

## JAPAN

*Despite continuous growth over the past five years, a large GDP-per-capita gap remains vis-à-vis the best performing countries, reflecting a major productivity shortfall.*

### Policy priorities

#### **Further liberalise retail and professional services**

**Challenge and recommendations:** To boost competition in the retail sector and professional services, it was recommended to ease entry restrictions and zoning regulations and to facilitate the entry of foreign workers.

**Actions taken:** The new zoning regulations that took effect in autumn 2007 are intended to re-vitalise urban areas, but may limit the entry of large stores in suburban areas. The Economic Partnership Agreements with the Philippines and Indonesia (which have not yet entered into force) allow nurses and care-givers from these countries to provide services in Japan on a temporary basis if they pass qualification examinations in Japanese.

#### **Reform employment protection legislation for regular employment**

**Challenge and recommendations:** To reduce labour market dualism, it was recommended that more transparent statutory guidelines on the dismissal of workers be introduced and that employment protection for regular workers be relaxed, thereby lowering incentives to circumvent strict conditions for dismissal by hiring non-regular workers.

**Actions taken:** No action has been taken to ease employment protection for regular workers. The revised legislation on part-time workers, which will come into force in 2008, aims at achieving more balanced treatment between part-time and regular workers. While this may improve the treatment of non-regular workers, it may also discourage firms from hiring part-time workers, thus depressing overall employment.

#### **Reduce producer support to agriculture**

**Challenge and recommendations:** To reduce distortions to trade and production and lower prices for consumers, it was recommended that the level of support to agriculture be decreased, while shifting its composition away from market price support and towards direct support for farmers.

**Actions taken:** The proportion of agricultural support linked to market prices may be reduced by the introduction of three new direct payments in 2007 as part of the effort to concentrate support on more efficient farms. The system of administered prices for wheat and barley was relaxed in 2007, although the impact will be limited by the continued high level of border protection for these products.

#### **Encourage innovation**

**Challenge and recommendations:** To increase the return on investment in innovation, it was recommended that framework conditions be improved by removing obstacles to developing venture capital markets, upgrading the education system through further reducing regulations and abolishing barriers to the entry of foreign researchers.

**Actions taken:** The government's "Innovation 25" plan, announced in June 2007, aims to encourage innovation up to 2025 by enhancing the mobility of researchers among universities, public research institutes and private firms, expanding the use of competitive research grants and extending the length of visas for foreign researchers.

#### **Raise productivity through higher foreign direct investment**

**Challenge and recommendations:** To encourage greater foreign direct investment (FDI), it was recommended that obstacles to inflows be removed by fully opening the mergers and acquisitions (M&A) market to foreign firms and by easing product market regulations, especially in the service sector and network industries.

**Actions taken:** The revision of the Corporation Law will facilitate cross-border M&As by allowing "triangular mergers" in which foreign companies establish subsidiaries in Japan, which can then use their parent company's stock to acquire a Japanese company. The decision to permit, under certain circumstances, deferral of related capital gains taxes should further encourage such mergers.