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SA164 Short-Term Forecast (2015/10-12—2018/1-3)

***Fiscal 2015 Forecast Remains Unchanged,
but 2016 Projections Revised Downward
- Languid Recovery Down the Road for a Yet Sluggish Economy***

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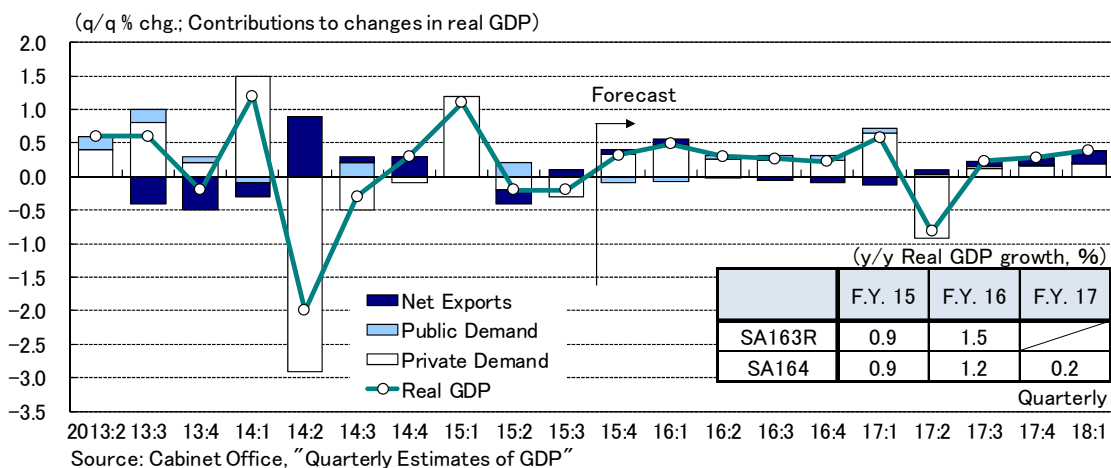
Overview

Real GDP contracted by 0.2% in July–September 2015 over the previous three months, marking the second straight quarter of negative growth. Exports of goods failed to rebound appreciably from the sharp decline of the previous quarter, but service exports registered robust growth of 7.0%. Personal consumption edged up 0.5% after contracting by 0.6% in April–June, and residential investments showed strong growth for the third consecutive quarter. Inventory investment contributed negatively, pushing down GDP by 0.5 percentage points, while capital spending fell by an additional 1.3% after contracting by 1.2% the previous quarter.

Although real GDP contracted in July–September, inventory investment accounted for 0.5 points of the decline, so economic conditions as a whole are still “sluggish,” with no need for excessive pessimism. We maintain our projection for 0.9% growth in real terms in fiscal 2015. But given the slowdown in overseas demand and the cautious attitude toward investment in the corporate sector, growth in fiscal 2016 is likely to reach only 1.2%. Demand will plummet in the wake of the April 2017 consumption tax hike to 10%, so our growth forecast for fiscal 2017 is much lower at 0.2%.

Below we outline the prospects for overseas and domestic markets.

[Figure: The Outlook for Real GDP Growth]



Trends in Overseas Markets

The US economy decelerated in July–September 2015, growing 1.5% in real terms compared to 3.9% in April–June. Inventory accounted for the bulk of the slowdown, making a 1.4-point negative contribution to the growth rate. Personal spending centered on autos and other consumer durables, on the other hand, expanded by 3.2%, so the state of the economy as a whole appears quite healthy. Residential investments, too, maintained a higher growth rate of 6.1%. These trends are being buoyed by a brighter job picture, cheaper fuel costs, and a stronger dollar. The ISM index for manufacturers has fallen to its lowest level since May 2013, though, owing to the strong dollar, while the index for nonmanufacturing companies shot up to 59.1—the second highest figure over the past decade. Given the strength of domestic demand, manufacturers should be able to prevent a further slide, and the economy can be expected to expand at a rate slightly above its potential growth rate of 2.0%–2.5%.

Real GDP in the eurozone grew by 0.3% in July–September, edging down slightly from 0.4% in April–June but nonetheless registering the tenth consecutive quarter of expansion. The pace remains tepid, however, with Germany decelerating to 0.3% from 0.4% in the previous quarter, and France creeping up to 0.3% from 0% over the same span. The euro depreciated following the quantitative easing measures taken by the ECB in March 2015, but the currency regained its strength over the summer—resulting in weaker exports, particularly to emerging markets. There is overreliance on consumption to drive growth.

China’s real GDP growth was 6.9% in July–September, edging down from 7.0% in the two previous quarters. The slowdown is probably more acute than what Beijing’s official figures suggest, though; indeed, when we applied our own calculations for China’s GDP deflator, the July–September growth rate in real terms was just 4.8%. The Fifth Plenary Session of the 18th Central Committee, held in late October, issued a new target for average annual growth of no lower than 6.5%, but we believe this will be difficult to achieve. China is now in the process of transforming the structure of its economy from one reliant on investment and heavy industry to one centered on consumption and the service sector. It remains to be seen whether China can transition smoothly to a “new normal.” As the pace of the slowdown is steeper than anticipated, Beijing is doing what it can to ease the deceleration through monetary relaxation and infrastructure improvements, but the impact of such measures will be limited, given the large debts and excess capacity at SOEs and real estate brokers. China recently announced an abolition of its one-child policy, enabling families to have a second child, but the move may have been too late, as the total fertility rate tends to decline when income levels rise.

Given the above trends in the international economy, Japanese exports are expected to maintain cruising speed, rising by 1.4% in fiscal 2015, 3.9% in fiscal 2016, and 3.7% in 2017.

[Table: The Outlook for Foreign Economies]

	(%)											
	World		United States		Euro Area		China		NIEs		ASEAN	
	SA163R	SA164	SA163R	SA164	SA163R	SA164	SA163R	SA164	SA163R	SA164	SA163R	SA164
2014		3.8		2.4		0.9		7.3		3.3		4.4
2015	3.6	3.4	2.6	2.4	1.3	1.4	6.8	6.9	2.4	2.2	4.6	4.4
2016	3.9	3.6	2.9	2.6	1.6	1.5	6.7	6.6	3.4	3.0	5.1	4.7
2017		3.0		2.5		1.6		6.2		3.3		4.9

Note: World economic growth rate is an average weighted by exports from Japan. Estimates are calendar year base.

Domestic Demand

As for the fiscal outlook, a reduced rate for certain items is likely to be introduced when the consumption tax is raised to 10% in April 2017, but we have not taken this into account in our projections because neither the items to be included nor the timing of such a lower rate have yet to be clarified. Implementing differentiated rates will require an invoicing system similar to that introduced by the EU to calculate taxes for categories of items with different tax rates. The introduction of such a system—even if not in time for the scheduled consumption tax hike—would contribute to ensuring transparency and fairness by eliminating the problem of *ekizeji*, or “profit tax,” that is, the consumption tax businesses collect but are not paid to the tax office because a transaction involves suppliers that are tax exempt or utilize a simplified tax format. Some businesses fear that an invoicing system would push up costs, but countries that have introduced the system have seen such costs more than offset through enhancements in accounting and management efficiencies.

Prospects for personal consumption appear robust, given the low rate of unemployment at 3.4% and a jobs-to-applicants ratio of 1.24 in September—the highest since 1.25 was registered 23 years and 8 months ago in 1992. But on closer inspection, we notice that the tightness of the job market varies greatly depending on industry, with the lowest-paying sectors experiencing the biggest shortages of workers. These industries tend to hire more part-timers, so there has been little growth in overall income levels despite a tighter market. In this context, we expect personal spending to rise by only 0.6% in fiscal 2015 and by 1.4% in fiscal 2016. It is likely to decline by 0.1% in fiscal 2017, as a higher consumption tax will dampen spending.

We project 3.7% growth in residential investments during fiscal 2015 and 3.8% the following year. The widely reported falsification of piling data in a number of condominium construction projects has not been taken into consideration, as the fallout from this disclosure on purchasing behavior will be hard to gauge. Revelations in 2005 that earthquake-resistance data had been fabricated resulted in the 2007 revisions to the Building Standards Act and other laws; should the piling data scandal again lead to legal amendments, a bottleneck in housing starts could emerge as construction firms make adjustments to the new requirements. Residential investments are forecast to plummet by 5.5% in fiscal 2017 following the consumption tax hike. This is because attempts have already been made to “borrow” from future demand; many people made last-minute, pre-hike purchases when the tax was raised from 5% to 8% in April 2014, and buying has subsequently been propped up with a variety of policy incentives.

The outlook for capital investment is mixed. Corporate earnings are at their highest levels in years, regardless of business scale or sector. Dividends and royalties from overseas subsidiaries are contributing to strong earnings, and cash and deposits are registering near record highs. Overseas direct investment (including M&As not involving plant and equipment purchases) continues unabated, despite the yen's devaluation since the start of Abenomics. Domestic capital spending, on the other hand, has been rather restrained, perhaps reflecting a lack of faith in medium- to long-term growth prospects.

We anticipate 0.7% growth in capital investment in fiscal 2015 and 2.8% in fiscal 2016. There is likely to be a flurry of last-minute spending before the next consumption tax hike, especially among tax-exempt and simplified-tax businesses, as well as schools, hospitals, and other organizations with high shares of tax-free sales, as consumption tax deductions cannot be claimed for purchases of new facilities and equipment. This will stifle post-hike investment, resulting in just 0.6% growth in fiscal 2017.

Consumer Prices

Japan's core CPI (excluding the impact of the consumption-tax hike) will remain flat at 0.0% during fiscal 2015 in the light of continued low oil prices. As the impact of the lower prices wears off and with the anticipated narrowing of the supply-demand gap, we maintain our view that the index will start moving upward. We forecast 0.9% core inflation for both fiscal 2016 and 2017, prompted by higher service prices in view of a growing worker shortage in the service sector.

Summary of the 164th Quarterly Forecast

四半期／年度／暦年 Quarter / Fiscal Year / Calendar Year	単位 Unit	Forecast												Forecast							
		2015				2016				2017				年度(FY) 2014 (実績) Actual	年度(FY) 2015 (予測) Forecast	年度(FY) 2016 (予測) Forecast	年度(FY) 2017 (予測) Forecast	暦年(CY) 2014 (実績) Actual	暦年(CY) 2015 (予測) Forecast	暦年(CY) 2016 (予測) Forecast	暦年(CY) 2017 (予測) Forecast
		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 (2005暦年連鎖価格) Real GDE (Chained 2005 Yen)	前期比% ** 前年同期比% ****	-0.2	-0.2	0.3	0.5	0.3	0.3	0.2	0.6	-0.8	0.2	0.3	0.4	-0.9	0.9	1.2	0.2	-0.1	0.6	1.0	0.5
国内需要 Domestic Demand	寄与度%ポイント ++	0.0	-0.3	0.2	0.4	0.3	0.3	0.3	0.7	-0.9	0.2	0.2	0.2	-1.5	0.8	1.2	0.1	-0.1	0.2	0.9	0.6
民間最終消費支出 Private Consumption	前期比% **	-0.6	0.5	0.3	0.3	0.2	0.2	0.4	1.0	-1.8	0.6	0.3	0.3	-3.1	0.6	1.4	-0.1	-1.3	-0.6	1.0	0.5
民間住宅投資 Private Residential Investment	前期比% **	2.4	1.9	0.8	0.3	1.0	1.1	2.0	-0.8	-2.2	-4.2	-1.7	0.0	-11.6	3.7	3.8	-5.5	-5.1	-2.1	4.4	-2.7
民間企業設備投資 Private Non-Residential Investment	前期比% **	-1.2	-1.3	1.5	0.9	0.6	0.8	0.4	1.1	-1.2	0.6	0.2	0.2	0.5	0.7	2.8	0.6	4.0	0.2	2.0	1.4
公的固定資本形成 Public Investment	前期比% **	2.1	-0.3	-2.7	-2.7	0.2	0.2	0.2	0.2	-0.7	-0.7	-0.7	-0.8	2.0	-0.7	-3.0	-1.4	3.8	0.4	-4.1	-0.5
外需 Net Exports of Goods & Services	寄与度%ポイント ++	-0.2	0.1	0.1	0.1	-0.0	-0.0	-0.1	-0.1	0.1	0.1	0.1	0.2	0.6	0.1	0.0	0.1	-0.0	0.4	0.1	-0.1
財貨・サービスの輸出 Exports of Goods & Services	前期比% **	-4.3	2.6	0.6	1.0	0.8	0.8	1.0	0.8	0.9	0.9	1.0	1.1	7.9	1.4	3.9	3.7	8.4	3.1	2.9	3.6
財貨・サービスの輸入 Imports of Goods & Services	前期比% **	-2.8	1.7	0.2	0.5	1.1	1.2	1.8	1.7	0.5	0.5	0.5	0.1	3.6	0.7	4.3	3.7	7.4	0.8	2.7	4.8
名目国内総支出 GDE at Current Prices	前期比% ** 前年同期比% ****	0.2	0.0	0.5	0.3	0.4	0.5	0.3	0.7	-0.2	0.2	0.2	0.4	1.6	2.4	1.6	0.9	1.6	2.8	1.4	1.3
鉱工業生産指数 Indices of Industrial Production	前期比% **	-1.4	-1.2	2.1	0.6	0.1	0.4	1.2	1.9	-1.8	0.3	0.3	0.5	-0.4	0.0	2.6	0.8	2.1	-0.2	1.6	1.6
企業物価指数 Corporate Goods Price Index	前年同期比% ****	-2.2	-3.6	-2.6	-0.9	-1.0	0.2	0.7	0.8	2.4	2.4	2.2	2.0	2.8	-2.3	0.2	2.3	3.1	-2.0	-0.2	1.9
消費者物価指数(生鮮食品除く) Consumer Price Index excl. Fresh Food	前年同期比% ****	0.1	-0.1	-0.2	0.2	0.3	0.9	1.1	1.2	2.2	2.2	2.3	2.1	2.8	0.0	0.9	2.2	2.6	0.5	0.6	2.0
名目雇者報酬 Compensation of Employees	前期比% ** 前年同期比% ****	0.3	0.9	0.0	0.2	0.6	0.3	0.7	0.1	0.0	0.3	0.6	0.4	1.7	1.3	1.5	1.1	1.5	1.3	1.5	1.2
完全失業率 Unemployment Rate	% *	3.3	3.4	3.3	3.3	3.3	3.3	3.2	3.2	3.3	3.3	3.3	3.4	3.5	3.3	3.3	3.3	3.6	3.4	3.3	3.3
新発10年国債流通利回り(店頭基準気配) 10-Year Government Bond Yield	%	0.4	0.4	0.3	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.5	0.5	0.5	0.4	0.4	0.4	0.5	0.4	0.4	0.4
日経平均株価 Nikkei Stock Average	円 / yen	20,058	19,475	19,203	19,624	19,673	19,901	20,160	20,333	20,241	20,533	20,723	20,908	16,253	19,590	20,017	20,601	15,460	19,241	19,839	20,458
IMFベース経常収支 Current Account Balance (IMF)	千億円/100 Billion yen* 名目GDP比% #	42.2	36.9	46.7	52.9	46.7	39.8	38.2	41.8	38.3	34.1	35.6	45.1	79.3	181.1	168.2	155.1	26.5	166.3	179.4	151.6
対ドル円レート Yen to US Dollar Exchange Rate	円/ドル yen / dollar	121.4	122.3	121.3	123.5	124.3	124.3	125.0	125.0	125.1	125.2	125.3	125.5	109.7	122.1	124.7	124.9	105.8	121.0	124.3	125.2
WTI原油価格 WTI Crude Oil Price	ドル/バレル dollar / barrel	58.0	46.5	47.0	49.9	51.7	52.9	53.9	54.2	54.5	54.8	55.1	55.4	80.8	50.3	53.2	54.9	92.9	50.0	52.1	54.6
米国実質国内総支出 U.S. Real GDP (2009 Dollars)	前期比年率% ***	3.9	1.5	2.8	2.7	2.7	2.7	2.6	2.5	2.5	2.5	2.5	2.5	2.7	2.4	2.6	2.5	2.4	2.4	2.6	2.5
中国実質国内総支出 China Real GDP (1990 Prices)	前年同期比% ****	7.0	6.9	6.6	6.7	6.5	6.4	6.5	6.5	6.3	6.1	5.8	5.8	7.2	6.8	6.5	6.0	7.3	6.9	6.6	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