

## U.S. AND JAPAN TO BE AFFECTED BY ASIA'S PROBLEMS

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### *The U.S.: Continued Growth but Growing Inflation Worries*

The U.S. economy continued its robust growth during the first half of 1997. The annual growth rate of the real GDP was 4.9% in the first quarter and 3.3% in the second quarter. However, despite the high growth rate of GDP, the inflation rate during the first half of this year was low enough for the Federal Open Market Committee (FOMC) to leave the Fed funds rate unchanged since March of 1997. The monthly Producers Price Index (PPI) fell each month for the first seven months of this year. The price index for GDP rose at 1.4% annual rate in the second quarter, down from 2.4% in the first quarter.

The third quarter seems to show continued strong growth, but with growing concern about inflation. The growth rate during the third quarter is estimated to be higher than 3%. The PPI increased by 0.3% in August and 0.5% in September. However, demand is growing. Retail sales rose in September for the fourth consecutive month. Although productivity has increased for the last two years, the capital spending on basic capital equipment has also increased to accommodate increasing demand for consumption goods. The increasing capacity could lower the unemployment rate and raise wages, which could cause higher inflation rates.

The sudden drop of U.S. stock prices on October 23 after the crash of the Hong Kong stock market should press down U.S. prices. When the Hang Seng index of Hong Kong crashed sharply, investors sold off U.S. stocks for profit taking. U.S. stocks were regarded as being overvalued by 10-15% before the Black Monday crash of the Dow Jones index by 7.1%

on Oct. 27. The recovery of Dow index by 4.7% on Oct. 28 implies that the collapse was caused by psychological reasons, not by the fundamentals of the U.S. economy. The economic crises in Asia will probably lower the growth rate of the U.S. economy mainly because of the decrease in U.S. exports to East Asia.

### *Japanese Economy Still Stumbling*

The Japanese economy is still in a slump, which more or less began in the early 1990s. During this long stagnation period, Japan has tried to use fiscal policy to stimulate its economy to recover; however, the increasing government expenditure has failed to do so. This policy increased government debt to about 90% of its GDP in the 1996 fiscal year. Japan lowered its discount rate to 0.5% in 1995 to devalue its currency and reduce the bad debt of financial institutions as well as to increase industrial investment. Although the Japanese economy grew more than 3% in 1996, it has once again become stagnant the increase in the purchase tax in April this year. The Japanese government announced a policy to stimulate the economy on Oct. 21, but the structural weakness of Japanese economy has undermined its chances of success.

The crash of Hong Kong stock market attacked the weak Japanese economy. Japan exports 40% of its total exports to East Asia and holds a large amount of financial assets within the region. Many Japanese firms are producing their goods in Asia. Japan may suffer a recession until the recovery of the East Asian economy. In addition, the worsened financial system of Japan will delay any economic recovery. **VIP**

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