

THE ORIENTAL ECONOMIST

A L E R T

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BOJ SAYS RECESSION COULD BE WORSE THAN 1997-98 WORSE BY THE DAY

Key points:

- A new BOJ “Outlook” update projects that GDP will fall 1.8% in fiscal 2008 (ending March 2009) and 2% in fiscal 2009
- If so, this would be a worse recession than in 1997-98
- Meanwhile, December exports plunged a worse-than-expected 30% from the year before, leading to more forecasts of a 10-12% (annualized) drop in GDP during October-December
- 2009 could see worst export fall in postwar era

BOJ Revises Outlook Sharply Down

In a just-released update of its “Outlook” for the economy, the BOJ now believes that GDP will fall 1.8% in fiscal 2008 (ending in March 2009) and another 2% in fiscal 2009. It will then rebound a meager 1.5% in 2010, says the BOJ (Figure 1). The 2% fall projected for fiscal 2009 is more bearish than many private forecasts, an unusual situation for the BOJ. The BOJ also forecast a return to mild deflation (-1.1% in fiscal 2009 and -0.4% in fiscal 2010).

The BOJ did not indicate any change in its monetary policy, but we suspect this will lead to more use of unconventional measures.

Could Be Worse Than 1997-99

If the BOJ is right, this recession will be worse than the one in 1997-99. In the late 1990s episode, GDP declined sharply in calendar 1998 but only slightly in 1999. The average

decline over the two years was 1.1%. If the BOJ is right, GDP will decline sharply two years in a row (fiscal 2008 and 2009) for an average decline over the two years of 1.9% (Figure 2).

Worse yet, if we expand our vision to a four-year period, calendar 1997-2000 vs. fiscal 2007-2010, the current performance will also be much worse, not only because the decline is more prolonged and steeper, but because the recovery is expected to be tepid compared to the late 1990s episode. Over 2007-2010, according to the BOJ, GDP will have declined an average of 0.2% a year. By contrast, in the four years of 1997-2000, GDP rose an average 0.6% a year. What made the last episode so terrible was that, no sooner did the GDP get up off the mat in 2000 than it was knocked down again by the dot.com bust (see again Figure 2).

(One note: although the recession began in 1997, GDP began the year so much higher than the average for 1996 as a whole, that 1997 as a whole was still 1.5% higher than 1996.)

30% Export Plunges Cause Yet Further GDP Downgrades

December exports were a disaster. The plunge in global exports accelerated in December, falling 30% from year-earlier levels. Most shockingly, exports to Asia also fell 35% from year-earlier levels. Both global and Asian sales are now below the levels of 2005 and still headed downward (see Figures 3-6).

Given the plunge in China and Asia's own exports and domestic GDP, and therefore their need for imports, it is not inconceivable that exports could even fall all the way back to the levels of 2002, the beginning of the most recent recovery's export boom.

This fall is unprecedented in postwar Japanese history. Hitherto, the worst annual fall was in 2001, when price-adjusted exports fell almost 10% during the dot.com bust. Even if exports fall no further during 2009, the year as a whole will end up 22% below the level of 2008 (Figure 7).

As a result of the December results, many forecasters now believe that a fall in Japan's trade surplus will deduct about 8% from GDP (annualized rate). Combined with falls in domestic demand, many forecasters now project that GDP will show a 10-12% fall in October-December.

Richard Katz
The Oriental Economist Report
212-868-4380 www.orientaleconomist.com

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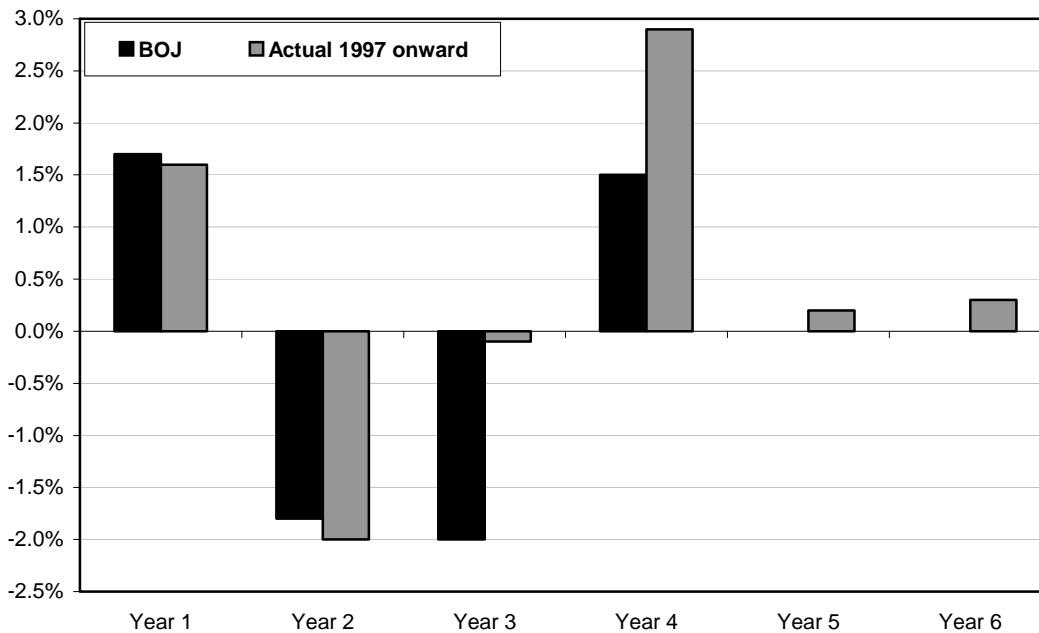
Figure 1: BOJ Sees GDP Falling Two Years In a Row

Forecasts of the Majority of Policy Board Members

y/y % chg.

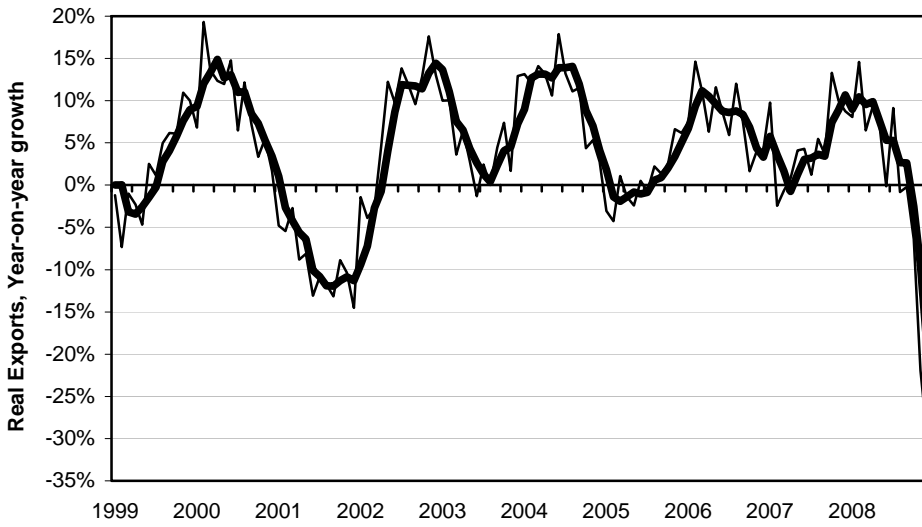
	Real GDP	Domestic CGPI	CPI (excluding fresh food)
Fiscal 2008	-2.0 to -1.7 [-1.8]	+3.0 to +3.2 [+3.1]	+1.1 to +1.2 [+1.2]
Forecasts made in October 2008	+0.1 to +0.2 [+0.1]	+4.3 to +4.8 [+4.6]	+1.5 to +1.6 [+1.6]
Fiscal 2009	-2.5 to -1.9 [-2.0]	-7.0 to -6.0 [-6.4]	-1.2 to -0.9 [-1.1]
Forecasts made in October 2008	+0.3 to +0.7 [+0.6]	-1.4 to -0.4 [-0.8]	-0.2 to +0.2 [0.0]
Fiscal 2010	+1.3 to +1.8 [+1.5]	-1.5 to -0.8 [-0.9]	-0.6 to 0.0 [-0.4]
Forecasts made in October 2008	+1.5 to +1.9 [+1.7]	-0.3 to +0.5 [+0.3]	+0.1 to +0.5 [+0.3]

Figure 2: Could Be Worse Than 1997-99



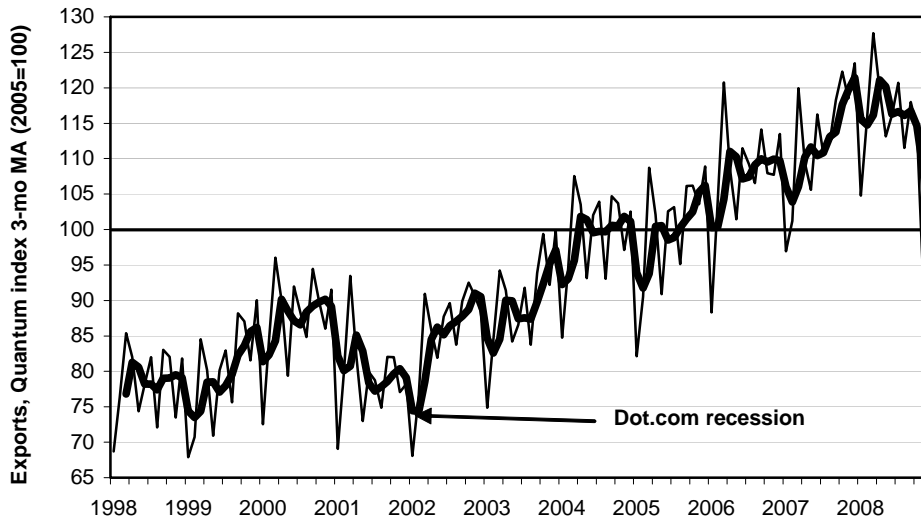
Note: In black column, year 1 is fiscal 2007; in grey column, year 1 is calendar 1997; see text for further explanation

Figure 3: Exports In Record Plunge: Down 30% From a year Ago



Note: Thin line is year-on-year change; thick line is three-month moving average of that year-on-year change

Figure 4: ... To Below 2005 Level



Note: Thin line is monthly level; thick line is three-month moving average

Figure 5: Asia Market Collapses to 35% Below Year Ago

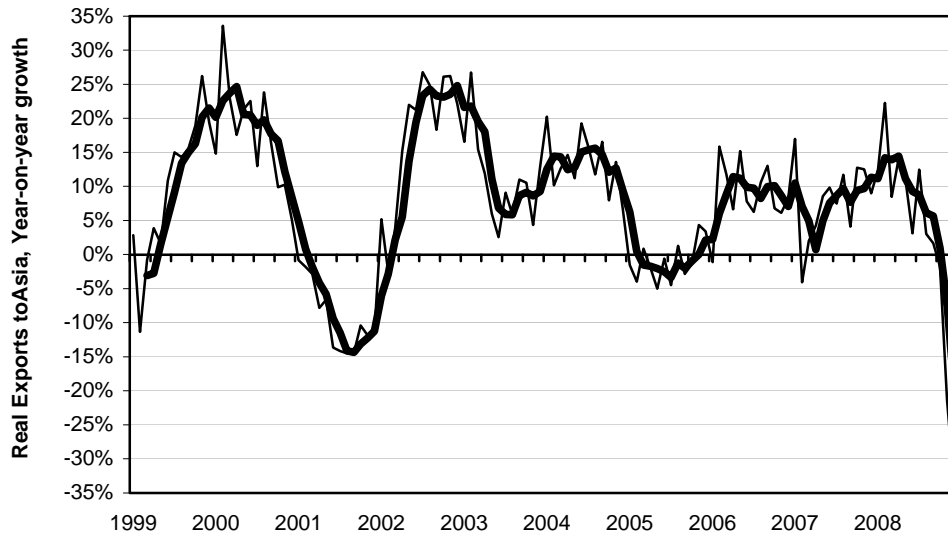


Figure 6: Exports to Asia Fall Below 2005 Level

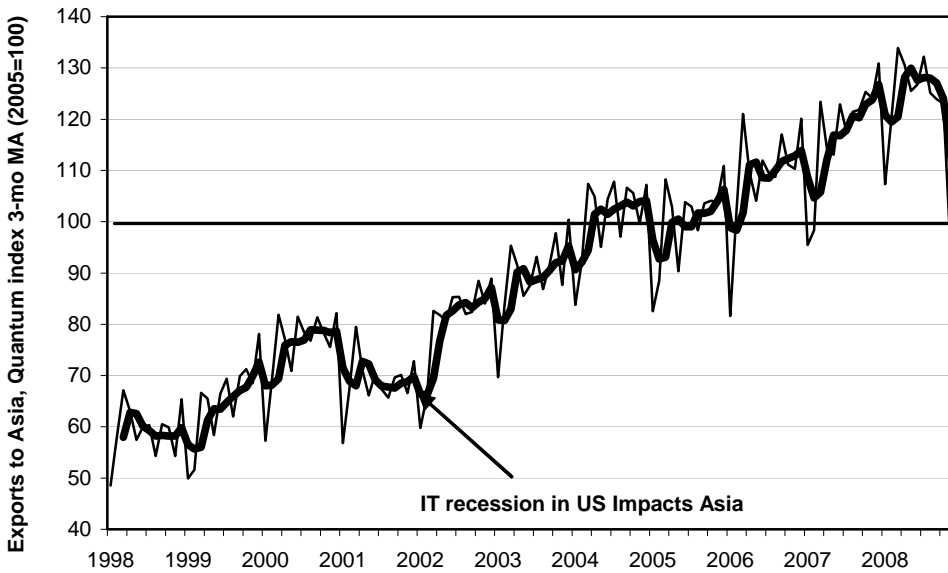


Figure 7: 2009 Could Show Worst-Ever Postwar Export Decline

