

## *Summaries*

## **Japan's economic policies and its risk premiums in the international financial markets in the era of the international gold standard**

**Makoto Kishida**

In the era of the international gold standard from the 1870s to early 1930s, Japan issued large amounts of foreign currency bonds from the international financial markets for its economic development and military expansion. For continued fund procurement, it was essential for the country to maintain its creditworthiness. This paper reveals the yields and risk premiums of the Japanese governmental foreign bonds in the London and New York capital markets, and uses historical facts to analyze how changes in government's fiscal or economic policies affected Japan's risk premiums in the markets. As a result, it became clear that the change in the stance of the government's fiscal policy and its adherence to the gold standard was more or less consistent with the changes in the country's risk premiums.

## **Politics and firm dynamics: Empirical analyses of the banking industry in prewar Japan**

**Michiru Sawada**

This paper conducts an empirical analysis about what impacts political connections have on corporate dynamics, using data from prewar Japan's banking industry, where the relation between the corporate and politics were more observable than that from contemporary Japan. In the analysis, we focused on the presence of "politician directors" in order to understand the connection between banks and politics. We identify banks which had at least one director who was also politicians (members of the House of Representatives), as "politically connected banks." As a result of analyzing data on the years 1926 and 1931, it turned out that around five percent of banks had political connections through their politician directors. Further, when focusing on positions of political directors in their banks, it was confirmed that there was a lower percentage of politician directors among senior executives (presidents and managing directors) than among junior executives (directors and auditors). It can be conjectured that the role of cultivating political connections was delegated to the junior executives, as the senior executives had to give their undivided attention to the management of the bank.

The paper also analyzed whether there were any differences between banks with political connections and those without, in the probability or patterns of a bank's exit from the market. Using a multinomial logit model, in which exit patterns were divided into the two categories, consolidations and bankruptcies, we analyze the impact of political connections on banks' exit from market. Regression results showed that while banks with political connections tended to exit due to consolidations at a higher probability, they tended to exit due to bankruptcies at a lower probability. Those impacts, however, were not statistically significant. Further, as the result of an analysis to consider heterogeneity regarding impacts of political connections, it was confirmed that political connections did not have a statistically significant impact on market exit of large banks. On the other hand, there was strong evidence that political connections decreased the probability of bankruptcies among small banks. It can be interpreted that the advantages of political connections were significant for small banks as they faced a relatively greater risk of bankruptcy.

# **Household Income and Consumption After the Collapse of the Bubble Economy in Japan – An Empirical Analysis Based on VAR**

**Shuji Watanabe**

This paper examines the relationship between household income and consumption before and after the collapse of Japan's bubble economy by applying a vector autoregressive (VAR) model to its GDP data. It particularly focuses the role of the built-in stabilizer that the Japanese government provides to absorb various shocks to the economy. The results of this study indicate that the built-in stabilizer plays a critical role in the Japanese economy. After the collapse of the bubble, partially due to the sharp drop in interest income, the household income growth slowed down and finally stopped in 1997. We find that the system as a whole, including the built-in stabilizer, absorbs a considerable portion of the shocks to household income and maintains the stability of consumption spending. The estimation result also indicates that the rapid drop in interest income finally caused the decline in wage income. Although the built-in stabilizer protected household consumption from these shocks, the Japanese economy has suffered from its low growth more than 25 years.

The Bank of Japan has maintained the low interest rate policy for many years but the policy had rather limited stimulus effects on the economy. We need to reexamine the hypothesis that this policy damages the household purchasing power if we pay more attention to the fact that more than half of household financial assets are held as bank deposits. While the built-in stabilizer protects the consumption, we have to consider its long-term costs. The government debt outstanding has piled up and already reached more than 1000 trillion yen and this could cause unprecedented damage against the Japanese economy. The government must understand the costs and benefits of the built-in stabilizer financed by the tremendous debts and reconstruct the current system in order to avoid the worst scenario. Unfortunately, the "democratic political system" in Japan has a very strong tendency to minimize the immediate pains at the expense of the long-term stability of its economic system.

## **Impact of political reform on inter-regional resource allocation and income distribution in Japan**

**Takashi Sakuma**

The diversity of economic and political spatial characteristics, social security systems, and relationship between central and local governments seen among countries have attracted the interest of economists, political scientists and geographers. Of late, there is an increasing body of interdisciplinary research works that take into account the correlation between these factors to come up with theories for the formation of systems and empirically analyze them.

This paper, while taking into account the results of prior research, compares the situation before and after the reforms of the Japanese political system implemented in the 1990s, and attempts to verify, based mainly on prefecture-level data, how changes in the political system affected inter-regional resource allocation via fiscal policy.

By introducing three categories of areas by spatial characteristics – rural areas, urban areas and intermediate areas, it became possible to elucidate the consequences of political reforms within the context of different regions.

It became clear that the switch from a political system based on medium-sized electoral districts, under which rural areas were over-represented and urban areas were under-represented, to a system based on small electoral districts narrowed the disparities significantly. Also, looking at the regional distribution of districts from which Liberal Democratic Party (LDP) Diet members were elected, it is also supported that the LDP's policy decisions and election campaign promises have changed from mainly reflecting the interests of rural districts to greater balance in terms of reflecting the interests of both rural and urban areas.

The impact of political reforms on inter-regional resource allocation became manifested not in terms of a lowering of the excessively high share of public works to rural areas, but rather in the form of a large cut in the total amount of public work investments, although the government final consumption expenditures, which tend to be rather even among regions, were maintained to increase. The negative impact of this move on the regional economies was greater in the case of rural areas and worked to shrink the income of rural areas gained via public work projects.

An unexpected result of the current study was to portray the process of dissolution of the “construction state.”

# A Study on Income Levels and Value Judgments<sup>1</sup>

Masumi Kawade

In recent years, Japan's fiscal situations have deteriorated greatly as a result of the demographic aging and repeated natural disasters beginning with the 2011 Tohoku earthquake and tsunami disaster. Consequently, fiscal reconstruction has become a pressing necessity, and it has become necessary to increase the public burden starting with an increase in consumption taxes. In a democratic country, the understanding of the general public is essential for fiscal reconstruction to go ahead, and this depends on citizens' value judgment. For instance, implementing policies that will go against the values of the people are politically infeasible. Meanwhile, value judgment itself is thought to be related to the economic situation in which people are placed, so it is important to encourage research on the relation between the two.

This paper used the Keio Household Panel Survey (KPHS) and investigated the Japanese public's value judgment based on individual data that took into consideration not just tax but also social insurance contributions, with a view to evaluating the differences in value judgment among the different income brackets, as well as the effects of income redistribution. Data from the KPHS surveys conducted from years 2009 through 2012 was used. To the incomes for years 2008 through 2011 given in response to the question asking the "previous year's income," the rules of the tax and social insurance contribution systems were applied, and the tax and social insurance contribution burdens were recalculated. The contribution amount as well as contribution rate for each decile was then totaled based on equivalent total income (arrived at by adding any public transfer amounts).

And the KPHS survey's questions pertaining to value judgment were used to re-tally what kind of value judgment each household respondent had, given their economic situation. Specifically, the responses of the value judgment questions were tallied for each decile of equivalent total income, and an assessment was made to see if there were any specific tendencies common to respondents from each income bracket. With regard to the main categories of value judgment, the ratio between gross income and initial income as well as respondent category was used to attempt a cross-section analysis.

As a result, it was found that the higher the income level of the household, the more likely the affirmative responses to questions about mental and physical wellbeing and happiness; in terms of political value judgment, the income level did not significantly affect party affiliation, but it was seen that the higher the income bracket, the greater the interest in politics; the effects of income

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redistribution were not found to be statistically significant when compared with income level and respondent category.

# Quantitative and Qualitative Monetary Easing and Japanese Bank Stock Returns<sup>\*</sup>

Koji Sakai<sup>†</sup>

This paper verified the impact of the BOJ's Quantitative and Qualitative Easing (QQE) policy introduced on April 4, 2013 on the stability of the financial system. The study placed particular focus on banks among financial institutions, and adopted the method of an event study using time series data for banking industry stock price indices as well as for individual banks' stock prices.

As a result of the study, it was indicated that the introduction of the QQE policy had the effect of boosting future cash flows for the banking industry as a whole, and can be said, on the whole, to have contributed to stabilizing the financial system, but the effect was heterogeneous in nature. In particular, among second-tier regional banks, which are facing a harsh business climate, for those that are highly reliant on the lending business and have not made progress in terms of business diversification, the policy has resulted in shrinking the overall profit margin and depressing future cash flows. This suggests that the further protraction or expansion of the QQE policy is bound to further deteriorate business conditions for second-tier regional banks and would ultimately invite serious consequences in terms of destabilizing the regional financial system.

Key phrases: Qualitative and Quantitative Easing (QQE) policy, financial system, banks, event studies

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