Economic Planning Agency Declares Economic Recovery

By Sakamoto Sakae

In a governmental assertion that the economy is recovering, the Economic Planning Agency said in its monthly economic report for February that "We are again seeing the modest beginnings of economic recovery."

Economic stagnation had held on longer than expected due to the structural factor of the bursting of the bubble. Last year, a recovering economy was stopped in its tracks by a super-strong yen in the first half of the year. But in its February report this year, the Economic Planning Agency indicated its confidence in a recovery, observing that "In addition to positive trends in capital investment and home building, the downturn in exports is coming to a halt. Against this background has emerged a moderate increase in production."

Since the bursting of the bubble, the Economic Planning Agency has expressed its changing view of the economy thus:

June 1993: "The shift toward recovery is apparent" (declaration of economy bottoming out)
October 1993: "Shift toward recovery at a standstill—overall slump persists" (acknowledgment of mistake in declaring the market had bottomed out)
September 1994: "The economy is moving in the direction of a moderate recovery" (actual declaration of economic recovery)
July 1995: "Apparent standstill in recent moderate base of recovery" (declaration of fears of a stalled recovery)
September 1995: "Bearish trend as standstill persists" (deletes the word "recovery" for the first time in a year)

As is clear in the quotes above, a recovery was declared in September 1994, but that declaration was withdrawn as the strong yen rekindled fears of deflation (in April, the yen hit a record high of ¥79 to the dollar).

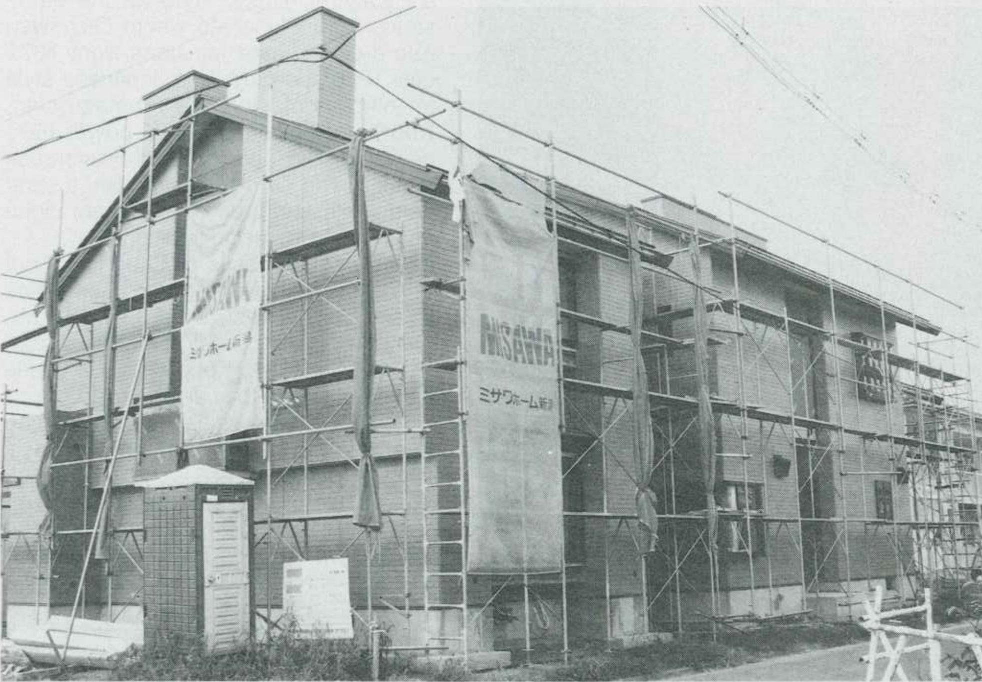
Economy increasingly driven by private demand

One worries whether this time it will really be all right, but Shimanaka Yuji, chief researcher at Sanwa Research Institute Corp., is optimistic. He says that the economy has been on a trajectory for recovery since October or December of 1995, and that potential threats to recovery have receded. Trends in capital investment, which the monthly report termed "positive," are being helped along by lower interest rates and investment in information systems, and the proportion of the GDP accounted for by capital investment is up. Shimanaka sees this recovery as lasting 30 months.

Of the "harsh" employment conditions mentioned in the monthly report, Shimanaka says, "To be sure, the levels are at their worst ever, but are still only to the point of putting a slight damper on the outlook, and their effect on consumer trends is minimal."

And of the "slowdown in public enterprise" that so many economists are worried about, Shimanaka says, "Public projects in fiscal 1996 will drop about 20% from post-revision 1995 levels, and they may run out of steam in the second half of the next fiscal year. But [by then], private demand will be chomping at the bit." His prediction is that Japan's economic reins will be passed from public works to private demand.

Tanaka Tsutomu, a consultant at Mitsubishi Research Institute, Inc., agrees that the issue for the current recovery is how smoothly this switch can be accomplished. To make the changeover work, he says, fiscal reconstruction should



Maintaining economic recovery dependent on increased consumer demand.

be carried out steadily from fiscal 1997 with a long-term goal. In other words, during the next fiscal year (1996) the economy must come first, with additional measures (debt increases) to go into effect in a worst-case scenario.

Authorized intervention network completed

As of the end of February, the exchange rate hovered at about ¥105 to the dollar, but will it never dip back to the level of ¥90 to the dollar? The Finance Ministry and Bank of Japan have sent a message to the market that they will block further hikes in the yen's value by intervening with large volume dollar purchases (estimated at $17 billion in February). The Finance Ministry's February 20 announcement of the conclusion of an agreement with monetary authorities in Hong Kong and Singapore for cooperation in authorized intervention is another link in its campaign to stop the strong yen. The Bank of Japan has already made an agreement with the finance ministries and central banks of the U.S. and European members of the G7 as well as with Australia, thereby sewing up a global network for authorized intervention.

Looking back at the exchange market's movements on February 20, the yen was being bought in high volume on the Tokyo market, having climbed to ¥103 per dollar in European markets on the previous day. This was a setback for Japan's monetary authorities, who had been fighting the strong yen since the previous spring. The Bank of Japan predictably began its dollar-buying intervention to try to bring the yen back to ¥105 per dollar, but without as much effect as had been expected.

Then, before noon, a news flash hit the wire: "The Finance Ministry will announce this afternoon an authorized intervention agreement with authorities in Hong Kong and Singapore." In response, the yen, which had been around ¥104 to the dollar, quickly weakened, at one point hitting ¥106 to the dollar.

The Finance Ministry's message that it would intervene on behalf of the yen in Asian markets, too had a stunning impact on the exchange rate.

The Finance Ministry's announcement seems not to have been deliberately timed to coincide with a strengthening yen, despite appearances. The International Finance Bureau of the Finance Ministry had already planned the announcement in both markets for February 20th, which was a holiday (Chinese New Year), and it just happened to be when the yen surged. Sakakibara Eisuke, director-general of the International Finance Bureau and also known as Mr. Weak Yen because he brought the yen back from its all-time high by ¥25 to the dollar, must have a lucky star.

Formation of monetary version of EAEC

The Asian exchange market intervention network is wider than Japan-Hong Kong and Japan-Singapore. Last November 20, the monetary authorities of Australia, Hong Kong, Indonesia, Malaysia and Thailand gathered in Hong Kong for a conference of Asian-Pacific central banks, and concluded a mutual lending agreement for the procurement of intervention funds (US$) to stabilize currency in their home countries.

Under this agreement, a country in need of U.S. dollars can take out short-term dollar loans from other countries, using as collateral U.S. treasury bonds it holds as part of its foreign reserves.

China, Japan, South Korea, New Zealand and the Philippines were also present at the conference, but did not participate in the dollar-lending agreements reached by the other countries. According to knowledgeable sources, however, the other five countries (including Japan) are weighing the pros and cons of participating in this liquidity agreement, and in the near future may create an "Asian-Pacific agreement on monetary stability."

The East Asia Economic Caucus, whose goal is regional agreements in trade and investment, has been stymied by U.S. objections, but it is quietly working on a monetary version.

In what may be a temporary measure until such a monetary conference is formed, Singapore has signed separate agreements with Thailand, Indonesia and Malaysia. Hong Kong and China also have a similar agreement. These 10 countries in the Asian-Pacific region are quietly working to stabilize their currencies in the mesh of such agreements, which may progress to the point of becoming an Asian BIS (Bank for International Settlements).

Avoiding a Mexican-style crisis

According to the joint statement by the Hong Kong conference in autumn of last year, "the combined GNP of our 10 countries is $7.368 trillion (matching that of the U.S. and Canada, and the combined GNP of the EU), and foreign reserves have reached $403 billion (a little more than 40% of world reserves)."

At this conference, they "reviewed the development of financial markets and considered cooperation among central banks," "exchanged opinions on regional monetary speculation," "reaffirmed the necessity of strengthening cooperation to maintain monetary stability and improve the stability of the monetary system," and "discussed how to respond to trends towards unstable capital." Of note are the phrases "regional monetary speculation" and "trends towards unstable capital."

This conference was created on the rebound from last January's Mexican monetary crisis (in which the Mexican peso took a sharp fall, which led to confusion in Mexico's capital markets, creating confusion in financial and capital markets in Central and South America that dried up investment in emerging nations). In other words, the goal of the Asian-Pacific central bank conference was to avert a Mexican-style crisis; its initial outcome was the five-country mutual lending agreement for intervention funds. JJTI

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