Global Challenges: The Lessons of Japan

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Yale Jackson Institute for Global Affairs

October 2013
Conceptual Framework: Forensic Macro

- Japan as the Template
- Policy Blunders or Structural Malaise?
- Bubbles, Imbalances, and “Zombies”
- The Hangover: Debt, Deflation and Lost Decades
- Exit Strategies: A Way Out?
## Made in Japan?

<table>
<thead>
<tr>
<th></th>
<th>Japan</th>
<th>United States</th>
<th>Europe</th>
<th>China</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Model</strong></td>
<td>Developmental state</td>
<td>Invisible hand</td>
<td>State-directed Capitalism</td>
<td>Market-based Socialism</td>
</tr>
<tr>
<td><strong>Mandate</strong></td>
<td>Lifetime employment</td>
<td>Full employment</td>
<td>Union of peace and prosperity</td>
<td>Growth vs stability</td>
</tr>
<tr>
<td><strong>Policy blunder</strong></td>
<td>Yen suppression and the Plaza Accord</td>
<td>Condone bubbles Clean not lean</td>
<td>Flawed currency union</td>
<td>Anti-consumer</td>
</tr>
<tr>
<td><strong>Regulatory blunder</strong></td>
<td>Evergreen bank lending (MiTI)</td>
<td>Mortgage abuses Lax bank oversight</td>
<td>No banking union No fiscal union No political union</td>
<td>State-directed bank lending (NDRC)</td>
</tr>
<tr>
<td><strong>False prosperity</strong></td>
<td>Equity and Property bubbles</td>
<td>Property and Credit bubbles</td>
<td>Convergence bubble</td>
<td>Export bubble</td>
</tr>
<tr>
<td><strong>Economic distortion</strong></td>
<td>Zombie corporates</td>
<td>Zombie consumers</td>
<td>Zombie PIIGS</td>
<td>Zombie SOEs? Zombie LGFVs?</td>
</tr>
</tbody>
</table>
The Rise and Fall of Modern Japan

Japanese Real GDP Growth
(Averages over designated intervals)

Abenomics: Japan’s Phoenix?

Three Arrows
- Monetary: QE on steroids
- Fiscal: Public works
- Structural reforms

Three Foils
- QE traction and deflation
- Fiscal quagmire
- Yen, equities, and complacency

Source: T. Ito and International Monetary Fund WEO database
## Decomposition of Japanese Economic Growth

(Average annual % changes over designated 5 year intervals)

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<thead>
<tr>
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</thead>
<tbody>
<tr>
<td>GDP Growth</td>
<td>3.9</td>
<td>4.2</td>
<td>5.2</td>
<td>1.6</td>
<td>1.2</td>
<td>1.3</td>
</tr>
<tr>
<td>Labor</td>
<td>0.9</td>
<td>0.9</td>
<td>0.7</td>
<td>-0.1</td>
<td>-0.1</td>
<td>-0.1</td>
</tr>
<tr>
<td>Capital</td>
<td>1.7</td>
<td>2.0</td>
<td>2.5</td>
<td>1.9</td>
<td>1.3</td>
<td>0.9</td>
</tr>
<tr>
<td>TFP</td>
<td>1.3</td>
<td>1.2</td>
<td>1.9</td>
<td>-0.2</td>
<td>0.0</td>
<td>0.4</td>
</tr>
</tbody>
</table>

1974 to 1990 TFP average: 1.5%

1991 to 2005 TFP average: 0.01%

### Abe’s “Third Arrow” Agenda

- Agriculture
- Medical Care
- Energy
- Employment
- Immigration
- Education
- Tax System
- Gov. Reform
- Electoral System

Source: KLEMS database
US Consumption Binge...

Personal Consumption
As a share of GDP

1970-99 average: 64.6%

Last plotting:
2013-Q2: 68.7%

...Was Not Supported by Income Effects

Real Private Compensation
Index=100 at Business Cycle Troughs
- Average of Past 4 Cycles
- Current Cycle

103-month shortfall:
$1626.3 billion or 15.9% of real disposable personal income

But Driven by Wealth and Credit Bubbles

Personal Consumption
As a share of GDP

1970-99 average: 64.6%

Last plotting:
2013-Q2: 68.7%
Lingering Headwinds of U.S. Balance Sheet Repair

**Deleveraging**

Household Sector Debt Outstanding (% of Disposable Personal Income)

1970-99 average: 40.3%

**Rebuilding Saving**

Personal Saving Rate (% of Disposable Personal Income)

1970-99 average: 9.3%

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**America’s Zombie Consumers**

(US real consumption: Average annualized growth)

- The Balance Sheet Recession
  2008-I to 2009-II: -1.8%

- Anemic Recovery
  2009-III to 2013:2 +2.2%

- 22-Quarter Average
  2008-I to 2013-II: +1.1%

- Pre-crisis trend
  1996 to 2007: +3.6%

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Source: Federal Reserve flow-of-funds and U.S. Department of Commerce, BEA
**Growth European Style**

**European Long-term Interest Rates**
(Yields on 10-year notes)

- Germany
- Greece
- Ireland
- France
- Italy
- Spain

**Real GDP in Local Currencies**
(Index: 1999=100)

- High Flying PIIGS
  - Ireland
  - Greece
  - Spain
  - Portugal
  - Italy

- Sluggish Core
  - France
  - Germany

Sources: European Central Bank and International Monetary Fund

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Developing Asia’s Growth Bonanza

Real GDP Growth Disparities

<table>
<thead>
<tr>
<th>Year</th>
<th>Developing Asia</th>
<th>Adv. Economies</th>
<th>World</th>
</tr>
</thead>
<tbody>
<tr>
<td>2000-13</td>
<td>8.2%</td>
<td>1.8%</td>
<td>3.7%</td>
</tr>
</tbody>
</table>

Source: IMF *World Economic Outlook* data base (April 2013)
Global Rebalancing Imperatives

Investment Shares of GDP

Source: IMF *World Economic Outlook* database (April 2013)
Export-Led Developing Asia

GDP Shares: Developing Asia

Source: IMF, national data sources
Shares of World Trade Indexed at “Takeoff”

Index, period 0=100

Source: International Monetary Fund
Global Saving Disparities

Source: IMF World Economic Outlook (April 2013 WEO database)
China’s Unbalanced Growth Model

“Unstable, unbalanced, uncoordinated, and unsustainable.”
— Premier Wen Jiabao, March 16, 2007

Source: National Bureau of Statistics of China
China’s Internal Imbalances

**Labor-Saving**

Average GDP and Employment Growth: 2000-2008

<table>
<thead>
<tr>
<th>Country</th>
<th>GDP Growth %</th>
<th>Employment Growth %</th>
</tr>
</thead>
<tbody>
<tr>
<td>China</td>
<td>11.8</td>
<td>9.8</td>
</tr>
<tr>
<td>India</td>
<td>6.4</td>
<td>6.8</td>
</tr>
<tr>
<td>Indonesia</td>
<td>6.0</td>
<td>5.8</td>
</tr>
<tr>
<td>Korea</td>
<td>5.6</td>
<td>4.8</td>
</tr>
<tr>
<td>Thailand</td>
<td>3.6</td>
<td>3.8</td>
</tr>
</tbody>
</table>

**Resource-Intensive**

China’s Share of World Total: 2008

- Crude Oil: 15%
- Aluminum: 30%
- Steel Products: 20%
- Iron Ore: 50%
- Coal: 35%
- Cement: 45%

China’s Pro-Consumption Rebalancing

The 12th FIVE-YEAR PLAN

<table>
<thead>
<tr>
<th>MECHANISM</th>
<th>GOAL</th>
</tr>
</thead>
<tbody>
<tr>
<td>JOBS BLUEPRINT FOR LARGE-SCALE SERVICES INDUSTRIES</td>
<td>LABOR ABSORPTION</td>
</tr>
<tr>
<td>WAGES SUPPORT TO RURAL HOUSEHOLD INCOMES</td>
<td>HARMONIOUS SOCIETY</td>
</tr>
<tr>
<td>FINANCIAL SECURITY SAFETY NET IMPERATIVES</td>
<td>REDUCE PRECAUTIONARY SAVING</td>
</tr>
</tbody>
</table>

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The Potential in Chinese Services

A Lagging Chinese Services Sector

Labor Intensity: Jobs per RMB Million GDP

Targeted in the 12th Five-Year Plan

Manufacturing and Construction (Secondary)
Services (Tertiary)

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Income Leverage of Urbanization

**Urban Share of Chinese Population**

- 2012: 52.6%
- Projected urban population growth: 2030: 316 million (OECD)

**Ratio of Urban to Rural Income**


Source: UN, OECD

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Urbanization Drives Investment

Chinese Capital Stock Per Capita Relative to the U.S. and Japan

Source: Penn World Tables and International Monetary Fund
Source: International Monetary Fund, National Bureau of Statistics (China), National Social Security Fund (China), Xinhua News Service, BBVA Research
<table>
<thead>
<tr>
<th>5-year Plan</th>
<th>Dates</th>
<th>Key Feature</th>
</tr>
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<tbody>
<tr>
<td>First</td>
<td>1953-57</td>
<td>Stalinist Central Plan</td>
</tr>
<tr>
<td>Second</td>
<td>1958-62</td>
<td>Great Leap Forward</td>
</tr>
<tr>
<td>Third</td>
<td>1966-70</td>
<td>Agricultural Push</td>
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<tr>
<td>Fourth</td>
<td>1971-75</td>
<td>Cultural Revolution</td>
</tr>
<tr>
<td>Fifth</td>
<td>1976-80</td>
<td>Post-Mao (Reforms and Opening Up)</td>
</tr>
<tr>
<td>Sixth</td>
<td>1981-85</td>
<td>Readjustment and Recovery</td>
</tr>
<tr>
<td>Seventh</td>
<td>1986-90</td>
<td>Socialism with Chinese Characteristics</td>
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<tr>
<td>Eighth</td>
<td>1991-95</td>
<td>Technical development</td>
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<tr>
<td>Ninth</td>
<td>1996-00</td>
<td>SOE Reforms</td>
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<tr>
<td>Tenth</td>
<td>2001-05</td>
<td>Strategic Restructuring</td>
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<tr>
<td>Eleventh</td>
<td>2006-10</td>
<td>Rebalancing Alert</td>
</tr>
<tr>
<td>Twelfth</td>
<td>2011-15</td>
<td>Pro-Consumption</td>
</tr>
</tbody>
</table>

China’s Strategic Advantage
Codependency and Rebalancing Imperatives

**Personal Consumption Share of GDP**

- **United States**
- **China**

Source: U.S. Department of Commerce and National Bureau of Statistics (China)
Global Imbalances and the Lessons of Japan

Current Account Disparities
(as % of World GDP)

Surpluses

Deficits

Forecast


Total Imbalances 1.2% 2.0% 3.2% 3.2% 3.8% 5.6% 5.1% 3.8% 3.4% 3.0% 2.8%
(as % of World GDP)

Source: International Monetary Fund (October 2012 WEO database)

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