Japanese finance minister quits

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The resignation of Hirohisa Fujii as Japan's finance minister on January 6 is the first clear sign of crisis in the country's Democrat-led government. The Democratic Party of Japan (DPJ) won national elections last August, ending half a century of virtually unbroken rule by the conservative Liberal Democratic Party (LDP).

Fujii's decision to step down was a blow to the Democrats. He was one of the few ministers with government experience. A long-standing finance ministry bureaucrat, he served as finance minister in the 1993-94 coalition government that briefly displaced the LDP. After last year's election, he was again appointed finance minister in a bid to reassure big business circles that their interests were in safe hands. Prime Minister Yukio Hatoyama has replaced Fujii with one of his closest allies—deputy prime minister, Naoto Kan.

Fujii, 77, resigned for health reasons after being hospitalised for high blood pressure and exhaustion. Quite directly, his health was a reflection of the state of the economy—he had been labouring to resolve the country's intractable economic woes by formulating a strategy for the next decade and pushing through a $1 trillion budget for fiscal 2010, Japan's largest ever.

Japan's economy, which has been stagnating for most of the past two decades, has been hard hit by the global recession. The latest data shows that output continued to contract in the third quarter of 2009—at an annualised rate of 5.1 percent. A Reuters poll of 24 economists last month estimated that the economy would grow by a mere 0.2 percent in the first half of 2010.

Fujii's "roadmap" of 2 percent annual growth for the new decade was widely regarded as too ambitious. It outlined sweeping aims in six major economic areas, proposed creating four million jobs and sought to create more than 100 trillion yen ($US1.08 trillion) in new demand during the decade. However, as critics pointed out, it was short on detail and failed to answer the obvious question—how was it going to be financed?

The government, not just the finance minister, confronts a basic dilemma: if it spends money to stave off recession, it adds to the mountain of debt created by previous stimulus packages. Public debt now stands at $US8.96 trillion—greater than the US federal debt of $8.78 trillion—even though Japan's GDP is just a third of America's. An IMF report last November projected that Japan's budget deficit would still be 8 percent of GDP in 2014 and its debt would hit 246 percent of GDP.

To reassure the markets, Fujii publicly declared upon taking office that he was a fiscal conservative determined to rein in public spending. He promised to keep the issuance of new government bonds under 44 trillion yen or $US474 billion in the new fiscal year. However, with a trillion dollar budget and expected tax revenue of about $400 billion that is proving impossible. The only alternatives are reducing the budget's size by slashing essential services, increasing taxes or printing money.

Fujii's replacement Kan previously criticised Fujii for proposing a cap of $474 billion on government bonds, arguing instead for more stimulus measures to boost the major corporations and banks. Declaring that the Bank of Japan must do more to combat deflation, in November he called for the injection of more money into the banking system.

As the leader of the DPJ from 2002 to 2004, Kan was an advocate of pro-market restructuring. He appealed to the urban middle classes by criticising the LDP government for its spending on the state bureaucracy and heavy subsidies to rural electorates. After the DPJ won power, Kan headed an administrative reform council aimed at establishing firm control over the state bureaucracy and slashing jobs and spending.

On becoming finance minister, Kan indicated he would open up a debate on the highly unpopular consumer tax. During the election, the DPJ promised not to raise the tax for five years. But Kan insisted the government had to discuss tax hikes, as “there is no way of finding new fiscal resources”. He claimed that he wanted to prepare the public for a consumer tax increase after the 2013 elections, but he may have more immediate aims.

Any rise in the consumer tax is politically risky. The tax provoked widespread protests when it was first introduced. The country’s economic crisis is undermining the DPJ’s ability to fund other election promises, including child allowances, free education and the axing of road tolls. Increasing the consumer tax could produce broad opposition. Moreover, the government’s popularity has slumped already from more than 70 percent last September to 42 percent.

The Hatoyama government is under siege on another front. Last week, Tokyo prosecutors arrested three aides to DPJ secretary general Ichiro Ozawa, over the violation of political funding laws. Ozawa is one of the most powerful figures in the DPJ. He was party leader until the scandal erupted last year and is widely regarded as the strategist behind the DPJ’s election victory.

The scandal highlights the heterogeneous character of the DPJ, which includes breakaway factions from the LDP and the former Socialist Party, pro-market reformers and advocates of continued economic regulation. It is alleged that Ozawa’s fundraising organisation received donations from construction corporations—a common practice associated with the LDP, which in return handed out large contracts in rural areas to favoured companies.

At this stage, Ozawa has not been directly implicated. But if he were to be charged, it would be another major blow against the party and the government, which is facing upper house elections in the middle of the year. Less than six months after taking office, Hatoyama is confronting a looming political crisis as the initial euphoria of ousting the LDP wears off and working people start to recognise that the new government is carrying out similar policies to its predecessors.