

# Monthly Report of Prospects for Japan's Economy

December 2019

Macro Economic Research Center  
Economics Department



The Japan Research Institute, Limited

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

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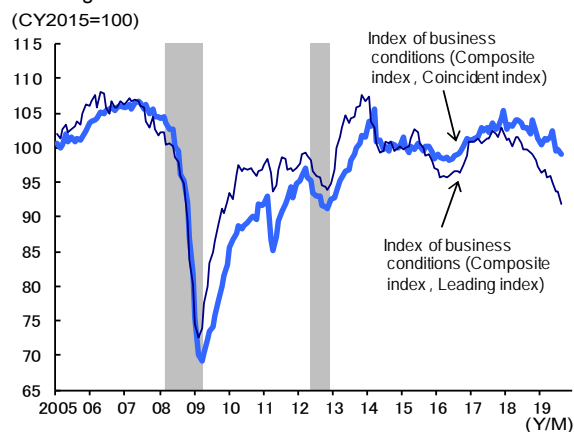
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# The General Situation of Japan's Economy – A Sense of Standstill Is Felt in Economic Activity

**Figure 1-1 Economic Activity**

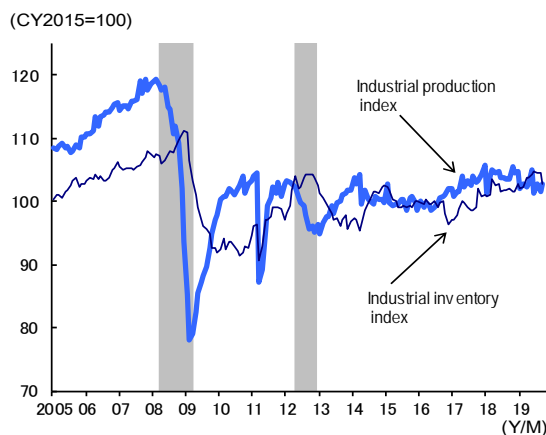
Indices of business conditions remained on a declining trend both in terms of the CI coincident index and the CI leading index.



Source: The Cabinet Office.

**Figure 1-2 The Corporate Sector**

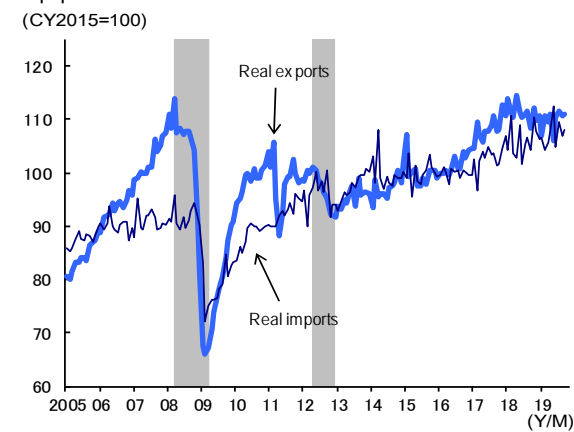
Industrial production was sluggish, mainly for producer goods and consumer goods.



Source: The Ministry of Economy, Trade and Industry.

**Figure 1-3 Overseas Demand**

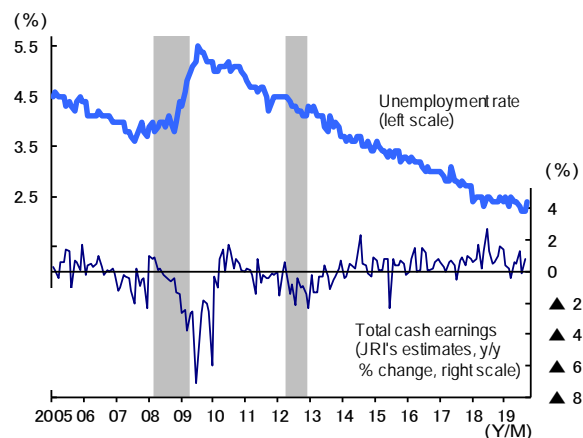
Exports, mainly to the United States, declined. Imports increased, particularly of chemical products and electrical equipment.



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.

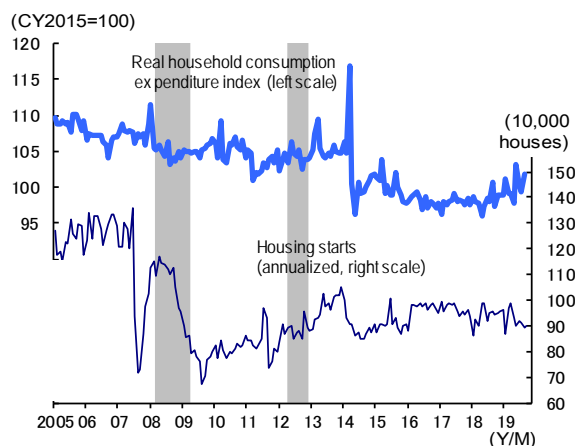


Source: The Ministry of Internal Affairs and Communications, The Ministry of Health, Labor and Welfare.

\* The shaded area indicates the recession phase.

**Figure 1-5 The Household Sector**

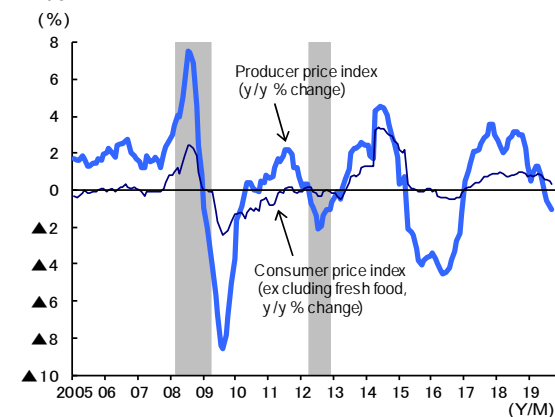
Real household consumption picked up, albeit with fluctuations. Housing starts saw a moderate decline.



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 of raw materials. The pace of increase in consumer prices has slowed down.



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 December 2019  
The Japan Research Institute, Limited

# Manufacturing Production Activities Remain Sluggish, While Nonmanufacturing Stays Firm

## ◆ Industrial Production Stalls

The Industrial Production Index for September increased for the first time in two months, up 1.7% from the previous month, while growth in producer goods and consumer goods remained subdued.

As for the outlook for production, it is difficult to expect a clear recovery, with the slowing down of growth in overseas demand and concerns about a decline in demand following the consumption tax rate hike weighing on production plans. Specifically, industrial production is forecast to increase by 0.6% month-over-month in October and to decrease by 1.2% in November.

## ◆ Public Investment Is on the Rise

Meanwhile, public investment is on an upward trend. Completed amount of public works is accelerating on the back of an increase in public works spending in

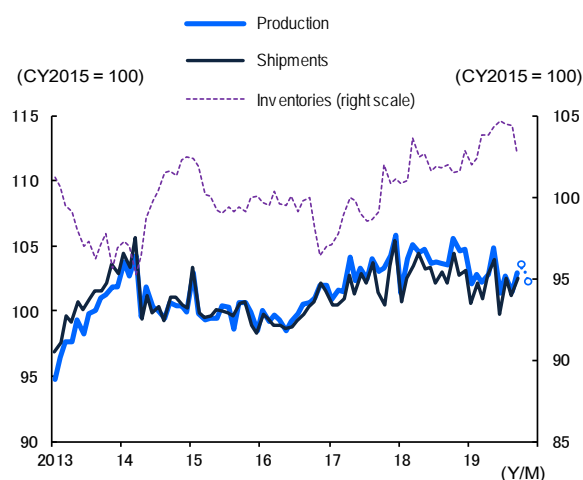
preparation for the economic downturn following the consumption tax rate hike. The contract amount for public works projects, which serves as a leading indicator, was up 4.6% year-on-year in September, recording an increase for the eighth straight month.

## ◆ Private Consumption Remains Firm

Amid an improvement in employment and income conditions, private consumption remained firm. The real consumption activity index (travel balance adjusted) in August increased by 3.2%, the first increase in two months.

In addition to a reaction to the decline in July due to the extended rainy season, a rush in demand prior to the consumption rate hike also contributed to boosting consumption. By goods, consumption increased for durable goods, such as air conditioners, as well as service goods mainly among food services.

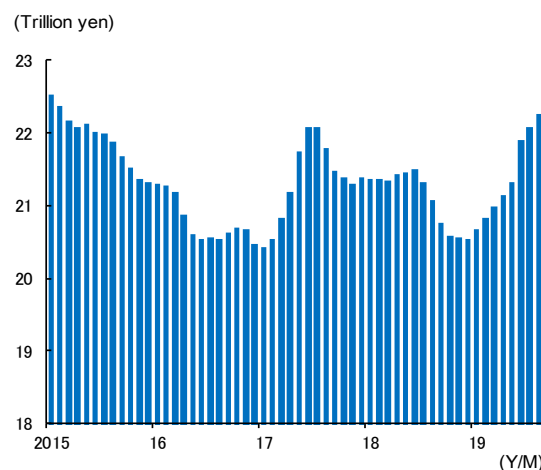
Figure 2-1 Industrial Production Index  
<seasonally adjusted>



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 October and November based on the production forecast index.

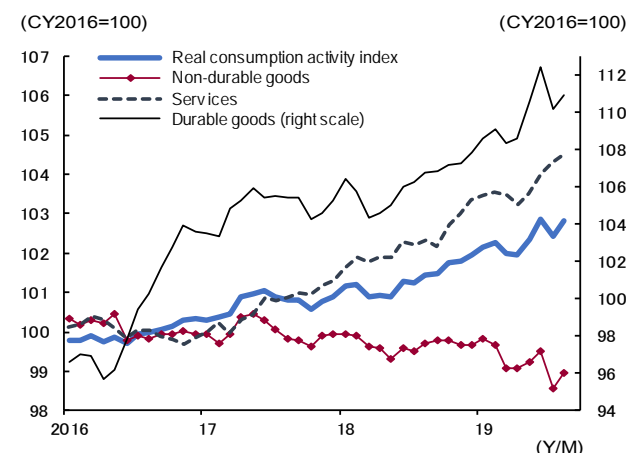
Figure 2-2 Completed Amount of Public Works  
<annualized, seasonally adjusted,  
3-month moving averages>



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

Note: Non-dwelling.

Figure 2-3 Real Consumption Activity Index  
<seasonally adjusted,  
3-month moving averages>



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

Note: Inbound consumption is adjusted.

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

# Exports Remain Lackluster

## ◆ Exports of Goods Continue to Stagnate

Exports of goods have been sluggish. Looking at exports by category, while exports of electronic parts and devices increased as global IT demand had bottomed out, exports of capital goods, mainly to Asia including China, continued to stagnate.

As for the 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.

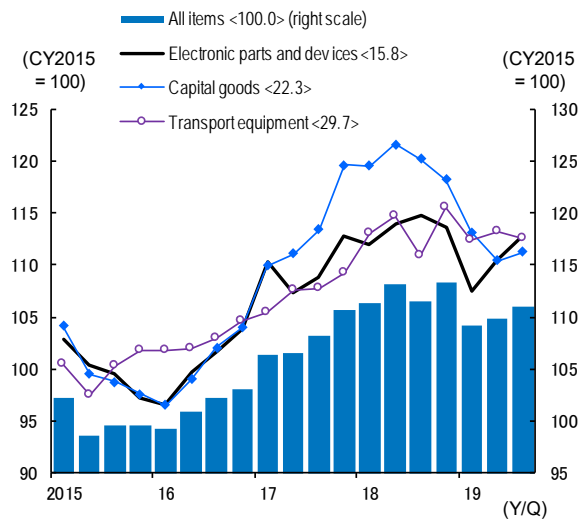
However, amid the lack of momentum for the global economy on the whole, a strong recovery of overall exports will be difficult to achieve.

## ◆ Demand Related to Inbound Tourism Declines

The number of tourists that visited Japan in September remained unchanged from the previous month. While the number of Korean tourists visiting Japan continued to decline against the backdrop of the deterioration in the relationship between Japan and Korea, the number of visitors from participating countries increased for Rugby World Cup 2019.

The number of Korean visitors to Japan is expected to remain low for the time being, while the number of foreign tourists visiting Japan may decline due to the damage caused by the typhoons and floods that hit Japan in October. Demand related to inbound tourism is expected to weaken again after November when demand from Rugby World Cup spectators runs its course.

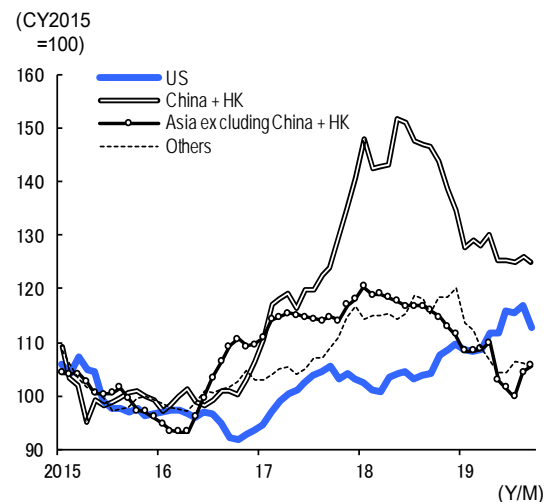
Figure 3-1 Real Exports by Item  
<seasonally adjusted>



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

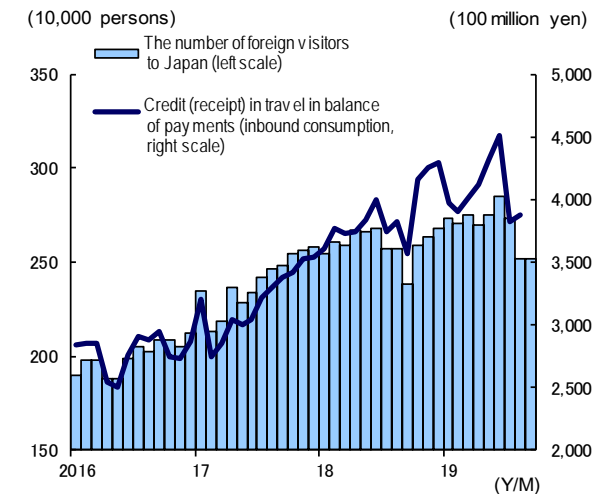
Note: Figures in the angled brackets show the shares in total nominal exports in CY2018.

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 December 2019  
The Japan Research Institute, Limited

# Business Fixed Investment Likely 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.

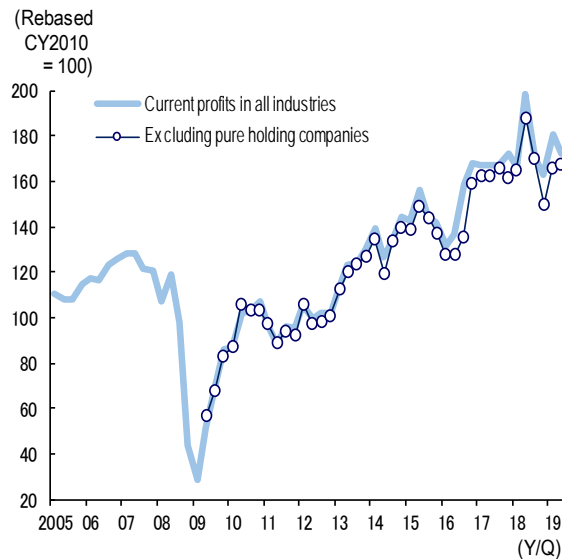
As for the outlook for corporate earnings, while sluggish growth in exports will exert downward pressure, overall corporate earnings are anticipated to remain at a high level backed by firm domestic demand.

## ◆ Business Fixed Investment Is Expected to 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.

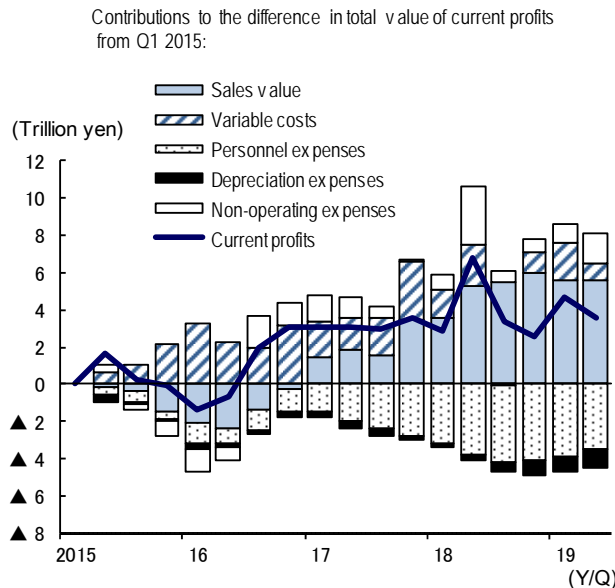
Figure 4-1 Current Profits of Japanese Corporations  
<seasonally adjusted>



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

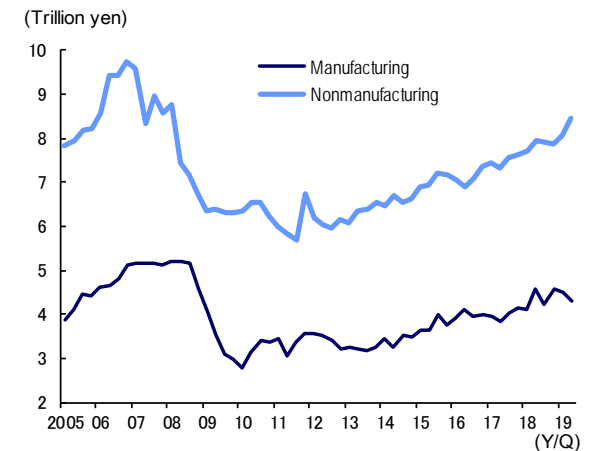
Note: All industries except for financial services and insurance.

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 December 2019  
The Japan Research Institute, Limited

# Income Is Expected to Increase Steadily

## ◆ The Income Situation Continues 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.

The number of new job openings in both the manufacturing and nonmanufacturing sectors remained at a high level, although labor demand in the manufacturing sector was somewhat weak against the background of the delayed recovery in external demand. In addition, 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.

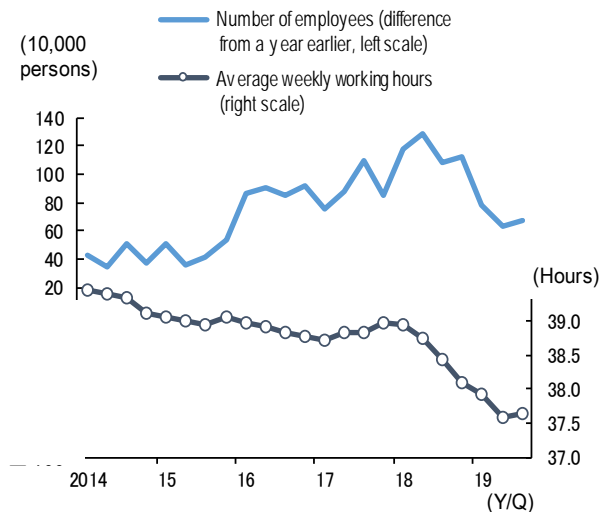
Meanwhile, on the wages front, nominal wages have remained on a rising trend. Excluding the effects of sample changes, the total sum of cash earnings of full-time

workers in August rose 1.1% from the previous year. Scheduled salaries remain on a rising trend driven by the implementation of pay scale increases, which has contributed to the upward trend in nominal wages.

## ◆ Real Income Is Likely to Increase Firmly

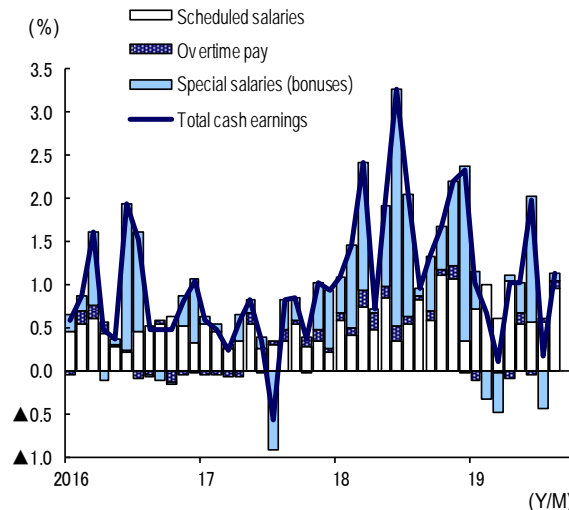
As for the future prospects, it shows a high likelihood that moderate growth in the number of employees will continue as a strong sense of labor shortage is still being felt by many industries. Nominal wages will likely remain on a steady rise given the tight labor supply/demand conditions. On the other 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 rate. 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



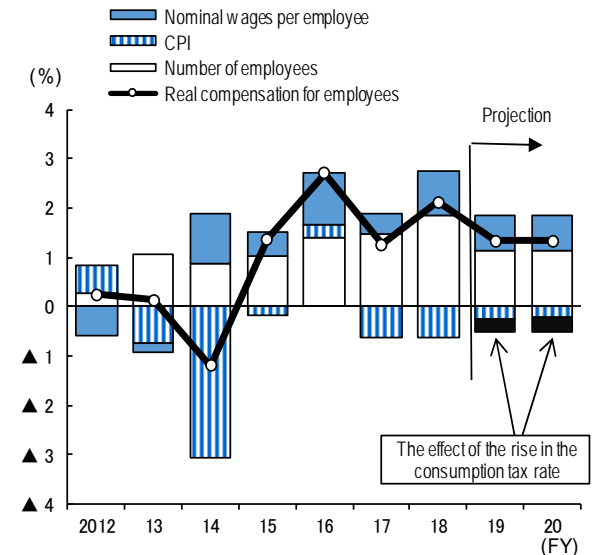
Source: The Japan Research Institute, Ltd. based on data of The Ministry of Internal Affairs and Communications.  
Note: The figures in average weekly working hours are 4-quarter moving averages.

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 December 2019  
The Japan Research Institute, Limited

# Private Consumption Expenditure Is Forecast to Recover Moderately

## ◆ Rush in Demand Appears to Have Been Limited

In September, Japan saw a rush in demand for durable consumer goods such as home appliances and automobiles as well as cosmetics and daily necessities ahead of the planned consumption tax rate hike. However, the rush in demand was concentrated in the month before the tax rate hike. On a quarterly basis, the growth rate appears to have been only half that of the previous tax increase.

As for the future prospects, a moderate recovery in private consumption expenditures is anticipated to continue.

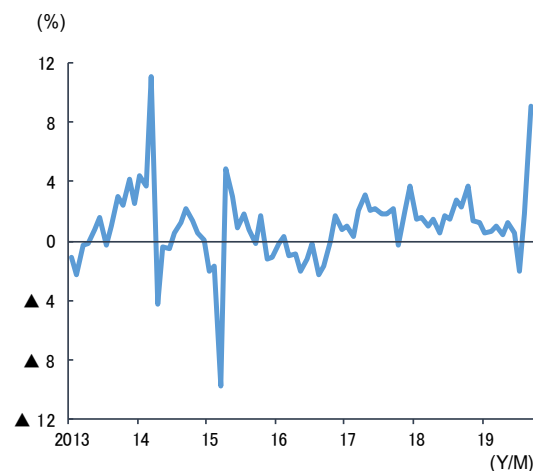
The negative effects of the hike in consumption tax rate will likely be mitigated significantly thanks to the measures to reduce tax burdens including the provision of free education on top of the solid growth in income driven by a serious labor shortage. Moreover, the recent rise in stock prices is expected to support personal expenditure by improving consumer sentiment.

## ◆ Housing Investment Sees a Moderate Decline

The number of housing starts in September increased for the first time in three months, up 0.7% month-over-month. The number of housing starts was boosted by an increase in construction of condominiums in line with redevelopment mainly in the urban areas. Meanwhile, the number of housing starts for owner-occupied and rental housing plunged for the third consecutive month.

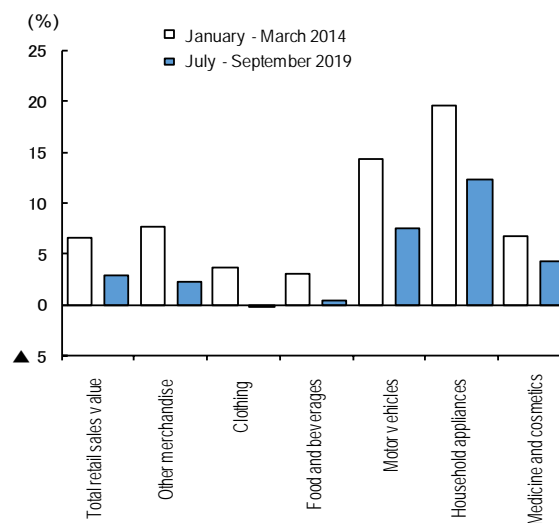
As for the future outlook, the number of housing starts for owner-occupied and subdivision detached housing, which had benefited from the rush in demand prior to the consumption tax rate hike, will likely remain on a diminishing trend going forward. Having said that, as the tax rate hike was smaller than the previous one and the government has implemented measures for levelling demand in line with the tax rate hike, the rise in rush demand was limited. For this reason, a sharp drop in the number of housing starts due to a backlash will likely be avoided.

Figure 6-1 Retail Sales Value  
<year-on-year % change>



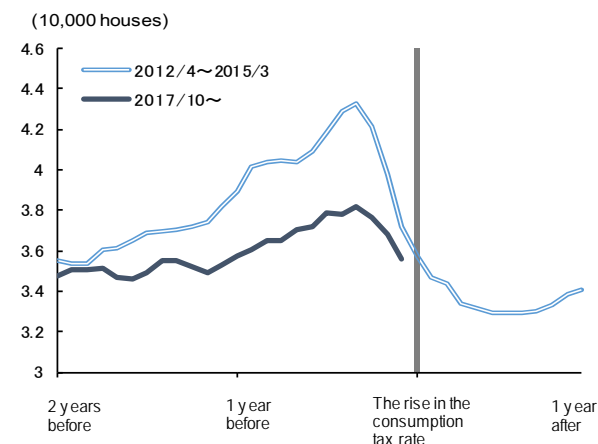
Source: The Japan Research Institute, Ltd. based on data of The Ministry of Economy, Trade and Industry.

Figure 6-2 Retail Sales Value by Item Just before the Consumption Tax Rise  
<year-on-year % change>



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

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: R&D Investment in the DX Related Field Is Expected to Expand

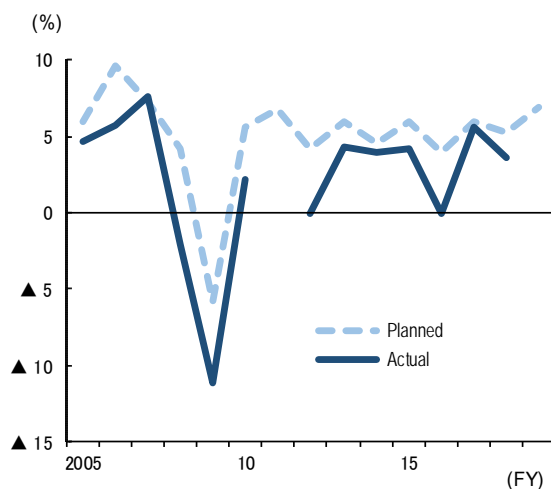
## ◆ DX Is Leading R&D Investment

At present, R&D expenditures by companies are steadily increasing. This is attributable to the fact that companies are actively investing in research and development related to DX (digital transformation: creating new businesses using digital technologies). In fact, R&D expenditures in the information and communications (IT) sector have been on the rise since fiscal 2016. Although there has been a headwind of shrinking R&D spending for information and communications equipment due to a decline in the competitiveness of smartphones among other products, R&D investment in the IT field has been actively promoted by other industries towards the realization of DX. Companies in a wide range of industries have been promoting DX including such areas as transportation machinery (automated driving) and machine tools (smart plants).

## ◆ Further Expansion Is Anticipated

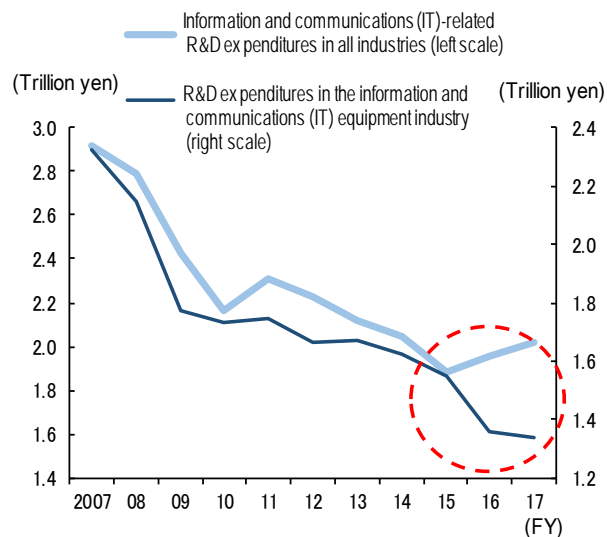
Corporate R&D spending is expected to continue rising for the time being. Given that companies with a strong sense of crisis about future environmental changes tend to increase R&D expenditures, it is likely that more companies will boost their R&D investment, especially in the DX related field, in order to survive as the business environment surrounding them changes more rapidly. In addition, the fact that companies have increased the number of researchers hired in recent years can also be evaluated as a positive attitude toward strengthening research and development over the medium to long term. An increase in R&D expenditures, including capital investment, will contribute to boosting GDP and will become an important growth engine for Japan.

Figure 7-1 Plans and Actual Results of R&D Expenditures in Large Enterprises  
<year-on-year % change>



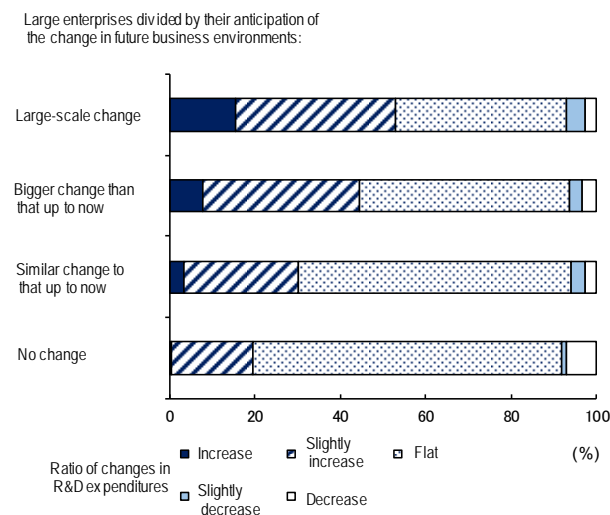
Source: The Japan Research Institute, Ltd. based on data of The Development Bank of Japan, Inc.  
Note: Enterprises capitalized at one billion yen or more.

Figure 7-2 Information and Communications (IT) - related R&D Expenditures



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

Figure 7-3 Correlation between Anticipation of Business Environments and Change in R&D Expenditures



Source: The Japan Research Institute, Ltd. based on data of The Ministry of Economy, Trade and Industry.  
Note: The survey was conducted as of December 2018.

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

### ◆ Mild Recovery of the Japanese Economy Is Predicted to Continue, Driven by Domestic Demand

(1) Japan's real GDP for the July-September 2019 period increased by 0.2% on an annualized quarter-on-quarter change basis (up 0.1% from the preceding quarter), achieving positive growth for the fourth consecutive quarter. However, growth slowed considerably from the April-June period, which recorded positive growth of 1.8% on an annualized quarter-on-quarter change basis. The main factors behind the slowing were a decline in service exports due to a fall in the number of Korean tourists visiting Japan and a decrease in inventory investment.

Meanwhile, final demand in Japan remained firm. Consumer spending rose for the second straight quarter on the back of rush demand ahead of the consumption tax rate hike. Capital investment also grew at a high rate. Declines in inventory investment amid an increase in final demand suggest that companies are making progress in inventory adjustment, giving a positive outlook to the economy.

(2) As for future prospects, a sense of economic slowdown is likely to strengthen over a short term as a pullback in demand and a decline in households' purchasing power following the tax rate hike weigh on economic activity. The real GDP growth for the October-December period is expected to be negative for the first time in five quarters.

(3) However, a serious drop in personal consumption, similar to that after the 2014 tax rate hike, is expected to be avoided. As the surge in demand ahead of the tax rate hike was limited, it is unlikely that a sharp drop in demand will occur due to the backlash as it did with the previous tax increase. The number of employees continues to increase and the household income situation is improving steadily. Consumption is thus expected to return to a moderate uptrend as the pullback from the rush in demand comes to an end.

(4) Capital investment is also expected to continue to rise due to strong demand for capital investment stemming from structural factors, such as labor-saving investment on the back of labor shortages and workstyle reforms, replacement of aging facilities and equipment and investment in labor-saving measures to utilize new technologies. Although uncertainty in overseas economies remains strong, the fact that the decline in exports has come to a halt against the backdrop of a recovery in the global semiconductor market also has a positive effect on investment sentiment in the manufacturing sector.

(5) Consequently, Japan's economy is forecast to return to a moderate recovery path from the beginning of 2020. With the growth rate expected to be +0.8% for FY2019 and +0.7% for FY2020, solid growth is anticipated to continue despite the negative influence of the consumption tax rate hike.

### ◆ The Rate of Increase Year-on-year in the Core CPI Will Likely Narrow

(6) In September, core CPI growth slowed mainly because the pace of decline in energy prices accelerated. As for future prospects, although upward pressure from the supply-demand side is expected to strengthen, the extent of decline in energy prices is predicted to widen. As a result, the year-on-year increase rate in the core CPI will likely remain at around the mid-0% level, 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 November 14, 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)	(Actual)	(Projection)	(Actual)	(Actual)	(Actual)	(Actual)	(Projection)	(Actual)	(Projection)	(Projection)
Real G D P	2.0	1.8	0.2	▲ 1.9	1.3	1.6	0.7	0.6	1.2	0.7	0.8	0.7
Private Consumption Expenditure	▲ 0.1	2.4	1.4	▲ 4.6	2.6	2.3	▲ 0.8	1.4	1.0	0.4	0.6	0.6
Housing Investment	4.3	2.0	5.7	▲ 5.6	▲ 3.1	▲ 1.5	0.2	1.3	0.8	▲ 4.3	2.1	▲ 1.1
Business Fixed Investment	▲ 1.5	2.8	3.5	▲ 2.1	1.4	2.1	1.8	1.8	2.1	3.5	1.6	1.5
Private Inventories (percentage points contribution)	( 0.3)	(▲ 0.2)	(▲ 1.2)	( 0.0)	( 0.2)	( 0.1)	( 0.0)	( 0.0)	( 0.0)	( 0.1)	(▲ 0.2)	(▲ 0.0)
Government Consumption Expenditure	▲ 0.1	4.8	2.2	0.0	0.2	1.0	2.2	▲ 0.5	1.0	0.9	2.0	0.8
Public Investment	7.4	8.8	3.4	2.5	1.2	▲ 2.8	▲ 1.2	1.6	1.3	▲ 4.0	3.6	0.0
Net Exports (percentage points contribution)	( 1.6)	(▲ 1.2)	(▲ 0.6)	( 1.2)	(▲ 0.6)	(▲ 0.1)	( 0.5)	(▲ 0.5)	( 0.1)	(▲ 0.1)	(▲ 0.3)	( 0.0)
Exports of Goods and Services	▲ 7.9	2.0	▲ 2.6	4.9	▲ 1.2	2.3	3.3	▲ 1.2	2.0	1.6	▲ 0.9	1.4
Imports of Goods and Services	▲ 15.6	8.8	0.9	▲ 1.9	2.1	2.9	0.3	1.4	1.6	2.2	0.5	1.3
(Ref.) Domestic Private Demand (percentage points contribution)	( 0.1)	( 1.6)	( 0.3)	(▲ 3.1)	( 1.8)	( 1.7)	(▲ 0.1)	( 1.1)	( 0.9)	( 0.8)	( 0.5)	( 0.5)
(Ref.) Public Demand (percentage points contribution)	( 0.3)	( 1.3)	( 0.6)	( 0.1)	( 0.1)	( 0.1)	( 0.4)	(▲ 0.0)	( 0.3)	(▲ 0.0)	( 0.6)	( 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	FY2018	FY2019	FY2020
Nominal G D P	1.1	1.3	1.9	1.9	1.2	1.2	1.1	1.1	1.3	0.5	1.6	1.2
GDP deflator	0.1	0.4	0.6	1.3	0.9	0.8	0.7	0.1	0.3	▲ 0.2	0.8	0.5
Consumer Price Index (excluding fresh food)	0.8	0.8	0.5	0.8	0.9	0.8	1.0	0.7	0.8	0.8	0.7	0.8
(excluding fresh food, consumption tax, education free of charge)	0.8	0.8	0.5	0.4	0.5	0.5	0.7	0.8	0.9	0.8	0.5	0.7
Unemployment Rate (%)	2.5	2.4	2.3	2.3	2.3	2.2	2.2	2.2	2.2	2.4	2.3	2.2
Exchange Rates (JY/US\$)	110	110	107	108	108	108	108	108	108	111	108	108
Import Price of Crude Oil (US\$/barrel)	63	72	66	63	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.