# The Economic systems of Japan as compared to that of the USA

## Abstract

Japan and USA have a mixed economy, with the free market as the driving element. Japan has witnessed stagnation in its economic growth, while USA has seen an increased growth in GDP of $18.57 trillion. This paper focuses on the key drivers of Japan's economy and how its financial systems play that role. The research also identifies the economic systems that have a low productivity and how Japan can turn things around on such sectors. This research also shows how both GDP's, of Japan and the USA, are affected by the economic systems. Equally, this paper looks at the USA, the world's largest economy and how its free market and hands off policy on private business have aided its economic growth. Finally, this paper draws the strengths and weaknesses of both economies influenced by their policies.

## Introduction

An economic system refers to institutions and laws that regulate the economy of a country. Different countries have various economic systems, which govern their trade. An economy can be a free market, controlled market or a mixed market, which involve both free and control elements. Japan is a mixed market economy, with a market oriented approach, which is the second largest economy in the world (IMF, 2017; World Bank, 2017). The free market economy has allowed Japan to develop competitive economic systems, which have enabled it to rise as one of the steady and open economies in the world ("Japan | Data," 2017). Its economy is majorly driven by industrialization and service sectors, with agriculture accounting for about 3.9% of its GDP.

On the other hand, USA remains the largest economy in the world, with a GDP of $18.57 trillion, as at 2016. It has the largest mixed economy based on a free market, with diverse sectors, which contribute to its growth hence its economy is competitive. USA economy largely depends on industries, net exports, services, and agriculture ("Japan | Data," 2017). It has witnessed an economic growth since the 2009 recession, which affected many countries.

This research paper will compare the financial systems to outline the significant similarities and differences of the economic systems. Equally, this paper will establish the key drivers of economic systems of both countries – Japan and the USA (IMF, 2017; World Bank, 2017). The comparison will also be based on GDP and drivers of their economies. Consequently, the research will also evaluate the protection of critical sectors of each economy and the potential of easing control of such sectors of the economy.

This paper will discuss scholarly articles and peer reviews on the economic systems of Japan and that of the USA. The literature review will focus on GDP and key sectors of both countries. Consequently, the research will discuss the methodology to be used in the research. The method will be based on data and comparative analysis, as the critical way to obtain data. Equally, this paper will analyze the comparative data and draw a critical comparison to both economic systems of Japan and the USA. The final section of this paper will draw a conclusion and recommendations of the research.

## Literature Review

International trade has been the key element that has sustained Japan’s economy with strong productivity in less protected economic sectors. It had a nominal gross domestic product (GDP) of $ 4.939 trillion in 2016 ("Japan | Data," 2017). The free market approach has attracted many international companies to trade with the USA (Montgomery & Takahashi, 2014). The USA has a strong free market economy, where individuals produce goods and services and decide the price of such commodities. However, the economic systems of Japan face a major challenge to a slow economic growth, and many economists have called for economic structural changes before making an economic recovery ("Japan: Financial System Stability Assessment," 2017). The agricultural sector is highly protected in Japan, with imports and exports of agricultural products controlled by authorities.

Small, medium enterprises (SMEs) have not witnessed the needed growth to propel Japan into a steady economic output. The service sector in Japan contributes almost 75% of its GDP. Japan plans to double its productivity in the service industry by 2% annually, through to 2020 (Montgomery & Takahashi, 2014). The productivity in Japan is almost a half that in the USA. Montgomery and Takahashi (2014)show that even though Japan has a mixed economy, its economy needs serious reforms to charter a new economic front for Japan. Financial reviews of Japan have demonstrated that its protection of agricultural sectors and SMEs has hindered productivity, hence pulling back the much-needed growth (Montgomery & Takahashi, 2014). Its economic growth has consistently remained at 1.2%.

The export trade has considerably contributed to its economic growth, even though; it still maintains nontariff barriers that hinder efficiency and productivity but raises domestic prices. The bilateral trade with other countries has been minimal, and Japan's lack of willingness to open its protected economic sectors to international competition is cited as the contributor (IMF, 2017; World Bank, 2017). Equally, Nikkei Heritage (2017) shows that the financial sector market is competitive, even though, the government is involved as opposed to the USA, where the government has minimal control over banks and capital markets. Banks in Japan are well capitalized and have small shares of nonperforming loans.

## Methodology

This research will use a comparative analysis method to evaluate the economic structure of Japan and the USA. The data will mostly consist of GDP, purchasing power parity (PPP) and different economic sectors, which are free markets and controlled or protected. The comparative analysis method offers a clear view of the financial systems of both countries. The comparative method also will allow the research to critically evaluate the disparity in both economic systems and draw an objective result. The GDP of both countries will span from 2012 to 2016 with growth and stagnation being the point of focus. Data collection of GDP will be from an authenticated financial organization, such as International Monetary Fund (IMF) and World Bank (WB).

The comparative analysis method will also compare the economic culture of Japan versus that of USA. Commercial culture plays a significant role in the development of any economy. The significance of such commercial culture will influence the research on how economic systems fall and rise based on economic customs (Rafiq, 2012). Equally, a comparative analysis is the best way to look at this paper since it will not only identify the active economic systems of each country but also reveal the weak links in their financial systems. Japan, for a long time, has had a stagnating economy. In particular, this is important, especially, through a comparative analysis method to evaluate which sectors of the economy are holding it back from achieving its potential economic growth.

This research will compare the population of Japan to that of the USA with the aim of determining what impact the people of Japan have on its financial systems as compared to the USA. The comparison will be based on both the present population and the future estimated economic influence by decreasing population in Japan, as compared to that of the USA. Further, this is illustrated in table 1 below, which shows the GDP of Japan and USA from 2012 to 2016.

|  **GDP of Japan and USA from 2012 to 2016 ($trillion)** |
| --- |
| Year | Japan | USA |
| 2012 | 6.203 | 16.155 |
| 2013 | 5.155 | 16.691 |
| 2014 | 4.848 | 17.393 |
| 2015 | 4.383 | 18.036 |
| 2016 | 4.939 | 18.57 |

##  Analysis and Results

Even though Japan and USA have a closely related mixed economy with free markets orientation, it still lags behind in many fronts. The economic stagnation witnessed by Japan has held it back. The macroeconomics in Japan has been affected by the stagnation of Total Factor Productivity (TFP) growth, which has stalled the overall growth. Japan faces the dilemma of an aging population with reducing productivity (Rafiq, 2012). The agricultural sector is protected by the government. Mainly, this is through controlled imports of agricultural products and screening of agriculture related investments.

Japan’s GDP has shown a mixed growth with an up and downwards trend revealing the economic systems challenges from 2012 and 2016. For example, in 2012, Japan achieved a GDP of $6.203 trillion, which was the highest in a decade. The growth has influenced the growth of service systems in the country. The increase in export trade across the world, especially with Asian countries and America, mainly contributed to its economy, further increasing about 73% to the GDP (Rafiq, 2012). However, the agricultural sector still has a low productivity. The low productivity is notably as a result of protection approach by the government and the aging population.

### Financial Markets Systems Analysis and Comparison

Japan's banks are both privately and state owned, but the government controls the financial market. The banks buy shares in different companies and can also acquire other banks to form a business group (Ogawa, Sterken & Tokutsu, 2012). These business groups are about six in Japan, one of such groups is Mitsubishi (Ogawa et al., 2012). Consequently, private organizations, with sole ownership or majority shares, exist in Japan with a broad base in the financial markets. Such groups are closely monitored by the government (Rafiq, 2012). However, in the USA, the financial corporates are allowed to form a conglomerate and decide what to produce and, as well, set the retail prices. The USA government almost has a handed off policy on private property (Ogawa, Sterken & Tokutsu, 2012). The banks in the USA can give loans and have directors on such firms. Hence they have acquired a monopoly and make decisions on key issues in the financial markets. However, today, Japan has a vibrant commercial market, with banks recording high profits and investment outlook. The banks are well capitalized and regulated, while the USA also has a steady financial market but more free and broad based.

The export trade has continued to grow with 2016 recording one of the highest exports since economic stagnation (Nakamura, 2002). The export market is vibrant with a 13.4% growth in July 2017. Japan depends on USA, Europe and predominantly, the Asian countries for its exports. The increased growth in export trade has considerably contributed to the GDP growth. Conversely, the export trade in the USA has been on the rise, with the USA posting over $194 billion in exports in June 2017 as compared to $192, the same period in 2016. USA export market is Canada, with over 35 States reported having export goods to Canada as compared to any other country. However, the USA has a high productivity, with both the agricultural sector and the manufacturing industry being privately owned (Nakamura, 2002). High productivity ensures high export, hence GDP growth, while Japan continues to experience a low productivity. In particular, this hinders the GDP growth with a stagnant annual growth of 1%. The GDP growth in any economy must be influenced by high productivity (Nakamura, 2002).

### Demographic Economic System (Labor)

The economic population in Japan is at a critical stage, with an increasing number of aged work forces. The concept of the demographic economy requires a productive labor, which is affordable to the investors (Kajitani & Tatano, 2014). Japan has one of the highest aging populations in the world, with an estimated number of annual declines in the population at 308,084 by January 2017. Inadequate labor workers’ productivity and the economy can be slowed or left stagnant. The economic systems of any country largely depend on work as one of the factors of production. Some economists have referred to the Japan's population decline as a "demographic time bomb" a concept that matched the decline in population and a decrease in consumer spending (Jorgenson & Nomura, 2007).

However, the USA has witnessed an increase in population, which means it has a firm working with a great percentage of the labor force employed or actively seeking employment. Active labor force means that the country can achieve a high productivity and influence GDP growth. The USA also estimates to have a population of 420 million by 2060, which is 38% increase in population as compared to 301million in 2007(Jorgenson & Nomura, 2007). One of the high economic assets it has today is its young population.

### Capital (the value of capital goods)

Japan is one the countries, in the world, with the largest value of the equipment. In 2010, Japan exported capital goods and equipment worth $110 billion to East Asian countries, including China and Singapore. The capital of Japan has risen since 2016, with exports being the largest contributor. Conversely, USA has a capital base wider than that of Japan due to large manufacturing industries and equipment (Georgiou, 2013). Increased construction and development projects in the US have grown since the recession in 2009. In particular, this has led to an increase in capital and overall value.

### Natural resources as an economic system

Japan has several natural resources, including a wide variety of minerals such as gold, copper and rare metals used in individual industries. In the commercial industry, Japan has, cement, steel, iron, petroleum, natural gas and rare earth (Weller, 2017). The vast minerals found in Japan have aided it in its economic recovery and self–sustenance, during economic woes. Significant exports of minerals have contributed to its GDP growth. Japan has the natural reserve of minerals, such as Silica sand and Silica stones, limestone Dolomite and iodine (Weller, 2017). Equally, America has vast natural resources, such as oil, natural gas, nickel, copper, gold, and silver. The economy of USA greatly depends on oil and gas just as seen in the case of Japan.

### Entrepreneurship as a factor of production

 Overall, Japan has a bureaucratic process when starting a business, a factor which is cited as an impediment to its economic growth. The protectionist approach taken by Japan prevents investors from taking the risk in its market (Fukao & Yuan, 2016). The entrepreneur aspect is not encouraged due to limiting factors, such as bureaucracy and control. Conversely, in the USA the risks takers are free to conduct business, as there is less red tapes and control of companies. The efficiency in the market allows many investors to invest in different businesses. These investors are allowed a level playing field.

### Consumer purchasing power

 Japan is facing a decline in consumer spending, which contributes to a decline in the population and slow economic recovery. The element of purchasing power parity in Japan continues to stagnate despite the low nonperforming loans and job creation (Weller, 2017). Japan has mostly benefitted from exports of its local products with domestic consumption not yielding as it should. On the other hand, USA has highly benefitted from its growing population since an increase in population, with a thriving economy. The economy in the USA has continued to grow with consumers witnessing a rise in the purchasing power.

## Conclusion and Recommendation

Japan remains one of the major economies in the world, and its economic systems are crucial to the overall global economic growth. The agricultural sector continues to perform dismally due to government protection of the industry. The mining sector is the vibrant area with vast resources. Financial markets in Japan continue to play better with banks witnessing a viable growth and stability. Japan's mixed economy, based on free market, has the prospect of achieving an expanded macroeconomic growth. Economic systems in the USA are more vast and vigorous as compared to that of Japan in respect to industries, financial markets, transport network and overall economic growth. The USA’s GDP remains the highest in the world and the projection of its macro, and micro economic growth remains vibrant with the increase in consumer spending.

## References

Fukao, K., & Yuan, T. (2016). China's Growth Slowdown: Lessons from Japan's Experience and the Expected Impact on Japan, the USA, and Germany. *China & World Economy*, *24*(5), 122-146.

Georgiou, M. (2013). Restricting Shadow Economy versus Macroeconomic Impacts. A Panel Data Analysis in EU, Japan, USA. *SSRN Electronic Journal*.

*Japan | Data*. (2017). *Data.worldbank.org*.

Japan. (n.d.). *Comparative Economic Systems,* 123-142.

*Japan: Financial System Stability Assessment*. (2017). *IMF*.

Jorgenson, D., & Nomura, K. (2007). The Industry Origins of the US–Japan Productivity Gap. *Economic Systems Research*, *19*(3), 315-341.

Kajitani, Y., & Tatano, H. (2014). Estimation of production capacity loss rate after the great east japan earthquake and tsunami in 2011. *Economic Systems Research*, *26*(1), 13-38.

Kremer, M. (2006). Globalization of Labor Markets and Inequality. *Brookings Trade Forum*, *2006*(1), 211-228.

Montgomery, H., & Takahashi, Y. (2014). The economic consequences of the TARP: The effectiveness of bank recapitalization policies in the U.S. *Japan And The World Economy*, *32*, 49-64.

Nakamura, M. (2002). Mixed ownership of industrial firms in Japan: debt financing, banks, and vertical keiretsu groups. *Economic Systems*, *26*(3), 231-247.

Ogawa, K., Sterken, E., & Tokutsu, I. (2012). Financial distress and industry structure: an inter-industry approach to the lost decade in JAPAN. *Economic Systems Research*, *24*(3), 229-249.

Rafiq, S. (2012). Is Discretionary Fiscal Policy in Japan Effective?. *The B.E. Journal of Macroeconomics*, *12*(1).

Weller, C. (2017). *Japan's population is falling faster than it ever has before*. *Business Insider*.