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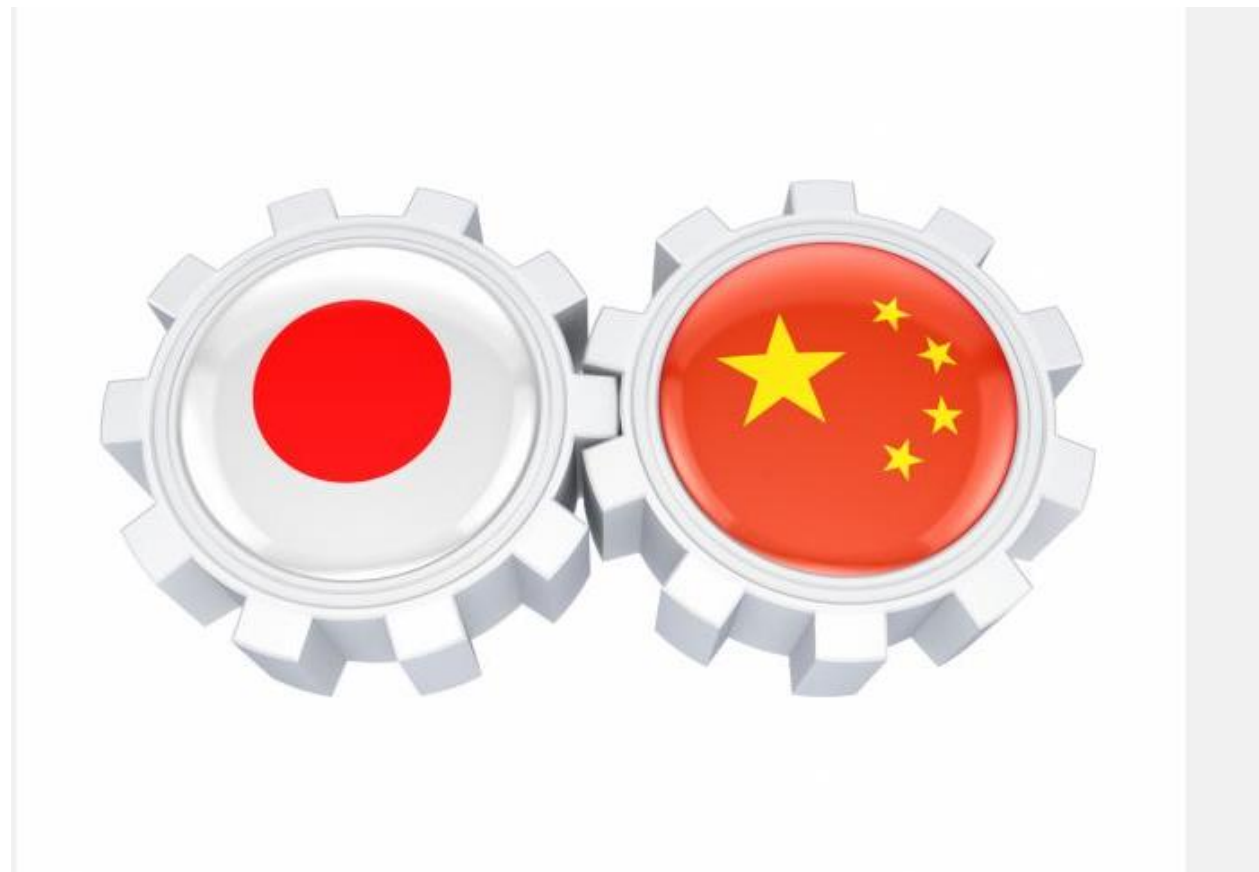
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## The pains of economic reforms in China and Japan

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*Asia's two biggest economies face up to their most difficult challenges*

When China concluded the Third Plenum of the 18th Communist Party of China (CPC) Central Committee in November 2013, the resulting call by CPC leaders to “let the market play a decisive role in allocation of resources” got the most attention from China observers. Some of them view this as an acknowledgement that the heretofore model of economic development – government-led exports and manufacturing that ultimately resulted in unproductive over-investment – must give way to more fundamentally sound methods of economic growth.

According to former World Bank president, **Robert Zoellick**, much of what was announced at the Third Plenum could have been attributed to the work of the financial body.

“When I was at the World Bank, some Chinese officials suggested to me that I should propose to their superiors the idea of a report to look at these structural changes,” recalls Zoellick about the document which ultimately became the China 2030 report. “If you look at that document, you’ll see that it’s raw material for a lot of what came out of the Third Plenum. The challenge now is the sequencing and pursuit of those reforms.”

“From the discussions I had with Chinese reformers, they feel the country is at a different stage. I think Chinese President Xi Jinping’s historical goal is to have an accomplishment for China like Mao Zedong did in setting up the Republic, and Deng Xiaoping did in opening up the economy.”

## **It’s a Xi change**

Zoellick, who was the speaker at the recent Singapore Management University Presidential Distinguished Lecture Series event, “Perspectives and Prospects for the Contemporary Global Economy through the Eyes of Asia”, believes Xi would find it difficult to push through his reforms.

“In the past, you could break the system and rebuild it; now it’s just too complicated. A lot of reforms will start out taking the form of changes in governance, or modernisation of structures.

“For example: the issue of revenues and expenditure between the provinces and the central government. Because the central government controls the flow of money, when the local authorities need extra cash, they take land – that’s a socially destabilising issue. Then there are the hukou system and environment issues.” Hukou is China’s household registry system to manage rural-urban immigration, among other things.

Over the past 30 years, leaders at various levels had a clear objective: growth. Now they have to deal with multiple objectives.

“This is why Xi Jinping has consolidated power more quickly than most China observers have expected, with the seven-member Standing Committee of which he is the dominant figure, and moving to the chair of the Central Military Commission much sooner than (former President) Hu Jintao did. This is combined with the anti-corruption campaign. All this suggests that Xi will push for reforms, but it’s no easy task.”

*"In China, the prime concern is the preservation of the CPC. For Japanese Prime Minister Abe, it's all about restoring Japan's influence."*

Indeed, the anti-corruption campaign is causing consternation within the CPC leadership. Former President Jiang Zemin urged in March 2014 for Xi to rein in the drive to cut out graft, which has led to more than 30 suicides since the beginning of 2013.

In June, Xu Caihou, a former top army general, became the most senior figure to be hauled up to face bribery charges; he is alleged to have taken money and property for promotions. Jiang, seeking to contain political fallout, warned that “the footprint of this anti-corruption campaign cannot get too big”.

## **Abe's arrows**

It is in this context that China's recent territorial disputes may be viewed. As Xi risks losing support amongst China's elite by stepping on too many toes, popular support is drummed up through nationalistic fervour against neighbour and old foe, Japan. Interestingly, Japanese Prime Minister Shinzo Abe is using China in a similar way to revive the moribund Japanese economy.

“Japan's developments in recent years have come from shocks: The Black Ships of the 16th to 19th centuries; World War II; and the oil shock of the 1970s. What Prime Minister Abe is trying to do is take the rise of China and the potential dangers for Japan and congeal it into another force to change the Japanese system. In China, the prime concern is the preservation of the CPC. For Prime Minister Abe, he's all about restoring Japan's influence.”

The first two arrows of “Abenomics” – a huge fiscal stimulus programme along with monetary easing – achieved eye-catching success, most notably the Nikkei 225 index that has gained about 50 percent since the start of 2013.

Abe tried firing the so-called third arrow in June 2013 to fix structural problems, but was met with resistance by various lobbies. One major obstacle is Japan's system of lifetime employment that hampers productivity and prevents young Japanese from gaining full-time employment, which touches on the broader issue of demographics.

"Japan shrinks by about 250,000 people every year. Will the country be more open to immigrants?" Zoellick asks while pointing out the lack of female participation in the workforce.

"From my 25 years' experience of working with Japanese on these issues, I'm a bit skeptical but I'm hopeful. The key obstacle is this: 'It's a comfortable society. It's working pretty well; why should we change?'"

## **Globalisation: Equal opportunities, unequal outcomes?**

Japan is one of the few developed countries that have been relatively untouched by globalisation. Foreigners make up just two percent of the resident population despite Japan accounting for eight percent of global GDP.

Compared to countries such as Singapore or the United States, where the economy is more open but the income disparity is much higher, Japan is relatively egalitarian. When asked about his thoughts on globalisation and its effects of income inequality, Zoellick provided a big-picture answer.

"Let's look at this globally. If you look at poverty worldwide, the last decade has been a great reducer of poverty. A big part of that has been globalisation, but it does put pressure on the less skilled in developed countries."

"One of the ironies that I found while working in the field of development is that by opening up the markets in the United States to create more opportunities for poor people in Vietnam and China etc, it puts pressure on poor people in the country.

“Could there be a better policy to prevent that development? Can the status quo be preserved in the United States? Or should there be another policy to encourage the dynamism that has taken 600 million people out of poverty in China, while helping the United States to continue climbing up the ladder at the same time?”

“I am interested in equality of opportunity, not equality of outcome,” he emphasises.