

COUNTRY PROFILE:**REPUBLIC OF JAPAN****DATED:****AUGUST 2009****CREDIT GUARANTEE:**

IES/02: ATTACHMENT A

Recent Political Highlights

- Political leaders took to the streets on the 18th of August as campaigning began in one of the most hotly contested elections. The ruling Liberal Democratic Party (LDP) has governed alone or in coalitions for the past 55 years, except for a 10-month respite in the early 1990's. The Democratic Party of Japan which was founded 10 years ago has controlled the upper house since elections in 2007, but the party that controls the lower house has the power to install the Prime Minister. The ruling party's support has been plunging because of a weak economy, increasing unemployment, a perceived lack of leadership and its support of higher taxes. News that the economy grew in Q2'09 provided an opportunity for the LDP to direct voters' attention to its measures to fight the recession. The elections for the 480 seats in the lower house to be held on August 30th are one of the biggest tests the LDP has ever faced. If media forecasts are correct, it could cost the party control of the government.

Recent Economic Highlights

- Japan came out of recession in Q2'09 after its economy recorded annualised growth of 3.7%, up 0.9% on the first quarter. The growth comes after four consecutive quarters of contraction, including a 14.2% contraction in Q1'09 with unemployment rising to a six-year high of 5% in April. Government stimulus packages totaling \$260bn helped to boost the economy, including cash handouts and subsidies to buy energy-efficient cars and home appliances. Correspondents say the rise is due to the government stimulus package and it's unclear whether the momentum will be sustained as domestic private consumption rose only 0.8% despite the stimulus measures. If Japan's latest quarterly rate is maintained for a full year, GDP growth would register 3.7%.
- The EIU expects GDP to contract by 6.8% this year following a collapse in exports and investments. The IMF forecasts a contraction of 6% this year. Fiscal stimulus packages combined with lower tax revenue will cause the budget deficit to widen to 7.9% of GDP in 2009 and 8.5% of GDP in 2010. The government recently abandoned its aim of eliminating the primary budget deficit by 2011 and instead it plans to halve the gap within five years. According to the IMF, the fiscal deficit is projected to widen to 11.5% of GDP in 2009.
- Manufacturers also benefited from recovering demand in China and other markets, with overall exports up 6.3% during Q2'09. The EIU estimates the current account surplus to average 2% of GDP in 2009-2013.
- Japan's central bank kept its key interest rate unchanged at 0.1% in August and maintained a cautious view on the economy's strength of recovery. Inflation is forecast to remain negative until 2011 and the Bank of Japan is also expected to hold interest rates near 0% at least until 2011. Reflecting improvements in the credit markets and companies' sluggish demand for operational and capital investment, bank lending rose 2.1% in July from a year earlier.
- Japan's industrial output declined by an average of 29% y/y in April and May. Japan's construction-machinery shipments are expected to decline almost twice as previously estimated as the recession cuts demand from developed nations. Factory shipments of excavators, tractors, cranes and other machines used in construction and mining may fall 42% to \$12.1bn in the year to March 31. Domestic shipments may drop 38%. A recovery in capital spending is not assured until demand picks up.
- The number of Japanese corporate bankruptcies in July rose 1% from a year earlier to 1,386 cases with debt involved totaling \$3.8bn, the smallest amount this year. Compared with June, the number of bankruptcies fell 2.5% in July and the amount of bankruptcy debt was down 22.2%. By sectors, bankruptcies of manufacturers grew 16.1% from a year earlier to 216 cases. Failures in construction firms decreased 8.2% to 390 cases.
- Japan's businesses stand to pay as much as \$95 million more in monthly electricity bills under a new plan to encourage solar-power generation. Starting in November, the government will compel utilities to buy surplus solar power generated by households and factories and pay twice the regular rate as an incentive for installing solar panels. The country's 10 regional power producers will be allowed to pass on increased costs to customers starting in April.
- At least 12 people were killed in torrential rains in Japan, while typhoons caused casualties and destruction in other parts of Asia. The hardest-hit prefectures were in western Japan.

Latest Trade Developments

- SA exports to Japan totalled R49.5bn in 2007, R66.5bn in 2008 and R14.5bn in the year-to-May 2009. SA imports from Japan totalled R36.9bn in 2007, R40.6bn in 2008 and R11.4bn in the year-to-May 2009.
- A WTO panel has rejected a US appeal in a case that struck down how it calculated import duties, handing over victory to Japan. The case against the zeroing calculation was brought by Japan in April and inflates imports duties. Zeroing considers the difference in the price of the products in its home country and in the US, except when the item is sold at a higher price in the US, resulting in higher anti-dumping duties. Last year, the WTO asked judges to permit sanctions of up to \$250 million within the first year.
- Japan has sent a letter of concern to the US on the recently passed 'Buy American' bill. Japan is opposing a provision in the appropriations bill for energy and water development that says funds should not be used to buy cars other than those made by the Big Three (Ford Motor Co, General Motors and Chrysler) as it violates the WTO fundamental principle of non-discrimination.