

Japan: 'Abenomics' has NOT resigned

Prime Minister Abe's successor is likely to focus on continuity

The LDP will elect a new leader in two weeks who will succeed Shinzo Abe as Japan's prime minister. Continuity is expected in terms of fiscal and monetary policy, but it will not be easy to handle the pandemic, prepare for the Olympics, engage on the global stage, and enact further regulatory reform all while striving to win the hearts and respect of a nation. Even so, candidates willing to face the challenge are already lining up



Source: Håkan Hedström, NHK 2020

“ I cannot be prime minister if I cannot make the best decisions for the people. I have decided to step down from my post ... before accomplishing my goals.

”
PM Shinzo Abe

Had the COVID-19 pandemic not erupted Prime Minister Abe would have been in the global spotlight last month during the Olympic and Paralympic opening and closing

ceremonies. Instead, he was making headlines last Friday by resigning from his post as prime minister due to health reasons, only days after having become Japan's longest serving prime minister. Prior to the start of his second term in 2012, Abe served as prime minister from 2006 to 2007 before having to step down, also due to health reasons.

Abe's public support had faltered recently following a vote-buying scandal involving a former Cabinet member and dissatisfaction

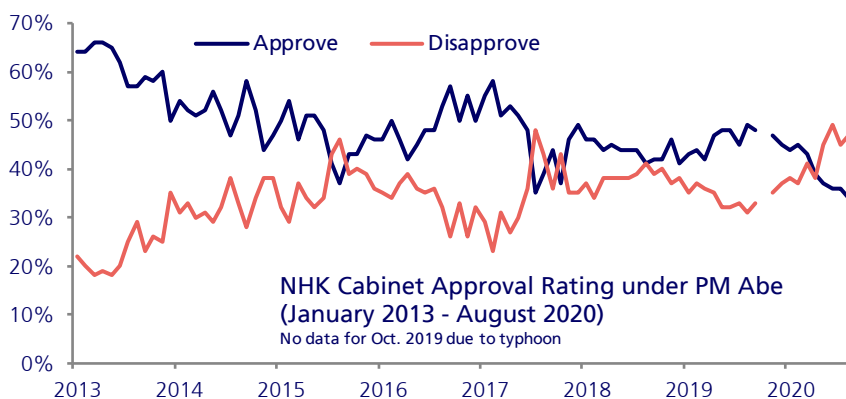
with the government's handling of the COVID-19 crisis. Indeed, the Cabinet's approval rating fell to a record low of 34% in a poll conducted by Japan's major public TV broadcaster NHK (Nippon Hoso Kyokai). 69% of those polled opposed Abe serving as Liberal Democratic Party (LDP) leader for a fourth term. It is also interesting to note that despite falling support for the Cabinet, the overall support rate for the LDP remains far above that of opposition parties. The opposition camp remains highly fragmented, and even though the Constitutional Democratic Party (CDP) and the Democratic Party for the People (DPFP) will merge, both together have a support rate of less than 5% in the latest polls.

Candidates are already lining up

A few high-ranking Liberal Democratic Party members have already announced their intention to stand as new LDP leader candidates and, if selected, prime minister until the term ends in autumn next year.

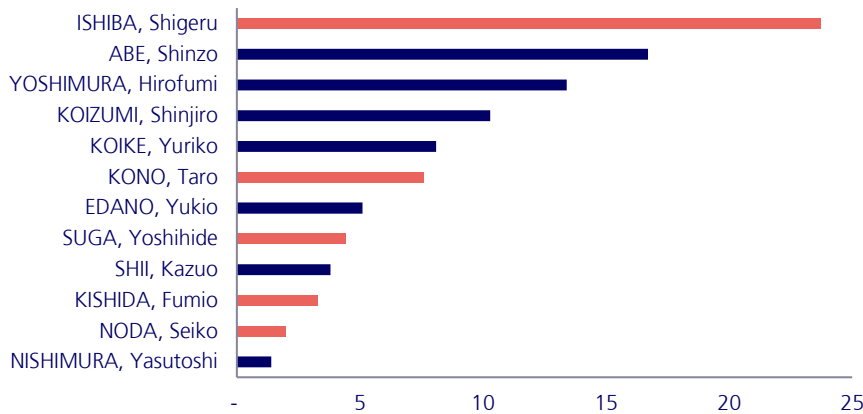
Candidates currently include the former Foreign Minister and faction leader Fumio Kishida and the former Defence Minister and faction leader Shigeru Ishiba, who has been a prior contender for the position of LDP President. It is Chief Cabinet Secretary Yoshihide Suga, however, who currently seems to be the main contender, enjoying PM Abe's support as well as that of three of the

Cabinet approval had been waning prior to PM Abe's resignation



Source: NHK

Politicians preferred as next Prime Minister (in %, June 2020)



Source: www.go2senkyo.com; Note: The salmon colour refers to candidates who are eligible to become LDP President

major LDP factions. Meanwhile, Deputy Prime Minister and faction leader Taro Aso, Economic Revitalisation Minister Yasutoshi Nishimura as well as Defence Minister Taro Kono, who were previously considered to be top candidates, have announced that they will not stand for election. Kono would likely have had better chances if the option of a broader LDP election process had been selected, and he may be a strong contender in future elections. Former Internal Affairs and Communication Minister Seiko Noda, who had announced her candidacy over the weekend, has also withdrawn following the LDP's decision to hold simplified elections.

It is interesting to note that politicians favoured by the public, like Shinjiro Koizumi, the son of former Prime Minister Junichiro Koizumi, Osaka Governor Hirofumi Yoshimura and Tokyo Governor Yuriko Koike, are either not LDP members or are viewed as needing more political experience.

The election date has been set for September 14

396 LDP Diet members from both the Lower and the Upper House are eligible to vote, while the 47 regional LDP leaders will each have three voting rights. This simplified voting format comes into play in case an LDP President steps down before regular elections. The regular, broader voting format would have been comprised of up to 788 votes, which would have benefitted candidates less reliant on inner circle LDP support. It is important to know that candidates need to seek support from the biggest LDP factions, dubbed 'parties within the party'. The LDP comprises seven factions, with only 65 out of 396 members with voting rights not belonging to any faction. PM Abe belongs to the mighty Hosoda faction (97 members). Other strong factions include the Aso faction, the Takeshita faction, the Kishida faction and the Nikai faction. Each of these factions have between 47 and 55 members. While not transparent, negotiations among top representatives of the mighty factions are likely to give some guidance before the vote.

Once the new LDP President has been elected on September 14, a special Diet session will be called to elect the new prime minister, most likely on September 17. After appointing

his cabinet members, the prime minister and his new government will take office. New snap elections for the Lower House cannot be ruled out for later this year as long as opposition parties lag in public polls. The latest NHK poll shows that all opposition parties together achieve an approval rate of only 11.1%. However, it is interesting to note that half of those participants polled have no preference, have not yet made up their mind or do not want to show their preferences.

A look back at 'Abenomics' — success and failure

'Abenomics' (安倍ノミクス) has been the buzzword since Abe was re-elected as Prime Minister in December 2012. Abe's 'three arrows' ignited a stock market boom, catapulting the broad Tokyo Stock Price Index (Topix) up by more than 130% in the following three years, to a good extent driven by foreign buying. The 'three arrows' stood for aggressive monetary policy easing, fiscal consolidation and structural policies to boost Japan's competitiveness and growth perspectives.

In May 2016, PM Abe launched 'Abenomics 2.0'. It outlined the plan for the 'dynamic engagement of all citizens', a collection of 43 long-term demand-side and supply-side initiatives including a nominal GDP target of JPY 600tn by 2021, up 20% from 2015.

Progress was intended to be achieved by increasing female employment in the workforce, bolstering productivity through robotics, drones, artificial intelligence, FinTech, Big Data and automated driving, as well as fostering new developments in fields like environmental research, medicine, tourism and housing. All these measures were designed to increase capital expenditure and to lift productivity. By 2025, the birth rate was expected to rise, helped by such endeavours as improving childcare facilities. Finally, the nursing care infrastructure was to be improved by 2020 in order to prevent workers from having to leave their jobs to take care of ailing elderly family members.

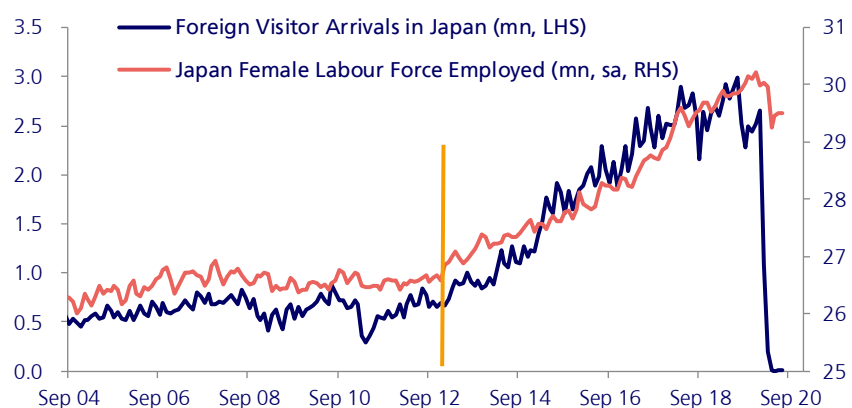
While Abe's aggressive monetary policy easing deserves a high rating in terms of achievement, fiscal consolidation has been moving into focus again since autumn last year, when the consumption tax rate increased from 8% to 10%. More time is needed to tackle structural reform, however, and as such Abe will only receive partial credit for any success.

Foreign tourism and 'womenomics' are considered Abe's core achievements

On the positive side, it is interesting to highlight the boom in inbound tourism that was enabled by relaxing visa rules and providing proper infrastructure. Particularly neighbouring Asian countries made Japan one of their prime foreign sight-seeing and shopping destinations. However, tourism collapsed and effectively came to a standstill once Japan closed its borders following the eruption of the COVID-19 pandemic.

Apart from the surge in inbound travellers, some believe that the focus on 'womenomics', which resulted in continuously increasing female labour participation, has been one of the successful elements of the 'third arrow'. Strong progress has also been made in the field of corporate governance and work-style reforms. The latter refers to regulations that limit overtime work or promote a change in habit like not wearing a tie during the hot summer.

Abe's success in promoting inbound tourism and 'womenomics'



Source: MIC, JNTB, Bloomberg; Note: Yellow line marks the begin of 'Abenomics'

The Topix during PM Abe's second term as prime minister



Source: Bloomberg

PM Abe's geopolitical influence has set the standard, will his successor be able to build on this legacy?

It will be interesting to see how the difficult issue of revising the constitution will be tackled, a prime focus of PM Abe that he had wanted to get resolved before October 2021. The revision of Article 9, a pacifist clause, is controversial both domestically and internationally. Abe's successor will probably act cautiously considering that not only the majority of the electorate, but even the majority of LDP supporters do not favour a revision. On the geopolitical front, it seems likely that Abe's successor will try to keep or rebuild good relations to the US, China and South Korea, while trying to resolve the difficult abductee issue with North Korea. However, a special effort will be required to achieve the same standing that PM Abe has built over the years.

Digitalisation will be a major focus of structural reform

More reforms are needed to increase Japan's productivity, however, which is still far below the OECD average and far away from Ireland and most Scandinavian and Benelux countries, for example. Case in point, less than 10% of Japanese individuals use internet services for administrative purposes compared to more than 70% in Sweden and Iceland, which may also be linked to the fact that the 'hanko' personal stamp is still required to sign official documents. Outdated regulations and procedures have also been hampering the application and disbursement process of COVID related cash handouts. These types of issues have already been picked up on and a boom in automation and teleworking related developments is just starting. Digitalisation is a key theme that will be the major focus going forward, as outlined in 'Basic Policies', an annual report recently updated by Japan's Council on Economic and Fiscal Policy. The report will play an important role in next year's budget negotiations. The gap to other countries is surprising given Japan's leading edge in the technology sector.

'Abenomics' will prevail for now

Even though the political focus of the various candidates for prime minister differ from one another due to their prior careers and political convictions, it is likely that the principle policies set by PM Abe will not be altered, particularly with respect to monetary and fiscal policy. While some of the potential candidates favour fiscal consolidation, it seems likely that fiscal policy will remain accommodative as long as the pandemic is having a severe impact on the economy.

Following two big fiscal packages financed by supplementary budgets, it is likely that even more fiscal support may be in the offing, particularly considering that the so called 'clear water' impact on the economy has been far smaller than the headline number has suggested. It would not be surprising if a third FY20 supplementary budget and an expanded FY21 budget were drafted to support both households and corporates amid the negative consequences of the enduring second wave of the pandemic. There is also rumour of a

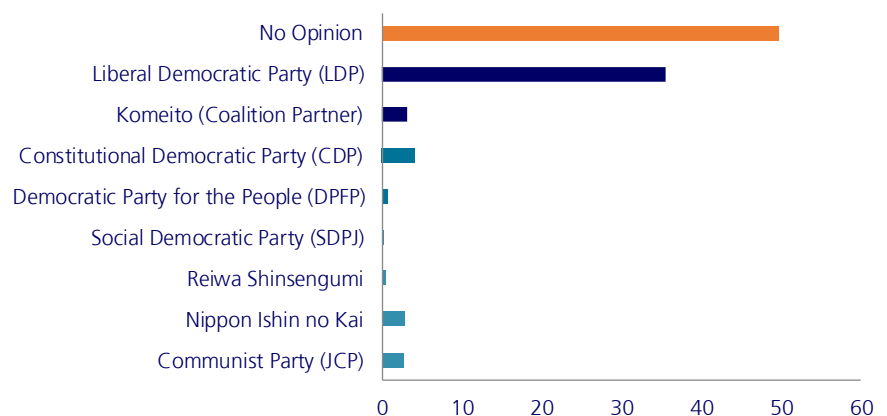
temporary cut of at least 2% to the consumption tax that was hiked from 8% to 10% on October 1 last year, along the lines of the German example. This seems rather unlikely. Instead of a six-month long cut, like in Germany, an option being discussed is a two-year long temporary cut, in order to alleviate the burden caused by the pandemic.

Monetary policy is expected to remain stable

In terms of monetary policy, it seems likely the Bank of Japan will keep monetary policy unchanged as long as Bank of Japan Governor Haruhiko Kuroda, who is considered to be an anchor of monetary stability, maintains his position until his term ends in April 2023. Additional major monetary easing seems unlikely. The status quo may be the most likely scenario, with perhaps the exception of a more flexible use of the ETF buying quota in case of equity market turbulences.

Although deregulation and an emphasis on structural policies are seen as urgent, particularly by foreign investors, they will probably have to wait until the threat of the COVID-19 pandemic has receded and until the end of the current Lower House term in October 2021.

Public Approval Rating by Party (% , August 2020)



Source: NHK

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