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Japan's Economic Weakness: A Security Problem for America

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The Japanese economy shrunk dramatically in the first quarter of 2009, its weakest performance in at least 54 years. Japanese GDP fell at an annualized rate of 15.2 percent, a staggering decline worse than the lowest point of the oil shock of the 1970s or the “lost decade” of the 1990s.¹ Exports have collapsed (at least temporarily), the internal economy remains stagnant, and neither firms nor consumers have any confidence in the strength of the eventual recovery. In an all-too-familiar story, the national government's response has been ineffective and misguided.

Japan's dismal economic performance further constrains American efforts to induce Tokyo to adopt a larger security role. Although it would benefit the U.S.–Japanese alliance if Japan assumed a greater voice and more responsibilities, Tokyo seeks to maximize security and economic benefits while taking minimal action. Tokyo has reduced its defense spending for seven consecutive years, and polls indicate there is little support within the Japanese electorate to alter a comfortable *status quo*. Japan's growing military capabilities should make it a significant alliance partner and a force capable of pursuing global objectives. Instead, Japan has chosen not to translate this capacity into international influence, and now its economic power may be diminishing as well.

The U.S. should encourage economic reform in Japan, continue to press Japan to do more in pursuit of mutual security interests, and hedge toward South Korea in creating a more equitable distribu-

tion of responsibilities as America's principal allies in the Pacific.

Shrink-to-Fit Economics. Calling the 1990s the “lost decade” for the Japanese economy² is a mistake—the loss has extended well beyond the 1990s. The economy is now smaller than it was in the first quarter of 1991, so Japan is actually approaching its *second* lost decade.³ In that timeframe, among other events, China has surged past Japan in GDP adjusted for purchasing power.⁴

Perhaps even more important, there is no prospect of a sustained reversal. Japan's brief period of economic expansion earlier this decade was driven primarily by exports.⁵ That is, Japan had to rely on the strength of foreign economies for its one stretch of expansion over the past 20 years. This is hardly the profile of a great economic power.

To reclaim that mantle, Japan needs efficiency-oriented reform that will create domestic sources of growth. Political paralysis has been such, though, that a third decade of effective economic stagnation seems more likely.⁶ In that case, China will pass Japan in terms of nominal GDP, and any Japanese claim to being the world's second-largest economy will be lost. Further, India will pass Japan in terms

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of GDP adjusted for purchasing power. Already in the 30s in world rankings of *per capita* income, Japan will drop further down the list.⁷

Tokyo has been similarly complacent in altering its security paradigm to meet an increasingly dangerous threat environment. The Japanese executive and legislative leadership have failed to convince the public of the need to redefine the role of the self-defense forces to achieve national objectives—let alone budgeting sufficient resources to do so. Tokyo has subsumed its ability to achieve national strategic objectives to Ministry of Finance guidelines. One might expect an economic payoff from such prioritizing, but the opposite has occurred.

Although there have been evolutionary improvements to the U.S.–Japanese alliance, they have occurred at an insufficient pace to match rapidly escalating Asian and global threats. Even in those instances when Japan has deployed defense forces overseas to respond to international crises, it has done so with overly restrictive rules of engagement that undermine their utility. The most recent example is the Japanese deployment of naval ships to combat Somali pirates, which were far less effective than similar missions by South Korea and China.

The U.S. Policy Response. Throughout the 1980s, the Reagan Administration hounded Japan to engage in internal economic restructuring.⁸ Some of that was purely self-serving—the U.S. wanted to decrease the pressure that imports were exerting on domestic manufacturers. However, the self-interested American claims that Japan needed to reform have proven correct. While the details can legitimately be disputed, the U.S. was right that the Japanese economic model was fundamentally flawed.

Due to apparent Japanese success then, American demands fell on deaf ears. It is possible, however, that American pressure now would be more productive. With Japan no longer much of an economic competitor and the U.S. also grappling with the financial crisis, Tokyo could offer reciprocal proposals with some chance of seeing them accepted by Washington. In any case, the U.S. should push either informally or formally for reforms aimed at reducing Japanese dependence on exports and enhancing efficiency in the domestic economy to offset an aging population. The alternative is an ally who is increasingly enfeebled—even economically.

Japan's fiscal constraints and economic weakness, combined with its passivity and risk-avoidance on security issues, should concern U.S.

1. Yuka Hayashi, "Japan's GDP Shrinks as Consumer Spending Feels the Pinch," *The Wall Street Journal*, May 21, 2009, at <http://online.wsj.com/article/SB124280029530738327.html> (May 21, 2009).
2. As one of many examples, see Fumio Hayashi, "The 1990s in Japan: A Lost Decade," *Journal of Economic Literature*, at <http://www.minneapolisfed.org/research/wp/wp607.pdf> (May 21, 2009).
3. Quarter-to-quarter comparison controls for some variation. Various method changes may mean the Japanese economy could be slightly larger in historical perspective, better described as roughly the same size as it was in the first quarter of 1992. See "Dataset: 1. Gross Domestic Product," OECD, May 22, 2009, at http://stats.oecd.org/wbos/Index.aspx?datasetcode=SNA_TABLE1 (May 22, 2009); "Quarterly Estimates of GDP: January–March 2009," Department of National Accounts, Economic and Social Research Institute, May 2009, at <http://www.esri.cao.go.jp/jp/sna/qe091/jikei1.pdf> (May 21, 2009); Derek Scissors and J. D. Foster, "Two Lost Decades? Why Japan's Economy Is Still Stumbling and How the U.S. Can Stay Upright," Heritage Foundation *WebMemo* No. 2307, February 23, 2009, at <http://www.heritage.org/Research/AsiaandthePacific/wm2307.cfm>.
4. Central Intelligence Agency, "Country Comparisons: GDP," May 14, 2009, at <https://www.cia.gov/library/publications/the-world-factbook/rankorder/2001rank.html> (May 21, 2009).
5. Kazuo Ueda, "Solving Japan's Economic Puzzle," *Far Eastern Economic Review*, May 1, 2009, at <http://www.feer.com/essays/2009/may/solving-japans-economic-puzzle> (May 21, 2009).
6. Bruce Klingner, "Japan's Opposition Buoyed by Leader's Resignation," Heritage Foundation *WebMemo* No. 2444, May 14, 2009, at <http://www.heritage.org/Research/AsiaandthePacific/wm2444.cfm>.
7. Central Intelligence Agency, "Field Listing: GDP," May 14, 2009, at <https://www.cia.gov/library/publications/the-world-factbook/fields/2195.html> (May 21, 2009), "Country Comparisons: GDP (per capita)," May 14, 2009, at <https://www.cia.gov/library/publications/the-world-factbook/rankorder/2004rank.html> (May 22, 2009).
8. Michael Armacost, *Friends or Rivals* (New York: Columbia University Press, 1996).

policymakers beyond the offices of the United States Trade Representative and the Department of the Treasury. The current trajectory of Japan's economic future will increasingly degrade Tokyo's utility as an alliance partner. Tokyo and Washington should understand that there is a cost to Japan's economic indecision and security self-marginalization. Tokyo's unwillingness or inability to make tough decisions risks Japan losing influence and even relevance in a region increasingly dominated by an ascendant China.

The U.S. should strengthen the alliance by:

- Securing greater Japanese commitment to its own defense,
- Emphasizing interoperability to enhance deterrent and warfighting capabilities, and
- Extending the alliance to address international security threats inimical to both the U.S. and Japan.

Yet even as it continues to press Tokyo to adopt a security posture commensurate with its economic and military capabilities, Washington should acknowledge that other allies, particularly South

Korea, are more likely to be a reliable partner. Seoul does not face the same constitutional, legal, and societal constraints to military action as Tokyo does and in the past has provided more extensive and effective military support.

An Unfortunate Scenario. President Barack Obama has called for greater contributions with fewer restrictions from U.S. allies, including Japan. If American allies fail to answer this call, the U.S. will find itself either having to abandon strategic objectives—such as stabilizing Afghanistan—or again having to assume the lion's share of military responsibilities. Tokyo should be aware that, in the latter case, Congress and the American taxpayer will increasingly question the utility and cost of devoting significant military resources to defend Japan rather than diverting them to more immediate requirements. Such a result would present an unfortunate scenario for an economically struggling Japan.

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