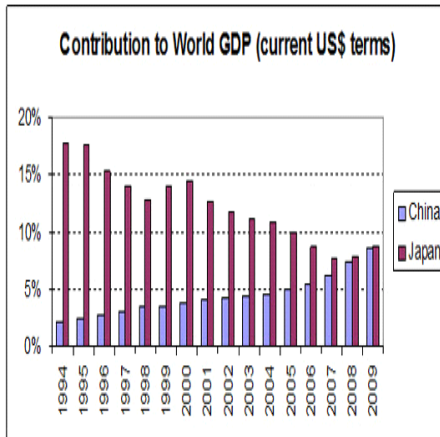


## Global Economic Impact – Japanese Disaster



Source: World Bank; Plexus Asset Management.

### Economic Overview of Japan

Japan until recently was the 2nd largest economy in the World, knocked to 3rd by China last year. Japan contributed 8% of the world's GDP in 2009, in a close 2nd to China's 9%. The 10th most populated country in the world, with a staggering 128 million residents (2009) and 30 million in Tokyo, listed as the world's largest metropolitan area, Japan is a heavy player on industrial, economic and technology fronts.

### A short view of Japan's market movement

**1960-1980s-** Japan's Post War Economic Miracle: Japan's Big Mac Index showed a swift growth from 10%, 5% then 4%

**Late 1980s:** The Japanese Asset Bubble Economy overheated due to falling stock and real estate prices

**1989:** Tokyo Stock Exchange Crash

**1990- 2000:** Growth slow, only 1.5% increases in GDP annually

**2000s:** Growth shows a slight increase, with GDP increase 0.8% annually

**2003-2007:** Growth increase 2.1% a year

**2008:** GDP shrinks by 1.2%

**2009:** GDP further decreases by 5%

### Effect on the Japanese market

Japan's Nikkei, is showing downward pressure due to the Tsunami disaster. Further Japan's decision to ease their fiscal policy could be the answer to its troubled economy. The supplementary budget of approximately 1-2% of GDP would increase its debt burden, but would also be a potential way out of deflation risk. The incoming economic assistance from the US and other countries are helping boost the yen-dollar rate,

The injection of 37 trillion yen into the Japanese economy through an asset buying scheme by the Bank of Japan showed the central bank's desire to stay on a moderate path to recovery.

An effective stimulus program could stay a potential downgrade by Moody's from the current Aa2 rating, which would occur from increased

fiscal spending. The long term health of Japan's government financial situation are still too early to be judged, but analysts suggest debt monetization aid to overcome a deflation in the already shaky structure. Overall, Japan should keep a positive outlook on the situation, drawing from past strengths and resilience, according to analysts.

### **Japan and Sri Lanka**

Japan and Sri Lanka share a friendly economic history, with diplomatic relations from 1952. Japan has been a major contributor to Sri Lanka's socio-economic development, and also provided relief at times of conflict, floods, droughts and the tsunami. The Japanese Government provided 1.1 billion (Rs 1.4 billion) at the end of December 2010, in assistance through various funding schemes aimed to help people in conflict affected areas. The assistance focused mainly on Consolidation of Peace and Reconstruction and the Medium and Long Term vision for Development. Japan has further used international agencies as a conduit for Sri Lankan aid, such as the World Bank and Asian Development bank. Both nations have benefited from a good bilateral relation in trade and investments. Japan has been able to maintain a presence in the Sri Lankan private sector, with about 60 companies operating in Sri Lanka in 2009. Further Sri Lanka is a net importer from Japan therefore, making Japan not export destination for Sri Lanka.

### **Global impact**

The crisis is expected to have a negative impact on a global scale. The shipping firms might redirect their ships to other ports due to expectations of an aftershock. This will further effect the goods movement into Japan. The ports are not accessible due to the damage caused by the Tsunami, which will affect the cost of imported goods within the country.

If Japan plans to move from nuclear generated power to coal power plants, this will affect the commodity prices and would have a global effect. The commodity prices are currently trading at historically high prices. Oil prices fell Monday because of an expectation that Japan, a big oil importer, will need less oil in the short run if its economy is shut down. The crude oil prices are reflecting rising trends due to the heavy demand that is expected from Japan in light of the rebuilding. This might have an effect on the already slumped global economy due to increase in prices.

The steel mills are expected to suffer as demand for iron ore will drop by 20million tons, (<http://leeuniversal.blogspot.com/2011/03/macroeconomic-indicators-tsunami-likely.html>). The drop in demand is to affect the Australian iron ore industry and the miners. On the contrary this might result in an increase in demand for steal by China.

If the Japanese government has to liquidate the global investments to finance the rebuilding, a likely source will be the US treasury bonds. This is likely as Japan is one of the major holders of US treasury bonds. This is likely to put more pressure the already strained US public finances. (<http://www.globalpost.com/dispatch/news/regions/asia-pacific/japan/110313/japan-tsunami-global-economy>)

Japan's economy depends on its exports. The most exported goods are cars, machinery, raw materials and manufactured goods. Japan experienced an increase of 25% in exports after 3 years. The closure of ports will lead to delays in exports and cancellation of orders. This has a likely outcome of affecting the global supply network. This will have a negative impact on the global economic growth. Because of global supply chains, halting the production of one little component of something in Japan may affect the production of other components in other countries. This holds true for car manufacturers to mobile phones.

Economic activity will adjust to the market. Therefore production will move to the country that has a comparative advantage. Therefore the shutdown of vehicle producing plants in Japan will increase production in other auto producing countries. In light of this, Toyota might lose its market share in the US and globally.

## Economic Impact – Sri Lanka

Sri Lanka will have a least impact from the Japan's disaster since Sri Lanka records less economic exposure to the Japan.

Japan, though a substantial investor in Sri Lanka does not pose a direct effect on exports or imports from Sri Lanka. Sri Lanka records only 2% share of exports to Japan while accounting 2% of tourist's arrivals from Japan. Manufacturers in Japan have back up plants and factories around the world, making the output of products only a small issue. Further, Toyota Lanka commented that Sri Lankan vehicle market does not affect considerably due to the availability of adequate vehicle stocks. Further, they pointed out that a delay in new shipments could be observed short term leading to a limited range of vehicle products available in the market.

The emanating threat to Sri Lanka and other world economies would be Japan's decision to substitute oil and coal power for its nuclear power generation, resulting an additional demand on oil which leads to an oil price hike.

More over, Sri Lanka records LKR 462 billion worth of loans from Japan as at end of 2009, as the single biggest lender to Sri Lanka. The Japanese Yen appreciation against major currencies will cause pressure on national debt on Sri Lanka, while increasing the burden on balance of payments and government budget but this considers to be a short term issue since G7 countries will interfere to stabilize the Japanese Yen shortly.

Further, Japan is one of the major aid providers to Sri Lanka and this situation may lead to a possible reduction of those activities short term.