

# Decreasing Population, Increasing Profits

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THE economic growth of a country equals the population growth plus the per capita productivity growth. The population of Japan will start declining from 2006. Unless the increased per capita productivity growth can offset this negative factor, the country's economic growth will be much smaller than before. Japan's population used to increase by 1% each year, so when its per capita productivity growth rate was 3%, its economic growth rate was 4%. If the population declines by 1% every year, however, the economic growth rate would only be 2%. If per capita productivity improves by 1% in addition to the 3% mentioned above, Japan's economic growth rate would still be 3%, offsetting the negative impact caused by population decline. How is this possible?

Japan's productivity rate for competitive manufactured goods is said to be 20% higher than that of the United States. However, for other goods and services, Japan's productivity is about 40% below that of the United States. Japan's productivity for agriculture and construction is especially low. Since competitive manufactured goods only account for 10% of Japan's economy, its average productivity is only two-thirds of the US rate. So Japan has to improve its productivity from the standpoints of catching up with the United States and coping with population decline. There are two possible scenarios for Japan.

The first one would be to improve the productivity of goods and services other than competitive manufactured goods. If female and elderly people who have not been seeking jobs start working, Japan's per capita productivity will surely increase because additional goods or services which are the numerator for calculating productivity would increase regardless of their skills whereas Japan's entire population,

the denominator, would remain unchanged. In addition, FTAs with other countries would be able to play a big role to improve productivity. If Japan's agriculture and service sectors are exposed to more foreign competition due to FTAs, their productivity should be improved for survival. Of course strong political leadership is needed for this scenario to be realized.

The second scenario would be to shift resources such as labor and capital to more productive sectors. However, the most productive sectors such as automobiles may not need any additional resources. Promising service industries such as health care, tourism, business support and entertainment contents would need them. Tourism includes businesses for convention centers. Business support includes agencies that introduce or dispatch workers to companies.

From the viewpoint of the supply side of a national economy, economic growth can be attributed to three factors, namely the increase of labor input, the increase of capital input and total factor productivity (TFP) growth brought about by technological development and others. Although Japan's population will not decline until next year, the labor force has been declining since 1999. However, labor input has not played a big role in Japan because it is not a labor-intensive economy. Regarding capital input, saving would have the best effect. Therefore less saving means less capital input. In this regard, there are at least two problems. The first is the decrease of the absolute amount of saving due to the decline of the entire population of Japan. The second is the decline of the saving ratio. Japan is an aging society and the share of population aged 65 or older will increase from 20% in 2005 to 30% in 2030, and aged people spend more than they save. Since Japan is a capi-

tal-intensive country, the reduction in capital input would be a big blow to its economy. Increasing the number of foreign workers might mitigate the negative impact but they may remit a good amount of money to their home countries leaving hardly any money in Japan. Extending the retirement age will stave off the decline of the saving ratio. The reason why aged people spend more than they save is that they cannot earn enough money to save after retirement. If they can keep working they will save to some extent. Of course the real solution would be to improve TFP by enhancing productivity through employee training and deregulation, which is now hindering the free movement of resources to more productive sectors.

I have assumed that population decline or aging in Japan per se would have a negative impact on its economy. However, some people predict a bright future for Japan's economy despite population decline and aging. For example, the labor market will become tight because of population decline in general and the retirement of the baby boomers in particular. Wages will go up, offsetting the decline in consumption. In addition, companies will be able to make big profits out of the retirement of the baby boomer generation that will start from 2007. The number of Japan's baby boomers who were born between 1947 and 1949 is conspicuously larger than other age groups. 2.2 million people will turn 60 in 2007 followed by 2.3 million in 2008 and 2009 respectively. In an ordinary year the number of people who are the same age is around 1.6 million. In a sense Japan's companies may have been carrying an excessive workforce because of the baby boomers. After their retirement, Japan's companies can enjoy a reduction of personnel costs, therefore increase their profits. **JS**