

Economic Policy Trilemma: Macroeconomic Politics in the 2021 Election*

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Abstract

Highly accommodative monetary policy during nine years of Abenomics allowed fiscal expansion to become the center of the Japanese government's COVID-19 stimulus and the further economic measures were the primary issue facing the 2021 Lower House Election. Under monetary constraints, the economic policy choice among Japan's conventional growth strategy, distribution, and fiscal discipline creates trilemma, where the government can pursue only two of these three goals. In this election, the LDP-Kōmeitō coalition managed to straddle between distribution and growth strategy, while exploiting policy space for the opposition parties. Although the coalition maintained the electoral majority, the inroad made by Ishin, Reiwa, and the Democratic Party for the People whose campaigns neglected fiscal discipline in favor of both growth and distribution foreshadows the challenge against the Japanese government's future fiscal health.

Keywords: Monetary policy, Fiscal stimulus, Distribution, Growth strategy, Economic policy, Trilemma

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Japan's Lower House Election on October 31, 2021, came at the heels of 18-month massive COVID-19 stimulus measures where the Liberal Democratic Party (LDP) was judged based on the effectiveness of these measures and future economic plans. Opposition parties criticized the failures of the LDP economic policies, not only against the ongoing COVID responses but also the detrimental impacts of Abenomics of the last nine years. In the end, the LDP-Kōmeitō coalition won and kept the majority in the Lower House, but ongoing massive stimulus appeared to contribute little to the long-term growth of Japan's economy.

While Abenomics contributed to low unemployment, ascending stock prices, and relatively robust economic growth prior to the pandemic, its measures constrained the Japanese government facing the COVID-induced economic crisis. On the one hand, its signature first arrow known as "bold monetary policy" has exhausted monetary measures to stimulate the economy. On the other hand, despite Japan's prolonged primary balance deficit and significantly high level of public debt, low interest rate on government bonds maintained by the Bank of Japan (BOJ) has opened the possibility of fiscal expansion. Consequently, fiscal stimulus, the second arrow, has become the main measure in response to the COVID-19 pandemic during the fiscal year 2020 (April 2020–March 2021). As such, the Abe and Suga administrations implemented massive fiscal stimulus, totaling ¥76.8 trillion, as they promised to revitalize the Japan's post-pandemic economy.

How did the COVID-19 stimulus and economic challenges shape the LDP's economic policies and electoral strategy? There are two major revelations. First, while the size of the direct payments to households and small businesses was unprecedented, a closer examination of the fiscal packages suggests that the fiscal target shifted toward the end of the fiscal year to indirect subsidies to local governments and the LDP's client businesses such as construction and tourism. Second, despite Prime Minister Kishida Fumio's new economic plan under the slogan of "New Form of Capitalism," where economic growth and redistribution go hand-in-hand (on the selection of Kishida, see Nemoto, 2022, and Harris, 2022), its distributive tone had to be paired with the traditional growth strategy with the focus on supply-side

at the time of the Lower House Election. Therefore, we argue that the LDP’s economic policies have straddled between distribution and traditional supply-side growth strategies in the face of the 2021 Lower House Election without loosening the current fiscal discipline¹. How did such strategy, in turn, affect the opposition parties’ strategic choice of the economic policy, and the election outcome? We claim that this straddling strategy pursued by the LDP-Kōmeitō coalition exploited the policy spaces for the opposition parties, which led to positive electoral outcome for the LDP. Given the condition where the LDP-Kōmeitō coalition has already encompassed the distributive policies and conventional growth strategy relying on existing industries, the only alternative way to calm people’s distress and gain voter support was to conduct further fiscal stimulus in the form of hand-outs spending. Thus, the policy choice left for the opposition parties was either transferring resources from the rich and established industries to the poor by imposing progressive taxes—“redistributional (saibunpai)” policy—or compromising on the fiscal discipline by public debt expansion.

We call this struggle a trilemma of economic policy among Japan’s conventional growth strategy, distribution, and fiscal discipline. The trilemma is more applicable when the monetary policy space is limited after the massive policy actions through Abenomics. This very monetary policy, nonetheless, paved the way for fiscal expansion, which was further stretched by the pandemic responses. The Constitutional Democratic Party (CDP) and the Japanese Communist Party (JCP) coalition pursued the fiscal discipline and distributive policy, whereas other parties including the Democratic Party for the People (DPP), Ishin, and Reiwa, promoted both distribution and growth strategies by loosening fiscal discipline through massive corporate tax cuts and issuance of new government bonds. As the 2021 election outcome would reveal, the strategic choice by the CDP-JCP coalition failed to gain support from a wide range of voters.

¹ We define distributive economic policy as a resource allocation toward demand-side of the Japanese economy consisting of consumers and workers, where the typical policy menu is to implement series of direct payments or reductions on income and sales tax. On the other hand, the supply-side growth strategy focuses on the producers, industries, and businesses where the government executes public expenditure programs to stimulate private investments and exploit regulations.

This chapter proceeds by first reviewing the Japanese government’s economic policy responses to the COVID-19 pandemic. We then assess Prime Minister Kishida’s New Form of Capitalism. Following the assessment, we examine the trilemma of economic policy that the opposition parties faced and how the trilemma helped the LDP-Kōmeitō coalition achieve their victory in the 2021 General Election and allowed a few smaller parties to gain grounds. The last section concludes with the implication of the LDP’s winning economic strategy on Japan’s long-term growth.

Economic Policy Response to the COVID-19 Pandemic

Prime Minister Abe Shinzō’s economic growth strategy, dubbed as Abenomics implemented since late 2012, has shaped Japan’s choice of economic policy response to the COVID-19 pandemic that started in early 2020. Abenomics’ first arrow, massive monetary policy, was the most impactful macroeconomic policy (Park 2021; Park et al. 2018). This aggressive monetary policy under Governor Kuroda Haruhiko of the BOJ appointed by Prime Minister Abe in March 2013 has continued for eight years with the aim to reach the 2% inflation target. Since this target was never achieved, in the process, the BOJ has exhausted almost all the possible monetary policy options to stimulate the economy even before the COVID-19 struck Japan. The short-term call rate set by the BOJ was already in the negative territory from January 2016, and with the massive “qualitative and quantitative easing” (ijigen no kinyū kanwa), the BOJ held almost half of the outstanding Japanese Government Bonds (JGBs). The monetary policy had changed little since the introduction of the yield curve control policy (YCC) in September 2016, as the YCC allows the BOJ to focus on the long-term interest rate by maintaining the rate at around zero percent. Thus, the BOJ has not conducted the level of bond buying as their policy target, and the pace of buying bonds has slowed. Moreover, the level of asset purchase programs other than the JGB had already been high. For instance, the BOJ committed to purchasing Exchange Traded Funds (ETFs) at annual paces of about ¥6 trillion despite concerns that the ETF purchase deteriorates the

corporate governance².

Facing the pandemic, therefore, the BOJ's response has been limited to minor adjustments. In March and April 2020, under the stock market jitters and as the initial response to the pandemic, the BOJ increased the maximum amount of additional purchases of Commercial Papers, corporate bonds, ETFs, and Japan Real Estate Investment Trusts (J-REITs). The BOJ also facilitated new funds-supplying operations to support corporate financing through bank lending³. These measures were incremental compared to the policy actions that the BOJ had implemented in the last several years. Despite the limited monetary policy space, the BOJ's YCC with its large asset purchase has greatly contributed to widening fiscal space for the government by deliberately depressing the cost of government's borrowing (Buiter 2021).

As a result, the main task of stimulating the Japanese economy under the pandemic has fallen in the realm of fiscal policy, and the Japanese government implemented massive fiscal measures to respond to the crisis. The analysis of the budget and its implementation leads to three observations. First, there has been a massive demand for a fiscal stimulus under the pandemic despite Japan's dire fiscal health being exacerbated during the last 30 years under the country's stagnant economy. Second, there was a clear shift in the fiscal stimulus measures over the course of early 2020 to 2021 from direct payments toward households and small businesses to conventional supply-side growth strategy of industrial subsidies and public infrastructure investments. Third, despite massive budget commitment, the execution rate of these stimulus measures shows not only the concerns for absorption capacity of the Japanese economy but also electoral motivation behind such allocation.

² Nomura Security reported that in December 2020, the BOJ became the largest shareholder of the Japanese stocks followed by Government Pension Investment Fund. See Nikkei, "Nichigin, hajimete saidaino kokunaihoyushani," February 5, 2021, available at: <https://www.nikkei.com/article/DGXZQDF057000V00C21A2000000>.

³ See BOJ, "Enhancement of Monetary Easing in Light of the Impact of the Outbreak of the Novel Coronavirus (COVID-19)," available at: https://www.boj.or.jp/en/mopo/mpmdeci/state_2020/k200316b.htm/, and "Enhancement of Monetary Easing," available at: https://www.boj.or.jp/en/mopo/mpmdeci/state_2020/k200427a.htm/.

Table 17: Japanese Government’s COVID-19 Fiscal Measures (in billions of JPY)

Expenditure category	First Stage		Second Stage		Third Stage	
	First	Second	First	Second	Third	Annual
	Emergency Response FY 2019	Emergency Response FY 2019	Supplementary Budget FY 2020	Supplementary Budget FY 2020	Supplementary Budget FY 2020	Regular Budget FY 2021
Infection control & Health and long-term care	7.8 <i>51.2 %</i>	46 <i>10.6 %</i>	758 <i>3.0 %</i>	2,784 <i>8.7 %</i>	2,519 <i>13.1 %</i>	—
RD for test kits, drugs, vaccines, etc.	2.1 <i>13.5 %</i>	3 <i>0.6 %</i>	52 <i>0.2 %</i>	206 <i>0.6 %</i>	161 <i>0.8 %</i>	—
Support for households	—	21 <i>4.8 %</i>	13,046 <i>50.8 %</i>	341 <i>1.1 %</i>	434 <i>2.3 %</i>	—
Support for workers and firms	0.6 <i>3.9 %</i>	276 <i>64.1 %</i>	8,981 <i>35.0 %</i>	16,231 <i>50.9 %</i>	7,769 <i>40.5 %</i>	—
Support for educational institutions	—	68 <i>15.8 %</i>	229 <i>0.9 %</i>	124 <i>0.4 %</i>	120 <i>0.6 %</i>	—
Special grants to local governments	—	—	1,000 3.9	2,000 6.3	1,500 7.8	—
Others	4.8 <i>31.4 %</i>	17 <i>4.0 %</i>	126 <i>0.5 %</i>	226 <i>0.7 %</i>	6,674 <i>34.8 %</i>	—
Contingency funds	—	—	1,500 <i>5.8 %</i>	10,000 <i>31.3 %</i>	—	5,000 <i>100.0 %</i>
Total	15.3 <i>100.0 %</i>	431 <i>100.0 %</i>	25,691 <i>100.0 %</i>	31,911 <i>100.0 %</i>	19,176 <i>100.0 %</i>	5,000 <i>100.0 %</i>
Share of Annual Reg. Budget	0.0 %	0.4 %	25.5 %	31.6 %	19.0 %	4.7 %
Date of Diet Approval	Feb 13, 2020	Mar 10, 2020	Apr 27, 2020	June 12, 2020	Jan 28, 2021	Mar 26, 2021

Notes: Share of each policy package in italic.

The numbers are aggregated by the authors following the categories by Ando et al. (2020).

Sources: Ministry of Finance etc. The details of the data and documents referred to in the table are available at the author’s GitHub repository <https://github.com/kenyamano/JapanDecides2021>.

The fiscal responses to the COVID-19 pandemic came in three stages (Table 17)⁴. The initial response during fiscal year 2019 (February and March 2020) focused on infection control and healthcare provision. The initial policy action was quite urgent because of the outbreak of the COVID-19 on a cruise ship, Diamond Princess, in late January 2020, and the evacuation of Japanese nationals from Wuhan by the government-chartered aircrafts. Infectious controls, the PCR test, and healthcare system preparedness was urgently established (Takenaka 2020). Because there was no time to approve an additional budget at the Diet at that point, the amount of the expenditure was limited. On February 13, 2020, nonetheless, the Japanese government announced the Novel Coronavirus Disease (COVID-19) Emergency Response Package totaling ¥15.3 billion followed by the second package announced on March

⁴ All data on the budget presented in this section are obtained from the Ministry of Finance and other sources and aggregated by the authors. The details of the data and documents referred to in the table are available at the author’s GitHub repository: <https://github.com/kenyamano/JapanDecides2021>.

10, which amounted to ¥430.8 billion. The second and third column of Table 17 shows the detailed expenditure by each category⁵.

Following the first stage, the government introduced two supplementary budgets to support households and businesses in the first quarter of the fiscal year 2020. In the first, supplementary budget passed the Diet in April 2020. The largest expenditure category, consisting of half of this first fiscal package, was “support for households” for ¥13 trillion, was mostly dedicated to the Special Cash Payments Program that credits ¥100,000 to each registered resident in Japan. The second largest category in the budget was “support for firms and workers” (35% of this supplementary budget). The largest expenditure item under this category was financial support for small and medium enterprises (SMEs). This category also included the expansion of the existing Employment Adjustment Subsidies and the Labor Insurance Special Account. Likewise, the second supplementary budget of approximately ¥32 trillion, larger than the first one, was passed on June 12. The largest component of this supplementary budget was “support for firms and workers,” which was almost double the amount of the first supplementary budget. In this category, the budget was allocated to expand loan programs for firms, to establish a new rent support grant for SMEs, and to expand the Subsidy Program for Sustaining Businesses in support of SMEs established in the first supplementary budget. Overall, the economic packages doled out in the first quarter of the fiscal year 2020 aimed mainly at supporting households and firms by directly and widely distributing funds, which accounted for 57.1% of the annual regular budget of the fiscal year 2020.

The third stage of the fiscal stimulus, whose supplementary budget was implemented in January 2021, the beginning of the last quarter of the fiscal year 2020, however, weakened the focus on direct supports toward households and firms. The components of this policy package were similar to the second supplementary budget (see the fifth and sixth column of Table 17). For instance, “support for firms and workers” still took the largest share of

⁵ These initial responses were covered by the contingency funds in the regular budget of the fiscal year 2019. The total amounts of the expenditures were 0.4% of the annual regular budget.

this supplementary budget package, and it allocated almost the same amount of budget to “infection control/health and long-term care” as the second supplementary budget.

What is notable, however, was a dramatic increase of the amount allocated to “other categories,” which were not directly related to the imminent pandemic response. The policy statement indicated that the purpose of this finance was to realize the transformation of the economic structure and a virtuous economic cycle under the post-pandemic era. Despite such claim, this budget category offered only broad and vague expenditure plans such as “Digitalization and Green society,” “Productivity improvement by structural reforms and innovation,” and “Realization of the consumer-led virtuous economic cycle in the region, society, and employment.”

Moreover, apart from the response to the COVID-19 pandemic, this third fiscal package included expenditure on infrastructures to enhance disaster prevention and national resilience. Therefore, while the third supplementary budget continued to support the health providers and firms, the main target has shifted toward the classic supply-side focus labeled a long-term growth strategy. In sum, this trend suggests that the governing coalition of LDP and Kōmeitō pursued the supports from the specific interest groups while appealing to the broad public by the straddling strategy that combined direct distributions, which parties on the left traditionally promote, and the conventional LDP-style infrastructure investments and public expenditure policy.

Finally, summing up all these fiscal stimulus packages, the total budgets were unprecedented: the size of these three supplementary budgets amounts to 76% of the initial regular budget of the fiscal year 2020. Vocal concerns presented by the Vice Minister of Finance Yano Kōji immediately before the Lower House Election sounded the alarm against lack of fiscal discipline and eminent fiscal disaster emerging in the horizon⁶. The economic impacts of these fiscal stimulus packages have also invited reservations as their execution rates are low. Comparing the actual expenditures to the aggregation of regular and supplementary

⁶ See Yano Kōji, “Konomama deha Kokka zaisei ha Hatansuru” November 2021, Bungei shunju, available at: <https://bunshun.jp/articles/-/49082>.

budgets related to the policy response to COVID-19, the Board of Audit of Japan (BAJ) reported that only 65% were executed in the fiscal year 2019 and 2020⁷. Although it is true, as some argue, that the third supplementary budget was put in place in the last quarter of the fiscal year without enough time for implementation⁸, these lower execution trends are observed in many projects across all the supplementary budgets and in various categories of expenditure. For instance, the BAJ pointed out in its annual audit report that the subsidy to the local governments called Special Allocation for Revitalization to Cope with COVID-19 (*chihō sōsei kōfukin*), and the financial support for travel, culture, and arts industries executed only 33.1% and 35.0%, respectively⁹. Even for the core policies that help people and firms in need, the record showed low execution rates of 72.7% (help people) and 47.7% (help firms under financial duress). Moreover, the financial support for medical providers recorded 67.6%.

There was clear evidence of some projects having been executed inefficiently¹⁰. For instance, the BAJ identified the case in which a fair and competitive procurement process in the Subsidy Program for Sustaining Businesses was stifled by the government not sufficiently disclosing information in the pre-bid contract when the project was outsourced. There is evidence of the contractor repeatedly subcontracted up to nine subcontractors generating a large amount of intermediate margins. The BAJ concluded that the project was outsourced in an inefficient manner demonstrated by the level of actual spending as a subsidy below the headline budget. Another example is the contract flaws in the “Go-To” travel campaign program, where the Ministry of Agriculture, Forestry and Fisheries contracted about half of the contractors without written contracts for outsourcing. The Japan Tourism Agency did not ensure how the contractors distributed the cancel fees paid by the government, either. Lastly, there were financial losses in the cloth mask distribution project, so-called “Abe

⁷ See BAJ, “Reiwa 2nendo kessan kensa houkoku no honbun,” available at: https://www.jbaudit.go.jp/report/new/summary02/pdf/fy02_gaiyou_zenbun.pdf.

⁸ See Nikkei, “Seifu yosan no kurikoshi gaku, kako saikō no 30.7 choen,” July 30, 2021, available at: <https://www.nikkei.com/article/DGXZQQUA29DQP0Z20C21A7000000/>.

⁹ See footnote 7.

¹⁰ All cases presented here are in the BAJ’s annual audit report. See footnote 7.

no masuku” (Abe’s masks), because millions of the masks have been damaged and gone unused, languishing in storage. These low execution rates as well as visible waste indicate how hyperbole the headline budget was and reveal strong electoral objectives in the face of imminent Lower House Election waiting in fall 2021.

Overall, despite the aggressive fiscal policy measures implemented by the Japanese government, which cushioned short-term shocks created by the pandemic (Lipsy 2022), the country’s economic growth rate remained low among other major advanced economies¹¹. In terms of the level of fiscal measures (as a percentage of GDP) among these economics, Japan’s fiscal packages constitute the third largest after the United States and the United Kingdom (Gornostay and Sarsenbayev 2021). Nonetheless, according to the International Monetary Fund (IMF), Japan’s average forecasted economic growth for the next five years (2022–2026) is 1.3%, lagging way behind others’ average of 2.6%¹².

Kishida’s New Form of Capitalism and the LDP’s Manifesto

Similar to the fiscal relief on the COVID-19, the LDP’s policy stance in the face of the General Election shows the straddling strategy balancing a distribution and conventional supply-side growth strategy. The concept of New Form of Capitalism, according to Prime Minister Kishida, is based on a plan to revitalize the Japanese economy with “a virtuous cycle of growth and distribution¹³.” Instead of “reform” that Abenomics had emphasized for the last nine years, “distribution” has become the key feature of Kishida’s plan. At his administration’s initial step in early October, Kishida established New Capitalism Revitalization Headquarter and floated the idea of increasing the rate of taxation on financial and security transactions from the current flat rate of 20%. This was a strategy to increase Japan’s fiscal revenue to the investment income that has risen among the wealthy Japanese¹⁴.

¹¹ Canada, France, Germany, Italy, Japan, the United Kingdom, and the United States.

¹² IMF, October 2021, “World Economic Outlook Database.”

¹³ Prime Minister Kishida’s first policy speech at the Diet on October 8, 2021, available at: https://www.kantei.go.jp/jp/100_kishida/statement/2021/1008shoshinhyomei.html.

¹⁴ For “Ichioku-en-no kabe (The wall at the ¥100 million income)” discussion, see Nikkei, October 7, 2021, available at: <https://www.nikkei.com/article/DGKKZ076408430X01C21A0EA2000/>

Kishida also promoted a “stakeholder” economy, where firms distribute profits to workers, customers, and subcontractors, and not just to the “shareholders.” He especially focused on the SMEs and proposed tax incentives for the companies that raise the wages for their workers.

Kishida’s thinking on New Form of Capitalism derives its origin from the “National Income Doubling Plan (shotoku baizō keikaku)” of the 1960s led by the then-Prime Minister Ikeda Hayato, the founder of Kōchikai, a leading faction of the LDP that Kishida has headed since 2012¹⁵. Although the policy details of New Form of Capitalism are yet to fully emerge (at the time of the writing), the rise of this new strategy is in reaction to the decades of neoliberal policies in pursuit of economic efficiency following market fundamentalism and deregulation. Concomitantly, this was a way to deflect Abenomics’ shortfalls in terms of the income distribution (Saiki and Frost 2020 inter alia) especially in the face of stagnating wage growth (Vogel 2021). The opinion polls taken just prior to the Lower House Election demonstrated such view as more than 60 percent of those polled responded that Abenomics has to be overhauled¹⁶. Furthermore, inequality for the first time became an important electoral issue as the country faced the pandemic (Lee 2022). In short, Kishida’s strategy in the LDP presidential election was to emphasize distribution and address people’s dissatisfaction with Abenomics and the government’s COVID-19 responses.

Despite the progressive components of the New Form of Capitalism plan at the time of the LDP Party Presidential Election in September 2021, the LDP’s party manifesto shelved such progressive ideas at the time of the October General Election campaign. One direct and obvious reason of this shift is the decline in stock prices in response to Kishida’s capital gain tax increase idea, which was later withdrawn. But this shift was also in line with LDP’s traditional clientelistic supply-side economic growth strategy taken since the rapid

¹⁵ For the summary, see Shimada Haruo “Atarashii shihon shugi no honrai no hōkō o tsuikyūseyo.” Yomiuri Shinbun online, January 31, 2022, available at: <https://www.yomiuri.co.jp/choken/kijironko/ckeconomy/20220128-OYT8T50087/>.

¹⁶ Jiji reports 62 percent (<https://www.jiji.com/jc/article?k=2021101500743&g=pol>), Kyodo reports 68 percent (reported by Reuters: <https://www.reuters.com/article/idJP2021101701000471>).

economic growth period of the late 1950s. The Japanese economy relied heavily on public investment not only to build necessary physical infrastructure devastated after World War II, but also to pump in pork-barrel projects to politically important rural areas and in support of construction contractors (Woodall 1996). Such heavy reliance on public works continued for Japan into the twenty-first century¹⁷. Despite the 1994 electoral reform that structurally reduced the political power of special interest by introducing single-member district votes, the local clientelism and attraction of public works has persisted particularly in the rural areas in Japan (Scheiner 2007). Thus, by dedicating 15 out of its 34-page manifesto to these issues¹⁸, the LDP’s economic plans emphasized “strong economy” and the measures following the National Resilience Plan adopted in the aftermath of the 3/11 triple disaster of earthquake, tsunami, and nuclear plant meltdown of 2011, and laid out under National Land Resilience Basic Law that came into effect in 2013 under the LDP leadership¹⁹.

The rest of the LDP’s manifesto included, in line with Kishida’s initial vision, (re)building a robust middle-class economy with the wage increase, particularly in sectors such as nursing, home- or day-care, and by providing incentives for companies that raise workers’ pay, which partly co-opting the opposition ideas. Meanwhile, the LDP was opposed to any sales tax cut, and in general in support of fiscal discipline. Therefore, Kishida and the LDP manifesto constituted the LDP’s straddling strategy that, the internal politics in the LDP formed the policy agenda that perpetuated the conventional growth strategy through industrial policies, public expenditure, and infrastructure investments, yet it underscored the change from Abenomics by promoting the distributive policies.

¹⁷ Among most countries of the OECD, the ratio of public investment to GDP has slowly declined from 4 to 5 percent in the early 1970s to around 2 percent. Yet, Japan and South Korea have maintained a high ratio above 5 percent in the 2000s (Kohsaka 2007).

¹⁸ See LDP, “reiwa 3nen seiken kōyaku,” available at: https://jimin.jp-east-2.storage.api.nifcloud.com/pdf/manifest/20211018_manifest.pdf.

¹⁹ At the time of the LDP Party Presidential Election, one of Kishida’s opponents, Takaichi Sanae, promoted these ideas.

Economic Policy Trilemma Facing the Political Parties During the Lower House Election

The LDP's straddling strategy exploits the policy space for the opposition parties, especially the CDP-JCP coalition. The distinct priorities taken by the parties demonstrated the trilemma among the three economic goals to demonstrate a credible commitment on their economic policies. The first goal is the economic growth capitalizing on the "old way of business" resorting to the supply-side of producers and large businesses, and catering to the vested economic interests and clientelism through measures such as infrastructure investment, be it green or traditional. The second goal is the emphasis on distribution with various types of hand-outs measures some targeted certain demography such as the poor or unemployed, as well as consumer-focused measures such as time-limited suspension (or reduction) of sales tax. The third and final goal is the fiscal discipline of the central government.

Taking the first two goals, the trade-off between supply-side focused growth strategy and distribution under neoliberalism has been the topic of extensive research in the fields of both economics and political science. In the late 1990s, "permanent austerity" (Pierson 2001), a precondition of policy credibility among the OECD countries, intensified the political conflict between the organized economic interests of businesses and mass public (especially in support of welfare state). Seminal work of Przeworski and Wallerstein (1988, p. 13) argues that "governments face a trade-off between distribution and growth, between equality and efficiency." That is particularly so when there is prominent structural dependence of the state on capitalists since the performance of the economy is the key for the legislators to achieve success in their re-election and maintain their popularity (Swank 1992). In such a context, however, the ideologies of the political parties play an important role in the choice within the trade-off. Generally, the conservative parties adopt supply-side growth strategy by increasing the productivity of capital, while socialist governments tend to depend on distribution to increase the productivity of workers (Boix 1998).

What is different in 2021 from the arguments seen in the existing literature, however,

is the introduction of the third element, which is the prevailing acceptance from voters on the relaxation of fiscal austerity that used to be the pre-conditions of the trade-off. In the twenty-first century under the macroeconomic environment of “secular stagnation” (Summers 2016), and particularly in the aftermath of the 2008 global financial crisis and now the pandemic, the possibility of “helicopter money” (monetized fiscal stimuli) ushered in a new era of (potentially) governments’ free spending without revenue constraints. Furthermore, the governments facing such environment, the challenge is to try to minimize the electoral costs associated with the state of crisis (Breunig and Busemeyer 2012, p. 924). While the traditional trade-off implies redistribution that transfers money from rich to poor, in the world under massive crisis-driven monetary and fiscal expansion, the trade-off between the two goals expands by adding the third dimension of fiscal discipline, leading to the economic policy trilemma²⁰. Therefore, a strategic party could propose to fill in this new political space, by being a traditionally “irresponsible government” and neglecting fiscal discipline, and pursue both supply-side growth and distribution with the risk of inflation. Meanwhile, those parties that insist on fiscal discipline and stick to the two traditional policy dimensions continue to face the trade-off.

Based on this trilemma, we evaluate parties’ manifestos to map their economic policies onto the three goals (Figure 17). Specifically, we examine the parties’ positions on public debt expansion, and introduction of progressive income tax, and corporate tax increases (fiscal discipline); distributive policies such as direct payments to households and sales and income tax reductions (distribution); and deregulation and public investment in a range of areas from renewable energy, digital economy, green innovation to supply chain and infrastructure resilience (supply-side growth strategy). As discussed above, after the Party Presidential Election, the LDP’s manifesto tilted to the growth strategies compared to distributive policies. However, with support from the Kōmeitō, whose electoral campaign promise included

²⁰ It may be true that three economic goals could be achieved at the same time when the economy is supported by the economic boom cycle (See Dore 1994). We consider, however, that the policy stance to pursue all three is impossible to realize and gain voters’ support under the condition which Japanese economy faces persisting structural headwinds of low growth and the pandemic.

direct payment to household, the LDP-Kōmeitō coalition cover wider areas of both growth and distribution policies that narrowed the choice for opposition parties. In addition, despite its emphasis on fiscal discipline, the LDP as the governing party has the power to set the budget ceiling in the face of pandemic. In contrast, the CDP-JCP coalition locates in the narrower area with low score in growth strategy, moderate score in distribution, and high fiscal discipline with progressive tax plan.

Moreover, opposition parties largely emphasized distribution in their electoral campaigns at the expense of fiscal discipline. The CDP, the DPP, and Ishin called for time-limited reduction of sales tax from 10 to 5%, while the JCP demanded its permanent reduction to 5%, and Reiwa called for its abolition. In addition, the JCP, the DPP, and Reiwa also supported issuing new bonds to finance national financial needs. When it comes to direct subsidies to households, all parties except for the LDP proposed these direct payments of hand-outs one way or another including even the LDP's coalition partner Kōmeitō. The DPP called for \$1,000 (¥100,000)-allowance across the board and additional \$1,000 for low-income population, and Ishin proposed introduction of the universal basic income.

When it comes to the balance between supply-side growth and distribution, in contrast to the LDP and Kōmeitō whose focus has been more on the producers, other parties have focused on the consumers. In addition to sales tax cuts and direct subsidies to individuals, the CDP, the JCP, the DPP emphasized support to households. Furthermore, Reiwa and the DFPP also demanded industrial policy and infrastructure investment via fiscal expansion. Meanwhile, most parties on the left of the LDP from the CDP, the JCP to the SDP emphasized the redistributive goal of fiscal policy by demanding more progressive income tax and supporting taxing the wealthy and capital gains more. In contrast, the DPP and Reiwa emphasized the new issuance of government bonds while Ishin mentioned nothing about fiscal management despite that they promote tax cut and fiscal expansion. We evaluate parties' position by scoring policies that are comparable across parties, then we aggregate these scores for three goals, even though some parties may have inconsistencies in their policies

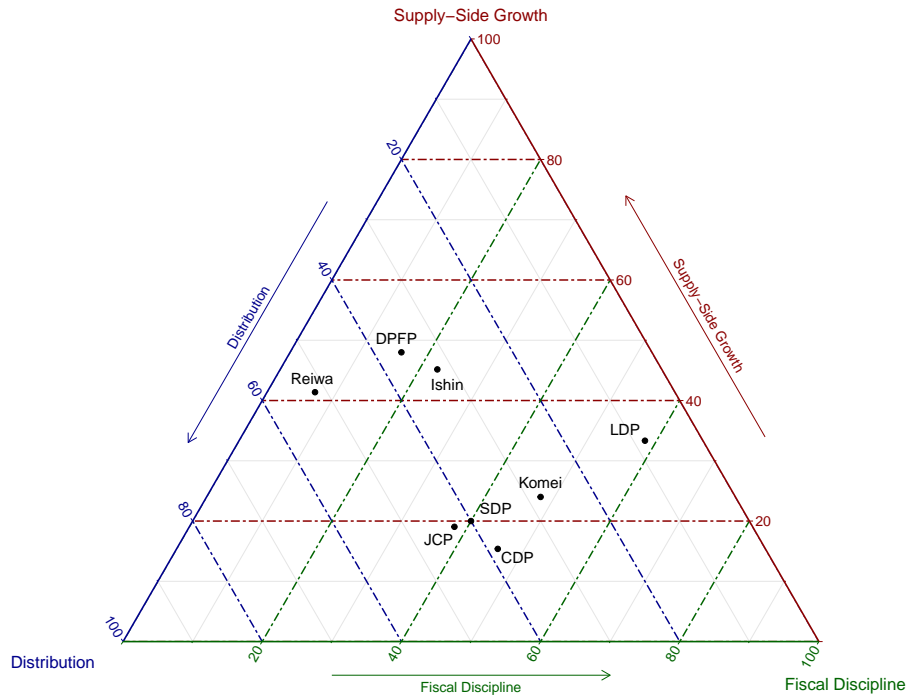


Figure 17: **Party positions in the trilemma: supply-side growth, distribution, and fiscal discipline at the 2021 Lower House Election**

Notes: Three dimensions of policy choice. We decompose the list of policies in parties’ manifestos into three categories: “Supply-Side Growth” based on public infrastructure investments, and deregulation and tax cut on manufacturing and other suppliers; “Distribution” based on direct household subsidies, and income and consumption tax cut; “Fiscal Discipline” based on tax increases, and issue of government bonds. The components of policy categories must sum to 100. Sources The details of the data and scores referred to in this figure are available at the author’s GitHub repository (<https://github.com/kenyamano/JapanDecides2021>). Coded by the authors based on each party’s manifesto

and goals, mapping onto the ternary plot in Figure 17.

Although the economic policy was not the only issue of competition on which the 2021 Lower House Election was fought over, we see a pattern of favorable electoral outcome for the parties located on the top-left area in the ternary plot (Figure 17), namely the DPP (the number of seats gained/lost:+3), Ishin (+30), and Reiwa (+3). These were the parties that straddled between distribution and supply-side growth strategies at the expense of fiscal

discipline. Meanwhile, those that neglected the growth strategy and positioned themselves in the bottom-middle between distribution and fiscal discipline such as the CDP (13), the JCP (2), and the SDP (0) did not do so well. Although the LDP (13) and Kōmeitō (2) lost some seats emphasizing growth with fiscal discipline (bottom right), the coalition was able to maintain the Lower House majority. The LDP's economic strategy in the middle of the pandemic led to its electoral success in 2021, but the visible electoral gains made by the parties that neglected fiscal discipline as in the case of Ishin foreshadows the future of economic policy priorities in Japan.

Conclusion

In this chapter, we examined the economic policies and strategies among the political parties in the face of 2021 Lower House Election as the Japanese economy faced the COVID-19 pandemic. Thanks to the macroeconomic actions taken under Abenomics and under the pandemic economic challenges, dramatic fiscal expansion was possible in 2020 and 2021. This shifted the conventional trade-off between production/supply-oriented and distribution-oriented economic policy to an economic policy trilemma including the third goal of a choice regarding fiscal discipline. In the context of the 2021 Lower House Election, the LDP-Kōmeitō coalition opted for straddling strategy to incorporate the supply-side growth policy but still with emphasis on distribution to households. This LDP economic strategy, in contrast to the opposition parties that emphasized either public debt expansion (DPP, Ishin, and Reiwa) or redistribution (CDP, JCP, and SDP), led to the LDP to win the majority in the election.

All in all, as mentioned above in the IMF's forecast, Japan's economic growth in the aftermath of the pandemic does not seem very likely. The third arrow of Abenomics, "the growth strategy through structural reform," aimed the Japanese economy to escape from the low growth equilibrium, but the progress was mixed: while the liberalization processes in the area of trade, agriculture, and corporate governance achieved significant progress, the

reforms for the gender gap, stagnated wage growth and low productivity have fallen short (Lechevalier and Monfort 2017, Katada and Cheung 2018, Kushida 2018, Hoshi and Lipsky 2021).

Notwithstanding, the economic policies proposed by the LDP before the elections suggest continuity of such landscape. The concern is financial absorption capacity in the face of insufficient structural reform, which continues to loom large in the choice of LDP's economic policy focusing on the supply-side. When Japan's rigid economic structure limits profitable investment opportunities, pouring in massive funds does not lead to growth. In addition, bureaucracy's implementation capacity and lack of digitalization have exacerbated this challenge. Even on the consumer demand-side, the criticism was that a large portion of the direct hand-outs did not lead to consumption by the recipients as many opted to save the money for the rainier days. Hence, these institutional and structural hurdles have diminished the growth impact of the fiscal stimulus and the economic strategies, which underscores the continued need for structural reform and innovation to unleash Japan's growth potential. Meanwhile, the electoral support for the growth-oriented expansionary fiscal policy could shape the fiscal stance of the ruling coalition at the expense of fiscal discipline in the future.

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