



A New Direction for Japan? Part II

Adam S. Posen explains how the Japanese leadership's concerns over the rise of China are galvanizing Prime Minister Abe to act, with consequences that could be both favorable and worrisome.

Transcript of interview recorded December 31, 2012. © Peterson Institute for International Economics.

Steve Weisman: Adam Posen, President of the Peterson Institute for International Economics is here with me, Steve Weisman, continuing our discussion about Japan and its new leadership. Adam just said that people might be surprised at how much change is in the offing, in part because of Japan's concerns about competition in its region, especially from China. Let's pick up on that, Adam. How much is Japan, as you earlier said, spooked by the rise of China and how is this influencing its economic thinking?

Adam Posen: I think the key thing I have to say at the start, Steve, is I'm not saying this is necessarily a good thing or that it's an accurate appraisal by Japan. But it's a factual statement that a lot of the business leadership, a lot of the government leadership, and a lot of average people are much more concerned about China's role in the region and as Japan's neighbor than they were in previous years. And this is mostly a national security thing.

We see China and Japan in conflict over these variously named islands. There are other potential conflicts in the region. God willing, particularly with U. S. involvement, nothing will escalate.

There have been demonstrations of strong anti-Japanese sentiment, which of course remains in China, including destruction of some property and some production in China owned by Japanese companies. It is scary.

On China, have no idea. I listen to the experts at the Institute. You know, I don't have any reason to think that they have particular territorial ambitions or anything hostile towards Japan. But they're clearly flexing their muscles in ways that make Japanese multinational companies, make Japanese average citizens, and especially make Japanese government officials nervous. And the return of the LDP [Liberal Democratic Party] can, to some degree, be attributed to not just extreme dissatisfaction with the economy over the last years—which certainly was a part of it—but the liberal Democrats are also associated with more—for want of a better term – hawkish positions on China, North Korea and so on—more military self-defense movements by Japan, and it certainly seems to be affecting behavior.

Steve Weisman: Like any political party, the LDP is a coalition of groupings. One of those groups that's always been influential is the right wing and even the extreme right wing in Japan. Prime Minister Abe has begun sending signals, for instance in reviewing the Japanese apology over the use of prostitutes during World War II. How much of a ripple effect is this having in the region?

Adam Posen: I prefer to stick to the economics. It's clearly negative. When the Japanese government has chosen to be less than forthright and apologetic about the war crimes committed by

the people in power in Japan during the World War II era, it understandably provokes a negative backlash, from China in particular, and in a number of previously occupied countries in the region. It's not a good sign. And it is, on a much lower key level, similar to different factions, say, within the Republican Party in the U. S. There's a piece of the Republican Party that wants to be very confrontational with China on economics, but also on the military. There's also a piece of the Republican Party that says this country isn't going anywhere. It's a huge opportunity for us. Let's be responsible grownups. Robert Zoellick [former World Bank president], who is visiting with us, used the term of trying to make China a "responsible stakeholder." Engage with them. For the most part, Japanese business—and again, the professionals in the Japanese government, the senior civil servants—have been along that line. They've been "Trust, but verify," not entirely trusting of Chinese officials, but they've done a lot to invest in China, to build networks with China.

Cooperation between the Bank of Japan, for example, and the Peoples Bank of China or the Ministry of Finance in Japan and their counterparts in China is actually quite good and has been for many years. So I fear, as an economist, as well as just someone who cares about Japan and peace in the region, that raising this very red flag of trying to do revisionist history. I understand there must be domestic reasons to cater to that, but I think it is an unfortunate thing to do.

Steve Weisman: Before we conclude, let me just circle back to one point that you made initially. When you talked about the Japanese stimulus efforts, you mentioned that besides monetary stimulus, they are talking about fiscal stimulus and trying to get the private sector to spend more or invest more. Is that likely to produce any dramatic results?

Adam Posen: No. That is where I—as opposed to where I very strongly agree with the general thrust on monetary policy—I strongly disagree on fiscal policy. Some people who have been following this may remember in the late 1990's, early 2000's, I was pointing out that fiscal stimulus was a good idea in Japan in that context. But that's 15 years ago now. And their current problems are not due to a generalized lack of demand. It's due specifically to deflation and an over-valued exchange rate. So it makes sense to do a lot of monetary stimuli. But they have accumulated more debt through the years, and it is a different situation and they have wasted a lot of the money they spent. And so, 15 years later, yes, they have, I think, run out of room. Not in the sense that literally tomorrow Japanese bond interest rates go through the roof, but that they've run out of room. It is no longer productive for them to be engaging in fiscal stimulus, at least beyond trying to rebuild the places that were hit by the tsunami.

So, I think the monetary impetus is right, but I think that a fiscal stimulus right now for Japan—it's always context specific when it works and when it doesn't—I don't think it's productive.

Steve Weisman: Thank you, Adam.

Adam Posen: Thank you, Steve.

