

JAPAN CHAIR PLATFORM

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The Best Scenario: Japan's Political Crisis as a Reform Driver

Kiyooki Aburaki

The Cost of Noda's Conviction

"Decide when it is time to decide, draw a conclusion, don't postpone; this is the type of politics I want to create."¹ Prime Minister Yoshihiko Noda made this declaration in a press conference on June 26 immediately after the passage of the consumption tax-hike bill in the Lower House of the Diet. Noda's conviction to pass a tax increase had a political cost: 57 lawmakers of the ruling Democratic Party of Japan (DPJ) voted against the bill, while 15 DPJ members abstained. Former DPJ president Ichiro Ozawa, who leads the anti-tax-hike movement, and his followers created a deep rift within the ruling party over the tax legislation and subsequently damaged Noda's political power base by defecting from the party on July 2.

The influence of the opposition Liberal Democratic Party (LDP) will increase because Noda needs the LDP's support to pass the tax hike through the Upper House, where the opposition has the majority, and also to reject a possible no-confidence motion in the Lower House should Ozawa try to further weaken Noda's political standing. No one can predict Japan's political landscape after the next election, given the low approval ratings of the DPJ and LDP and the rise of newly established parties. The general consensus is that the fallout over the consumption tax-hike bill will lead to political chaos.

In reality, however, this may be an opportunity for Japanese politics to move beyond the simple realignment of political parties and fully embrace structural reform. This becomes clear when one considers the worst-case scenario for the DPJ and opposition parties that are now wedded to the consumption tax-hike bill.

Insecurity that Mobilizes Politicians

We can assume the enactment of the consumption tax-hike bill because the LDP and other opposition parties, namely New Komeito, agreed to support it. The leaders of the three parties also agreed to discuss comprehensive welfare system reform, including public pension systems and healthcare systems for the elderly in a newly established "national council," and to take legislative action to achieve the reforms within a year. The worst-case scenario for the three parties is that they enter the next general election before producing any results that can satisfy their constituencies. A significant political setback would be inevitable if the Japanese public feels that they are just forced to pay more taxes without seeing any policy developments to wipe out a spreading sense of helplessness.

The three pro-tax-hike parties are facing fierce challenges from anti-tax-hike groups inside and outside of the Diet, including Ozawa's new party and Osaka Ishin-no Kai (Osaka Restoration Group) led by the popular mayor of Osaka, Toru Hashimoto. Even today, a majority of the public does not support the consumption tax increase.² In contrast with former prime minister Junichiro Koizumi, who in August 2005 dramatically increased public support for his bill to privatize Japan's postal services, Noda's declaration on the tax hike has not had a substantial impact on public opinion. Therefore, associated reforms of the welfare system are indispensable to the three parties, especially the DPJ and the LDP, if they are to maintain their political positions.

¹ 「決めるべきときに決める、結論を出す、先送りをしない、そういう政治を私はつくり出していきたい」 [Kimeru beki toki ni kimeru, ketsuron wo dasu, sakiokurishinai, sōiū seiji wo watashi wa tsukuridashiteikitai], <http://www.kantei.go.jp/jp/noda/statement/2012/0626kaiken.html>.

² In a Kyodo opinion survey conducted on June 26 and 27, 44.6 percent of respondents showed support for the consumption tax-hike, while 52.9 percent opposed it.

Even LDP lawmakers, who expect another political regime change in their favor in the coming election, would be subject to harsh criticism if structural reforms fail. Though the LDP attacked the DPJ party leadership for trying to reconcile differences between the rebels and supporters of the consumption tax increase, and subsequently declared a loss of confidence in the three-party agreement related to the bill, it is impossible for the opposition to switch its policy on the consumption tax-hike because that would damage its credibility with the public.

In several weeks, both the DPJ and the LDP will have their presidential elections, but this will not cause any changes in the two parties' positions on reform. The new party leaders will have no choice but to support reform. Since Ozawa and his followers left the DPJ, the new party president will have more latitude to lead comprehensive welfare reforms.

A Missing Agenda Item: The Employment System

Japan's employment system should also be on the agenda given the natural connection to pension reform, but thus far it has not received proper attention. Only incremental adjustments, such as increasing the legal retirement age for bureaucrats, have been discussed. But more significant changes in existing rules and traditions, such as seniority-based pay and lifetime employment, are necessary because these are no longer sustainable with large budget deficits and a rapidly graying society. A 10 percent reduction in central government personnel expenditures, which has already taken place, is not a real solution.

Changes in the government employment system in particular must accompany the administrative reforms Noda favors because seniority-based pay and lifetime employment have institutionalized *amakudari* (descent from heaven), a system to secure high-profile positions for retired bureaucrats in private or semi-governmental organizations.

Restructuring the government employment system could potentially serve as a catalyst for employment reform overall, which could increase productivity and opportunities for growth. Inflexible labor laws have impeded private investment. Though Japanese companies have been trying to change human resource management practices, their efforts have produced only nominal effects in the face of the seniority-based pay and lifetime employment systems in place since the postwar period.

TPP and Agricultural Reform

The consumption tax-hike bill also is central to the debate over economic growth because the tax increase is contingent on the growth rate (3 percent nominal and 2 percent real), which the government has tied in large part to trade liberalization.

The DPJ government is arguably the most pro-free trade administration in the history of Japan. Deepening economic partnerships with major countries constitutes the core of the "New Growth Strategy," endorsed by the Kan cabinet in June 2010. The "Basic Policy on Comprehensive Economic Partnership" adopted by the Kan cabinet in November 2010 states that Tokyo "will subject all goods to negotiations for trade liberalization and, through such negotiations, pursue high-level economic partnerships."³ The Noda cabinet expressed this intention to the U.S. government in February 2012 when it consulted on joining negotiations over the Trans-Pacific Partnership (TPP).

Observers in Washington might believe that a huge political deadlock persists inside Japan, but this concern is misplaced because Japan's political direction on TPP is foreseeable. Public opinion polls in major newspapers show that a majority of the Japanese public supports Japan's entry into TPP negotiations, and most of them back measures to encourage structural changes in agribusiness to include larger operations and more corporate involvement.⁴ In addition, the DPJ government has already announced that sustainable agriculture would not be possible in the future because of an aging farming population (averaging 65.8 years old in 2010), difficulty of finding replacement workers, and a low rate of profit.⁵

The government recently advocated large-scale operations for agribusinesses, and its goal by 2017 is for 80 percent of operators to have farmland of 20 to 30 hectares to improve cost competitiveness. Noda did not mention his intention to participate in TPP negotiations when he met with President Barack Obama in April this year, so as not to jeopardize the consumption tax-hike bill, but he might have more latitude after the bill becomes law.

³ Cabinet Decision, "Basic Policy on Comprehensive Economic Partnerships," November 9, 2010, <http://www.kantei.go.jp/foreign/kan/topics/20101109basicpolicyepa.pdf>.

⁴ "Nougyo Saisei, Tsuyoi-Kitai" [Agricultural Revival, Strong Expectations], *Yomiuri Shimbun*, November 20, 2011

⁵ Cabinet Decision, "Basic Policy on Comprehensive Economic Partnerships," November 9, 2010.

Time for Conviction

It could be said that Japanese government ministries have “veto power” over legislation within their own domains. And if you talk to bureaucrats who are not in charge of the labor market or agriculture, they might tell you how difficult it is to challenge the veto power of the ministries in charge. However, once a direction is set by the political leadership, policy implementation can proceed rather smoothly. A good example is the issue of bovine spongiform encephalopathy (BSE), or mad cow disease, and restricted imports of U.S. beef. Noda resolved to address this problem last year and the government has held positive discussions on the issue that could not be solved for years by bureaucrats, and there has been no domestic backlash since. (Public attention to the BSE issue peaked in 2006 when the Japanese government decided to resume imports of U.S. beef, but it has decreased since then and only bureaucrats continue to consider this a political issue.)

Of course, structural changes in the employment system and agribusiness are not easy, but these reforms are indispensable to Japan’s economic future and are possible if the political leadership can overcome bureaucratic hurdles. Fortunately, Noda seems ready to do so. As he noted on June 26: “We should accomplish the integrated reform of the taxation and welfare system, economic recovery, administrative reform, and political reform. All of these issues must be accomplished by April 2014 when the consumption tax rises to 8%.”⁶ In order to succeed, Noda has to mobilize his colleagues in the Diet to confront the challenges of an aging society and the political insecurity they apparently face.

Kiyoaki Aburaki is the U.S. representative for the 21st Century Public Policy Institute and a visiting fellow with the Japan Chair at CSIS.

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⁶ 「一体改革もやる、経済の再生もやる、行革も政治改革もやる、ありとあらゆることを 2014 年の 4 月に消費税率を 8% に引き上げるときまでにやり抜かなければいけない」 Ittai kaikaku mo yaru, keizai no saisei mo yaru, gyōsei mo seijikaikaku mo yaru, aritoarayuru koto wo 2014 nen no shigatsu ni shōhizeiritsu wo 8% ni hikiageru toki made ni yari nukanakerebaikenai, <http://www.kantei.go.jp/jp/noda/statement/2012/0626kaiken.html>.