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Short-Term Economic Survey ("Tankan")
(June Survey)**

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**Economics Research Center
Economics Department
The Japan Research Institute, Limited
<http://www.jri.co.jp/>**

For more information on the content of this report, please contact
Hideki Matsumura, Economics Department
Tel: 03-3288-4524 E-Mail: matsumura.hideki@jri.co.jp

**A Forecast of the Bank of Japan's
Short-Term Economic Survey ("Tankan") (June Survey)**

The latest edition of the Bank of Japan's *Short-Term Economic Survey ("Tankan")*, based on the June survey, which is due to be published on July 1, is likely to reveal that, although the business sector is still cautious in its outlook, business activity remains at a high level, reflecting improved profitability and the fact that a further slump in the macro economy has been avoided.

The business sentiment diffusion index for June is likely to be -27% points on an all industries/all sizes of company basis, 1% point down on the level recorded at

the end of March. In the manufacturing sector, despite the negative factor of a slowdown in export growth, business confidence is likely to remain at a similar a level to that recorded in the March survey, against a background of recovering profitability and steady exports and machinery orders. In the non-manufacturing sector, business confidence is likely to register a continued fall in view of the continued stagnation of domestic demand. This pattern of steady confidence in the manufacturing sector and diminishing confidence in non-manufacturing sector is highly likely to persist over the three months to September.

On an all industries/all sizes of company basis, the *Tankan's* forecast of the amount of capital investment in fiscal 2003 is likely to be down 2.1% points on the level recorded in fiscal 2002, representing a slight upward adjustment of investment plans as compared with the end of March. Although significant improvements in business profitability, among other factors, have led to the first rise in capital investment in three years in the manufacturing sector, the slow improvement of profitability in the non-manufacturing sector means that capital investment is likely to continue to fall year-on-year, especially among small businesses.

Thus, although the performance of the business sector remains unexpectedly firm, any worsening of negative factors such as faster deceleration of the US and European economies or a prolongation of the SARS crisis could, once more, force the economy into recession. To avoid recession, the government must not only ensure economic neutrality in its operation of macroeconomic policy, but also shift the emphasis of its structural reforms from dealing with the negative legacy of the past to fostering new industries, through measures such as drawing up an industrial development program comprising tax reductions, deregulation and the creation of next-generation social capital as an integrated package.