

Panel Discussion 2: What does the future look like in the post-crisis world economy?

Opening Address

(Naohiro Yashiro Professor, International Christian University)

During the Panel Discussion 1, we talked mainly about the issues associated the global financial crisis, but together with finance, the labor market is critical. Especially the investment flow is a critical factor in tackling the global imbalance. In order to address the issue, the Foreign Direct Investment (FDI), will play the increasingly important role. In order to have a more flow of the direct investment from advanced to developing countries, we have to have a higher capital productivity, and the population and the labor have a very important influence over the factors.

Through the FDI, the interdependence of the world will be strengthened, therefore, the countries with a large population like China, India, will play the important role. In those two countries, so far, the very large population has been the constraint to block the departure from the poverty but with some more liberalization of the capital, together with the capital from advanced country's abundant labor, has a positive factor. Then, as the G7 in the developed countries, without the big growth in population, what should we do?

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While the population in China and India is increasing, those in Europe and the United States remain stable. As for Japan, we are at a turning point historically; this year or last year or 2 years ago might be the peak of the Japanese population. Our population is expected to decline and in 2050 it will reduce to 100 million and 2.2 or 2.3 million will be eliminated from our population. With this pace, in 2300 there is no Japanese on the earth anymore. That is a rather extreme assumption, but for UK, although the pace is moderate, there is a growth in population.

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Aging has been progressing in all OECD countries. This is old-age dependency ratio, the percentage of old age population in the work age population, and Japanese old-age dependency ratio will dramatically increase and the labor population will decrease. Therefore, some people say that aging is a very significant factor to undermine the strength of the nation. That is very often considered as a symbol of weakness. However, this is not always true; we have the mechanism to turn this weakness into strength. For instance, we are able to alleviate adverse impact owing to the aging of population such as the decline in the work age population and greater burden of tax and social security by institutional reforms. What I would like to emphasize is that, from the vantage point of market, the aging of society brings more elderly customers to the market, so whether we are able to take advantage of the elderly customers or not is a big challenge.

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The issue of aging is very often taken as a gloomy issue because if government should bear responsibility for the nursing care, the medical care or pension, the size of government would become enlarged and the tax and the social-security burden would increase in step with the aging of population. This graph shows the population ratio of 60 and above in Japan, that of 80 and above in Japan, that of 60 and above in the UK, and that of 80 and above in the UK. According to the graph, elderly population will keep growing year after year. However, they are not poor. Now the elderly people are still poor but after the baby boomers retired, they are rather wealthy. In addition, in the developing countries, the population of middle class is growing. Therefore, the elderly people with ample means will increase substantially even in an aging society.

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Currently Japanese fiscal situation is difficult. Talking about national government debts, gross debt is 200% of the GDP and net debt is close to 120% of the GDP. If Japan was located in Europe, we will be certainly excluded from Euro because Japan cannot meet the qualification. Now Japan is under such miserable situation, so we are not able to depend on the public service because that may lead to the decline in service or increase in burden. Therefore, there is no way but using the market effectively in order to cope with the situation.

There was a discussion about excessive capitalism in former panel, and it might be true to an extent in financial market, but in the service market especially in the field of social welfare such as medical care or nursing care, market has not been used effectively yet. Under such circumstances there is a greater room for us to effectively utilize the market. Thus in aging society, Japan or Asia has to create age-free or gender-free society. At the same time, we have to create Silver Market, or the market for elderly people, and develop the service and products which cater the needs of the elderly people. That is a way to boost the domestic demand and to make the potential domestic demand realized.

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It is said that the extension of retirement age is a way to reduce the social welfare burden and increase the income. This is the result of comparative study on the Social Security System impact on the labor market conducted by the National Bureau of Economic Research (NBER). The horizontal axis shows the penalty incurred by elderly people who by engaging in work become unable to receive a pension and the vertical axis shows the labor force participation. You can see in the Netherlands, in France, and in Belgium, there is a higher penalty for work; on the other hand, in Japan, in the U.S., and in Sweden, that level is smaller. Thus, although there is cultural difference from country to country, we can account for 80% of the difference of the labor participation of the elderly people in

terms of how the Social Security System impose the penalty for the elderly people to work.

In order to reduce this penalty, we should have a very fair actuarial pension system. It means that those who retire early gain the lower pension and those who work long can be qualified for the higher pension, so in other words there is no penalty to work for a longer time. If we introduce that kind of pension system, we are able to effectively utilize the elderly workforce in Europe and the United States, in the midst of aging society.

I asked Mr. Bekx about the contradiction between supply and demand of the older labor force, but fortunately there is no such contradiction in Japan. Japanese elderly people wish to work as much as possible, and there is a lot of incentive to work long because there is a limited penalty for work due to the Social Security. What is problem is the demand for elderly workers, so if we reform the labor market and keep the corporate demands for the older labor force we are able to bring in the labor force of the elderly people into the labor market.

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One of the images about age-free society is we gradually need to change the definition of the elderly. That may sound a bit nonsense but if you look at the population ratio of age 65, age 70, age 75 and age 80, there is the constant increase. There in 2005 the percentage of the people aged 65 is 20% and then we fix the percentage of the elderly at 20%, in other words, in 2005 we consider the people age 65 or over as the elderly people, but in 2017 we consider the people aged 70 or over and in 2033 we consider the people aged 75 or over as the elderly. If that definition is used, the population ratio of the elderly people whom the society has to support will be quite stabilized. That means pension-level age can be delayed but also we would like to create the environment conducive for elderly people to continue to work.

As a global implication, as everybody emphasizes, we have to maintain the open market to eliminate protectionism and ensure the free movement of the labor and capital. In addition, we should create gender-free, age-free society and minimize disincentive of the Social Security System on the labor market. I think that is a challenge facing all the advanced countries.

Comment

(Jean-Pierre Lehmann Professor of International Political Economy, IMD; Founding Director, The Evian Group (Switzerland))

Firstly, I think it is legitimate to ask whether the title is justified, in other words, are we really in a post-crisis world economy? This may be a little bit optimistic. I think also that in looking towards what is going to be taking place, i.e. what is the post-crisis world economy, assuming we get post-crisis going to look like, one has to admit that there are lots of uncertainties. I presume that Nassim Taleb's book 'The Black Swan' has been translated into Japanese. I think one of the things

that we need to do in terms of this extremely turbulent environment that we are in, is trying to figure out what some of these surprises may be as the world goes through a transformation.

I have to say Professor Yashiro, with all due respect, that given the title of this presentation, it was really a very Japanese view of the world economy. I have spent a lot of time in Bangladesh, in Africa, in the Middle East, in Brazil and I think they would have great difficulty understanding this obsession that we have with aging because that is certainly not their problem, 60% of the population of the Middle East, North Africa, is less than 20 years old. So I think when we are looking at the world economy over the course of the next 10 years that the major challenge for the Japanese and the Europeans is not so much aging. I agree that aging is an issue but I myself consider being in that particular age bracket right now, I feel the more I am left alone the better and to focus on the next generations. So I think that the world economy that we are talking about must recognize these transitions that we are going through and also I think to recognize that these transitions may be very difficult.

But again, we have talked a lot about the emerging economies. The emerging economies have their own problems. What we have to make sure about is that the expectations of people who are going to be the very active population in this world economy are reasonably met, and this is where I agree with Martin Schulz, that there has to be job creation and also that labor markets have to be opened to be able to provide more opportunities. We must look towards a global and dynamic economy.

Now, I have done a work on scenarios for the global economies, and basically we say there are two vectors that are the most important. On the one hand, there is the degree of international cooperation versus the degree of international non-cooperation, and today we have a situation where our global financial institutions are not working. WTO is not working, IMF is not working and the World Bank is not working properly and these are creating bottlenecks. I must say that you do not mention in your paper the scenarios or risks of de-globalization and I believe this is very serious. I think that we could be going for a sort of increasingly fragmented global economy. I do not see collaboration, and everybody mentions Doha but nobody does anything about Doha, and I am prepared to make a bet of a fairly substantial amount of money that the Pittsburg commitment to finish Doha in 2010 will not be finished. This is one of the critical problems that we have.

Therefore, looking at the world economy post-crisis, we have to recognize the issue about the aging populations, but above all, we have to think about how we harness the new labor that is going to be coming on to the market, approximately a billion people over the course of this decade. This could be a tremendous driver of global growth. Japan would never be where it is, nor would Germany, nor would other countries in Europe, had it not been for the baby boom. Toshiba benefited enormously roundabout 1965, with all these bright, motivated, dedicated young people who created the Japanese economic miracle. So one thing, think youth, not just age. The second think is I think really everybody, including the business sector, has to do everything that it possibly can to make sure that

we have a collaborative global governance system rather than a conflictual global government system.

(Claude Meyer Associate Professor, Sciences Po, Paris)

I would like to stress 2 points. The first one is the world financial imbalances in the which have been at the root of the crisis and which have to be corrected. We have especially a global financial imbalance between the US and Asia, of which the most extreme case is the symmetric imbalance between China and the US. Gross national saving in China is representing 50% of the GDP against 15% for the US. If we take the other way around, Asia with the 60% of the world population represents only 20% of the world's consumption and the US with 5% of the population represents 30% of the consumption market. Four Asian countries own 50% of the US public debt owned by foreigners, or 25% of the total US public debt.

These financial imbalances, of course, trigger very detrimental effects in two respects at least. They introduce volatility in financial markets but also instability in monetary and financial policies. Even more, they divert from Asia much needed savings which would be necessary for its own economic and human development. I remind you that 40% of the population in Asia is below the poverty line at \$2 a day, and in the case of China, 35%. So, of course, the reduction of these imbalances will take time but it requires action, both in Asia and in the US. It requires in Asia a progressive switch from an export-driven model to a domestic private demand, in particular increased households' consumption. In parallel, increase of households' saving rate as well as reduction of consumer credit would be necessary in the US.

The second point concerns the benefits for Asia of an acceleration of its regional integration. From the European experience, Asia would benefit of a deeper integration at two levels, economic and financial. In trade and investment, we have seen many bilateral agreements, but it seems to me that maybe time has come for a large global agreement covering the Asia-Pacific region which would be more efficient, a kind of common market. A study by the JETRO in the white paper 2007 already computed that that would bring 1.3% incremental growth to the region, including 1% for Japan.

This common market would accelerate to some extent a closer financial coordination. I think that two aspects are most important about financial integration in Asia. One is the necessary development of domestic financial markets. Indeed, if the much-needed savings of the region fly to the US and Europe, it is mainly because the Asian financial markets are too shallow and not liquid enough. So, the Asian Bond Markets Initiative is in the right direction but it is far too slow. The second level would be the coordination between the various foreign exchange regimes because these differences represent an obstacle to capital movements within the region and a source of instability. As for the prospect of a common currency wished by Mr. Hatoyama, it is fine as a kind of goal but it is very remote. As an intermediary step, we could have progressively a system similar to the past EMS

(European Monetary System), where currencies are anchored to a key currency, with some fluctuation ranges.

But Asia could learn from the European example, not only on the positive side but also on the negative side. Indeed, there are some lessons to be drawn from the present experience concerning Greece. We have in Europe a common currency managed by an independent central bank who is the only one in-charge of the monetary policy but each country has its own autonomous economic policy, in particular budgetary policies. Consequently we have no coordination of economic policies and we have huge discrepancies between Eurozone members. Hence, the problem of Greece and possibly others (this awful word of 'PIGS'), which is hanging upon us with the extreme scenario raised by some journalists a few weeks ago of Greece exiting from the Euro. So, which solutions are viable? In the short term, the solution that has been approved yesterday night during the March 25 EU summit has some pros and cons. For the medium term, there might be something good in the Greek crisis as it shows the weak point of the monetary union, namely the lack of harmonization of economic policies. So maybe finally this crisis will force Eurozone countries to have a kind of coordination of their economic policies. It depends on what the concept of economic government means exactly respectively in Berlin and Paris.

Discussion

In an aging society, one of the possible social solutions is to reduce the penalty for work imposed on elderly people. This would be effective to reduce the burden of social security services. In Japan, however, while job opportunities for elderly people are increasing, the unemployment rate for people in their 20s is as high as 9 to 10%. In addition, a large number of youths have no other choice but to work in irregular employment for low wages, and the opportunities for them to move on to regular employment are rather limited. Then, if elderly people with low productivity work longer and young people with new ideas and the ability to work hard lose employment opportunities, it might have a negative impact on overall economic growth.

On the other hand, some argue that the country gains nothing by forcing retirement on those who are capable of working. If every elderly person retires, productivity on a population basis will decrease and pension costs will increase. Those costs would return to corporations as wage costs, and with that heavy burden, corporations would reduce employment opportunities. Thus, what must be done is make people work longer in order to reduce social security costs such as pensions. Then, corporations can expand youth employment opportunities in the long term. In order to achieve this, the labor market should be more flexible. Companies will fall apart if they employ elderly workers with the current strict employment security and age-based remuneration system. Therefore, if the elderly work for wages appropriate to their productivity—i.e. the lower the productivity, the lower

the wage—and the labor participation rate increases, the burden on youth will reduce.

A number of EU member states have reduced the generosity of their pension schemes, which has already reduced pressure on public finances. There are also other reforms taking place, such as those that could boost retirement incomes by extending people's working life. Doing so involves not only allowing people to work after they would normally have to retire but also introducing more flexibility into people's approach to work. For instance, a corporation might allow people to take sabbatical years in the meantime instead of extra labor periods after the retirement age or to increase employment for women, including education and training courses, during the whole course of their working lives. There should be reforms of the tax and benefit systems in order to reduce the disincentives to work.

In terms of aging, there are commonalities between Japan and Europe, but one big difference is the Japanese style of employment practice. Europe has a labor market that is segmented by trade, while Japan has one that is segmented by corporations, and this causes a big disparity in wages among companies and between regular and irregular employment. This issue has to be addressed in order to achieve equal pay for equal work. Without this effort, the rigidity of the labor market in Japan may not improve.

In Japan, the labor participation rate of elderly people is high; some people say this is because older Japanese people have a strong willingness to work, but others say it is because they have little choice but to continue working. Most Japanese people work in order to make mortgage payments, and after retirement age, they continue working in order to cover cost of nursing home care or to earn their living because they cannot live on their scanty pension. Moreover, most Japanese people tend to save their money in a bank instead of spending it for their old age, which may cause Japanese money to remain inside Japan and not get redistributed to the rest of the world.

On another front, the question of whether or not to work is faced not only by elderly people but also by all age groups. It is an individual choice: either you work intensively, save more, and retire early, or you do not save as much but rather continue working longer. The problem is that the government is regarding this uniformly. For example, the retirement age is currently 60, and the eligibility age for pension is 65. Another point is that in Japan, the return on savings is very low compared to that in the western world. Higher efficiency in the financial market will yield higher return on savings, which will increase the liquidity of capital and open up choices such as early retirement. In that sense, public sectors should create wider options in the labor and financial markets.

Japan is probably facing a period with growth rates comparable to those of the 1960s and early '70s. The reason for this is that massive emerging markets are entering the world economy. Asia and Africa has large populations of young people with good educations and willingness to work, and they need access to capital and technologies. On the other hand, in advanced countries there is too much capital sitting idle, destroying investment possibilities. In that sense, people in advanced

countries should not hide their money in banks as savings—they should invest it in developing countries with market possibilities and business opportunities. Even if the recent financial crisis has roots in excessive capitalism and market forces, the global trend of deregulation must be maintained. Even if the entire financial sector is nationalized, it does not mean that another financial crisis can be avoided. The recent financial crisis created a blip in world economy, but there must be big opportunities after the crisis, so government should support business sector.

Another possible countermeasure against aging is immigration intake. After World War II, Europe introduced immigrant workers to the market, and they have contributed to economic growth. At the world level, the problem of aging societies is not very acute because in countries like Bangladesh and in African nations, the majority of people are below 20 years of age. Some people argue that the aging societies would see increased immigration from those countries into the societies in which aging is a problem. Moreover, the suggestion that the definition of the age of senior citizens should be gradually raised according to the extension of the average life expectancy is slightly controversial. Even if elderly people nowadays can work longer than they did before, it is necessary to consider the age-related physical constraints and biological differences. There is also an argument that it is better to gain a younger labor force as immigrants rather than to make senior citizens work in order to support the national finances.

However, advanced countries may solve this issue not only by receiving more immigrants but also by exporting capital through foreign direct investments (FDIs) to developing countries. If advanced countries make products abroad with their capital and import such products, the shortage of labor can be compensated for to some extent, which would reduce social friction. Of course, the utilization of the foreign work force is important, but depending on immigrants alone will not be the solution for an aging society. Immigrants get old as well, so overdependence on immigrants is just deferring the moment of truth. The biggest problem in an aging society is who should bear a burden of support the elderly people; in other words, it is a choice whether the elderly work and earn their lives or let young people burden. In principle, the elderly, who are the source of the aging, should cope with it.

Anywhere in this globalized world economy, all companies need is those people who can engage in global business. Although not many Japanese people are active on the global stage now, the younger generations have to work in a growing market and in growing businesses and should acquire certain global skills rather than building their careers in a shrinking market. Immigration has some economic consequences, but it is a society's choice. In the area of globalization, people accept the circulation of goods, services, financial services, and so on, and it can be said that a time will come when countries more readily accept the circulation of people and the workforce.

Silver Market, or market of the elderly, will bring a significant opportunity in aging societies, not for the leisure industry, which targets the retired generation, but for the healthcare industry, which has technologies that support elderly people. This can be a large market. The medical sector is a

high-tech industry and Japan has a comparative advantage in that field. However, since this area is very severely regulated by the government, Japan is still not taking full advantage of it. By making it more flexible, there is a chance that the medical care market can be a leading sector in Japan to promote growth. In particular, some people have pointed out that quite recently, a much younger labor force has been put in nursing care of the elderly and will thereby harm productivity; however, technological innovations such as robot technology can enable the substitution of capital for labor. Then nursing care would no longer be a labor-intensive industry and seniors would be able to take care of other senior citizens. According to one calculation, the proportion of elderly people in Japan will reach around 45% in 2045, so Japanese people need to prepare for that. This really requires a long-term vision and investment that will provide these kinds of opportunities. Aging is not a problem for developing countries with young populations, but it is a problem in advanced economies, constraining growth in the long run. Thus, this is a typical problem, which requires some policy solutions and a long-term view.

Since the financial crisis, the structure of the global economy has changed dramatically, and advanced economies as well as developing economies are facing greater difficulties than before in many ways. Japan in particular requires structural reform in the short term in order to achieve a sustainable economic recovery and in the longer term in order to cope with its aging society. The aging of society means that average productivity is falling; thus, in order to achieve sustainable economic growth, structural reforms are required to yield benefits from globalization. However, concern is greatest for a kind of conservative attitude that is spreading among the younger generation. They have been given the excess burden from the aging population and the deteriorating labor market. Therefore, it is necessary to give the younger generation a chance. This is a very critical point.

When talking about growth models, it is necessary to move away from the idea that one size fits all. Each country has a different set of priorities and issues. Aging is very important problem for Japan or other advanced countries, but is not important for other countries with different demographic structures, and each country will have different solutions. Therefore, in the integrating world economy, a sort of macro perspective is needed; while at the same time keep an eye on national and regional differences. World economy is now exiting the global economic crisis, and it must be avoided to go back to a situation with the global imbalances. It is very important that the major economies in the world look at that and derive collaborative solutions, such as the G20 framework for growth, in order to get the world economy back on a path toward sustainable growth.