Japan in the World
Moving from With-Corona to Post-Corona
January 2021
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The COVID-19 outbreak which originated in China at the end of 2019 has changed the face of the global economy.

In particular, it is thought that economic recovery to pre-COVID-19 levels will be difficult for many developed regions to accomplish in 2021.
On the other hand, while stock markets experienced major adjustments in early March of 2020 when COVID-19 began to spread to developed regions, they actually began to rise from late March as lockdowns and other harsh restrictions on economic activity were put in place in the US and Europe and the economic slump grew severe.

Following that, global share prices stayed strong, and on November 5, the Nikkei Stock Average reached a new high for the year.
Unprecedented Provision of Liquidity and Strategic Shift for Monetary Policies

The impetus for the recovery in global share prices after the crash in early March 2020 was major central banks’ success in staving off a “fire sale” chain reaction by resolving investors’ concern over cash on hand through swift monetary easing and the provision of huge amounts of liquidity.

Furthermore, in August, the US Federal Reserve Board (FRB) announced a strategy shift for monetary policy, displaying a commitment to continued monetary easing to meet inflation targets, even if inflation temporarily exceeds the annual target of 2%.

The FRB’s strategy shift led central banks in other regions to promote monetary easing as well, leading to peace of mind that global low interest rates would be prolonged, and providing force to boost the stock markets.

Source: Bank of Japan, FRB, and ECB materials
Joe Biden overcame incumbent Donald Trump in the November 2020 US presidential election to become the next president-elect. The concurrent congressional elections were also a focus of attention, as people watched to see if the split congress, with different parties holding majorities in the Senate and the House, would be resolved. It is growing more likely that the large-scale economic countermeasures and fiscal mobilization expected by the market will not come to pass.

A failure to increase the scale of fiscal measures or an inability to translate upscaled fiscal measures into accelerated economic growth following the US presidential election is likely to promote a prolongation of monetary easing based on low inflation. Due to this, it is predicted that relatively active risk-taking based on an outlook for prolonged low interest rates will continue in financial markets, and the environment will remain conducive to funds flowing into futures markets for non-ferrous metals and other commodities in addition to stock.
Rapid Rise in Savings Rates Due to Disappearing Demand

Structural changes in economic fundamentals are thought to be having an effect on prolonged low interest rates in developed regions outside the US as well, in addition to any policy changes after the US presidential election or new FRB strategy.

A rise in savings rates has been noticed in developed regions including Japan and the US in recent years, in tandem with the aging of their populations. The COVID-19 pandemic accelerated this trend. This trend in savings rates is the flip side of stagnation in consumption-centric demand, and can be identified as one of the factors behind the low growth and low inflation underpinning prolongation of low interest rates.

Source: Cabinet office, Government of Japan and U.S. Department of Commerce materials
Prolongation of significant global monetary easing in an attempt to break free from low growth and low inflation has been combined with the wide-reaching expansion of fiscal policy to deal with the effects of the pandemic, promoting what is effectively an integration of fiscal and monetary policies in each region.

There are concerns that should a connection be drawn between this integration and a subordination of central banks to fiscal authorities or an implicit loss of political independence, it will bring about a loss of confidence in currency and disrupt global financial markets.
The US dollar grew weaker on an effective basis following the expansion of monetary easing during the COVID-19 pandemic. Based on the large drop in US dollar interest rates, and the prolongation of such rates, this is proof that investors are increasing their risk appetites and shifting their funds from safe dollar-denominated assets to higher risk assets. The Japanese yen, with lower interest rates than the dollar, is not becoming a target of risk-taking investors, so there is little concern of an accelerated strengthening of the yen.

On the other hand, taking into account the risk of reduced confidence in currency in the US due to integration of fiscal and monetary policy, caution is required regarding the possibility that over the long term the dollar may grow even weaker out of anxiety over its status as a key currency.
Another thing that must be anticipated with the birth of the Biden administration is the possibility of change in US policies regarding China. However, there is little chance of a significant shift in economic security policies.

Assuming that the US will not change its tough stance, China is launching a “Dual Circulation Strategy” promoting domestic development and production of advanced technologies and high-tech products.

The Dual Circulation Strategy simultaneously seeks to resolve China’s reliance on foreign demand. It seems that there is now a need for caution regarding the risk that over the long term, China’s massive trade and current surpluses will shrink, along with the money glut that China has provided to the world.
China’s shift toward an inward-looking focus is an important change in direction for the economies of Japan and other developed regions that are facing shrinking domestic demand due to aging populations. Despite China’s own shrinking and aging population, increased difficulty in accessing the economic demand of over 1 billion consumers with rising income levels will be a heavy blow to the economies of developed regions.

Japan and other developed regions should consider the need to lay out visions for post-pandemic economic recovery while launching new growth strategies that do not rely on the giant Chinese market.
As commonly discussed lately, the COVID-19 pandemic is radically transforming our lifestyles, and normalizing a new way of life. At the same time, the current changes to economic and social structure dubbed With-Corona are by no means temporary, and will likely be carried on to the Post-Corona era.

One example of this is the mainstreaming of working from home and remote work. The establishment of new work styles is also changing the face of the labor shortage which grew rapidly through the eight years of the Abe administration on the back of demographic change. Some industries may be gaining the outlook that changes in work styles during the pandemic will lead to a systemic improvement of labor shortage.
A Pressing Need to Address Disparities

Supply-demand and salary levels by industry

The changes in work styles brought about by the COVID-19 pandemic are presenting Japan’s economic and social structures with serious challenges leading up to the Post-Corona age.

In Japan, average salary levels tend to be higher for industries with relatively smaller labor shortages or an ability to quickly shift to other work styles such as working from home, but lower for other industries. The normalization of new work styles leading up to Post-Corona may act as a driver to continued shifting of employment from high-income industries where labor shortages are easy to address, to low-income industries with high labor shortages. If this trend is realized, it may further widen domestic income disparities and intensify social friction.

Source: Ministry of Health, Labour and Welfare, Bank of Japan materials
Economic Growth Supported by Digital Transformation

Decomposition of the potential growth of the Japanese economy

One key to resolving potential structural economic and social issues leading up to the Post-Corona age is digital transformation (DX).

Investment in digitalization should not be perceived merely as a means to streamline work tasks and reduce required labor, rather, using digitalization to both mitigate labor shortages through streamlining of work and achieve higher added value could ultimately boost Japan’s overall productivity while raising employee income levels, and heighten the country’s capability for growth.

Source: Bank of Japan materials
A Focus on the Sustainability of Japanese Corporations

In terms of change leading up to the Post-Corona age, there is one area where Japan and Japanese corporations can exercise an advantage. This area is sustainability.

The traditional stance of Japanese corporations to aim for long-term stable growth in profits, combined with a financial strategy of retaining relatively generous levels of liquidity on hand, has not always been praised by global investors.

However, a heightening interest in sustainability brought about by the COVID-19 pandemic may mean there is room for reconsideration of the advantages of the Japanese style of corporate management.

If challenges leading up to the Post-Corona age, such as the ones stated earlier, can be overcome, there is potential for a dramatic rise in the world’s appraisal of Japanese economy, industry, and corporations.
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