

[報 告]

Keynote Speech by Professor Koichi Hamada  
at the 22nd PBFEM (Pacific Basin Finance,  
Economics, Accounting and Management)  
Conference at Aichi University,  
Nagoya, September 4, 2014\*

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Yasuo Hoshino  
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Cheng-Few Lee  
Motohiko Sato

- Address by Professor Motohiko Sato, President of Aichi University
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- Introduction by Professor Yasuo Hoshino, Co-director of PBFEM Conference, Professor, Aichi University and Professor Emeritus at University of Tsukuba
- Keynote speech by Professor Koichi Hamada, Tuntex Emeritus Professor

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\* We are grateful to Ms Marina Eguchi of the University of Tokyo, for editing the text of Prof. Koichi Hamada.

of Economics, Yale University and Professor Emeritus, University of Tokyo, and Special Advisor to the Prime Minister of Japan, Mr. Shinzo Abe

Professor Kosaka

Good morning, everyone. Welcome to this keynote speech by Professor Koichi Hamada. My name is Atsuko Kosaka, and I am a faculty member of Aichi University. First of all, I would like to ask President Motohiko Sato of Aichi University to deliver the welcoming address.

Address by Professor Motohiko Sato

This is the 22nd PBFEAM conference, a little bit long abbreviation for me to deliver. The conference was set by the greatest group of administrators of our Aichi University. I also welcome our special speaker, Professor Koichi Hamada, Professor of economics at Yale University and Professor Emeritus at the University of Tokyo. As you know well, he is also a special advisor to the Prime Minister of Japan, Shinzo Abe. Well, let me have a chance to refer to the history of our university on this special occasion. Our university was established in 1946 as a private university. However, there is a history of our university even before. Our roots go back to 1901, when a private institution of higher education named Toa Dobun Shoin was founded in Shanghai. While Toa means "East Asia", Dobun means "the same cultural background", and Shoin means "some kind of educational institution". This institution was established by the Toa Dobun association which was led by Mr. Atsumaro Konoé who was also President of the House of Peers at that time. Located in Shanghai, the institution attracted

many Japanese and Chinese students in a climate of academic freedom, imparting them with an awareness of international affairs that paid a particular emphasis on China, Japan and Asia. However, Japan's defeat in World War II led to the Chinese requisition of the institution, resulting in the conclusion of the half century of history. Our Aichi University was established mainly by those who worked as academic staff at the institution. Professor Kiichi Honma, the last president of the institution, played a central role in founding Aichi University. Based also on the educational tradition of Toa Dobun Shoin, our university put a special emphasis on educating students with a global outlook and with the idea of contributing to culture and peace. Hosting the 22nd PBFEM conference as one of the distinguished academic associations in the Pacific basin region has therefore very important bearings for our university in this connection. Finally, again, I cordially welcome all of you to Aichi University. Please enjoy a good time at our university. Thank you for your kind attention. (Applause).

Professor Kosaka

Thank you very much President Sato. Next is Professor Cheng-Few Lee, a founding organizer of this conference and also founding editor of two famous journals, Review of Quantitative Finance and Accounting (RQFA) and Review of Pacific Basin Financial Markets and Policies (RPBFMP). Professor Lee will now deliver his opening speech.

Address by Professor Cheng-Few Lee (Co-director of 22nd PBFEM Conference)

Good morning ladies and gentlemen, Professor Hoshino and Professor

Hamada, I really appreciate Aichi University that has spent a lot of effort to conduct this 22nd PBFEM conference. This conference started in Rutgers University in 1993 and then came to Asian countries like Taiwan, Singapore, Hong Kong, Australia, Vietnam, Thailand, China and so on and next year this conference is going to Ho Chi Minh City, in Vietnam again. and I will invite professors at PBFEM to discuss more about this conference. The history of this conference has been raising and raising its programmers. The progress of this conference is about 50-60% about academic and some policy and activity. and hopefully this conference has turned out to be getting more momentum in future of worldwide economic activity with an Asian emphasis. This is my second time to visit Nagoya City. Professor Hoshino invited me some 13.. 14 years back at Nagoya City University and I see the progress has advanced fast in the last 13 years. Finally I really appreciate professors coming from all over the world attending this conference and thank you very much.

Professor Kosaka

Thank you very much Professor Lee. This morning we have two keynote speakers. Our first keynote speaker is Professor Koichi Hamada, I would like to ask Professor Yasuo Hoshino of Aichi University, who is the Chair of this session, to introduce Professor Hamada.

Introduction by Professor Yasuo Hoshino (Chair, co-director of the 22<sup>nd</sup> PBFEM, Professor at Aichi University & Professor Emeritus University of Tsukuba)

Thank you very much, Kosaka-sensei. We Japanese use family names among our faculty members in Japan. Many foreign people here use first

name usually. It is quite unusual to use first name among Japanese, So, I would like to use family names, like Kosaka-sensei, Hoshino Sensei (laughter), first name is used only for close or personal relationships (laughing). Well, Kosaka-sensei, thank you so much. Now, I would like to introduce Professor Hamada, I have some slides here to show. Professor Koichi Hamada is Professor Emeritus at Yale University, and at the same time at the University of Tokyo. Professor Hamada is Tuntex Emeritus Professor of economics at Yale University, where he specializes in the Japanese economy and international economics, and Professor Emeritus at the University of Tokyo, where he taught before coming to Yale. Professor Hamada is Professor Emeritus at two very famous universities in the US and Japan. I am Professor Emeritus only at University of Tsukuba, just one. (Laughter). He is now also Special Advisor to the Prime Minister of Japan, Shinzo Abe and also he is considered to be the pioneer of Abe's economic policies, "Abenomics" (Abenomikusu) refers to the economic policies advocated by Shinzo Abe since the December 2012 general election, which elected Abe to his second term as Prime Minister of Japan.

Professor Hamada did his Ph. D. in Economics from Yale University. Professor James Tobin and Professor Tjalling Koopmans were members of his Ph. D. dissertation committee, both received, later the Nobel Memorial Prize in Economic Sciences. So we Japanese hope that he will receive it in the near future. Professor Hamada was on leave from Yale University to serve as the first President of the Economic and Social Research Institute (ESRI), Cabinet Office of the Japanese Government. The ESRI engages in policy-oriented research and compiling the GDP statistics. Professor Hamada was in a position to advise the Council on Economic and Fiscal Pol-

icy (CEFP), a body created to promote the administrative reform chaired by the Prime Minister. And he was the founding President of the Japan Law and Economics Association from 2001 to 2003 (now its honorary fellow). In 2006 Professor Hamada was awarded with the imperial decoration, the Order of the Sacred Treasure, Gold and Silver Star, 'Zuiho-sho' we say in Japanese, which is given to those who have accumulated distinguished achievements for Japan. Professor Hamada is the foreign fellow of the Econometric Society: An International Society for the Advancement of Economic Theory in its Relation to Statistics and Mathematics. Professor Hamada served as President of the Japanese Association of Economics and Econometrics (now the Japanese Economic Association) from 1994 to 1995. This is the largest social science association in Japan. Professor Hamada is also the founding President of the Japan Law and Economics Association in 2003 (now its honorary fellow). Professor Hamada also serves as one of the associate editors for many journals including *Econometrica*, *Journal of International Economics*, *Journal of Economic Theory*, *Journal of Public Economics*, *Journal of Development Economics* and *Journal of the Japanese and International Economies*. His books in English after 2007 include; *Financial crises in Japan*, *Ageing and the Labour Market in Japan: Problems and Policies*, *Towards Monetary and Financial Integration in East Asia*, and *Japan's Bubble, Deflation and Long-term Stagnation*. Now, Professor Hamada please. (Applause).

Keynote speech by Professor Koichi Hamada (Tuntex Emeritus Professor of Economics at Yale University & Professor Emeritus at University of Tokyo, Special advisor to the Prime Minister of Japan, Mr. Shinzo Abe)

Good morning ladies and gentlemen, I am very pleased to meet my old

friend Yasuo Hoshino and speak here at this conference mainly about the present economic policy in Japan. Yasuo reminded me of our friend and mentor Professor Kazuo Sato of Rutgers. He was from Hokkaido. I went to Yale Graduate School after his stay and he gave me advice on schooling at Yale. Most of all, Kazuo Sato taught me that rather than collecting good grades, an economist should try to discover new perspectives and try to convey them clearly. First of all, this gathering is a Pacific Basin Finance Economics, Accounting and Management conference. So this meeting is not necessarily about economics but also about accounting, management and so on. Before I go to topics in economics, let me talk about my study life and why I had not obtained good knowledge of accounting in my life. I went to the University of Tokyo and was told that in accounting classes if you make calculating mistakes, you will get B or C. I avoided it as I was scared of making calculating mistakes. Professor Richard Ruggles who was the advisor to Kazuo Sato, taught National Accounting at Yale Graduate School but I skipped his course, So I got Ph. D. in economics without taking any courses in accounting. But I regret this now. I should have taken accounting courses very seriously because accounting is very important in understanding economics. This discipline is based on the information about business. Nowadays we study asymmetry of information that is the science of cheating. One cannot know how to negotiate without information about economics and accounting. The work of Stiglitz and Akerlof show that study of information is the crucial field where economic science is making pioneering progress. I should not have worried about grades in accounting. Another thought on the topic is the stock market. I will talk about how the stock market in Japan is helping the recovery of the current Japanese economy. However, my comments are restricted by being a special advisor of

Prime Minister Abe. As an official in the US Treasury told me, I should not talk about the market price or rate which I might have a slightest influence in the future. So this is my personal opinion. I may convey my view to the Prime Minister, but it is independent of the Government policies, particularly the new government. The Lehman crisis took place in the US, the UK and Europe. Their economies plunged about 4 or 5 percent. On the other hand, the Japanese GDP fell down as much as 7 or 8 percent. This contrast was true despite of the fact the Japanese financial industry was not affected much by the Lehman crisis. The reason is that the Japanese GDP was seriously affected by the yen appreciation that came like a Tsunami by the enormous monetary expansion of central banks abroad. The Japanese monetary policy makers reacted to stabilize its financial market, but kept the yen very expensive. By Abenomics, monetary policy was expanded, the yen was moved more depreciated, and the interest rate was lowered to almost zero. Unemployment became close to three percent. The job offer-applicant ratio became over unity. Firms like Yoshinoya found it difficult to recruit new applicants. The Bank of Japan expanded supply of money to the economy. Employment improved drastically, firms' revenues became historically high, and even tax revenues dramatically improved.

Now it is time to look at the supply side in the same way. Structural reforms in industries, and deregulation are needed but they are difficult to implement because there is resistance from those who enjoyed power, benefits from existing inefficiency. There are so many systematic difficulties with the supply side. Stronger growth of supply side is not straightforward. We cannot catch up to the advance technology as we could do 20 years ago by the industrial policies. No longer, Japanese management maintained the growth rates. However, probably I should say that the



stock market is important in Abenomics, the opponents of Abenomics say that a monetary stimulus does not work because people accumulate so much money in their pocket. So additional money would not stimulate spending. Then BOJ Vice-Governor Iwata said that if people know that inflation is coming, they will know their cash will depreciate in value and then they will start spending. So there is a real balance effect. The third arrow is a structured policy and there are also relevant to the stock market. The rest of the structured policies are basics. About one year ago Mr. Abe was addressing the Diet and explaining each item of these structural policies, that is, reading the manuscript wrote, the stock market started to decline. I joked that the first arrow should be given a grade A. For the second arrow, I have some reservations to the government spending, I might give a grade B, and for the third arrow have so many reluctances but I couldn't give F, failure, so I give a grade of E (Laughter). So ABE completes the theory. Back to the third arrow. There are so many difficulties and I will discuss some of these. The first thing is industrial policy. Hopefully, we can manage by giving some subsidies and they see the growth because it was the time when the automobile industry had the future and in the long term that was partially successful. However, these kinds of measures can have some political economy-wise problems that the greater benefit for one industry can be captured by a greater loss to others. You give greater subsidies to a particular sector and at the same time you may get some balancing effect by shooting some other industries. So this type of policy which cannot help so much deregulation is important, but many bureaucrats enjoy the power of control. So they don't want to give up. Japanese bureaucrats push Japanese sunrise government for protection, so the structural reforms, first of all, should be deregulation. But at the same time be-

cause the steps are to be taken by bureaucrats it has political difficulties. The deregulation is conducted mainly by bureaucrats. Therefore, deregulation is a process that group of samurai warriors give up their robe (yoroi) that is so comfortable to them. The only hope is that Mr. Abe and cabinet secretary Mr. Suga are very eager to accomplish this. They have made enough of necessary legislations for reforms during the first half of the year. So they are serious to do reforms and that is the hope for the economy. The problem is to find out what government need not to do. There are many stories. For instance medical school is recently approved but the rest of the medical schools were approved 34 years ago, and in 34 years many clinical progress has been made. So the bureaucracy confined the way of producing doctors, who were very talented by preventing to increase the number of doctors, so there is problem of the lack of doctors for the population. TPP is sort of in danger of disappearance in the US. It would improve Japan's trade prospects considerably, including sensitive sectors like agriculture, where exporters of fast-moving consumer goods like flowers and vegetables would benefit. We have flower industry in Aichi that is the best export industry of the prefecture. Holland has a leading example in flowers with long history of tulips. And vegetables are not protected by the Government. Yet they are indispensable in making excellent Japanese cuisines. In the large, they are export from Japan. About the population growth, still women are great resource. Legislation is still biased that women who are at home serving her husband and taking care of her children are subsidized. For children as well, isn't it better to be parented by mothers who have social and working experience? About the corporate tax. See the illustration. (Referring to slide 12) This is in English: Effective rate of corporate tax rates in several countries, Japan first, then the US,

France, Germany, China, (Seoul) Korea, England, and Singapore. So and the most important finding is that the lowest one is Singapore, and the second lowest is England in this figure, China, Korea and so on. The US is highest but it depends on the states. Japan has the highest corporate tax rates. In my first paper, I wrote that there is an element of game in the tax competition. The point is that if the country tries to reduce taxes, it will have some competitors. So England had a very high corporate tax, but now it has started some tax wars. This may work for Japan, which needs to reduce drastically, not one percent each time, to give incentives or so to the investors. Then there will be shifts in investments. So if Japan reduces 1% of the corporate tax rate, it doesn't mean that investments will come to Japan, or that the Japanese investors investing in other countries will come back. But still it is a measure that government can use. For instance, if the government reduces the corporate-tax rate to align it more closely with international standards, amid increasingly intense international competition to attract foreign investment, reducing the corporate tax would actually increase Japan's tax revenues, by spurring companies to invest their vast cash stockpiles in more productive activities. While bringing investment is something that will not increase the demand side, it will increase the supply side, and that is the reason why I advocate this. One thing regarding the demand side is that the population growth in Japan is very slow. One relatively simple solution would be to integrate more women into the labor force. That's what I have explained quantitatively. Suppose that 20 percent of women come to work after child birth. A 10 percent increase in Japan's female labor-force participation rate would be translated into an almost 5 percent gain in total labor-force participation. Unfortunately, you cannot continue this for a long time and something will come from outside, proba-

bly immigration. Immigration is something that is most logically following, but it may not be compatible with Japanese sentiment. So we need to work to expand the labor force step by step. And depending on your time, scheduled time, now I will take questions.

Professor C. F Lee: I think this is a very interesting talk and combined with practice this essentially will go with our Journal, Review of Pacific Basin Financial Market and Policies, and I hope you can put it on paper, and probably you will make a leading article in my journal, I hope.

Professor Hamada: Yes, I hope.

Professor Lee: And in addition I would like to say that in our Pacific Basin Journal we are really set for more on the Policy and Market interaction, even US research and more into macro finance research. So I really enjoy your talk. Thank you.

Professor Hoshino: Any questions, or comments from the audience?

Question from the Audience: Thank you very much. I enjoyed your talk. I wonder whether you will recommend increasing the consumption tax to 10 % next year. Do you have any advice for Mr. Abe?

Professor Hamada: Are there some people from the media here?

Professor Hoshino: No, I don't see any media. (Laughter)

Professor Hamada: I think this year, this second quarter is the combination of up and down shocks so that it is not the best time to decide. This is my personal opinion and I don't know what Mr Abe is thinking. So if the third quarter GDP stays slow, we can postpone this 10% raise or we can make it one by one, say, next April one percent, after one and a half years, say, 10%. My interest is now shifting to corporate tax, because lowering the tax can bring more FDIs to Japan when the world is engaging in tax wars. Korea, for instance, will be going for a drastic cut in corporate tax. The current corporate tax rate is so high in Japan. The second highest among the large seven nations. If we go a few more years with the high level of corporate tax it will raise concerns. Reducing the corporate tax would actually increase Japan's tax revenues, by spurring companies to invest at home. Consumption tax has a less demand elasticity, say, for instance, if you increase one percent consumption tax on hamburger then people will reduce the consumption much less.

Question from the Audience: I am not so interested in what Mr. Abe will say but specifically along the lines you discussed about the tax increase further, they have the Abenomics suffering, right now, because Japanese people understand it's a kind of major contradiction like make a small increase and if it fails to recover then next year will increase it further, till three years. So it continues like that. But Japanese people know how the tax revenue continues to shrink every year, because if it continues to be shrinking it will make the economy suffer a lot.

Professor Hamada: The Japanese finance ministry has a special accounting system. It's the pool of tax revenue that always remains constant. So if we

do this calculations of consumption tax rate it will circulate revenue as given amount of tax rate given by the system behind. So it may not the direct answer to you. But Ministry of Finance should stop thinking of forgetting economics. They get the old brightest university graduate, or they use to do so, and so they should stop ranking it on that system. So, I will rather say, we should instead of looking at the consumption tax issues shifting our attention to cooperate tax is much more important. For example, special tax measures that each company are given, some special measures, some of them are given because of the employment, because of technical reasons. They also give power to the bureaucrats. So Ministry of Finance should also change that kind of things. Anybody can answer, I have actually, I was raised in the theoretical field and all the numbers of the US were calculated by my colleagues or some assistants. But US numbers were not very different from Japanese numbers, until 2012, the Japanese economy was very slow thus the rate of corporate tax was very low, and the Ministry of Finance says that corporate tax is not the place where we should avoid our tax.

Professor Hoshino: Ok, next question.

Question from the Audience: Thank you very much Professor Hamada for the talk. I am from Keio University, Institute of Energy Economics of Japan. The Bank of Japan has about 2 percent inflation targeting. Until now about 1.2 percent is achieved. Do you believe how many percent, how much portion of this percentage is because of easy money of monetary policy, and how much portion of this percentage is because of high energy prices.

Professor Hamada: The general price increase is more related to the monetary policy abstractly. In a very abstracted sense, your question should be analyzed more carefully in terms of many things, in terms of exchange rates, consumption tax rate, and expectations. I do not think hitting an inflationary target is very important.

Professor Hoshino: Could we have the last question?

Question from the Audience: The actual problem that Japan suffering is, as number one, I would say, is low rate of birth. The population of Japan is declining tremendously and its a matter of 200 years before the nation of Japan will become extinct. (Laughter) I am to say that, I want to hear, what do you want to suggest regarding this apparent social issue and the government human policy and economy of society that have worked on this issue. I will be happy if you give some of your ideas.

Professor Hamada: This is a joke by Columbia Prof. David Weinstein, that Japan will be extinct by 20-- (Laughter). However, women constitute about half of the population, so that a 10 percent increase in participation would make a significant short term solution for the working force.

Professor Hoshino: Thank you very much. I think that is about all for this session. Now we will go for the photo session, please.

## Reference

Cheng-Few Lee, Yasuo Hoshino, and Mohd Fazli Mohd Sam, Review of Pacific Basin Fi-

Financial Markets and Policies 18, 1596001 (2015) [15 pages] <https://doi.org/10.1142/S0219091515960016>



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# CONTINUING THE SUCCESS OF ABENOMICS

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Presentation by Koichi Hamada  
Special Advisor to the Cabinet, Japan,  
Aichi University, September 4, 2014

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## Caveat

- I will present my own personal views here that is independent of the current policy positions of the Japanese government.

## PBFEAM

- Accounting
  - (1) in my life,
  - (2) as a cradle of an asymmetric information,
  - (3) as a part of government reform.
- 
- Kazuo Sato as my mentor.

## Three Arrows

- Motonari Mohri, Daimyo of Chugoku District where the Prime Minister was born, gave an arrow to each of his children asked told them to break it which they did easily. He then told them to tie the arrows together and try to break them, --- it was difficult --- thereby demonstrating that “cooperation” would make the bond stronger.
- And so the “three arrows” of Abenomics are meant to work in co-operation. They are:
  - (1) Bold monetary policy;
  - (2) Flexible fiscal policy; and
  - (3) Strategies to promote growth.

## Relationship between the Arrows

- Arrows are not necessarily parallel, but connected by structural relationships:
- (1) Monetary policy, the first arrow, is effective when deflation and the high yen leave excess capacity in the economy. This arrow already hit the bull's eye!
  - The asset markets, stock and the yen immediately responded.
  - Monetary ease was successful through real balance effect, portfolio rebalance (Tobin's q) and acceleration effect in the credit channel.
  - Already it is working effectively through to goods, and labor market.
  - High economic growth rate of 4.1% (1st quarter), 3.8% (2<sup>nd</sup> quarter) and improvement of labor (offers/applicants) ratio to over 0.9 are indications of success. <Display 1 and 2>

## Important to note

(1) The first arrow is unusable, for example, in the Euro area.

Mobility of labor and capital can mitigate the difficulties.  
Banking Union may be only *partially* helpful.

(2) The currency war under the flexible rates is a fallacy!

## The First and Second Arrows (continued)

- As long as there is excess capacity, easy money works even without growth strategy (the third arrow). When the economy hits the level of full employment, then money does not increase output or employment and may trigger inflation.
- (2) Fiscal Expenditures, the second arrow, are necessary to maintain the quality of public services. As Robert Mundell shows, however, under the flexible exchange rate, the role of this second arrow is quite limited if not accompanied with accommodative monetary policy.

## The Third Arrow

- (3) Growth Strategy, the third arrow, will enhance the full employment capacity growth path through structural reforms, technological innovation, TPP (Trans-Pacific Partnership) and corporate tax policy.
- Expectations of the the third arrow---Growth Strategy
  - The Old Fashioned MITI type Industrial Policy --- No! When Japan operates at the frontier of industries, the government can't choose the winners.
  - Exceptions are when externalities and public goods exist. There is a strong case for the carbon tax.
  - Mainly, growth strategy is hidden in competition and markets ---along the Koizumi-Takenaka regulatory reform lines.

## From Wishful Thinking to What Government Can unDo

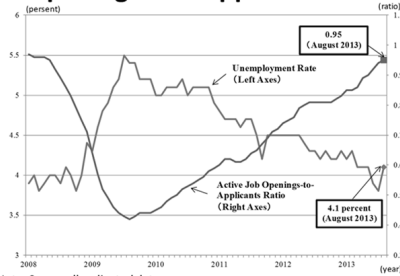
### Now

- To encourage investment in the Japanese economy, rather than “wishing to the stars”, consider what the government can do right now, for example:
  - (i) Deregulate,
  - (ii) Participate in the TPP, and
  - (iii) Reduce the corporate tax burden, or introduce the system to encourage investment such as accelerated depreciation, and a longer loss-offsetting period.
- The pursuit of the third arrow without the first may be even deflationary.

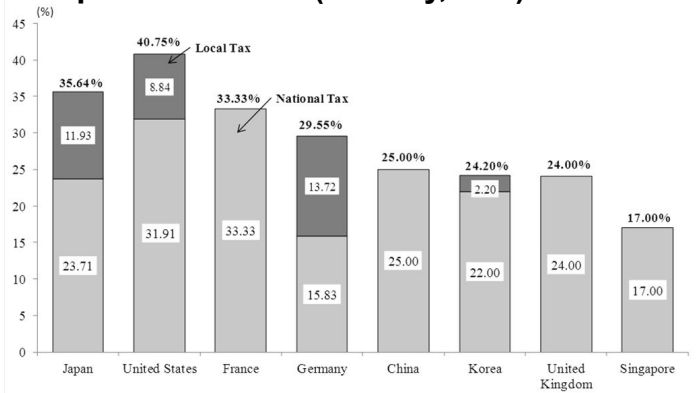
## Appendix: Regarding Tax Competition of Reducing Corporate Taxes

- Government has a large deficit, playing a “civilized” Ponzi game. But the Ministry of Finance highly exaggerates it home and abroad.
- The effective corporate tax rate is higher than abroad. (Display 3) In order to survive tax competition, corporate tax burden should be lowered.
- Any tax raise will be accompanied by allocative deadweight losses. Among The consumption tax may be the least harmful. However, the right timing of consumption tax hike is important not to suffocate recovery. I raised my reservations but the government decided to go forth because of the recent rapid recovery.
- As long as monetary policy through exchange and stock market is effective, I hope the recessionary effect of the hike will be limited.

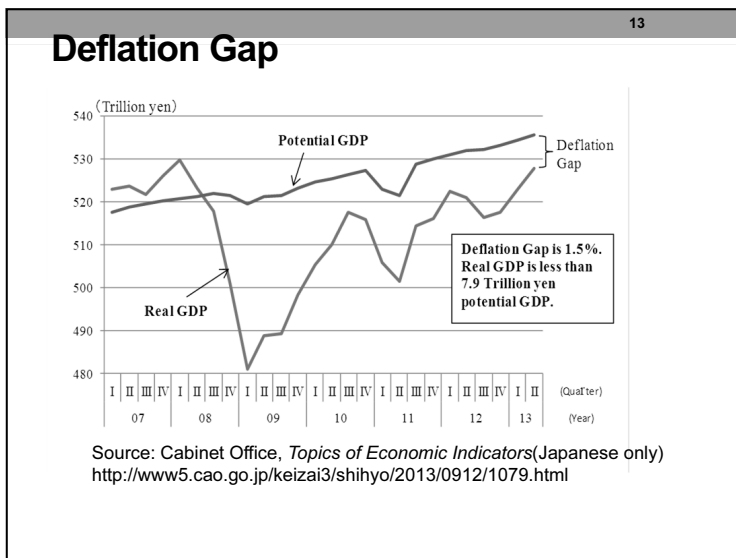
## Unemployment Rate and Active Job Openings-to-Applicants Ratio



## International Comparison of The Effective Corporate Tax Rate (January, 2013)



Source: Ministry of Finance Japan Data (Japanese Only)  
([http://www.mof.go.jp/tax\\_policy/summary/corporation/084.htm](http://www.mof.go.jp/tax_policy/summary/corporation/084.htm))





22nd PBFEM, Sept. 4-5, 2014, Aichi University at Meitetsu Grand Hotel