

Labor Market Reform under Abenomics and Productivity

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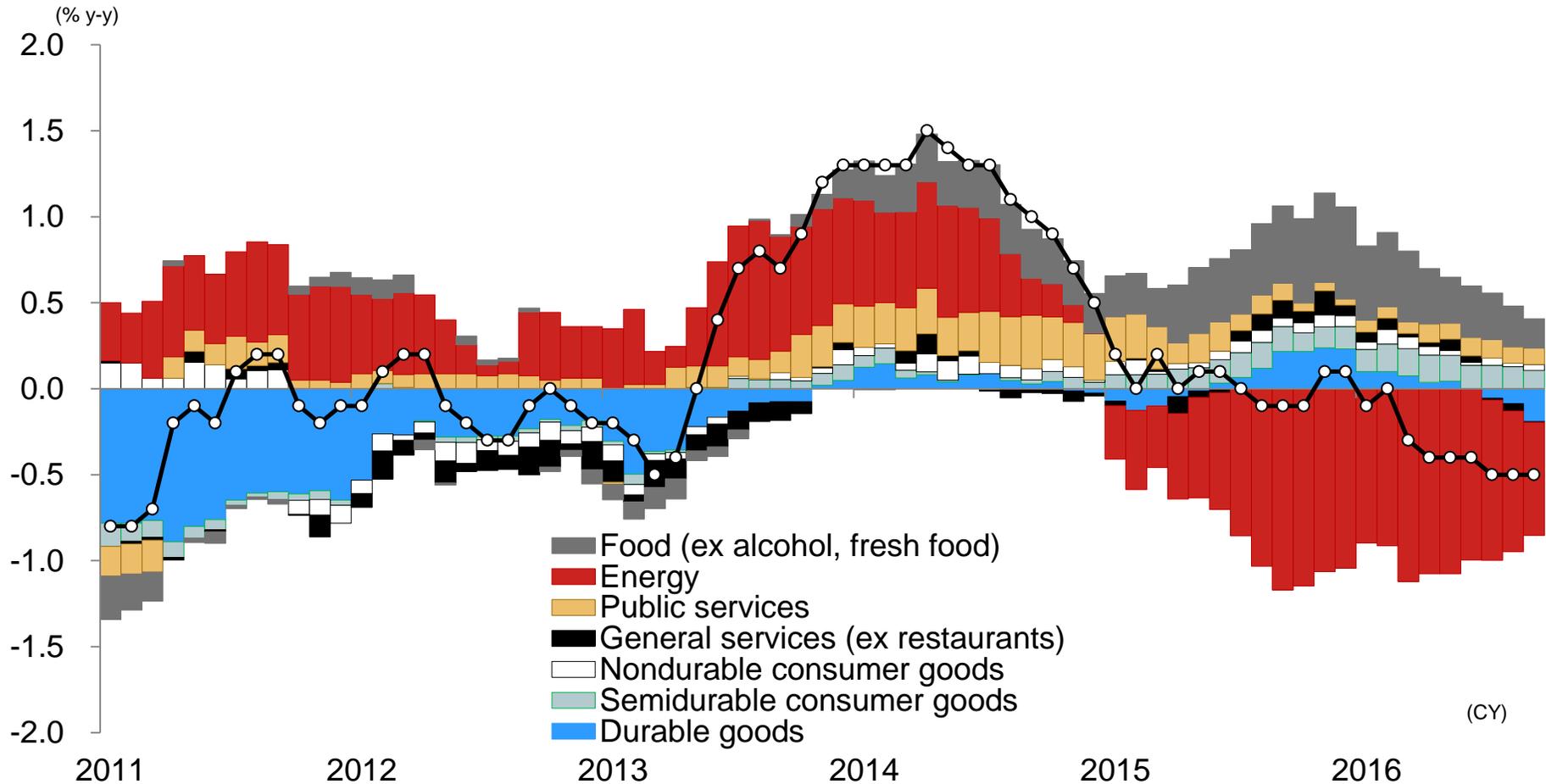
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- Introduction - what Abenomics achieved in general
- What Abenomics achieved in terms of labor market
- The remaining tasks and challenges
- The solutions that Abenomics will provide for the remaining labor market issues
- The assessment of the policy in terms of productivity, in particular

■ Growth was back, no longer deflation, but 2% inflation target yet to be achieved...

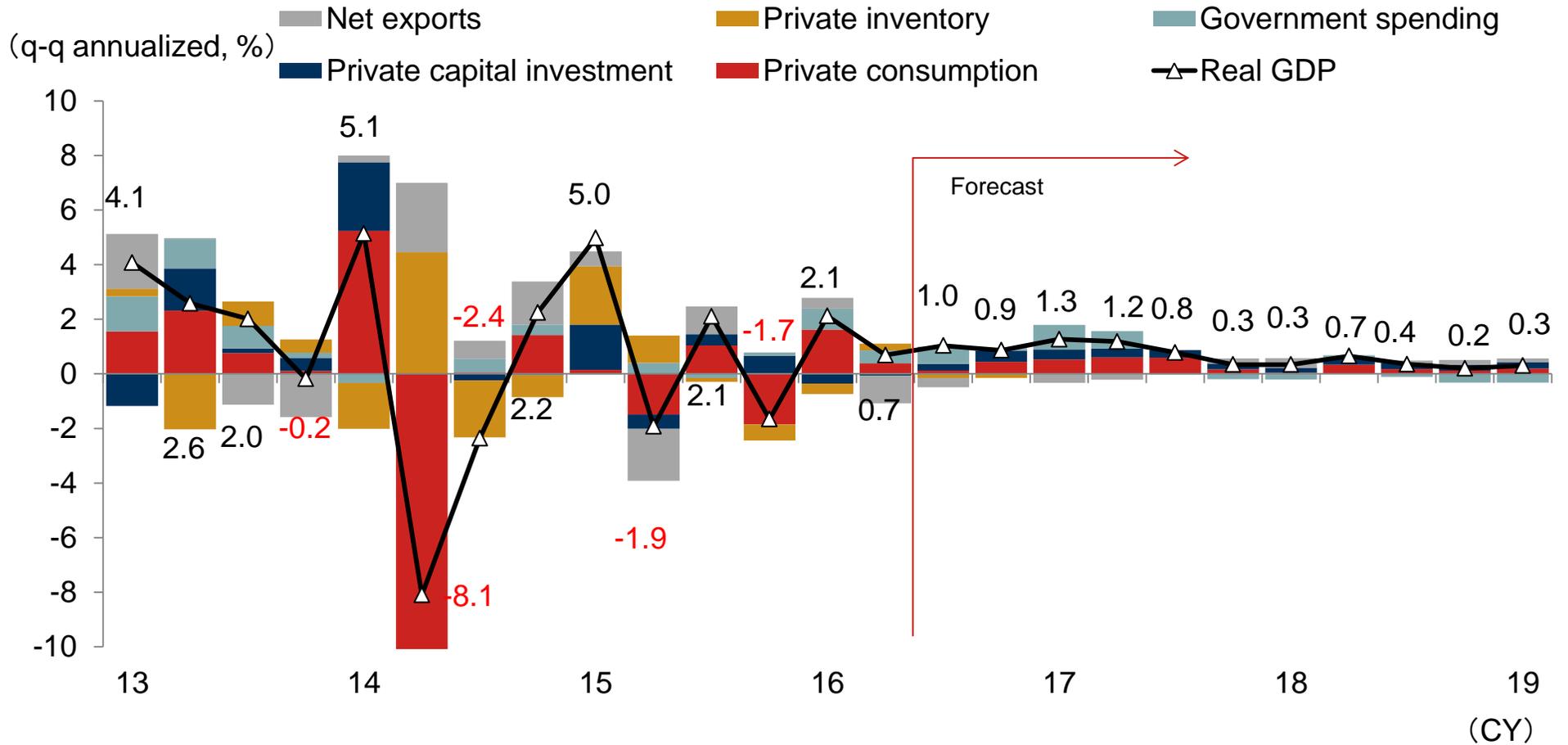
Nationwide core CPI inflation and its decomposition



Source: Nomura, based on Ministry of Internal Affairs and Communications data.

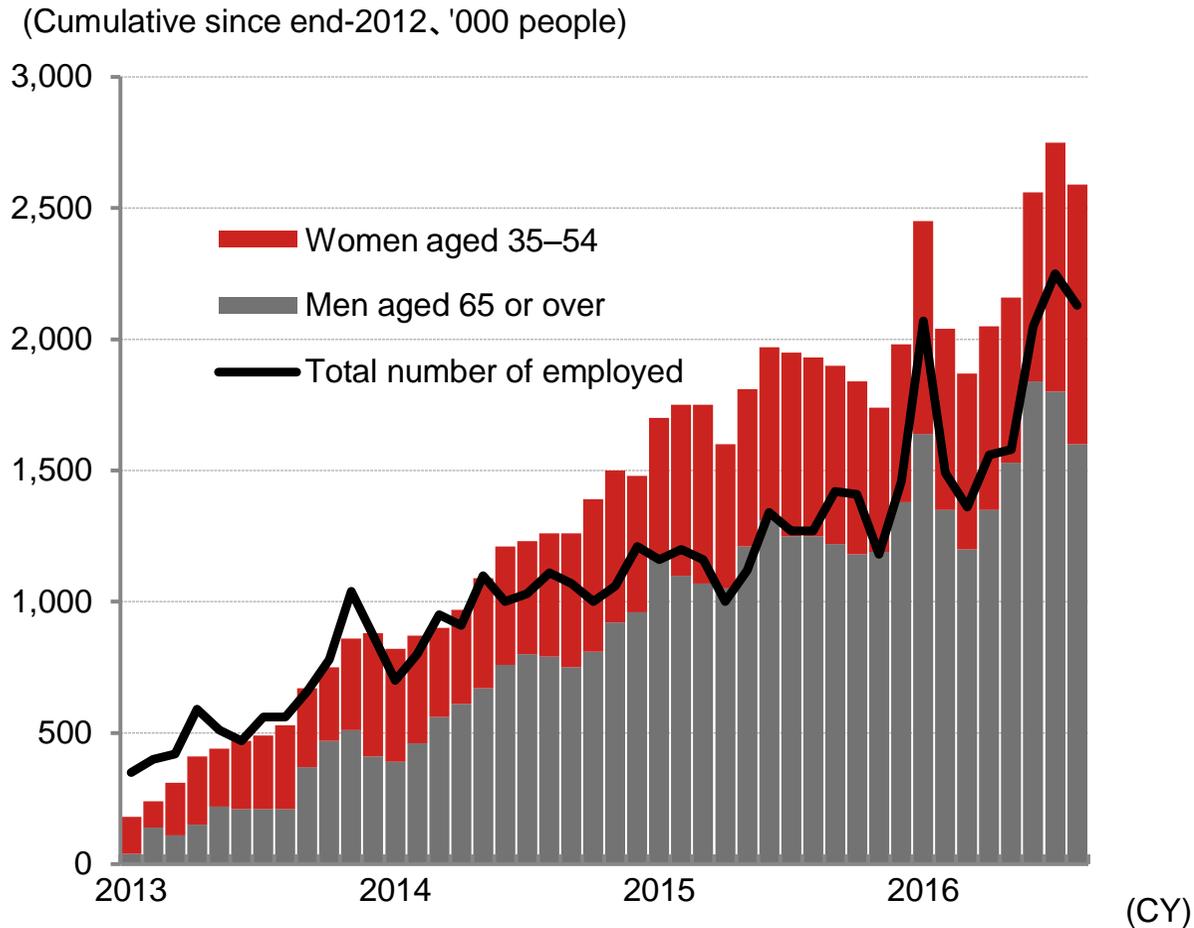
■ Real growth is likely to stay stagnant for a moment...

Real GDP growth forecast and a breakdown by demand components



Achievement of Abenomics in the past four years in terms of labor market

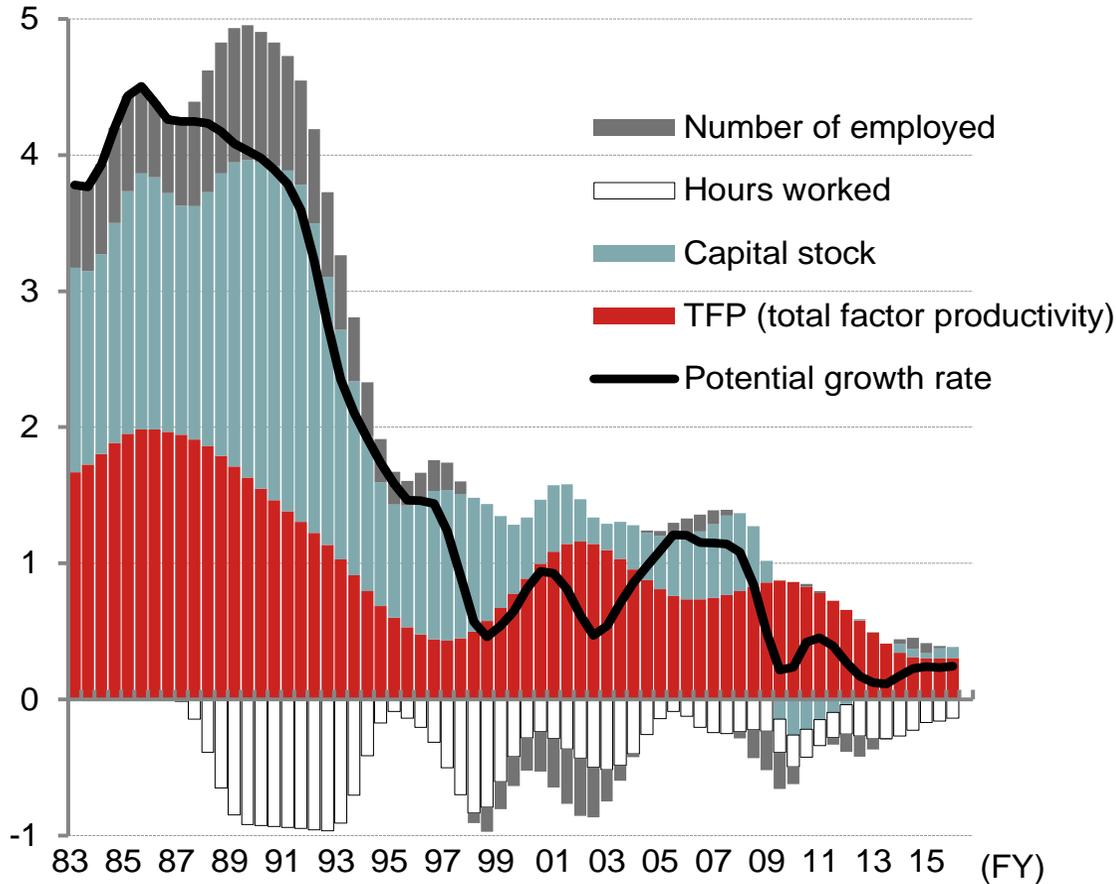
Number of people in employment since end-2012 (cumulative change)



Increasing number of employed sustained the potential growth

Japan's potential growth rate (BOJ estimate) and its contributing factors

(y-y, contribution, %)



An elevated concern for inflation might bring female and elder people into labor market

Household inflation expectations

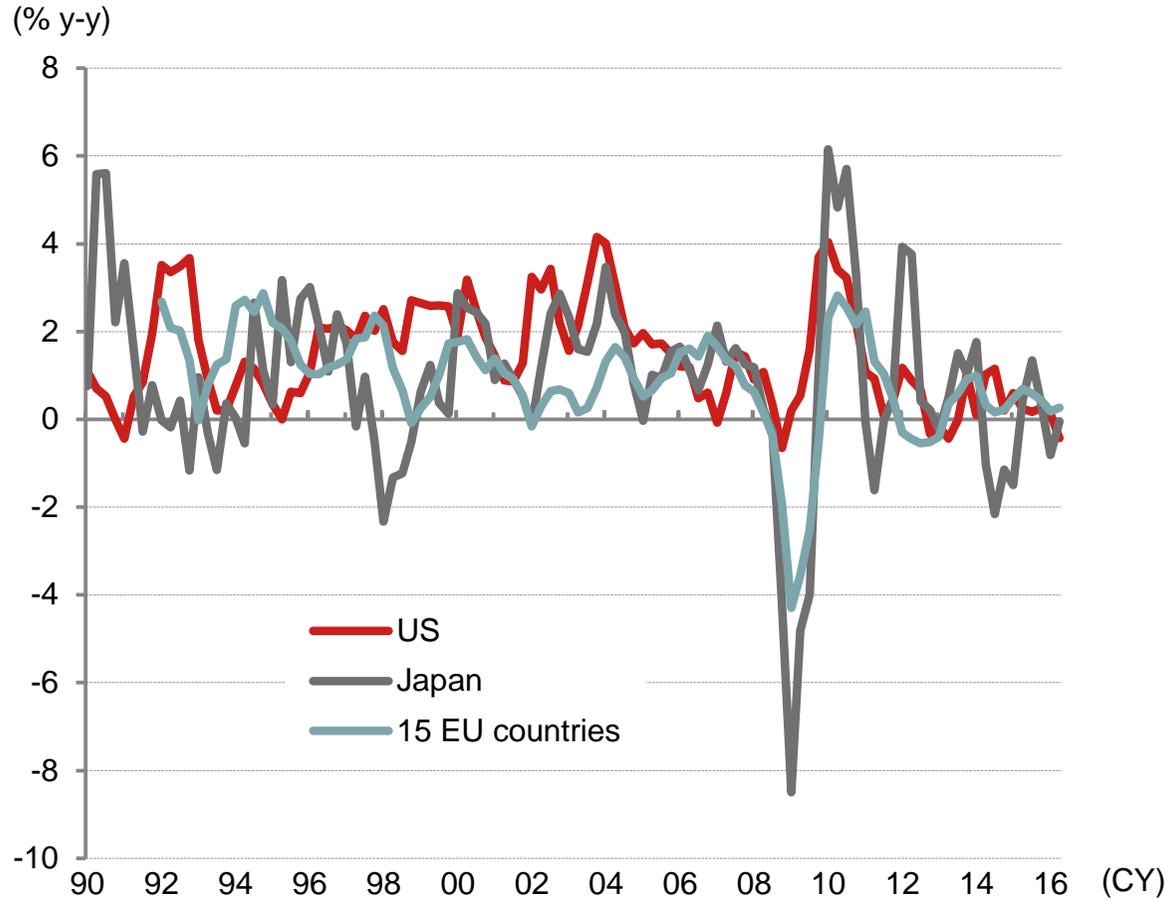
(annualized, %)



Note: Weighted average of Consumer Confidence Survey data on household inflation expectations (all-household basis)
Source: Nomura, based on Cabinet Office data.

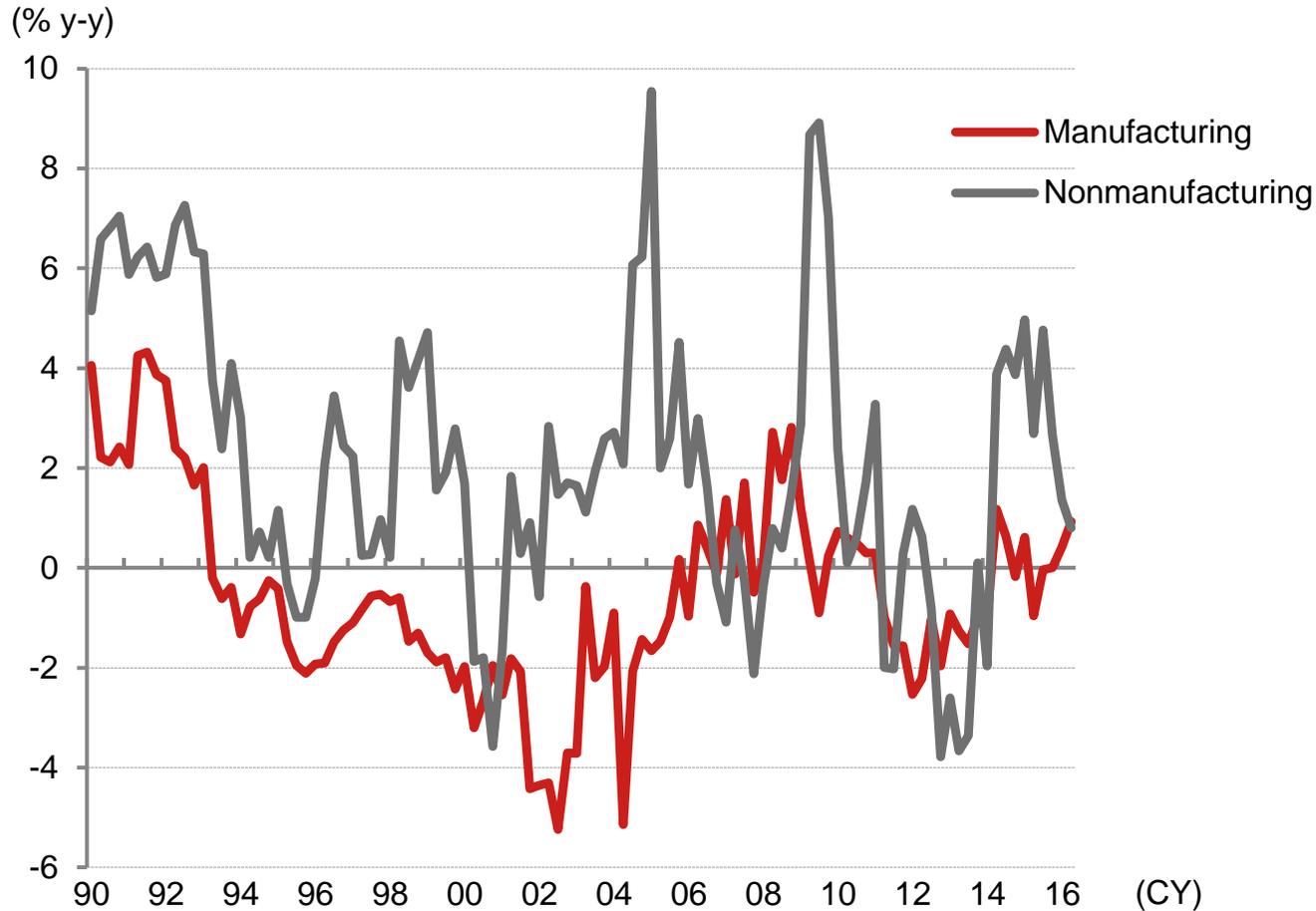
A diminishing rate of productivity – Japan is not a exception

International comparison of labor productivity (OECD basis)



The increase in the number of employed was concentrated in non-manufacturing industries

Change in number of employees by industry

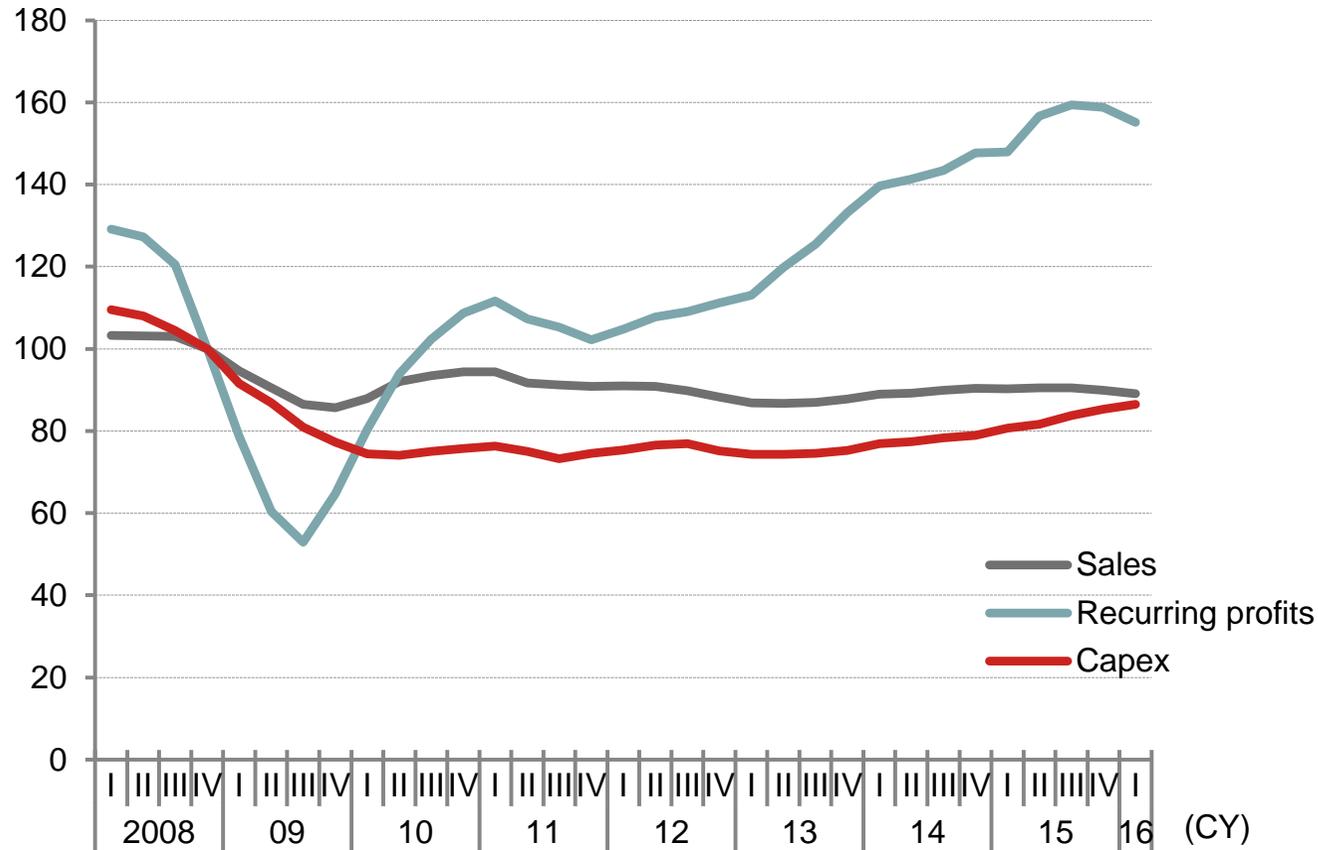


Note: The data are for companies capitalized at ¥100mn or more in Financial Statements Statistics of Corporations.
Source: Nomura, based on MOF data

A stagnant corporate capital expenditure despite the significant recovery in corporate profits

Japanese companies' sales, recurring profits, and capex

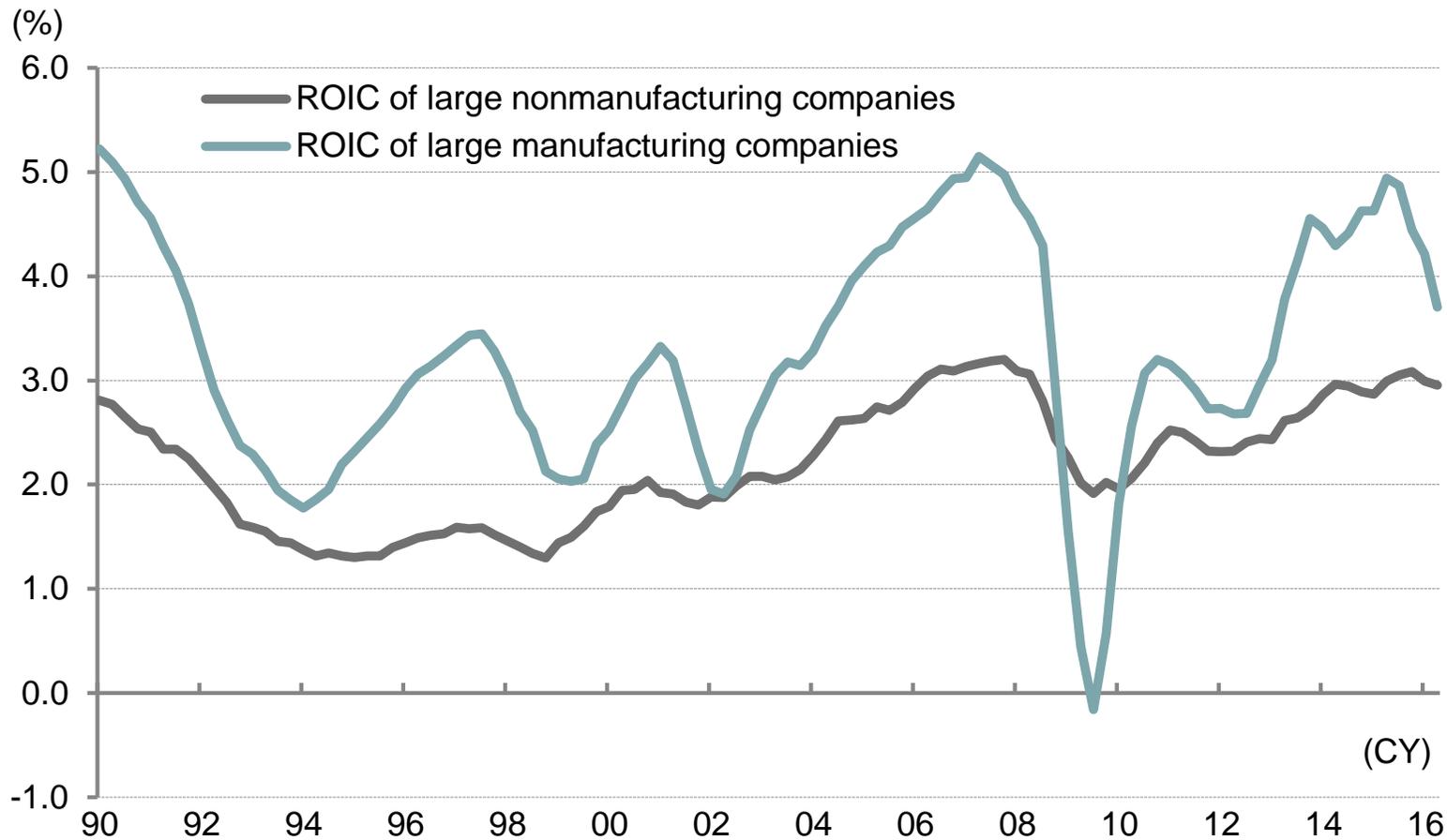
(2008 avg = 100)



Note: The data are for companies of all sizes and in all industries in Financial Statements Statistics of Corporations.
Source: Nomura, based on MOF data

Capital efficiency and asset efficiency have seen an underlying improvement

ROIC by sector



Note: The data are for companies capitalized at ¥1.0bn or more in Financial Statements Statistics of Corporations.
Source: Nomura, based on MOF data

-Efforts to increase labor inputs

- Efforts to adhere to the principle of "an equal wage for an equal job" by bringing the wages of nonregular employees, which compare less favorably with those of regular workers than in other countries, into line with those of regular employees, thereby removing a disincentive for them to participate in the labor force.
- Efforts to reduce nonparticipation in the labor force as a result of inadequate childcare and long-term care.
- Efforts as part of its "working practice reforms," particularly to reduce the long working hours of regular male employees and remove impediments to the participation of women in the labor force.
- Efforts to correct any tax distortions, such as the existing married person's allowance, which act as a disincentive to women to participate in the labor force.

Barriers for increasing labor inputs

- **Still constrained by the desire to respect traditional Japanese employment practices and the traditional family hierarchy**

The government's desire to reform Japan's labor market while respecting traditional Japanese employment practices will inevitably restrict the ability of Japanese companies to make personnel expenses a variable cost.

The abolition of the existing married person's allowance and the introduction of a new allowance aimed at encouraging women to participate in the labor force is likely not only to be opposed by MOF, which is concerned about the loss of tax revenue, but also to face stiff resistance from conservatives within the ruling coalition who want to maintain the traditional family hierarchy.

- **Question: whether the Japanese on their own and Japan's hidden labor resources as implied by the name of the government's plan to mobilize them will be enough to offset the structural decline in Japan's labor force**

Although the Abe administration has begun to discuss whether to allow immigrants and foreign workers to enter the country, we think it is unlikely that traditional very cautious and conservative attitudes toward immigrant workers are going to change significantly, at least in the short term.

- Efforts (under the banner of a "fourth industrial revolution") to speed up technological innovation in the fields of IoT, big data, and artificial intelligence, thereby achieving efficiencies in production processes.
- Efforts to make full use of private-sector potential by means of deregulation and institutional reform.
- Policies to create bigger markets in and increase the competitiveness of individual industries such as farming, fisheries, and forestry and tourism, especially in combination with efforts to revitalize the regions.

The cases for and against enhancing productivity

- **The Japanese economy and Japanese companies, facing structural labor shortages as a result of demographics, will have no choice but to speed up innovation to enhance productivity.**

However...

by virtue of the fact that the use of technological innovation to raise productivity is labor-saving, we see it as an alternative to the use of higher labor inputs to raise Japan's potential growth rate.

The ideal way to raise Japan's potential growth rate would be to increase investment in line with the increase in demand, thereby creating new job opportunities as efficiently as possible.

- **In this regard, we think that the Abe administration still has some way to go to carry out the deregulation needed to create new demand and industries. As well as encouraging investment in particular industries it has identified, the government urgently needs to remove regulatory impediments (so-called bedrock regulations) to the kind of entrepreneurial innovation that creates demand.**