

EASTASIAFORUM

ECONOMICS, POLITICS AND PUBLIC POLICY IN EAST ASIA AND THE PACIFIC

Vol.6 No.3 July-September 2014 \$9.50

Quarterly



A Japan that can say 'yes'

Adam S. Posen What can we learn from Abenomics?

Masakazu Toyoda Planning an efficient energy future

Yuki Tatsumi Can Japan's security strategy outlive Abe?

Hiroshi Yoshikawa Economic growth never gets old

Tessa Morris-Suzuki East Asian memory wars . . . **and more**

ASIAN REVIEW: SOURABH GUPTA ON CREATING A SEA OF PEACE

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ISSN 1837-5081 (print)
ISSN 1837-509X (online)

From the Editor's desk

After two decades of stagnant growth and the Fukushima triple disaster, Japan appears more confident both domestically and internationally. The economy has been inflated, much-needed social change is being discussed and progress is being made, and international diplomacy is once again active.

Slower growth is to be expected with an ultra modern economy that has a shrinking population. And Japan has continued to contribute to the peace and stability of the region, underpinned by the US alliance and the Article 9 peace clause of its constitution. As the last East Asia Forum Quarterly on Japan in 2012 concluded, if Japan was thought to have had two lost decades since the bubble burst in the early 1990s, perhaps we need to rethink what failure is. Japan is secure, rich and prosperous.

What has changed in the last 18 months is the renewal of Japanese confidence. The economic policy package of Prime Minister Abe—Abenomics—is bold and defines a clear strategy for economic growth. What is still to be seen is whether the difficult reforms necessary for the success of this strategy will be delivered. As many authors in this issue detail, Japan needs to transform how women and foreigners are treated, open up protected sectors to competition and to rethink many of its institutions. The jury is still out and the longer we have to wait for those reforms to be put in place, the larger the risks to the economy from the first two arrows of Abenomics: the printing and spending of money. Signs of weakness are beginning to show in the recovery.

In the international arena confidence manifests itself in Japan's strengthening alliances and its chipping away at Article 9 of the constitution. A real test for Abe and Japan moving forward will be managing the relationship with China, which has until now been dismal.

Despite anxieties over whether the economy and society can live up to these new ambitions and the changes to Japan's security posture and place in the world, there is more evidence here of a Japan that can say 'yes'.

Shiro Armstrong
Australia-Japan Research Centre

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Why 'womenomics' is the way forward



ADAM S. POSEN

ONE OF the striking things about the past few decades of Japan's economic history has been the fact that textbook macroeconomics could have predicted most of it. Back in the late 1990s, this was a controversial point of view. Many people spoke about the 'specialness' of the Japanese economy, just as they have about the 'specialness' of recent monetary policy. This over-complication seems unnecessary. In the political economy of reform, as in macroeconomics, we can learn a lot from the Japanese experience.

The first lesson is that policy change is always possible, but ambition is required. In Japan, since the bubble, there have been periods of policy

inaction during which leaders too timid to implement reform found thousands of reasons not to do so. Then, every once in a while, along come figures such as Junichiro Koizumi and Heizō Takenaka, or Shinzo Abe and Haruhiko Kuroda. And, with no fundamental change in the party system or the form of government, action is shown to be indeed possible.

Sometimes the excuse for inaction is that only a crisis can provoke fundamental reform. But waiting for a crisis—or worse, trying to provoke one—in order to be able to deal with a social or economic problem is a fundamentally flawed idea. In Japan, there have always been repeated cries to do something about some problem (decline of traditional industries, say,

The sweet taste of success: Prime Minister Shinzo Abe (second from right) and members of Japan's delegation show their jubilation at the announcement that Tokyo will host the 2020 Olympic Games.

or fiscal sustainability) only to hear the response 'we will when there is a crisis.' But the crisis never arrives.

The problem here is that the very definition of 'crisis' is circular. To people with this point of view a 'crisis' is a situation in which you are forced to act; and since they are not forced to act, there's no crisis, and therefore no need to act. But in countries like Japan or the United States, there will never be definitive crises. Smaller, less systemically important nations may indeed experience a definitive

EASTASIAFORUM

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COVER: Ready to fly? This origami crane nestled in a girl's hands seems poised to soar aloft. Picture: Alexander Gatsenko, iStock.

The views expressed are those of the individual authors and do not represent the views of the Crawford School, ANU, EABER, EAF, or the institutions to which the authors are attached.



Published by ANU Press
The Australian National University
Canberra ACT 0200, Australia
Email: anupress@anu.edu.au
Web: <http://press.anu.edu.au>

episode of capital flight or a definitive fiscal crisis. But Japan—like the United States—is, if not too big to fail, then at least too big to fall apart.

Similarly, in democracies with relative price stability, governments with legitimacy and an absence of large-scale political violence, massive populist movements that can force change are very infrequent. Some may have wondered why there were no protests against the Bank of Japan during the country's long stagnation. But the same has happened in the United States: despite the terrible destruction of wealth during the global financial crisis, the Occupy movement hardly had an impact.

Second, in fiscal policy, specifically, there are important lessons to be learned from Japan's policy shift. There used to be a widespread view that fiscal consolidation was difficult and that markets considered this difficulty a major threat to the functioning of economies. Also, it was widely thought that tax cuts were preferable to spending as an instrument of fiscal policy and that monetary and fiscal policy ought to be independent, with monetary policy not accommodating fiscal policy.

But each of these contentions—which have underpinned the dominant policy discussion in the United States, Japan and especially Europe over the past 15 years or so—is wrong.

The problem in most countries that have sustained large fiscal deficits is an unwillingness to raise taxes or an inability to enforce taxes, not runaway public spending. Meanwhile, the major problem in the short term from bad fiscal policy is not that government spending crowds out private investment; the proven is that it crowds out better public investments, or, when consolidation happens, public investment is cut first, whereas public

consumption is not.

Of course, Japan furnishes a cautionary tale: it is possible to have a lot of economically useless public investment, whether on infrastructure or education. But the other side of this coin is that the public and markets need to be more realistic and realise that large government investments take place as part of a portfolio. Not every project will yield a positive return.

In monetary policy, too, Japan's recent experience shows that there is nothing wrong about central banks cooperating with fiscal authorities as long as it is on a voluntary basis. The Euro Group repeatedly misses this point. Japan, on the other hand, has seen very constructive cooperation between the Bank of Japan and the Abe government since January 2013.

THE BIG question now for Japan is the shape that Abe's third arrow will take. There is always room for structural reform and, as I argue, no need to wait for a crisis to enact it. But the third lesson is that there is no platonic ideal of reform to which policymakers can appeal, no laundry list of perfect policy settings that can be applied universally to all countries. Instead, governments must put productivity impact as the criterion for prioritising reforms.

Despite some clamouring for it, corporate tax reform should not be a particularly high priority for the Abe government. There are much more productive structural reforms that can be made first. Of course, there is a justified concern that in Japan the burden of corporate taxes falls primarily on the most competitive companies and not on inefficient small companies. But fixing this problem will not have very big effects on the Japanese economy.

After all, what are the channels through which corporate tax cuts would stimulate growth? They are unlikely to promote corporate investment, since Japanese companies have been sitting on vast piles of cash and have not responded to interest rate incentives to invest it productively. This is increasingly common in companies worldwide but it is entrenched in Japan with its high capital-to-output ratio.

Some say that a tax cut will attract foreign investment. But it's difficult to believe that the biggest impediments to more foreign investment in Japan are corporate tax rates rather than legal, cultural, linguistic and regulatory barriers. Perhaps, some say, corporate tax cuts would help rein back offshoring. But this would be a bad goal for the Japanese government to pursue. Offshoring has been a net source of productivity and growth for Japan. In fact, Japan is falling behind China, which has been actively deepening its supply chains within Asia.

It is a shame to see Abe's reform opportunity wasted in part on worrying about corporate tax rates, just as it is depressing to see that the United States spends an unbelievable amount of time on marginal tax rates rather than tackling education and health reform. In both the US and Japan, health care is abysmally inefficient. If there were proper reform there, then either nation could live for a decade or more off of the attendant boost to economic growth.

SIMILARLY, the returns on tackling the underutilisation of human capital in Japan dwarf the impact of everything else, including the problem of a declining workforce. If Japan were to get more of its university-educated women into the



Contrasting work lives: commuting women file past a smiling model on a Tokyo billboard. Although about 420,000 women have rejoined the Japanese workforce over the past year, that number is a fraction of those who might be available to boost female participation in the labour force.

workforce, the demographic problem would go away for 20 years. If Abe accomplished this, the fatalistic whining about Japan's supposedly intractable demographic crisis would cease to be an excuse or a constraint for its economic future. But the efforts made to date, while encouraging, are insufficient. About 420,000 women have rejoined the workforce over the past year or so. This is an impressive achievement. In absolute terms, though, this is a small fraction of what is possible for female labour force participation.

If Abe focuses his attention on the important structural impediments in the Japanese economy then there

is every reason to believe that the Japanese economy can grow strongly in the future. And, if Abenomics does succeed, then there are plenty of benefits as well as lessons for the rest of the world. [EAFQ](#)

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Immigration: a solution for plummeting population?

JUN SAITO

JAPAN'S declining population is a serious problem. Unless the nation can devise policy strategies either to arrest the decline or deal effectively with its impacts, in the long run Japan will find its path to sustained economic growth blocked.

The most fundamental solution to the problem is to raise the birth rate while allowing mothers to work. The number of child-care facilities needs to be increased, regional child-rearing support systems need to be established and working arrangements reformed to achieve a better balance between work and family. Increasing child allowance to parents is an area which also requires immediate attention.

However, even if Japan were to succeed in raising the birth rate tomorrow, it would be 20 years before any impact on Japan's economic growth were noticed.

One policy option that has received high priority is lifting the employment rate for women. However, lifting the female employment rate is only a medium-term solution to the declining population problem. When the female employment rate has increased to the point where the so-called M-curve (so named because the shape of the curve plotting female participation against age looks like the letter M) disappears, Japan will still need to find alternative means to offset the negative impacts of a declining population. Another option is to lift the employment rate among the aged, but even this is a medium-term solution.

The remaining option is to allow more foreign workers to find employment in Japan, offsetting the negative economic impact of the declining population. There has not been enough discussion of this option in Japan.

Among the various policies on foreign workers, there seems to be a consensus for moving toward accepting more highly skilled foreign professionals. In fields where creativity is critical, the meeting of people with different social and cultural backgrounds stimulates the creation of new ideas, leading to innovation. Prime Minister Shinzo Abe is aware of this important dynamic. It was with it in mind that The *Japan Revitalization Strategy* (or 'Japan is Back' document), announced in June 2013, initiated a revision of the existing point-based preferential immigration treatment system for highly skilled foreign professionals.

POLICIES focussing on unskilled workers, however, are more controversial. There are certainly merits in receiving more unskilled workers. Even if unskilled workers engaging in domestic economic activity produce additional output and contribute to economic growth (of course, if the worker sends a part of his wage home, the contribution to the Japanese GNI will be different from the contribution to GDP). As long as they pay taxes and social security premiums, workers also contribute to the sustainability of the fiscal and social security systems.

On the other hand, accepting unskilled workers would nudge Japan's comparative advantage from capital, knowledge, and technology-intensive goods towards more labour-intensive ones. This would intensify competition with emerging and developing economies, and may make Japan's problems worse.

There are other, more political problems with accepting unskilled workers, too.

As in other countries, there will be fears that foreign workers will take jobs that might otherwise have gone to Japanese citizens. This is a risk for both skilled and unskilled Japanese workers. Many advanced economies have introduced 'labour market testing' which requires that an increase in the intake of foreign workers does not affect the employment of domestic workers, in response to such concerns. However, Japan's declining population implies a shortage of labour so there should be increasingly less competition for work. Furthermore, accepting more unskilled foreign workers should free up domestic workers who have benefited from Japan's advanced education system to engage in more high-value added activities, resulting in an overall positive economic impact.

There are also concerns that increased social tension between foreigners living in Japan and Japanese citizens may result, at least in some cases, in a decrease in public peace and order. It has also been pointed out that local governments would have to increase spending on housing and

Finding a way to resolve the 'comfort women' question

education for foreign workers and their families if the number of foreign workers increases.

But deciding not to accept more foreign workers on the basis of an uncertain increase in crime ignores the potential positive impact of having a more multicultural society. The social and economic impacts of an increased number of foreign workers should be addressed by separate sets of policies. As for the required increase in social

spending by local governments on foreign workers, it could be offset by the additional tax revenue that economic growth brings to the region.

Discussion about these issues is necessary, but action must be swift. Neighbouring countries, such as South Korea, have reformed immigration policy and become more open to receiving foreign workers. Starting with the Act on Foreign Workers Employment in 2003, South Korea has introduced legislation to smooth the way for more foreign workers, and to support the children of international couples.

Japan is behind the pack. Even if reforms are implemented, they may not be enough to attract foreign workers, who may be more inclined to migrate to countries which have been more proactive.

Perhaps the best thing would be for Japan to allow its own youth—who have far more of a stake in these matters than the traditionally powerful older generations—to shape Japan's immigration policy. The choice that faces them is stark: let Japan's economic power wane as its population ages, or open Japan up to immigration so that it can re-emerge as a dynamic economy. **EAFQ**

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KAZUHIKO TOGO

JAPAN'S relations with South Korea have reached a new low. Six issues continue to plague bilateral relations, exacerbating the divide on historical memory: a lack of trust between Japan's Prime Minister, Shinzo Abe, and the Republic of Korea (ROK) President, Park Geun-hye, the 'comfort women' issue, the Takeshima/Dokdo dispute, ROK judicial decisions on forced labour, Japanese politicians' Yasukuni Shrine visits and Japan's moves toward collective self-defence. The 'comfort women' issue may be the most serious bilateral friction point, but it also presents the greatest opportunity for a breakthrough.

Some analysts in Japan argue that problems in Japan's relations with South Korea are structural. The power shift in East Asia, it is argued, has encouraged South Korea to cooperate more closely with China and forgo alignment with Japan as a key power. Japan's internationally weakened position also now allows South Korea to give full expression to its deeply rooted suffering under Japanese colonial rule from 1910–1945. And this has been a convenient tool for generating support and unity in the ROK domestic political arena.

But, given that Japan and South Korea are both economically advanced democracies and allies of the United States, it is in the long-term interest of both countries to improve ties.

Besides, today's deterioration in relations contradicts the close historical ties between the two countries that have existed since the time of Korea's Three Kingdoms and Wa Japan.

There may be some political forces in Japan who rely on 'Korea-hatred' for their sustenance but they are politically marginal.

Among some of Abe's so-called 'nationalist' supporters, the 1993 Kono Statement has been a source of indignation. 'Nationalists' have criticised the Kono Statement for giving the impression that Japanese state officials deported these women by 'physical coercion' to serve at comfort stations. But there are no surviving documents that prove women were subject to 'physically coerced' deportation.

After Abe's visit to Yasukuni Shrine on 26 December 2013, the media speculated that the next 'nationalist' agenda would be to revise the Kono Statement. The United States grew concerned that Japan and South Korea, its two allies in Northeast Asia, would fall out more deeply, with disastrous consequences for security relations. Subsequently, a combination of US pressure and diplomatic contact between Seoul and Tokyo saw Abe, on 14 March, make an important statement in the Diet that 'his cabinet [was] not going to revise the Kono Statement' and that 'his heart [aches] thinking of those who

had gone through indescribable pain, and that feeling is the same as all his predecessors’.

This paved the way for the Obama–Abe–Park trilateral meeting in The Hague on the sidelines of the Nuclear Security Summit in late March and US President Barack Obama’s visits to Tokyo and Seoul in April. But, while taking these decisions towards rapprochement with South Korea, Abe’s cabinet also decided to re-examine the drafting process of the Kono Statement.

It is not entirely clear what Abe’s government wanted to achieve by going back to the process of drafting the statement. But since the decision was presumably made as a political compromise to the Kono Statement deniers in Japan, the purpose should have been to prove something that is useful in defence of the nationalists’ position.

So when the review was issued on 20 June, the ROK Ministry of Foreign Affairs (MOFA) almost instantaneously issued a statement expressing their ‘deep regret’ at the review. The statement stressed that ‘the review by the Japanese government itself runs counter to its pledge to uphold the Statement’. The ROK MOFA also maintained that the Kono Statement is the result of Japan’s ‘own investigation and judgment’ and ‘the ROK government merely expressed its views informally’ after ‘repeated requests from the Japanese side’. International views were not kind to Abe either and as early as 22 June the *New York Times* carried an editorial titled ‘Japan’s historical blinders’. The official mood in Washington concurred that the review was a useless addition to efforts to resolve the issue.

Such criticism is understandable. The review put the ROK MOFA in

PICTURE: AHN YOUNG-JOON / AP PHOTO / AAP



Emotion overcomes Lee Sun-duk at a rally outside the US Embassy in Seoul in July 2007 welcoming a resolution of the US Congress calling on Japan to formally apologise to those forced to work as ‘comfort women’ during World War II.

an awkward position given domestic political dynamics—nuanced positions are politically difficult because any ‘cooperative attitude’ towards Japan is a source of criticism in present-day South Korea.

But the overwhelmingly negative bilateral and international commentary, such as that in the *New York Times* and of the ROK MOFA, that followed after 20 June neglected the content of the report as well as how the review has affected Japan’s domestic positioning of the Kono Statement.

Most importantly, for those who read the review in its entirety, it gives an affirmative impression of the way the Kono Statement was drafted and conveys great respect for the South Korean diplomats who did their best by advising their Japanese counterparts what kind of attitude and language

was most conducive for eventual reconciliation. Those Japanese politicians and diplomats did their best at the time to acknowledge the great pain Japan caused. Their hearings with the comfort women were not made in an environment aimed at ‘legally proving’ their statements but in an atmosphere of listening with sincerity and consideration of the present-day feelings of those who suffered tremendously some 50 years prior.

Advice from the South Korean side was accepted so as to create an effective statement for reconciliation, while leaving no doubt that the ultimate responsibility lay on the Japanese side. Furthermore, on the evening of 20 June this year, Yohei Kono, the original speaker of the Kono Statement and widely considered a progressive within the Liberal Democratic Party, issued another historic statement in which he emphasised that the review ‘does not add or subtract anything’ from the work he did 20 years ago. All these developments stand on Abe’s confirmed statement in March that his cabinet has no intention of revising the content of the statement.

This has given hope that the Abe government may open a window for a breakthrough. Whatever the position of Kono Statement deniers, in the wake of the review there has emerged the unexpected situation that the statement has now found a certain historical legitimacy in Tokyo not only with long-time supporters but also among its long-time ‘nationalist’ deniers. This is an astonishing ‘yes’ that has sprung up in Tokyo in recent times.

It is in Japan’s interest to reach reconciliation on this issue, which emerged in Japan–ROK relations towards the end of the 1980s and has dragged on for more than 25 years.

A Bank of Japan that can say 'yes'

PICTURE: KIMIMASA MAYAMA / EPA / AAP



PAUL SHEARD

In the other countries and regions which suffered severely—namely Taiwan, the Philippines, Indonesia and the Netherlands—the issue has been largely resolved through the activities of the Asian Women's Fund. But with South Korea political resolution has become exceedingly difficult.

It is important to focus on achieving reconciliation while the women who suffered are still alive—only they have the moral authority to give real forgiveness. Abe and his officials need to now work with maximum humility and goodwill, based on the resolute position of the Kono Statement.

A word of caution is required on the magnitude of the task. Cooperation with Abe and his government may be politically risky for Park. Abe and Park will need to move quickly giving consideration to the happiness of those who suffered most. Moves to study and recognise the goodwill of those who worked in and around the Asian Women's Fund will need to be freed from short-term political populism and be considered more broadly from the perspective of South Korea's long-term national interests.

Japan must work to provide an atmosphere conducive to reconciliation, but at the same time South Korea must make its own decision as a nation in a calm and considered way. The past 25 years and more of Japan–ROK exchanges show not just how difficult the comfort women issue is to resolve but also that with a bit of hard work and political commitment the two sides can find reconciliation. **EAFQ**

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UNDER the leadership of Governor Haruhiko Kuroda, the Bank of Japan (BOJ) in March–April 2013 did a 180-degree turnaround: it declared that it had the monetary policy wherewithal to end Japan's chronic, mild deflation and secure a rate of inflation of around 2 per cent and announced bold monetary action to that end. For BOJ-watchers this was revolutionary stuff—and it was coming from establishment Japan.

Depending on the price index used, Japan's economy has been in deflation for 15–20 years. Under the previous BOJ governor, Masaaki Shirakawa, the official line was that the bank could not end deflation using monetary policy. The BOJ argued then that the root cause of deflation in Japan was the steady decline in real potential growth, which was driven largely

Bank of Japan Governor Haruhiko Kuroda: his bold experiment to end deflation will be a valuable lesson for central bank governors whether it succeeds or fails.

by demographic factors and so was not directly amenable to monetary policy cures. When it came to ending deflation, the BOJ's position essentially was one of 'no, we can't, therefore we won't'. Instead, the primary responsibility was held to lie with the government.

This was a remarkable position for a central bank to take. While it was correct to argue that monetary policy could not make much of a dent in real variables like potential growth, it flew in the face of standard economic analysis to argue that monetary policy could not control a monetary or nominal phenomenon, namely the path of the aggregate price level.

Moreover, the BOJ's position was

self-defeating. The central idea in modern monetary theory and practice is that the central bank needs to, and is able to, 'anchor' the public's inflation expectations around its inflation target: central banks control inflation to a significant extent by convincing the public that they can and will meet their inflation target. If the starting point is one of deflation, supported by the public expecting deflation to continue in the future, and the central bank itself tells the public that it does not believe it has the tools to end deflation, then that just serves to entrench deflation even further.

In a remarkable turn of events, Prime Minister Shinzo Abe made holding the BOJ accountable for ending deflation the centrepiece of his economic policy program. To do so he used the once-in-five-years opportunity to appoint a new governor and two deputy governors. With Governor Kuroda at the helm, the BOJ has completely changed its tune and its behaviour. When it comes to ending deflation, the message now is 'yes, we can; yes, we will'.

It is often observed, somewhat stereotypically, that while change can be a long time coming in Japan, when it does occur, it can come very suddenly and dramatically. That begs two questions. First, why, for so long, did the BOJ resist—and why did its political masters allow it to resist—adopting a conventional central bank stance on the deflation issue? And second, why did the Japanese polity suddenly grab the BOJ by the scruff of the neck when it did?

One can only speculate about both questions. The BOJ's resistance, having been dealt a bad hand on deflation by the government's banking and fiscal policy failures of the 1990s, may have been a case of bureaucratic logic and inertia meeting cognitive

dissonance. Lacking the boldness and decisiveness to take the kind of policy action necessary, it may have settled for the more expedient course of redefining the problem and the solution, and as an institution started to believe its own alibi.

But that kind of intransigence had consequences—not least in chronic deflation contributing to Japan's fiscal woes, to dampened 'animal spirits' and to a downbeat national psyche. A confluence of factors likely conspired to wake the Japanese polity from sleep-walking into graceful ageing and declining global relevance, and then to produce a coherent policy mix headlined by a resolve to reflate.

Those factors likely were: a post-global financial crisis fall in real GDP twice the magnitude of that in the US; the fiscal wake-up call from the Eurozone sovereign debt crisis; the game-changing nature of the 3/11 disaster, particularly for business investment prospects in Japan; the continuing rise of China, seemingly impervious to the worst global financial and economic shocks since the Great Depression; yet another round of deflationary yen strength; and a growing sense of 'enough is enough' when it comes to political musical chairs and mediocre leadership.

... theory also suggests that there is some set of monetary policies which, if sustained, would succeed in ending deflation

While the Kuroda-led BOJ may be saying yes to ending deflation, will it succeed? Despite encouraging early progress, the jury is still out. Economic theory suggests that, once deflation is 'soft-wired' into the fabric of an economy (via self-fulfilling expectations and behaviour), it is not easy to expunge.

On the other hand, theory also suggests that there is some set of monetary policies which, if sustained, would succeed in ending deflation.

By a *reductio ad absurdum* argument, the BOJ could surely trigger high inflation if it proceeded to buy up all of the available financial assets in the world—and financed this by 'printing' central bank money (reserves). So there must be some less dramatic set of policy actions that would end deflation and produce just the right amount of inflation—it is just a matter of calibrating policy to find out where that point lies.

But, given generally uncooperative fiscal policy, that deflation-expunging tipping point may require surprisingly aggressive policy, far beyond what the BOJ is currently doing, and Mr Kuroda may be hamstrung by other policy board members, some of whom disagree with his assumptions and framework. If so, the BOJ may come up short. That would be unfortunate and not only for Japan. After all, Mr Kuroda is attempting to be to deflation (too-low inflation) what US Federal Reserve chairman Paul Volcker was to too-high inflation in the 1980s. If Mr Kuroda's 'can do' approach succeeds, he will be creating a valuable precedent for all future central bankers. Much is at stake. **EAFO**

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Planning an efficient energy future

PICTURE: TOMOHIRO OHSUMI / AFP PHOTO / AAP



Staff of Tokyo Electric Power Co (Tepco) examining the No.4 reactor area at the Fukushima Dai-ichi power plant.

MASAKAZU TOYODA

THE Great East Japan Earthquake, the tsunami and the subsequent nuclear power plant accident in Fukushima on 11 March 2011 changed Japan's energy future drastically. The revised Strategic Energy Plan, which the Japanese Cabinet approved in April 2014, outlines a new conceptual framework for Japan's energy policy.

The basic framework of the Strategic Energy Plan encompasses more than earlier plans, as it has expanded the '3Es'—energy security, environment and economic efficiency—to include safety: '3Es plus S'. It is a great pity that 'S' needed to be added to the plan's primary goals, because safety had always been

regarded as a basic premise. But the Fukushima disaster reminded Japan that it is necessary actively to prioritise safety to prevent serious accidents that could cause casualties.

The new emphasis on '3Es plus S' is supported by policy pillars of diversification and resilience.

The plan stresses the need to diversify energy resources. The previous Strategic Energy Plan, drawn up in 2010, attempted to increase Japan's dependence on nuclear energy and renewable energy to up to 50 and 20 per cent, respectively, of total power sources. The plan now seems to minimise dependence on nuclear energy while maximising dependence on renewables. Regrettably, it does not specify numerical goals, which may

hopefully be determined in the very near future. The plan does provide qualitative goals which indicate that nuclear energy will be an important base load power source in the future.

The plan also emphasises the importance of developing a resilient energy supply structure. This will include enhanced cooperation in expanding relations with oil-producing countries as well as East Asian countries.

It is important to create a more open and competitive business environment, permitting newcomers to enter the electricity and gas markets. This change envisages a complete liberalisation of the power market, including spreading region-wide grid management across nine

power companies, liberalising retail markets and unbundling transmission from power generation.

The Strategic Energy Plan seeks to realise a super energy-efficient society by accelerating energy-saving activities, particularly in the household and commercial sectors where energy consumption has continued to increase.

Japan is aiming to improve its self-sufficiency and address climate change, which were already important policies before the 3/11 accident. Self-sufficiency is to be improved by speeding up the commercialisation of unconventional domestic energy sources such as methane hydrate. Addressing climate change requires accelerating technological innovation through initiatives, such as the newly established Innovation for Cool Earth Forum. It will invite many world experts representing research institutions, industries and governments to participate.

There remain several challenges that need to be dealt with before Japan can finalise the design of its energy policy to achieve '3Es plus S'.

First, nuclear power reactors should be restarted one after another, once safety inspections have been completed. Since the 3/11 accident Japan's nuclear safety regulatory scheme has been fundamentally reorganised and improved. The most important change has been the establishment of an independent regulatory commission in September 2012. In July 2013 this commission announced world-class safety standards. And 19 out of the existing 50 reactors had undergone inspections as of 15 July 2014.

The review process took much longer than originally anticipated (around one year) but finally inspections for two reactors in Kyushu

were completed on 16 July. Actually restarting those two reactors may require an additional three months in order to respond to public comments and receive final approval from the local community. Inspections for the remaining 17 reactors should reach completion soon.

The Institute of Energy Economics, Japan, recently published an analysis of the impact of restarting nuclear power stations on the Japanese economy. According to this analysis the most optimistic case would be that 32 reactors are restarted by the end of March 2016. In that scenario, the cost of power generation could drop by 2.3 yen (US\$0.02) per kilowatt hour, a reduction of about 15 per cent of power tariffs for large users. The import cost of fossil fuels would be reduced by about US\$20 billion and carbon dioxide emissions would decrease by about 6.5 per cent. Japan's self-sufficiency ratio would increase by 7 per cent.

ANOTHER interesting outcome of this scenario would be a substantial reduction of liquefied natural gas (LNG) imports (by about 14 million tons) while imports of unconventional LNG could increase to 17 million tons per year after 2017. The return of nuclear reactors combined with the arrival of unconventional LNG would substantially ease the supply and demand situation in Asia.

The second challenge is to obtain the urgently needed numerical goals for the 2030 energy mix. The new Strategic Energy Plan states these goals should be determined as soon as possible so that the appropriate investments can be made. But it might be difficult for the Abe administration to make a decision before March, due to the lack of clear information regarding the restarting

of nuclear reactors, the penetration of renewable energy introduced through feed-in-tariffs and the outcomes of international negotiations on climate change mitigation.

At the Advisory Committee for Natural Resources and Energy, three scenarios regarding the share of nuclear energy in the total power source composition have been discussed: zero, 15 per cent and 20–25 per cent. As a member of this Council, I have been advocating for the 20–25 per cent case—diversification is key. Fossil fuels raise issues about energy security and climate change, renewable energy raises issues about cost and dependence on weather conditions, and nuclear energy certainly raises safety concerns even if world class regulatory systems are in place. No energy is perfect in light of '3Es plus S'. The more diversified the energy sector is, the better it is for the economy.

The details of the new Strategic Energy Plan need to be scrutinised to determine the potential for effective electricity and gas market reform. This is easier said than done. There are still many problems with market reform in the UK, the US and other advanced economies. The typical problems associated with relying on market mechanisms are a shortage of investment and an inappropriate energy mix—particularly with respect to addressing Japan's carbon emissions.

The challenges of safely using nuclear energy, accomplishing an appropriate energy mix and wisely designing utility market reform are common to all countries in the world. I hope that Japan can work towards the best model through ongoing experiments in energy supply and use.

EAFQ

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Remembrance, reconciliation and East Asian memory wars

TESSA MORRIS-SUZUKI

THE past, as William Faulkner once wrote, 'is not dead, it isn't even past'. Nowhere is this more true than in today's East Asia. The recent 'memory wars' between the countries of the region—particularly (though not exclusively) between Japan and its neighbours China and Korea—are eloquent testimony to the power of the past to haunt the present and influence the course of domestic and international politics.

As Cold War tensions in East Asia diminished from the 1980s onwards and as the events of the Asia-Pacific War receded, it might

have been assumed that memories of war and colonialism would also fade. Instead, the opposite has happened. Unresolved issues of historical justice and restitution have smouldered and, fanned by the winds of rising nationalisms, emerged as sparks which threaten to ignite new regional antagonisms.

In the past two years particularly, the governments of the region have staged a series of contending political performances to enshrine or to erase the memory of particular historical events, particularly events associated with Japan's early 20th century imperial expansion and the Asia-Pacific war. The December 2013 visit

by Japan's Prime Minister Shinzo Abe to Yasukuni Shrine—the Shinto shrine to the war dead in which executed war criminals are also venerated—evoked fierce criticisms from Korea and China.

These criticisms were amplified in mid-2014, when the Japanese government appointed a committee to re-examine the process that led to the issuing of the 1993 Kono Declaration, which is the Japanese government's most significant apology to women from Korea and elsewhere coerced into military brothels during the war. The committee's report is widely perceived as having undermined public confidence in the declaration



African and Asian women leaders outside the Japanese embassy in Seoul in January 2014. A rally supporting 'comfort women' is held each Wednesday.

PICTURE: YONHAP / EPA / AAP

and undone much of the good achieved by the 1993 apology.

Meanwhile, in January 2014 a new museum was opened inside a railway station in the Chinese city of Harbin, the site of the assassination in October 1909 of Japanese elder statesman and former resident-general of Korea Ito Hirobumi. The memorial, proposed during the meeting of the South Korean President, Park Geun-hye, with China's President Xi Jinping in 2013, was greeted with expressions of outrage from the Japanese government and from many sections of the media in Japan, for it honours the memory not of Ito but of his assassin, prominent Korean nationalist Ahn Jung-geun, who was subsequently executed for the crime by the Japanese Kwantung military administration. Japan's Chief Cabinet Secretary, Suga Yoshihide, lodged official objections with the South Korean and Chinese governments, describing Ahn as 'a terrorist who was sentenced to death for killing our country's first prime minister'. The memorial's proponents, on the other hand, retort that Ahn was not a mere assassin but a political idealist and the author of a visionary (though incomplete) plan for peace in East Asia.

But it is perhaps a small incident, little reported in the global media, that most poignantly highlights the destructive, and self-destructive, nature of these conflicts. In 2004, a group of concerned citizens from Japan's Gunma prefecture erected a monument to Korean forced labourers in a local park. The monument commemorates Koreans who were forcibly brought to Japan during the war to work in mines and on construction sites, where many died. It is a simple stone structure, whose inscription includes the words 'remembrance, reflection and

friendship' in Japanese, Korean and English. Memorial ceremonies at this site have brought together Japanese locals and members of the Korean community in Japan in shared acts of commemoration.

The Gunma monument is just one of many small-scale local efforts by Japanese citizens and Korean residents in Japan to inscribe the memory of war in public consciousness and to promote a better shared understanding of wartime history between Japan and its neighbours. Dozens of similar citizens' initiatives have emerged over past decades in a number of local communities from Hokkaido in the north to Kyushu in the south. Japanese academics, publishers, schoolteachers and others have also initiated a wide range of cross-border networks with counterparts in China and South Korea in an effort to create better common understandings of history.


Though these grassroots actions have had relatively little effect on government policy, and have rarely been reported by the media inside or outside Japan, they demonstrate a widespread and sincere popular Japanese recognition of the wrongs of the past and a hope for peaceful relationships with the other peoples of the region.

But now, with the rise in nationalist emotions in Japan and the region more widely, the Gunma memorial has come under attack from a variety

Elsewhere, similar attacks on the work of reconciliation groups are gathering force

of right-wing groups whose members have bombarded the prefectural government with complaints that the monument is 'anti-Japanese'. In July 2014, the prefectural authorities announced that they would not renew the planning permission that allows the Gunma monument to remain in place, forcing the citizens who created this symbol of reconciliation and goodwill to remove it. Elsewhere, similar attacks on the work of reconciliation groups are gathering force.

Reading news reports on the Gunma monument, one wonders how world opinion would react if complaints from German far-right groups led to the destruction of that country's monuments to its forced labourers. The removal of the Gunma memorial, if it goes ahead, will not change the facts of history nor will it make the world forget those facts.

The Japanese authorities, rather than trying to undo the decades of good work that has been done by their own citizens to build bridges to Asian neighbours, should be celebrating and supporting that work. Japan's rich tradition of grassroots reconciliation action has generated a wealth of networks and knowhow that political leaders could use and learn from. The Gunma memorial and others like it should be preserved and embraced as small but precious monuments, not just to the victims of imperial violence and war but also to the goodwill of the many Japanese citizens who long for regional peace, cooperation and understanding. 

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Hard line or soft line? Xi Jinping's diplomatic choices

SATOSHI AMAKO

PRESIDENT Xi Jinping has tackled serious domestic and foreign policy challenges since he assumed the leadership of China in November 2012. He has put great effort into an astonishingly large-scale domestic anti-corruption campaign and has invested diplomatically in enhancing his country's image as a major country and leader in the region.

Xi's mission, emphasised repeatedly after the 18th Communist Party Congress, is realising the 'Chinese dream.' This dream involves a 'great revitalisation of the Chinese race' by building a rich and powerful nation that is prosperous and happy. The party announced that it would promote the noble-minded enterprise of peace, tolerance, international trust, justice and cooperation. Yet, in security and diplomacy, political reports from the 18th Party Congress have emphasised building 'powerful armies in accordance with [China's] status in international society' and that China should resolutely defend its maritime resources and 'build a strong maritime nation.'

This line has led to an extremely delicate balance that Xi must maintain between international cooperation and a hard-line foreign policy. But as long as China's priority is to become a great power, it is expected that strengthening national defences and protecting resources will be prioritised.

Ten years have passed since China



PICTURE: KAZUHIRO NOGI / AFP PHOTO / AAP

Wellwishers greet Xi Jinping, then China's vice-president, at Haneda airport in December 2009. As president, Xi has the responsibility for promoting peace, tolerance and international trust, and at the same time building 'powerful armies' and a 'strong maritime nation'.

became the second-largest economic power in the world, and over this time the country has also rapidly strengthened its military muscle. Following the increase of economic and military power and the heightened self-awareness as a superpower, political leaders, think-tanks, scholars and young people have started to

argue that China's diplomatic strategy *taoguang yanghui* (biding one's time while strengthening oneself) should be abandoned.

China over the past few years has increasingly asserted its 'core interests' in the South China Sea, and is embroiled in territorial disputes with South Korea, Japan, Vietnam,

Malaysia, the Philippines, Brunei and Taiwan.

China's shift from passive diplomacy was first highlighted in its dealings with Japan. China took an extremely hard-line diplomatic stance over the maritime collision in disputed waters near the Senkaku/Diaoyu islands in September 2010. After a Chinese trawler collided with Japanese coast guard patrol boats, China summoned the Japanese ambassador to Beijing six times (and once at midnight). Communication and tourism between the countries was seriously affected, and official meetings were cancelled. Vigorous protests broke out in both China and Japan—and China issued a travel warning for Japan after Chinese tourists were attacked in Fukuoka.

During this time Wang Jisi, Dean of the School of International Studies at Beijing University and one of the top brains at the Ministry of Foreign Affairs, had maintained that *taoguang yanghui* was still valid and that 'things should proceed in a discreet manner'. However, he changed to a more aggressive tone after Japan's nationalisation of the Senkaku/Diaoyu islands in 2012, saying, 'now, the occasion to use *taoguang yanghui* is only limited to when we refer to the attitude toward the US'.

A clearer picture of China's vision for the 21st century international order was put forward by President Xi Jinping at his meeting with President Barack Obama in June 2013. He proposed a special or Group of Two (G2) relationship of superpowers and started to demand that the US recognise their relationship as the only relationship of world superpowers. Obama did not make any comment on this, but China would repeatedly demand it going forward.

At this same meeting between Obama and Xi Jinping, Xi also stated,

'in the Asia Pacific region, there remains broad space that China and the US can share'.

The way that China has treated its relationship with Japan starkly contrasts with its relations with the US. In October 2013 senior Japanese statesmen, including former prime minister Yasuo Fukuda, gathered in Beijing and met Chinese senior officials in order to break the stalemate in the bilateral relationship. In the meeting, Tang Jiaxuan, chairman of the China-Japan Friendship Association (and a former member of the State Council) insisted that 'Japan should clarify whether it stands on the Western world or Asia'. This is in line with comments by hardliner Yan Xuetong—that if Japan defines itself as a Western country there will be fewer 'shared interests'—and is related to the idea of a 'Greater China Zone', which China has been promoting as it extends its influence in economics, politics, culture and the military.

But here there is a paradox. The more China emphasises the 'China model' and the theory of 'China's uniqueness', the more it conflicts with universal, widely accepted concepts in international society. If this is the case, the world will not accept the 'China model' or the theory of 'China's uniqueness' even if China does catch

Former Chinese president Hu Jintao asserted that 'injudicious use of force does not create a beautiful world'

up with the US in an economic and military sense.

China took the same path as other developed nations, of modernisation and industrialisation, by fully leveraging the advantages of being a developing country.

If China accepts reality and agrees to developing the current international order, rather than trying forcefully to create a new international order, international society will welcome it. China itself has expressed the need for such a framework.

Former Chinese president Hu Jintao asserted that 'injudicious use of force does not create a beautiful world'. This statement positions China's path of survival in the current international order. Hu Jintao continued: 'We advocate the spirit of equality, mutual trust, tolerance ... Cooperation and "win-win" mean to advocate the idea that all humans share the same destiny, pay attention to other countries' legal rights while pursuing his/her own country's interests, work together to overcome difficulties, share rights and responsibilities, and increase common benefits'.

This is in line with China's position since the end of the Cold War, emphasising the principle of international collaboration. In this argument, Hu advocates an international strategy in which China should contribute from the universal perspective, not from the perspective of the theory of 'China's uniqueness'.

If China can lead the new international order, accepted and respected by other countries, it would fulfil the first criterion for becoming a true world leader. **EAFO**

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Creating a sea of 'peace, cooperation and friendship'

PICTURE: FREDERIC J. BROWN / AP PHOTO / AAP

SOURABH GUPTA

IN MAY 2008, when Japan–China relations were altogether happier, China's then president Hu Jintao paid a state visit to Japan and inaugurated a 'mutually beneficial relationship based on common strategic interests' with then Japanese prime minister Yasuo Fukuda. In Tokyo, Hu refrained from touching on Japan's wartime aggression in the 1930s and 1940s and praised the peaceful path trodden by post-war Japan—the first time that a Chinese leader had expressed such sentiment in a joint statement.

The two leaders thereafter concluded a far-sighted framework agreement, the Principled Consensus, to jointly develop seabed oil and gas resources in a disputed section of their overlapping exclusive economic zones in the East China Sea. This was to be the first step to transforming these waters into a 'sea of peace, cooperation and friendship'. In May 2010, then-premier Wen and then-prime minister Hatoyama resolved to launch negotiations to implement the Principled Consensus.

Four months later, this goodwill was shattered.

A private Chinese trawler was caught fishing in the territorial waters of the disputed Senkaku/Diaoyu islands and recklessly rammed two Japanese coast guard vessels as they tried to enforce Tokyo's writ in these waters. Beijing's cautious willingness to jointly manage the political fallout from the incident turned to anger when the government under



Yasuo Fukuda and Hu Jintao, authors of the far-sighted Principled Consensus between China and Japan.

Naoto Kan chose not to deport the Chinese captain and prosecuted him under domestic law. This was a break with precedent. In previous instances of intrusion, such as in 2003 during Junichiro Koizumi's prime ministership, offenders had instead been handed over to immigration bureau officials for prompt deportation. The trawler captain was ultimately deported but was tried under Japanese domestic law in absentia.

Anger turned to fury two years later in September 2012 when the Noda government disregarded Chinese and American concerns and further undermined the status quo on the Senkaku/Diaoyu islands by purchasing—and thereby effectively

nationalising—three of the islands from their private owner. The Chinese coast guard immediately began asserting China's sovereignty in the territorial seas of the Senkaku/Diaoyu islands and intermittently continues to do so to this day. By late September 2012, Beijing had deposited a chart and list of geographic coordinates with the UN Secretary-General that delineated its territorial sea baselines for the Senkaku/Diaoyu islands.

Soon after, China submitted an extended continental shelf claim, referencing the islands and their baselines, to the UN Commission on the Limits of the Continental Shelf. Finally, in November 2013, it established an air defence

identification zone (ADIZ) over the East China Sea which overlaps Tokyo's ADIZ in the airspace above the Senkaku/Diaoyu islands and beyond. Air defence patrols across the length and breadth of the overlapping portion of the ADIZs, with the exception of the airspace above the Senkakus/Diaoyu islands, have been conducted ever since.

In response to China's assertive policy stance, Japan and the US conducted an unprecedented small-island amphibious assault drill in June 2013 which simulated the recapture of the Senkakus/Diaoyus following a hypothetical Chinese invasion.

The China–Japan action–reaction cycle in these contested waters appears set to continue. Earlier this July, the Abe government granted the Self-Defense Forces (SDF) wider latitude to repel a so-called 'grey zone' infringement—an infringement on the Senkakus/Diaoyu islands that does not amount to a full-blown armed attack. The reinterpretation of Article 9 of the Japanese constitution further allows the SDF to provide logistics support that is 'integrated with the use of force' to the US military in all but the most extreme combat locations. Implementing legislation to give effect to these changes is expected to clear the Diet in the months ahead.

The revised US–Japan Defense Guidelines, which are expected to be released in 2015, will operationally integrate the provision of SDF support to US forces in case of an emergency in the East China Sea. Joint plans to enable the US to assist the SDF in repelling a 'grey zone' infringement are also expected to be finalised.

Clearly, the strategic environment in the East China Sea is at a tense crossroads. A Japan–China maritime communications mechanism that

simply regulates this emerging high-stakes game of naval chicken within formal parameters and fails to address its underlying drivers will succeed neither in reducing tensions nor restoring trust. It could even generate a false sense of assurance that contingencies can be avoided or their fallout satisfactorily managed.

Political pathways to conflict management also appear to be headed towards a dead end. China insists that it will not receive Abe in Beijing until Japan acknowledges that a dispute regarding the Senkaku/Diaoyu islands exists and agrees to a 12 nautical mile no-entry zone around the territory. Abe insists that Japan will make no such concession because there is no issue of territorial sovereignty to be resolved.

To seek a solution based on international law, as Noda's foreign minister fleetingly floated, seems hopelessly unrealistic. Beijing does not currently submit to the compulsory jurisdiction of the International Court of Justice and cannot be summoned to the Hague against its will. For Tokyo, as administrator of the islands, to press a case would be an acknowledgement of the less-than-final status of the Senkaku/Diaoyu islands.

The legal option is also politically risky as neither party has a watertight case. Imperial Japan incorporated the islands by stealth as 'unclaimed

At this juncture it is necessary for both Japan and China to individually practice political restraint and moderation

territory' in the shadow of imperial victory—cognisant that its terra nullius claim was false and wouldn't withstand legal scrutiny. The veil on how the Senkaku/Diaoyu islands were incorporated by Japan was lifted only once the territorial provisions of the San Francisco Treaty came into effect. This reinforced the (false) perception that the Senkaku/Diaoyu islands were not a part of the imperial conquests that Tokyo was duty-bound to relinquish.

Equally, Mao's China was unsure whether final sovereignty over the islands belonged to Okinawa or to Taiwan and might have contemplated compromising on this score at the post-war conference to finalise the peace settlement in the Asia Pacific. In the end, China was not invited to participate at San Francisco. But for almost two decades following the San Francisco Treaty, Beijing failed to lay out a formal claim to the islands.

At this juncture it is necessary for both Japan and China to individually practice political restraint and moderation to avoid further conflict. Both sides must assume important responsibilities so that the prevailing status quo can be maintained.

Beijing must desist from violating the airspace over the Senkakus/Diaoyus as part of its ADIZ patrols over these waters. It should ensure that its coast guard neither conducts boarding operations in the territorial sea of the Senkakus/Diaoyus nor launches helicopters in the islets' proximity. Inflammatory actions at sea—like the instances of training fire-control radar on a Japanese Maritime Self-Defense Force destroyer and helicopter in January 2013—are also incompatible with maintaining the status quo.

Tokyo must maintain its present policy of 'not entering, not researching

and not constructing' on and around the islands for the time being. It should ensure that activities, such as constructing a port of refuge for fishing boats, upgrading the islands' lighthouse or deploying civil servants to manage and preserve the islands' forestry endowment or survey its marine resources, are deferred until Japan–China relations heal. Provocative activities such as stationing Self-Defense Force members around the clock on the Senkaku/Diaoyu islands would also escalate tensions.

Once a period of political quiet in the surrounding waters and in the larger (post-Abe) Sino–Japanese diplomatic relationship takes firmer hold, practical and creative ways of cooperation to achieve win-win outcomes on both sides can be contemplated. Tokyo could acknowledge—without prejudicing its legal claim—that an explicable Chinese claim to the Senkakus/Diaoyus exists and, bearing in mind that the stability of the surrounding area is of mutual concern to both countries, resolve to maintain the existing status quo on the islands indeterminately.

Beijing would express its appreciation for this declaration, resolve not to disturb the status quo or peace and stability in the area surrounding the islands and, to the extent that the status quo remains undisturbed, renounce the use of force to alter the administrative control of the islands. Gradually, China's maritime law enforcement assertions in the territorial sea of the Senkakus/Diaoyus could be withdrawn and the situation would operationally revert to the status quo ante as existed prior to the purchase of the three islands. No scope for joint administration of the Senkaku/Diaoyu islands is likely to be admitted.

... detailed fishing rules in these disputed waters can be consensually arrived upon

Correspondingly, Japan could remain committed to the absolute maintenance of the status quo on the islands, and any and all measures that reinforce its effective control—such as conducting lighthouse repairs, pier and shelter construction, and temporarily deploying personnel on the islands—could be informally vetted in advance with China. With the passage of time, detailed fishing rules in these disputed waters can be consensually arrived upon and negotiations towards a maritime communication mechanism or hotline, as a confidence-building measure, could follow.

The East China Sea has historically been a sea of peace, cooperation and commerce as ideas and goods have regularly crossed its shores. In 2008 the then leaders, Hu and Fukuda, sought to restore the sea and the wider China–Japan relationship—which had been damaged by Koizumi's repeated visits as prime minister to Yasukuni Shrine—to this historical norm. Setting the politically sensitive issue of maritime delimitation in the East China Sea aside, the two leaders agreed to jointly develop the sea's bounty in overlapping zones without prejudice to their respective sovereign rights and jurisdiction claims.

As an indication of the sensitivity surrounding the Senkaku/Diaoyu islands, the seabed area in proximity to the islands was excluded from the agreed list of areas to be jointly developed. The Japanese side resisted

the inclusion of the islands in the framework agreement and China did not deem it prudent to force the issue at a moment of growing warmth in the bilateral relationship.

The current tensions and chill in relations over the Senkakus/Diaoyus have since led to the suspension of negotiations to implement the Principled Consensus. As the Sino–Japanese relationship heals, it is hoped that this joint development agreement will once again be placed on the front burner and realised in full. In time, Beijing and Tokyo should aspire to go a step further. Rather than focusing on the sovereignty dispute itself, Beijing and Tokyo should concentrate on the opportunities arising from the islands' sovereign rights and jurisdiction by jointly prospecting for oil and gas in seabed areas in the islands' vicinity.

The peripheries of empire in pre-modern Asian international relations were loosely institutionalised zones that served both as a limit to expansion from within as well as a belt of contact and commerce with valued neighbours beyond. Often these zones belonged to neither side and both refrained from imposing their occupancy or authority over this semi-governed space. Indefinitely shelving the Senkaku/Diaoyu islands ownership issue, while jointly formulating win-win economic and political arrangements, would be in line with this cooperative spirit that has underwritten peace, prosperity and stability in East Asia for extended periods of time. The East China Sea would be transformed into a 'sea of peace, cooperation and friendship'.

EAFO

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PICTURE: PRAKASH SINGH / AFP PHOTO / AAP

AMITABH MATTOO

WHEN India—newly independent of British rule—opted for constitutional democracy in 1947, few gave it much of a chance. Democracies had thrived where there was a reasonable degree of homogeneity and where the basic needs of citizens had been met. In contrast, India's diversity—linguistic, ethnic, religious and regional—was overwhelming and it was home to some of the world's poorest. But, except for a brief period between 1975 and 1977, Indian democracy has not just thrived but succeeded beyond the expectations of even the most optimistic.

The puzzle of Indian democracy is even more intriguing because other countries within the region (which gained independence from Britain about the same time) and parts of Africa and Latin America which experimented with democracy have had a less fortunate history with the ballot box.

The debate on the survival and success of Indian democracy remains robust. What has been responsible for India's democratic success? Was it wise leadership at birth that was committed to the democratic way? Was it India's comprehensive constitution, in which elaborate checks and balances have prevented a descent into authoritarianism? Was it the policies of affirmative action which allowed social mobility and thus dampened any popular revolutionary zeal? Was it the conservative bureaucracy that ensured that institutional processes not individual whims defined the way India would be governed? Or was democracy, as the Nobel Laureate Amartya Sen would put it, part of a long-standing Indian tradition of debate, dissent and even heterodoxy—almost in the DNA of the



Narendra Modi and the future of Indian politics

Indian Prime Minister Narendra Modi: if his government can deliver its promises, it will make history.

‘argumentative’ Indian?

Whatever the cause, the 16th general election held in April–May this year once again demonstrated the faith of most Indian citizens in democracy, despite its many imperfections.

Voting in India is not compulsory—yet more than 66 per cent of those eligible to vote did so in the world’s largest democratic exercise. The logistics of this massive operation, with 815 million registered voters (more than 100 million of them voting for the first time) were a huge challenge. The Election Commission, an independent statutory authority, deployed 11 million poll and security personnel at 830,000 polling stations. Voting for 543 seats was held on 10 dates across the country using electronic voting machines rather than ballot papers.

For the first time ever, the Bharatiya Janata Party (BJP), seen as a right-wing nationalist party, won an outright majority—282 of the 543 seats in the Lok Sabha, the lower house of parliament. It was also the first time in 30 years that a single political party has won power on its own.

For the three decades after India became independent in 1947 the Congress Party dominated India’s government. Congress was an umbrella party, accommodating diverse interests, but its decline in the late 1980s and 1990s led to a succession of coalition governments. The last five years saw a particularly dysfunctional Congress-led coalition, characterised by policy paralysis and allegations of massive corruption—even though it was led by an honest but weak prime minister.

In contrast, the BJP fought the election on a single issue: the personality and track record of its prime ministerial candidate, Narendra Modi, the three-time elected chief

minister of the prosperous state of Gujarat. Modi spoke at nearly 400 public rallies during the campaign, and at each rally he was treated—as the journalist Swapan Dasgupta put it—like a rock star. A decisive, clear-thinking leader, Modi had a simple message: the magic of the Gujarat model of development under his decade-long administration and how it could be replicated in the rest of India.

He communicated this forcefully to an impatient and, crucially, young India (600 million people under the age of 25) angry with the establishment and the ruling Congress party for letting them down, and looking for hope. In contrast, Congress’s much younger heir apparent, Rahul Gandhi, seemed disconnected, elusive and unable to defend the Congress government, which seemed—at least in the last five years—directionless. As things stand today, the BJP could continue in power well beyond this election, marking the return of a one-party dominated national government.

CASTE has been an abiding feature of Indian politics, particularly in the northern states of Uttar Pradesh and Bihar. Political mobilisation and voting patterns in the past have tended to follow caste loyalties. The 2014 elections changed that: voters from all castes chose the decisive leadership and good governance promised by the BJP.

The BJP, traditionally seen as a party of upper castes, has rarely done well in Bihar and Uttar Pradesh. This time however it won 71 of the 80 parliamentary seats in Uttar Pradesh. Its share of the vote rose 25 percentage points, leaving behind caste-based parties such as the Bahujan Samaj Party, which failed to win a single seat, and the Samajwadi Party, which won

only four. The marginalisation of caste politics is also evident nationally: the BJP won more votes among Dalits (lowest in the caste hierarchy) than the Congress, seen as a champion of lower castes.

In Bihar, the BJP increased its vote share from 22.2 per cent in 2009 to 55 per cent in 2014, winning 22 of the 40 seats and leaving behind caste-based parties like Janata Dal (United), which won two seats, and Rashtriya Janata Dal, which won four. It is too early to conclude that caste will play no further role in Indian politics, but the result does signal that fundamental issues of governance and basic needs are gaining in salience.

Indians, particularly the young, are becoming increasingly impatient with poor governance. This has much to do with the IT revolution, which has ensured access to information is no longer restricted to the privileged. India has the second largest number of mobile phones in the world—more than 800 million. As suggested above, the single most important plank on which Narendra Modi fought this election was his promise to provide good governance, under the slogan ‘minimum government, maximum governance’. He held up Gujarat as an example of how good governance could be delivered, and made the Gujarat model the mantra of his campaign.

While opinions differ about the model’s efficacy, Gujarat ranks consistently highly among Indian states on the available indicators. The Cato Institute’s Economic Freedom of the States of India report places Gujarat number one in economic freedom for the last three years, during which time its lead over other states has widened. Economic freedom does not of course equate to good governance—but the lack of it does

signify poor governance.

A World Bank report, which studied the impact of e-governance in Gujarat, concluded that it had contributed to reducing corruption and increasing state revenues. A London School of Economics study suggested that over the last decade, Gujarat and Maharashtra have been consistent top performers in growth and per capita income.

It is not only Gujarat. Other BJP-ruled states such as Madhya Pradesh under Shivraj Singh Chauhan, Chhattisgarh under Raman Singh and Rajasthan under Vasundhara Raje Scindia are considered far better in terms of governance than Congress-ruled states.

IF THERE was one negative about the election result, it was the lack of adequate representation from Muslims, who constitute more than 13 per cent of India's population. The BJP has traditionally been seen as a pro-Hindu party, part of a family of right-wing organisations known as the Sangh Parivar. Narendra Modi himself has been a Manichean figure, inviting adoration from his supporters and fear among his detractors, particularly within the Muslim population. While in this election Modi seems to have united more than 80 per cent of Hindus (who in turn constitute 85 per cent of the population of India) across caste, linguistic and regional divisions, few among India's Muslims (13 per cent of the population; about 140 million) trust him.

Unfortunately, of the BJP's 282 members of parliament, not one is a Muslim. Of the 80 seats in Uttar Pradesh, about 32 have 15 per cent or more Muslim voters. Yet because of the vagaries of India's first-past-the-post system, for the first time since independence Uttar Pradesh does not

have a Muslim member of parliament.

Even in Bihar, the BJP won 12 of the 17 seats where Muslims number around 15 per cent. In Maharashtra, where Muslims are 14 per cent of the electorate, the BJP and its allies swept the polls, winning 42 of 48 seats. As chief minister of Gujarat and then as a prime ministerial candidate, Narendra Modi could afford to ignore minorities. As the Prime Minister of India he can no longer do so.

One of his first tasks will be to reassure the minorities that they can be safe, secure and successful in Modi's India. The best way to do this is by focusing on the agenda for economic growth and good governance (and the opening up of new opportunities for young people) that has made Gujarat the envy of other states. Modi must pay little heed to the many inside and outside his party who will want him to advance potentially divisive social and political issues.

Those who had expected Modi's foreign policy to take a more muscular stance—the wielding of the conventional big stick—will probably be disappointed. Instead, Modi has emphasised using the carrots of economics and soft power. This suggests a thoughtful understanding of the importance of what the Harvard academic Joseph Nye terms 'smart power': a clever combination of conventional military and economic power and soft power.

The incipient Modi foreign policy doctrine has four main elements. First and most important is the idea that a strong, self-reliant and self-confident India will pursue a foreign policy of enlightened national interest. National interest is a contested term, enlightened national interest even more so. Often national interest is defined as *raison d'état*, or 'reason of state'—viewed as the selfish pursuit of

national ambitions, mostly as defined by the government of the day.

Enlightened national interest adds a moral aspect to the policy. In the early 19th century Alexis de Tocqueville, in *Democracy in America*, described enlightened self-interest as that which made the United States unique: the ability of its citizens to work for the common good because the pursuit of a better life for everyone serves the self-interest of all. In international diplomacy, enlightened national interest is arguably the recognition that the narrow pursuit of self-interest in an interdependent world can lead to suboptimal policy outcomes.

Second is the idea that India will help to build and strengthen a democratic, peaceful, stable and economically interlinked neighbourhood. What was both novel and encouraging at the swearing-in of Modi and his cabinet was the presence of heads of government or senior representatives from all the South Asian countries, which effectively turned the ceremony into a regional celebration of democracy.

THIRD is Modi's emphasis on soft power, explained through yet another Modi alliteration, the 'five Ts': trade, tourism, talent, technology and tradition. Translating this into reality will require real effort.

Fourth, the Modi doctrine moves beyond the former fine distinctions between non-alignment, non-alignment 2.0 and alignment to suggest that India could follow a policy of 'multi-alignment' with all the great powers. This was emphasised in the president's address to the new parliament (reflecting the Modi government's policy) that explicitly stated that the government would work with China to develop a strategic and cooperative partnership; would

work with Japan to build modern infrastructure; would build on the firm foundations of the relationship with Russia; would pursue the relationship with the United States with renewed vigour and would make concerted efforts to achieve progress in key areas with the European Union.

If the government can deliver on the promises made, Modi will make history. If he lets himself be distracted by divisive social issues or is provoked into adopting zealous nationalism, he will prove his critics right. As the election results were announced, I was interviewed by a Chinese radio station. The first question they asked me was whether Modi would be India's Deng Xiaoping. I replied tentatively that it was too early to tell and that, in any case, India was a messy democracy and not an authoritarian state.

However, if Modi does want to be like an Indian Deng, it is worth recalling the great Chinese leader's 24-Character Strategy: 'Observe calmly; secure our position; cope with affairs calmly; hide our capacities and bide our time; be good at maintaining a low profile; and never claim leadership'. In other words, India requires stability within and peace in our neighbourhood and beyond for at least the next decade to emerge with the standing of a great power. During that period it is best not to get dragged into external conflicts, assume leadership or prominence on the international stage, or attract too much attention. That is Modi's biggest challenge. **EAFQ**

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Asia's nutrition time bomb

DON GUNASEKERA
AND
DAVID NEWTH

AN important nutrition and health transition is unfolding alongside Asia's economic transformation. Continuing income growth and changing patterns of food consumption among Asian economies are creating unintended effects on nutrition and health. These developments, if left unmanaged, will have long-term adverse impacts on health care budgets, labour productivity and economic activity.

Economic transformations and rapid income growth in many Asian economies have been accompanied by changes in food consumption patterns and gains in life expectancy, education and living standards. Many consumers in Asia, and particularly those in rapidly growing economies, have gradually shifted away from a predominately starchy staple diet towards one that is rich in fats, meat, dairy products and sugar.

This trend began four to five decades ago in South Korea, Taiwan, Singapore and Hong Kong. It then extended to Malaysia, the Philippines, Indonesia and Thailand and more recently to China and other emerging economies in the region. According to UN Food and Agriculture Organisation (FAO) statistics, Chinese

consumption of vegetable oils, meat and sugar has continued to increase dramatically in recent decades.

It seems that regional and global changes in food consumption patterns are happening at earlier stages of economic transformation than in the past. Countries such as China and other emerging Asian economies have been experiencing changed food consumption patterns considerably sooner and at a much lower level of gross national product (GNP) compared with many developed economies. Moreover, the changes in food consumption patterns appear to be occurring at a faster rate among those in middle- and lower-income groups.

Several factors could account for this: rapid urbanisation, trade liberalisation and market reforms, the rise of intensive farming, rising incomes and greater affordability of food, changes in consumer preferences and attitudes, changes in retail trading and the emergence of supermarket chains, the greater availability of many types of food all year round, increases in the shelf life of food products, and expanded food industry marketing and commercial advertising.

It is important to recognise that, in addition to the factors described above, several other factors influence individual food consumption patterns. These include: biological or genetic

factors that vary among individuals; personal food choices and preferences underpinned by traditions, custom, religion and beliefs; and the increasing participation of women in the workforce. It seems that income is becoming a weaker determinant of diet and nutrition over time. Still, income will remain an important factor influencing changing patterns of food consumption and diet.

In emerging Asian economies, per person food consumption in caloric terms has risen alongside income growth. This has reduced the prevalence of under-nutrition—particularly in comparison with developing regions in Africa and Latin America—and improved child health.

Relatively modest increases in per person consumption of fruits and vegetables and a decline in the consumption of pulses is an important aspect of the shifts in dietary patterns across many rapidly developing countries—including those in Asia. Again, this is in contrast to the continuing substantial increases in per person consumption of fats, meats, dairy and sugar. According to the World Health Organisation (WHO), per person consumption of fruits and vegetables needs to be around 150 kilograms per year for a healthy and balanced diet. But in most Asian countries vegetable and fruit consumption per person is around half what the WHO recommends, with considerable differences across the region and between different socio-economic groups.

Changes in food consumption patterns (and the associated ‘nutrition transition’) are tied up with adverse shifts in dietary patterns, physical activity and human health risks. There are shifts towards more sedentary lifestyles and changing patterns of leisure, such as extensive television

viewing and lengthy engagement in computer games. This transition has sparked an epidemiological transition as infectious diseases are giving way to chronic diseases.

In emerging Asian economies, and across the world, this is seen in the rising prevalence of such nutrition-related non-communicable chronic conditions as obesity, diabetes and cardiovascular diseases.

It is important to recognise that the main contributor to the regional and global burden of disease is still malnutrition. One of the key challenges for governments in emerging Asian economies is to continue resolving under-nutrition while seeking to prevent nutrition-related non-communicable diseases.

The Asia Pacific Cohort Studies Collaboration (APCSC) has estimated that the combined prevalence of overweight and obesity increased by 414 per cent in China—from 3.7 per cent in 1982 to 19 per cent in 2002. According to the Milken Institute in the US, the prevalence of obesity in China in 2010 for ages 15 years and

over was 4.1 per cent for males and 3.6 per cent for females.

The rates of obesity in economies such as China and India are relatively small in comparison with those of developed economies such as the US and Australia, although the absolute number of obese people is much higher due to population size. India currently has the largest population of people living with diabetes, an example of an obesity-related chronic disease.

Domestic policy regimes in developing countries that are focused on economic growth are double-edged. Economic growth helps to reduce poverty and bring down malnutrition rates, resulting in increased life expectancy and future income earning potential. On the other hand, in some instances, it spurs harmful nutrition transitions and related future health risks.

There are several health and economic related implications—for individuals in particular and nations in general—resulting from the growing risks of nutrition-related non-communicable disease conditions. Individuals, living longer than before, are becoming relatively more obese, and hence suffering more chronic diseases. This places additional burdens on health care budgets while reducing labour input to the economy and labour productivity. The highest economic burden will be for treatment in countries, such as Bangladesh, Myanmar, and Pakistan, that today spend less than US\$10 per person on all forms of health care as well as the cost associated with disability and loss of life in future generations.

In Asia some emerging economies’ health systems are facing growing challenges in coping with an ageing population. This is in the context of the rapid transition from infectious to

Individuals, living longer than before, are becoming relatively more obese, and hence suffering more chronic diseases. This places additional burdens on health care budgets . . .



A patient receiving massage treatment at a Shanghai hospital. Although nutrition-related chronic diseases are rising, malnutrition remains a problem in Asia.

chronic diseases on the one hand and nutrition-related chronic conditions—including the growing incidence of childhood obesity and diabetes—on the other.

A host of intellectually challenging and important practical questions require greater attention in addressing the mixed blessings of economic growth. They include: what kind of market and regulatory initiatives are needed to have optimal net impacts on poverty, nutrition and health? How do agricultural policies and food systems affect obesity? How do food prices shape long-term food consumption habits? Should food, nutrition and health sectors work together within a multidisciplinary

framework against obesity? How could this multidisciplinary approach be achieved?

To answer these questions, there is an increasing need for evidence-based multidisciplinary analysis covering economic, health, agriculture and food system sciences. Such analysis could provide insights into what could be done to minimise or prevent some of the adverse nutrition and health-related effects of economic transformations.

Policy actions taken in isolation—whether in food, nutrition or health sectors—are unlikely to achieve the cross-sectoral outcomes that are essential to sustainable economic growth and development. Interactions

between the food, nutrition and health sectors are complex and require more investigation, including the involvement of public and private sectors.

Societal transitions, accompanied by sustained economic transformation, will require governments to avoid the assumption that with higher economic growth other unintended and adverse nutritional and health outcomes will take care of themselves. **EAFQ**

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Creating architecture to sustain spectacular progress

WENDY DOBSON

ECONOMIC institutions, international and national, are key factors in Asian development strategies. Those economies which have exhausted the growth gained from the traditional mobilisation of capital and labour are now reforming the supply-side institutions that encourage new sources of growth from innovation and productivity.

Nobel laureate Douglass North calls institutions the ‘software’ of sustained long-term growth. They include the provision of public goods and setting and enforcing incentive frameworks and the rules of the game. Public rankings such as the World Bank’s *Ease of Doing Business* regularly shed light on institutional differences among nearly 200 countries.

Looking to the future, institutions are of increasing significance for taking up at least three roles: governing efficient global value chains, meeting the challenges of returning G20 growth to its long-term potential, and addressing climate change, the most important collective issue of our time.

Global value chains have become significant drivers of integration, relying on institutions and policies to reduce trade costs, facilitate investment and encourage efficient and competitive services industries. Half a decade after the global financial crisis, G20 output remains below trend, with the International Monetary Fund (IMF), OECD and World Bank stressing the importance of returning

output to its potential, rebalancing growth between surplus and deficit countries and raising long-term potential. Mitigating climate change is at earlier stages.

Within the region governments are cooperating to remove barriers to trade in goods, services and investment flows, and to provide financial oversight. Establishing a secure and predictable environment for investment has gained importance as Asian economies have become significant outward investors.

In the early stages of Asian integration governments relied mainly on global institutions and on unilateral dismantling of border barriers as business opportunities for domestic firms proliferated in nearby markets. Cooperative trade institutions were only created in the early 1990s, when the ASEAN free trade area was negotiated. The free trade area has since become a pillar of the ASEAN Economic Community Blueprint for a single market and production base to be negotiated by 2015. By some estimates full realisation of the single market will increase members’ total GDP by five percentage points if goods, services, capital, investment and skilled labour flow freely among them.

Much progress has been made on removing tariffs on goods and reducing trade costs, but there has been less action to remove restrictions on services trade and investment, achieve mutual recognition of credentials, harmonise standards and

implement infrastructure agreements.

Such cooperation is subject to conflicting pressures. National sovereignty concerns, historical mistrust and unresolved tensions remain close to the surface, while concerns about China’s growing influence are on the rise. Nervous neighbours are accelerating the formation of collective economic and security institutions to engage China as the region’s largest economy, the world’s largest merchandise exporter, holder of the world’s largest stock of foreign exchange reserves and issuer of an internationalising currency, the renminbi. It is also a nation that is increasingly assertive on boundary issues in offshore waters.

A complex network of bilateral free trade agreements now criss-crosses the region. Many were initially intended to be instruments of friendly foreign policy while freeing up gains from trade. Sensitive issues like agriculture were avoided and their contents were often light on services liberalisation. By 2013 governments and ASEAN had completed 76 agreements, with more in the works. Many are complex and difficult for enterprises to understand, particularly with respect to inconsistent rules of origin specifying the amount of value added in a duty-free product that must originate within the trading partners. These weaknesses raise questions about the net benefits to enterprises—which may conclude that paying the tariff is less costly than documenting the origins of a product’s components.

The scope of trade agreements is also changing. Previously sub-regional agreements were confined to reducing tariffs on goods, but these barriers are shrinking in importance in modern agreements, which aim to free up investment flows and services in global value chains. Competition policy, government procurement, technical barriers to trade, investment performance measures and trade remedies are integral to more recent agreements, such as those between ASEAN and Japan, Australia and New Zealand or South Korea with the United States and Singapore. Notably, a trade agreement linking China, South Korea and Japan remains elusive although an investment agreement has been completed.

Consensus is also emerging that the largest gains from trade are to be found in region-wide or trans-Pacific agreements and institutions. ASEAN's Regional Comprehensive Economic Partnership (RCEP) aims to complete negotiations among ASEAN and six other countries by 2015 and intends to harmonise the maze of differing rules of origin for goods, expand trade in services and investment, and promote economic and technical cooperation to narrow development gaps among members—all to be phased in by 2025. It remains to be seen whether such ambitious targets will be met.

It has proved difficult to maintain the commitment to a comprehensive high-quality 21st century agreement among the 12 parties negotiating the Trans-Pacific Partnership (TPP). While members have met the bar for admission—willingness to negotiate such issues as services, investment, competition policy, government procurement and behaviour of state-owned enterprises—the diversity of economic systems and sensitivities about sectors such as agriculture has



The Asian Development Bank's Manila headquarters. In the early stages of Asian integration governments relied mainly on global institutions and on unilateral dismantling of border barriers.

increased the complexity of the talks. Uncertainty about US negotiators obtaining 'fast track' approval authority from Congress has also slowed things down.

A process of competitive liberalisation is under way between the RCEP, which includes China, and the TPP, which does not (yet). Neither negotiation precludes consolidating the two and access to both the Chinese and US markets is the big potential prize for the other players. The most desirable outcome would be US–China cooperation in consolidating the two agreements into APEC's vision for a Free Trade Area of Asia and Pacific. This precedent of multiple pathways could be a catalyst for reform of the global trading system and WTO.

Institutionalising finance began after the 1997–98 Asian financial crisis with the Chiang Mai Initiative (CMI) in 2000 by ASEAN+3 finance ministers and central bank governors. Developing capital market institutions followed with the 2003 Asian Bond

Market Initiative and the Asian Bond Fund that pooled foreign exchange reserves from member central banks to invest in bonds issued by members in their own currencies. Since the 2008 global financial crisis there is wide acceptance of the importance of financial regulation that is sufficiently robust to moderate boom and bust behaviour that damages the real economy.

Pooling the CMI's bilateral swap agreements in the Chiang Mai Initiative Multilateralisation (CMIM) and doubling resources to US\$240 billion in May 2012 have moved things along. Like the IMF, CMIM will provide its members with short-term liquidity or balance of payments support. A potentially significant feature of this institution is the ASEAN+3 Macroeconomic Research Office (AMRO), based in Singapore, which monitors each member's economic performance and provides early warning of potential systemic dangers. Since its founding in 2011,

AMRO has carried out regular peer surveillance. Looking to the future, at least two questions can be asked about CMIM's direction. First, some member governments engage in bilateral currency swaps despite CMIM, raising questions about its credibility. Second, as banks in the region increasingly engage in cross-border transactions, cooperative banking supervision may need to be added to the CMIM mandate to identify and prevent systemic risks.

Renminbi internationalisation and China's plan for capital account opening is the other significant institutional development. Restrictions on such transactions ensured the stability of key domestic prices and insulated China from external shocks during its high growth period, but as the industrial economy becomes more complex, market forces are to play a 'decisive' role. Opening the capital account provides the narrative for a sequence of integrated and comprehensive microeconomic and institutional reforms which China must undertake first. Trade settlement has already been liberalised with investment following, but it is in the interests of both China and its increasingly integrated neighbours that risks of volatile capital flows and exchange rate movements are minimised by delaying the removal of controls on short-term capital flows to the end of the liberalisation process.

Establishing a secure, predictable environment for investment is an essential public good in Asia in light of the major role that foreign investment has played in its development. Moreover, the large current account surpluses of Asian economies are now leading to large-scale investment abroad by sovereign wealth funds, state-owned enterprises (SOEs) and private enterprise. Thus Asia's interests

Establishing a secure, predictable environment for investment is an essential public good

range from institutions that ensure access to foreign assets that might be considered strategic (for example, in resource and technology industries) to protecting the personnel, technology and financial resources of foreign-invested firms.

Companies that invest in Asia seek stronger protection through bilateral or multilateral investment treaties. Global initiatives to create treaties that embody such protection have so far failed, but a dense network of bilateral treaties now connects most major trading countries. China remains the most restrictive of more than 50 countries ranked in the OECD's 2013 FDI Regulatory Restrictiveness Index. China's FDI regime is likely to normalise as the current push to modernise the financial system extends to investment. And, for its partners, the issue of how to respond to investment from China's SOEs is a top priority.

Are Asian institutions creating the necessary public goods to mitigate climate change? The answer is mixed. China is the world's largest emitter of greenhouse gases in absolute terms although it ranks far down the list in per capita terms. Asian nations have dragged their feet on introducing binding emission reduction targets, given the vague commitments of wealthier nations at the United Nations talks. Divisions on climate change policies also exist due to

diverse levels of development.

Yet, with its many islands, long coastlines and high population concentrations in low-lying port cities, Asia is perhaps the region most acutely threatened by climate change. Local demands for cleaner environments at home are pushing governments to act. Many have committed themselves to reducing energy intensity. China is pursuing renewable energy and green technologies. State involvement through industrial policies has attracted complaints of unfair trade from US and EU producers while leading to innovation at home. But Japan and South Korea are leaders in green technology and alternative energy is a significant new growth industry in the region.

'Behind the border' institutions in Asian economies, particularly those that inhibit the efficient use of productive inputs, are under increasing pressure to reform. Pragmatic self-interest is turning the region toward more active policies that raise long-term growth potential and create advantages in global value chains. Finding solutions to regional challenges by liberalising trade and investment and mitigating climate change could become the bases for new global architectures. But continued focus on needed institutional reforms and innovations will also depend critically on those institutions that maintain the peace and political stability that have been the foundation stone for Asia's spectacular progress. 

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Ships of the Japan Maritime Self-Defense Force during a fleet review near Sagami Bay in October 2012.

Then and now: 120 years after the Sino-Japanese war

LIU JIANGYONG

THE year 2014 marks 120 years since the Sino-Japanese War of 1894-1895. While the two nations have enjoyed several decades of peace, there is an uneasy feeling in China that recent developments and revisions to the Japanese constitution draw parallels with the decade prior to 1894.

In that year, under the pretence

of defending their consulate and expatriates, the Japanese government sent troops to the Korean peninsula and invaded China. Four years earlier, in December 1890, the then Japanese prime minister and 'father' of Japanese militarism, Aritomo Yamagata, issued a policy speech claiming that there were two lines to be guarded if Japan wanted to be capable of self-defence. The first was the 'sovereignty line,'

which traced the border of Japan's national territory. The second was the 'interest line', which referred to any area within which the safety of the sovereignty line was intimately related.

The Korean peninsula was of course the first to be regarded as part of the 'interest line' by Japan. Yamagata, an aggressive proponent of this expansionist theory, became commander of the Japanese First Army

in 1894, during the administration of Hirobumi Ito. Under his leadership Japanese troops invaded the Korean peninsula up to Pyongyang before marching straight on to Liaodong, China. After the annexation of the Korean peninsula, with the expansion of its so-called sovereignty line, Japan expanded its 'interest line' towards northeast China. By the same logic, the Japanese military subsequently created the Mukden Incident in 1931 and the Incident of 7 July in 1937, and launched an all-out invasion in China, leading to a legacy of war crimes.

TODAY, nearly 70 years since the Second World War and the retreat of Japanese imperialism, similarities have emerged between Sino-Japanese relations now and the relations in the decade before the outbreak of the war of 1894-1895. Despite strong public opposition in Japan, Prime Minister Shinzo Abe has recently made cabinet resolutions to amend the interpretation of the Japanese constitution to lift the ban on collective self-defence and proceed with amendments to the Self-Defense Forces Law. There have also been discussions with the United States about modifying the Japan-US defence cooperation guidelines and the division of military responsibilities. All of this indicates that Japan has abandoned its 'special defence' policy and is paving the way for joint operations with the military forces of the United States and other close allies.

At this stage the scenarios set by the Abe Cabinet that would permit use of military force include those when nations in close relationships with Japan are under attack and those needed to defend the life and liberty of Japanese people. There is an uneasy feeling in China that this expansion of

Japan's conception of its self-defence marks a return to the 'line of interest' referred to by Yamagata in 1890. The mood is that these seemingly unwarranted excuses and vague assumptions are being made with the Korean peninsula and China in mind.

Japan will not only be looking to continue strengthening its US alliance but will also include countries such as the Philippines and Vietnam among those nations with which it shares a close relationship. These countries have maritime territorial disputes with China, and placing them in this category would allow Japan to provide them with patrol boats and other such support. Furthermore, Japan has been strengthening its ties with NATO—signing a new accord this year to increase cooperation. And Abe, on his latest visit to Australia, announced that the two countries would deepen military cooperation. These seeming attempts to form a wider strategy to contain China mark the first time Japan has acted in this way in nearly 70 years since the end of the Second World War.

The Japanese people are beginning to realise that this revision to the Japanese constitution is a flagrant violation of the conception of peace set down in that document. Rather than protecting the Japanese people, it is setting up a regional military posture which risks the lives of

Japanese soldiers. It is little wonder then that the Abe cabinet's actions will inevitably be strongly opposed by Japan's peace-loving people, and cause vigilance and resistance from its Asian neighbours.

Abe is playing a delicate game of international diplomacy. While expressing his willingness to meet with Chinese leaders, Abe is simultaneously launching a diplomatic battle against China. He has shown no sign of repentance after visiting the Yasukuni Shrine late last year. While claiming that the door is always open for dialogues, he refuses to hold dialogues with China on the territorial issue of the Diaoyu/Senkaku islands. Japan appears to be looking forward to the Sino-Japanese summit in November but in fact refuses any communication when it comes to the most urgent issues to be addressed, such as the Diaoyu/Senkaku dispute. The Japanese side is fully aware that without formal lines of communication it will be nearly impossible for the Sino-Japanese summit to take place.

ONE important motive for Japan behaving in this way is to create the impression that it is China that does not act in accordance with international practice, so enabling it to seize the higher ground of public opinion. Yet no matter how elaborate Abe's plan is, as long as it goes against the current of developing global peace and the will of the Japanese people, it will eventually become a complete failure. One hundred and twenty years since the outbreak of the war of 1894-95, relations between the two countries are as troubling as ever. **EAFQ**

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IN OUR NEXT ISSUE . . .

***The state and
economic
enterprise***

Reconciling security policy with North Asian stability

PICTURE: KYODO / AP / AAP

BEN ASCIONE

On 1 July 2014, the Abe government made a cabinet decision to reinterpret the Article 9 peace clause of Japan's constitution to recognise the exercise of collective self-defence under limited circumstances. While the scope of the proposed changes are an evolution rather than a revolution in Japanese security policy, especially due to the tough negotiations with Abe's coalition partner New Komeito, furore and misconception have surrounded the move.

The cabinet decision addresses four areas. First is the remit for the Self-Defense Forces (SDF) to respond to grey-area infringements short of an armed attack against Japan. Second is narrowing the definition of activities which are banned because they constitute an integral part in the use of force. This would enable the SDF to provide more rear-area logistical support from non-combat zones to 'armed forces of foreign countries engaging in activities for the security of Japan or for the peace and stability of the international community'.

The third area is the loosening of restrictions so that SDF personnel participating in UN peacekeeping operations will be able to use weapons in line with UN rules of engagement. The final area is allowing the SDF to come to the aid of a 'foreign country in a close relationship with Japan' if three conditions are satisfied: the attack threatens the Japanese people's constitutional right to 'life, liberty



Prime Minister Abe paying an official visit to Yasukuni Shrine in December 2013, the first such visit by a Japanese prime minister in seven years.

and pursuit of happiness'; there are no other means to repel the attack; and the use of force is limited 'to the minimum extent necessary'.

So why the backlash, given the limited scope of these changes? The UN Charter declares that collective self-defence is a prerogative of all sovereign states, and the cabinet decision merely seeks to move Japan from a total self-ban to partial recognition of this internationally recognised right. Moreover, the Japanese Diet needs to amend a number of existing laws before the new

interpretation can be implemented.

Abe has long called for formal revision of the constitution to abolish Article 9, but the military allergy—or anti-militarism—in Japan remains strong nearly 70 years after World War II. Defenders of Article 9 promote it as a model for Japan to hold up to the world, challenging the idea that the ability to go to war defines 'normal' state behaviour and confers prestige. They fear that Abe's changes will provoke and entangle Japan in conflict rather than bolster the country's security.

Japanese protesters also distrust Abe's intentions and the ideology he represents. Ignoring popular sentiment, he recently forced through a state secrecy law and relaxed Japan's weapons export ban. Abe also leads or participates in numerous parliamentary study groups with extreme revisionist convictions related to topics including history, patriotic education, the Yasukuni Shrine and the 'comfort women' issue. Abe does not have a broad mandate for change on any of these issues. The majority of the public would prefer him to focus on revitalising the economy.

There are pockets of support in Japan for Abe's moves on security policy. Right-wing nationalists believe that Article 9 besmirches the honour of Japan's imperial past and is a shackle to its just place as a fully sovereign state. But many moderate Japanese defence specialists have welcomed the cabinet decision on the grounds that the country's security policy needs to respond to security challenges in the post-Cold War era.

Some have expressed frustration that the new move is a symbolic rather than a substantial recognition of the right to exercise collective self-defence. By their reckoning more should be done, including expanding the scope of permissible peacetime activities that the SDF can conduct with other nations to allow for enhanced contingency planning and joint military exercises. Legal inconsistencies due to the peculiarities of Japan's positive list system of what functions the SDF may perform also need addressing.

But riding Abe's wave to generate momentum and break through the military allergy and change Japan's security policy has come with unwanted side effects. Japan's relations with China and South Korea have

hit unprecedented post-war lows, and the task of upgrading Japan's security policy has been unnecessarily complicated by Abe's stance on revisiting Japan's history issues.

China and South Korea stress that Abe's historical revisionism means he must not be trusted on collective self-defence. Such pronouncements, including during President Xi Jinping and President Park Geun-hye's joint summit in Seoul in early July, offer an easy opportunity for cheap political point scoring at home. But Abe handed them the issue on a silver platter when he visited Yasukuni Shrine in December 2013, where 14 class-A war criminals are enshrined, and by his government's 're-examination' of the Kono Statement on the treatment of wartime 'comfort women'.

The US, having long called for Japan to take on greater security roles commensurate with its economic capacity, has welcomed the cabinet decision as a positive step to strengthen US-Japan alliance cooperation and increase Japan's contributions to regional peace and stability. America's support should also be understood in the context of President Obama's emphasis on multilateral cooperation and the US 'rebalancing' to Asia.

. . . the Japanese government must not undermine but strengthen official positions . . . which acknowledge wartime transgressions

With this approach to security it is hoped that Japan's exercise of collective self-defence can contribute to alleviating some of the US defence budget pressures after the billions spent on Afghanistan and Iraq, the global financial crisis and the US government shutdown in October 2013. A sense of urgency is involved, as the US and Japan have declared their intent to upgrade their defence cooperation guidelines by the end of the year.

But for Japan to be able to say yes to collective self-defence in a more meaningful way, where it will truly be able to make 'proactive contributions to peace', it has to convince more than its own defence specialists and the United States. China, South Korea and the broader Japanese public also need to be brought on board. The domestic political dynamics in China and South Korea make this a complicated task. But there are a number of measures Japan can take to lay the groundwork.

First, the Japanese government must not undermine but strengthen official positions, such as the Kono Statement and the Murayama Statement, which acknowledge wartime transgressions. This should include a moratorium on Yasukuni Shrine visits by Japanese prime ministers.

Second, Abe's assertion that the door for dialogue is always open must go beyond political rhetoric, and greater efforts must be taken to realise bilateral leaders' summits with China and South Korea. A bilateral meeting with President Xi Jinping while Abe is in Beijing for the APEC Leaders' Meeting in November presents an excellent opportunity to start.

Third, Japanese, Chinese and South Korean leaders must publically acknowledge the mutual importance of the Japan-China and Japan-ROK bilateral relationships. The frame



Riot police keep a cordon around nationalist demonstrators taking part in an anti-Korean march through a street in Tokyo's Shin-Okubo district in May 2013. Prime Minister Abe's efforts to break through Japan's military 'allergy' and change the country's security policy has had unwanted side effects and helped to push relations with China and South Korea to their lowest point in decades.

through which the public in each country perceives the bilateral relationship must be broadened to emphasise areas of cooperation rather than the relentless focus on the territorial disputes and history issues that dominate mainstream media. The Senkaku/Diaoyu islands issue presents a particularly dangerous scenario and greater efforts from both countries are needed to reduce tensions and avoid an accident that could spark conflict. Establishing a military-military hotline to deal with emergencies would be a good first step.

Fourth, Japan's cooperation with China and South Korea should be boosted in areas of mutual

importance, such as the environment and energy efficiency.

Finally, military-level confidence-building among the three Northeast Asian states should be bolstered. The recent announcement of joint military exercises in Australia with China and the US under Exercise Kowari in October shows that such cooperation is possible. Such exercises could be expanded in the future to include Japan and South Korea.

China and South Korea have often interpreted Japan's adherence to Article 9 as a message that the country is a non-actor in security affairs, with the underlying implication being that Japan might still be a

dangerous country were it not for the strict legal barriers and the US cork in the militarist bottle. Japan must emphasise its post-war record as a peaceful nation and demonstrate that it can play a positive and active role in security affairs that can be reconciled with the interests of all regional actors.

EAFQ

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Prime Minister Abe reviewing Self-Defense Forces in October 2013.

Can the National Security Strategy outlive Abe?

YUKI TATSUMI

ON 17 December 2013, Prime Minister Shinzo Abe issued Japan's first National Security Strategy (NSS). The document declares that Japan will make a more 'proactive contribution to peace' based on the principle of international cooperation. It also outlines three basic goals for Japan's national security—ensuring the nation's territorial sovereignty, improving the security environment in the Asia Pacific region by

cooperating with the United States and other regional partners, and active participation in global efforts to maintain international order. While all these goals are admirable, the real question is whether the policy priorities defined by Abe can outlive his term.

During his visit to Washington DC in February 2013, Abe said he believed that Japan should remain a 'first-class nation.' That is, it should belong to a group of nations that shape international rules and norms, and

contribute to the stability of the global security environment. In a sense, the NSS is a document that outlines Abe's perception of what Japan should do to join this group. The quick ascension of China—which has been emboldening Beijing for the last few years—no doubt influences Abe's views. He sees Japan's 'proactive contribution to peace' as critical to countering the rise of China.

The Japanese prime minister's commitment to the principles identified in the NSS predates

its release. Abe has spearheaded important changes in Japanese diplomacy since his cabinet was inaugurated in December 2012. So far he has focused his efforts on strengthening bilateral security cooperation and promoting respect for international norms.

Abe has sought to deepen bilateral security cooperation not only with the United States but also fellow US allies and other key security partners. For example in 2007, during Abe's first term as prime minister, he paved the way for deeper Japan–Australia bilateral security links by signing the Joint Declaration on Security Cooperation. Since December 2012, Japan–Australia security relations have reached a new level of closeness, with the Tokyo 'two-plus-two' meeting (that is, a bilateral ministerial meeting that includes both foreign and defence ministers) in June 2014 followed by Abe's visit to Australia on 8–9 July 2014.

ABE has also demonstrated a clear desire to forge a closer security relationship with India. Although Japan moved to forge a closer relationship with India in 2000, Tokyo's diplomatic outreach to India also accelerated between 2006–2007 when Abe was prime minister for the first time. Strengthening Japan–India relations has enjoyed bipartisan support since then, culminating in the signing of Japan–India Economic Partnership Agreement (EPA) in February 2011. Similar to Japan–Australia relations, Abe clearly intends to pursue qualitative enhancement in this bilateral relations. In 2013, Emperor Akihito and Empress Michiko visited India as state guests in 2013 (Emperor Akihito returned to India for the first time in 53 years), which carries considerable diplomatic

significance. About eight weeks following their visit, Abe himself visited New Delhi in January 2014, when he signed the Joint Declaration for Strategic and Global Partnership.

Southeast Asia and Europe are also included in the diplomatic foray—two regions in which Japan has had enduring foreign policy interests but where it has been unsuccessful in establishing concrete policy initiatives. In regards to Southeast Asia, Abe has become the first Japanese prime minister to have visited all 10 ASEAN member states. He also was the first Japanese prime minister to be invited to deliver the keynote speech at the annual Shangri-La Dialogue in Singapore in May 2014. Among ASEAN members, Abe has placed particular emphasis on reaching out to the Philippines, Vietnam and Myanmar—countries that share Japan's concern about China's increasingly assertive stance on territorial disputes.

In Europe, Abe participated in the North Atlantic Council meeting and NATO meeting in Brussels on 6 May 2014 to articulate why Japan and Europe are 'natural partners'. Leveraging efforts to institutionalise closer ties between Japan and NATO, including the 2010 agreement on securing classified information and related material, Japan convened joint research on humanitarian assistance and disaster relief with NATO. Furthermore, Abe and NATO Secretary General Anders Fogh Rasmussen signed an Individual Partnership and Cooperation Program during his visit to Brussels. Japan has also aggressively pursued security dialogue with NATO member states on a bilateral basis. For example, it held its first 'two-plus-two' meeting with France in January 2014. A Japan–UK 'two-plus-two' meeting is also in the works for later this year.

Also high on Abe's agenda is promoting respect for international norms. Abe has emphasised the importance of an open and free global commons in the sea, air, cyberspace and space. In his first foreign policy speech in January 2013, he discussed the importance of a free and open maritime domain—a consistent theme in most of his major foreign policy speeches, including his keynote address at this year's Shangri-La Dialogue. From Washington to Singapore, to Brussels, to Canberra, the central focus of Abe's speeches has been the preservation of free and open seas, and the necessity of upholding international norms such as freedom of navigation.

ABE is also seeking to revamp Japan's foreign and security policy toolkit. This includes institutional adjustments such as establishing the National Security Council (in November 2013) and legal adjustments such as enacting laws to protect classified information and the recent controversial decision to alter Japan's position on the self-imposed complete prohibition on exercising the right of collective self-defence. Also, his efforts include revising past policies, such as the release of the National Defence Program Guidelines in December 2013 and the recalibration of Japan's arms export controls in April 2014. In addition, the Official Development Assistance Guidelines are to be further revised by the end of the year to create greater room for Japan to provide foreign assistance to help aid recipients to boost their security capacity.

These changes, if implemented fully and consistently by the governments that succeed Abe, will go a long way to putting Japan in a position where it can help to shape the global

and regional security environment. It will allow Japan to have robust partnerships with countries other than the United States (Tokyo's only treaty ally) while continuing to anchor Japan's foreign and security policy to strong ties between Tokyo and Washington.

Abe's efforts have already borne fruit, mainly in broadening the potential for Japan's cooperation on defence equipment with US allies worldwide. Japan's relations with the UK and Australia are most notable in this regard. On 4 July 2013 Japan signed an agreement to jointly develop defence equipment with the UK as well as an agreement to protect classified information. This institutionalised the security relations between Japan and UK based on the defence co-operation memorandum of understanding, which was signed in 2012. Japan and Australia have signed an agreement on joint research in submarine technologies. In Southeast Asia, Japan is already working with Indonesia and the Philippines to transfer Japanese coast guard equipment to help shore up their coast guard capacities.

But momentum is critical to build on these initial successes. As these agreements proceed to the implementation phase, it will be easy for the process to be bogged down by interagency competition as well as domestic resistance. The ultimate success of Japan's multifaceted engagement outlined in the NSS depends on whether Japanese leaders, including Abe himself, can continue to exercise strong leadership.

The policy principles that are laid out in the NSS, while effective, are designed for Japan's peacetime activities. How Japan can expand its participation in activities in times of crisis or post-conflict—whether as a part of peacekeeping forces that are organised under the UN or



Emperor Akihito pays a floral tribute to India's great independence leader during his visit to the Samadhi of Mahatma Gandhi at Rajghat, Delhi, which was part of the royal tour in December 2013. The visit by the emperor and empress added impetus to Japan's intention to pursue closer relations with India.

multinational forces that may or may not have UN mandates—still has not been thought through. While there has been an ongoing debate inside Japan over the right to collective self-defence, discussion about its participation in regional and global collective security frameworks has been absent. This suggests that Japan may still be unable to act promptly in times of crisis.

Japan's strained relationship with South Korea also continues to handicap its efforts to expand cooperation with its fellow US allies. Both Tokyo and Seoul share responsibility in allowing the historical animosity to severely limit areas of practical policy cooperation. Without reconciliation with Seoul, another key US ally in Northeast Asia, Japan's ability to play a robust and visible role in regional and global security issues will continue to be constrained.

Finally, the fact that the current NSS strongly reflects Prime Minister

Abe's own policy outlook may work against the longevity of the document. In principle, the NSS replaced the 1953 Basic Principles of National Defense and is expected to continue to define Japan's national security policy priorities even after Abe departs. But, because it is very clear that the document reflects Abe's own foreign and security policy views, it is just as likely that Abe's successor will decide to revise the NSS to communicate his or her own policy preferences. Whether the policy of 'proactive contribution to peace' will have an enduring impact on Japan's core foreign and security policy principles after Abe remains to be seen. **EAFQ**

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Is this as good as it gets?

TOBIAS HARRIS

AS THE second year of Abenomics progresses, Prime Minister Shinzo Abe's program of coordinated monetary and fiscal stimulus and structural reform has lost some of its lustre. Not only have Abe's approval ratings fallen below 50 per cent for the first time since he took office in December 2012, but a recent poll in the right-wing Sankei Shimbun found that, for the first time, disapproval of Abe's economic policies had exceeded its approval ratings, with 47 per cent opposed and 39 per cent in favour. Coming amid reports of slowing inflation following the consumption tax rate increase in April and weak export data, slumping public support for Abe and Abenomics suggests that the Japanese government's policy experiment could be losing steam.

To the extent that Abenomics depends on Bank of Japan (BOJ) Governor Haruhiko Kuroda's quantitative and qualitative easing program, the experiment is insulated from the vagaries of public opinion. However, from the beginning, the BOJ's radical measures to defeat deflation were only a first step towards a broader revitalisation and transformation of the Japanese economy that would strengthen Japan's global competitiveness and raise its long-term growth potential. Restoring inflation would create the right economic and political environment to implement extensive reforms to the labour market (including increasing the role of women in the workforce) and the inefficient agricultural and service sectors, foster a new system

of corporate governance to generate greater returns for investors, and reshape how the public and private sectors invest in next-generation technologies.

To realise these policy changes, which have in many cases been pursued by Japanese prime ministers for decades, Abe would have to overcome resistance from entrenched interests in the bureaucracy, the ruling Liberal Democratic Party (LDP) and in the economy more broadly, wielding strong public support—and the vote of confidence in Abenomics from foreign investors in the form of buoyant equity markets—as a weapon against defenders of the status quo.

DESPITE his rhetoric, Abe has proven to be a reluctant reformer, unable to translate his political capital into concrete policy outcomes. His 2013 and 2014 growth strategies, the centrepieces of the so-called 'third arrow' of Abenomics, have disappointed, signifying more a return to old-style industrial policy than a dramatic break with past practice. When it comes to difficult structural reforms like labour market reform, the growth strategies have offered only modest changes and do little to introduce more flexibility or reverse the growth of low-paid part-time and other temporary employment.

More significantly, in setting lengthy implementation timelines, the Abe government has allowed bureaucrats, LDP backbenchers and lobbyists to fill in the details of the strategy's skeletal proposals, further watering down the government's reform agenda. With most of the 2014 growth strategy's

legislative items delayed until the 2015 regular session of the Diet, Abe continues to show no great urgency in his pursuit of structural reform.

Why have Abe's achievements thus far lagged behind his promises?

The reasons are numerous. First, structural reform is difficult. Were it easy, one of Abe's reform-minded predecessors would surely have found a way to achieve it. But in practice, structural reform means uprooting economic institutions that have endured since the 1930s, when they were introduced by Japan's militarist government and then were retained by the post-war US occupation.

As the leader of a messy, pluralistic democracy populated by interest groups that have profited from existing institutions, Abe cannot simply change the Japanese economy by decree. Of course, Abe's pursuit of structural reform is further complicated by the fact that his LDP has profited from the status quo more than most. The LDP is at best ambivalent about structural reform and, despite Abe's personal popularity and the broader power shift to the prime minister's office, the party is still capable of undermining the government's agenda, as happened when Abe's regulatory reform council floated a proposal to abolish JA-Zenchu, the national council of agricultural cooperatives. The reform council's trial balloon met with fierce resistance from LDP backbenchers who forced the government to back away from outright abolition and allow JA-Zenchu to participate in the reform process.

Finally, Abe may himself be ambivalent about reform or, at the

EDUCATION RACE

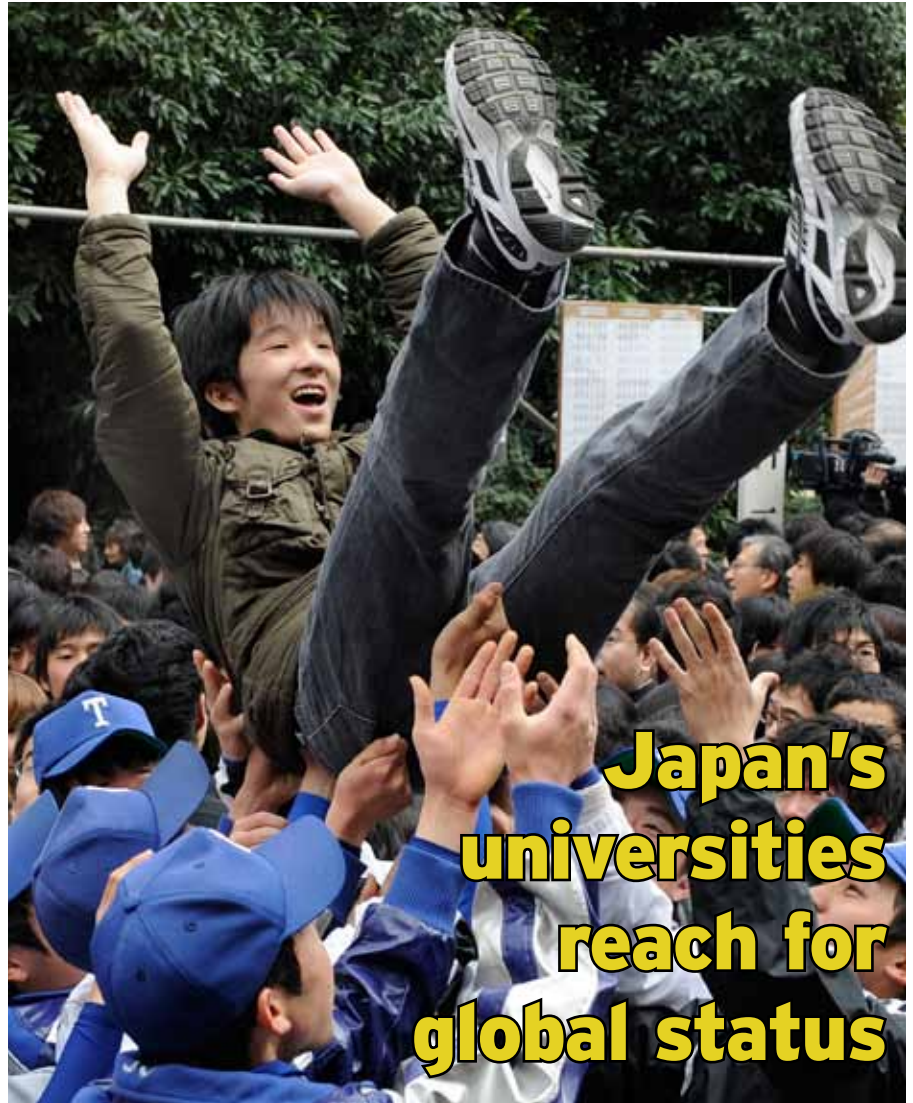
PICTURE: TORU YAMANAKA / AFP PHOTO / AAP

very least, be reluctant to engage in open conflict with members of his own party about structural reform. It is significant that one of Abe's first decisions when he became prime minister for the first time in 2006 was to readmit LDP members who had been expelled in 2005 for opposing the postal system reforms of the then prime minister, Junichiro Koizumi. Abe appears to prefer stability to reform, which may make for durable government but which makes economic transformation less likely.

If Abe's popularity has in fact peaked, it is even less likely that he will be able to deliver the long-term economic revitalisation he has promised. Instead, as his political capital declines—and as his government prepares for local elections in April 2015 and legislative elections sometime in 2016—he may be tempted to pursue politically expedient policies rather than difficult but necessary reforms. This logic may guide the prime minister's decision to devote the forthcoming extraordinary session of the Diet to revitalising uncompetitive rural regions, which could potentially bear fruit in next year's nationwide local elections.

But if Abe shrinks from the challenge of structural reform, it raises an uncomfortable question about whether Japan's economy can be reformed at all. If a prime minister with historically high levels of public support, command of both houses of the Diet and the approval of foreign investors and international organisations cannot prosecute anything more than incremental changes to long-standing economic institutions, can anyone? **EAFQ**

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VERONICA L. TAYLOR

LOOK at any global ranking of universities worldwide and Japan's 'big-name' universities will feature in the top 100. University of Tokyo, for example, ranks well within the top 50 universities in the world for science and technology and sits at number nine among universities in Asia for overall performance in the QS rankings.

But in the Asian rankings, placed well ahead of Japan's top universities, are institutions such as National University of Singapore, Peking

An uplifting moment for a student who has passed the entrance exam to Tokyo University. Japan's elite universities are now competing more vigorously in the international education market and forming partnerships with other leading East Asian institutions.

University and Korea Advanced Institute of Science and Technology, all national champions that are funded generously by home governments and compete vigorously in the globalised market for higher education and university-based research.

In a bid to change this, top-ranked

Japanese universities are now valiantly competing in the global 'education race'. Japanese prime minister Shinzo Abe is reported as saying that 'the number of foreign students at a university will define its success'. Higher education in Japan must open up to global markets because international enrolment revenues will be necessary to support the system into the future.

Twenty five years ago, at the peak of its bubble economy, Japan tried to 'internationalise' higher education. This largely translated into investment in English language programs (often taught by Anglo-American academics) and increased opportunities for students and professors to study abroad.

What didn't change in the 1990s was the basic regulatory framework within which Japan's public and private universities operated: higher education remained, for the most part, a protected domestic market. The premium product within Japanese universities—the degree program—was required to be taught exclusively in Japanese. There were no incentives for faculty to publish outside Japan or in languages other than Japanese. Until recently university rules also prevented foreigners from being hired into regular tenure or tenure-track appointments.

Two trends throughout the '90s and the 2000s posed additional challenges for the system. Demographic change meant that Japan's 778 universities had saturated the market. The rapidly ageing population and shrinking number of university entrants pointed to revenue vulnerabilities. At the same time, students fearful of their job prospects in a shrinking economy became less and less willing to study abroad.

The Abe government is seeking to

solve this dual problem by recruiting increased numbers of foreign students to plug the revenue gap, and revisiting structural and regulatory barriers. The emblematic announcement is that Kyoto University, a top-tier research institution, may open applications for its next university president to external candidates, including foreigners.

The challenge here is significant. The government's original flagship initiative launched in 2009 by the Ministry of Education, Culture, Sports, Science and Technology (MEXT) was the Global 30 program—so called because of its recruitment target of 30 X 10,000 (300,000) foreign students to study at Japan's 13 lead institutions. The results have been mixed, in part due to the effects of the 2011 Tohoku/Fukushima disaster. International student enrolment in Japanese universities sits at about 3 per cent of total enrolments, in comparison with a 7 per cent OECD average. In raw numbers this amounted to about 138,000 international students in Japan in 2012. In countries with more open university sectors, such as Australia, international students make up 22 per cent of total enrolments.

A new, follow-on policy initiative, the Super Global program, was announced in 2013. This program aims to increase educational mobility, foreign-student recruitment and research linkages for 30 Japanese

Deregulatory changes now on the table include degree programs that can be taught entirely in English

institutions.

Deregulatory changes now on the table include degree programs that can be taught entirely in English, permission for joint or dual-degree programs with strategic international partners and the full institutionalisation of non-Japanese faculty. Abe has announced that eight national universities will hire 1500 foreign faculty members over the next three years as replacements for retiring professors. This is a bold initiative, but countries such as China and Canada have much better resourced programs, which are designed to entice high performers from the national diaspora back to home-country universities.

So will 'super' globalisation succeed where the 1990s 'internationalisation' failed?

Current indications are that it might because both institutional postures and fundamental policy settings now align in important ways. This 21st century 'globalisation' is, at its heart, regional integration—while Japanese universities aspire to have top-tier Anglo-American partners, there is a parallel push for deeper linkages with peer institutions in China and Korea. This is evident in the decision by elite universities such as Tokyo, Kyoto, Keio and Waseda to partner with leading East Asian universities.

Among second-tier players, nimble and aggressive private institutions, such as Ritsumeikan, stand out for establishing satellite campuses explicitly to recruit international students from developing Asian nations. Ritsumeikan has also developed mobility programs that give students the opportunity for semester-long linguistic and substantive immersion in China, Korea and Japan.

Underpinning these changes is a second imperative—training cohorts of Japanese and foreign students

Economic growth never gets old

for deployment in Japanese-funded enterprises within Asia. The Japan Business Federation and large Japanese enterprises have a clearly expressed interest in creating a Japan-friendly globalised workforce. Small and medium-sized domestic enterprises that now find themselves either internationally exposed or looking to go abroad also need students with these skills.

A potential brake on this new wave of globalisation is the failure to re-examine the governance of Japanese universities. In the 1990s, foreign faculty were recruited primarily for English language support duties. Ambitious teachers and researchers were dismayed by the underfunded environment, the lack of professional staff, the abundance of administrative 'busy-work' for academics, the lack of gender balance and the absence of professional development opportunities, including a sabbatical system, in many Japanese universities.

Although appraisals of teaching quality are now widely used in Japan, most universities still lack an academic performance evaluation culture. A micro effect of this is that hardworking, talented academic staff in Japanese institutions often carry a faculty or department. In the aggregate, having no incentives for academic research performance makes it difficult to compete effectively in global rankings.

The Super Global program is, arguably, the reform opportunity of the decade. If Japanese universities are more efficient and more attractive than global academic talent is much more likely to follow. **EAFQ**

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HIROSHI YOSHIKAWA

JAPAN'S ageing, shrinking population will cause serious problems for the country throughout the 21st century. Although the fertility rate has recovered to 1.39, this is still very low by international standards. Current official projections estimate that Japan's present population of 120 million will decline to 40 million by 2110. And the proportion of elderly (65 years and older)—now 25 per cent of the population—is expected to rise to 40 per cent by 2060.

But Japan's ageing population is not just a challenge. It is also an opportunity.

Let's start with the challenge. Despite efforts to cut Japan's public deficits, they continue to rise due to the significant cost associated with sustaining the social security system. The debt-to-GDP ratio is now roughly 200 per cent. In contrast, the Maastricht criterion requires EU member countries to have a debt-to-GDP ratio lower than 60 per cent. The Koizumi administration, however, slashed public investment during the 2000s, and it has now fallen to less than half its peak level.

Social security related expenditures are steadily rising. Each year, more than a million people start receiving the public pension and so the government must put more money into that system. The medical cost per person for the aged is five times as high as that for the working population. Again, the government

must put more money into medical insurance, placing serious stress on public deficits. To mitigate this problem, Japan raised its value-added tax rate from 5 per cent to 8 per cent in April this year. It is to be raised from 8 per cent to 10 per cent next year.

Another challenge caused by demographic changes is regional. Many small towns and cities are likely to be unable to overcome the rapid ageing and shrinking of their populations and will simply 'vanish'.

Japan's declining and rapidly ageing population is also a major source of widespread pessimism about the future of the Japanese economy. Pessimism has taken hold of both the supply side and the demand side of the economy. It is widely believed that as the working population (labour supply) shrinks, so does the economy. Although this argument is appealing for its simplicity, the economy is not determined simply by the number of workers alone.

JAPAN'S past record proves this. The Japanese economy grew at 10 per cent per year in real terms during the 1950s and 60s, its rapid growth era. But the average growth rate of the working population during the same period was a mere 1 per cent per year. The difference between the two, namely 9 percentage points, is nothing but an annual increase of labour productivity. It came from the higher endowment of capital per worker—the bulldozer instead of the shovel—and innovations. Though a declining



Generations united by fashion: models young and old wait to strut the catwalk at a grandmother and granddaughter show in Tokyo in 2014. Despite all the perceived problems, dealing with the challenge of ageing can also be a source of innovation.

population is a negative factor for economic growth, its impact is not quantitatively decisive because growth in an advanced economy is mainly growth of income per person.

What about the demand side? Many Japanese business people complain about the shrinking domestic market. So Japanese firms are looking to the growing markets of China, India and beyond. But should they give up on Japan's 'shrinking' domestic market?

If you produce and sell the same product, then your sales may depend tightly on the number of potential buyers, or population. But usually new goods and services command higher value added. That's why an advanced economy grows. In short, the size of the market is not mechanically determined by population.

History tells us that major new

goods and services appear first in the markets of advanced countries rather than in developing countries. This is exactly why we can be optimistic about the future of the Japanese economy.

AGEING, which is not unique to Japan but a global problem, requires widespread changes—ranging from automobiles, medical services, distribution systems and public attitudes to buildings and cities. Ageing is, therefore, a major seed of unbounded innovations.

In this respect, Japan's domestic market has advantages. First, the level of incomes is high enough so that the market can accommodate expensive new goods and services. Second, the size of the market is, crucially, big enough. Luxembourg and Norway, though their income levels are high,

may be disadvantaged by their small markets. Third, Japan remains highly competitive in basic sciences and technologies.

Rapid ageing itself is an advantage; necessity is the mother of invention!

Declining population and rapid ageing are no doubt the big challenges facing Japan in this century. The problems are well recognised even if the solutions are yet to be discovered. Widespread pessimism for the future of the Japanese economy, however, is overstated. Ageing is not only a challenge but also a great opportunity for Japanese firms. They must not forget the importance of the domestic market for innovation. **EAFQ**

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Why 'womenomics' is the way forward

NAOHIRO YASHIRO

WOMENOMICS' is a key pillar of Prime Minister Shinzo Abe's economic growth strategy. In 2013, just 64 per cent of Japanese women aged 15–64 were participating in the labour force—a low rate by OECD standards. As Japan's labour force is already in decline, it is wasteful that women, and particularly those who have a higher education, have been underutilised. To address this, Abe has set a target to increase the ratio of female managers to over 30 per cent by 2020. In response, several large firms have set similar numerical targets.

But some are sceptical. The ratio of female managers (including section chiefs) in Japanese firms was just 11 per cent in 2012, so it will be difficult to triple this figure in eight years. As well, if firms randomly increase the number of female managers regardless of their ability, this may be costly or discouraging to their male counterparts.

Why is raising the percentage of female managers so important for economic growth?

The current one-to-nine ratio between female and male managers indicates a serious misallocation of human resources, given that male and female management abilities do not significantly differ. It is often said that the lack of female managers is not attributable to discrimination on an individual basis, but that there simply are not enough female candidates. But such logic depends on the *nenko jyoretsu* system, whereby seniority

within the firm is largely determined by how long one has worked there rather than merit.

So current employment practices, such as women being de facto forced into temporary or secretarial streams and out of work when they have children, have resulted in significant underutilisation of female human resources.

The extremely low female manager ratio is a result of outdated labour market practices. Seniority-based promotions used to be efficient when the industrial structure was dominated by the manufacturing industry where on-the-job training is essential. This is no longer the case, but the memory of Japan's successful economic past has led to a strong inertia in Japanese firms. The older generation also has a vested interest in maintaining seniority-based wages.

Japanese employment practices are based on the need for multi-skill formation in the firm. Employees are frequently shifted from one job to another in the process of climbing up the occupational ladder to managerial positions. This is accompanied with on-the-job training, which is time consuming and, in

The average length of female employment is shorter than that of their male counterparts,

the case of large firms, often means that an employee must relocate. Most Japanese employees have an implicit employment contract that guarantees long-term employment and seniority-based wages on the condition that employees are subject to the firm's decision on what jobs they will do and where they will work. This employment style is a hangover from the social norm that husbands would earn money while wives would manage the household. Until the end of the 1980s most Japanese families followed this 'social norm'. Today this model is still subsidised by the tax and social security system, which waives the social security contribution of dependent spouses.

Current employment practices are a major obstacle for married women who wish to work full time. 'Full-time work' in Japan does not mean eight hours per day—it requires constant overtime. This practice has been an important means of adjusting down labour inputs during recessions in order to avoid lay-offs. But if both the husband and wife are persistently working overtime, who will take care of the children? In this sense, under current employment practices, there is a trade-off between increasing women's workplace participation and raising birth rates. In addition, when a firm orders either partner to relocate, families have to choose between family separation and one partner quitting their job. In most cases women leave their job.

A major factor behind the extremely low ratio of female managers in



Graduates ready to plunge into the world of work. Labour market reform is critical to letting young women fully use their abilities.

Japan is that it is necessary to stay in a particular firm for a long time to secure a promotion. The average length of female employment is shorter than that of their male counterparts, due mainly to women's disproportional responsibility in the home. Thus if promotions were not based on seniority alone the gender disparity among managers would be smaller.

Whether or not a move away from seniority-based promotions is feasible depends on the type of skills required. If the necessary skills are firm-specific and can be formed only through on-the-job training, age-related promotion is inevitable. But if the necessary skills are general, or will easily become obsolete through information technology

changes, seniority need not matter. Though general skills are becoming more prevalent as information and communication technologies develop, many Japanese firms still find it difficult to change traditional promotion practices.

Thus the easiest way to 'achieve' the target of 30 per cent female managers, and unfortunately what some firms are doing, is to create 'nominal female managers with no authority' while maintaining current employment practices. But the alternative would be better—discarding the current internal promotion system and recruiting qualified managers, either male or female, Japanese or foreign, from both inside or outside of the firm.

Abe's 30 per cent female manager ratio is not a target for its own

sake: it aims to transform Japanese employment practices to a more market-based system. This would entail promoting the principle of the same wage for the same job instead of the seniority based wages; establishing a compensation scheme for professional jobs that is independent of the length of working hours; and developing a tax and social security scheme that does not implicitly support a particular division of labour within the family. These policy targets can only be achieved through structural reform of Japanese labour markets. **EAFO**

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The Australian National University receives Australian Government funding under the 'Enhancing Public Policy Initiative'.
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