

Japan Topics

New prime minister, new manifesto, and the upper house election

21 June 2010

Naoto Kan, who was finance minister in the Hatoyama cabinet, has been elected as the new leader of the ruling Democratic Party of Japan (DPJ). As a result, Mr Kan became Japan's 94th prime minister on 4 June. Mr Kan's appointment instantly boosted popular support for the Democratic Party of Japan.

Mr Kan took office with a mandate to rebuild the DPJ's reputation, which had been battered by allegations that Yukio Hatoyama, his predecessor, and Ichiro Ozawa, the party's powerbroker, had received improper political funding. Mr. Hatoyama stepped down, together with Mr Ozawa, in an effort to restore the public's trust in the DPJ and improve its prospects in upper house elections next month. This has been so far successful; upon Mr Kan's appointment as prime minister, support for the DPJ has risen. This is good news for the DPJ, which has little time to regain the trust of the public ahead of the upper house elections on 11 July.

"Irritable Kan" - The profile of the new prime minister

As a politician, Naoto Kan is the polar opposite of Yukio Hatoyama, who he replaced. Mr Hatoyama was born with the proverbial silver spoon in his mouth. In contrast, born in Ube, Yamaguchi Prefecture, into a salaried worker's family, Kan had to claw his way up the political ladder on his own merit. While Hatoyama is a prince of a political dynasty, Kan started out at the grass roots level, working in citizens groups.

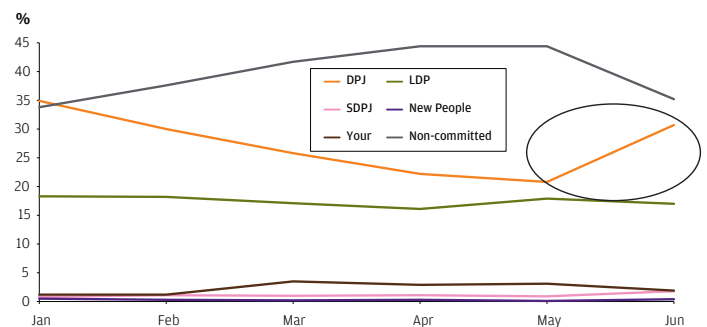
Being outspoken and decisive, Mr Kan is not a typical Japanese politician. Mr Kan is a graduate of the prestigious Tokyo Institute of Technology, and he set up a patent office after university. He was long active in the civic movement and did not enter mainstream politics until fairly late in his career, winning a seat in the lower house of the Diet. During his political career Mr Kan has become known as "irritable Kan," who was once the bane of bureaucrats. As health minister in 1996 he exposed a government cover up of HIV-tainted blood products that caused thousands of haemophilia patients to contract the virus that causes AIDS. The unprecedented step of exposing the responsibility of the ministry in a tainted blood scandal made him popular among the Japanese public. As finance minister since January 2010 Mr Kan has performed well despite his lack of fiscal or economic expertise, and stood out after calling for discussions on raising the consumption tax.



"I will tackle and pull Japan out of deflation through comprehensive measures from the government and the Bank of Japan." Mr Kan has called for action on deflation and has hinted that he would seek greater cooperation from the central bank. (Kan Naoto, the Prime Minister of Japan)

Opinion polls in 2010: party to support

Even with the DPJ's popularity declining during the Hatoyama administration, people were not reverting to the old guard LDP, which clearly shows that Japanese voters are demanding change. Mr Kan's appointment instantly boosted the DPJ's support rate.



Source: The NHK Broadcasting Culture Research Institute, J.P. Morgan Asset Management

Fresh developments: bid to rebuild the party's image as modern, clean and transparent

Mr Kan unveiled his cabinet line up on 8 June. Mr Kan retained most of the ministers who served under Yukio Hatoyama, but at the same time his appointment of young DPJ members to the cabinet – such as Renho as minister for administrative reform, and his choice for key positions within the DPJ reflect Mr Kan's bid to rebuild the party's image as modern, clean and transparent. Mr Sengoku, newly appointed chief cabinet secretary, has been critical of public works projects in general and supportive of drastic deregulation and market liberalisation. Many Japanese people voted for the DPJ because of its young, confident politicians – expectations that Mr Kan seems to be making efforts to meet.

Economic policy implications

Mr. Kan is one of those people who has realised and expressed strong concerns over Japan's fiscal deficit and deflation, which are the two prominent mid-to-long term issues that the country needs to tackle. Interestingly Mr Kan supports a rise in the consumption tax. He believes that consumption taxes do not necessarily decrease demand. Japanese government debt is so far domestically financed. Mr Kan seems, however, to be well aware that he has to appeal to the international community, so he is keen to show that he is committed to tackle Japan's high debt-to-GDP issue, especially in light of the Greek sovereign debt crisis. Currently, bond issuance is exceeding tax revenues. He knows that structurally this is unsustainable, so he is trying to increase taxation. Mr Kan is also deemed to be a supporter of a weaker yen.

New manifesto: “Strong economy, strong finances and strong social security”

On 17 June the DPJ published its manifesto for the upcoming upper house election, with policy direction focused on a strong economy, strong finances, and strong social security. The new manifesto shows a shift in policy away from the emphasis on government spending towards providing support for household spending, as espoused by the manifesto for the 2009 lower house election. The manifesto seeks to rebuild the nation's finances via tax hikes and economic growth. The DPJ is the first government to declare a strong will to fight deflation. In its manifesto, the party made two key commitments. First, the “DPJ will aim to achieve average annual growth in nominal GDP of 3% through to 2020 and growth of more than 2% in real GDP terms.” Second, the “Government and Bank of Japan will cooperate to put an end to deflation as soon as possible”.

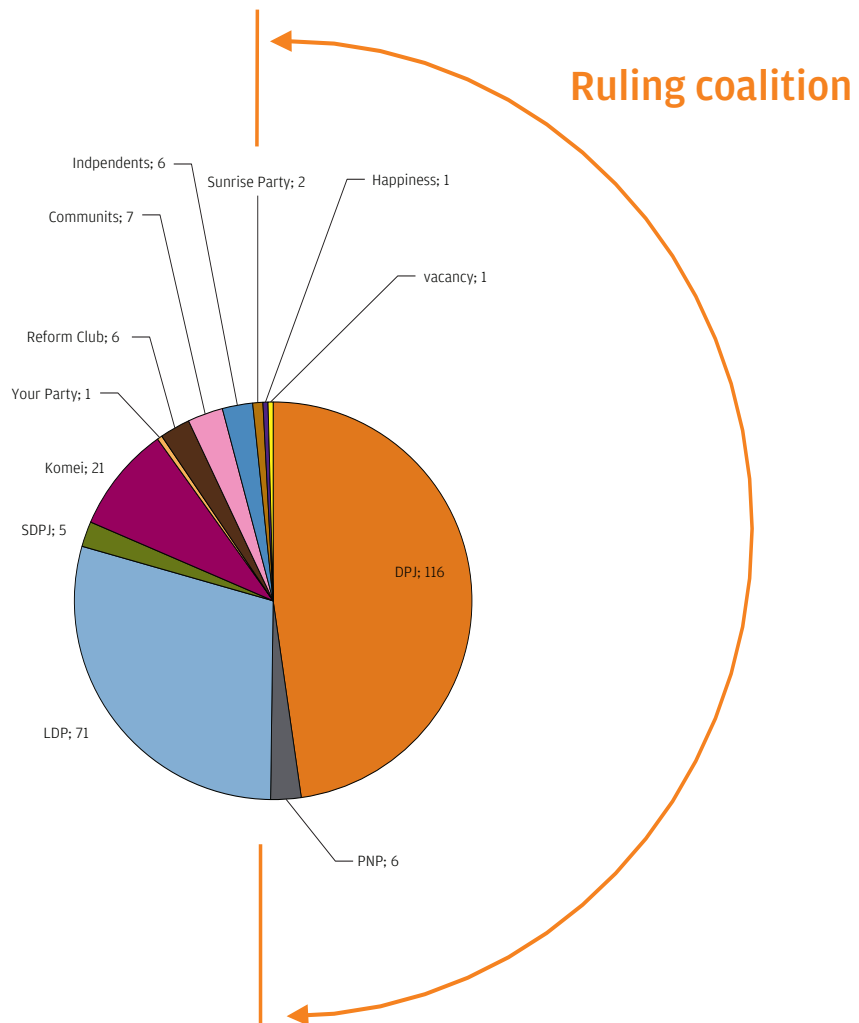
In the manifesto, there are two main focus points in terms of the DPJ's economic policy:

Manifesto focus point (1) tax reform. The key focus in the context of economic policy was tax reform. The manifesto included lowering the corporation tax rate as one of its pledges. It does not include specifics on the size or timing of corporation tax cuts, however, reducing Japan's very high effective corporate tax rate, currently at around 40% (international average 25-30%), should improve the global competitiveness of Japanese companies. The manifesto also includes a pledge to begin cross party talks on a radical overhaul of the tax system, including raising consumption taxes, to gain consensus as quickly as possible. A drastic rise in consumption taxes may have a negative impact on consumption, however, a gradual rise in expectations for a future increase in consumption taxes may help to end Japan's deflationary mindset. The current consumption tax rate in Japan is 5%.

Manifesto focus point (2) economic growth strategy. The promotion of infrastructure exports and the promotion of Japan as a tourist destination feature highly in the manifesto. One notable shift in advance of the new manifesto is a policy of getting Japan to benefit from infrastructure demand via direct lobbying of Asian governments. This should have a positive impact on companies active in areas such as railways, water, smart grids, and nuclear power generation. Policies aimed at promoting Japan as a tourist destination are also key.

Upper house election - 11 July 2010

The government's decision not to extend the current regular session of the Diet makes it certain that the upper house election will be held on 11 July. This follows a rapid recovery in support for the DPJ in the latest opinion polls, suggesting that the party could control majorities in both houses after the election.



Sources: Jiji Press Co., Nomura Securities, J.P. Morgan Asset Management.
Data as of 12 May 2010.

Winning 59 seats in this July's election would give the DPJ a standalone majority

Of the 242 upper house seats, 121 seats will be contested in the upcoming election. The upper house cannot be dissolved like the lower house, and seats have a six-year term of office, with half the seats contested every three years. The DPJ is currently the largest party in the upper house, with 117 of the 242 seats, but it is five short of the 122 seats needed for a standalone majority.

Winning 59 seats in this July's election would give the DPJ a standalone majority, since it already holds 63 seats that are not up for re-election. A majority would give the party control of both houses, the first time that would have happened in Japan since 1998, and it will bring political stability for three years until the next general election. This should allow sufficient time for the government to work on beneficial policies from a long-term view point.

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