

Trials of a superhero

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The ordeals that lie ahead for Japan's prime minister and his bold economic experiment

Shinzo Abe, Japan's prime minister, reminds the people who voted for him of a hero from a legend. His programme for the economy, known as "Abenomics", has made him unusually popular. Mr Abe has promised to slay the monster of deflation, to shatter the bedrock of excessive regulation and to kiss Japan's stagnant economy back into life. But 2014 will be a year of reckoning. A series of trials will reveal whether Mr Abe really is a fairy-tale prince, or just another political frog.

His most fearsome test will be to raise the consumption tax, Japan's version of value-added tax. Only one politician before Mr Abe has ever dared to increase it, so it remains, at 5%, among the lowest in the rich world. He will push it up to 8% in the spring. There seems to be little alternative since large cuts to social spending are for now politically infeasible. Japan badly needs to get a grip on its borrowing. Having passed the ¥1 quadrillion (\$10.3 trillion) mark in 2013, in 2014 the country's giant debt will gobble up a record ¥25 trillion in interest costs alone.

The sales-tax increase could spell doom for Abenomics. It is likely to cause Japan's economy to contract for a quarter, as people who rushed to spend ahead of the increase guard their cash afterwards. The last time the tax was raised, in 1997, shoppers took fright, and the economy suffered a long stagnation. A crisis in financial markets in the region at the time did nothing to help. Mr Abe will brandish a large fiscal stimulus to try to counter the dampening effect. But if the optimists are right, and the country's upbeat mood continues, growth will pick up again.

That revival could quickly fade if Mr Abe does not measure up to the year's second big trial. So far he has avoided the most daunting task of Abenomics, which is to deregulate the economy and bring about long-overdue structural reform. His excuse was an election for the upper house of the Diet, Japan's parliament, in 2013. Mr Abe's Liberal Democratic Party (LDP) persuaded him not to alarm anti-reform vested interests just before the poll, which it won easily.

Seeking a Goldilocks economy

The year ahead, by comparison, will be calm on the political front. There are no national elections. The LDP now dominates both halves of the Diet in coalition with its partner, New Komeito, a Buddhist-supported party. That means no further excuses. In the coming year's sessions of parliament, Mr Abe is expected largely to finish the job of passing new laws to enact real reform. If he has not managed it towards the close of 2014, disappointed foreign investors may flee, meaning the stockmarket could prove volatile. The bond market, too, might react.

By the end of the year the Bank of Japan's radical monetary experiment will be almost complete. It should be clear whether or not Mr Abe's handpicked central banker, Haruhiko Kuroda, can banish deflation. His deadline to conjure up inflation of at least 2% arrives in

the spring of 2015. The betting is that he will succeed in generating price rises, but of slightly less than 2% (see chart). Thanks chiefly to the rising cost of imported energy and food, inflation is starting to appear. But the Bank of Japan's bold monetary gambit also depends on Mr Abe improving the fiscal position and achieving real structural reform.

Tense relations with Japan's neighbours badly need to improve. Instead, they will be pulled in opposing directions. A staunch nationalist, Mr Abe will seek to reach out to China and South Korea, as he did when prime minister in 2006-07. He will try hard to secure the first summit meetings with Xi Jinping, China's president, and with Park Geun-hye, South Korea's leader.

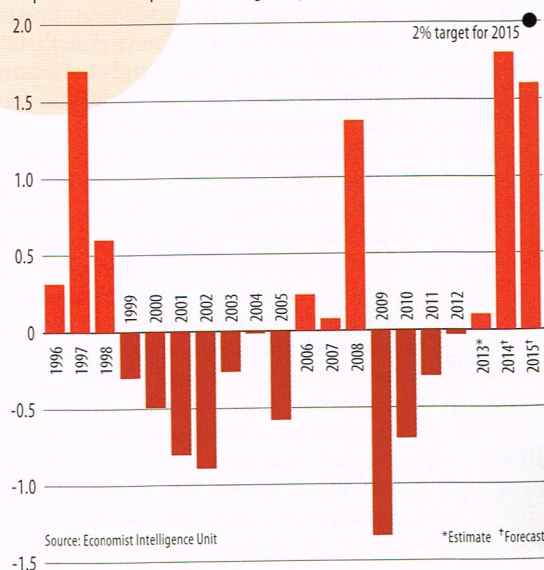
But confrontations over a disputed group of islands in the East China Sea will undermine overtures to China (see "A long winter", in this section). The government has said it may station "public officials", a category that includes its armed forces, on the Senkaku islands (known in China as the Diaoyu). That would badly worsen relations. Meanwhile, Mr Abe will push through a plan to shift Japan away from its post-war

pacifism. In 2014 he may well succeed in lifting a self-imposed ban on collective self-defence. Japan's armed forces would be able to come to the aid of an ally—for instance, America—if it were attacked. Its neighbours will sound the alarm at what they will portray as a revival of Japanese military expansionism.

There is a slight chance that an able opposition to the LDP and to Mr Abe will emerge during the year. After a crushing defeat in the upper-house election in 2013, the Democratic Party of Japan, the LDP's chief rival, is agonising over its future. Shifting alliances and splits may lead to a revitalised new force in politics. But it will be hard to distract voters from the progress of Abenomics, and the coming climax of the tale. ■

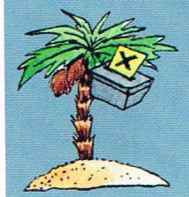
Japan rising

Japan's consumer prices, % change on previous year



2014 IN BRIEF

Fiji holds its first elections since a military coup in 2006



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