Economist: Japan needs weaker yen

Currency’s rally is a ‘knee-jerk’ reaction in the market

By Gabriel Chen
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THE yen should “fundamentally” be weaker not stronger because Japan faces mammoth reconstruction that will test its already huge budget deficit, according to the economist who predicted the global financial crisis.

Dr Nouriel Roubini told a gathering here that Japan already has the industrialised world’s biggest public debt, at around 200 per cent of gross domestic product (GDP).

“If there’s going to be large budget deficits that are going to be monetised, the yen may become weaker rather than stronger,” said Dr Roubini at the Singapore Management University (SMU) yesterday.

“Japan probably needs a weaker yen because even before this earthquake disaster, the yen was too strong given that domestic demand is anaemic as real wages are not growing very much, and the major source of economic growth for Japan was net export growth.”

The economic impact of the disaster is widely expected to be at least as bad as that from the 1995 Kobe earthquake and there are early estimates that damage could amount to as much as US$35 billion ($45 billion).

Expectations that Japanese insurers and companies will repatriate funds to help pay claims and reconstruction costs pushed the yen to a high of 80.60 to the American dollar on Monday, not far off its record high of 79.75 to the greenback in 1995.

Dr Roubini, who is based in the United States, called the yen’s current rally a “knee-jerk reaction in the market”, but also lauded the actions taken by the Bank of Japan in the last few days to unleash trillions of yen into the financial system to help ease liquidity.

“I would say that the policy response in the short term as of today by the Bank of Japan has been the correct one,” he said.

Dr Roubini explained that Japan, which had its credit rating recently downgraded, will need to invest in a major stimulus program to reconstruct.

This, in turn, will increase the country’s debt at a time it is trying to limit deficit growth.

“Given the domestic shocks that have occurred right now, they need to sustain growth through further net export growth through a depreciation of the yen… and therefore on a fundamental basis, the yen should be weaker rather than stronger,” he added.

Apart from Japan, where there is uncertainty over “how severe things are going to get”, Dr Roubini also expressed concern about the “anaemic” pace of growth in advanced economies.

He cited unemployment and public finances in the US and the ongoing sovereign debt crisis in the euro zone.

Dr Roubini was one of the few economists to predict the 2007 crash and earned the nickname “Dr Doom” for his typically pessimistic views on economic situations.

His fame has spread beyond Wall Street to Hollywood.

He played a character based on himself in the recent Oliver Stone movie Wall Street: Money Never Sleeps.

“Sometimes people refer to me as being Dr Doom, but I prefer to be called Dr Realist,” Dr Roubini told students and academics at SMU yesterday.

“I try to give an objective assessment of what can go wrong and what can go right.”