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Nuclear crisis rocks Japanese, global markets

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The worsening nuclear crisis in Japan on Tuesday triggered a crash in that nation's financial markets, major losses in markets around the globe and widening fears that last week's devastating earthquake will take a major economic toll.

While analysts are generally predicting a modest impact on the economies of the United States and Japan's other major trading partners, the risk of a significant blow to the world economy has been increasing along with the difficulties the Japanese have had in stabilizing their damaged nuclear reactors.

The economic cost to Japan itself is certain to be massive, though it's too early to gauge the exact toll. Estimates of the direct damage — the cost of rebuilding homes and factories destroyed in the earthquake and ensuing tsunami — range from \$160 billion to \$200 billion.

Early forecasts also predict that the disasters could reduce the nation's economic output by half a percentage point this year, an additional \$25 billion hit. Analysts say it could be much larger if Japan experiences prolonged power outages or if one or more of the reactors suffers a total meltdown.

Japanese stocks fell 10.5 percent Tuesday. In the three trading days since the earthquake struck, stocks are down 17.5 percent, equal to a 2,000-point drop in the Dow Jones industrial average. But the Nikkei average rebounded Wednesday, closing at 9,093.72, a gain of 5.7 percent. The Bank of Japan also pumped money into the financial markets, injecting 3.5 trillion yen, or \$43 billion, after having put in 23 trillion yen, or \$283 billion, over the past two days.

The damage has spread to markets worldwide, with the Standard & Poor's 500 closing Tuesday down 1.1 percent. The losses in U.S. markets were deeper earlier in the day, before the Federal Reserve said that it considers the U.S. economic recovery to have

achieved a “firmer footing.” Money gushed into U.S. Treasury bonds as global investors sought haven.

Essentially, global investors were beginning to price in the risk of some catastrophic possibilities.

Mark Luschini, chief investment strategist at Janney Montgomery Scott, said he believes the drop in the markets has been caused by panic selling as investors ponder the worst-case scenario: If “the radiation impacts someplace with a dense population like Tokyo” or elsewhere in the world, Luschini said, “all bets are off.” Traders, he said, are acting like “armchair nuclear physicists.”

There were some curious patterns on display in global markets that defied economic intuition, reflecting the sheer uncertainty surrounding this moment.

For example, stocks were down steeply in such Asian nations as South Korea and Taiwan, even though their manufacturers of everything from semiconductors to automobiles could benefit from reduced Japanese competition.

The value of the yen rose against the dollar, meanwhile, even though the Japanese economy has suffered a big blow and the Bank of Japan is looking to pump more money into the economy. Analysts attributed the appreciation in the yen to expectations that insurers and Japanese corporations will need to move money overseas into the country to pay for reconstruction.

And the price of oil fell to its lowest level in two weeks, \$97.18 a barrel from \$102.70 before the earthquake, even though Japan will probably need to consume more fossil fuels than before to power the nation, given that damaged nuclear plants may be out of service for years.

For the United States and the rest of the world, the risks are hard to predict. The direct economic impact on such things as trade flows is likely to be modest. Japan accounts for less than 5 percent of American exports, and U.S. exporters could even get some advantage as they ramp up output to make up for production shortfalls while Japan is recovering.

More worrisome is that the disaster in Japan could affect consumer and business confidence in the United States. For example, the European financial crisis last spring had little obvious direct impact on the U.S. economy, but it coincided with a slowdown in growth here.

The uncertainty over the extent of Japan’s nuclear disaster “may add to a sense that global events are spinning out of control,” said Nariman Behraves, chief economist at IHS Global Insight. “This can make consumers — and, perhaps, businesses, too — more fearful,” he said, and slow down purchasing and hiring.

“Such reactions to natural disasters are usually short-lived, but we cannot yet know when events in Japan will stabilize,” he said.

Luschini said it's worth recalling the effect of the Kobe earthquake in 1995. In the week after that disaster, the Nikkei fell almost 7 percent. It continued to fall as much as 25 percent before fully recovering its losses by year's end.

The major difference between that disaster and the current one is the risk of a nuclear catastrophe, which has exacerbated fears in Japan and beyond.

“There is still a great deal of uncertainty how bad the human and economic toll will be in Japan,” said **Bernard Baumohl**, chief global economist at the Economic Outlook Group. “The tragedy has certainly been horrific, but there is still no sense the nuclear crisis is over.”