By Scott Bessent

Abe's Complicated Legacy

His foreign policy architecture may help avert an international conflict, but his economic policies may have sown the seeds for a major financial crisis.

Shinzo Abe, the two-time and longest serving prime minister of Japan, assassinated on July 8, 2022, should be remembered as one of the great transformational government leaders of the past fifty years. Similar to Margaret Thatcher, Ronald Reagan, and Helmut Kohl, who all led their countries through economic shocks, foreign threats, and domestic makeovers, Prime Minister Abe was reelected in 2012 for his second tenure and faced a period fraught with internal malaise and rising external tensions.

From 2012 to 2020, he reconstructed his country's security, economic, societal, and financial structures. He led a domestic economic revival and re-established Japan's geopolitical leadership. Abe believed that a strong Japan required a strong economy. In 2012, he and his economic advisors devised the financial market catchphrase of the year, the "Three Arrows": loose monetary policy, fiscal flexibility, and structural economic reforms. These policies constituted the core of Abenomics, arguably the most talked about financial agenda in 2012 and 2013.

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Ultimately, parts of his agenda carry on today, while other pieces were never fully implemented.

Foreign writers have consistently catalogued his achievements in narrow fashion along single topical lines, rather than viewing them, and the man who reframed his country, in a more holistic way. It is important to examine Abe's background, the unsure moment in 2012 of Japan's place in the world order, the Japanese people's guarded longing for strong leadership, and his unconventional method of governing in order to appreciate fully how his policies continue to shape his country, global markets, and international institutions today. Just as Germany's Chancellor Kohl advocated for more European integration as a co-author of the Maastricht Treaty and supported U.S. President Reagan to weaken the Soviet Union, Abe reframed an alliance of Asian, European, and American democracies to counterbalance China.

Abe should be remembered as one of the great transformational government leaders of the past fifty years.

In many ways, Abe and UK Prime Minister Thatcher shared an uneasy relationship within their parties and with vast swathes of the electorate who still continued to vote for them. Thatcher was an outsider, a trailblazer in a male-dominated arena, and a relentless free-marketeer. She eschewed the polite compromise politics of her Etonian-Oxbridge colleagues. She led Britain through a ferocious miner's strike, a war with Argentina, and into the coalition to liberate Kuwait. While she was a *bête noire* for those on the left, it was ultimately the uneasy relationship with her Tory party colleagues that brought her down.

Abe elicited strong emotions from both sides of the political spectrum. His family history, especially the career of his maternal grandfather, Nobusuke Kishi, the controversial founder of the LDP Party and prime minister, drew support from Japanese nationalists. However, his support for revising Japan's constitution, specifically Article 9 to allow for a standing army, was met with mixed feelings from centrist voters and howls of disapproval from left-wing constituents. At the end of their careers, both Abe and Thatcher enjoyed a greater popularity on the world stage than in their own countries.

In 2012, Japan was a sleeping giant poised for a constructive awakening to remake the country's post-war identity, replacing tired domestic policies and a vacuum in Indo-Pacific security. The island nation was facing a crisis of national spirit, driven by several seemingly intractable forces: a debt overhang, a deflationary mindset, and a population both aging and shrinking.

Prime Minister Thatcher and President Reagan came to power in periods of similar national self-doubt in their respective countries. Abe re-entered as prime minister just in time to prevent the world's third-largest economy's irrelevance on the global stage. From 2006 to 2012, Japan had six different prime ministers, beginning with Abe whose first ignominious iteration lasted less than a year. China had just passed Japan to become the second largest economy in 2010.

Two decades of economic debilitation, resulting from the unwind of the post-bubble economy, had sapped the previous dynamism of many Japanese corporations. Households were in retreat, hoarding savings and witnessing ever-declining birthrates. The central government had engaged in an economic smoothing operation for most of the past twenty years. This long-term fiscal stimulus was leading many economic and financial analysts to believe that Japan's budget situation and debt stock were unsustainable. Japan's stock indices hovered near forty-year lows, corporate profitability metrics were among the lowest in the developed world, and foreign brokers and banks had abandoned Tokyo for Hong Kong, Singapore, and Shanghai.

In 2012, the people of Japan were still disheartened by the horrific images of the Fukushima nuclear tragedy that occurred in March 2011. As the world watched aghast at scenes of what might have been a nuclear meltdown, the Japanese government mounted a hapless response that demoralized the nation. As a precautionary measure, the government shut down the country's nuclear power plants that had provided the backbone of Japan's electric grid. Recriminations grew between the utility companies, regulators, and the anti-nuclear segment of the population.

Abe's complicated legacy is likely to grow more so in the coming few quarters or years.

China's rise and assertiveness took on a physical manifestation in 2012. When the Japanese government purchased three of the uninhabited Senkaku Islands in September of

"The Man Who Broke the Bank of Japan"

In the larger article, I delineate from an economic, historical, and financial markets point of view the mostly good but also the inconsistent and uncompleted work of the Abe administration. Below is a brief narrative of my personal views, experiences, and outlook on the decade since Abe re-emerged as prime minister.

In the summer of 2012, George Soros suggested I get in touch with his friend, the distinguished journalist and think tank head Yoichi Funabashi. Funabashi-san had just alerted him to the nascent plans of former Prime Minister Shinzo Abe to mount a run for the LDP leadership on a platform that would dramatically alter the path of Japan and in many ways forever transform the world's security and financial markets arrangements. Abe proclaimed to both domestic and international audiences that "A strong Japan required a strong economy." In mid-2012, this seemed an impossibility as Tokyo had gone from the center of the financial world to a near-backwater.

It was more than a market ride for me. As I shuttled back and forth from New York to Tokyo on a monthly basis, it was inspiring over the years to watch a coordinated effort between the government and its citizens to reinvigorate a nation.

Soon after, on a day I'll never forget, I met with Abe advisor, Japanese expatriate, and Yale economics professor Koichi Hamada. Soros, my associate Francis Browne, and I dined among athletic trophies in the storied private Mory's club on Yale's campus as Professor Hamada outlined the early formulations of Abenomics. The professor and George were both hard of hearing, a fact that was exacerbated by their respective Hungarian and Japanese accents. Much of the conversation had to be repeated. With each of the professor's pronouncements, I grew increasingly excited by the potential magnitude of the market moves if these policies were implemented. I became convinced that Abe and his circle of advisors would commit to directing all of the resources of the prime minister's office to this multi-pronged and daunting task.

On the drive back to Manhattan, George asked me if I thought this plan would work. I gave him a blunt assessment. "I'm not sure whether it will work, but it will be the market ride of a lifetime."

And so it was. But it was more than a market ride for me. As I shuttled back and forth from New York to Tokyo on a monthly basis, it was inspiring over the years to watch a coordinated effort between the government and its citizens to reinvigorate a nation. Along the way, I met some wonderful people in both the public and private sector whom I am still privileged to call friends: Professor Hamada, Professor Takatoshi Ito, Seiichiro Takahashi, and Nobuchika Mori, to name a few.

A major financial news organization called me "the Man Who Broke the Bank of Japan," but that was not accurate. The Bank of Japan did not need to be broken—all it needed were market participants who would believe newly appointed Governor Haruhiko Kuroda's determination to apply massive monetary easing. Unlike many typical currency devaluations, it was not a fight against the central bank, and I was their willing messenger. Capital flows to where it is treated well. Under the corporate stewardship program and other shareholder-friendly measures, Japanese assets regained their role in portfolios around the world.

President Trump's most enduring achievement may have been to wake the United States and the world to the growing dangers of an ever-more-antagonistic China. In response, Abe's greatest foreign policy achievement was taking this awakening and developing a multilateral solution for containment.

Abe proved that you can put your nation's interest first, while still maintaining a strong alliance with your allies. It is unfortunate that Abe is not with us today as a sagacious voice in this multi-crisis world.

On the financial front, today, almost ten years later, we are moving into the end game for the Bank of Japan's fantastical decade of ultra-loose monetary policy. These policies have nurtured Japan but created a relentless asset inflation in the rest of the world. The Bank of Japan's policy of yield curve control has anchored interest rates around the globe, suppressing fixed income term premiums. Perhaps the home stretch of the financial experiment is upon us within the next six months—and it may prove the wildest part of the ride yet.

Along with the rest of the world, I was in shock when Abe was assassinated in July. He was the ultimate insider, the scion of two political dynasties, who governed like an outsider. Abe's teenage friend and lifetime confidant, legendary investor Takahashi-san, relayed to me that over a round of golf in May Abe had told him that Japan was on the brink of exiting its deflationary period. He concluded by saying, "Abe was a man of deep insight and an extraordinary ability to get things done."

Many thought Abe might have come back for one more round as prime minister. We will never know if that would have been as big a success as his second term. With Xi Jinping consolidating control of the Chinese Communist Party in a manner unseen since Mao Zedong, Western democracies would have surely benefited from his statecraft and leadership.

—S. Bessent

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that year, a wave of protests swept China. The islands had been the subject of a territorial dispute between the two countries since 1970. Beijing responded with increased air-force sorties into the islands' airspace combined with aggressive positioning of both civilian and military vessels in the area. The BBC described the situation as "the most serious for Sino-Japanese relations in the post-war period in terms of the risk of militarized conflict." The specter of kinetic conflict against a much larger and emboldened opponent loomed large in the Japanese psyche.

Shinzo Abe, like the lionized British Prime Minister Winston Churchill, was one of the rare developed world leaders given a second chance after being removed from office. Remarkably, it is unlikely that Abe's unique ability to govern in the consensus-driven Japanese system would have been possible without his earlier missteps. Abe the important domestic and global leader could not have existed without Abe the failed politician.

Upon arriving in office in December 2012, the former prime minister hit the ground running. He better understood how to manage the bureaucracy, wielding the levers of power with confidence and aplomb. "Abe was a statist," according to award-winning journalist, editor, and think tank founder Yoichi Funabashi, but in his second iteration he moved the power of the state away from the civil servants and back to the Kantei (the prime minister's office) and the ministers. Funabashi believes that Abe was also a restorationist, adopting Meiji-era leader Shimazu Nariakira's mantra, "If we take the initiative, we can dominate; if we do not, we will be dominated."

Two aspects of Abe leaving and returning to office were notable. First, Abe's personal disquiet with his unsuccessful initial term caused him a great deal of personal grief, according to close friends and family. It is said that his mother, the daughter of a former Japanese prime minister, lectured him on how he had mishandled his office, coaching Abe on how to be a more effective leader.

Whether it stemmed from maternal advice, another confidant, or his own reevaluation, Abe remade his approach to government in his second time in office, forming committees of outside experts to establish corporate governance codes. Abe refashioned the world's largest pension fund, Japan's Government Pension Investment Fund, or GPIF, and used its power to further his corporate stewardship agenda and to buy foreign assets, weakening the Japanese currency. In January 2013, he created a memo of understanding between the prime minister's office and the Bank of Japan. Using this document, Abe then appointed a dedicated reflationist, Haruhiko Kuroda, as governor to implement the most powerful of the Three Arrows, aggressive monetary easing.

The Japanese bureaucracy is world-renowned: equally admired and derided for its formidable attention to detail, planning, and dedication. As in all bureaucracies, it is designed to avoid mistakes and see to the smooth running of government. It is constructed to administer, rather than to lead. Often this administration bumps up against governing on behalf of the electorate. In the chaotic period from 2006 to 2012

Abe believed that a strong Japan required a strong economy.

with the revolving door for prime ministers, the bureaucracy was in charge as it had not been since the days before popular and long-serving Prime Minister Junichiro Koizumi.

Abe had served as Chief Cabinet Secretary for Koizumi. He watched as his party leader fought through red tape to achieve his longstanding goal of passing a bill to privatize Japan Post Bank. This single achievement used up much of Koizumi's political capital.

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Abe also surrounded himself with a strong team that was mostly able to badger and work around the permanent state. This team was led by Chief Cabinet Secretary Yoshihide Suga. Taro Aso, arguably one of Japan's most important political leaders in recent decades, also played a key role. Suga became known as an enforcer of the wishes of the Kantei, making his displeasure known when the Abe government received negative publicity, there were adverse market movements in the yen or the equity markets, or Abe's policies were not being implemented with appropriate speed. Suga followed Abe as prime minister. It is widely believed that the bureaucracy that he had bashed during the Abe era got its revenge by throwing sand into the gears during his time as prime minister.

Team Abe

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The key element in grand strategy, according to Yale military historian John Lewis Gaddis, is the consistency of aspirations and capabilities. Abe had great aspirations but understood that he was constrained by domestic politics and low military power. According to respected Tokyo economist Robert A. Feldman, "Abe was one of the few global leaders to align aspirations and capabilities. He was also the rare leader who understood the economic basis of geopolitics." Feldman's remarks harken back yet again to Abe's mantra of a strong Japan requiring a strong economy. His Three Arrows plan formed the basis for this economic rejuvenation.

Since the jarring events in Fukushima in 2011, the Japanese yen had consistently screened as among the most overvalued currencies in the world. This overvaluation, accompanied by disordered domestic policies, had caused Japanese corporates to offshore production, forcing down wages and creating a surfeit of workers. The strong exchange rate also retarded profits and did little to entice consumption in an economy where consumers were clinging to their savings. Prior to the full national ban on nuclear power in May 2011, Japan had been running a persistent current account surplus of approximately 3 percent of GDP. After this date, when fossil fuel imports dramatically increased, the current account swung to a several-point deficit.

Both Shinzo Abe and Margaret Thatcher enjoyed a greater popularity on the world stage than in their own countries.

SEIICHI OTSUKA

Award-winning journalist and think tank founder **Yoichi Funabashi:** *Abe was a statist, but in his second iteration he moved the power of the state away from the civil servants and back to the Kantei (the prime minister's office) and the ministers. Funabashi believes that Abe was also a restorationist, adopting Meiji-era leader Shimazu Nariakira's mantra, "If we take the initiative, we can dominate; if we do not, we will be dominated."*

Many operators in the foreign exchange market were perplexed by the yen's continued strength in a weak economy mired in deflation. Then-Bank of Japan Governor Masaaki Shirakawa was not one of them. The conservative deflationist refused to deploy many of the experimental tools with which his counterparts at the Federal Reserve, European Central Bank, and Bank of England had become enamored. The Bank of Japan limited its nonstandard operations to a mild form of quantitative easing under Shirakawa, buying very-short-duration securities that ran off the balance sheet in a matter of months.

With guidance from economic advisors such as Professor Takatoshi Ito, then of the University of Tokyo, and Yale Professor Koichi Hamada, a student of Nobel Prize-winning economist James Tobin, Abe formulated a plan to achieve 2 percent economic growth and 2 percent inflation within two years. Early followers of this plan may recall that it originally called for three, three, and three, but was quickly scaled back to more realistic but still ambitious assumptions.

Much of the monetary scheme centered on the retirement of several Bank of Japan board members and their replacement by members inclined toward greater central bank stimulation in the form of lower rates, large-scale asset purchases, extensive forward guidance, and perhaps even expanding the toolkit to more experimental policies.

The culmination of the Bank of Japan makeover was Shirakawa's retirement in March 2013. Abe had signaled to the market as early as the previous December that a new governor with a willingness to accelerate the pace of asset accumulation and extend the maturities of the debt it was buying would be put in place. In late February 2013, former Ministry of Finance official and then-head of the Asian Development Bank, Haruhiko Kuroda, was announced as Abe's choice for the new Bank of Japan governor. Kikuo Iwata, an even more radical academic reflationist, was nominated as deputy governor. These nominations marked the end of the Shirakawa board—known to some observers as the Guardians of Deflation.

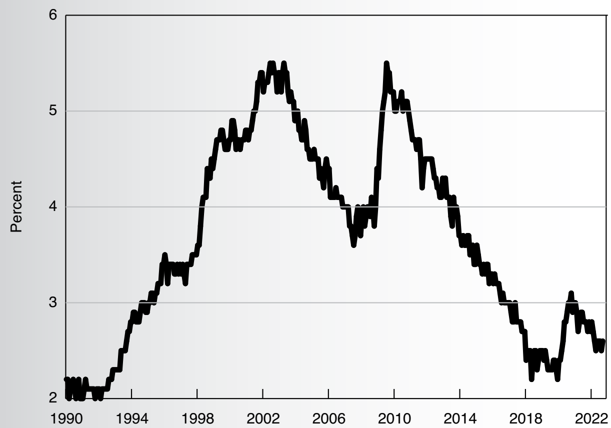
The First Arrow was launched with great power and accuracy at the April 2013 Bank of Japan meeting. Kuroda announced a substantial increase in the bond-buying program, an extension of the duration of the assets to be purchased, and the purchase of risk assets including exchange-traded funds and JREITs. The markets obliged the Bank of Japan signals with the yen weakening substantially over the coming months and the Tokyo stock indices skyrocketing. The Bank of Japan's initial aim was to double the money supply in two years.

A fledgling and contorted form of Modern Monetary Theory was born. With the central bank under his control, Abe's next arrow to launch was a fiscal one. In essence, his administration was providing a real-time experiment for Warren Mosler, L. Randall Wray, and Stephanie Kelton's untested doctrine.

The Second Arrow of Abe's revitalization plan was perhaps the least well understood, and likely the most ineffective, particularly at the outset. While it was commonly termed "fiscal stimulus" by the Western press, an idea perhaps encouraged by an administration eager to drum up interest in Japan, the reality was more nuanced. Government expenditure did indeed rise throughout Abe's tenure, aided by a series of large, infrastructure-heavy stimulus packages. However, fiscal stimulus was not seen as an end in itself. Rather, Abe viewed short-term stimulus as a necessary salve to make palatable the long-term structural and fiscal reforms he envisioned. Ultimately, Abe wanted to stabilize Japan's massive public debt load, and to achieve a primary budget surplus. Initially, this primary surplus goal was set for 2020, but was later pushed back to 2025 as it became increasingly out of reach.

Unemployment Plummeted Under Abe

Japan unemployment rate



Abe Reinflated Japan

Consumer price index excluding fresh food and energy, change year over year

To stabilize the debt load and put Japan on a firmer fiscal footing, Abe twice raised Japan's consumption tax rate. In both instances, this was a controversial move, as the prior consumption tax increase in 1997 had been widely blamed for triggering a deep recession. However, Abe pushed ahead with the first increase as scheduled in 2014, raising the tax rate from 5 percent to 8 percent. This did come at some cost. Domestic consumption fell markedly following the increase as did inflation, when adjusted for tax effects. Consequently, while the fiscal situation

Masaaki Shirakawa, *governor of the Bank of Japan from 2008 to 2013.*

What Yen Problem?

After 2011, when fossil fuel imports dramatically increased, the current account swung to a several-point deficit. Many operators in the foreign exchange market were perplexed by the yen's continued strength in a weak economy mired in deflation. Bank of Japan Governor Masaaki Shirakawa was not one of them. The conservative deflationist refused to deploy many of the experimental tools with which his counterparts at the Federal Reserve, European Central Bank, and Bank of England had become enamored. The Bank of Japan limited its nonstandard operations to a mild form of quantitative easing under Shirakawa, buying very-short-duration securities that ran off the balance sheet in a matter of months.

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improved, Abe's goal of achieving 2 percent inflation was put further out of reach.

Following the 2014 experience, Abe twice postponed the second consumption tax increase, which raised the rate from 8 percent to 10 percent. After the second postponement, Abe declared that nothing short of "the global financial crisis triggered by the collapse of Lehman Brothers" would cause further delay. Ultimately, the increase took effect in October 2019, and the economic impacts were mitigated by a number of stimulus measures, including government-provided "gift certificates" and rebates for cashless transactions. However, the fiscal benefit of the increase would prove short-lived. While Abe was successful in reducing the primary deficit from 7 percent in 2012 to 2 percent in 2019, the progress was largely undone during the Covid pandemic, from which Japan is only now beginning to recover.

As the fiscal failing became more and more of a feature, rather than a bug, of the Three Arrow ecosystem, the Bank of Japan's expansive monetary policy was called on to compensate. As will be discussed below, the denouement of this overreliance—and the effects of a decade of transmission to global asset markets—may prove to tarnish the numerous other admirable achievements of Abenomics.

ABE'S STRUCTURAL CHANGES

Structural reform in the Japanese economy was always going to be a more heavy lift than even the heightened fiscal stimulus. Abe's greatest achievement may have been in expanding the workforce by increasing the female participation rate. This subset of his platform became known as "Womenomics." Female workforce participation had been low by developed country standards when Abe returned in 2012. Professor Hamada maintains that "I considered him more liberal on some economic issues than me." Abe understood well that while the overall population was declining, it was the growth of the workforce that mattered for GDP. "Abe invented a metric 'wages per family' that he liked to look at when more women came into the workforce," according to Hamada. "He cared deeply about Japanese workers and the security of his country." A decade later, Japan now stands at 72 percent of working-age women in the workforce, more than ten percentage points above the starting point in 2012 and six percentage points above the rate in the United States.

On the corporate front, the Abe administration had victories in corporate reform, shareholder rights, and a push for higher corporate returns on capital. The prime minister personally praised companies that increased their returns. Jesper Koll, a Tokyo-based economist and one of the keenest observers of Japanese policy intricacies, summed up the management style of Abe Redux well: "He built a core team of not only allies but real partners to turn Japan back toward a respected first-tier nation. He used the stewardship code as a blueprint and GPIF as a strong enforcement mechanism," according to Koll.

Much of this work was done initially by Akira Amari, minister in charge of economic revitalization, and his successor in that position, Toshimitsu Motegi. Large swathes of Abe cabinet contributed to the micro-focused "Japan Revival, through strong, sound companies." Yoshimasa Hayashi, Hiroshige Seko, and Yasutoshi Nishimura were just a few of his inner circle who put forth the policies of reducing cross-shareholdings, promoting the introduction of

From 2011 to 2020, the foreign labor force in Japan more than doubled.

independent outside directors, and formulating a new corporate governance code. Even the Ministry of International Trade and Industry got on board in 2019 with a directive outlining fair merger and acquisition guidelines. Indeed, in 2014 only 21.5 percent of the largest Tokyo Stock Exchange-listed companies had two or more independent directors. This figure reached over 93 percent by 2019, according to Feldman.

In June 2013, the government published a paper written by the Liberal Democratic Party on May 23, 2014, entitled "Japan Revival Vision." It was widely regarded at the initial blueprint for much of the Third Arrow.

The quadruple combination of promising shareholder friendly initiatives, short-term fiscal interventions, monetary stimulus, and a rapidly depreciating yen sent a generation of investors taught to shun Japan scrambling to Tokyo and beyond in search of cheap stocks and clues about the Abe government's next moves. Within the Kantei, the performance of the stock indices became a symbol of the renewed strength of the Japanese economy, projecting a confidence not seen in the nation for more than two decades.

It was assumed that the new emphasis on profitability and return on capital would find its way into long-overdue outsized wage gains for Japanese workers, but this did not occur. As will be discussed in greater detail below, the intransigence of Japanese employers was a key factor in preventing Kuroda from achieving escape velocity in his inflation fight. This has created an odd equilibrium of sorts: Japanese inflation remains below target; Kuroda provides ever more monetary stimulus; and this monetary expansion has weakened the yen and flooded into asset markets around the world. Japanese investors condemned to negative real returns by the Bank of Japan have become amongst the largest investors in Australian bonds, French bonds, U.S. credit, private equity investments, and Asian lending. It is indeed a perverse outcome that benign domestic inflation in Japan has inflated assets and subdued term premium around the globe. It is clearly not the result that Abe and his advisors envisioned in the autumn of 2012.

Abe the important domestic and global leader could not have existed without Abe the failed politician.

Corporate intransigence and the fiscal stop-and-start caused two arrows to miss their target. While Abe was a statist, he was reluctant to take the monumental step of imposing a dramatic increase on the annual spring wage rounds in Japan known as the Shunto. The prime minister and his team were willing to exert public and moral pressure on the powerful Japanese business federation, Keidanren, but they were never willing to cross the rubicon and mandate a level of wage hikes. Even with a weaker yen, increased domestic spending, and a strong global economy, Japanese corporates, scarred by the aftermath of the bubble years, refused to raise wages to a level that would have given domestic inflation escape velocity. This was even after Japanese non-financial company profit as a

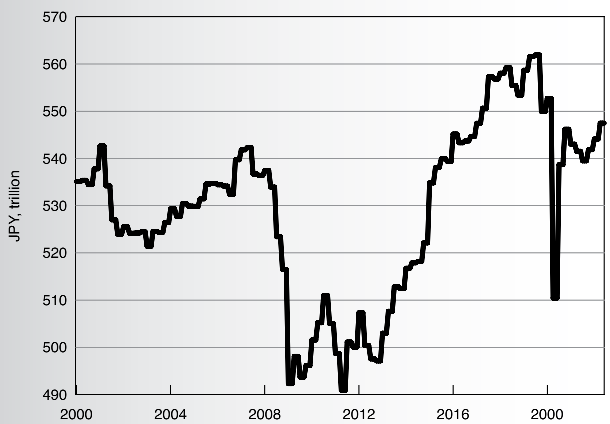
Eye-Popping Demand Shock

Adding fuel to the monetary bonfire, Prime Minister Fumio Kishida's government has announced a supplementary budget of ¥29.1 trillion. To put this into context, this is larger than those following the Lehman shock (¥19.7 trillion) and the 3/11 tsunami disaster (¥16.6 trillion), as well as Abe's Second Arrow 2013 budget (¥15.7 trillion). The current fiscal stimulus will amount to approximately 6 percent of GDP—an eye-popping number.

—S. Bessent

Abe Jolted Japan Out of Post-GFC Slump

Japan nominal GDP

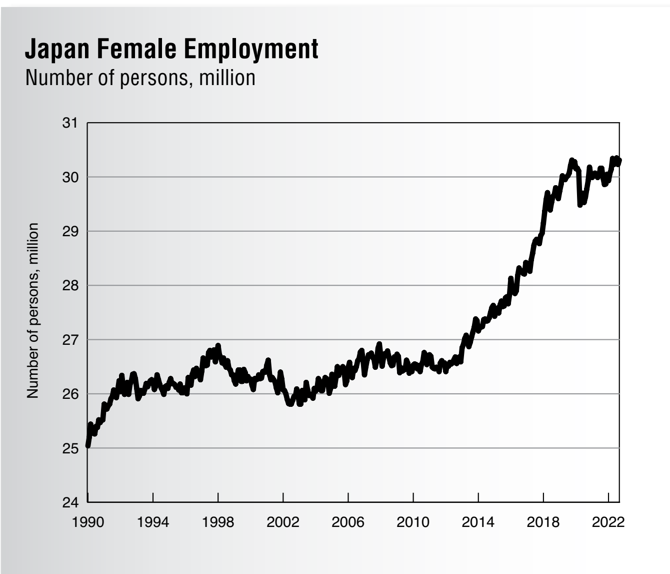


percent of revenue reached 8 percent—more than double the peak in 1990.

Abe's plan for reordering Japan was not just on the corporate front or in the markets. He recognized that tourism could become a major source of revenue and employment for the Japanese economy. The weak yen and a welcoming tourist campaign increased Japanese visitor arrivals from 8.5 million the year he took office in 2012 to 32 million in 2019. The 2020 Olympics were supposed to be Abe's crowning achievement in his campaign to attract overseas visitors. The games were delayed due to the Covid pandemic, and Japanese arrivals collapsed to a negligible number under the island nation's strict lockdowns. Japan will be reopening this year. Given the substantial depreciation of the yen in the most recent twelve months, the country is expecting a tourism boom even above the Abe years, especially when international travel restrictions in China are eventually lifted.

Long regarded as an unwelcoming place for inbound immigration and guest workers, Japan was quietly transformed by one of Team Abe's most invisible achievements. From 2011 to 2020, the foreign labor force in Japan more than doubled. The practical prime minister who many called an ultra-nationalist was also an ultra-pragmatist. He and his advisors understood that Japan's growth would be constrained if the newly created construction and tourism jobs remained vacant. With little fanfare, they passed two new visa categories making it easier for foreigners to gain work permits. Again, the need for a strong economy overrode any lingering anti-immigration instincts.

With Japan's economy on the uptick, the prime minister worked closely with his Minister of Defense Taro Kono and his longstanding foreign policy advisor Tomohiko Taniguchi early in his administration to formulate a strategy for Japan to reassume its geopolitical leadership role. According to Taniguchi, the core of this blueprint included reengaging with the United States and expanding diplomatic ties with Australia and India. The Quad was reinvigorated as a counterbalance to China.



Abe courted Indian prime ministers Manmohan Singh and Narendra Modi. He managed to maintain good relations with President Obama and formed an especially strong relationship with President Trump. The two shared a concern for China's rise and a love of golf.

Abe had great aspirations but understood that he was constrained by domestic politics and low military power.

The Chinese foreign ministry and Xi Jinping himself were likely surprised by Abe's ascendancy in 2012. Undoubtedly, the disarray around the short tenures of the six previous prime ministers suited Beijing's hegemonic ambitions in Asia. Eventually, the Chinese leadership acknowledged that Abe had returned Japan to a top-tier power, proffering Abe a state visit in 2018.

In her 2018 book *The Third Revolution,* Elizabeth Economy, a senior fellow at Stanford University's Hoover Institution and senior advisor for China at the U.S. Department of Commerce, examines how under President Xi, Beijing assumed a more ambitious geostrategic posture, reversing its low-profile foreign policy since the days of Deng Xiaoping. This shift was obvious to Abe even before he took office, according to his close advisors. As the world watched Xi anointed to his third term as president in late October, it became clear that his autocratic ambitions are greater than Abe or Economy would have predicted a few years ago.

In his tribute shortly after Abe's death, former Australian Prime Minister John Howard described his Japanese counterpart as the "driving force behind the vision of a free and open Indo-Pacific region and the establishment of the Quad." Howard went on to note that while Abe's statesmanship and courage in addressing the threat of China's rise was obvious to many, it was his "warmth and personal commitment" that caused the leaders to coalesce around his ideas.

The multi-faceted, complicated leader met an ending in July that set off a wave of recriminations in Japan about the

LDP's shadowy relationship with the Unification Church. His assassination was carried out by suspect Tetsuya Yamagami, who admitted to police he killed Abe because of his affiliation with the South Korean-based church. Outside of Japan, this goes largely unnoticed, but inside the country this association has muddied Abe's legacy.

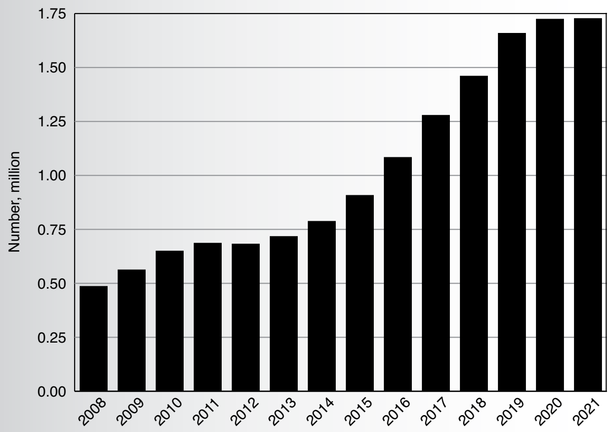
As we note the tenth anniversary of Abe's second election as prime minister in 2012, many aspects of his legacy as previously discussed are settled as successes, failures, or stalemates, but two of the most important are unresolved and likely approaching their respective endgames.

Abe's construction of an Indo-Pacific alliance is likely to be tested in the near future as China defines a new status quo with its relationship with Taiwan. Since U.S. Speaker Nancy Pelosi's visit to Taipei in August 2022, China has increased its incursions into Taiwanese sea and air space and raised the level of aggressive rhetoric, refusing to renounce the use of force for reunification.

Without Abe's leadership on the frontlines, how will Asian neighbors and Western democracies respond to a kinetic attack by the PRC on Taiwan? When Russia crossed the internationally recognized borders of Ukraine in February, Abe drew a grim parallel to what may await Taiwan. We do not know when or if it will happen, but it is clear his early coalition building will prove prescient.

In the financial markets, the Bank of Japan's aggressive easing measures are being tested by the global post-Covid inflationary surge, spurred by monetary and fiscal injections in 2020 and 2021. These have been exacerbated by commodity supply shortages stemming from the Russian invasion of Ukraine and generally tight crude and refined product supplies. The Bank of Japan stands alone as the one major central bank, other than the People's Bank of China, not to raise rates. Governor Kuroda has stated that he does not believe domestic Japanese inflation is on a sustainable path after nine years of ultra-loose policy. Thus far in 2022, the Japanese yen has been the weakest major currency against the U.S. dollar. In uncharacteristically chaotic fashion for the normally hyper-coordinated Japanese policy apparatus, the Bank of Japan is running an expansive monetary policy while the Ministry of Finance intervenes in the currency markets in record one-month amounts to avoid a disorderly depreciation of the yen.

Abe's greatest achievement may have been in expanding the workforce by increasing the female participation rate.



Japan Foreign Labor Force
Number, million

Adding fuel to the monetary bonfire, Prime Minister Kishida's government has announced a supplementary budget of ¥29.1 trillion. To put this into context, this is larger than those following the Lehman shock (¥19.7 trillion) and the 3/11 tsunami disaster (¥16.6 trillion), as well as Abe's Second Arrow 2013 budget (15.7 trillion). The current fiscal stimulus will amount to approximately 6 percent of GDP—an eye-popping number absent a gigantic demand shock. This aggressive combination of monetary and fiscal stimulus is almost surely unsustainable. Given the amount of Japanese capital that has flowed overseas, Cambridge professor and macro strategist Mohamed El-Erian has written that the Bank of Japan's inevitable pivot has the potential to cause substantial worldwide adverse market reactions across asset markets. "The risk scenario here is the possibility that large losses and margin calls pressure certain overexposed Japanese entities to dispose of assets in a disorderly manner fueling contagion against markets and borders.

Abe's complicated legacy is likely to grow more so in the coming few quarters or years. He built a foreign policy architecture that may help avert an international kinetic conflict, but his First Arrow may have sown the seeds for the first major financial crisis of the 2020s. History will judge whether it was his initial creation of these policies or the current stewards of these programs who bear the glory or the blame.

As they forge ahead with these unproved strategies, the current authorities should never forget Abe's lodestar: "A strong Japan requires a strong economy." ◆