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## Japan

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# IMF's Shock Therapy 'Just Not Functioning'

by Kathy Wolfe

According to official statistics just released, Japan is now in its worst economic crisis since the 1971 break of the dollar from gold and the 1974 "oil shock." A flat loss of 1.03 million jobs, net, in the 12 months to October 31, has brought unemployment to a record high of 5.4%. It was the first loss of 1 million jobs in a year since 1974, dwarfing anything during the 1997-99 "Asia Crisis." Most layoffs were in basic industries such as manufacturing, transportation, communications, and construction.

*Another 2 million jobs, net, are slated to go by Spring.*

The Nikkei Commodity Index hit a record post-war low on Nov. 30, of 99.2% on the scale of 1970=100; wholesale prices of physical goods used in production, such as steel, chemicals, and refined fuels, are actually lower than in December 1970, before Nixon pulled the plug on the dollar in 1971 and almost doubled the yen's value. Consumers, fearing layoffs, have slashed buying. Businesses, fearing that banks will call in loans, are cutting outlays and prices.

This *deflation* of the physical-goods sector has accelerated, with both wholesale and consumer prices falling at increasing rates for the past seven months, despite extreme central bank monetary hyperinflation.

Standard & Poor's, London Fitch Ltd., and Moody's Nov. 28-Dec. 4 reports downgraded Japan Government Bonds (JGBs) a third time, from AA+ to AA, putting the nation's credit at the bottom of the Group of Seven industrialized nations, after it began 2001 at the AAA top notch. S&P cited "deep-seated economic woes."

The International Monetary Fund (IMF) meanwhile sent its fourth high-level delegation to Tokyo this year on Dec. 6, to check on "serious problems" at Japan's banks, a source close to IMF senior adviser Stanley Fischer said.

### 'Put People On The Streets'

The IMF has been privately demanding mass layoffs in Japan for months. "Officials in Japan are too reluctant to see people on the streets," the IMF's Japan Desk officer said in June, as *EIR* reported. "There's not enough pressure by the Japanese government on banks to act to close companies! Banks are sustaining their corporate customers at low rates by just rolling their loans over, and the regulators let this proceed. We want the regulators to get tough on the banks. If they do, the banks will be forced to get tough on the borrowers."

That would lead to many more bankruptcies — and that's what they need. That may mean a lot of unemployed forced onto the streets, but this is what is needed." (See *EIR*, June 15, 2001.)

After "annual consultations" on Japan's economy in Tokyo in August, the IMF stepped up pressure on the Financial Services Agency (FSA), Japan's key regulator. In a 66-page assessment of the economy on Aug. 10 which the media ignored, the IMF on paper endorsed the views of Wall Street "private analysts" such as those at Goldman Sachs and Morgan Bank, who are calling for layoffs.

The outright bankruptcy of major Tokyo retailer Mycal Corp. on Sept. 17, indicated new FSA concessions to the IMF, the Japan Research Institute said. Mycal's bank Mizuho Holdings called in both "at-risk" (i.e., "bad") loans and also "loans requiring caution," a.k.a. "grey zone loans," not usually considered bad. The FSA officially totals \$343 billion in loans as "bad," but classifies three times that much as "grey," meaning that forced bankruptcies could triple if this standard were generally applied. The FSA then launched a new round of "special examinations" in mid-November, combing over banks' books to spotlight the status of loans to all large corporate borrowers. Lo and behold, in the last week of November, Tokyo's 13 major banks wrote off a record \$52 billion in bad loans, 3.4 times the amount projected for the quarter.

### IMF Is 'Way Out Of Line'

Behind the scenes, Tokyo and Washington officials say, a showdown is brewing: between the IMF, which is demanding that Japan adopt the 1997-99 IMF program which destroyed South Korea, and Japan's technocrats, who say that the IMF free-market model is "simply is not functioning."

U.S. diplomat Steven Bosworth told Nikkei on Nov. 23, that Japan's government interference in the credit system is "very similar to South Korea's before 1997." So, the IMF's deregulation of Korea, during which Bosworth was ambassador to Seoul, "should be a model for Japan."

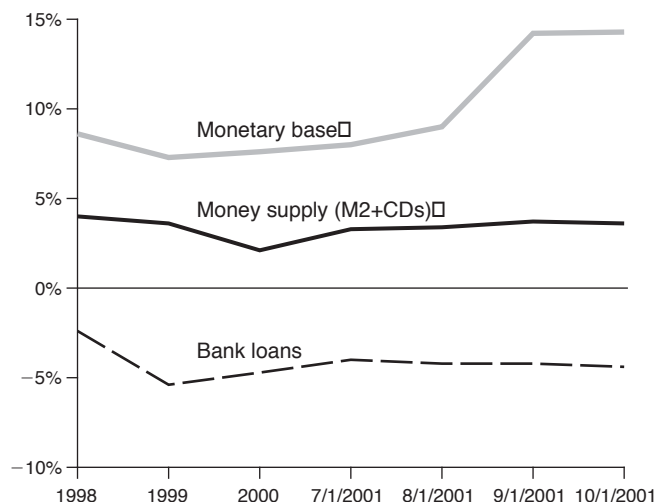
The IMF is only chartered to make short-term cash loans to countries such as Japan and Korea, which have trade and payments surpluses. Asian analysts charge that it overstepped its bounds in Korea, by demanding that hundreds of banks and industrial companies be simply shut down or sold to the highest foreign bidder. Twice in November 2000, the IMF issued "recommendations" that Seoul "liquidate" a dozen U.S.-based Daewoo subsidiaries, or 50 medium-size companies in Korea. "The IMF was way out of line, but it was profitable for Wall Street buyers," said one source.

The IMF's Aug. 10 "assessment" of Japan was just as "out of line," stating that "unviable financial institutions should be encouraged to exit." Where a bank is deemed viable but the government has to give it a capital transfusion, the banks' loans require "strong restructuring plans involving debt workouts and satisfactory returns on equity"—i.e., a lot of corporate borrowers have to be shut down like Mycal was—or else "it will be critical for the government to take appropriate action" and close the bank. "Directors emphasized that suc-

FIGURE 1□

## The More Japan Prints Money, The Less Banks Loan To The Economy□

(Percent Change)



Source: Bank of Japan.□

cess of the program to accelerate bad loan disposal depends on achieving the restructuring of distressed firms and the prompt exit of nonviable entities.”

With this deflation, the IMF is simultaneously promoting hyperinflation. Their August assessment noted that the Bank of Japan (BOJ) has raised its target for the monetary base—current deposits of cash available to banks at the BOJ at the end of each day—from 4 trillion yen at the start of 2001, to 5 trillion yen in March, but demanded that “the BOJ should not delay in raising its quantitative target.” The BOJ then raised the monetary base to 8.6 trillion yen (\$72 billion) by the end of November. Now the IMF and Washington are demanding the BOJ go beyond its “zero interest rate” policy to “inflation targetting,” in which the BOJ would agree to add “whatever it takes” to the monetary base to stop prices from falling.

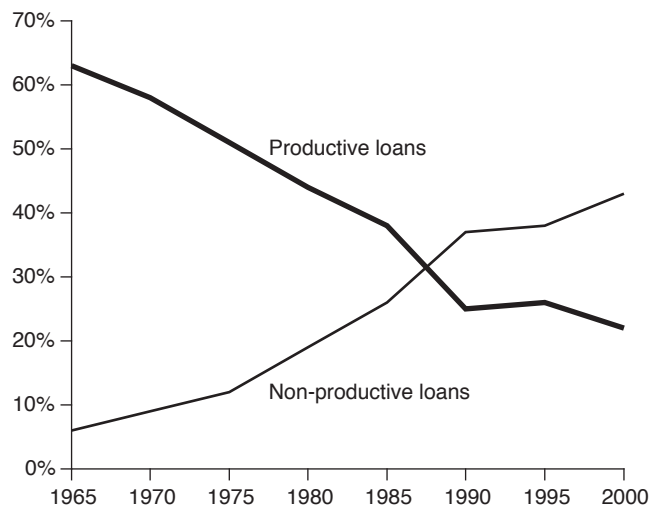
Tokyo sources say this is insane. The BOJ, itself alarmed enough to take any measure available to stop the physical commodity deflation, simply has no mechanism to do so. No matter how much cash it forces into the banking system, consumers and corporate borrowers are cutting back activity and repaying loans: “No one wants to borrow any money,” as one official put it, “and the banks are being told to cut their loan portfolios, so no one wants to lend any. The banking system is entirely dead.”

The rate of growth of the BOJ’s monetary base (Figure 1) has gone up drastically lately, to 14.3% in October. But money supply growth—the total amount of cash and bank certificates of deposit which consumers and businesses are actually putting into circulation by doing business—continues at a flat 3-4% rate, no matter what the BOJ does. And bank lending is responding *in opposition*: The more the BOJ

FIGURE 2□

## Japan Banks’ Domestic Loans To Productive And Non-Productive Economic Sectors□

(Percent Of Total Loans)□



Source: Bank of Japan Economic Statistics Annual.□

prints, the more the banks cut back their loans. The IMF keeps talking about the market, “but the market simply is not functioning any more,” he stated.

After downgrading Japan’s government debt on Nov. 28, Standard & Poor’s also warned that it may soon cut its ratings on 12 major Japanese banks, including the largest and second-largest banks in the world. S&P said it had placed on “credit watch,” with negative implications, the Bank of Tokyo-Mitsubishi, Dai-Ichi Kangyo Bank, Fuji Bank, the Industrial Bank of Japan, Yasuda Trust, and others. “There is a high risk that the financial condition of corporate borrowers will continue to deteriorate and at a faster pace,” said S&P.

Most of the loans to Tokyo’s 1980s real estate speculation “bubble” have been written off. The problem now, officials agree, is basic commercial and industrial loans, loans to manufacturing *across the board*, going bad. “What sectors the borrowers are in for the non-performing loans, is highly confidential,” one official says, “but if you just look at the published figures for where Japanese banks are making their total loans, sector by sector, you can figure it out.”

As *EIR* showed in a 1995 study, until 1965 over 63% of loans by the top 150 banks went to the productive activity—manufacturing, agriculture, construction, utilities, transport, and communications. Little of this was to production of Pokémon-style consumer opiates. Only 6% of loans went to physically non-productive sectors such as finance, insurance, real estate, and other services (Figure 2). By 2000, non-productive loans had taken over. Now Japan will have to choose between the Pokémon economy, and the challenge of building something new.