

Monthly Report of Prospects for Japan's Economy

November 2019

Macro Economic Research Center
Economics Department



The Japan Research Institute, Limited

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

This report is the revised English version of the October 2019 issue of the original Japanese version.

Disclaimer:

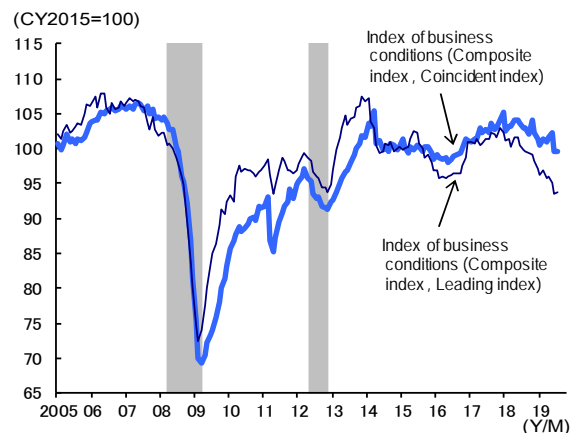
This report is intended solely for informational purposes and should not be interpreted as an inducement to trade in any way.

All information in this report is provided "as is", with no guarantee of completeness, accuracy, timeliness or of the results obtained from the use of this information, and without warranty of any kind, express or implied, including, but not limited to warranties of performance, merchantability and fitness for a particular purpose. In no event will JRI, its officers or employees be liable to you or anyone else for any decision made or action taken in reliance on the information in this report or for any damages, even if we are advised of the possibility of such damages. JRI reserves the right to suspend operation of, or change the contents of, the report at any time without prior notification. JRI is not obliged to alter or update the information in the report, including without limitation any projection or other forward looking statement contained therein.

The General Situation of Japan's Economy – A Sense of Standstill Is Felt in Economic Activity

Figure 1-1 Economic Activity

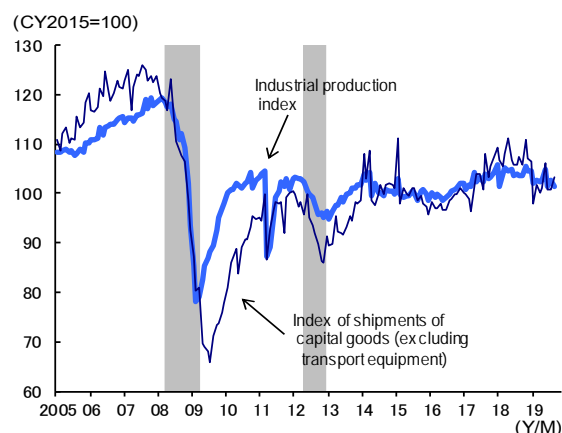
CI remained on a declining trend both in terms of the CI coincident index and the CI leading index.



Source: The Cabinet Office.

Figure 1-2 The Corporate Sector

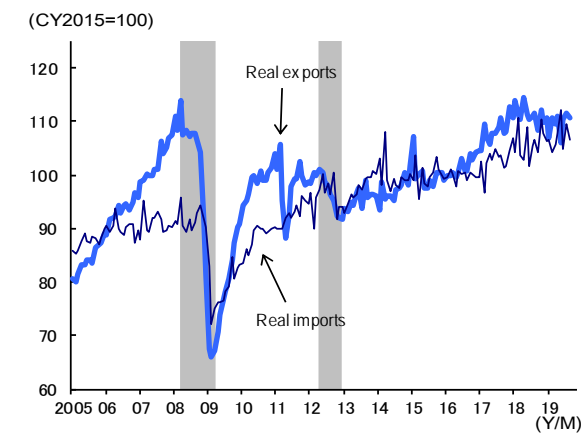
Industrial production was sluggish, mainly for producer goods and durable consumer goods.



Source: The Ministry of Economy, Trade and Industry.

Figure 1-3 Overseas Demand

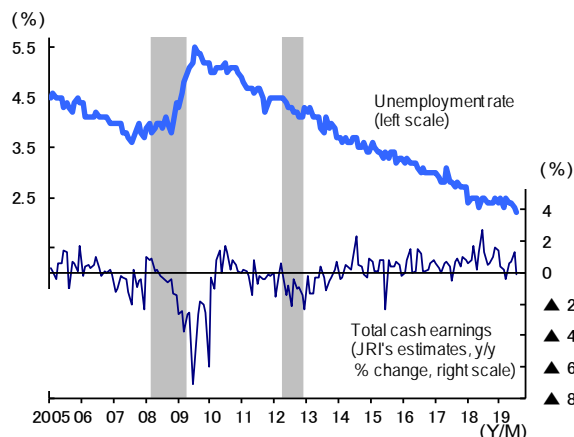
Decline in exports, mainly to Asia, bottomed out. Imports decreased, particularly of crude oil and LNG.



Source: The Bank of Japan.

Figure 1-4 Employment and Income

The unemployment rate is hovering around its lowest level since 1992. Nominal wages have been on a rising trend despite some ups and downs.

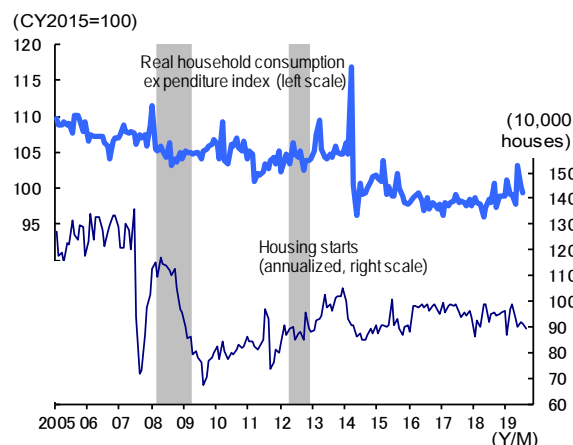


Source: The Ministry of Internal Affairs and Communications, The Ministry of Health, Labor and Welfare.

* The shaded area indicates the recession phase.

Figure 1-5 The Household Sector

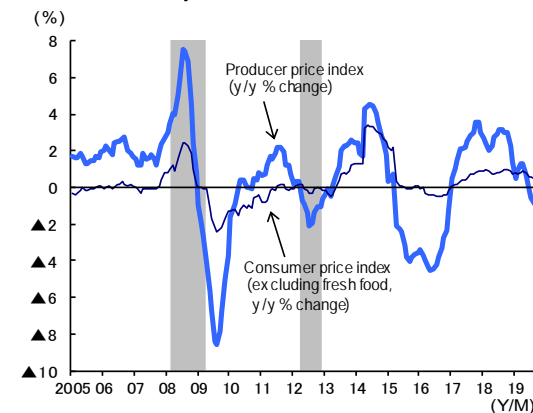
Real household consumption picked up, albeit with fluctuations. Housing starts were sluggish.



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 declined mainly for raw materials. The pace of increase in consumer prices has slowed down moderately.



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

Monthly Report of Prospects for Japan's Economy November 2019
The Japan Research Institute, Limited

Manufacturing Production Activities Remain Sluggish, While Nonmanufacturing Stays Firm

◆ The DI for Business Conditions Turned Downward

In the Tankan September 2019 Survey taken by the Bank of Japan (BoJ), large manufacturers' DI for business conditions was down 2 percentage points from the previous survey, showing a decline for three consecutive quarters. DI deteriorated for industries including general-purpose machinery and production machinery against the backdrop of sluggish exports.

At the same time, DI for large nonmanufacturers remained at a high level, although it declined for the first time in two quarters, down 2 percentage points from the previous survey. DI saw a decline in the retail and wholesale sectors as well as in hotel and food services due to a reaction to the consecutive long holidays in May, among other factors. However, information and communications services and the construction and real estate industries remained resilient, driven by strong software investment and construction investment.

In terms of future outlook, DI is anticipated to deteriorate, dropping 6 percentage points across businesses of all sizes and in all industries. In addition to uncertainties

remaining in the overseas situation, concerns over a decline in domestic consumption following the hike in the consumption tax rate will likely apply downward pressure on business sentiment.

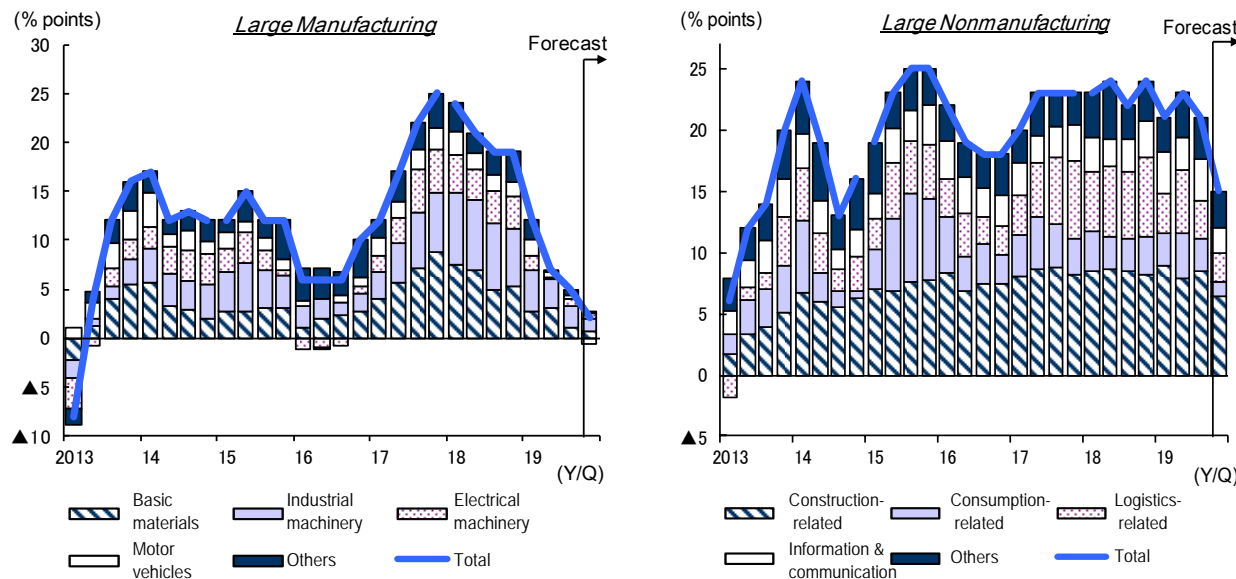
◆ Industrial Production Has Seen Some Ups and Downs

The Industrial Production Index for August decreased for the first time in two months, down 1.2% from the previous month. Due to the effects of sluggish overseas demand and persistently high inventories, the outlook of production plans will likely remain lackluster. Specifically, industrial production is forecast to increase by 1.9% month-over-month in September and to decrease by 0.5% in October.

◆ Private Consumption Remained Firm

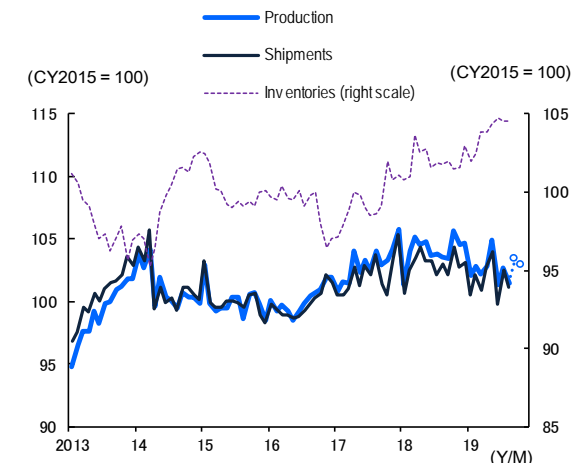
Amid improvement in employment and income conditions, private consumption remained firm. Given the fact that the significant decline in July was temporary and caused by weather factors, the overall trend indicates that private consumption has been growing moderately.

Figure 2-1 Contributions to the Business Conditions Diffusion Index by Industry
<diffusion index of "favorable" minus "unfavorable," and percentage point contribution to total DI points>



Source: The Japan Research Institute, Ltd. based on data of The Bank of Japan, "The Tankan September 2019 Survey".

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 September and October based on the production forecast index.

Monthly Report of Prospects for Japan's Economy November 2019
The Japan Research Institute, Limited

Exports Are Expected to Pick up

◆ Exports of Goods Are Expected to Pick up

Exports of goods have been sluggish. Looking at exports by category, while exports of electronic parts and devices increased as sales of smartphones in emerging countries had bottomed out, exports of capital goods mainly to Asia including China continued to stagnate.

As for future prospects, since the Chinese economy is expected to pick up due to the government's economic stimulus measures, Japan's exports of capital goods to Asia are anticipated to return to growth in the future.

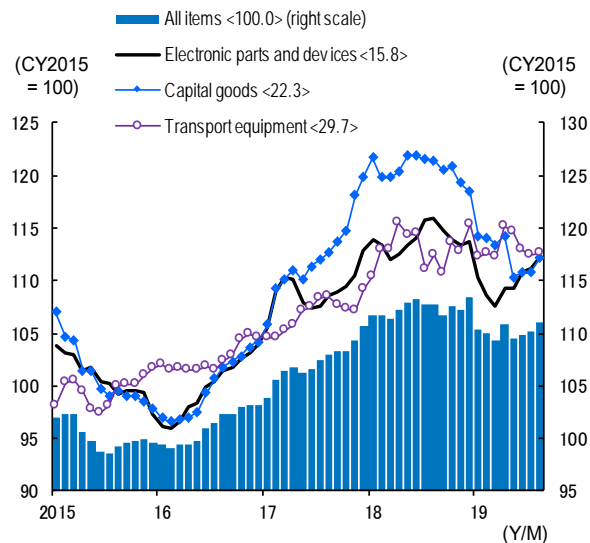
However, amid the lack of momentum for the global economy on the whole, a strong recovery of overall exports will be difficult to achieve.

◆ Demand Related to Inbound Tourism Has Declined

The number of tourists that visited Japan in August declined by 8.0% compared with the previous month. The number of Korean tourists visiting Japan halved from the previous year, against the backdrop of the deterioration in the relationship between Japan and Korea in line with the tightening of export controls.

As for the future outlook, while demand related to inbound tourism is expected to pick up temporarily due to those visiting Japan to watch the Rugby World Cup 2019, the demand is expected to stagnate again toward the end of the year if the number of Korean tourists visiting Japan, which accounts for 13% of total inbound spending, remains low.

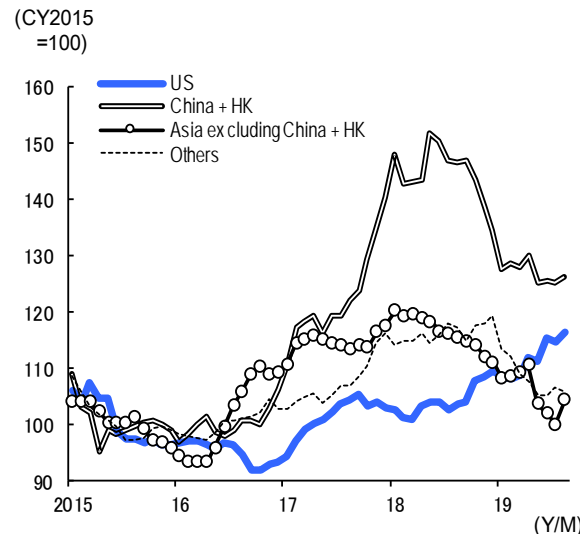
Figure 3-1 Real Exports by Item
<seasonally adjusted,
3-month moving averages>



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

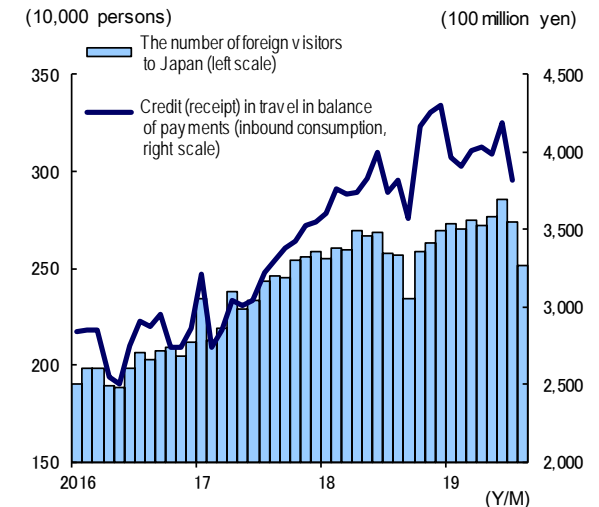
Note: Figures in the angled brackets show the shares in total nominal exports in CY2018.

Figure 3-2 Real Exports of Capital Goods 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.

Figure 3-3 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).

Monthly Report of Prospects for Japan's Economy November 2019
The Japan Research Institute, Limited

Business Fixed Investment Will Likely Be on the Rise As Profits Remain at a High Level

◆ Corporate Profits Remain at a High Level

Corporate earnings have seen some fluctuations but have remained at a high level. According to the Financial Statement Statistics of Corporations by Industry quarterly report, current profits for the period from April–June 2019 declined for the first time in two quarters, down 5.0% from the previous quarter. Since the decline was attributable to a reaction to the large dividend income of specific companies (pure holding companies) in the previous quarter, the overall trend has remained virtually flat.

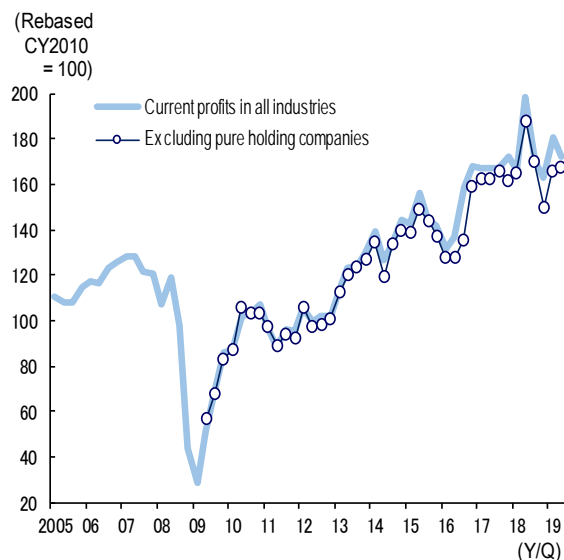
As for the outlook for corporate earnings, while the current appreciation of the yen will exert downward pressure, overall corporate earnings are anticipated to remain at a high level backed by firm domestic demand.

◆ Business Fixed Investment Will Likely Remain on a Rising Trend

Capital investment has remained on an increasing trend. Looking at business fixed investment for the April–June 2019 period by industry, while investment in the manufacturing industry declined due to adverse external conditions including the trade conflict between the United States and China and the slowdown in China's economy, investment in nonmanufacturing industries surged mainly for software investment aimed at labor saving and digitalization.

As for the future outlook, a favorable earnings environment is expected to support the appetite for investments by the corporate sector. Capital expenditures are forecast to remain on a rising trend as demand for investments for rationalization and labor saving as well as maintenance and replacement continues to grow firmly.

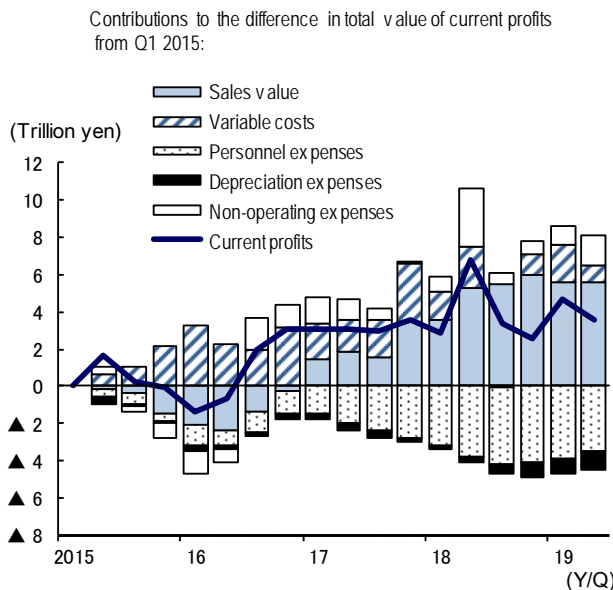
Figure 4-1 Current Profits of Japanese Corporations
<seasonally adjusted>



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

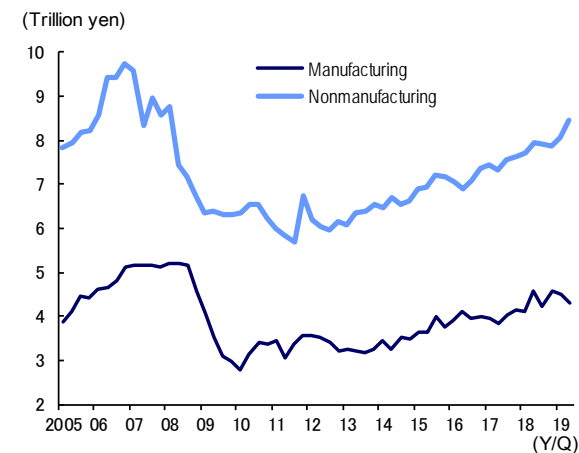
Note: All industries except for financial services and insurance.

Figure 4-2 Contributions of Factors to Change in Total Value of Current Profits



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

Figure 4-3 Value of Business Fixed Investment Based on Financial Statements
Statistics of Corporations by Industry
<seasonally adjusted>



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

Note: Including software investment.

Monthly Report of Prospects for Japan's Economy November 2019
The Japan Research Institute, Limited

Income Is Likely to Increase Steadily

◆ The Income Situation Has Continued to Improve

While the pace of growth in the number of workers has declined compared with the previous year, the rising trend has continued with the number of workers increasing by around 700,000 year-on-year. Currently, the number of work hours per employee has been decreasing due to the effect of workstyle reforms among other factors, which has also contributed to boosting the number of workers.

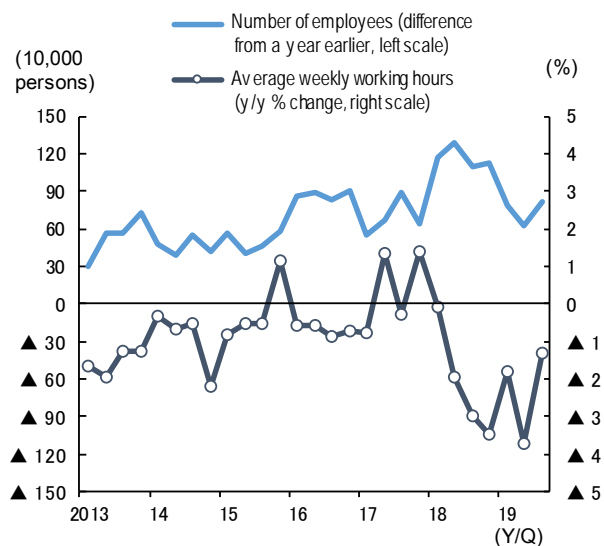
Meanwhile, on the wages front, nominal wages have remained on a rising trend. As for the total sum of cash earnings of full-time workers, growth slowed in July due to downward pressure on special wages. However, given the large increase in special salaries in the previous month, this could be a temporary decline due to the difference in the dates of bonus payments. We believe that the upward trend in

nominal wages has not significantly deteriorated as scheduled salaries remain on a rising trend driven by the implementation of pay scale increases.

◆ Real Income Is Likely to Increase Firmly

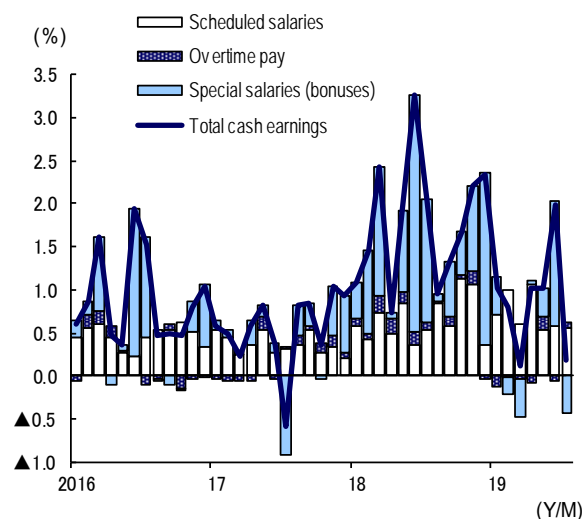
A look at future prospects shows a high likelihood that moderate growth in the number of employees will continue as a strong sense of labor shortage is still being felt by many industries. Nominal wages will likely remain on a steady rise given the tight labor supply/demand conditions. On the other hand, on the price front, it is expected that the provision of free education and nursery care and the introduction of the reduced tax rate will help minimize price increases as a result of the hike in the consumption tax. As a result, growth at around the mid-1% level will likely be maintained in real compensation for employees.

Figure 5-1 Number of Employees and Average Weekly Work Hours



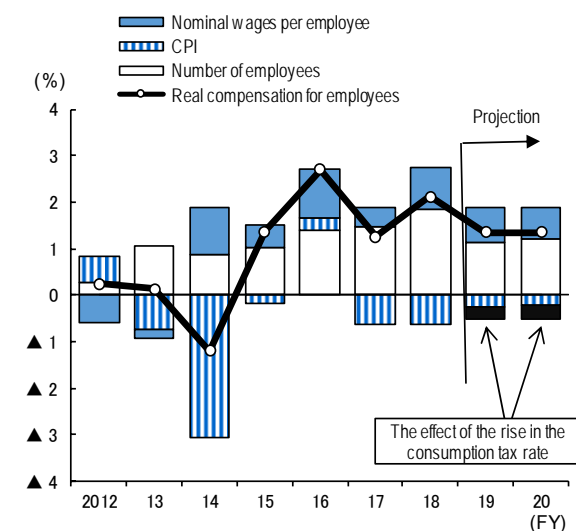
Source: The Japan Research Institute, Ltd. based on data of The Ministry of Internal Affairs and Communications.
Note: The figures in Q3 2019 are for July-August 2019.

Figure 5-2 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 5-3 Real Compensation for Employees <year-on-year % change>



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

Monthly Report of Prospects for Japan's Economy November 2019
The Japan Research Institute, Limited

Private Consumption Expenditure Is Forecast to Recover Moderately

◆ Downward Pressure Caused by Unseasonable Weather Has Dissipated

Personal consumption is picking up. Consumer spending in August was brisk for a wide range of items. A rise in the number of holidays contributed to boosting consumption, in addition to falling downward pressure stemming from unfavorable weather and sluggish sales of seasonal goods. By item, sales of home appliances such as air conditioners and restaurant services have been recovering from a slump in July.

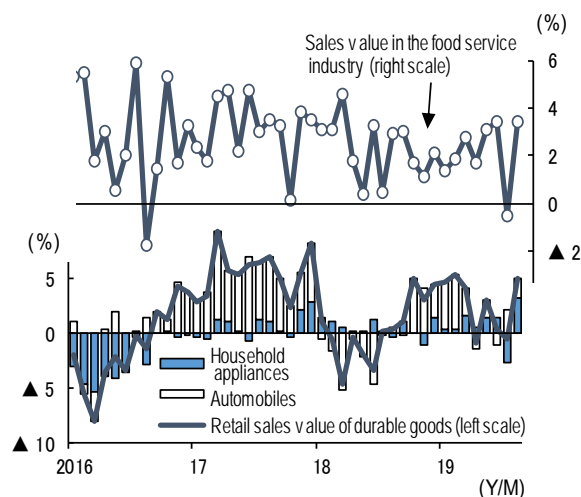
As for future prospects, a moderate recovery in private consumption expenditures is anticipated to continue. The negative effects of the hike in consumption tax will likely be mitigated significantly thanks to the measures to reduce tax burdens including the provision of free education. Income growth remains firm, driven by a serious labor shortage, which is expected to support personal consumption.

◆ Housing Investment Has Turned to a Declining Trend

The number of housing starts in August decreased for the second consecutive month, down 2.1% month-over-month. The number of housing starts for owner-occupied housing saw a significant plunge by 5.6% month-over-month, while the number for rental housing remained weak, reflecting the ongoing effects of strict screening by financial institutions.

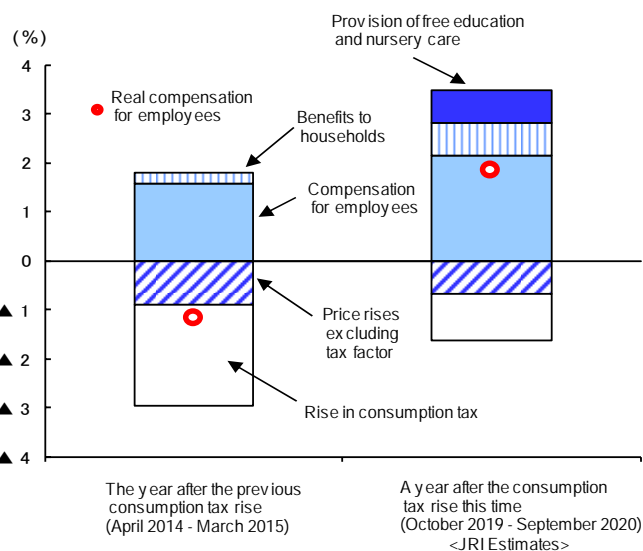
As for the future outlook, the number of housing starts for owner-occupied and subdivision housing, which had benefited from the rush in demand prior to the consumption tax rate hike, will likely remain on a diminishing trend going forward. Having said that, as the government will implement measures for levelling demand in line with the tax rate hike, the rise in rush demand will be limited compared to that for the previous tax rate hike. Given this situation, a significant decline in the number of housing starts after the tax rate hike will likely be avoided.

Figure 6-1 Retail Sales Values of Durable Goods and Sales Value in the Food Service Industry
<year-on-year % change>



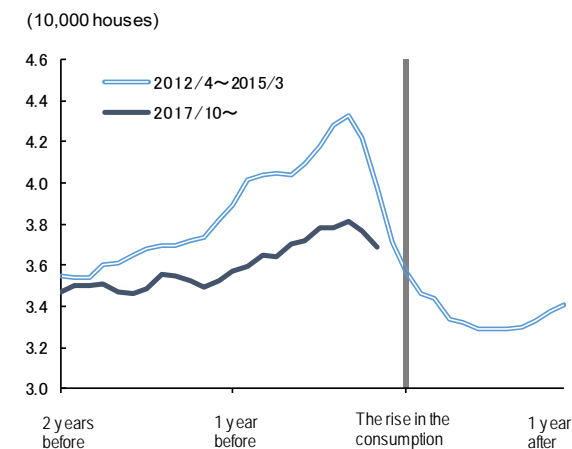
Source: The Japan Research Institute, Ltd. based on data of The Ministry of Land, Infrastructure and Transport, Japan Food Service Association.

Figure 6-2 Real Compensation for Employees after the Consumption Tax Rise
<year-on-year % change>



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

Figure 6-3 Housing Starts for Owner-occupied and Subdivision Detached Houses
<seasonally adjusted, 3-month moving averages>



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

Topic: Increased Unpaid Overtime Is a Concern behind Reduced Work Hours

◆ Work Hours Have Been Decreasing at an Accelerated Pace

Since 2018, the number of working hours for full-time workers has been decreasing at an accelerated pace. In response to the enactment of a law related to workstyle reforms, there has been a progress in efforts by companies to reduce work hours.

◆ There Is a Concern over an Increase in Unpaid Overtime

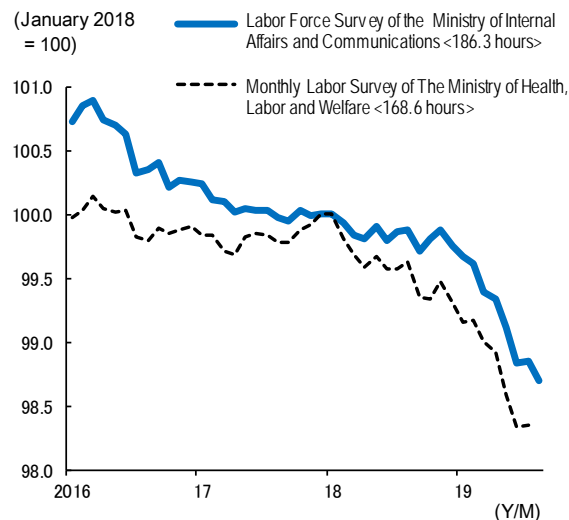
In reality, however, there are concerns that unpaid overtime is increasing. For example, the Labor Force Survey showed a smaller decrease in working hours than the Monthly Labor Survey. In contrast to the Labor Force Survey, which counts the number of hours actually worked, the Monthly Labor Survey counts only the number of hours worked for which wages were paid. It can be interpreted that the discrepancy between the two survey results includes “unpaid overtime hours,” where no wage payment occurs.

The difference between the two survey results led to an increase in unpaid overtime after 2018, when the decline in total working hours began to accelerate. It is possible that unpaid overtime work has increased due to the promotion of workstyle reforms amid insufficient work efficiency.

By industry, unpaid overtime declined in the financial and insurance services industry as well as the information and communication industry, but rose in most other industries. The growth was particularly prominent in the lifestyle-related services and entertainment industry.

In April 2020, the upper limit on overtime work will be applied to small- and medium-sized enterprises, which may result in further increases in unpaid overtime. Improving productivity is essential to rectifying this situation and achieving a real reform of the way people work.

Figure 7-1 Monthly Work Hours of Full-time Workers by Survey



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

Note: Figures in the angled brackets show the total work hours in January 2018.

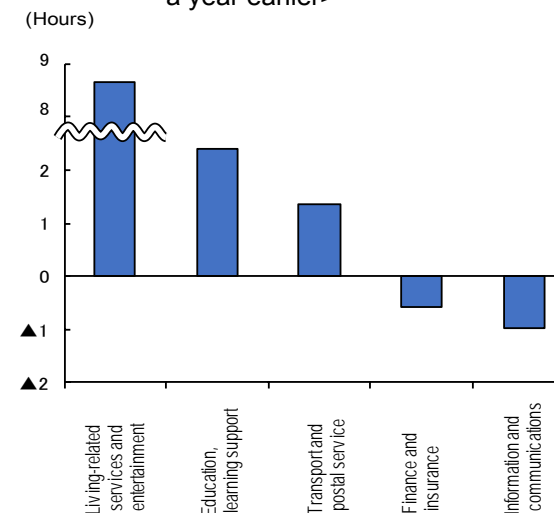
Figure 7-2 Monthly Unpaid Overtime of Full-time Workers <JRI estimates, 12-month moving averages>



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

Note: Monthly unpaid overtime (estimates) = the total work hours (Labor force survey) - the total work hours (Monthly labor survey)

Figure 7-3 Changes in Monthly Unpaid Overtime of Full-time Workers by Industry <JRI estimates, difference from a year earlier>



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

Monthly Report of Prospects for Japan's Economy November 2019
 The Japan Research Institute, Limited

Prospects for Japan's Economy - Projected Real GDP Change; 0.8% in FY2019 and 0.7% in FY2020

◆ Mild Recovery of the Japanese Economy Will Likely Continue, Driven by Domestic Demand

(1) Japan's Economy Will Remain on Mild Recovery Path

As for future prospects, while a sense of economic slowdown may increase over the short term due to the effects of the reaction to higher growth and the consumption tax rate hike, Japan's economy is anticipated to continue to grow moderately, driven by domestic demand.

Exports are expected to pick up slightly against the backdrop of the bottoming out of global IT demand, among other factors. Amid the lack of momentum in the global economy on the whole, however, there is little hope for a robust recovery.

Business fixed investment, on the other hand, is forecast to remain on a rising trend, reflecting resilient demand for investments backed by structural factors, including investments aimed at labor-saving against the backdrop of labor shortages and workstyle reforms, as well as the need for updating worn out equipment and R&D investments for the utilization of new technologies.

(2) Decline in Consumption Due to the Tax Rate Hike Will Be Limited

Personal consumption is also anticipated to continue to grow moderately, underpinned by the improvement in the income environment. While the consumption tax rate was hiked last month, measures to minimize the impact of the consumption tax rate hike—such as the introduction of a reduced tax rate and the provision of free education and nursery care—are expected to significantly reduce the burden on households. Therefore, we believe that a substantial decline in consumer spending is likely to be avoided.

Consequently, Japan's economy is forecast to continue to grow steadily even with the impact of the consumption tax rate hike, with the growth rate expected to be +0.8% for FY2019 and +0.7% for FY2020.

◆ The Year-on-year Change Rate in the Core CPI Will Likely Be Slightly below 1 Percent

(3) In August, core CPI growth slowed. The impact of the increase in the out-of-pocket medical expenses of elderly people in the previous year was over, and upward pressure on health and medical care was alleviated. In addition, due to the slowdown in the rise in gas and electricity bills, energy prices turned negative from the previous year for the first time since January 2017.

Although upward pressure from the supply-demand side is expected to intensify, the pace of decline in energy prices is expected to widen. As a result, the year-on-year increase rate in core CPI will likely remain somewhat lower than 1% (excluding the impact of the consumption tax rate hike and the provision of free education).

Figure 9 Projections for GDP Growth and Main Indicators of Japan (as of October 1, 2019)

	(seasonally adjusted, annualised % changes from the previous quarter)									(% changes from the previous fiscal year)		
	CY2019				CY2020				CY2021	FY2018	FY2019	FY2020
	1 ~ 3	4 ~ 6	7 ~ 9	10 ~ 12	1 ~ 3	4 ~ 6	7 ~ 9	10 ~ 12	1 ~ 3	(Actual)	(Projection)	(Projection)
	(Actual)	(Actual)	(Projection)		(Projection)				(Projection)			
Real G D P	2.2	1.3	0.7	▲ 2.0	1.3	1.3	1.0	0.7	1.2	0.7	0.8	0.7
Private Consumption Expenditure	▲ 0.0	2.5	1.0	▲ 4.0	2.2	2.0	▲ 0.4	1.4	1.0	0.4	0.6	0.6
Housing Investment	3.1	0.3	0.0	▲ 5.8	▲ 3.1	0.0	1.0	2.5	0.8	▲ 4.3	0.6	▲ 0.8
Business Fixed Investment	▲ 1.0	0.8	2.6	▲ 0.5	1.9	1.6	1.8	1.8	2.0	3.5	1.3	1.6
Private Inventories (percentage points contribution)	(0.3)	(▲ 0.2)	(▲ 0.2)	(0.1)	(0.0)	(0.0)	(0.0)	(0.0)	(0.0)	(0.1)	(0.1)	(0.0)
Government Consumption Expenditure	▲ 0.4	4.9	0.4	0.0	0.4	1.0	2.5	▲ 0.5	1.0	0.9	1.7	0.8
Public Investment	6.1	7.2	0.5	0.0	▲ 2.5	▲ 0.6	0.7	1.6	1.3	▲ 4.0	1.9	▲ 0.1
Net Exports (percentage points contribution)	(1.7)	(▲ 1.2)	(▲ 0.1)	(0.5)	(▲ 0.1)	(▲ 0.2)	(0.3)	(▲ 0.4)	(0.1)	(▲ 0.1)	(▲ 0.2)	(0.0)
Exports of Goods and Services	▲ 7.6	▲ 0.1	1.3	1.7	1.4	1.4	2.6	▲ 1.2	2.0	1.5	▲ 0.9	1.4
Imports of Goods and Services	▲ 16.0	6.9	1.8	▲ 1.0	2.1	2.4	0.6	1.3	1.6	2.1	0.2	1.3
(Ref.) Domestic Private Demand (percentage points contribution)	(0.2)	(1.3)	(0.8)	(▲ 2.4)	(1.4)	(1.4)	(0.1)	(1.1)	(0.9)	(0.8)	(0.6)	(0.6)
(Ref.) Public Demand (percentage points contribution)	(0.2)	(1.3)	(0.1)	(0.0)	(▲ 0.0)	(0.2)	(0.5)	(▲ 0.0)	(0.3)	(▲ 0.0)	(0.4)	(0.2)

	(% changes from the same quarter of the previous year)									(% changes from the previous fiscal year)		
	1 ~ 3	4 ~ 6	7 ~ 9	10 ~ 12	1 ~ 3	4 ~ 6	7 ~ 9	10 ~ 12	1 ~ 3			
Nominal G D P	1.1	1.3	2.0	1.7	1.1	1.3	1.1	1.3	1.2	0.5	1.5	1.2
GDP deflator	0.1	0.4	0.5	1.1	0.9	0.8	0.8	0.3	0.2	▲ 0.2	0.7	0.5
Consumer Price Index (excluding fresh food)	0.8	0.8	0.5	0.9	1.0	0.9	1.1	0.8	0.8	0.8	0.8	0.9
(excluding fresh food, consumption tax, education free of charge)	0.8	0.8	0.5	0.6	0.6	0.6	0.8	0.8	0.9	0.8	0.6	0.8
Unemployment Rate (%)	2.5	2.4	2.3	2.2	2.2	2.2	2.2	2.2	2.2	2.4	2.3	2.2
Exchange Rates (JY/US\$)	110	110	107	107	107	107	107	107	107	111	108	107
Import Price of Crude Oil (US\$/barrel)	63	72	66	65	66	67	68	68	68	72	67	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.