



## **Forecast of GDP Statistics for April-June Quarter 2001**

**August 23, 2001**

**The Japan Research Institute, Limited**

**Economic Research Center**

**Economics Department**

### **1. Annualized Negative Growth of 3.7% in the April-June Quarter**

Real economic growth in the April-June quarter is thought to have been  $-0.9\%$  on the previous quarter (equivalent to annualized rate of  $-3.7\%$ ), indicating a strengthening of the mood of economic adjustment. Although public investment just managed to maintain positive growth thanks to the continuing effect of economic stimulus measures, the rapid fall in exports continued, and demand from the household sector, owing in part to temporary factors, also fell sharply. Against this background, the business sector showed increasing caution with regard to capital investment.

#### **Movement of major demand factors**

**1) Consumer spending** (Real:  $-0.7\%$  on previous quarter; annualized rate  $-2.7\%$ )

Consumer spending returned to negative growth for the first time in two quarters. In addition to the increasing severity of employment and income conditions, a reaction to the demand rush ahead of the implementation of the Home Appliance Recycling Law has become distinct.

*Note:* Real spending on the 4 items subject to this Law (refrigerators, washing machines, air conditioners, television sets) among households of 2 persons or more fell by 47.5% on the January-March quarter. Contribution to real consumer spending and growth on previous quarter estimated at around  $-0.3\%$  points.

**2) Housing investment** (Real:  $-7.3\%$  on previous quarter; annualized rate  $-26.1\%$ )

Housing investment took a sharp fall for a second quarter. The main reason appears to be that the demand rush ahead of the initial limit on measures to expand tax cuts on housing loans (dwelling to be occupied by end of June 2001) has faded out, especially with regard to the purchase of owner-occupied housing financed by the Housing Loan Corporation.

**3) Capital investment** (Real:  $-2.2\%$  on previous quarter; annualized rate  $-8.6\%$ )

Capital investment saw negative growth for a second quarter. The downward trend became clearer especially in the manufacturing sector, centering on the IT-supply industries, where profit deterioration has been significant. However, investment in IT on the user side is still robust.

**4) Public investment** (Real:  $+0.4\%$  on previous quarter; annualized rate  $+1.4\%$ )

The effect of additional spending on public works under the fiscal 2000 supplementary budget continued, and public investment just about maintained positive growth to the mid-year (growth for two consecutive quarters). However, the decline in the volume of public works funded independently by local government continues, and from the July-September quarter, when the effect of the supplementary budget fades, public investment is likely to fall once more.

**5) Exports** (Real: -3.5% on previous quarter; annualized rate -13.3%)

Exports saw another sharp fall, following on from that registered in the January-March quarter (Real: -3.6% on previous quarter). The effect of the deceleration of overseas economies was particularly apparent in the IT sector.

**6) Imports** (Real: -2.3% on previous quarter; annualized rate -8.9%)

Imports fell for a second quarter. A fall in imports of production goods in conjunction with the decline in domestic production activities and a fall in imports of personal computers in conjunction with the slowing of the growth of domestic demand, especially from the household sector, were the main factors.

## **2. Negative Growth Highly Likely for Fiscal 2001 Overall**

If, as forecast, the real economic growth rate in the April-June quarter is -0.9% on previous quarter, Japan will have to maintain a growth rate of +0.5% on the previous quarter from the July-September quarter onwards in order to avoid negative growth for the full fiscal year 2001.

However, the following three factors suggest that this rate of growth will be difficult to achieve, and that, if anything, the mood of economic adjustment is likely to strengthen:

(i) Given that worldwide demand for IT continues to weaken, and that business profits continue to fall, it is likely that capital investment will continue to fall, especially in the semiconductor industry, and that, the decline in consumer spending will be prolonged owing to the deterioration in income and employment conditions.

(ii) Public investment has fallen sharply since the beginning of the summer, especially in terms of public works independently financed by local governments.

(iii) The influx of cheap manufactured goods of greatly improved quality from Asia is exerting a strong downward pressure on domestic production activities.

Nevertheless, it should be possible for Japan to avoid falling prey to a deflation spiral.

(i) Investment in IT on the user side, including investment in software, remains firm.

(ii) Thanks to the establishment of a financial safety net Japan is unlikely to suffer another financial system crisis of the kind seen at the end of 1997.

(iii) If a supplementary budget for fiscal 2001 that does not conflict with the pursuit of structural reform is adopted, this is likely to have a beneficial effect on share prices and business and consumer confidence.

*Note:* The JRI forecast of economic growth for fiscal 2001 as a whole is due to be published in mid-September, after the publication of the GDP statistics.