Proceedings of the 3rd International Conference on Financial Technology and Business Analysis
DOI: 10.54254/2754-1169/135/2024.18592

The Current State and Future Prospects of Japan's Macroeconomy: Challenges and Opportunities

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Abstract: With the continuous evolution of the global economic landscape, the stability and growth potential of Japan's macroeconomy have received widespread attention from society. Since the 1990s, Japan has been in a state of long-term economic downturn. Faced with this challenge, the Japanese government has successively introduced economic stimulus plans, including zero interest rates and monetary easing policies. However, the pace of recovery of the Japanese economy is still slow and has not been able to get rid of the shadow of deflation. This article deeply analyzes the current situation of Japan's macroeconomy, including economic growth, employment, and wage levels, as well as prices and inflation, to evaluate the economic situation in Japan. The study shows that although the easing policies have produced some effects, Japan has not fundamentally escaped the dilemma of deflation. Moreover, Japan's structural problems such as the aging population and the weakening of the labor force ratio have hindered Japan's economic stimulus efforts. This paper suggests that while implementing monetary policies, Japan should also focus more on reforming economic structural issues and actively implement the Society 5.0 plan to promote scientific and technological innovation, thereby improving the level of economic development and leading Japan out of the long-term dilemma of economic stagnation.

Keywords: Japanese economy, deflation, aging population, macroeconomic policy, Society 5.0.

1. Introduction

In the early 1990s, Japan experienced a severe economic bubble, which subsequently triggered a comprehensive and prolonged economic crisis. The crisis marked a significant turning point in Japan's economic growth trajectory, with growth rates declining sharply. In 1993, Japan's gross domestic product (GDP) growth rate fell to -0.5%, reflecting a significant contraction in Japan's economic activity [1]. The Bank of Japan and the government adopted a series of policies aimed at revitalizing the economy. However, these measures did not effectively promote rapid economic recovery and failed to lead Japan out of a deflationary state. As global economic conditions continue to recover, Japan has continued to adjust and optimize its policies. Since 2021, the Japanese economy has shown obvious signs of economic recovery [2]. In September 2021, Japan's inflation rate achieved a historic transformation from negative to positive, gradually reaching the 2% inflation target set by the Bank of Japan [2]. This shift marks that the Japanese economy is gradually getting rid of the impact of long-term deflation and entering a more positive phase of development. Against this background,

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scholars have conducted increasingly in-depth research on Japan's economic conditions and policy responses. Nishizaki points out that the long-term deflation since the 1990s is the joint effect of multiple economic factors [3]. Among them, the decline in inflation expectations, the rise in the exchange rate and the decline in import prices are the key reasons for Japan's deflation. Nishizaki also emphasizes that the public's attitude towards price levels, weakened growth expectations, and the zero lower bound of nominal interest rates could be key explanations for Japan's prolonged deflation [3]. Another study analyzed the causes of Japan's deflation and the problems it may bring, emphasizing that when inflation and interest rates are close to zero, fiscal and monetary policies that exceed conventional expectations should be adopted to effectively address long-term economic stagnation and improve the future economic environment [4]. This paper aims to deeply explore the current specific development status of Japan's economy, analyze the interaction mechanism between its internal dynamics and external environment, and evaluate the sustainability and potential of this growth trend.

2. Current State of Japan's Macroeconomy

2.1. Economic Growth Status

In 1990, the Japanese economy collapsed from the foam of the housing market. Japan's GDP growth rate began to slow down. In 1993, Japan's GDP growth rate was -0.5%, which was the first negative growth after the bubble economy. There were different degrees of negative growth in 1998, 1999, 2008, 2009, 2019, and 2020[1]. After 2020, Japan's GDP growth rate began to rebound, from -4.1% in 2020 to 2.6% in 2021, an increase of 6.7%, which is the highest growth rate in the last five years [1]. The growth rates for 2022 and 2023 were 1% and 1.9% respectively, indicating that Japan is in a state of economic recovery [1]. From the 1990s to the present, Japan's economic growth rate is slower than China and the United States, but it is still in a state of continuous growth. Although this growth is not significant, it shows that the Japanese economy has a certain ability to recover and can find a way to grow after multiple economic crises.

2.2. Employment and Wage Levels

Employment and wage income levels have also had an important impact on the Japanese economy. Since the collapse of the bubble economy in 1990, Japan's unemployment rate has risen rapidly. It rose from 2.1% in 1991 to a peak of 5.4% in 2002. From 2002 to 2008, the unemployment rate slightly decreased, the number of employed people rose, and the economy showed signs of improvement. Due to the outbreak of the global economic crisis, the unemployment rate rose in 2009, reaching a peak of 5.1%. In 2011, the impact of the financial crisis began to fade, and Japan's unemployment rate began to decline continuously. From 2017 to 2023, Japan's unemployment rate has been at a normal level of 2%-3%, and the employment situation is relatively stable, which has a favorable trend for Japan's economic situation [5]. Although Japan's unemployment rate has experienced many fluctuations, the employment market has shown a recovery trend in recent years. Japan's labor market reform measures have begun to show results, and the unemployment rate in recent years has stabilized at a normal level before the crisis. Between 1990 and 1996, Japan's income level was not affected by the economic recession and continued to grow rapidly. However, starting in 1996, Japan's income level began to fluctuate, falling from $43,940 per capita in 1996 to $34,320 per capita in 1999 [6]. Subsequently, the increase in income level became smaller, and the trend of continuous rise turned into a state of fluctuation. By 2023, although the government has implemented many measures to stimulate the economy, the wage level has increased slowly. In 2023, Japan's per capita gross national income is $39,030, which is not much different from the $34,090 per capita in 1993, 30 years ago [6]. Japan's income level has stagnated. Although it has not continued to decline, it is slow compared with

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the trend before 1990. At the same time, since there has been no significant increase in income levels and purchasing power, consumption levels have remained low and have not changed the state of deflation.

2.3. Prices and Inflation

Since the 1990s, the Japanese economy has fallen into a state of long-term weak growth, characterized by a significant slowdown in economic growth rates. At the same time, price changes have tended to be mild and the inflation rate has dropped significantly, marking the Japanese economy entering the "lost decades" or a new economic normal of "low inflation and low growth". In April 1997, Japan's CPI index was at 98 points, and by 2021, it was only at 99.1 points, with no major fluctuations in the intervening period [7]. Japan's CPI growth rate has stabilized during the past 24 years. Price levels have not risen sharply, and this state continued until 2021. In 2021, the yen began to depreciate. As a major import and export country, Japan heavily relies on the import of energy sources such as oil. The depreciation of the yen means that import prices are higher, which leads to a gradual increase in the prices of domestic daily necessities, which causes the CPI index to begin to rise rapidly [8]. In May 2024, the CPI index has reached 108.1 points [7]. In the three years from 2021 to 2024, the growth rate of the cpi index will far exceed the growth rate of the previous 20 years [7]. Since the bubble burst in 1990, Japan's inflation rate has begun to decline rapidly. By 1994, Japan's inflation rate began to grow negatively, and Japan began to enter an era of deflation. Until 2021, Japan's inflation rate has been in a state of positive and negative fluctuations [2]. From 1999 to 2007, and from 2009 to 2013, negative expansion rates occurred every year [2]. Negative inflation growth also occurred in 2016, 2020, and 2021 [2]. These phenomena indicate that Japan has not completely emerged from the deflationary dilemma. Long-term deflation will change people's expectations for the future. When people think that expected prices will fall in the future, they are more inclined to save money and delay purchases or investments, which will further reduce demand and lead to more severe deflation. Although the inflation rate has reached the 2% target after 2021 due to exchange rate changes, it remains uncertain whether this can bring Japan out of its long-term economic downturn and sustain continuously.

2.4. Fiscal and Monetary Policies

To effectively curb the trend of deflation and achieve the goal of getting the economy out of the deflationary dilemma, the Japanese government and the central bank implemented loose monetary policy measures. The Bank of Japan began to implement low interest rates and quantitative easing (QE) policies [9]. Since the bursting of the real estate bubble, Japan has faced the dilemma of low economic growth and deflation. The Bank of Japan lowered interest rates to near zero to reduce borrowing costs, promote investment, and stimulate consumption. However, the effect was minimal, and the inflation rate still did not reach normal levels. In 2016, the Bank of Japan further implemented a low-interest rate policy, from zero interest rates to negative interest rates to promote consumption and stimulate the economy. The negative interest rate policy did stimulate some consumption. From 2016 to 2020, the inflation rate was higher than 0%, but it did not reach the target inflation rate of 2% [2]. At the same time as the low-interest rate policy, Japan also carried out a quantitative easing policy. The Bank of Japan invested a large amount of funds in the market by purchasing many government bonds and assets, making the liquidity of funds higher and lowering long-term interest rates to increase people's expectations of high inflation in the future. Once people's expectations of future prices increase, it will stimulate consumption, thereby truly getting out of the dilemma of deflation and reduced demand.

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3. Problems and Challenges Facing Japan's Macroeconomics

3.1. Insufficient Domestic Demand

In the past few decades, Japan has been facing the problem of insufficient domestic demand. The root cause is that supply exceeds demand and production capacity is not fully utilized, resulting in overcapacity. Japan's insufficient domestic demand is attributed to a variety of factors, including the aging of the population, low fertility rate and high savings rate, which will cause a decline in consumption capacity and thus inhibit economic growth [10]. Japan is one of the countries with the most severe aging population in the world. In 2023, the proportion of the Japanese population aged 65 and older soared from 12% in 1990 to 30% [11]. The aging population has changed the consumption pattern of the population. The consumption habits of the elderly are more inclined to increase savings and reduce spending, which weakens the overall consumer demand. Since 1990, Japan's fertility rate has begun to decline sharply. The decline in fertility rate will lead to a reduction in the labor supply and a decrease in the size of the young consumer group. The consumption proportion of the young group is the highest among the total consumer groups. The reduction of this group means that the number of people with consumption capacity in the market has decreased significantly, resulting in a decline in overall consumption capacity. At the same time, the reduction in the number of workers leads to insufficient labor supply, and the rising employment costs will inhibit the growth of enterprises and the economy. With an aging population and a low birth rate, a high savings rate has become a prominent feature of Japan. The high savings rate not only reflects Japan's consumption habits but also represents the public's concerns about future economic uncertainty. Since the collapse of the bubble economy, Japanese consumers' expectations for the future have also changed, which has further increased the tendency to save. Although a high savings rate can provide people with relatively stable protection during periods of economic fluctuations, it also limits the flow of money. When consumer activities decrease, the amount of money in circulation in the market decreases, and the market demand is insufficient to meet the needs of the supply side, leading to economic recession and reducing the speed of development. This will cause a negative cycle, and economic deflation will further reduce people's expectations, thereby further increasing the savings rate, and putting the Japanese economy into difficulty.

3.2. Uncertainty of the External Economic Environment

As a major importer and exporter, Japan is extremely sensitive to global economic fluctuations. The global market demand, supply, and exchange rate will have an impact on the Japanese economy. First, rapid or slow global economic growth will affect Japan's exports. When the global economy prospers, social demand will grow. As a major exporter of automobiles and electronic products, its export volume will also increase rapidly. When the global economy is in recession, the demand reduction will also affect Japan's export volume. For example, the 2008 economic crisis caused the global economy to slow down, Japan's export volume fell sharply, and the GDP growth rate immediately decreased, which had a great negative impact on the economy [10]. Secondly, exchange rate fluctuations will also affect Japan's imports and exports. When the yen appreciates, the price of Japanese export products becomes higher and lacks market competitiveness. When the yen depreciates, the price decreases, which is beneficial to exports, but at the same time, the price of imported goods becomes relatively higher, causing the price level of domestic goods to rise and affecting the domestic economy. As a floating exchange rate, the value of the yen is determined by the supply and demand relationship in the market, not by the central bank through fixed or direct intervention strategies. Therefore, the central bank cannot control the exchange rate, which makes

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Japan's economy more susceptible to changes in the external economic environment and increases the possibility of economic fluctuations.

4. Opportunities and Strategies

Amid the fluctuations in the global economic environment, Japan faces many internal and external challenges, including an aging population, a shrinking workforce, and international trade uncertainties. To address these challenges and seize possible opportunities in the future, the Japanese government could upgrade its industrial structure and promote technological innovation. Japan has therefore launched the Society 5.0 plan, which aims to combine emerging technologies such as the internet, data, and AI with social issues to create a new economic society centered on people [12]. This plan not only uses technology to solve economic problems but also promotes economic development by promoting technological innovation. To achieve Society 5.0, Japan has innovated in technologies such as semiconductors, artificial intelligence, and new energy. The government has invested more funds, such as R&D subsidies and tax incentives, to stimulate companies to enhance their technological innovation capabilities. Technological advancement will not only enable Japan to strengthen its competitiveness in the global technology industry but also help the economy transform and find new economic development directions to ensure continued economic growth in the future. In terms of education, the Japanese government has placed more emphasis on the importance of STEM and has cultivated more talents needed to support future technology. Through education reform, the curriculum will better meet the needs of the labor force and technology, and effectively address issues such as talent supply and demand. Through the implementation of the above strategies, Society 5.0 can use technological innovation and educational reform to better solve the problems of the aging population and social structure. For example, improving telemedicine or artificial intelligence systems can improve the quality of life of the elderly while reducing the burden of life for the younger generation. These innovations can not only solve social problems but also promote long-term economic development by solving structural problems.

5. Conclusion

This paper discusses in detail the current macroeconomic situation of Japan, the challenges it faces, and future opportunities and strategies. The study found that although Japan has tried to improve economic deflation and stimulate the economy through monetary easing and other policies, these measures have not been effective in promoting the sustainability of the economy. There has been no significant improvement in employment and wage levels, which also shows that Japan's economic recovery is slow. In addition, by studying the insufficient domestic demand and external economic fluctuations encountered by the Japanese economy, it is found that the aging of the Japanese population, the reduction of the labor force and the exchange rate are important problems faced by the Japanese economy. Due to its high sensitivity to external factors and insufficient internal flexibility, Japan has entered the dilemma of economic recession. Based on the analysis of the current situation, this paper proposes strategies to improve the industrial structure and promote economic development. Technological transformation and advancements in education can effectively address the fundamental issue of an aging population, and new technological innovations can stimulate the economy and create breakthroughs. Through Society 5.0 proposed by Japan, the upgrading of the industrial structure and technological innovation are promoted, and technological innovation is appropriately applied to society to solve Japan's long-standing economic problems. In summary, the future of the Japanese economy can rely on a series of close economic policies and technological innovations to complete Society 5.0, thereby ensuring stable competitiveness in the global economy and getting out of the state of deflation.

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