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SA172 Short-Term Forecast (2017/10-12—2020/1-3)

Expansion Will Continue, but at a Progressively Slower Pace

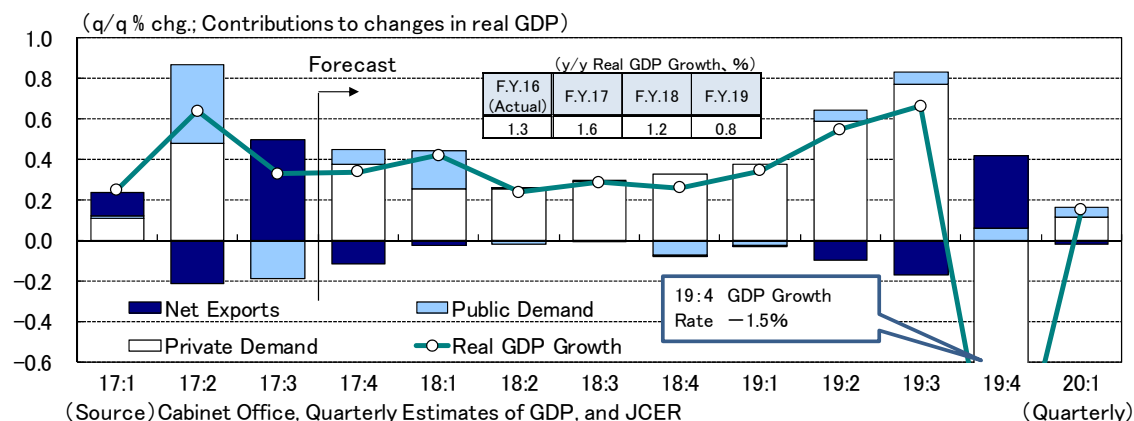
— Projections Revised Slightly Upward until Next Year; Fiscal 2019 Will Ease to 0.8%—

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July–September 2017 marked the seventh consecutive quarter of growth, with GDP edging up 0.3% in real terms, or an annual rate of 1.4%. While personal consumption and other domestic factors weakened, exports registered robust growth in the face of the continuing global upswing. There does not appear to be any change in the expansionary trend. The current recovery phase has been sustained since December 2012 and has overtaken the high-growth Izanagi boom to become the second longest period of growth in the postwar era.

We see the trend continuing for the foreseeable future, with real growth reaching 1.6% in fiscal 2017, buoyed by strong growth in global markets and a highly expansionary monetary policy at home. Our growth projection for fiscal 2018 is 1.2%—higher than the potential growth rate—in the light of sustained export growth, greater Olympics-related demand, and an upturn in investment for automation equipment in response to worker shortages. Growth should ease to 0.8% in fiscal 2019, though, as Olympics spending will have peaked, capital expenditures will enter an adjustment phase in the face of excess stock, and the scheduled October 2019 consumption tax hike will dampen spending [see figure].



Many economies around the world are experiencing their strongest recovery since the

Global Financial Crisis. There was steady growth in the United States in July–September, despite the disruption caused by devastating hurricanes and other natural disasters. With the Fed very cautiously normalizing its expansive monetary policy, the US economy should maintain 2.0%–2.5% growth before gradually settling to its potential growth rate of just below 2% in 2019. Domestic-demand-led growth is likely to continue in the eurozone, while growth of the UK economy is likely to remain weak due to continuing uncertainty over Brexit. We project slower growth in China, although the rate will nonetheless stay above 6%. The NIES, collectively, are likely to grow by 3.1% in 2017, 2.8% in 2018, and 2.6% in 2019. The four leading ASEAN economies of Indonesia, Malaysia, the Philippines, and Thailand are expected to maintain around 5% growth through 2019.

Steady growth in overseas markets suggests that exports will also continue to grow. Recent improvements in the IT cycle are mainly the result of expanding smartphone demand, which should persist through the first half of 2018. Even after the smartphone market becomes saturated, IoT-related demand for semiconductors should steadily increase, bolstering exports by Japanese manufacturers.

As for domestic demand, major companies, in particular, are going ahead with their capital expenditure plans for fiscal 2017. This should prevail in fiscal 2018 as well, with companies stepping up their factory automation investment and with redevelopment projects reaching a peak in anticipation of the 2020 Tokyo Olympic Games. Companies are also spending to upgrade or replace existing facilities and are moving aggressively to develop software and strengthen R&D to boost their competitiveness and productivity. By fiscal 2019, though, Olympics-related demand will have peaked, and companies will begin to review their capital expenditure plans in the light of the capital accumulated over the course of the long recovery phase. With regard to government spending, public capital formation during fiscal 2017 is projected to grow by 2.1%, as the impact of the sizable fiscal 2016 supplementary budget to stimulate economic activity tapers off. Infrastructure improvements will henceforth pick up in anticipation of the Tokyo Games, but projects could lag behind schedule due to a shortage of skilled construction workers. Public spending should contract in fiscal 2018, as the effect of the stimulus package adopted two years earlier will have dissipated, and it will likely decline further the following year, by which time Olympics-related demand will have peaked.

Looking broadly at employment and income trends, wages for part-timers and other nonregular workers are expected to climb further in the light of growing demand, but similar pay hikes for full-timers could remain elusive. Japanese Trade Union Confederation has outlined a policy of seeking a 2% raise in base wages (or 4% when annual pay hikes are included) during the 2018 spring labor offensive, and Prime Minister Shinzo Abe has taken the unusual step of encouraging management to offer at least 3% (including the annual raise). There is no denying that companies are coming under greater political and social pressure to boost wages for their employees. Given the economy's dubious future prospects,

a slackening of the anticipated growth rate, and structural factors like the high pace of technological innovation, management remains reluctant to offer higher pay for regular workers, since this would drive up fixed costs. Wages of regular employees are thus projected to rise only marginally, and the trickling down of the fruits of economic growth to the household sector will be minimal.

Under the circumstances, personal consumption should continue rising modestly at a pace just slightly higher than increases in compensation of employees. We do not see the household sector becoming the primary driver of growth, since (1) working families will still be prompted to put their earnings into savings due to future anxieties; (2) the shares of older, unemployed households will rise as baby-boomers (born between 1947 and 1949) enter their seventies, thereby dampening consumption in macroeconomic terms; and (3) an aging population will mean a bigger social security burden for all. The consumption tax hike scheduled for October 2019 will trigger last-minute buying in the first half of fiscal 2019, but spending will shrink in the second half. That said, in the absence of external shocks—like a dramatic downturn in global markets—the negative repercussions of a higher rate should be limited this time for three reasons. First, the decision to raise the rate to 10% had already been announced when the tax was previously hiked in April 2014, so people may already have made their last-minute purchases at that time. Second, the margin of next year's hike, from 8% to 10%, is smaller than in 2014, when the tax rate was raised from 5% to 8%. In addition, reduced rates will apply to certain items, such as foodstuffs and newspapers. And third, the household sector may now be more resilient to a tax increase, given the ongoing improvements in wage levels.

Housing investment will remain weak through the first half of fiscal 2018 as the number of households declines. A burst of last-minute purchases is anticipated between the second half of fiscal 2018 and the first half of fiscal 2019, after which investments will wane. As with personal consumption, though, we project the negative consequences of the upcoming tax hike to be smaller than in 2014.

Rising costs are applying significant upward pressure on prices in the face of a tighter demand-supply gap, but given the inelasticity of prices, a sustainable increase in the core CPI will require more time. Our projections are for this index (excluding the effect of a consumption tax hike) to rise by 0.7% in fiscal 2017, 0.9% in fiscal 2018, and 1.2% in fiscal 2019. The BOJ's 2% target will thus remain elusive over the next few years.

External developments present a number of major risks, including North Korea's nuclear weapons program. Should a military conflict or a US-China trade war break out, the Asia-Pacific supply chain would become seriously disrupted, leading to adverse consequences for the global economy. Continued vigilance is also required for the problems surrounding China's excess corporate debt.

Japan's mounting public debt, too, presents a formidable risk, and we need to keep an eye on how the Abe administration pursues the goal of fiscal consolidation. The prime minister may be retreating from his earlier commitments, as evidenced by the September 2017 decision to push back the target date for achieving a primary surplus. Restoring fiscal health requires more than simply relying on higher growth to boost revenues. Efforts are needed to streamline expenditures and secure stable, permanent revenue sources in order to retain the confidence of the market. With the economy in an expansionary phase, now is the time to build the mechanisms for self-sustained growth by reinforcing the current growth trend and alleviating future uncertainties.

Summary Table of the 172th Quarterly Forecast

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Forecast

| 四半期／年度／暦年 Quarter / Fiscal Year / Calendar Year | 単位 Unit | 2017 | | | | 2018 | | | | 2019 | | | | 年度(FY) 2016 (実績) Actual | 年度(FY) 2017 (予測) Forecast | 年度(FY) 2018 (予測) Forecast | 年度(FY) 2019 (予測) Forecast | 暦年(OY) 2016 (実績) Actual | 暦年(OY) 2017 (予測) Forecast | 暦年(OY) 2018 (予測) Forecast | 暦年(OY) 2019 (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% **** | 0.6 1.4 | 0.3 1.7 | 0.3 1.6 | 0.4 1.8 | 0.2 1.3 | 0.3 1.3 | 0.3 1.2 | 0.3 1.1 | 0.5 1.4 | 0.7 1.8 | -1.5 0.1 | 0.2 -0.1 | 1.3 | 1.6 | 1.2 | 0.8 | 1.0 | 1.5 | 1.4 | 1.1 |
| 国内需要 Domestic Demand | 寄与度%ポイント ++ | 0.9 | -0.2 | 0.5 | 0.4 | 0.2 | 0.3 | 0.3 | 0.4 | 0.6 | 0.8 | -1.8 | 0.2 | 0.5 | 1.3 | 1.2 | 0.9 | 0.4 | 1.0 | 1.3 | 1.2 |
| 民間最終消費支出 Private Consumption | 前期比% ** | 0.7 | -0.5 | 0.4 | 0.3 | 0.3 | 0.3 | 0.3 | 0.3 | 0.8 | 1.2 | -3.0 | 0.3 | 0.7 | 1.1 | 1.1 | 0.8 | 0.4 | 1.1 | 1.0 | 1.3 |
| 民間住宅投資 Private Residential Investment | 前期比% ** | 1.1 | -0.9 | -0.9 | -1.1 | -0.1 | 0.3 | 1.8 | 3.6 | 2.5 | 1.2 | -6.7 | -3.0 | 6.6 | 1.2 | 0.4 | 2.9 | 5.6 | 3.5 | -1.4 | 6.0 |
| 民間企業設備投資 Private Non-Residential Investment | 前期比% ** | 0.5 | 0.2 | 1.1 | 1.0 | 0.6 | 0.6 | 0.6 | 0.5 | 0.3 | 0.3 | 0.2 | 0.2 | 2.5 | 2.8 | 2.8 | 1.6 | 1.3 | 3.0 | 3.0 | 1.9 |
| 公的固定資本形成 Public Investment | 前期比% ** | 5.8 | -2.5 | -0.7 | 0.5 | -0.5 | -0.9 | -2.0 | -1.0 | 0.0 | 0.0 | 0.0 | 0.0 | -3.2 | 2.1 | -3.1 | -1.9 | -3.0 | 0.5 | -1.3 | -3.0 |
| 外需 Net Exports of Goods & Services | 寄与度%ポイント ++ | -0.2 | 0.5 | -0.1 | -0.0 | 0.0 | 0.0 | -0.0 | -0.0 | -0.1 | -0.2 | 0.4 | -0.0 | 0.8 | 0.3 | 0.1 | -0.1 | 0.6 | 0.5 | 0.1 | -0.1 |
| 財貨・サービスの輸出 Exports of Goods & Services | 前期比% ** | -0.2 | 1.5 | 0.6 | 0.7 | 0.9 | 0.9 | 0.8 | 0.8 | 0.7 | 0.7 | 0.6 | 0.6 | 3.2 | 4.9 | 3.4 | 2.9 | 1.2 | 5.9 | 3.2 | 3.1 |
| 財貨・サービスの輸入 Imports of Goods & Services | 前期比% ** | 1.4 | -1.6 | 1.2 | 0.8 | 0.9 | 0.9 | 0.8 | 0.8 | 1.2 | 1.6 | -1.5 | 0.6 | -1.3 | 2.7 | 3.1 | 3.2 | -2.3 | 2.6 | 2.7 | 3.5 |
| 名目国内総支出 GDE at Current Prices | 前期比% ** 前年同期比% **** | 0.6 1.0 | 0.6 1.7 | 0.3 1.5 | 0.9 2.4 | 0.2 2.0 | 0.3 1.7 | 0.5 1.9 | 0.7 1.8 | 0.5 2.1 | 0.8 2.6 | -0.0 2.0 | 0.4 1.7 | 1.1 | 1.7 | 1.8 | 2.1 | 1.3 | 1.2 | 2.0 | 2.1 |
| 鉱工業生産指数 Indices of Industrial Production | 前期比% ** | 2.1 | 0.4 | 0.5 | 0.6 | 0.6 | 0.6 | 0.6 | 0.6 | 0.5 | 0.4 | 0.3 | 0.3 | 1.1 | 4.3 | 2.2 | 1.9 | -0.1 | 4.4 | 2.6 | 2.1 |
| 企業物価指数 Corporate Goods Price Index | 前年同期比% **** | 2.1 | 2.9 | 2.6 | 1.2 | 0.7 | 0.5 | 0.7 | 0.6 | 0.6 | 0.7 | 2.8 | 3.1 | -2.3 | 2.2 | 0.7 | 1.8 | -3.5 | 2.1 | 0.8 | 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 | 0.9 | 0.9 | 0.9 | 0.9 | 1.0 | 1.1 | 2.3 | 2.4 | -0.2 | 0.7 | 0.9 | 1.7 | -0.3 | 0.5 | 0.9 | 1.3 |
| 名目雇用者報酬 Compensation of Employees | 前期比% ** 前年同期比% **** | 0.9 2.1 | 0.6 2.1 | -0.2 1.5 | 0.3 1.6 | 1.1 1.7 | 0.8 1.9 | -0.3 1.9 | 0.3 1.9 | 1.0 1.8 | 1.0 2.0 | -0.5 1.8 | 0.4 2.0 | 2.0 | 1.8 | 1.9 | 1.9 | 2.3 | 1.7 | 1.8 | 1.9 |
| 完全失業率 Unemployment Rate | % * | 2.9 | 2.8 | 2.8 | 2.8 | 2.7 | 2.7 | 2.7 | 2.7 | 2.6 | 2.6 | 2.6 | 2.6 | 3.0 | 2.8 | 2.7 | 2.6 | 3.1 | 2.8 | 2.7 | 2.6 |
| 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 | 0.050 | 0.050 | 0.100 | 0.100 | 0.100 | 0.100 | 0.200 | 0.200 | 0.200 | 0.200 | -0.046 | 0.047 | 0.100 | 0.200 | -0.051 | 0.053 | 0.088 | 0.175 |
| 日経平均株価 Nikkei Stock Average | 円 / yen | 19,520 | 19,873 | 21,474 | 21,566 | 21,638 | 21,717 | 21,795 | 21,875 | 21,933 | 22,030 | 22,115 | 22,196 | 17,519 | 20,608 | 21,756 | 22,069 | 16,920 | 20,028 | 21,679 | 21,988 |
| IMFベース経常収支 Current Account Balance (IMF) | 千億円/100 Billion yen* 名目GDP比% # | 47.7 3.5 | 61.3 4.5 | 50.3 3.7 | 50.8 3.7 | 53.2 3.8 | 53.1 3.8 | 53.1 3.8 | 53.1 3.8 | 53.0 3.8 | 49.0 3.4 | 54.0 3.8 | 53.8 3.8 | 203.8 3.8 | 209.9 3.8 | 211.8 3.8 | 209.6 3.7 | 203.4 3.8 | 210.7 3.9 | 211.6 3.8 | 207.7 3.7 |
| 対ドル円レート Yen to US Dollar Exchange Rate | 円／ドル yen / dollar | 111.1 | 111.0 | 114.1 | 114.2 | 114.5 | 114.8 | 115.0 | 115.2 | 115.5 | 115.6 | 115.7 | 115.9 | 108.3 | 112.6 | 114.9 | 115.7 | 108.8 | 112.4 | 114.6 | 115.5 |
| WTI原油価格 WTI Crude Oil Price | ドル／バレル dollar / barrel | 48.2 | 48.2 | 53.0 | 53.2 | 53.4 | 53.6 | 53.8 | 54.0 | 54.2 | 54.4 | 54.6 | 54.8 | 47.9 | 50.7 | 53.7 | 54.5 | 43.5 | 50.3 | 53.5 | 54.3 |
| 米国実質国内総支出 U.S. Real GDP | 前期比年率% *** | 3.1 | 3.0 | 2.7 | 2.1 | 2.3 | 2.1 | 2.0 | 2.0 | 2.0 | 2.0 | 1.9 | 1.9 | 1.6 | 2.4 | 2.3 | 2.0 | 1.5 | 2.2 | 2.4 | 2.0 |
| 中国実質国内総支出 China Real GDP | 前年同期比% **** | 6.9 | 6.8 | 6.8 | 6.7 | 6.5 | 6.4 | 6.2 | 6.2 | 6.2 | 6.2 | 6.2 | 6.2 | 6.8 | 6.8 | 6.3 | 6.2 | 6.7 | 6.9 | 6.4 | 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

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