Japan enters “technical recession”

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The Japanese economy has entered a technical recession, defined as two consecutive quarters of negative growth. The contraction in the third quarter, which was the result of a fall in business investment, has dealt another blow to the claims that so-called “Abenomics” would restore growth to the world’s third largest economy.

It is the second such recession since Prime Minister Shinzo Abe took office in December 2012 promising radical measures, based on increased fiscal stimulus and a major expansion of the money supply, to end the cycle of deflation and anaemic growth which has characterised the Japanese economy over the past two decades.

According to official government figures, gross domestic product declined at an annualised rate of 0.8 percent in the three months to the end of September, following a 0.7 percent contraction in the second quarter.

The main factor in the contraction was a fall in business investment, prompted by fears of the impact of lower growth in China and a weakening global economy.

Atsushi Takeda, an economist at Itochu Corp in Tokyo, told Bloomberg: “This report shows the increasing risk that Japan’s economy will continue its lacklustre performance. The weakness in capital spending is becoming a bigger concern. Even though their plans are solid, companies aren’t confident about the resilience of the economy at home and abroad.”

The fall in inventories subtracted 0.5 percentage points from growth in the third quarter as companies ran down stocks built up over the previous six months, while lower business investment shaved off a further 0.2 percentage points. Increased consumption spending added 0.3 percentage points to growth but it was insufficient to overcome the downward trends in the business sector.

Abe has appealed to businesses to advance their spending plans and use their record cash holdings for expansion but his urgings are falling on deaf ears, with investment falling by 1.3 percent in the three-month period.

Faced with the failure of its policies, the government is trying to put the best face on a bad situation. Akira Amari, the minister for state and fiscal policy, and said to be a key Abe economic adviser, told a press conference on Monday that Japan’s economic recovery was on track despite some risks in overseas economies.

But other remarks appeared to counter that relatively upbeat assessment. “The problem is that capital spending is not robust, which indicates that the mindset of company executives remains deflationary,” he said.

This situation points to the underlying contractionary trends. Business investment plays a key role in the capitalist economy and is the driving force of expansion. Increased capital spending leads to the hiring of more workers, thereby boosting consumption spending. Likewise, the increase in purchases for raw materials leads in turn to further growth and helps lay the foundations for a broad economic expansion. This is clearly not taking place.

Some economists have drawn comfort from the fact that the biggest factor in the third quarter contraction was the rundown of inventories, a process which can only go so far before there is a reversal.

The Chief Cabinet Secretary Yoshihide Suga struck an upbeat tone. “Corporate profits are at a record level and employment income is still rising,” he said. “The basic trend is gentle recovery.”

But the failure of companies either to undertake investment, or, where they do, to go overseas, belies that assertion.

According to Kiichi Murashima at Citigroup in Tokyo: “Unlike in 2014, when the consumption tax was raised, the economy contracted for two quarters in a row without any exogenous or systemic shock, which in our view highlights its underlying weakness.”

The ongoing stagnation of the Japanese economy and the failure of “Abenomics” to provide a boost will increase pressure in two policy areas.

There will be increased demands for the implementation of the so-called “third arrow” aimed at attacking working conditions and introducing great labour market

"flexibility."

Hiroshi Shiraishi, senior economist at BNP Paribas, told Reuters that the first two arrows of "Abenomics"—monetary and fiscal policy—were meant to buy time but Japan had "failed to make progress with painful reforms needed to boost its growth potential. Without reform (the 'third arrow'), the economy's growth potential remains low, making it vulnerable to shocks and to suffering recessions more often."

The contraction will also increase pressure on the Bank of Japan to step up its quantitative easing (QE) program, which at present involves increasing the money supply by about $920 billion per year—the largest such program for any economy.

The Bank of Japan did not increase QE at the last meeting of its governing council but that could change next January. "With rising slack dampening price pressures, we remain convinced that more monetary stimulus will eventually be needed," said Marcel Thieliant of Capital Economics in Singapore.

Further monetary expansion could have global consequences. In a comment published on Tuesday, Adam Carr, a columnist with the Australian *Business Spectator*, noted that the muted response to the news of Japanese recession—with so many over the past few years that another does not register—could be "a little too blasé."

"The reality is that renewed recession risks not only an intensification of the global currency wars, but also markedly higher financial market volatility," he continued.

This is because moves by the Bank of Japan to carry out additional monetary stimulus will further push down the value of the yen, increasing tensions with its competitors in the region. The yen is down about 60 percent against the Korean won and is at its lowest level against the Taiwanese dollar and the Chinese renminbi in a decade. This causes a problem for each of these economies because exports are critical—comprising up to 50 per cent of the total economy—and "export growth is already weak or non-existent."

In conditions of slowing Chinese economy growth and a stagnant world economy, opposition to the further devaluation of the yen will increase and possibly lead to retaliatory measures.

Coming as it did in the midst of the G-20 economic summit in Turkey, the Japanese announcement also underscored the fact that not only is "Abenomics" in tatters but all the commitments by the major economies to boost growth.

The G-20, which was largely concerned with discussing the military and political response to the Paris terror attacks, announced no new economic initiatives and simply reaffirmed the already empty commitment made at the Brisbane summit in 2014 to take measures to lift global growth by an additional 2 percentage points.

The official communiqué did, however, have to acknowledge reality, noting that "global growth is uneven and falls short of our expectations", that "risks and uncertainties in financial markets remain" and that a "shortfall in global demand and structural problems continue to weigh on actual and potential growth."

When the G-20 summit meetings were launched in the wake of the 2008 financial crisis, it was claimed they would provide a new forum to advance global economic expansion. Seven years on, their failure to do so prompted one commentator to pose the question "What on Earth is the point of the G-20?"

The same question could just as well be asked of other international bodies, including the G-7 group of major economies and the World Trade Organisation, where the so-called Doha Round of trade negotiations remains stalled amid fears growing of intensifying trade and currency conflicts.

It could also be extended to the United Nations as well. Set up in 1945, supposedly to prevent war, its 70th anniversary on October 24 passed without a ripple, an expression of the fact that the UN is going the way of its ill-fated predecessor the League of Nations in the period leading up to the outbreak of World War II.

The deepening recessionary trends, of which the Japanese data are the latest expression, the total inability of the G-20 or any other economic body to advance a remedy, coupled with the predominance of so-called "security" and military questions at every international forum, are a sure indication that the conditions that prevailed in the 1930s are making a return.