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*SA169 Short-Term Forecast (2017/1-3—2019/1-3)*

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## ***Exports Drive a Moderate Expansion***

***— Buoyed by Worldwide Demand for IT-Related Products —***

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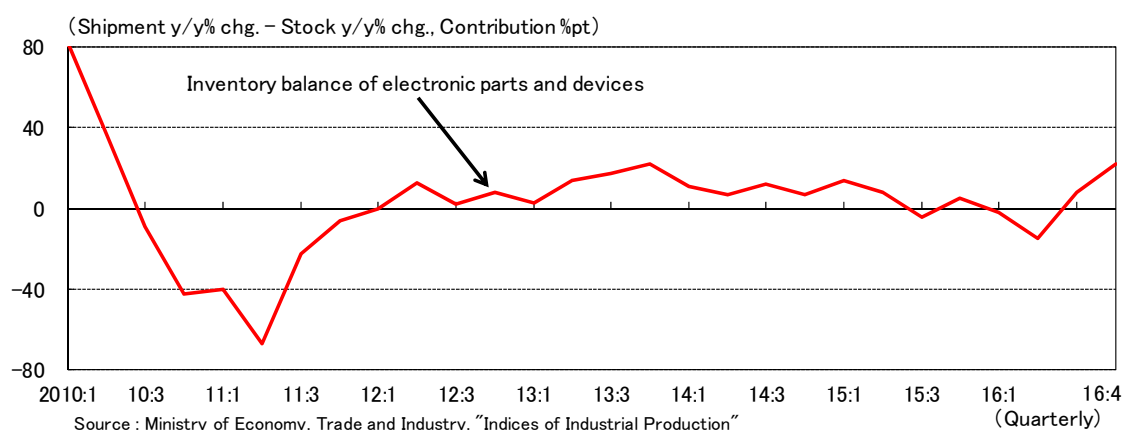
GDP in October–December 2016 grew in real terms for the fourth consecutive quarter, pointing to a moderate recovery of the Japanese economy. While growth had been languid through mid-2016, the uptrend has since firmed due to higher exports and production to meet stronger global demand for IT-related equipment.

The expansionary trend should continue, despite uncertainties in the future outlook owing to US President Donald Trump’s America First policy and the start of full-fledged Brexit negotiations. We project the Japanese economy to grow by 1.2% in real terms in fiscal 2017 thanks not only to higher exports but also continued strong commitment to quantitative easing and fiscal stimulus on a scale of ¥28 trillion. Growth in fiscal 2018 should ease to 0.8%—slightly above the economy’s potential growth rate—as the impact of the large-scale stimulus package attenuates.

Regarding international trends, our main scenario is for global growth to gradually rise with resource-rich countries and other emerging economies (with the exception of China) bouncing back from a slowdown phase as oil prices pick up. The US economy should grow by around 2.5% through 2018 thanks to tax cuts, infrastructure investment, and other expansionary policies of the new administration. The eurozone will continue to see a moderate recovery fueled by domestic demand. China, meanwhile, will enter a period of

adjustment as it attempts to shrink its growing mountain of corporate debt and excess capacity, with the growth rate decelerating to around 6% by the end of 2018.

These trends should further bolster Japan's exports, most notably of electronic parts and devices. Global demand is growing for such components, not just for smartphones but also for automotive applications as well as IoT and other industrial uses. There has been an improvement in the inventory balance since July–September 2016, and this should help boost domestic production (see figure). Projected increases in global semiconductor shipments will be a tailwind for Japanese IT-related exports.



Turning to domestic demand, business fixed investment will continue its moderate rise as money-on-hand in the corporate sector remains high. Spending will be spurred not just to boost capacity and enhance product sophistication in meeting higher foreign and domestic demand but also to upgrade or replace aging facilities and to achieve greater factory

automation in the face of a labor shortage. The Bank of Japan's *tankan* survey of business sentiment also reveals a desire, particularly among nonmanufacturers, to expand their production capacity.

The household sector, particularly the question of whether families will start spending more of their income, will hold the key to continued growth. Average jobless rate during 2016 was 3.1%, the lowest level since 1994, signaling that the economy is essentially at full employment. The figure points to a growing shortage of labor, which should push up wages. Indeed, for the past three years since 2014, workers have seen their base pay rise during spring labor negotiations—thanks partly to a government push to end deflation. Whether the trend will continue this spring still remains to be seen, but annual incomes should nonetheless continue to rise due to higher bonuses.

With nominal wages continuing their climb, the slump in personal consumption could soon be over. Sluggish sales of consumer durables following last-minute buying prior to the consumption tax hike in April 2014 are now recovering, as typified by recent upturns in sales of passenger vehicles and home appliances.

Still, the recovery in consumer spending will likely remain weak compared with improvements in employment and income. This is because rising wages are being partly offset by higher taxes and social security payments, meaning that growth of disposable income is suppressed. Families, especially younger ones, are channeling more of their income into savings due to anxieties about the future. Downward pressure on consumption is also being applied by rising shares of elderly households in the population whose members are not gainfully employed. Spending levels of such families tend to be lower than those with breadwinning members, so the rise in the share of older families will no doubt dampen overall consumption.

Another factor that could trip up a recovery is housing investment. Housing starts improved through the first half of fiscal 2016, thanks to low interest rates and as an inheritance-tax-saving strategy, but the momentum appears to have weakened in the second half. Future prospects are not very bright, moreover, given Japan's demographic trends, so housing investment is projected to decline from now on.

The conditions for retail prices to start rising already exist. The decline in crude oil prices has eased, the yen has been depreciating since the US presidential election in November 2016, and the supply-demand gap is narrowing as the economy expands. The core CPI (CPI, all items less fresh food) is projected to grow by 0.9% in fiscal 2017 and 1.0% the following year. The inflation target of 2% will likely not be reached, however, due to lingering deflationary pressures.

In spite of the brighter outlook for the real economy, there are also plenty of worrisome prospects. The most glaring of these are political risks in foreign countries, particularly the growing popular backlash against globalization. There could be negative repercussions for the global economy should Washington embrace inward-looking trade measures under its America First policy, and the process of deepening integration could hit a snag should EU skeptics score successes in elections in major European countries scheduled for 2017, further fueling uncertainties for the world economy.

To avoid the heavy damage afflicted by misguided protectionist measures in the past, governments must promote policies that deliver the benefits of globalization and technological innovation to all sectors of society. Japan needs to become a champion of free trade and take the lead in promoting the deeper integration of the global economy.

To achieve a strong and long-lasting business recovery fueled by domestic demand, Japan will need to not only carry out institutional reforms to mitigate future anxieties but implement measures to boost growth expectations.

Work-related reforms are an important part of the growth strategy; efforts should be made not only to improve the working conditions of nonregular workers and redress long working hours but also to enhance labor productivity. This will require new working procedures, changes in the workplace climate, effective use of IT, and enhancement of worker skills. Given the growing shortage of labor, we will need to seriously consider opening the domestic market further to foreign workers.

It has now become clear that bold monetary easing measures are not enough to achieve sustainable growth. Action must be taken now in order to prevent the Japanese economy from sliding back to zero growth over the medium and long-term.

# Summary Table of the 169<sup>th</sup> Quarterly Forecast

四半期／年度／暦年 Quarter / Fiscal Year / Calendar Year	単位 Unit	Forecast																			
		2016				2017				2018				年度(FY) 2015 (実績) Actual	年度(FY) 2016 (予測) Forecast	年度(FY) 2017 (予測) Forecast	年度(FY) 2018 (予測) Forecast	暦年(CY) 2015 (実績) Actual	暦年(CY) 2016 (実績) Actual	暦年(CY) 2017 (予測) Forecast	暦年(CY) 2018 (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 (2011暦年連鎖価格) Real GDE (Chained 2011 Yen)	前期比% ** 前年同期比% ****	0.4 0.9	0.3 1.1	0.2 1.7	0.3 1.3	0.3 1.2	0.4 1.2	0.2 1.2	0.1 1.0	0.2 0.9	0.2 0.7	0.3 0.8	0.3 1.0	1.3	1.2	1.2	0.8	1.2	1.0	1.2	0.9
国内需要 Domestic Demand	寄与度%ポイント ++	0.5	-0.1	-0.0	0.3	0.4	0.4	0.3	0.1	0.1	0.2	0.2	0.2	1.1	0.6	1.1	0.8	0.7	0.5	1.0	0.9
民間最終消費支出 Private Consumption	前期比% **	0.2	0.3	-0.0	0.3	0.3	0.3	0.3	0.3	0.3	0.2	0.2	0.2	0.5	0.6	1.0	1.0	-0.4	0.4	0.9	1.1
民間住宅投資 Private Residential Investment	前期比% **	3.3	2.4	0.2	-1.2	-1.5	-1.0	-0.6	-0.6	-0.2	-0.2	0.6	1.9	2.7	5.9	-3.0	-0.6	-1.6	5.6	-1.0	-2.1
民間企業設備投資 Private Non-Residential Investment	前期比% **	1.3	-0.3	0.9	0.4	0.5	0.5	0.4	0.4	0.4	0.4	0.4	0.3	0.6	1.8	1.9	1.6	1.2	1.0	2.0	1.7
公的固定資本形成 Public Investment	前期比% **	1.1	-0.7	-1.8	1.1	3.3	3.5	0.9	-2.8	-2.1	-1.3	-0.8	-0.7	-2.0	-1.9	5.5	-4.4	-2.2	-2.7	4.2	-2.1
外需 Net Exports of Goods & Services	寄与度%ポイント ++	-0.0	0.4	0.2	0.0	-0.0	-0.1	-0.1	-0.0	0.0	0.0	0.0	0.0	0.2	0.6	0.1	0.0	0.5	0.5	0.3	-0.1
財貨・サービスの輸出 Exports of Goods & Services	前期比% **	-1.2	2.1	2.6	0.4	0.3	0.3	0.4	0.4	0.5	0.6	0.6	0.6	0.8	2.6	2.9	2.1	3.0	1.2	3.6	1.8
財貨・サービスの輸入 Imports of Goods & Services	前期比% **	-1.0	-0.2	1.3	0.3	0.5	0.6	0.7	0.5	0.4	0.4	0.4	0.4	-0.2	-1.1	2.3	1.9	0.1	-1.7	1.8	2.0
名目国内総支出 GDE at Current Prices	前期比% ** 前年同期比% ****	0.3 1.3	0.2 1.0	0.3 1.6	0.3 1.1	0.4 1.2	0.4 1.5	0.4 1.5	0.2 1.4	0.3 1.2	0.3 1.1	0.4 1.1	0.3 1.3	2.8	1.2	1.4	1.2	3.3	1.3	1.3	1.2
鉱工業生産指数 Indices of Industrial Production	前期比% **	0.2	1.3	2.0	0.8	0.2	0.2	0.3	0.2	0.3	0.3	0.3	0.3	-1.0	1.5	2.5	1.0	-1.2	-0.2	3.4	0.9
企業物価指数 Corporate Goods Price Index	前年同期比% ****	-4.5	-3.8	-2.1	0.5	1.4	1.8	1.6	0.7	0.5	0.4	0.3	0.2	-3.3	-2.5	1.3	0.3	-2.3	-3.5	1.3	0.4
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	-0.5	-0.3	0.1	0.7	0.9	1.1	1.1	1.1	1.0	0.9	0.9	0.0	-0.3	0.9	1.0	0.5	-0.3	0.7	1.0
名目雇用者報酬 Compensation of Employees	前期比% ** 前年同期比% ****	0.2 2.2	0.6 2.3	0.5 2.0	0.4 1.7	0.3 1.8	0.3 1.5	0.3 1.3	0.4 1.3	0.4 1.4	0.4 1.5	0.4 1.5	0.4 1.6	1.5	2.1	1.5	1.5	1.3	2.3	1.6	1.4
完全失業率 Unemployment Rate	% *	3.2	3.0	3.1	3.1	3.1	3.1	3.0	3.0	3.0	3.0	2.9	2.9	3.3	3.1	3.0	2.9	3.4	3.1	3.1	3.0
新発10年国債流通利回り(店頭基準気配) 10-Year Government Bond Yield	%	-0.121	-0.128	-0.005	0.050	0.050	0.050	0.050	0.050	0.050	0.050	0.050	0.050	0.288	-0.051	0.050	0.050	0.360	-0.051	0.050	0.050
日経平均株価 Nikkei Stock Average	円 / yen	16,394	16,500	17,952	18,902	18,876	18,907	18,935	18,965	18,984	19,007	19,022	19,033	18,855	17,437	18,921	19,011	19,204	16,920	18,905	18,994
IMFベース経常収支 Current Account Balance (IMF)	千億円/100 Billion yen* 名目GDP比% #	46.4 3.5	49.8 3.7	54.0 4.0	51.4 3.8	51.7 3.8	50.5 3.7	49.1 3.6	48.5 3.5	48.3 3.5	47.8 3.5	47.8 3.5	47.7 3.4	180.0 3.4	207.1 3.8	198.6 3.6	189.7 3.4	164.1 3.1	206.5 3.8	203.5 3.7	190.2 3.5
対ドル円レート Yen to US Dollar Exchange Rate	円/ドル yen / dollar	108.0	102.4	109.5	114.1	113.0	113.0	113.0	113.0	113.0	113.0	113.0	113.0	120.1	108.5	113.0	113.0	121.1	108.8	113.3	113.0
WTI原油価格 WTI Crude Oil Price	ドル/バレル dollar / barrel	45.6	44.9	49.3	52.4	53.5	54.6	55.6	56.2	56.6	56.8	57.0	57.2	45.1	48.1	55.0	56.9	48.8	43.5	54.0	56.6
米国実質国内総支出 U.S. Real GDP	前期比年率% ***	1.4	3.5	1.9	2.3	2.3	2.3	2.4	2.5	2.6	2.6	2.6	2.6	2.2	1.8	2.4	2.6	2.6	1.6	2.4	2.5
中国実質国内総支出 China Real GDP	前年同期比% ****	6.7	6.7	6.8	6.6	6.4	6.3	6.2	6.1	6.0	6.0	5.9	5.9	6.9	6.7	6.2	6.0	6.9	6.7	6.3	6.0

(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