

Monthly Report of Prospects for Japan's Economy

April 2020

Macro Economic Research Center
Economics Department



The Japan Research Institute, Limited

<https://www.jri.co.jp/english/periodical/>

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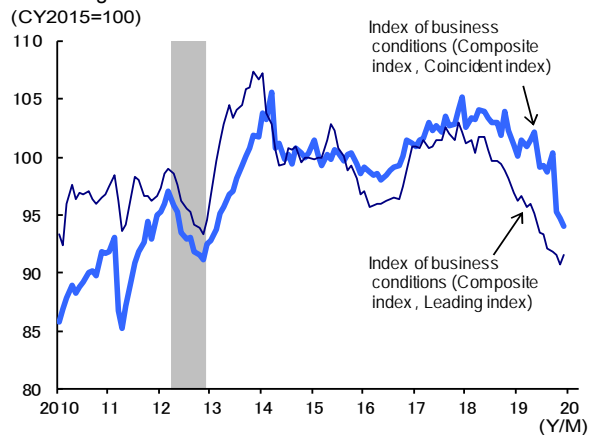
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The General Situation of Japan's Economy – Economic Activity Has Declined

Figure 1-1 Economic Activity

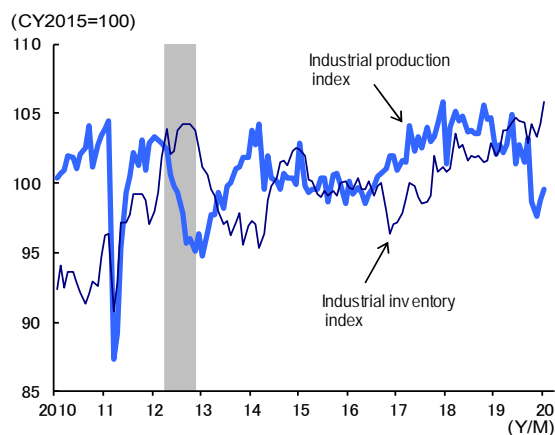
Indices of business conditions remained on a declining trend both in terms of the CI coincident index and the CI leading index.



Source: The Cabinet Office.

Figure 1-2 The Corporate Sector

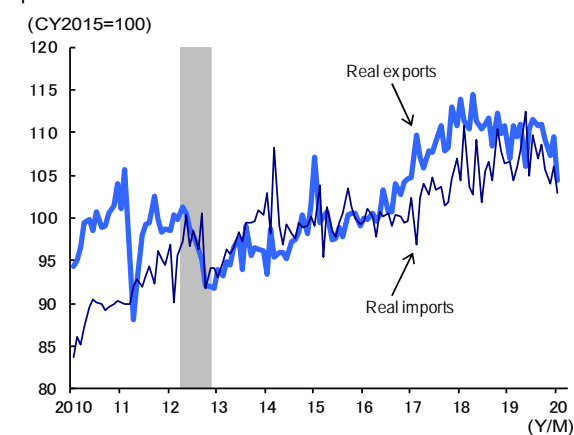
Industrial production index rose for the second consecutive month, as a result of the recovery in production following natural disasters.



Source: The Ministry of Economy, Trade and Industry.

Figure 1-3 Overseas Demand

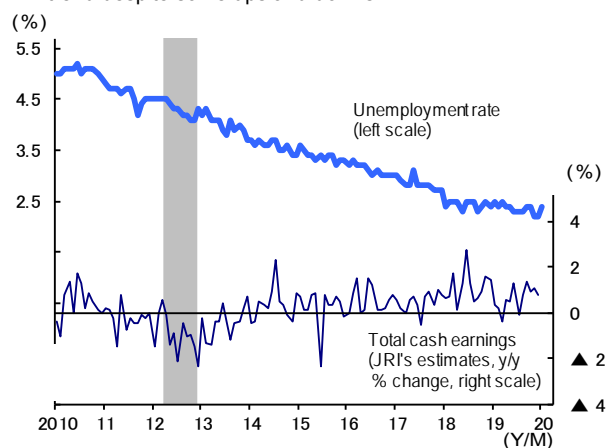
Exports, mainly those of automobiles to the United States, remained sluggish. Imports decreased, particularly of mobile phones.



Source: The Bank of Japan.

Figure 1-4 Employment and Income

The unemployment rate is hovering around its lowest level since 1993. Nominal wages have been on a rising trend despite some ups and downs.

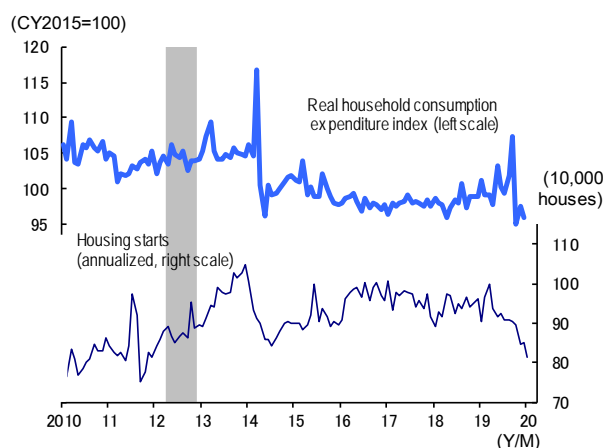


Source: The Ministry of Internal Affairs and Communications, The Ministry of Health, Labor and Welfare.

* The shaded area indicates the recession phase.

Figure 1-5 The Household Sector

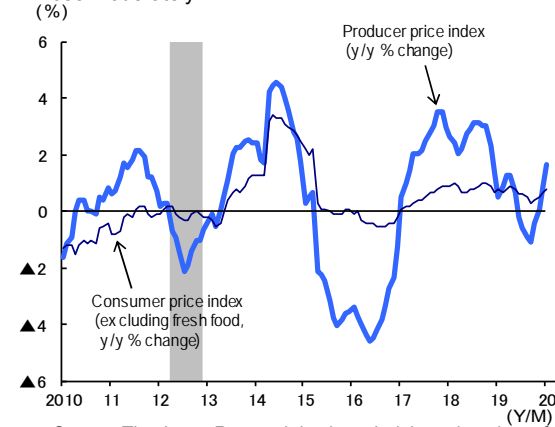
Real household consumption declined after the consumption tax rate hike. Housing starts have been sluggish.



Source: The Japan Research Institute, Ltd. based on data of The Cabinet Office, The Ministry of Land, Infrastructure and Transport.

Figure 1-6 Prices

Producer prices picked up, mainly for petroleum products. The pace of increase in consumer prices rose moderately.



Source: The Japan Research Institute, Ltd. based on data of The Ministry of Internal Affairs and Communications, The Bank of Japan.

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There Has Been Increased Downward Pressure on Both Domestic and Overseas Demand

◆ Real GDP Significantly Declined in the October to December Period

Based on the Second Preliminary Quarterly Estimates of the GDP, Japan's real GDP for the October to December 2019 period declined 7.1% on an annualized quarter-on-quarter change basis, showing significant negative growth for the first time since the previous consumption tax rate hike (when real GDP declined 7.4% on an annualized quarter-on-quarter change basis for the April to June 2014 period).

Looking at domestic demand, private consumption fell 10.6% on an annualized quarter-on-quarter change basis, due to a combination of negative factors such as large typhoons and a warm winter in addition to the effects of the consumption tax rate hike. Capital investment also fell 17.3%, owing to plant shutdowns caused by the typhoon. In overseas demand, exports, mainly to the United States, fell for the second straight quarter.

◆ Industrial Production Saw an Increase

The industrial production index for January rose for the second consecutive month,

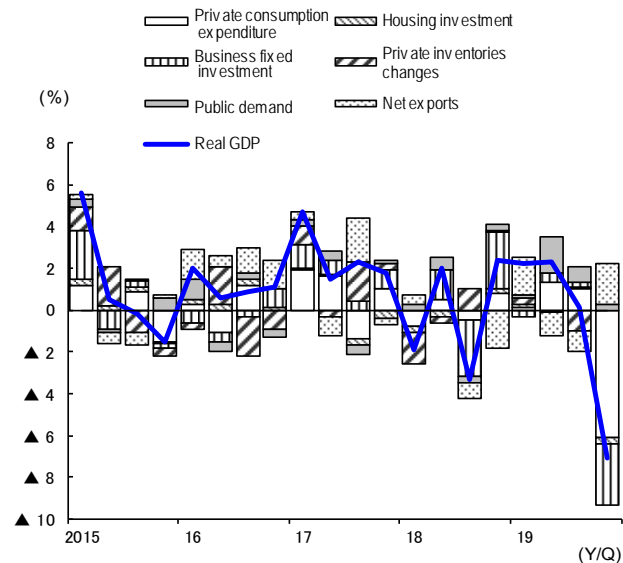
up 1.0% from the previous month. Production in the automobile industry substantially increased as a result of the recovery in production following natural disasters in autumn last year.

Looking at future production plans, industrial production is forecast to continue to increase in February, up 5.3% month-over-month. However, industrial production will likely decrease sharply in March, down 6.9% month-over-month. Since the effects of the spread of the novel coronavirus have not been fully reflected on production plans, there is a chance that industrial production will decrease substantially.

◆ Public Investment Has Remained Firm

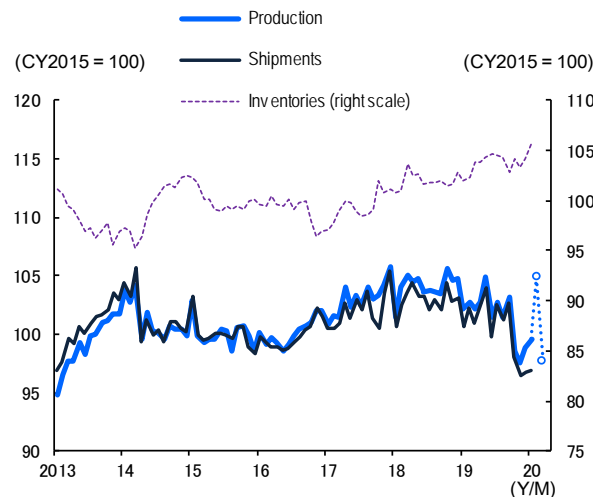
Public investment remained on a rising trend, as public works projects which had accumulated prior to the consumption tax hike have been implemented. The contract amount of public works projects, which serves as a leading indicator, is expected to increase again following the execution of the fiscal 2019 supplementary budget, although the increase has been sluggish currently.

Figure 2-1 Real GDP Change Rate by Demand Item
<the second preliminary estimates, on an annualized q/q change basis, seasonally adjusted>



Source: The Japan Research Institute, Ltd. based on data of The Cabinet Office.

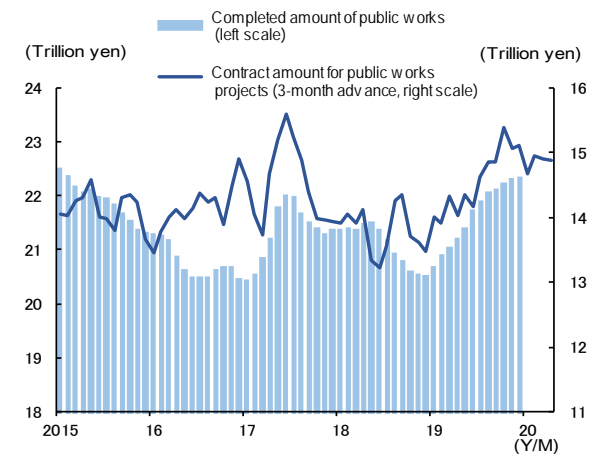
Figure 2-2 Industrial Production Index
<seasonally adjusted>



Source: The Japan Research Institute, Ltd. based on data of The Ministry of Economy, Trade and Industry.

Note: The latest two figures in the industrial production index are forecasts for February and March 2020 based on the production forecast index.

Figure 2-3 Completed and Contract Amounts of Public Works
<annualized, seasonally adjusted, 3-month moving averages>



Source: The Japan Research Institute, Ltd. based on data of The Ministry of Land, Infrastructure and Transport, East Japan Construction Surety Co., Ltd.

Note: Non-dwelling.

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Topic: Domestic Consumption Activity Slows Significantly Due to the Effects of the Novel Coronavirus

◆ The Novel Coronavirus Has Put Downward Pressure on the Economy

The economy is expected to fall sharply in the near term due to the spread of the novel coronavirus which arose from Wuhan, China.

The decline in production activities in China has had a negative impact on exports and production in Japan. However, domestic consumption has been more seriously affected. In addition to Chinese tourists, the decline in the number of visitors from other countries and regions to Japan has also pushed down consumption related to inbound tourism. Japan's GDP growth in the January to March period will likely be reduced by 1.3% on an annualized quarter-on-quarter change basis as a result of the decline in consumption related to inbound tourism alone.

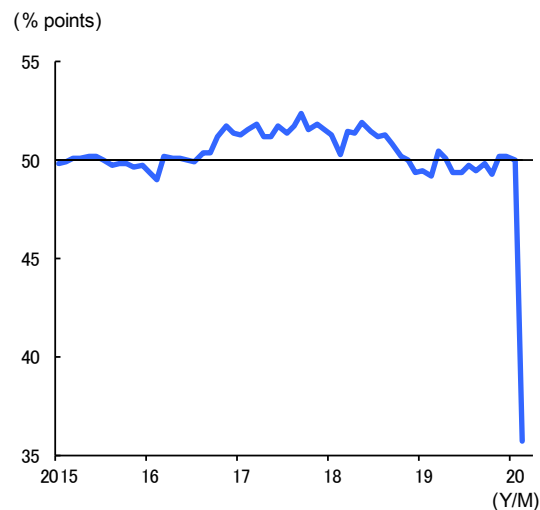
Furthermore, domestic household consumption has declined significantly due to the increase in the number of people who have been infected with the coronavirus in Japan. Recently, a growing number of people have refrained from leaving their homes because of fears of infection, and this has been weighing on overall

consumption. In particular, the consumption of leisure and other services, which is expected to be most negatively impacted, will likely continue to be restrained on a voluntary basis until the outbreak of the novel coronavirus is completely resolved.

◆ Economic Activity Will Likely Return to Normal Around Mid-year at the Earliest

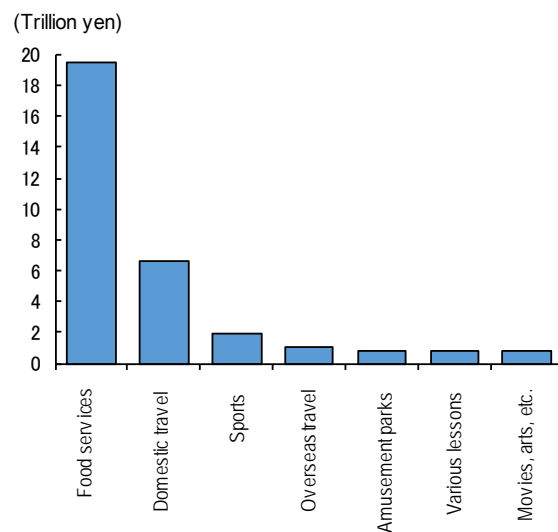
The future trend of the economy will depend on the spread of the novel coronavirus. If the outbreak comes to an end, the economy is expected to grow at a high rate as it normalizes. However, since it will take time to completely eliminate the adverse effects on consumption related to inbound tourism and domestic household consumption, economic activity is expected to return to normal around mid-year at the earliest. On the other hand, if the pandemic continues for a long time or becomes more serious, an increase in corporate bankruptcies could further dampen the economy.

Figure 3-1 Manufacturing PMI in China



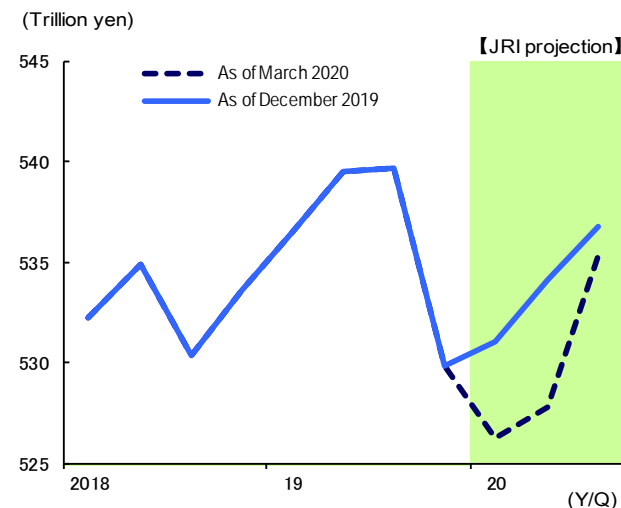
Source: The Japan Research Institute, Ltd. based on data of China Federation of Logistics and Purchasing.

Figure 3-2 Market Size of Services Consumption <CY2018>



Source: The Japan Research Institute, Ltd. based on data of Japan Productivity Center.

Figure 3-3 JRI Projections of Real GDP <seasonally adjusted>



Source: The Japan Research Institute, Ltd. based on data of The Cabinet Office.

Note: Projections by JRI.

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Temporary Decline in Exports of Both Goods and Services Is Inevitable

◆ Exports of Goods Continued to Stagnate

Exports of goods remained sluggish. By product, while exports of electronic components and devices are recovering as the global semiconductor market has bottomed out, exports of transport equipment have declined significantly. Looking at exports of transport equipment by region, exports to the United States, which account for approximately 30% of the total, declined significantly against the backdrop of a shift toward the local production of finished vehicles which had previously been exported from Japan. Exports to Asia, excluding China, also remained sluggish, reflecting stagnant sales in the local markets

At present, the expansion of the impact of the novel coronavirus has been weighing on the global economy. A temporary decline in exports of goods as a whole is inevitable.

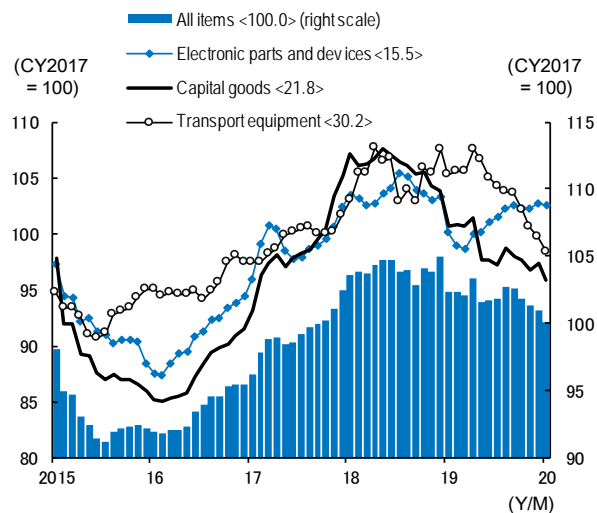
◆ Demand Related to Inbound Tourism Continued to Be Sluggish

The number of tourists that visited Japan in January 2020 increased by 1.4% from

the previous month. While the number of South Korean tourists visiting Japan continued to decline, the number of visitors to Japan from East Asia, excluding South Korea, increased as the Chinese New Year holiday fell in January this year.

However, consumption related to inbound tourism is expected to decline sharply, due to a decline in the number of tourists visiting Japan as a result of the effects of the novel coronavirus. At the end of January, the Chinese government banned group trips abroad, and the governments of other countries have also requested that their citizens refrain from traveling abroad. Consequently, a number of people have refrained from visiting Japan. Furthermore, the Japanese government took measures including the suspension of visas for tourists from China and South Korea in March. If the number of visitors from China, Hong Kong and South Korea were to drop by 90% and the number of visitors from other countries and regions was halved, consumption related to inbound tourism would fall by 70%.

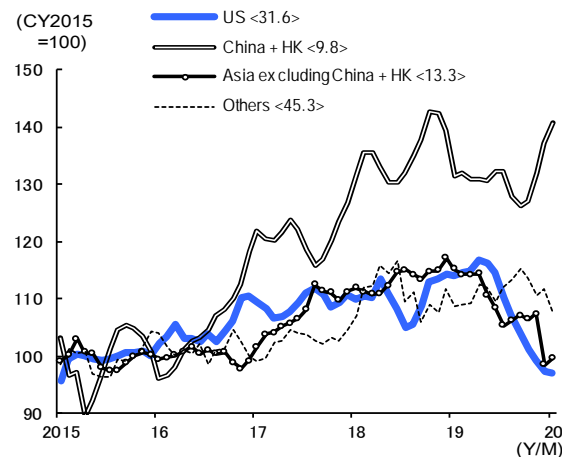
Figure 4-1 Real Exports by Item
<seasonally adjusted,
3-month moving averages>



Source: The Japan Research Institute, Ltd. based on data of The Ministry of Finance.

Note: Figures in the angled brackets show the shares in total nominal exports in CY2019.

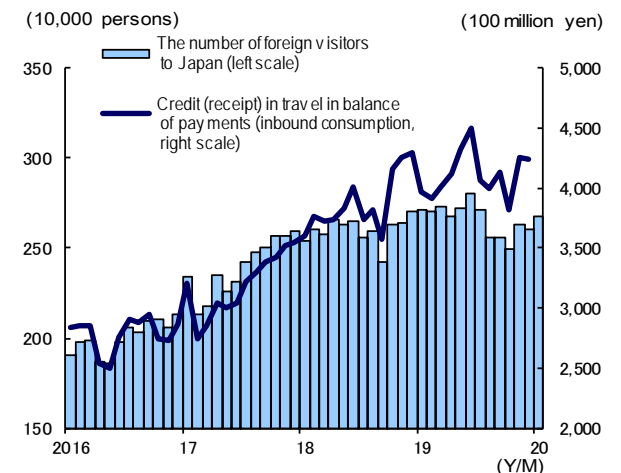
Figure 4-2 Real Exports of Transport Equipment by Destination
<seasonally adjusted,
3-month moving averages>



Source: The Japan Research Institute, Ltd. based on data of The Ministry of Finance, The Bank of Japan.

Note: Figures in the angled brackets show the shares in total nominal exports of transport equipment in CY2019.

Figure 4-3 Receipt in Travel in Balance of Payments
<seasonally adjusted>



Source: The Japan Research Institute, Ltd. based on data of The Ministry of Finance, Japan National Tourism Organization (JNTO).

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As Corporate Profits Diminish, Business Sentiment Has Become More Cautious Towards Capital Investment

◆ Corporate Profits Have Diminished

Corporate earnings have declined. According to the Financial Statement Statistics of Corporations by Industry quarterly report, sales value for the October to December 2019 period declined for the fourth consecutive quarter, down 2.9% from the previous quarter. Sales value both in the manufacturing and non-manufacturing sectors diminished due to a reactionary decline following the rush in demand prior to the consumption tax rate hike and the impact of large-scale typhoons, among other factors. Current profits declined for the third straight quarter, down 2.5% from the previous quarter. While current profits in the manufacturing sector fell sharply due to a decline in sales, down 8.6% from the previous quarter, current profits in the nonmanufacturing sector remained virtually flat thanks to the effects of cost reduction efforts, including labor saving.

Corporate profits for the January to March 2020 period are expected to fall further owing to the cooling of domestic consumption, the decline in demand related to

inbound tourism, and a decrease in exports to China in line with the spread of the novel coronavirus.

◆ Business Fixed Investment Has Declined

Capital investments for the October to December 2019 period decreased both in the manufacturing and nonmanufacturing sectors. While demand for investments in rationalization and labor saving driven by labor shortages remained strong, there has been a reactionary decline following the rush in demand prior to the consumption tax rate hike, and companies have taken moves to reduce capital investments due to the deterioration in corporate earnings.

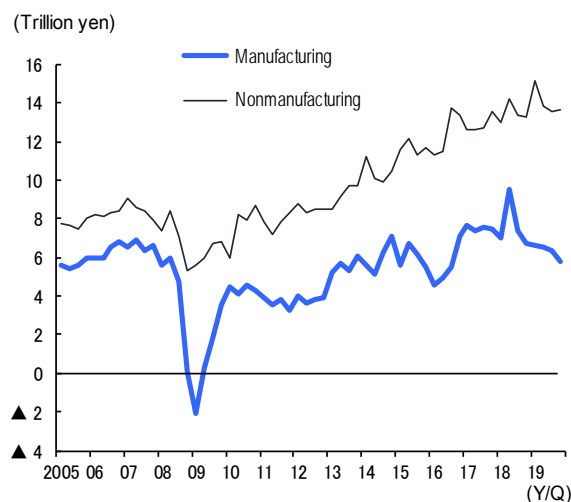
In the future, business sentiment is expected to become increasingly cautious as companies postpone capital investments against the backdrop of concerns over corporate earnings and postponement of business negotiations following the spread of the novel coronavirus.

Figure 5-1 Sales Value of Japanese Corporations by Type <seasonally adjusted>



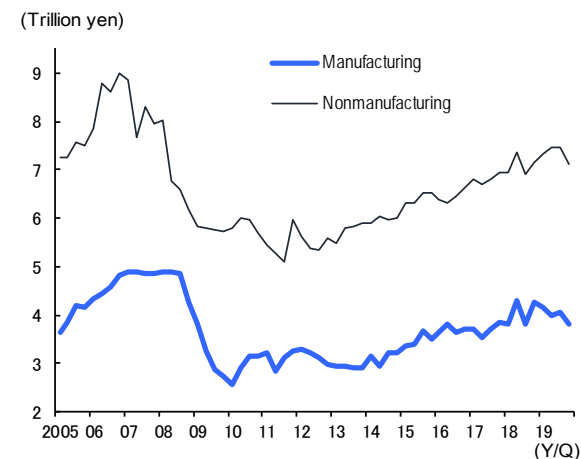
Source: The Japan Research Institute, Ltd. based on the data of The Ministry of Finance.
Note: All industries except for financial services and insurance.

Figure 5-2 Current Profits of Japanese Corporations by Type <seasonally adjusted>



Source: The Japan Research Institute, Ltd. based on the data of The Ministry of Finance.
Note: All industries except for financial services and insurance.

Figure 5-3 Business Fixed Investment of Japanese Corporations by Type <seasonally adjusted>



Source: The Japan Research Institute, Ltd. based on the data of The Ministry of Finance.
Note: 1. All industries except for financial services and insurance.
2. Excluding software investment.

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The Spread of the Novel Coronavirus Has Become a Downside Risk for Income

◆ The Income Situation Has Continued to Improve

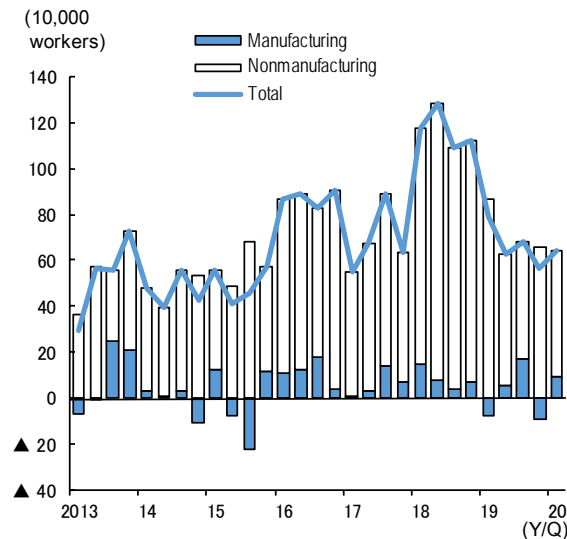
While the pace of growth in the number of workers peaked out in 2018, the rising trend has continued with the number of workers increasing by around 600,000 year-on-year. In the nonmanufacturing sector, where labor shortages are pronounced, the expansion of employment has been driven by the medical and welfare industries. In the manufacturing sector, employment of specialists such as IT engineers has increased.

Meanwhile, on the wages front, nominal wages have remained on a rising trend. Excluding the effects of sample changes, the total sum of cash earnings of full-time workers in December 2019 rose 1.0% from the previous year. Scheduled salaries remain on a rising trend, which has contributed to pushing up nominal wages.

◆ The Spread of the Novel Coronavirus Becomes a Serious Threat

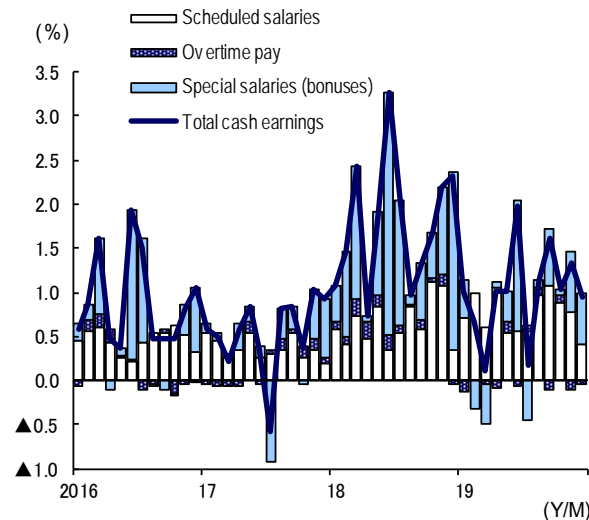
Looking ahead, however, a temporary decline in income is inevitable due to the outbreak of the novel coronavirus. The impact on part-time workers and day laborers is particularly serious. Income is expected to plunge temporarily due to the suspension of attendance at work and a decrease in working hours, reflecting shorter business hours and closures of commercial facilities and restaurants as well as the suspension of public works projects. Regular employees will also see their overtime pay decline due to a decrease in overtime hours. It is also possible that a deterioration in corporate earnings could adversely affect the wage negotiations this spring.

Figure 6-1 Number of Employees by Type
<difference from a year earlier>



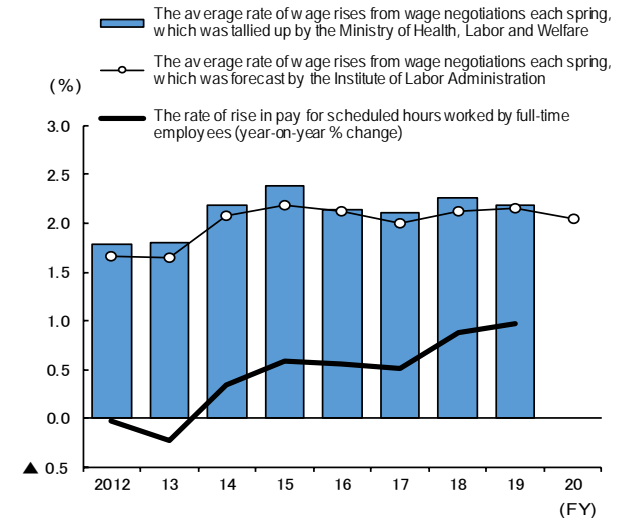
Source: The Japan Research Institute, Ltd. based on data of The Ministry of Internal Affairs and Communications.
Note: The figure in Q1 2020 is for January 2020.

Figure 6-2 Total Cash Earnings of Full-time Workers
<year-on-year % change>



Source: The Japan Research Institute, Ltd. based on the data of The Ministry of Health, Labor and Welfare.
Note: The effects of the sample changes in January 2018 and January 2019 were adjusted.

Figure 6-3 Average Rate of Wage Rises Resulting from Wage Negotiations Each Spring



Source: The Japan Research Institute, Ltd. based on the data of The Ministry of Health, Labor and Welfare, Japanese Trade Union Confederation, The Institute of Labor Administration.

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Rebound of Private Consumption Expenditure Will Be Delayed

◆ The Spread of the Novel Coronavirus Will Weigh on Consumption

The consumption activity index in January rose for the third consecutive month, following a plunge immediately after the consumption tax rate hike. The burden of the tax hike on households appears to be gradually easing.

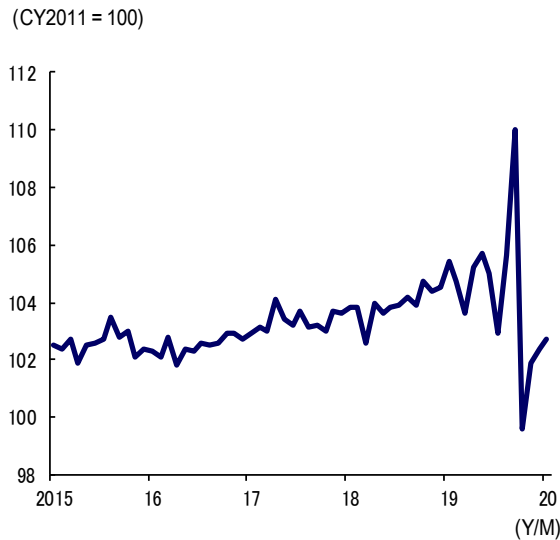
However, given the expansion of the effects of the novel coronavirus in Japan, a significant decline in private consumption expenditure is inevitable in the foreseeable future, mainly for service consumption such as leisure. In fact, according to the Economy Watchers Survey in February, the DI for current economic conditions related to household activity went down to 28.2, the lowest level since April 2011. In addition to a series of voluntary restraints on sports-related events, a growing number of people are refraining from going out. Unless the expansion of the number of people infected with the coronavirus comes to a halt, it is unlikely that personal consumption expenditure will fully recover.

◆ Housing Investment Has Seen a Decline

Housing starts in January fell 4.6% from the previous month, down for the first time in two months. Demand for housing for owner-occupied and subdivision housing remained on a declining trend in reaction to a surge in demand prior to the consumption tax hike, and housing starts for rental housing were sluggish, reflecting stricter screening for apartment loans by financial institutions.

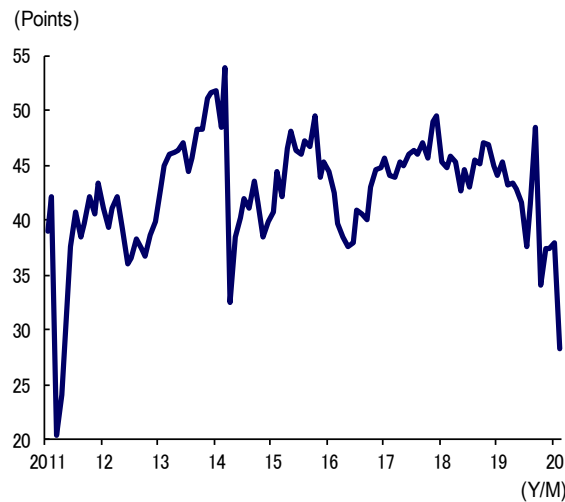
As for future prospects, the decline in the number of owner-occupied and subdivision detached housing is expected to come to a halt once the effects of the consumption tax rate hike have run their full course. However, housing starts are unlikely to recover strongly on the whole as housing starts for rental housing are expected to remain sluggish due to financial institutions' cautious attitudes toward real estate loans.

Figure 7-1 Consumption Activity Index



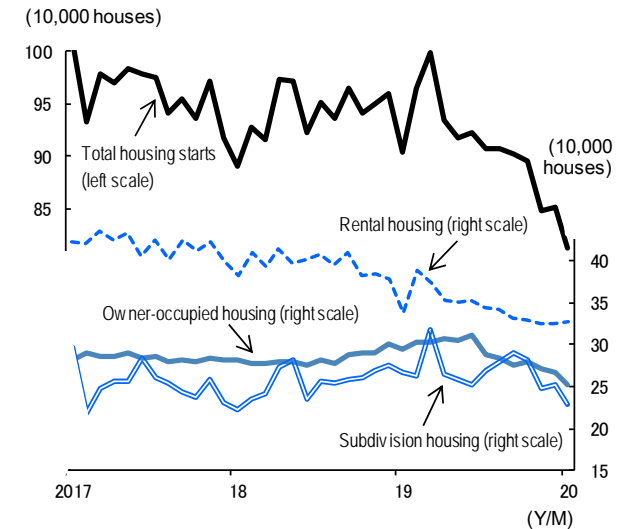
Source: The Japan Research Institute, Ltd. based on data of The Bank of Japan.
Note: Travel balance in balance of payments was adjusted.

Figure 7-2 Economy Watchers Survey
<household activity-related DI,
seasonally adjusted>



Source: The Japan Research Institute, Ltd. based on data of The Cabinet Office.

Figure 7-3 Housing Starts by Type
<annualized, seasonally adjusted>



Source: The Japan Research Institute, Ltd. based on data of The Ministry of Land, Infrastructure and Transport.

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Prospects for Japan's Economy - Projected Real GDP Change; -0.0% in FY2019 and 0.2% in FY2020

◆ The Japanese Economy Will Likely Have a Significant Downswing Due to the Expansion of the Effects of Novel Coronavirus

(1) According to the Second Preliminary Quarterly Estimates of the GDP (2nd QE), Japan's real GDP for the October to December 2019 period was revised downward to -7.1% on an annualized quarter-on-quarter change basis (down 1.8% from the preceding quarter) from the First Preliminary Quarterly Estimates of GDP (1st QE) (-6.3% on an annualized quarter-on-quarter change basis; down 1.6% from the preceding quarter) against the backdrop of a downswing in capital investment, public investment and inventory investment. It has become more apparent that the Japanese economy has declined following the consumption tax rate hike.

(2) In the revised prospects, the growth forecast has been revised downward significantly due to the increase in the impact of the novel coronavirus, which exceeded initial forecasts. First of all, there is a high possibility that the Japanese economy could see negative growth for two consecutive quarters in the January to March 2020 period. Exports dropped sharply against the backdrop of falling demand related to inbound tourism, mainly from Chinese tourists, and a downturn in the Asian economy.

Furthermore, domestic household consumption has declined significantly due to the increase in the number of people who have been infected with the coronavirus in Japan, which will likely result in negative growth in personal consumption for two consecutive quarters. Companies are also expected to become more cautious about capital spending amid uncertainty over their business performance.

(3) The future trend of the economy will depend on the spread of the novel coronavirus. While it is difficult to predict when the outbreak of the novel coronavirus will come to an end, the government has been urging people to refrain from non-urgent, unnecessary outings, and at this moment, it is predicted that the increase in the number of people infected with the coronavirus in Japan will come to a halt by the

end of April. If the outbreak comes to an end, demand related to inbound tourism and domestic household consumption is expected to pick up. Corporate capital investment, which has been postponed, is also expected to start moving again, resulting in higher economic growth. However, since it will take time to completely eliminate the adverse effects on demand related to inbound tourism and domestic consumption activity, economic activity is expected to return to normal around mid-year at the earliest.

(4) As a result of the above, Japan's economic growth for FY2019 and FY2020 are forecast to be -0.0% and +0.2%, respectively, with the growth rate hovering around 0% in both years. If the coronavirus pandemic lasts longer and becomes more serious, it could lead to more corporate bankruptcies in the retail, service and manufacturing sectors, where demand is falling sharply, and the Japanese economy could see negative growth for two straight years.

◆ The Pace of Year-on-year Rise in the Core CPI Will Likely Slow for the Time Being

(5) The rate of year-on-year increase in the core consumer price index (CPI) which excludes fresh food rose slightly in January from the previous month. This was mainly because the pace of the fall in energy prices slowed due to the rise in the price of crude oil toward the end of last year.

As for future prospects, reflecting weaker upward pressure from the supply-demand side against the backdrop of sluggish economy as a result of the spread of the novel coronavirus, the pace of year-on-year increase in the core CPI is expected to temporarily slow to around +0% (excluding the impact of the consumption tax rate hike and the provision of free child education and nursery care).

Figure 9 Projections for GDP Growth and Main Indicators of Japan (as of March 9, 2020)

	(seasonally adjusted, annualised % changes from the previous quarter)											(% changes from the previous fiscal year)		
	CY2019		CY2020				CY2021				CY2022	FY2019	FY2020	FY2021
	7~9	10~12	1~3	4~6	7~9	10~12	1~3	4~6	7~9	10~12	1~3	(Projection)	(Projection)	(Projection)
	(Actual)	(Actual)	(Projection)	(Projection)	(Projection)	(Projection)	(Projection)	(Projection)	(Projection)	(Projection)	(Projection)	(Projection)	(Projection)	(Projection)
Real GDP	0.1	▲ 7.1	▲ 2.7	1.2	5.8	1.2	1.5	0.7	0.4	0.6	0.7	▲ 0.0	0.2	1.1
Private Consumption Expenditure	1.8	▲ 10.6	▲ 2.0	0.8	5.7	1.4	1.1	0.9	0.6	0.6	0.8	▲ 0.5	▲ 0.2	1.2
Housing Investment	5.0	▲ 9.7	▲ 2.3	▲ 1.2	▲ 0.6	0.8	1.4	0.5	▲ 1.6	▲ 0.4	0.0	1.3	▲ 1.6	0.1
Business Fixed Investment	0.9	▲ 17.3	1.9	▲ 1.0	7.9	3.8	2.6	1.6	1.6	1.4	1.4	▲ 0.7	0.0	2.3
Private Inventories (percentage points contribution)	(▲ 1.0)	(0.0)	(0.1)	(▲ 0.2)	(0.0)	(0.0)	(0.0)	(0.0)	(0.0)	(0.0)	(0.0)	(▲ 0.1)	(▲ 0.1)	(0.0)
Government Consumption Expenditure	3.0	0.9	0.2	2.4	3.6	▲ 1.3	1.6	0.5	0.5	0.5	0.5	2.5	1.5	0.7
Public Investment	4.5	2.8	▲ 0.6	3.3	1.8	6.4	2.1	▲ 1.9	▲ 3.4	0.0	0.3	3.5	2.7	0.0
Net Exports (percentage points contribution)	(▲ 1.0)	(1.9)	(▲ 1.9)	(0.4)	(0.6)	(▲ 0.2)	(0.1)	(▲ 0.0)	(▲ 0.0)	(▲ 0.0)	(▲ 0.0)	(▲ 0.3)	(▲ 0.0)	(▲ 0.0)
Exports of Goods and Services	▲ 2.8	▲ 0.3	▲ 8.5	0.2	9.4	▲ 0.4	1.8	2.0	2.0	1.8	1.6	▲ 1.9	▲ 0.1	2.1
Imports of Goods and Services	2.8	▲ 10.2	2.5	▲ 2.1	5.9	1.0	1.4	2.3	2.3	1.9	1.9	▲ 0.4	0.1	2.1
(Ref.) Domestic Private Demand (percentage points contribution)	(0.4)	(▲ 9.5)	(▲ 0.8)	(0.1)	(4.4)	(1.4)	(1.1)	(0.8)	(0.5)	(0.5)	(0.7)	(▲ 0.4)	(▲ 0.2)	(1.0)
(Ref.) Public Demand (percentage points contribution)	(0.8)	(0.3)	(0.0)	(0.7)	(0.8)	(0.0)	(0.4)	(0.0)	(▲ 0.1)	(0.1)	(0.1)	(0.7)	(0.5)	(0.1)

	(% changes from the same quarter of the previous year)											(% changes from the previous fiscal year)		
Nominal GDP	2.3	0.5	▲ 1.0	▲ 1.0	▲ 0.1	1.6	2.7	2.4	1.2	1.1	1.0	0.8	0.8	1.4
GDP deflator	0.6	1.2	1.0	1.1	0.7	0.4	0.2	0.1	0.3	0.4	0.4	0.8	0.6	0.3
Consumer Price Index (excluding fresh food)	0.5	0.6	0.6	0.4	0.7	0.3	0.5	0.7	0.7	0.8	0.8	0.6	0.5	0.7
(excluding fresh food, consumption tax, education free of charge)	0.5	0.3	0.2	0.1	0.4	0.4	0.6	0.7	0.7	0.8	0.8	0.4	0.4	0.7
Unemployment Rate (%)	2.3	2.3	2.4	2.4	2.3	2.3	2.2	2.2	2.2	2.2	2.2	2.3	2.3	2.2
Exchange Rates (JY/US\$)	107	109	107	101	103	104	105	105	105	105	105	108	103	105
Import Price of Crude Oil (US\$/barrel)	66	66	65	59	65	67	68	68	68	68	68	67	65	68

Source: The Cabinet Office; The Ministry of Internal Affairs and Communications; The Ministry of Economy, Trade and Industry; The Ministry of Finance.

The projection figures are based on those of The Japan Research Institute, Ltd.

Note : "▲" indicates minus.