



World Owes Japan an Apology

Tamim Bayoumi says the case of Japan shows just how hard it can be for governments and central banks to stimulate growth and inflation when demand is weak.

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Pedro da Costa: Hi, I'm Pedro da Costa, editorial fellow here at the Peterson Institute for International Economics. I'm joined by Tamim Bayoumi. He's a senior fellow here at the institute and we're here to talk about Japan. Welcome.

Tamim Bayoumi: Well, welcome.

Pedro da Costa: And, first question is Japan has been undergoing this kind of great macroeconomic experiment, right? It had 20 years of deflation, then you had a new prime minister who came in and said, "Look, we're going to deliver growth. We're going to pull out all the stops." And it's been a couple years since that happened and what's happened? What's going on in Japan?

Tamim Bayoumi: Well, not as much as you might have heard. Abenomics as it was called had three basic--three arrows it was called. And of those three arrows, one was monetary expansion and we've seen a lot of that from the Bank of Japan. They've bought a lot of assets, they've done quantitative easing.

The second was structural reforms where they've done a certain amount certainly in the corporate governance area, for example, they've done quite a lot. They've also done a certain amount on female participation issues labor in Japan.

The third arrow is fiscal where the exact objective was less clear in terms of the fact that it both seemed to involve a certain amount of short term stimulus, but also of course, Japan has got the highest debt ratio basically of any advanced country. And so, at some point, they clearly also need to move back to a sustainable fiscal path. And that never seemed to be part of the story on Abenomics. So it seemed to be more about stimulus than it was about producing it sustainable.

Pedro da Costa: Now, the results have been fairly mixed. Japan has barely escaped the technical recession now that the third quarter GDP was revised higher. The Bank of Japan, again, has intervened with the new round of intervention. It's not exactly--not just bond purchases but they're buying ETFs. Have they really reached the limit in terms of ammunition of what they have and is Japan just at--and given its demographics and the aging population story that everybody talks about in Japan, has Japan just reached the limits of growth or is it a policy mistake that is being made?

Tamim Bayoumi: Well, firstly, it has been somewhat disappointing. There was originally a significant rise in inflation even taking to account the hikes in indirect taxes that they were putting into effect. But growth also went up a certain amount but now inflation is back to essentially

zero and growth as you say, they just avoided yet another technical recession. They've been bouncing up and down sort of either side of zero, possibly a little above zero for a while. But essentially it looks like the situation that they started with, with Abenomics.

So, in that respect, Abenomics does not seem to have been particularly successful. As a result as you say, they've been announcing a series of new measures. What's interesting is of course the background toward this was a lot of pressure from the rest of the world who said that one of the reasons that they were facing deflation and low growth was that they haven't tried hard enough on the take on the macroeconomics.

And to me, one of the lessons of the great recession and of what's just happened is that to some extent, the world slightly owes Japan an apology. The Japanese always argued that their deflation was much more structural than people realized they're much more difficult to get rid of. Well not only has the stimulus not seemed to have worked particularly well but the rest of the world is also facing problems raising inflation.

So to some extent, what seemed very easy to everybody else, they've turned out to be turning a little Japanese.

Pedro da Costa: Sure. And now, is it a cautionary tale for other central banks like the US Central Bank and the ECB, do you think that they'll have equal trouble raising inflation at this point? The Fed certainly has struggled?

Tamim Bayoumi: The Fed has struggled. The Fed seems to be moving back. Their latest CPI shows a reasonably high core although the headline is low because of oil prices largely. But I think particularly in Europe which is in many ways and they're much more in a situation which is rather more similar to Japan, the question about whether they can really raise inflation very successfully I think is a very pertinent one.

Pedro da Costa: Or maybe the refugee inflow will have an impact but we'll leave that for another conversation.

Tamim Bayoumi: Absolutely.

Pedro da Costa: Thank you so much.

Tamim Bayoumi: Thank you.

