive are the tasks which the Japanese politicians have to carry out.