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SA174 Short-Term Forecast (2018/4-6—2020/1-3)

Japan's Economy Stalled but Set for Further Growth

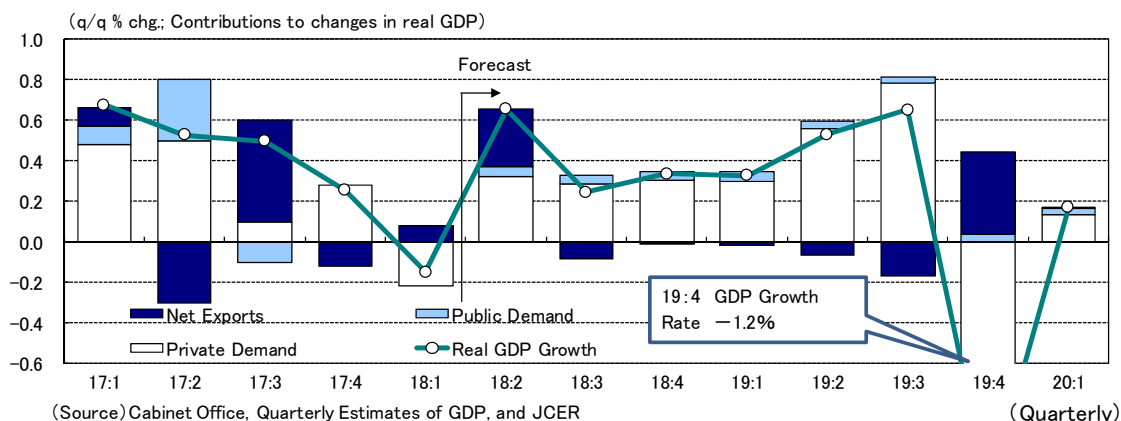
— Growth Projections Revised Downward for FY2018 but Unchanged for FY2019—

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In the January-March quarter of 2018, Japan's real growth rate declined 0.2% from the previous quarter and 0.6% on an annualized basis, contracting for the first time in nine quarters. Key factors suppressing the rate of growth to bring about this weakness were poor weather (heavy snow early in the year), changes in private-sector inventory levels, and recoil from previous high growth. There were no major changes in economic fundamentals, and the results can be regarded as a temporary leveling-off of the domestic economy in the January-March quarter. It is probable that the economy will rally in the April-June quarter and beyond.

As the global economy continues its robust recovery, Japan's economy is expected to keep expanding. The real growth rate is projected to rise 1.0% in FY2018, slightly above the potential growth rate of just under 1%. In January 2019 the current recovery trend that began in December 2012 is expected to set a new record as the longest period of economic growth in the post-war era. Although the impact of the consumption tax hike and cooling of demand associated with the Tokyo Olympics are likely to slow the rate of expansion somewhat, growth of 0.9% is still anticipated in FY2019. The corporate sector is expected to continue leading future economic growth. Unless wage rates rise sharply, it will be difficult for the household sector to drive self-sustaining economic growth. [see Figure]



The global economic growth rate was heightened in the second half of 2017, but slowed in the January-March quarter of 2018, partly due to cold snaps around the world suppressing economic activity. A brief rebound is predicted for the April-June quarter, but fundamental momentum for global economic growth is then expected to slow gradually. In the US, implementation of large-scale tax cuts is predicted to drive ongoing growth above the potential growth rate throughout the projection period (up 2.8% in 2018 and 2.5% in 2019). In the Euro zone, strong growth led by domestic demand will continue (up 2.2% in 2018 and 1.9% in 2019). However, the pace of growth in the UK economy is likely to remain sluggish (up 1.3% in 2018 and 1.5% in 2019), partly due to uncertainty surrounding Brexit. As China shifts emphasis from quantity to quality-based growth, high rates of growth are projected to continue: the government is focusing on a growth target of 6.5% in 2018, and although this pace will slow slightly in 2019, growth is still expected to be 6.2%. Newly industrializing economies (NIES) in Asia are expected to be capable of achieving future growth well above 2% (up 2.9% in 2018 and 2.5% in 2019). The ASEAN4 countries (Indonesia, Thailand, Malaysia, and the Philippines) are projected to maintain growth rates of a little under 5% until 2019.

Turning to the domestic economy, exports and production continue to increase amid ongoing growth in overseas economies. Although demand for smartphones has levelled off, overall exports will rise spurred by the increase in demand for semiconductors for data centers and in-vehicle applications as well as increasing demand for capital goods due to a recovery in overseas capital expenditure.

Although the outlook for the corporate sector is clouded by gradual deterioration in terms of trade due to a rise in crude oil price, companies are expected to maintain high levels of ordinary income. Capital expenditure is likely to continue rising throughout the projection period. The Bank of Japan's March Tankan survey predicts a strong increase in GDP-based capital expenditure plans (FY2018, all enterprise scales and all industries). This is expected to go beyond laborsaving investment and continue the trend towards forward-looking investment aimed at enhancing competitiveness, such as investment in intangible fixed assets. The peak of construction investment leading up to the Tokyo Olympics will also underpin capital expenditure. However, the rise in capital expenditure is projected to slow gradually in FY2019. As well as the leveling-off of construction demand associated with the Tokyo Olympics, the maturation phase of the capital stock cycle is expected to apply downward pressure on the pace of capital expenditure. From FY2018 onward, public-sector demand is likely to be bolstered by public works investment allocations made in the FY2017 supplementary budget and the FY2018 budget, and by infrastructure investment in a new economic policy package "productivity revolution" to be implemented through FY2020. On a GDP basis (public capital formation), however, such initiatives cannot be expected to boost growth rates to the extent seen in FY2017.

Moving on to the household sector, according to the results of a survey on the 2018 spring

labor offensive published by the Japanese Trade Union Confederation (the fifth survey in the series), average wages rose by 2.09%, the second highest rate since the second Abe administration took office, exceeded only by the 2.20% increase in 2015. There is a high possibility that the rate will increase from last year. However, it did not reach the government's 3% target for wage increases and cannot be anticipated to flow through to sustainable household-sector-led growth. Since future price hikes will suppress growth in real wages, there is a high probability that consumption will rise only moderately. Due to the impact of the consumption tax hike scheduled for October 2019, FY2019 consumption is projected to further slow below FY2018 levels.

Residential investment will remain steady for a while, due to gradual easing of downward pressure stemming from cooling of demand driven by efforts to reduce inheritance tax obligations. From the second half of FY2018 to the first half of FY2019 there will be last-minute demand in anticipation of the consumption tax hike, boosting residential investments, but is then projected to fall back in reaction to the tax hike.

Companies continue to maintain a cautious stance on raising consumer prices, and apart from certain sectors such as the transportation industry, have made limited moves to pass higher personnel expenses and purchasing costs through to selling prices. Many companies continue to absorb cost increases through laborsaving investment and greater operational efficiencies, and it is likely to take some time before consumer prices can be increased in a sustainable manner. The core consumer price index (excluding the impact of the consumption tax hike) is forecast to rise only slowly.

Regarding risks for the future, the short-term focus will be the direction of talks between the US and China on rectifying the bilateral trade imbalances. Trade friction has arisen between these two nations on two counts: additional duties imposed by the US on steel and aluminum products on the grounds of national security, and punitive customs duties on Chinese products on the grounds of intellectual property infringements. If the bilateral talks were to break down and plunge the parties into an all-out trade war, the negative impacts on Japan and the rest of the global economy could be severe.

Caution is also required over the impact of US withdrawal from the Iran nuclear agreement. If the US reimposes economic sanctions on Iran, not only will crude oil imports from Iran be halted, but the business activities of companies from many countries that operate in Iran could also be detrimentally affected. If a third country were to breach US economic sanctions, causing its financial institutions difficulty in procuring US dollars, the negative impacts on cross-border financing transactions would be immeasurable.

In international financial markets, rising US interest rates are causing investors to pull funds out of countries such as Argentina and Turkey where current account deficits are continuing and dependence on foreign short-term capital is relatively high. At present,

however, emerging economies as a whole are not expected to suffer extensive capital outflows. Nevertheless, if US interest rates were to shoot up at a pace exceeding market expectations, emerging economies in general would be thrown into disorder and we cannot deny the risk of worldwide recession.

In Japan, the focus is on the trajectory of the bill on working style reform. Introduction of a new remuneration system for advanced professionals that values workers' performance instead of hours worked is a point of contention, but it is hoped that debate on this measure will move forward, especially since the passing of the bill would herald major progress in labor market reforms.

Attention also needs to be paid to the new fiscal consolidation plan to be announced next month. The previous plan essentially aimed solely to achieve a surplus in the primary budget balance, but last year's Basic Policy added the objective of stably reducing the ratio of outstanding government debt to GDP. Media reports have also suggested that in order to secure flexibility for future fiscal stimulus, a third goal of achieving a numerical target for the fiscal balance will be added. If the fundamental goal of achieving a surplus in the primary balance is diluted, discussion of the need to increase taxes and reduce expenditure, which is the essence of fiscal consolidation, may be postponed. The need to ensure fiscal discipline and gain international trust calls for a fiscal consolidation plan that combines objectivity with prudence.

Summary Table of the 174th Quarterly Forecast

四半期／年度／暦年 Quarter / Fiscal Year / Calendar Year	単位 Unit	Forecast												年度 (FY) 2016 (実績) Actual	年度 (FY) 2017 (実績) Actual	年度 (FY) 2018 (予測) Forecast	年度 (FY) 2019 (予測) Forecast	暦年 (CY) 2016 (実績) Actual	暦年 (CY) 2017 (実績) Actual	暦年 (CY) 2018 (予測) Forecast	暦年 (CY) 2019 (予測) Forecast
		2017				2018				2019											
		4-6	7-9	10-12	1-3	4-6	7-9	10-12	1-3	4-6	7-9	10-12	1-3								
実質国内総支出 (2011暦年連鎖価格) Real GDE (Chained 2011 Yen)	前期比% ** 前年同期比% ****	0.5 1.5	0.5 1.9	0.1 1.8	-0.2 0.9	0.4 0.9	0.3 0.7	0.3 0.9	0.3 1.4	0.5 1.6	0.6 1.9	-1.2 0.3	0.2 0.1	1.2	1.5	1.0	0.9	1.0	1.7	0.9	1.3
国内需要 Domestic Demand	寄与度%ポイント ++	0.8	-0.0	0.2	-0.2	0.4	0.3	0.3	0.4	0.6	0.8	-1.6	0.2	0.4	1.1	0.9	1.0	0.4	1.1	0.7	1.3
民間最終消費支出 Private Consumption	前期比% **	0.7	-0.7	0.2	-0.0	0.4	0.3	0.3	0.4	0.8	1.2	-3.0	0.3	0.3	0.8	0.9	0.8	0.1	1.0	0.6	1.3
民間住宅投資 Private Residential Investment	前期比% **	0.9	-1.6	-2.7	-2.1	-0.3	0.2	1.1	1.7	1.7	0.8	-1.1	-2.2	6.2	-0.3	-2.6	3.1	5.7	2.7	-4.5	4.0
民間企業設備投資 Private Non-Residential Investment	前期比% **	0.8	1.0	0.6	-0.1	0.8	0.7	0.6	0.4	0.3	0.5	0.3	0.2	1.2	3.0	2.3	1.7	0.6	2.9	2.2	1.9
公的固定資本形成 Public Investment	前期比% **	4.7	-2.6	-0.4	0.0	-0.0	0.0	0.0	0.1	0.0	-0.1	-0.1	-0.1	0.9	1.5	-0.9	0.0	-0.1	1.2	-0.5	0.1
外需 Net Exports of Goods & Services	寄与度%ポイント ++	-0.3	0.5	-0.1	0.1	0.0	-0.0	-0.0	-0.0	-0.1	-0.2	0.4	-0.0	0.8	0.4	0.1	-0.0	0.6	0.6	0.2	-0.1
財貨・サービスの輸出 Exports of Goods & Services	前期比% **	-0.1	2.0	2.2	0.6	1.1	0.9	0.9	0.9	0.8	0.7	0.6	0.6	3.6	6.2	4.7	3.2	1.7	6.7	4.9	3.4
財貨・サービスの輸入 Imports of Goods & Services	前期比% **	1.8	-1.3	3.1	0.3	1.0	1.0	1.0	1.0	1.2	1.7	-1.6	0.6	-0.8	4.0	3.9	3.3	-1.6	3.4	3.8	3.8
名目国内総支出 GDE at Current Prices	前期比% ** 前年同期比% ****	0.9 1.2	0.8 2.0	0.1 1.9	-0.4 1.4	0.6 1.1	0.2 0.6	0.7 1.1	0.2 1.8	1.0 2.1	0.6 2.5	-0.4 1.4	0.0 1.2	1.0	1.6	1.2	1.8	1.2	1.4	1.1	1.9
鉱工業生産指数 Indices of Industrial Production	前期比% **	1.8	0.5	1.6	-1.3	1.1	0.7	0.6	0.6	0.5	1.2	-1.5	-0.3	1.0	4.1	2.0	1.5	-0.1	4.4	1.8	2.3
企業物価指数 Corporate Goods Price Index	前年同期比% ****	2.1	2.8	3.3	2.5	2.1	1.7	0.9	0.5	0.6	0.8	3.0	3.2	-2.4	2.7	1.3	1.9	-3.5	2.3	1.8	1.2
消費者物価指数 (生鮮食品除く) Consumer Price Index excl. Fresh Food	前年同期比% ****	0.4	0.6	0.9	0.9	0.7	1.0	0.9	1.1	1.2	1.2	2.1	2.2	-0.2	0.7	1.0	1.7	-0.3	0.5	0.9	1.4
名目雇用者報酬 Compensation of Employees	前期比% ** 前年同期比% ****	1.3 2.2	0.5 2.2	0.4 1.9	0.9 3.2	0.4 2.3	0.4 2.2	0.4 2.2	0.5 1.8	0.6 2.0	0.5 2.1	0.5 2.1	0.8 2.4	2.4	2.3	2.1	2.2	2.7	1.9	2.4	2.0
完全失業率 Unemployment Rate	% *	2.9	2.8	2.7	2.5	2.6	2.5	2.5	2.5	2.5	2.5	2.5	2.5	3.0	2.7	2.5	2.5	3.1	2.8	2.5	2.5
新発10年国債流通利回り (店頭基準気配) 10-Year Government Bond Yield	%	0.041	0.047	0.049	0.059	0.043	0.100	0.100	0.100	0.200	0.200	0.200	0.200	-0.046	0.049	0.086	0.200	-0.051	0.052	0.076	0.175
日経平均株価 Nikkei Stock Average	円 / yen	19,520	19,873	22,182	22,334	22,335	22,631	22,695	22,744	22,797	22,862	22,910	22,949	17,519	20,961	22,601	22,880	16,920	20,209	22,498	22,828
IMFベース経常収支 Current Account Balance (IMF)	千億円/100 Billion yen* 名目GDP比% *#	49.9 3.7	58.1 4.2	58.9 4.3	46.1 3.4	52.0 3.8	52.7 3.8	53.2 3.8	53.3 3.8	54.2 3.8	47.0 3.3	52.9 3.8	52.6 3.7	210.2 3.9	217.4 4.0	210.8 3.8	206.3 3.7	210.6 3.9	219.5 4.0	208.2 3.8	206.1 3.7
対ドル円レート Yen to US Dollar Exchange Rate	円/ドル yen / dollar	111.1	111.0	112.9	108.1	108.8	109.0	109.0	109.3	109.3	109.3	109.6	110.1	108.3	110.8	109.0	109.6	108.8	112.1	108.7	109.4
WTI原油価格 WTI Crude Oil Price	ドル/バレル dollar / barrel	48.2	48.2	55.3	62.9	68.2	67.2	65.7	64.6	63.5	63.5	63.5	63.5	47.9	53.6	66.4	63.5	43.5	50.9	66.0	63.8
米国実質国内総支出 U.S. Real GDP	前期比年率% ***	3.1	3.2	2.9	2.3	3.0	2.8	2.5	2.4	2.4	2.4	2.2	2.1	1.6	2.5	2.7	2.4	1.5	2.3	2.8	2.5
中国実質国内総支出 China Real GDP	前年同期比% ****	6.9	6.8	6.8	6.8	6.6	6.4	6.4	6.2	6.2	6.2	6.2	6.2	6.8	6.8	6.4	6.2	6.7	6.9	6.5	6.2

(注) 1. *季節調整値、**季節調整済み前期比
2. ***季節調整済み前期比年率換算、****前年同期比
3. # 名目GDP比
4. ++ 前期比寄与度

[Note] 1. * Seasonally adjusted, ** Seasonally adjusted changes from the previous quarter
2. *** Seasonally adjusted changes from the previous quarter in annual rate, **** Year-on-year percentage change
3. # % of nominal GDP
4. ++ Contributions to changes from the previous quarter