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**THE CHALLENGES OF ASIA IN THE NEAR FUTURE
AND THE COOPERATION WITH PORTUGAL**

**OS DESAFIOS DA ÁSIA NUM FUTURO PRÓXIMO
E A COOPERAÇÃO COM PORTUGAL**

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There are various dimensions to talk about Japan's economy, especially when it comes to do with its relationship with Asia. Today, I would like to start with the deflation that Japan has been experiencing over the past 30 years. This trend is the unique case among OECD member countries. In particular, from 1995 to 2021, negative inflation (which means deflation) was observed in 15 years. During the said period, even when positive inflation rates had occurred, its rate was near zero, and only three years exceeded 1%. In fact, this deflation reflects one aspect of the impacts of the expansion of economic globalization. The period of deflation in Japan's economy roughly coincides with the globalization trend that began in earnest after the end of the Cold War. Globalization has brought an unprecedentedly rapid and extensive movement of goods, money, and people. As a free-trade-system believer, Japan has promoted free trade in both multi and bi-lateral contexts. The essence of economic globalization is that free competition arises in search of suitable locations with lower costs. From the consumer's point of view, Japanese citizens enjoy a variety of products imported from various locations around the world at almost lowest prices. As the result, there is no reason why general domestic prices should not be deflationary. In terms of production, Japanese companies expanded their operations to low-cost locations, and built systems to produce good products at lower prices by introducing Japanese technology to the local inexpensive labour force. As represented by a word "kaizen" (improvement) activities, Japanese producers vigorously pursue efficiency. This has extended beyond borders, and elaborated supply chains were established first in East Asia, where products have been manufactured effectively in locations with a comparative advantage and then transferred to the next process. Today, the connectivity in production and distribution has become a global network, connecting the entire Asian region and other parts of the world. In this process, new challenges arose, such as the hollowing out of industries in Japan and the growing Chinese and Korean companies, as our competitors, to which Japan used to provide technical guidance. Nevertheless, Japan did not change its direction for globalization, and has continued to compete at a high level as one of the major economic players in the era of globalization. Even before the globalization, Japan, as the first Asian developed country, actively provided ODAs (Official Development Assistances) to other underdeveloped countries at the time, in order to construct basic social infrastructures such as major roads, bridges, water supply, electricity, healthcare, and education, through grant aid, technical assistance, and extremely low-interest yen loans. I must say that this was highly

effective investment, and provided the basis for the economic prosperity of each recipient country in the years to come.

However, continuous deflation is not all good things. Just as I mentioned that Japan's deflationary record is unique among OECD countries, another unique point is that wages have not risen nearly as much over the past 30 years. In an environment of continuously declining living costs, Japanese workers may have had little incentive to demand higher wages. Some experts point out to the increase in the number of non-regular and temporary workers. However, despite the benefits of globalization, most of the profits and a huge amount of gains has been accumulated as retained earnings in the companies. As a matter of fact, Corporate Japan's overseas retained earnings is one of the highest level in the world. Although such retained earnings are a sound management resource for each company to prepare for risks, in my personal opinion, more than a certain amount should have been used for salary increases for workers, dividends to shareholders, and reinvestment to enhance their own business because if only saved and retained, and not utilized enough it is same as a 'dead money'.

Although it was surpassed by China in 2010, Japan is currently the third-largest economy in the world. However, since wages and incomes have barely increased, Japan's per capita income has fallen from the world's highest level in the first half of the 1990s to 28th in 2009 (29th place is Italy). As economists teach that the rate of economic growth is proportional to the rate of increase in real wages, Japan's GDP has remained almost flat over the past 30 years. This period of economic stagnation is referred as the 'lost 30 years', which is used widely among Japanese.

The invasion of Ukraine by Russia has caused energy and food prices to skyrocket, bringing hardships for households and businesses around the world, but even before the war, prices of certain commodities and strategic goods such as semiconductors were rising due to the supply-demand imbalances and stagnant supply chains caused by COVID19. In Japan, where long-standing deflation makes it difficult to pass on rising costs to prices, sellers often resort to 'stealth price increases' as a desperate measure, in which sellers keep prices unchanged while reducing the product's volume. Even after the invasion of Ukraine, passing on rising costs to prices are not advancing, except fuel and food sector such as cereals. Therefore, many people expect that Japanese inflation rate of 2022 will be 2 or 3 %. So, the government decided to continue to take easing monetary policy not like United States FBR decision.

Let's go back to about 10 years ago. 'Abenomics' was a policy aimed at overcoming the deflationary economy in which lives of Japanese people were not improving even though they worked diligently. Abenomics consists of three arrows: 1) Bold monetary policy 2) Flexible fiscal policy, and 3) growth strategy to stimulate private investment. The bold monetary policy was promoted by the strong initiative of Mr. Kuroda, the governor of Bank of Japan, who called it 'extraordinary monetary easing' and indeed the enormous liquidity was supplied to

the market. About the flexible fiscal policy, it received mixed reviews. Although the government itself stimulated demand by investing the amount of approximately 10 trillion yen (one hundred billion dollar). It was not a simple matter to say that the policy was really flexible. Behind this scene, there was a tug-of-war between the proactive and the disciplined factions in the Japanese political and academic groups, and the Abe administration managed to achieve this second arrow by raising the consumption tax rate twice, as well as by including the objective of primary balance in its policy outline. The growth strategy to stimulate private investment is halfway through. Compared to the economic situation under the administration of Democratic Party of Japan (DPJ) prior to December 2012, Abenomics has achieved the following tangible results; the number of bankruptcies reached the lowest level in more than 20 years at that time, and the Nikkei Stock Average doubled.

Firstly, on monetary policy, the tolerance level for accumulated budget deficit becomes higher than in other countries, especially in a country like Japan with the right to issue its own currency, and in the economic systems, where over 90% of government bonds are owned by Japanese Central Bank and other banking institutes and individual Japanese, and not by foreign investors. Professor, Joseph Stiglitz said in the past that Japanese government deficit is covered by Japanese government bonds owned by Japanese Central Bank. For that reason, IMF also always accuses the management of Japanese government. And OECD always gives alarms on the level of accumulated budget deficit, which is as high as twice as Japanese total GDP. Secondly, on fiscal policy, twice raising consumer tax (VAT) discouraged demand side very much. PM Abe tried hard to fill up GDP gap but he failed to do so.

Prime Minister SUGA, who succeeded PM Abe, was expected to be a good political professional. In principle, he succeeded abenomics, and especially put importance on its 3 pillars. But his popularity dropped rapidly due to the pandemic situation, which was exacerbated by the outbreak of the Delta variant at the time, right before the Tokyo Olympic Games. If he had stayed on instead of leaving office prematurely after only about a year, he would have been able to reform drastically the healthcare system, overcoming various resistance, beside the reform on the cell phone carrier business, which he had already achieved.

As for the current Prime Minister Kishida's policies, we can refer to the 'Basic Policy on Economic and Fiscal Management and Reform 2022' and the 'Grand Design and Action Plan for New Capitalism' approved by the Cabinet in June of this year, two weeks ago from today. The budget discussion in parliament will follow later after this September. The document was the outcome of discussion between proactive budgetary group and disciplined group among the ruling party (Liberal Democratic Party (LDP)). Since they complement and resonate with each other, they can be summarized as 'turning the problem-solving-processes into an engine for growth and achieving a sustainable economy'. The implementation of the plan has two phases: an immediate phase and a medium

to long term phase. The former is to support people suffering from changes in the internal and external environment, including measures to deal with high prices due to exogenous shocks such as food and fuel prices as the result of Ukraine war and recovery from the Pandemics. To tackle the issues from the short to long term, it is worth mentioning that, while continuing the three arrows of Abenomics, the plan says that the government will not hesitate to make truly necessary fiscal stimulus, clarifying that 'The economy is the foundation of public finance. The government will faithfully rebuild the economy. (Then,) The government will also work to put public finances on a sound footing. For this reason, the budget policy is well-rounded on the defence budget and the promotion of science and technology ever than before.

Regarding the 'new capitalism', there are five priority investment areas: (1) investment in and distribution to people, (2) science, technology and innovation, (3) start-ups, (4) green transformation (GX), and (5) digital transformation (DX). Among these, the tax incentive for individual investment with the goal of doubling asset income is a novel point. This is because in Japan, there has been a tendency to value income of sacred labour and not much emphasis has been placed on gains from individual investment.

The 'Initiatives for Solving Social Issues' has four focal points: (1) Creation of social value in cooperation with the private sector, (2) Realization of an inclusive society, (3) Promotion of multipolarity and regional revitalization, which includes addressing virtual space and meta-verse, and (5) Ensuring implementation of economic security.

The plan also states 'All possible measures will be executed, taking on without hesitation the fiscal expenditures necessary to cope with the crises.' In addition to disaster prevention and mitigation and the promotion of a resilient territory, there are five points that must be addressed to cope with changes in the international environment. (1) Strengthening diplomacy and security, including a drastic increase in defense capabilities within five years, (2) Strengthening economic security, (3) Strengthening energy security, including the promotion of energy savings and the use of renewable energy, nuclear power, and other high decarbonization sources, (4) Strengthening food security and (5) Promoting foreign and international economic partnerships, including Trans-Pacific Partnership (TPP), Regional Comprehensive Economic Partnership (RCEP), Indo-Pacific Economic Framework (IPEF), and Data Free Flow with Trust (DFFT), etc. In relation to Europe, the EU-Japan Economic Partnership Agreement (EUEPA) was already signed. IPEF is especially important, since it could build supply chains of some key goods for the industry in the Asia-Pacific region, such as the semiconductor (2019 global share: 55% in the U.S., 21% in South Korea, 6% in Taiwan, 6% in Japan).

Without any doubt, it is extremely important for us to follow the rules and to abide by agreements in international economic activities. It is unfortunate, however, that a country that has now become the second-largest economy often

disparages the rules, alleging its domestic circumstances and its own interpretation claiming to be the “largest developing country”. For example, it has been 20 years since the country joined the WTO, but there is still much to be improved, such as the opaque flow of subsidies that are suspected of favouring domestic and state-owned enterprises and insufficient protection of intellectual property rights. In the period following the Tiananmen Square protests, which led to the armed suppression on the pro-democracy movement, there use to be the commonly held belief that as the country became economically prosperous through the benefits of the reform and open-door policy of the time, people would naturally pursue values such as freedom, democracy and human rights, however, it was disappointing. It is now not only economically powerful, but also militarily powerful, and its challenge to unilaterally change the status quo on land and at sea poses a threat to neighbouring countries. Today, after three decades of globalization, we cannot think about the activities of nations without discussing geopolitics. The geopolitics of the world is a matter of great importance to us all.

Here in Europe, we are witnessing Russians’ continuous invasion to Ukraine. The security environment surrounding Japan is also becoming more testing and uncertain at a remarkably faster speed; The nuclear and missile development by North Korea, the strengthening and modernization of military forces in a manner that lacks transparency and attempts to change the status quo in the region by force or coercion that goes against the rule of law and openness; and tension within the region growing over the maritime issues. The list of issues goes on.

The Indo-Pacific region, where Japan is located, and which stretches from the Asia-Pacific across the Indian Ocean to the Middle East and Africa, is the core of the world’s vitality and supports more than half of the world’s population. At the same time, it is a region which has seen complex power dynamics of countries and has experienced drastic shifts in the regional power balance.

Regarding China, as us being neighbouring countries; there exist a variety of matters of concern with China.

Before talking about the concern with China, I must say that the relationship with China is one of Japan’s most important bilateral relationships, and the two countries have close economic relations. The global spread of the new coronavirus has had a major impact on the Japan-China economy, and business traffic between the two countries continues to be restricted. On the other hand, even under such circumstances, economic activities between Japan and China have continued, and the total trade between Japan and China (excluding Hong Kong) amounted to about 305 billion US dollars in 2021 (14.8% increase year-on-year), and China has been the largest trading partner for Japan for 15 consecutive years. Moreover, according to Chinese statistics, Japan’s direct investment in China increased to about 3.37 billion US dollars (9.3% decrease year-on-year, as estimated from officially published information on investment) in 2020. (Figures for 2021 have yet to be announced) Japan ranks third in terms of the amount of direct investment to China (Singapore ranks first, the ROK second, and the Netherlands

fourth, US fifth). As being the world's second-largest economy, its actions are increasingly affecting the international community in many ways. In this context, Stable Japan-China relations are important not only for both countries, but also for the region and the international community.

But then, China has been increasing its defence expenditures about 42-fold over the past 30 years, but the breakdown of the budget and the intention behind the increase have not been disclosed sufficiently. Under such circumstances, China is extensively and rapidly enhancing and modernizing its military power centered on its nuclear and missile capabilities and naval and air forces. It is placing importance on ensuring its superiority in new domains of outer space, cyberspace and electromagnetic spectrum. In the East China Sea, China Coast Guard vessels continue to intrude into the Japanese territorial sea around the Senkaku Islands, recording 34 incidents during 2021 (the numbers were 24 in 2020, and 32 in 2019). There is no doubt that the Senkaku Islands are clearly an inherent part of the territory of Japan, in light of historical facts and based upon international law. Furthermore, China has been continuing its unilateral activities to develop natural resources while the Exclusive Economic Zone (EEZ) and the continental shelf between Japan and China in the East China Sea remain pending delimitation.

Taken into account these severe surroundings, it is essential to ensure peace and prosperity in the entire region and beyond, through establishing a free and open order based on the rule of law. To contribute to regional peace and prosperity as an Indo-Pacific nation, Japan will cooperate with like-minded countries and strategically implement measures, including effective usage of ODA for the realization of Free and Open Indo-Pacific (FOIP).

Although geographically distant EU, including Portugal, has also become increasingly involved in the Indo-Pacific region in recent years. Last April, EU released the 'EU Strategy for cooperation in the Indo-Pacific', and in September in the same year, EU presented a Joint Communication on the EU's Indo-Pacific Strategy which further elaborated the document released in April. From our side, in January last year, then our Foreign Minister MOTEGI attended, for the first time as Japanese Foreign Minister, EU Foreign Affairs Council meeting in the form of online and explained EU Member State Foreign Ministers the concept of "Free and Open Indo-Pacific".

Minister MOTEGI also visited Portugal in 2000, which marked 160th anniversary of the signing of the Peace, Friendship and Trade Treaty between the two countries. And he expressed his intention to work with Portugal to realize a "Free and Open Indo-Pacific" in order to maintain maritime order based on the rule of law in the Indo-Pacific, to which His Excellency, President Rebelo de Sousa and then Foreign Minister Augusto Santos Silva both expressed their support.

Furthermore, Japan was invited for NATO summit in Madrid at the end of last month, along with our partners in the Indo-Pacific region such as Australia and South Korea. The participation of our Prime Minister Kishida as the first Japanese leader ever is the evidence of extensive and enhanced coopera-

tion between NATO and Indo-Pacific region.

Needless to say, Russia's invasion of Ukraine is a serious violation of international law, which prohibits the use of force, and shakes the very foundation of the international order, which does not permit unilateral change of the status quo by force. Large-scale exercises by Russian forces are also taking place in the Indo-Pacific and China is also participating in these exercises. In fact, joint Sino-Russian naval exercises in which 10 Sino-Russian naval vessels 10 ships sailed around the Japanese archipelago took place even before the Russian invasion of Ukraine. Japan shares the objectives of strengthening the rule-based free and open international order with the U.S., Australia, and India as partners so-called QUAD, who share fundamental values and responsibilities in the region. The four countries have been promoting practical cooperation in various fields. In May of this year, QUAD summit meeting was held in Tokyo, and while Japan was hosting this Quad summit meeting, Russian and Chinese military planes conducted joint exercises to patrol for hours, over the Asia-Pacific region including Sea of Japan and the East China Sea. The fact this action was taken during the Quad summit is considered an act of demonstration against the hosting country, Japan,

Experts have often pointed out the relevance between the invasion of Ukraine and China's possible invasion of Taiwan. Nowadays, the security of the Indo-Pacific and Europe cannot be considered separately, and it is important to share a mutual security perspective and further strengthen cooperation. Japan and Portugal are important partners who share fundamental values such as liberty, democracy, the rule of law, and respect for human rights. Furthermore, we are upholding the maintenance of maritime order as maritime countries.

As Ambassador of Japan to Portugal, one of my important tasks is to share this idea not only with government officials but also with many Portuguese people in order to gain their understanding and cooperation. In this sense, today's opportunity is very valuable, and I would like to express my sincere gratitude to all people who contributed in the realization of this seminar.

I am especially grateful for the moderator, and my teacher, Dr. António Rebelo de Sousa.

Muito Obrigado.

USHIO shigeru
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