

# Japan's Lost Decade: From Crisis to Recovery

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# **We revisit Japan's "lost decade" for potential insights about the global outlook**

## **■ My presentation looks back and discusses:**

### **1. Three recovery attempts during Japan's crisis:**

1997 – recovery derailed by Asia Crisis.

2000 – recovery foundered again

2003 – recovery sustained

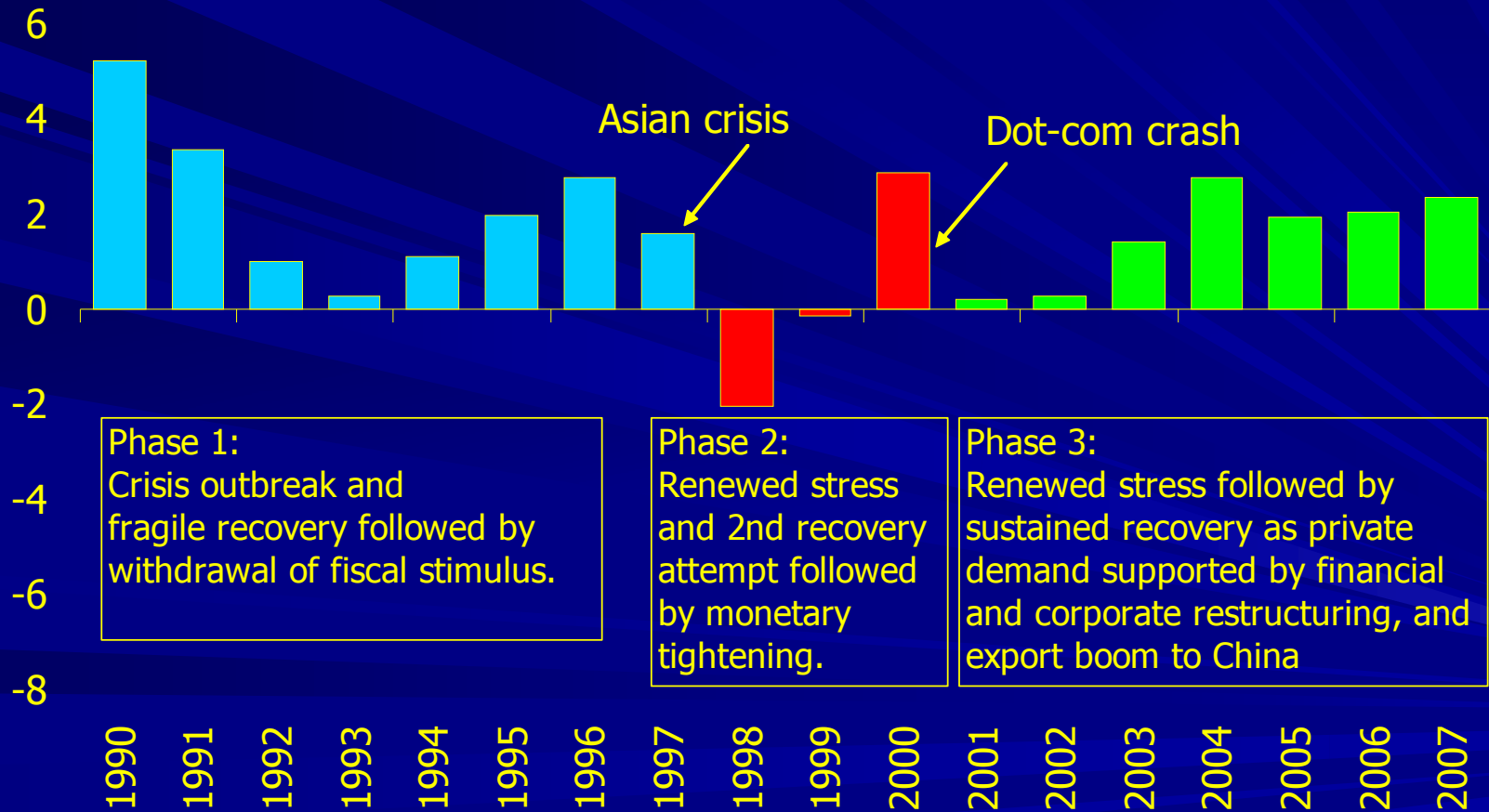
### **2. What was different about the third episode?**

## **■ Next presentation will discuss implications of Japan's experience for current global outlook and policies.**

# Japan's crisis spanned a dozen years with three phases of downturn and recovery...

## Phases in Japan's Banking Crisis

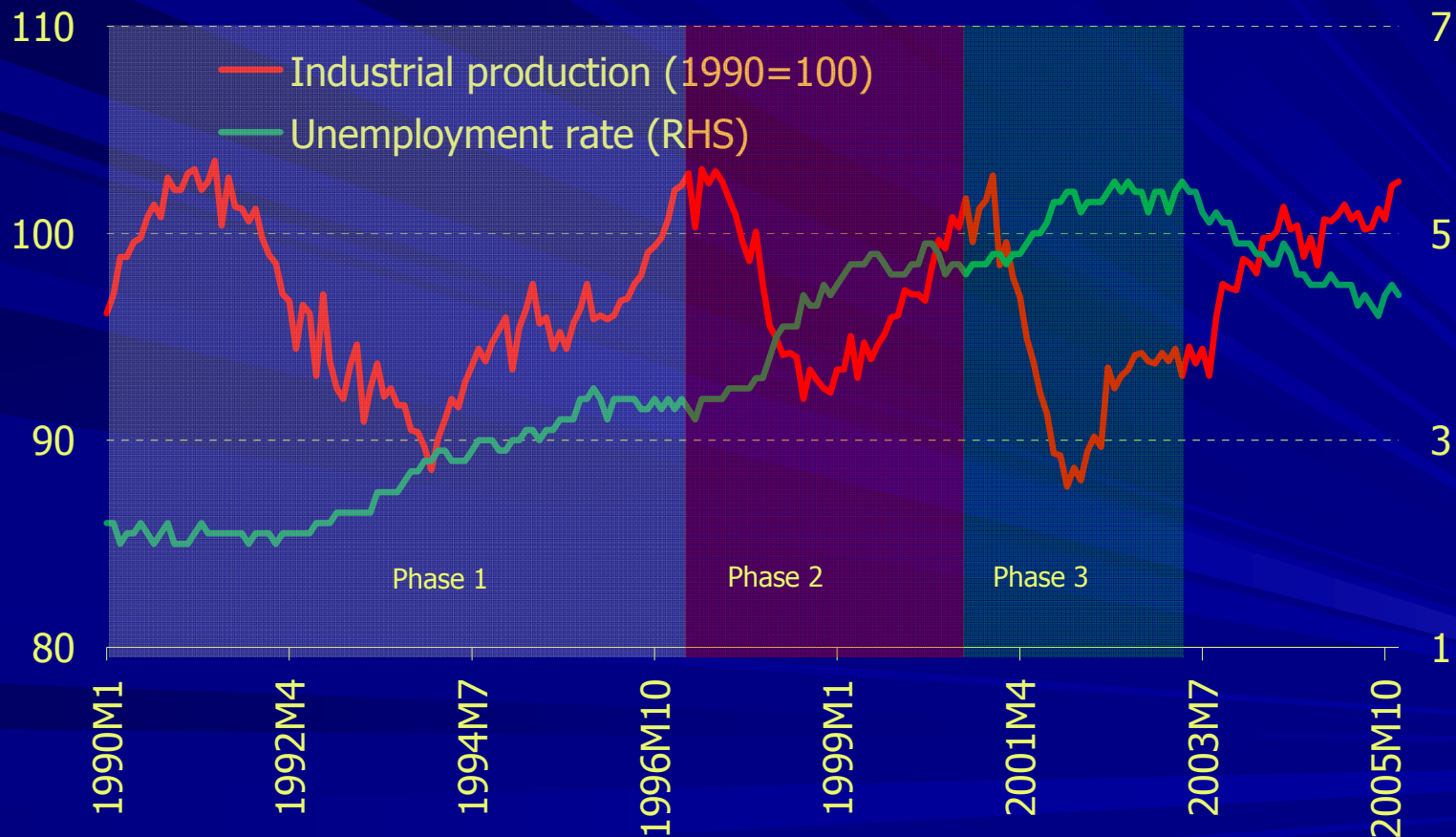
(Real GDP growth; in percent)



Source: Haver Analytics.

# Production and labor market indicators tell the same tale of two incipient pickups followed by a sustained recovery

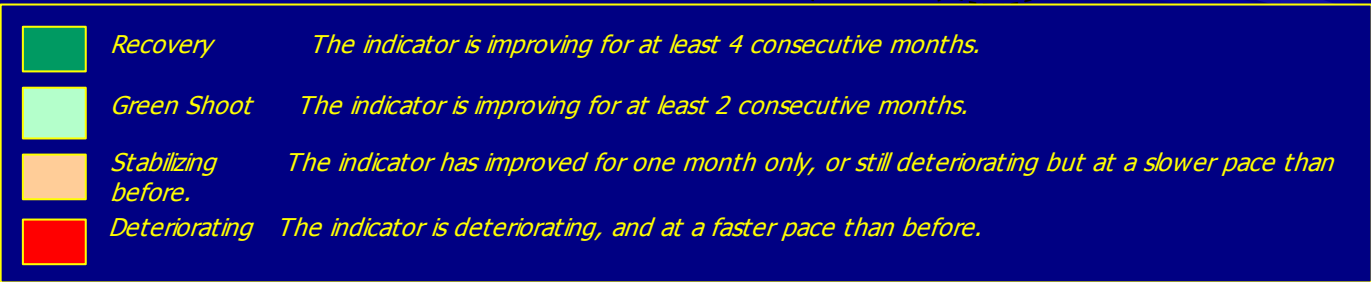
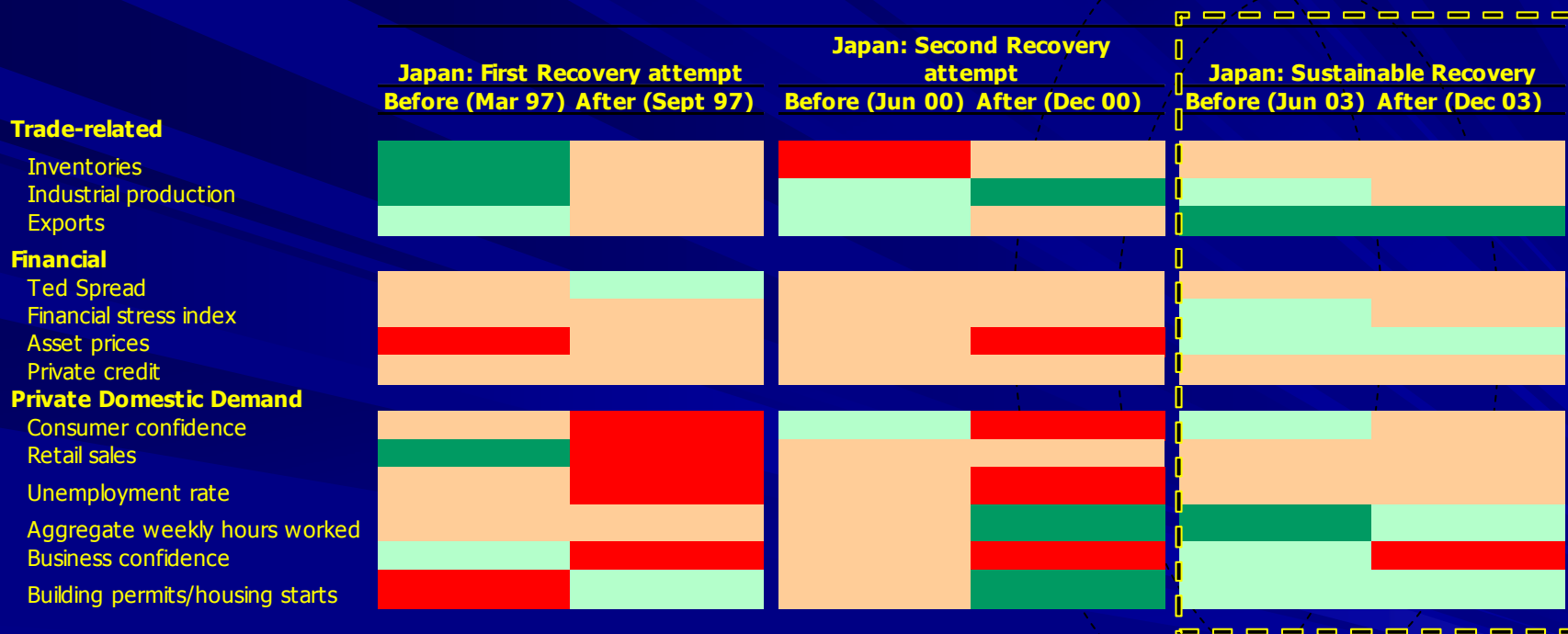
## Japan: Industrial Production and Unemployment



Source: Haver Analytics.

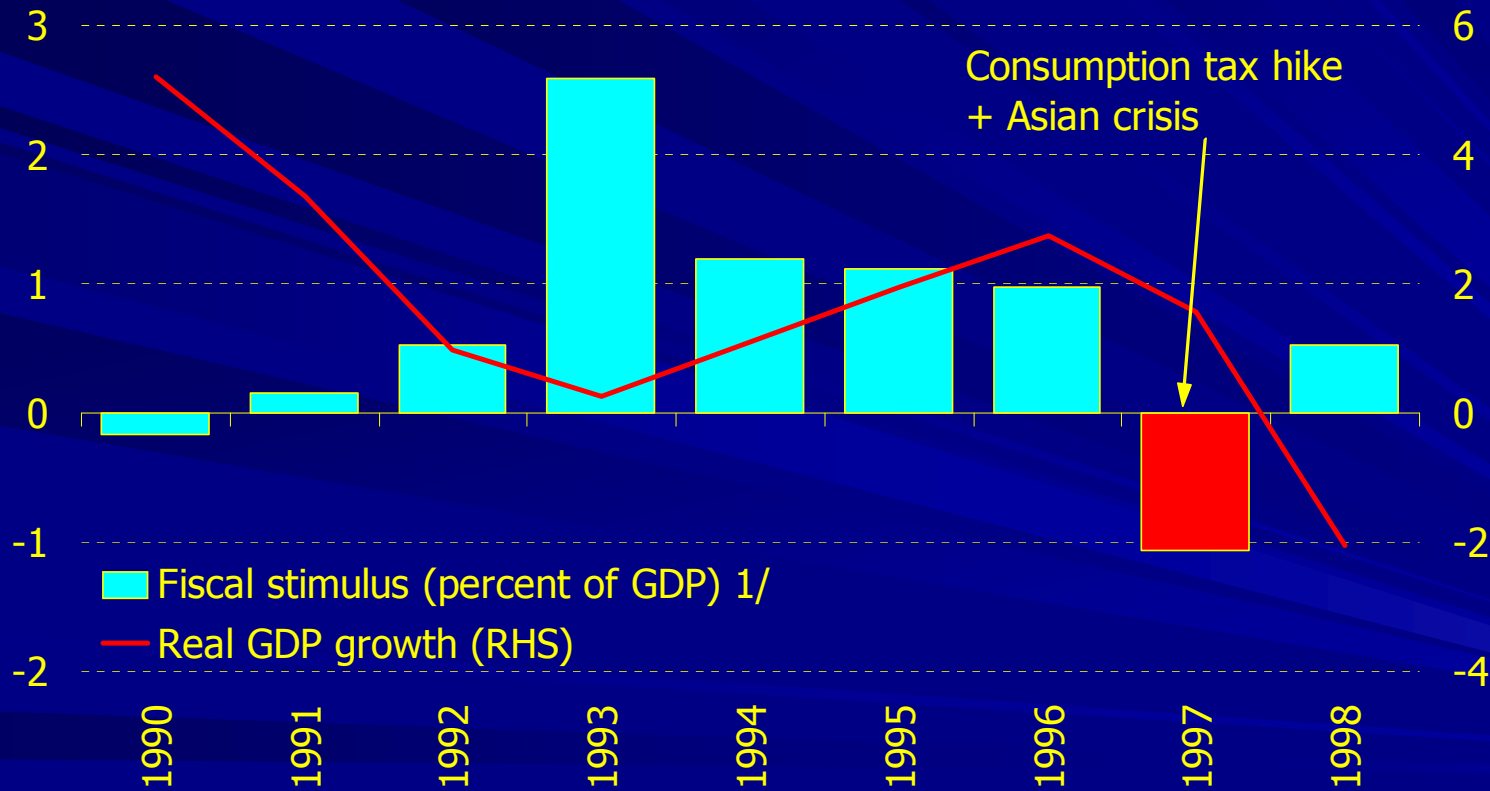
# What did the “Heat maps” show about the recovery at the time?

## The Three Phases of the Lost Decade: Recovery Heatmaps



# Episode 1: signs of recovery allowed fiscal stimulus to be withdrawn -- then Asian crisis struck.

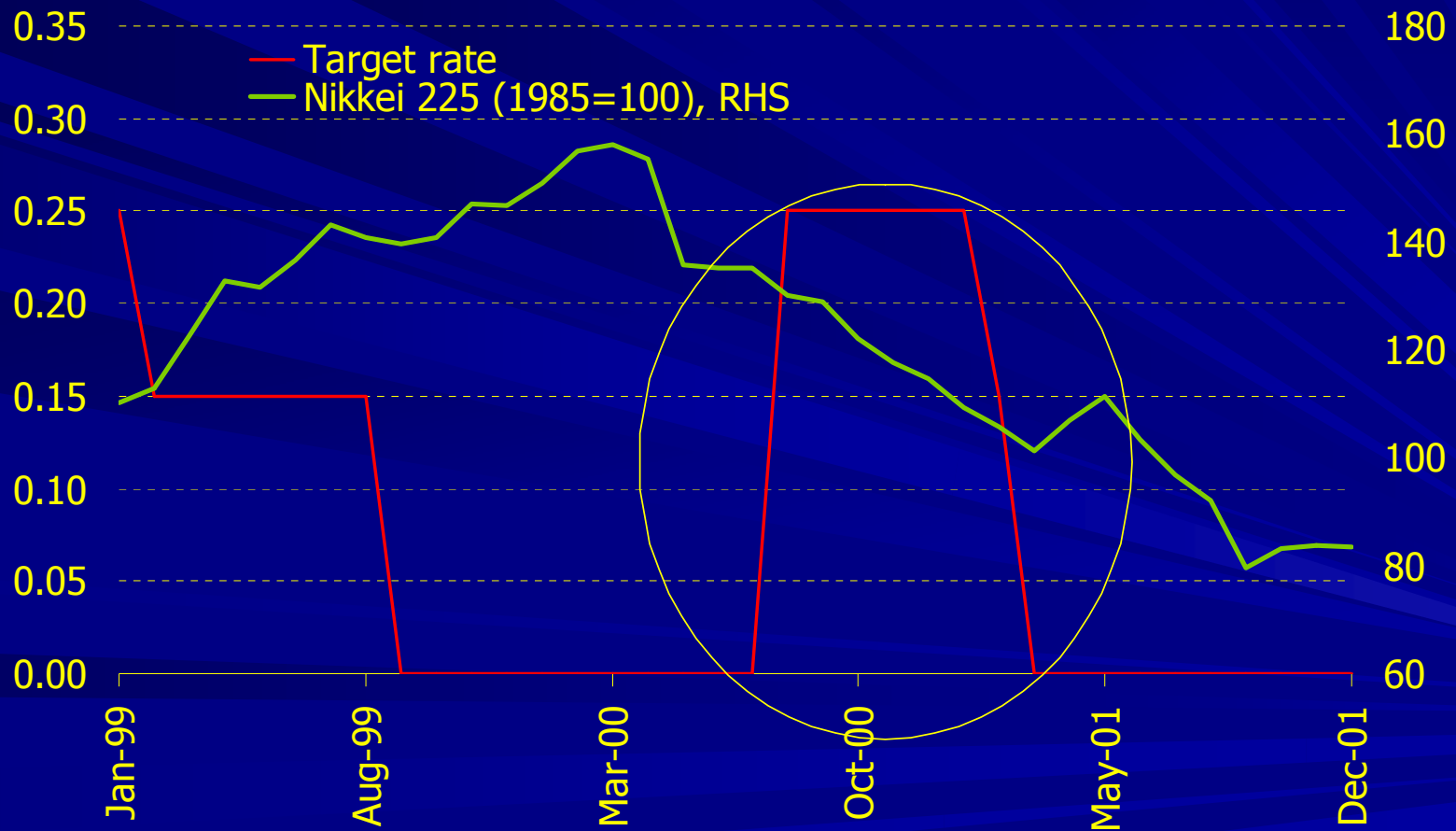
## Fiscal Stimulus and Growth



Sources: Ministry of Finance; Cabinet Office; and IMF staff estimates.  
1Defined as the change in structural balance

# Episode 2: economy on the mend again, but reversal after global IT crash – policy stimulus reintroduced

## Japan: Policy Rate and Stock Market Index

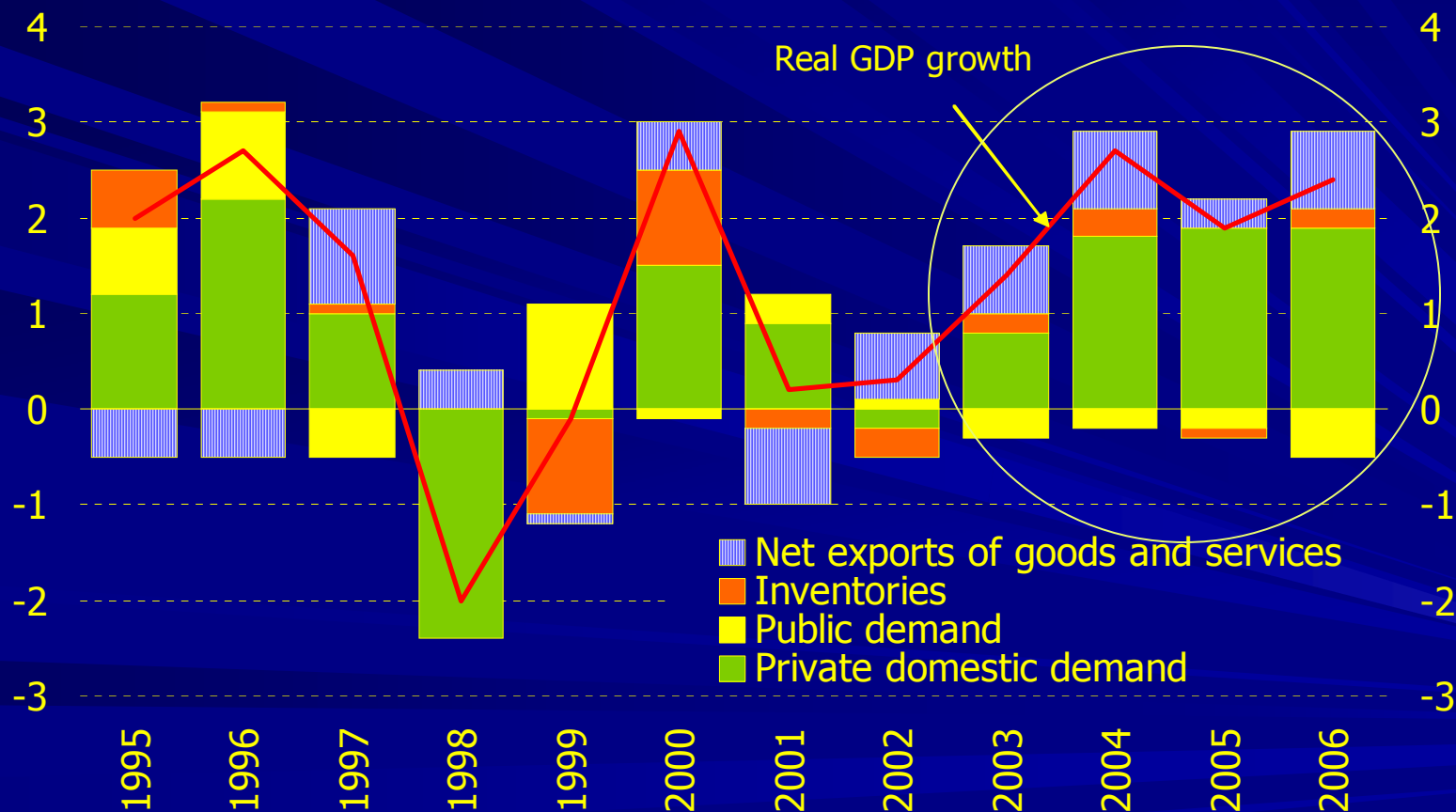


Source: Haver Analytics.



# Episode 3: only at third attempt in mid-2003 did lasting recovery take hold, led by domestic demand

## Japan: Contributions to GDP Growth



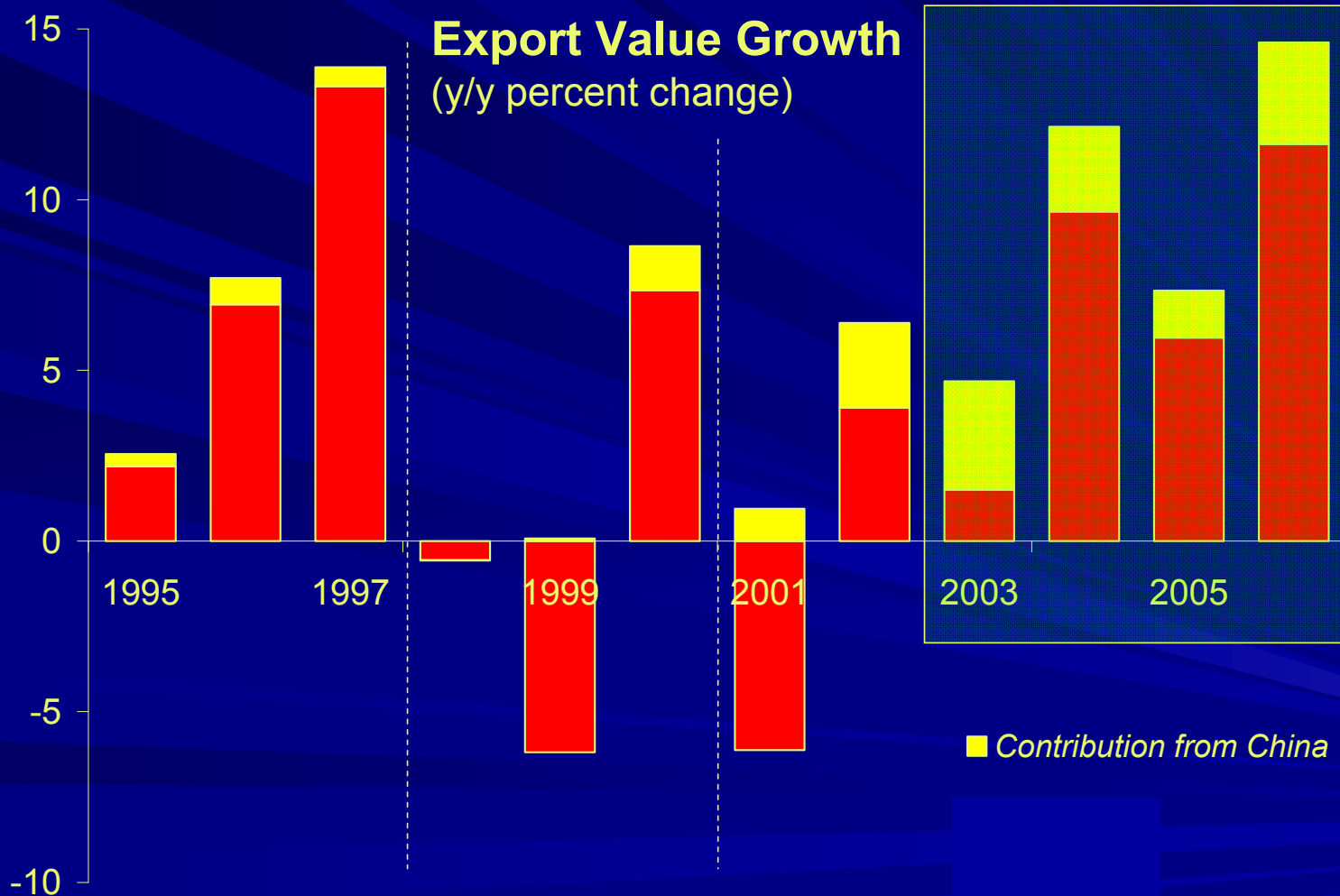
Source: Haver Analytics; and IMF staff calculations



# What was different about Episode 3?

- **External shock was positive**
- **Progress with financial sector reforms**
- **Progress with repairing corporate sector balance sheets**

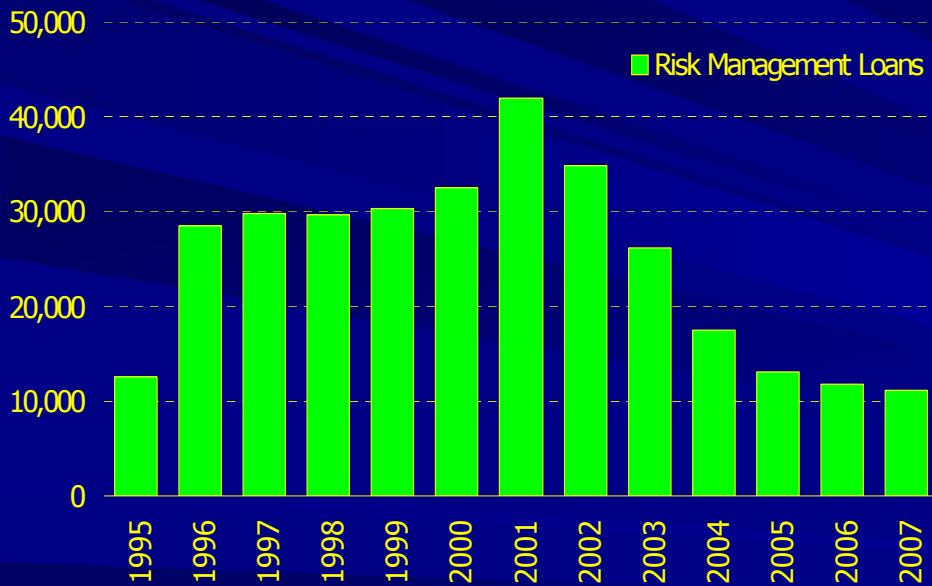
# External environment very favorable for exports, especially to China



# Financial sector: more aggressive approach to reducing NPLs and recapitalizing banks.

## Non-Performing Loans

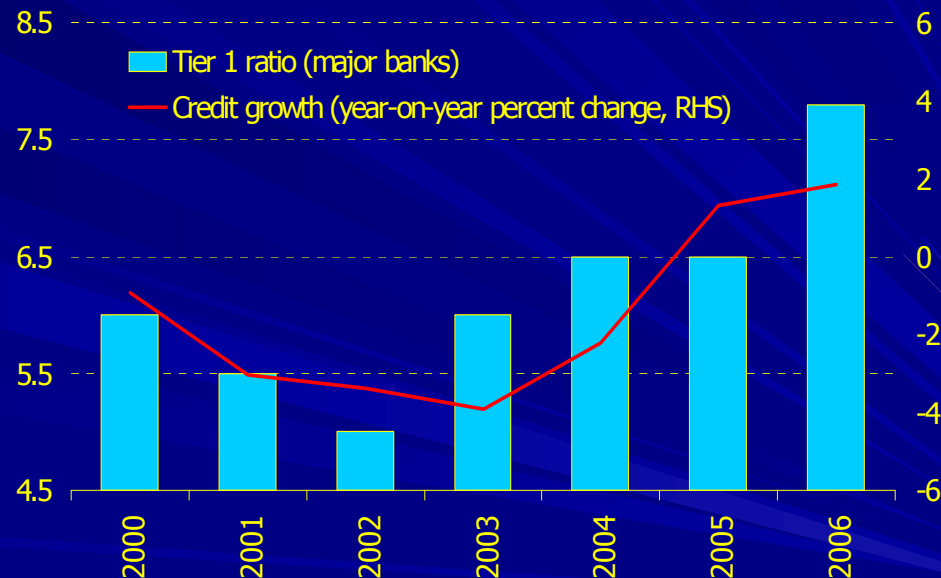
(In billions of yen)



Source: Financial Services Agency of Japan.

## Bank Capital and Lending

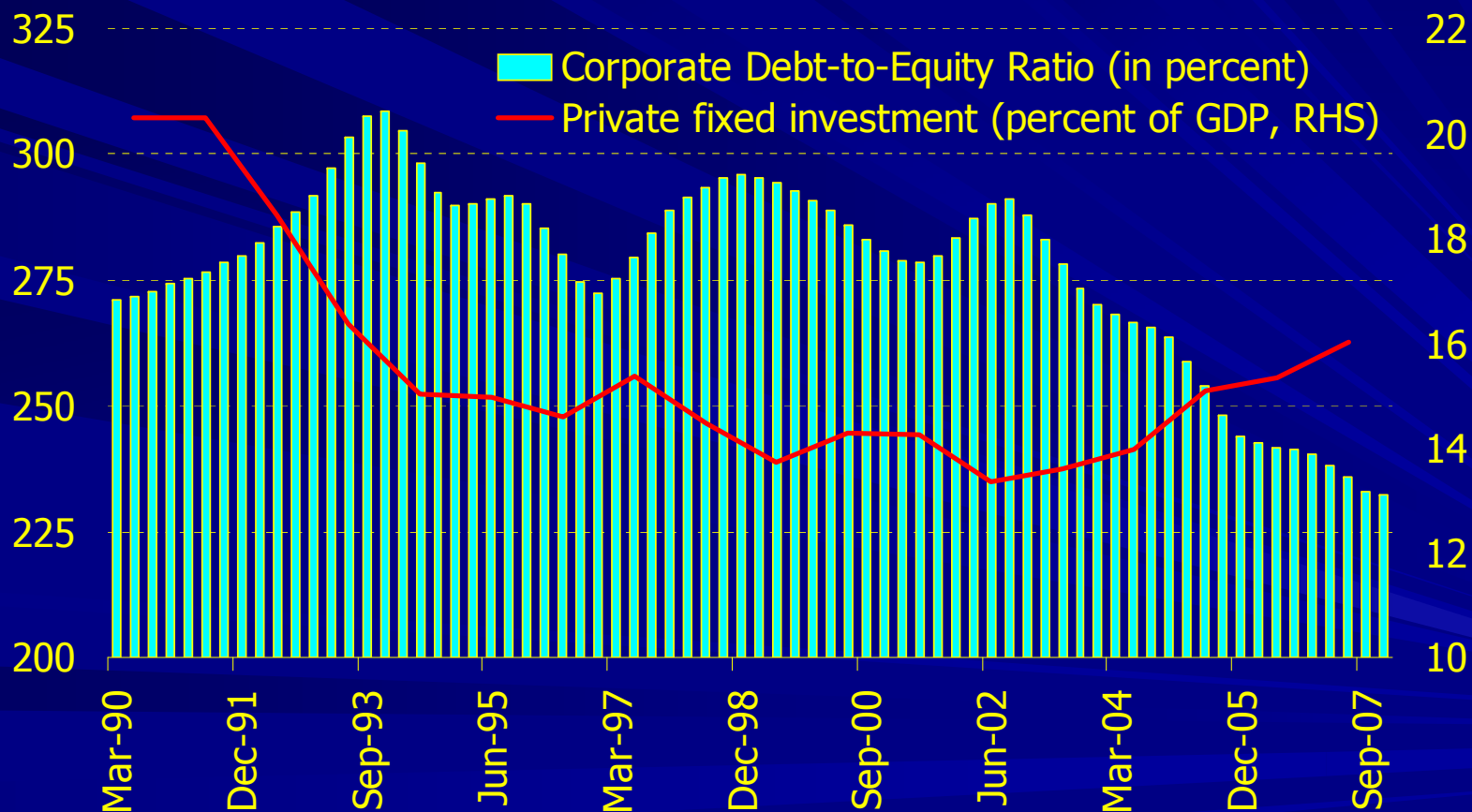
(In percent)



Sources: Haver Analytics; and Bank of Japan.

# Corporate sector: progress with deleveraging helped to lift investment.

## Japan: Corporate Leverage and Investment

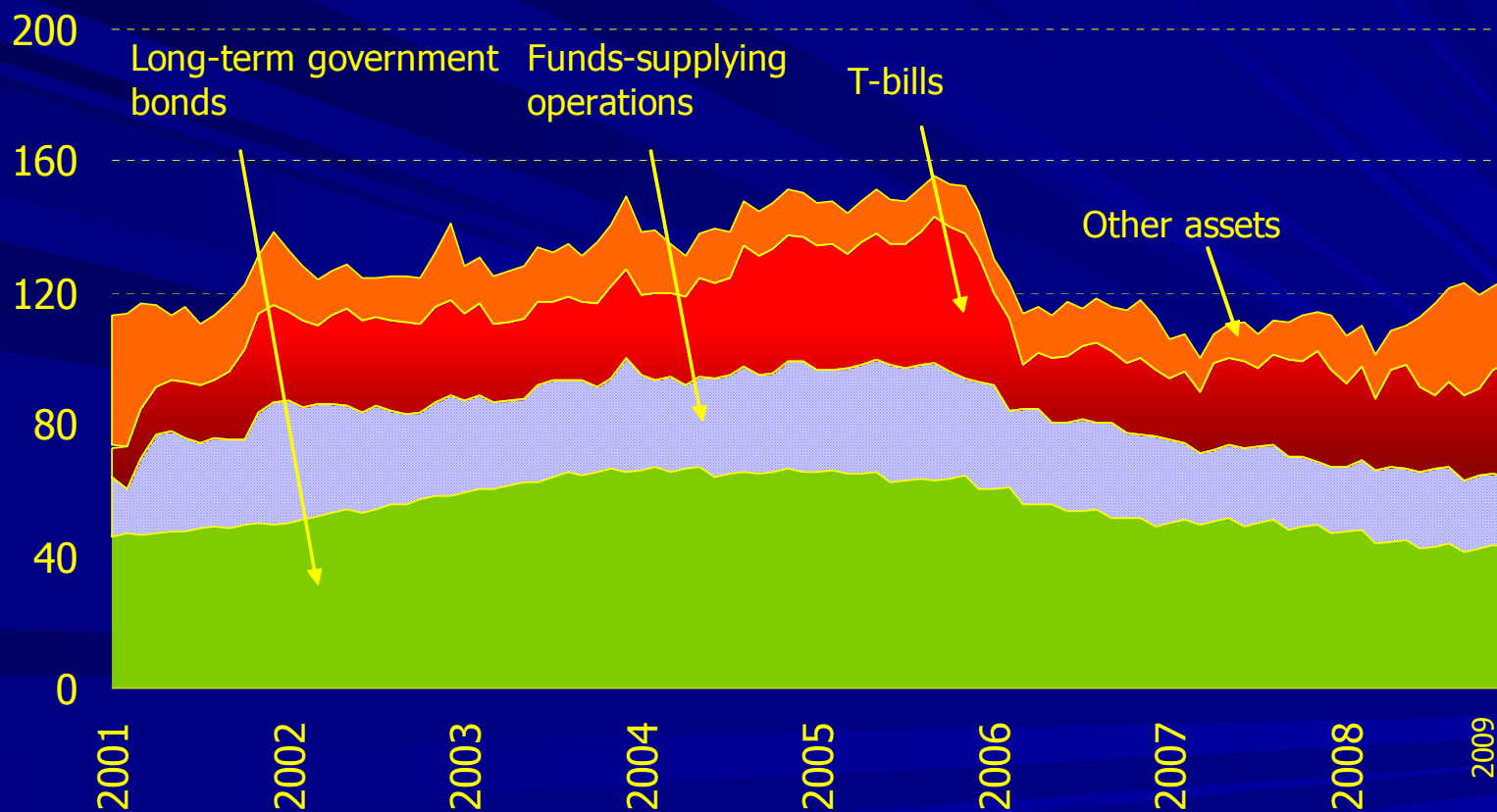


Source: CEIC Data Company Ltd.

# Note on Exit -- Monetary Policy: BoJ able to smoothly unwind its balance sheet

## Bank of Japan Assets

(In trillions of yen)

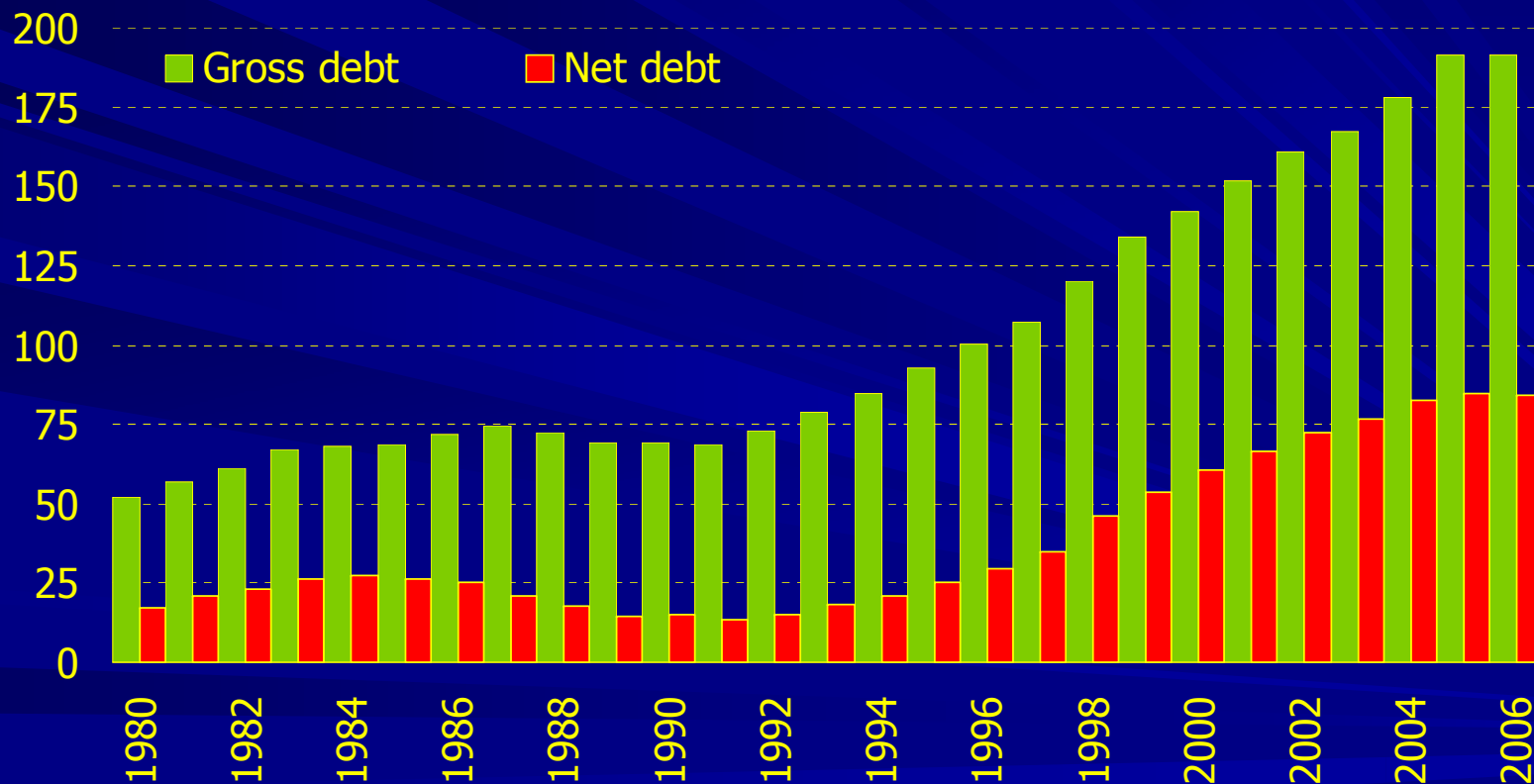


Sources: Haver Analytics; and Bank of Japan.

# Note on Exit -- Fiscal Policy: hampered by protracted downturn, delay in framing medium-term strategy.

## Public Debt

(In percent of GDP)



Source: Cabinet Office; and IMF staff calculations.

# How Does the Great Recession Compare with the Lost Decade? Potential Implications for the Global Outlook

Istanbul  
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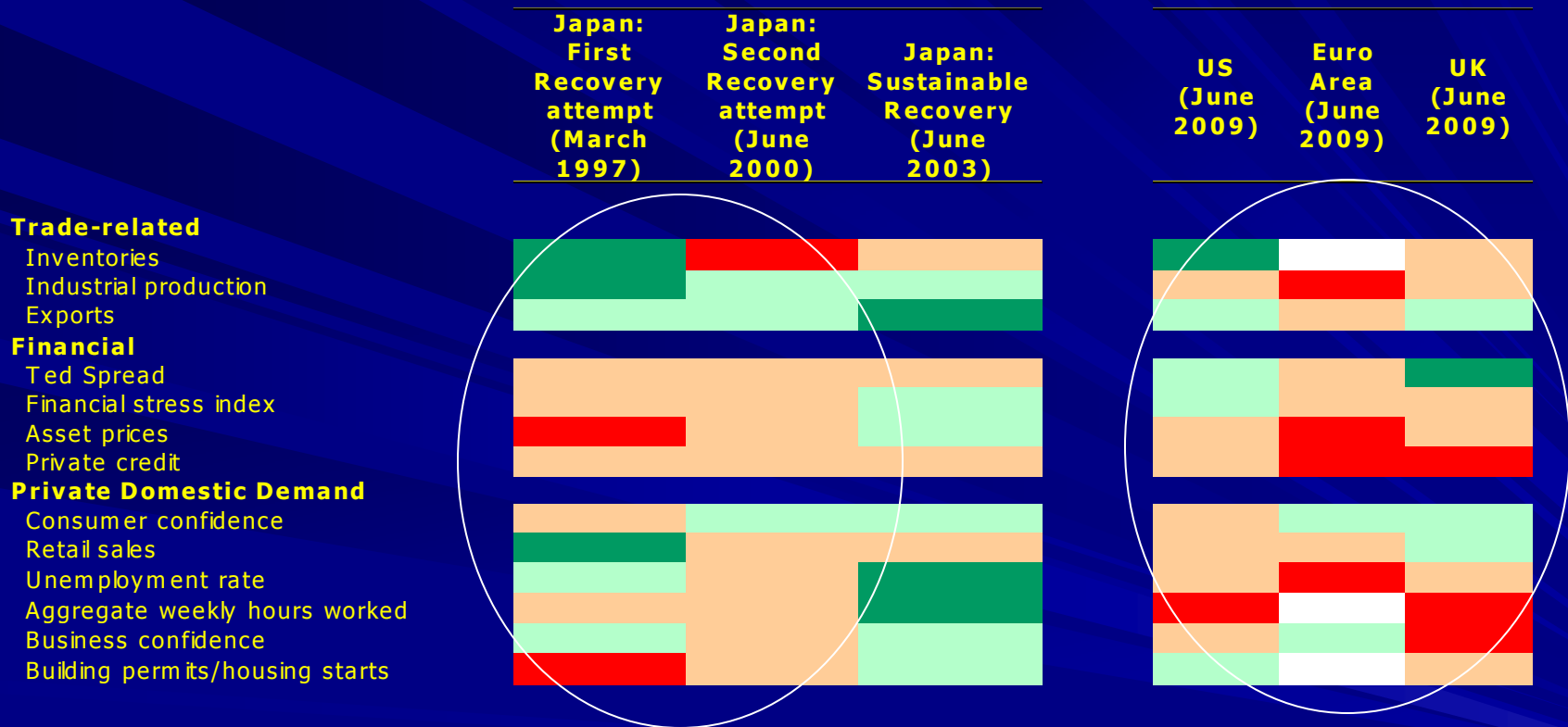


## **We will place Japan's experiences in the current global context**

- 1. What can Japan's experiences tell us about the likely durability of the global recovery?**
- 2. What do they imply about the appropriate policy stance?**

# Advanced economy heat maps resemble somewhat Japan's two early recovery attempts...

Recovery Heatmaps: Japan Then, Advanced Economies Now



Recovery

The indicator is improving for at least 4 consecutive months.



Green Shoot

The indicator is improving for at least 2 consecutive months.



Stabilizing

The indicator has improved for one month only, or still deteriorating but at a slower pace than before.

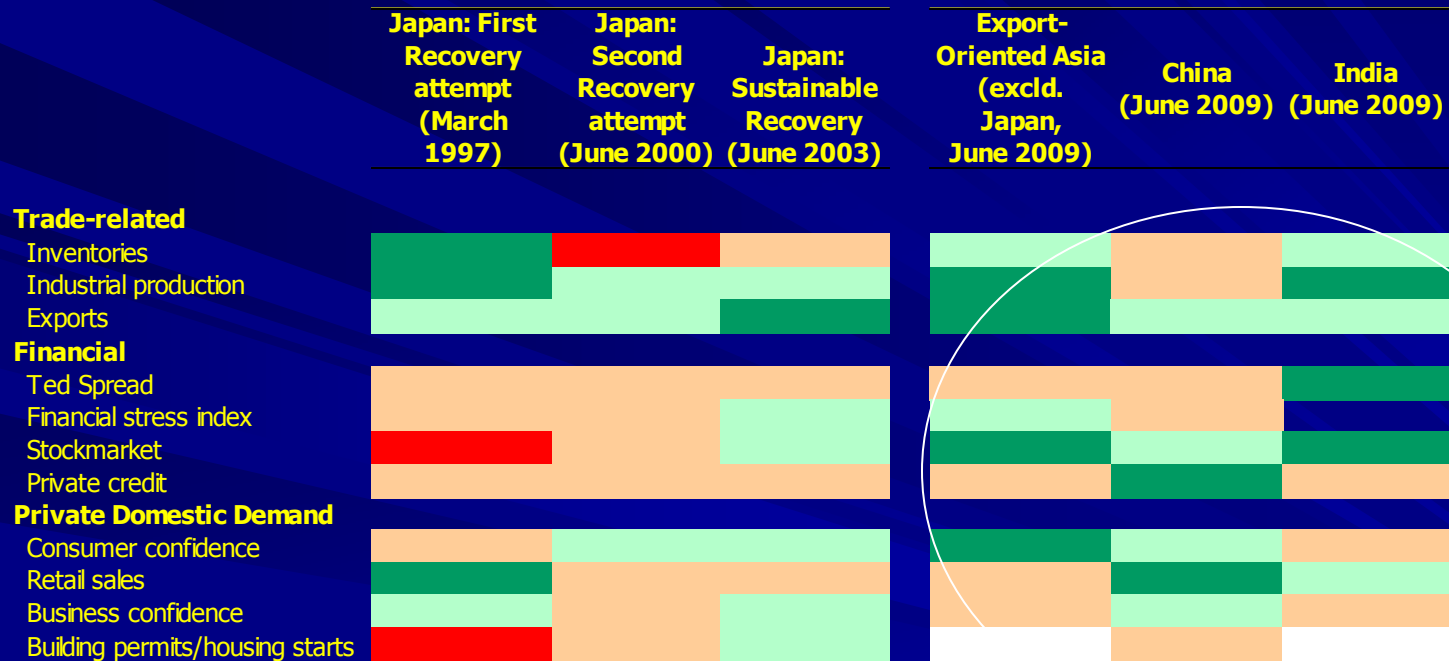


Deteriorating

The indicator is deteriorating, and at a faster pace than before.

# In Emerging Asia, aggressive stimulus and inventory adjustment helping offset weak external demand

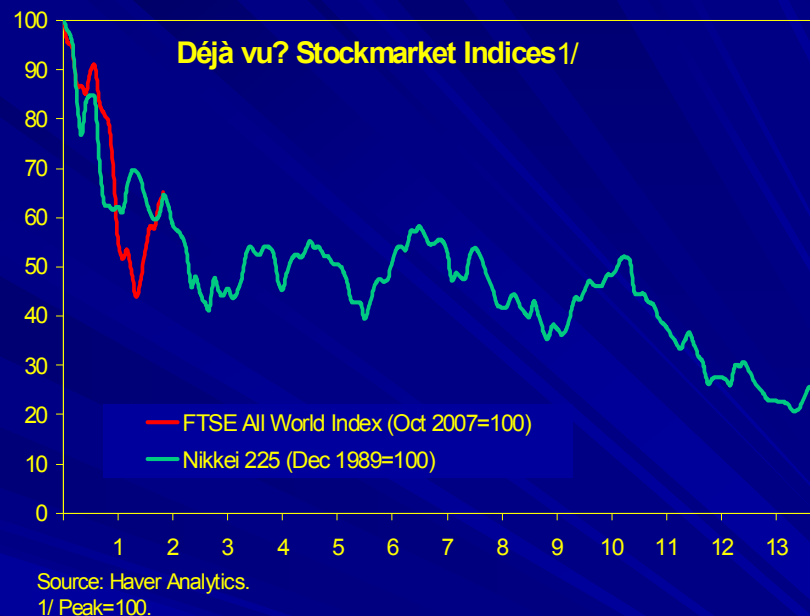
Recovery Heatmaps: Japan Then, Emerging Asia Now



- Recovery**     *The indicator is improving for at least 4 consecutive months.*
- Green Shoot**     *The indicator is improving for at least 2 consecutive months.*
- Stabilizing**     *The indicator has improved for one month only, or still deteriorating but at a slower pace than before.*
- Deteriorating**     *The indicator is deteriorating, and at a faster pace than before.*

# Potential Implications of Japan's Experiences for the Global Outlook

- “Green shoots” do not guarantee a recovery.
- Financial fragilities can magnify effects of adverse shocks on the economy.
- Weak global environment could limit prospects for an export-led recovery.



# Potential Implications of Japan's Experience for Policies

- Policy stimulus should be maintained for now, but no panacea
- Underlying financial problems need to be addressed for a durable recovery to take hold.
- Clear exit plans can help reinforce confidence.
  - Role for developing cooperative and coordinated exit strategies.