

Strategy Bulletin Vol.22**Can the DPJ administration quickly change its spots?****The DPJ's big loss is good news for the market; the end to the end of Japan's 55-year two-party system**

The Democratic Party of Japan (DPJ) suffered an unexpectedly big loss. Once again, the "twisted politics" phenomenon has started in Japan's parliament. No bills except the budget can be approved without opposition party support. There is a growing pessimistic view that Japan is increasingly likely to enter a period of political paralysis. But there may be a positive side of the DPJ's loss. Perhaps this will bring a complete end to the so called "1955 system" of two-party rule (Liberal Democratic Party (LDP) and Social Democratic Party of Japan (SDP)) and create an opportunity for a mature democracy to finally take hold in Japan. There are two reasons for embracing this view. First, the opposition LDP, Komei Party and Your Party have acquired veto power. Before, government policies mirrored the DPJ party line. But now exactly the opposite situation exists. Policies must prioritize the Japan-US relationship and be pro-business and pro-growth. This is certainly welcome news for Japan's economy and financial markets. Second, the SDP and DPJ are no longer held back by non-constructive opposition parties (opposition simply for the sake of opposition, distributions of goods while ignoring production, expenditures while ignoring revenues, disregard for markets), making it possible to hold constructive policy debates.

A brazen shift in the party line has started

The strong desire for reforms was behind the birth of the Hatoyama administration. But this administration's policies were precisely the same as the policies of irresponsible opposition parties of the "1955 System". However, the new Kan administration has started a surprisingly brazen transformation. Discussions with Nippon Keidanren had ended under the anti-business stance of the Hatoyama administration. But now these discussions have resumed. Furthermore, following the mistakes of the Hatoyama administration, Prime Minister Kan immediately after his election reaffirmed the importance of the US-Japan alliance. In addition, the new prime minister unveiled a specific proposal for tax reform: cutting the corporate tax rate to 25%. He also announced a growth strategy, which had been missing from the previous administration. On the other hand, postal system reforms (renationalization of the postal service and a higher limit on postal savings deposits) that had been agreed upon with the People's New Party appear to be dead on arrival. We are also seeing the start of corrections to anti-business policies and plans to hand out money to the Japanese public. For example, the DPJ seems to have given up on amending the Temporary Staffing Services Law and abandoned its plan to pay child-rearing subsidies to everyone demanded strongly by SDP. The DPJ has even stolen an idea from the LDP by suggesting a hike in the consumption tax to 10%.

The only option is to fully adopt opposition party policies – a positive development

In this political environment, the difference between DPJ policies and those of opposition parties has become so small that there is little room for argument. Japan lawmakers need to overlook petty differences and take forceful action regarding issues that clearly urgent: (1) ending deflation and restoring growth; (2) enacting administrative reforms; (3) enacting fiscal reforms and a plan to cut the national debt; and (4) rebuilding the Japan-US relationship in line with globalization. We must not forget lessons learned from financial crises. Not surprisingly, the 1998 financial crisis coincided with the "twisted politics" phenomenon in Japan's Upper and Lower Houses. Under the leadership of current Prime Minister Kan, the DPJ as an opposition party did not regard finance as a political issue. Instead, the party urged ending the financial crisis and reforming the financial system by using a new generation of policymakers as the main architects of change. This requires the knowledge to achieve a major breakthrough by using an unexpected initiative by a DPJ-LDP and other coalitions.

The successful policies of the Mitterrand administration in France

Can the DPJ learn from the success of the socialist administration of Francois Mitterrand in France? Francois Mitterrand, who belonged to the Socialist Party, became president of France in the early 1980s. At first, he announced a variety of anti-market policies based on socialist idealism. For example, he wanted to nationalize industries, increase taxes on companies and wealthy people, and pay income subsidies to low-income people. But these socialist policies threatened to slow economic growth and

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spark inflation. The Mitterrand administration abandoned these policies and switched 180 degrees to liberal policies like tax cuts and reductions in social welfare programs. France's economy subsequently began to stage an extended recovery. Finally, President Mitterrand named conservative Jacques Chirac as his prime minister, forming a conservative-reform coalition. The situation in Japan is very similar to France at that time. Depending on the skills of Prime Minister Kan and other DPJ leaders, we may see the current administration in Japan enact successful reforms by changing direction just as President Mitterrand did in France.

Countries worldwide have few options

In any case, the DPJ will be forced to make a fundamental change in its platform. We now live in an age in which companies and people can choose their nationalities thanks to globalization. Individual countries have much fewer policy options to choose from as a result. Governments now have one overriding mission: creating an advantageous position for global competition by their economies, companies and citizens. This requires an intent focus on national security, democracy and a market-based economy. That means the time has come to achieve a policy breakthrough even at the cost of accepting the policies of opposition parties with no arguments or revisions.