
The Legality of Japan's Current Monetary Policy under International Law

John Riley*

In response to the 2008 global financial crisis, many of the world's largest central banks initiated unconventional monetary policies such as quantitative easing when standard open market operations became ineffective. The Bank of Japan, the US Federal Reserve, the Bank of England and the European Community Bank were among those that aggressively increased their respective monetary bases to purchase specified financial assets from commercial banks and financial institutions in order to lower interest rates interest rates for specific debt securities and stimulate their economies. Japan, which has long suffered from years of debilitating deflationary cycles, has targeted and committed to open-ended purchases until a stable two percent rate of consumer price inflation is achieved. Several of Japan's chief exporting rivals, in particular China, have publicly criticized the Bank of Japan for using its current monetary policy to intentionally devalue its currency and thereby benefit from an unfair trade practice. This criticism is unwarranted and Japan's policy complies with international law.

Keywords

IMF, WTO, Currency Devaluation, Exchange Rates, Quantitative Easing, Bank of Japan

* Assistant Professor of Law at Sogang University School of Law, Seoul, Korea. J.D. (Pittsburgh). ORCID: <http://orcid.org/0000-0002-7512-9090>. The author may be contacted at: johnriley007@gmail.com / Address: Sogang University School of Law, 35 Baekbeom-ro (Sinsu-dong), Mapo-gu, Seoul 121-741 Korea.

DOI: <http://dx.doi.org/10.14330/jeail.2014.7.1.09>

1. Introduction

Japan's 'Lost Decade' (or "Lost Two Decades") is characterized as a period of chronic deflation and stagnation triggered by collapses in the Japanese real estate and stock markets beginning in the early 1990s.¹ Average GDP growth in Japan was just 0.8 percent between 1993 and 2012, and consumer prices fell steadily beginning in 1998.² In 2008, Japan's economy was particularly battered by the Great (Financial) Recession; it was followed by the devastating Tohoku earthquake and tsunami, which killed almost 20,000 people and destroyed 275,000 homes.³ The Great Recession caused output in Japan to fall 9.2 percent in the first quarter of 2009, from which it has not yet recovered, while the earthquake and tsunami were major culprits in reducing +4.7 percent GDP growth in 2010 to -0.5 percent in 2011.⁴ Japan's low birth rate has exacerbated the situation by reducing the size of the workforce and increasing the Japanese government's debt obligations to seniors, which has risen steadily compared to GDP, from 66 percent in 1991 to 244 percent in 2014.⁵

Under normal economic downturns governments and central banks will conduct monetary policy in a manner to stimulate lending, investment and overall economic growth. Central banks will typically engage in open-market operations to increase or decrease interbank interest rates to stimulate the flow of capital.⁶ If a central bank wishes to encourage lending and investment, *e.g.*, it will typically issue reserve notes and purchase short-term government bonds, thereby increasing money into the banking system. An increase in the supply of money will lower demand for short-term interbank loans, thereby lowering interest rates and stimulating lending, hopefully resulting in greater economic output, investment and low-to-moderate

¹ See generally P. Krugman, *It's Baaack: Japan's Slump and the Return of the Liquidity Trap*, Brookings Papers on Economic Activity 2:1998, available at http://web.mit.edu/krugman/www/bpea_jp.pdf (last visited on Apr. 15, 2014).

² See GDP growth (annual %), The World Bank, available at <http://data.worldbank.org/indicator/NY.GDP.MKTP.KD.ZG> (click 'Download Data' showing 8.3 percent growth); See also Inflation, consumer prices (annual %), The World Bank, available at <http://data.worldbank.org/indicator/FP.CPI.TOTL.ZG/countries?display=map> (all last visited Apr. 11, 2014).

³ For details on the impact of the Tohoku earthquake and tsunami, see Jun Hongo, *Still hunting shadows three years after 3/11*, JAPAN TIMES (Mar. 8, 2014) available at <http://www.japantimes.co.jp/life/2014/03/08/lifestyle/still-hunting-shadows-three-years-after-311/#.U0em5mqKDIU>. See also J. Hausman, & J. Wiel, *Abenomics: Preliminary Analysis and Outlook*, Brookings Panel on Economic Activity 6 (Mar. 2014), available at http://www.brookings.edu/~media/projects/bpea/spring%202014/2014a_hausman.pdf (all last visited on Apr. 14, 2014).

⁴ *Id.*

⁵ *Id.* at 7.

⁶ J. DANIELS & D. VANHOOSE, INTERNATIONAL MONETARY AND FINANCIAL ECONOMICS 213-219 (3d ed. 2005).