

# Return of the Living Dead: Japanese Economy in 2009

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# Outline

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1. Japan back to recession
2. Government policy responses so far
3. Problems ahead

# Subprime Related Products at Major Japanese Banks (Billion Yen)

End of	Subprime related products		Other CLO, CDO, RMBS, CMBS, Leveraged Loans		Total	
	Balance	Loss	Balance	Loss	Balance	Loss
Mar. 2008	933	775	17,668	1,303	18,602	2,076
Jun. 2008	876	817	18,533	1,394	19,410	2,212
Sept. 2008	719	867	17,693	1,909	18,412	2,776

- Tier I capital of major banks at the end of March 2008
  - 25,987 billion yen
- Low exposure compared to capital, but capital has been depleted since March 2008

# Capital Evolution for Japanese Banks 2003 to 2007 (¥ trillion)

	March-07	March-03	Change	Percent contribution to change
Official Capital	40.0	24.8	15.2	100.00%
Common stock	9.3	10.2	-0.9	-6.13%
Capital surplus	8.7	8.6	0.1	0.39%
Retained earnings	13.4	4.4	9.0	59.07%
Net unrealized gains on stocks and others	8.2	0.1	8.1	53.25%
Revaluation reserve for land	1.0	1.5	-0.6	-3.70%
Net deferred gains on hedging instruments	-0.3	0	-0.3	-2.07%

Note: Some small components have been omitted and because of this and rounding columns may not sum to totals.

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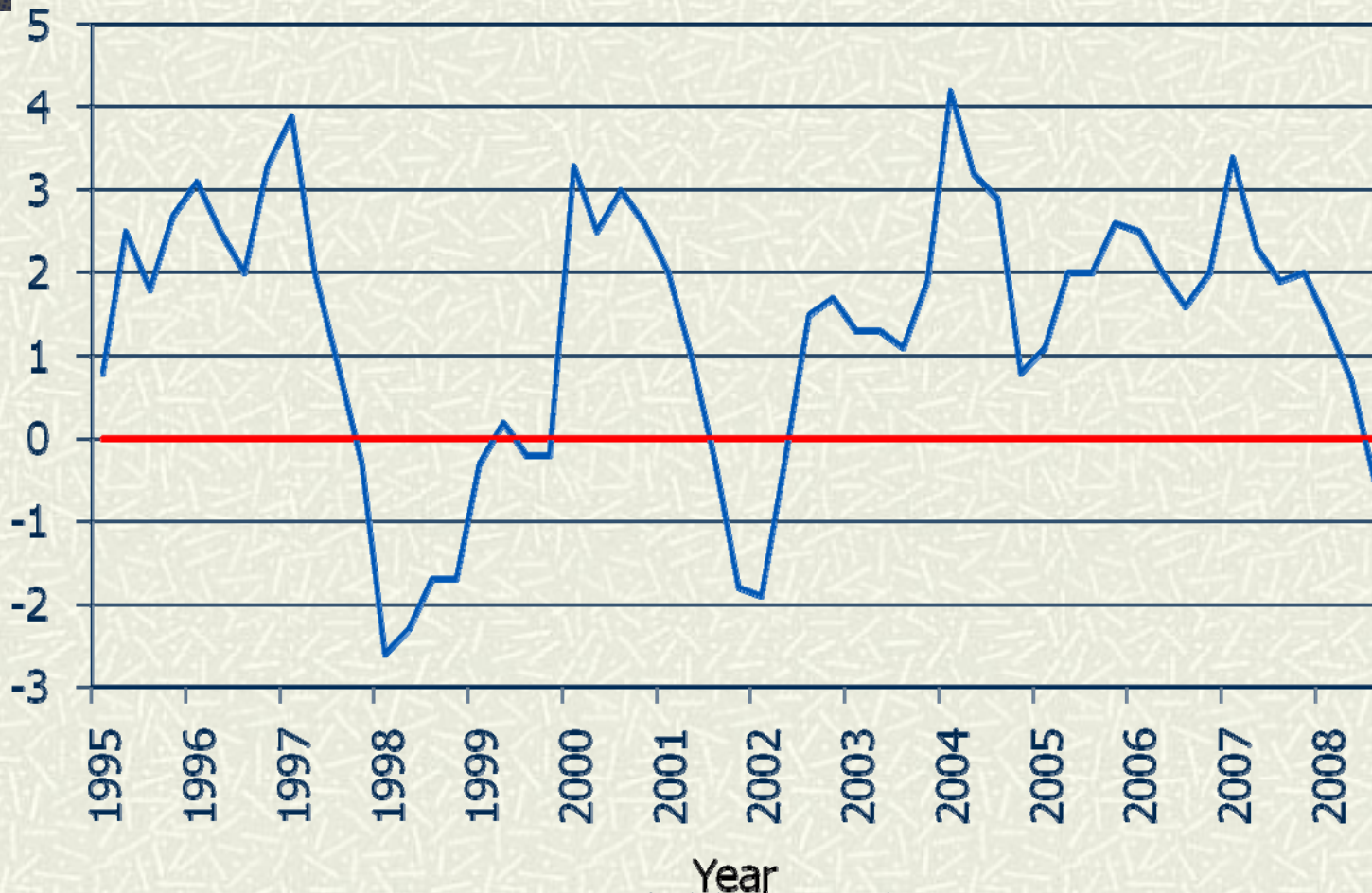
# Nikkei 225: Jul. 2008 – Feb. 2009



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# GDP Growth (% from a year ago)



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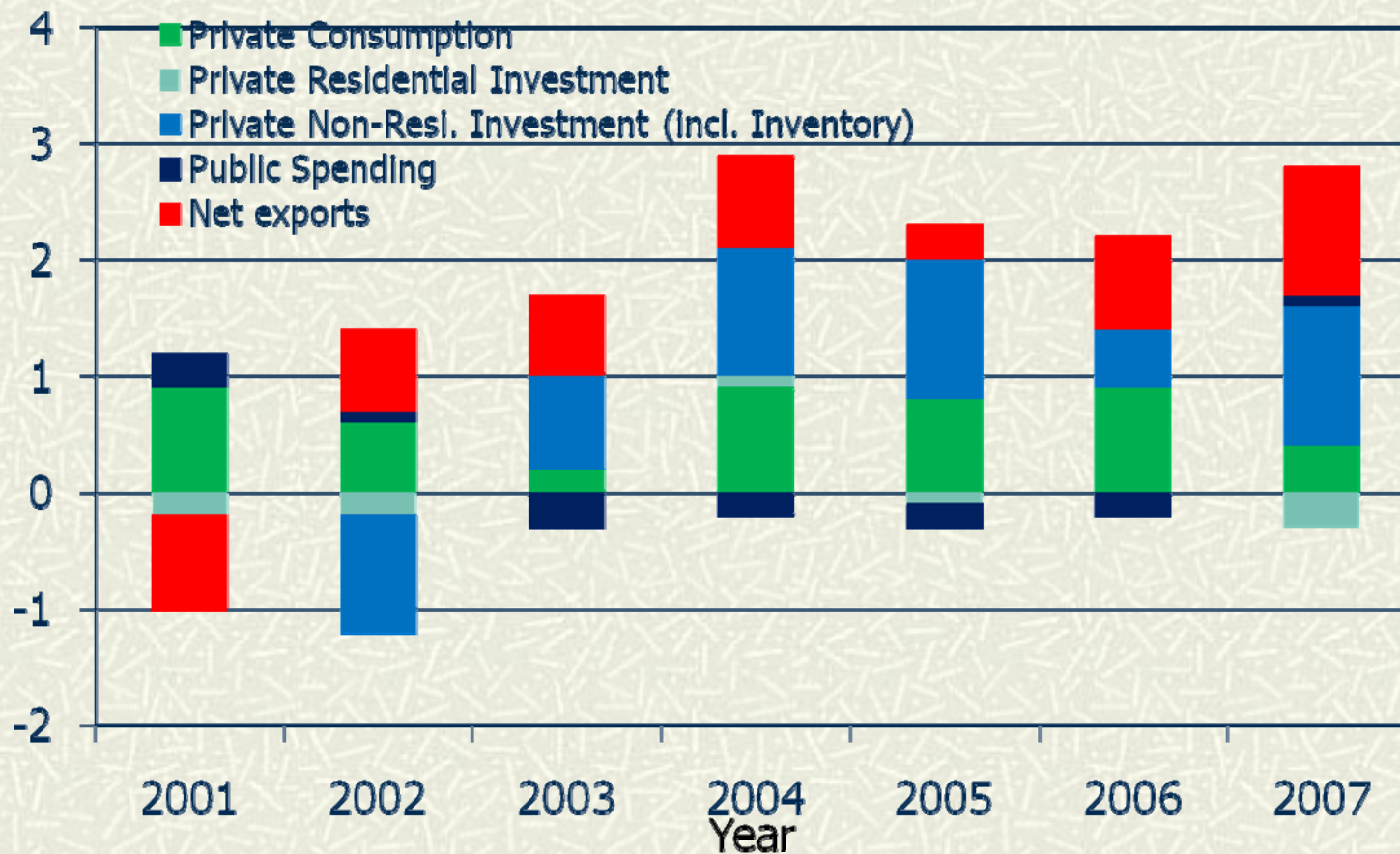
# Industrial Production (SA, 2005=100)



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# Recovery depended on exports, but not exclusively (contributions to growth, %)

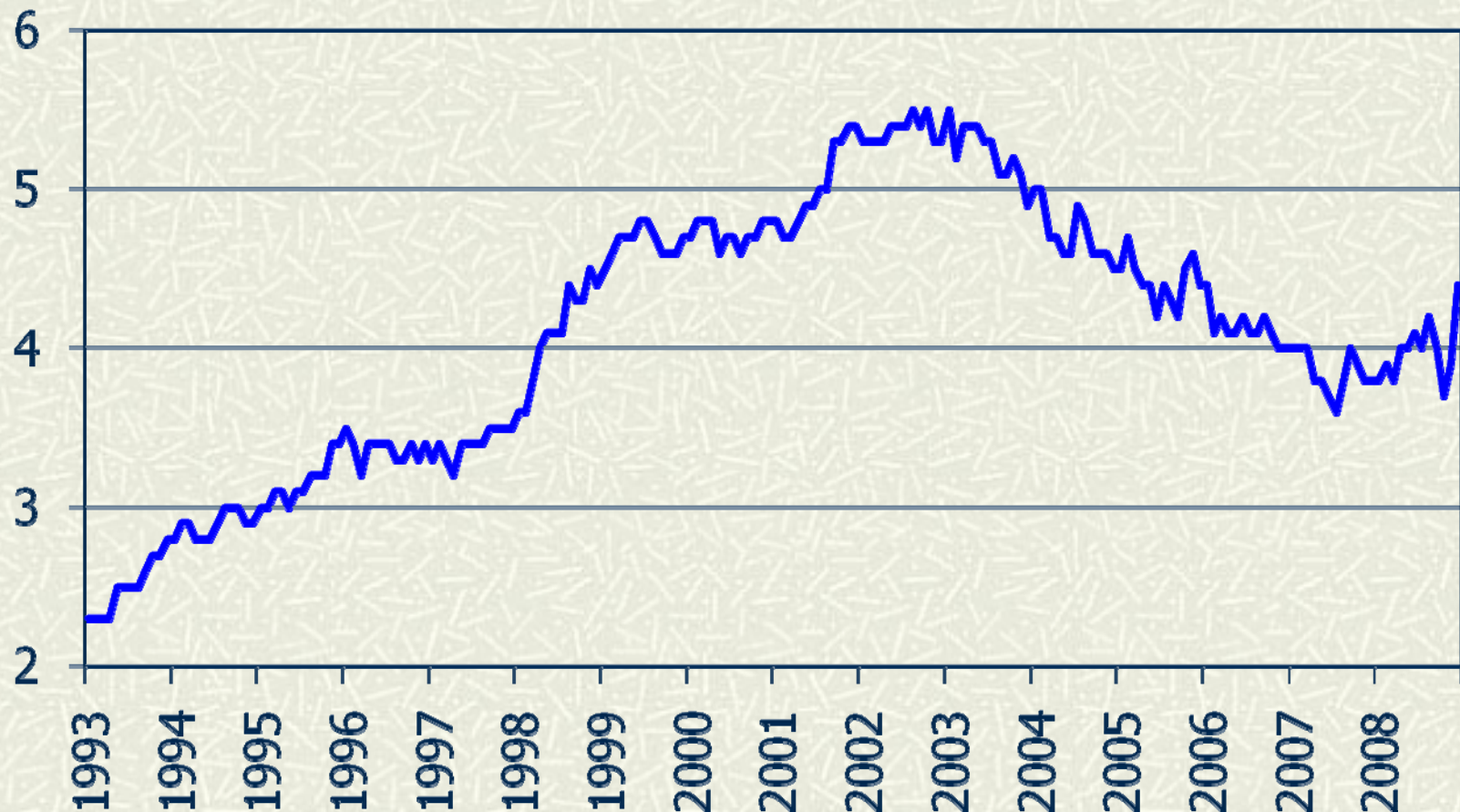


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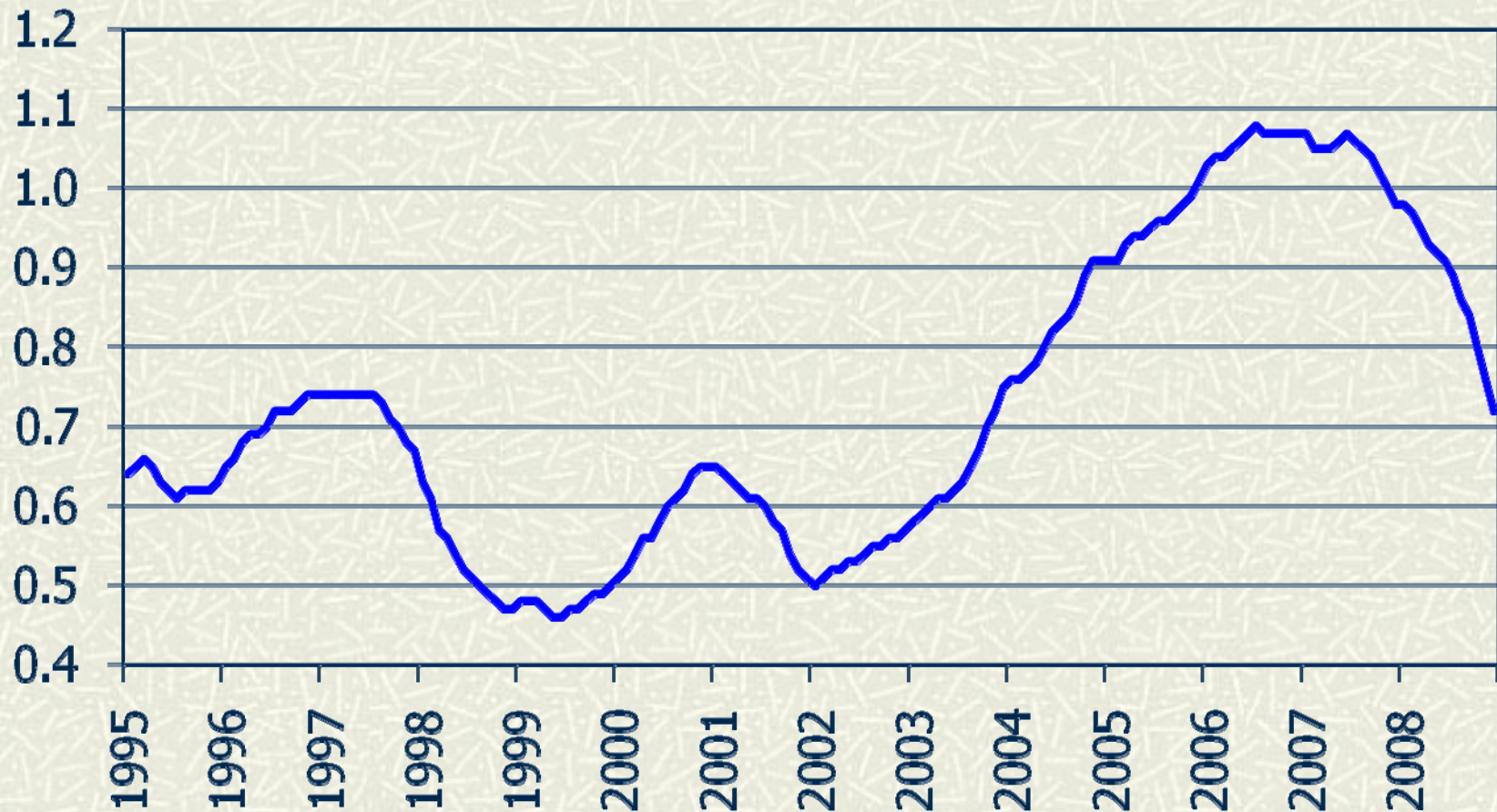
# Unemployment Rate (% , SA)



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# Effective Job-Offers to Applicants Ratio (SA)



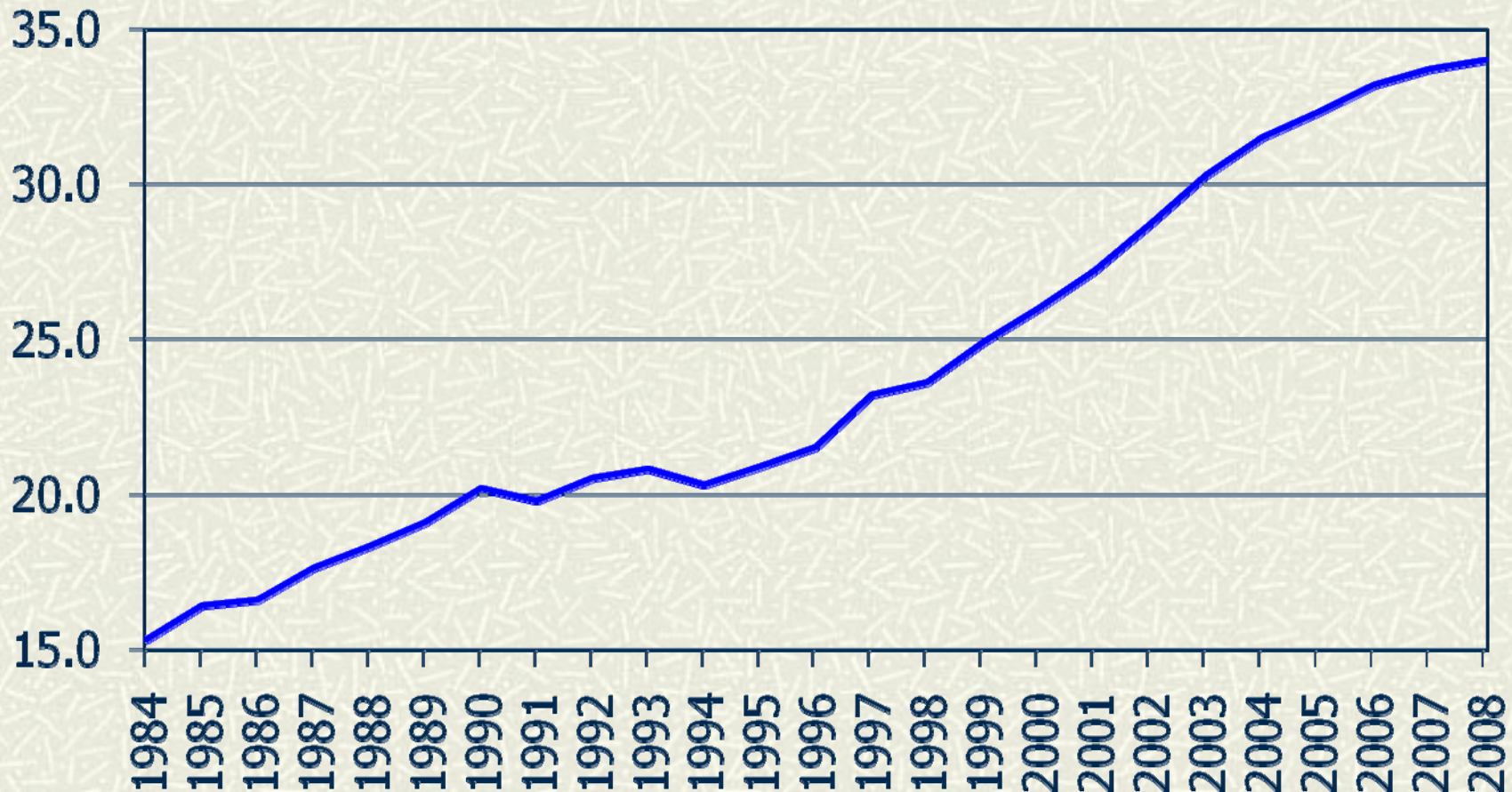
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# Policy responses so far

- Monetary policy: back to ZIRP (almost)
- Fiscal policy: expansionary (but tax hike as early as 2011), ¥2 trillion (0.4% of GDP) cash handout
- Act for Strengthening Financial Functions revived (with less stringent conditions for capital injections)
- Improved safety net for unemployed (especially non-standard employment), job creations in public sector
- Help (pressure) firms not to layoff employees, including non-regular workers
- Problems of non-standard employment attracted special attentions

# Proportion of Non-standard Employment (%)



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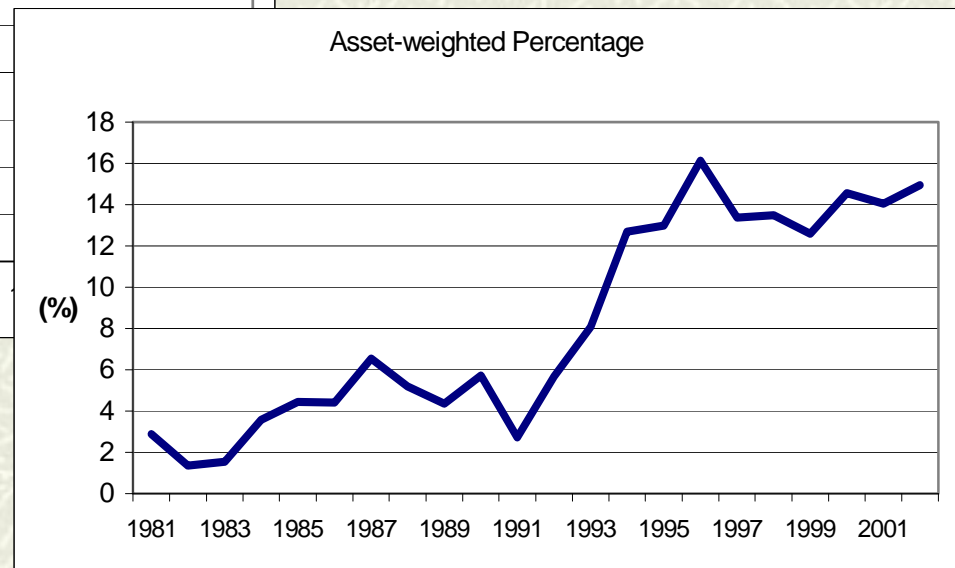
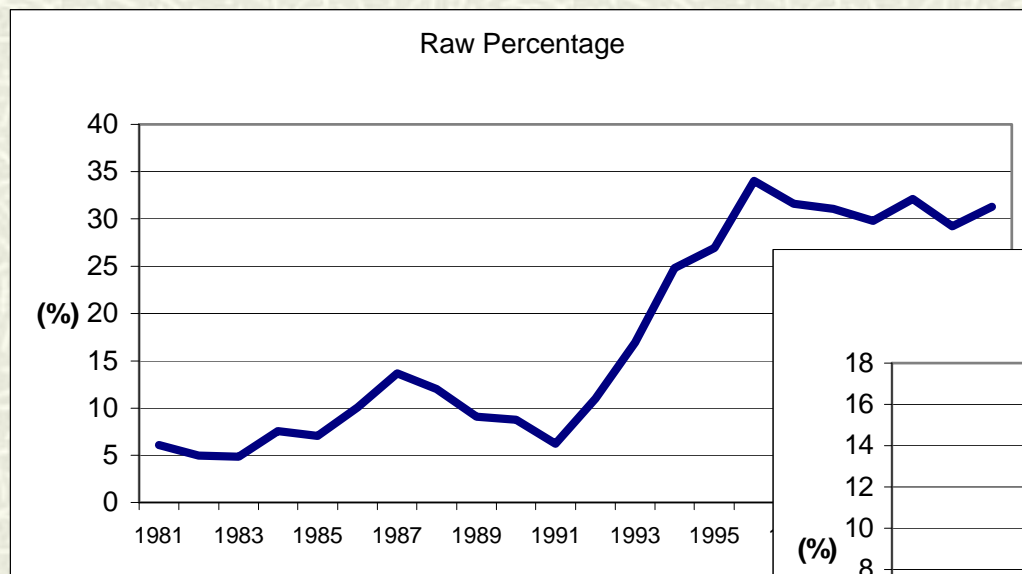
# Attempts to protect employment can create zombie firms

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- # Zombie firms: unproductive firms that should exit the markets but are kept alive by the help of creditors/government
- # Zombie firms hurt the economic growth by discouraging more productive firms from entering the market (or expanding) to create jobs (Caballero, Hoshi, and Kashyap, *AER*, 2008)
- # This was indeed a mistake Japan made during the long stagnation of the 1990s

# Zombies defined as firms getting subsidized credit

The sample is listed firms in manufacturing, construction, real estate, retail and wholesale (other than the nine largest general trading companies), and services



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# Zombies Hurt Non-Zombies

Employment growth or Investment

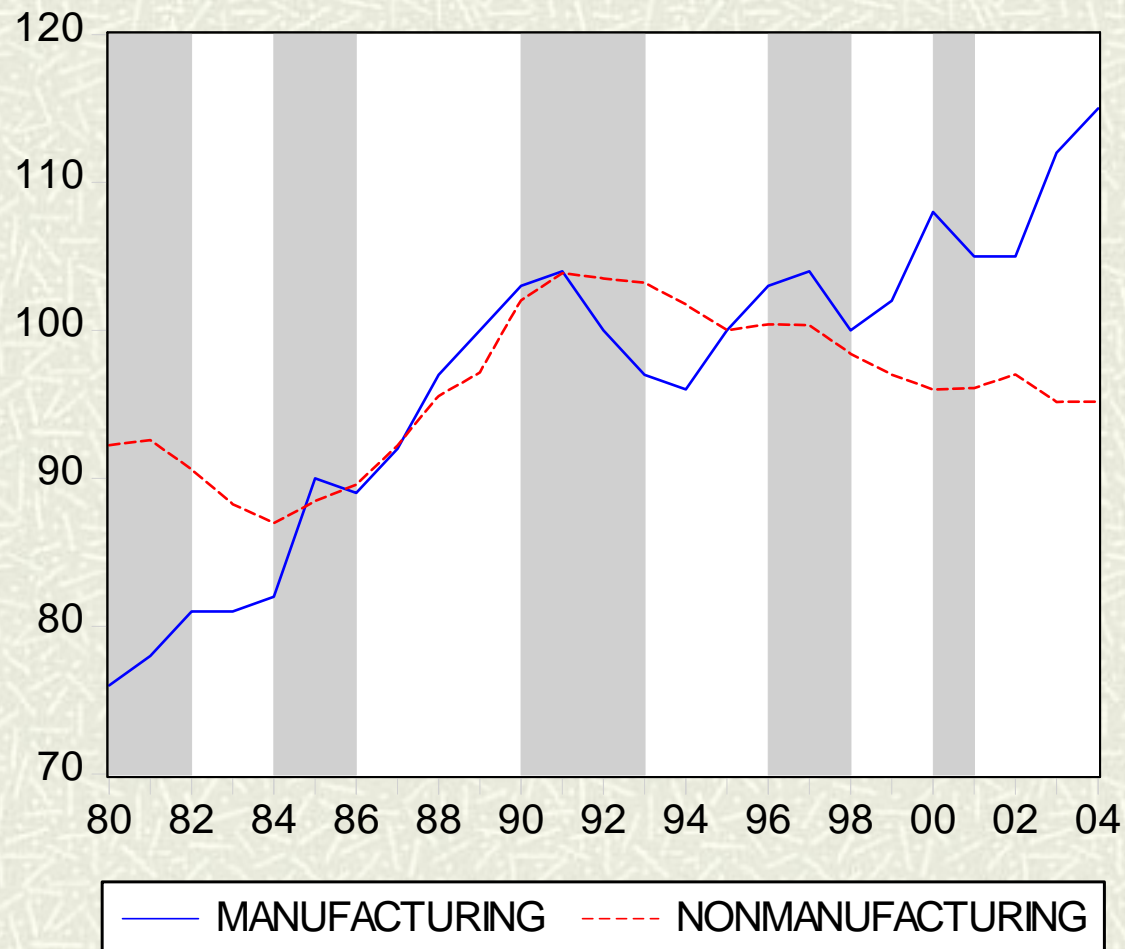
$$\begin{aligned} \text{Activity}_{ijt} = & \text{constant} + \alpha' \text{year}_t + \delta' \text{industry}_j \\ & + \beta \text{non-zombie}_{ijt} + \chi \text{industry zombie}\%_{jt} \\ & + \varphi \text{non-zombie}_{ijt} * \text{industry zombie}\%_{jt} + \varepsilon_{ijt} \end{aligned}$$

# Zombie's Hurt Non-Zombies

Dependent Variable	I/K	$\Delta \text{Log E}$
Sample	1993- 2002	1993- 2002
Constant	0.239 (0.008)	0.014 (0.002)
Non-Zombie Dummy	0.026 (0.006)	0.0011 (0.0018)
Industry Zombie %	-0.137 (0.038)	-0.045 (0.012)
Non-Zombie * Industry Zombie%	<b>-0.089</b> <b>(0.033)</b>	<b>-0.023</b> <b>(0.010)</b>
$\bar{R}^2$	0.054	0.090



## Total Factor Productivity by Industry: 1980-2002 (1995=100)



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# Summary

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1. Japanese economy: back into recession
2. Policy response: protect employment, help (pressure) corporations/banks to keep the employees
3. Watch out for the return of zombies

**THEY'RE BACK FROM  
THE GRAVE AND  
READY TO  
PARTY!**

