

Monthly Report of Prospects for Japan's Economy

October 2020

Macro Economic Research Center
Economics Department



The Japan Research Institute, Limited

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

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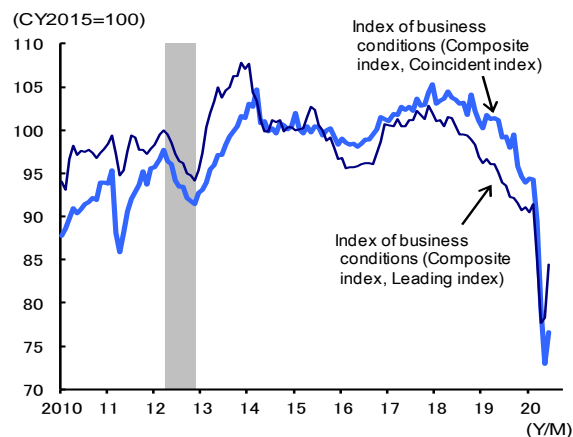
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The General Situation – Signs of Economic Recovery Have Been Seen

Figure 1-1 Economic Activity

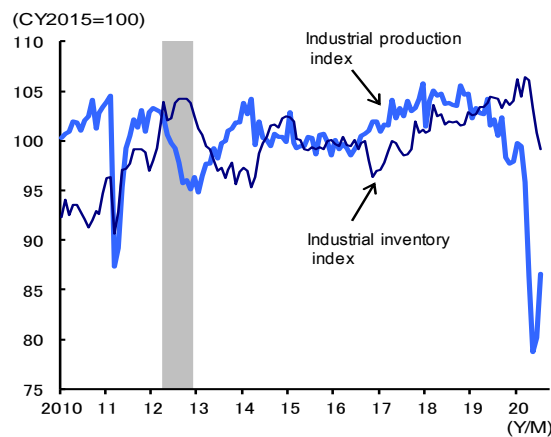
Indices of business conditions rose both in terms of the CI coincident index and the CI leading index.



Source: The Cabinet Office.

Figure 1-2 The Corporate Sector

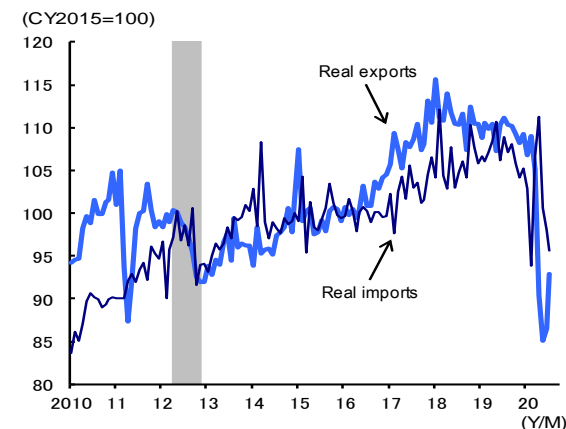
The industrial production index saw a significant rise on the back of increased production in a wide range of industries, particularly that of automobiles.



Source: The Ministry of Economy, Trade and Industry.

Figure 1-3 Overseas Demand

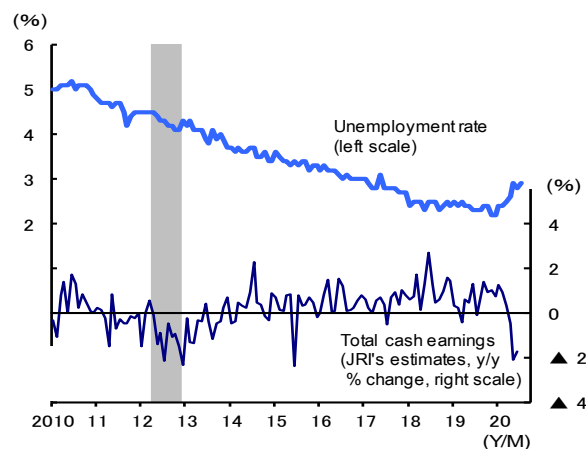
Exports increased, mainly those to the United States. Imports saw a decrease for crude oil and natural gas.



Source: The Bank of Japan.

Figure 1-4 Employment and Income

The unemployment rate rose once again. Nominal wages declined mainly for non-scheduled salaries (overtime pay).

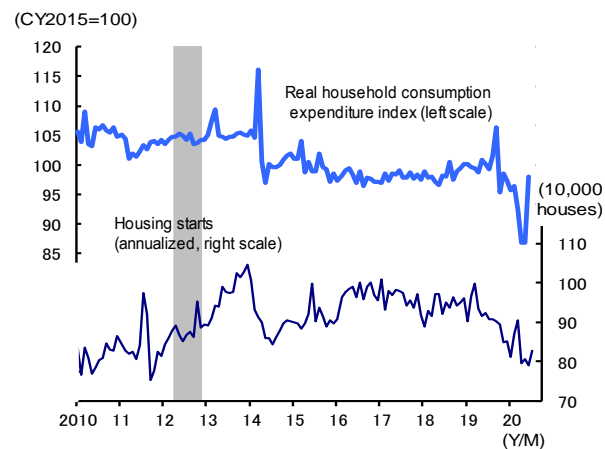


Source: The Ministry of Internal Affairs and Communications, The Ministry of Health, Labor and Welfare.

* The shaded area indicates the recession phase.

Figure 1-5 The Household Sector

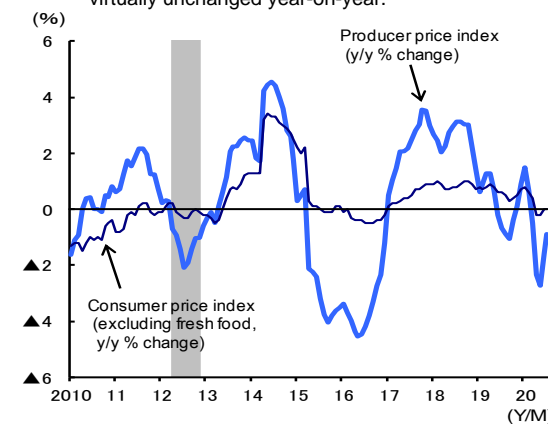
Real household consumption increased due to a reaction to voluntary restraints, among other factors. Housing starts were sluggish.



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

Figure 1-6 Prices

The decline in producer prices for petroleum and coal products slowed. Consumer prices remained virtually unchanged year-on-year.



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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Signs of a Rebound Were Witnessed in Exports and Production

◆ The April-June Period Saw Significant Negative Growth

Japan's real GDP (2nd preliminary report) for the April-June 2020 period declined 28.1% on an annualized quarter-on-quarter basis, surpassing the decline immediately after the collapse of Lehman Brothers. Personal consumption dropped substantially by 28.2% on an annualized quarter-on-quarter basis, reflecting voluntary restraints on outings following the declaration of a state of emergency by the government. Looking at external demand, exports plummeted by 56.0% on an annualized quarter-on-quarter basis against the backdrop of stagnant economic activities in the United States and Europe in addition to the loss of demand related to inbound tourism.

◆ Industrial Production Increased Due to the Bottoming out of Exports

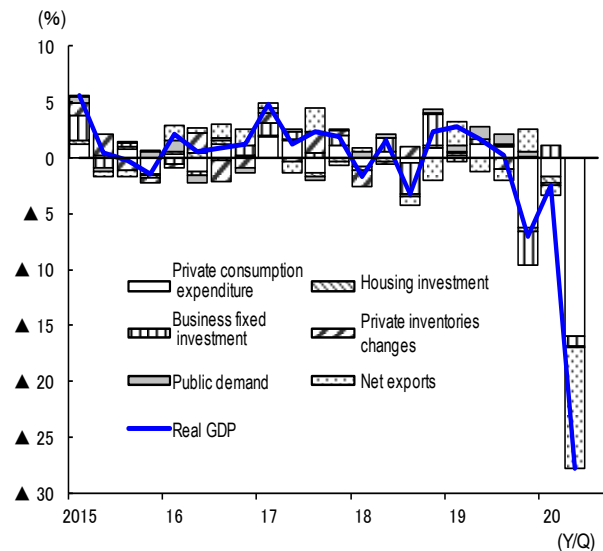
Despite the foregoing, there have been signs of recovery. Real exports in July rose 3.0% from the previous month. By region, shipments to China recovered almost to the levels seen before the outbreak of the novel coronavirus, while those to the

United States increased sharply, mainly for transport machinery.

In response to a recovery in exports, corporate production activities have shifted toward increased production. The industrial production index for July rose sharply by 8.7% from the previous month. Production increased in a wide range of industries, mainly in the automobile and parts industries. Looking at future production plans, industrial production is forecast to remain on a recovery path, up 4.0% month-over-month in August and up 1.9% month-over-month in September.

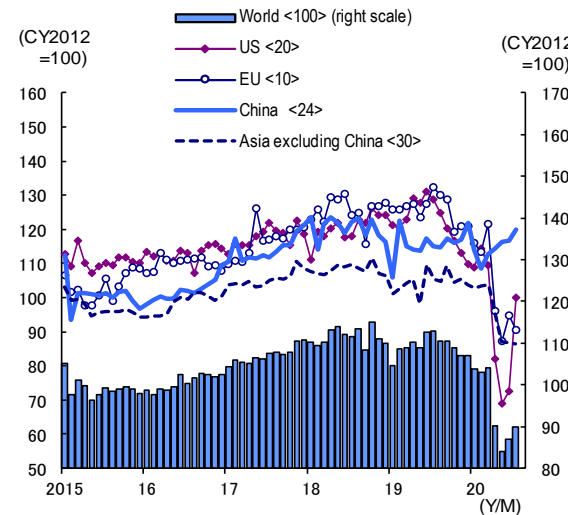
Personal consumption also recovered following the lifting of the state of emergency by the government. The consumer activity index rose 8.6% month-over-month in June, the first rise in seven months. By item, durable goods, such as furniture, increased, while service consumption, mainly in the food service sector, stopped declining. However, since July, the recovery seems to have paused due to a second wave of coronavirus infections.

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



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

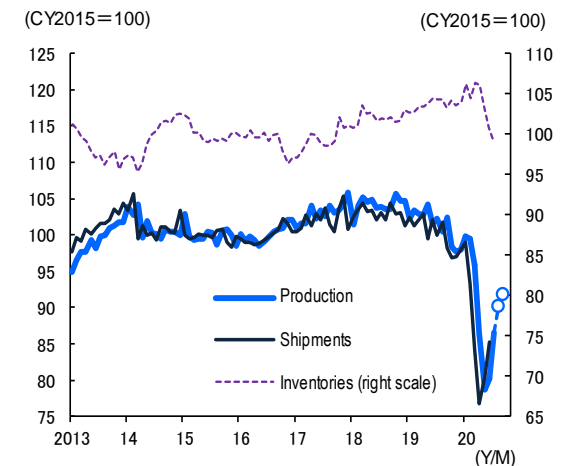
Figure 2-2 Real Exports by Destination
<seasonally adjusted>



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 CY2019.

Figure 2-3 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 August and September 2020 based on the production forecast index.

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The Decline in Goods Exports Has Come to a Halt, While Demand Related to Inbound Tourism Remained Virtually Nonexistent

◆ Goods Exports Have Picked up, Mainly for Transportation Machinery

Goods exports in July increased 3.0% from the previous month, recording the second consecutive month of rise. By item, shipments of transportation equipment continued to recover on the back of a recovery in global automobile sales, while those of capital goods, electronic parts and devices stopped declining.

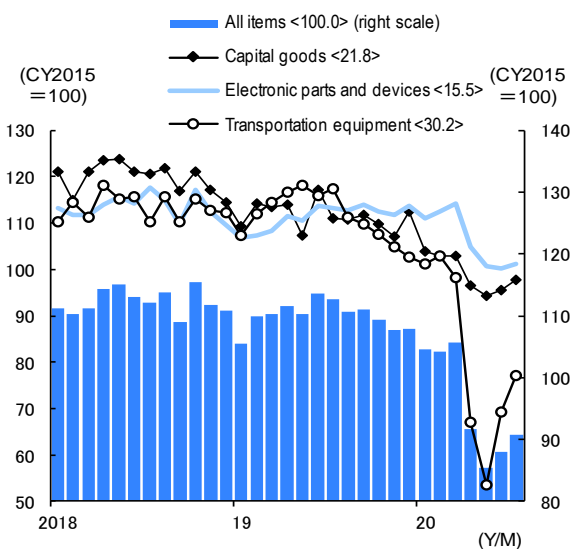
As for future prospects, exports are expected to remain on a recovery trajectory as the resumption of economic activity around the world exerts positive effects. However, as the global economic recovery is expected to remain slow due to the prolonged impact of the novel coronavirus, exports will be unlikely to return to the levels seen before the coronavirus outbreak until 2022.

◆ Demand Related to Inbound Tourism Was Almost Zero

Amid restrictions on overseas travel around the world, the number of tourists that visited Japan in July fell 99.9% on a year-on-year basis.

Although the Japanese government has started to ease some immigration restrictions, demand related to inbound tourism is expected to remain virtually nonexistent, as the easing of restrictions will be limited to business trips for the time being. In addition, the pace of recovery is anticipated to be moderate, as people will likely continue to refrain from overseas travel due to concerns over infection risks even if the restrictions on tourists are relaxed. In fact, the International Civil Aviation Organization (ICAO) predicts that even based on a scenario in which the number of international passengers picks up after July, the number will only recover to one-quarter of the previous year's level in September and about 40% in December.

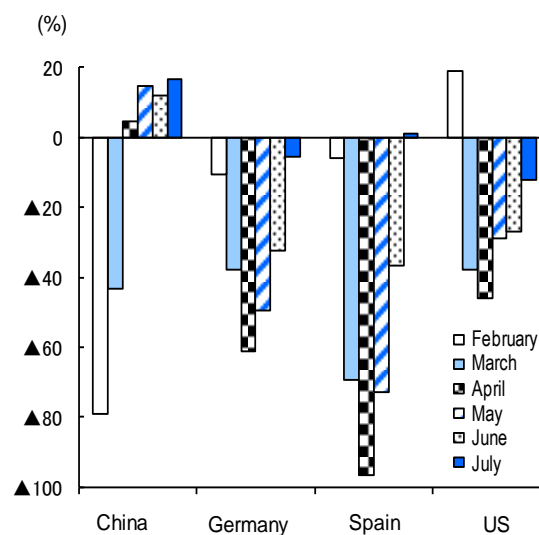
Figure 3-1 Real Exports by Item
<seasonally adjusted>



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

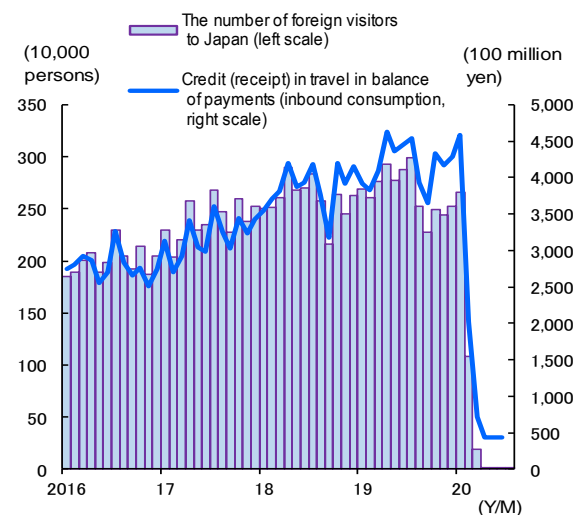
Note: Figures in the angled brackets show the shares in total nominal exports in CY2019.

Figure 3-2 New Car Sales by Country
<year-on-year % change>



Source: The Japan Research Institute, Ltd. based on data of European Automobile Manufacturers' Association and so on.

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).

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Business Fixed Investment Has Declined as Corporate Earnings Deteriorate

◆ Corporate Earnings Recorded their Biggest Ever Drop

In the April-June period, sales on an industry-wide basis fell 10.7% from the previous quarter, recording the biggest ever drop since statistics began. Sales in both manufacturing and nonmanufacturing industries declined substantially due to a sharp drop in domestic and overseas demand caused by the global outbreak of the novel coronavirus. In the manufacturing sector, sales of mainstay transportation machinery declined drastically due to a sharp drop in automobile sales at home and abroad. In the nonmanufacturing sector, sales dropped in a wide range of industries, including retail, services and transportation, following the declaration of a state of emergency by the government. Meanwhile, current profits were down 29.7% from the previous quarter, falling for the fifth consecutive quarter. Industries including food services, accommodation, living-related and entertainment services, and transportation services, all of which had been hit hard by the voluntary restraint on outings, have fallen into the red.

Corporate earnings for the July-September period are expected to pick up on the

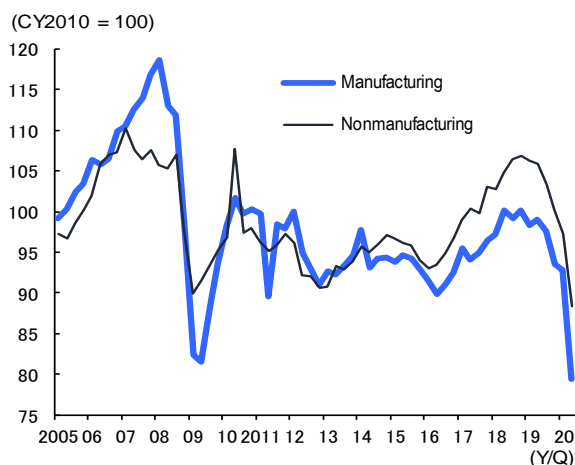
back of the easing of restrictions on business activities both in Japan and overseas. However, the pace of recovery will likely remain moderate as the recovery of overseas economies has been slow and measures to prevent coronavirus infection, including the avoidance of the “Three Cs (closed places, crowded places and close contacts),” will continue to be required in Japan.

◆ Business Fixed Investment Fell Again

In the April-June period, capital investment on an industry-wide basis fell 6.7% from the previous quarter, recording the first decline in two quarters. Companies have postponed or suspended nonessential or nonurgent capital investment due to deteriorating business performance and uncertainty over the future. However, capital investment was partly underpinned by the investment aimed at preventing the spread of coronavirus infection, such as investment related to teleworking.

As for future prospects, business fixed investment is expected to recover moderately, lagging the recovery of corporate earnings, although the prolonged impact of the coronavirus pandemic will likely continue to weigh on the recovery.

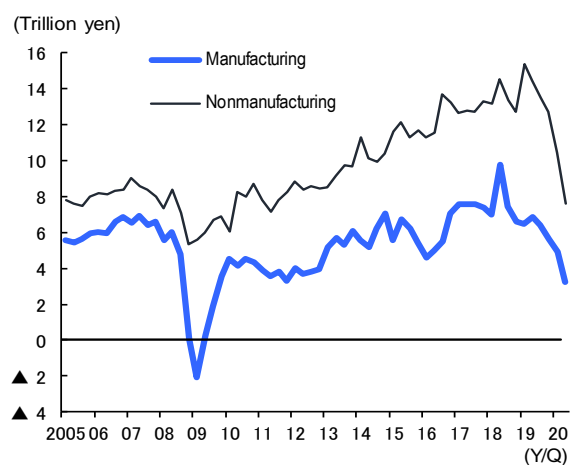
Figure 4-1 Sales Value of Japanese Corporations by Type
<seasonally adjusted>



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

Note: All industries except for financial services and insurance.

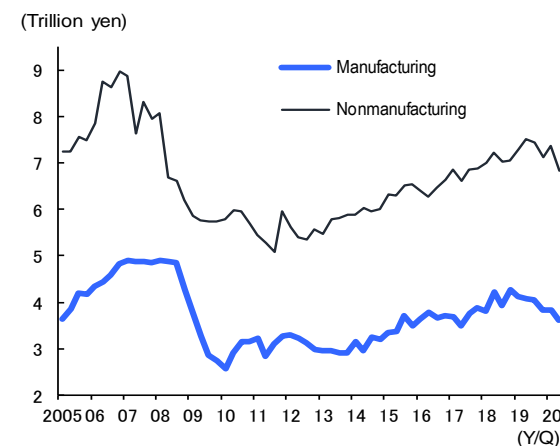
Figure 4-2 Current Profits of Japanese Corporations by Type
<seasonally adjusted>



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 4-3 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 Unemployment Rate Is Expected to Rise to Nearly 4% at Least Toward Year-End

◆ Corporate Appetite for Hiring Has Declined

The ratio of active job openings to applicants was 1.08 in July, down 0.41 points from the beginning of the year and the lowest level since April 2014. The number of active job openings has decreased around 20% during the same period, indicating a decline in the corporate appetite for hiring.

Meanwhile, looking at the number of workers in July, those on furlough, which had temporarily increased by 4 million, declined to a level virtually equivalent to that in the previous year. In line with this, the drop in the number of workers at work has also become smaller. This suggests that many employees on temporary leave or leaves of absence went back to their workplaces upon the resumption of economic activity in earnest.

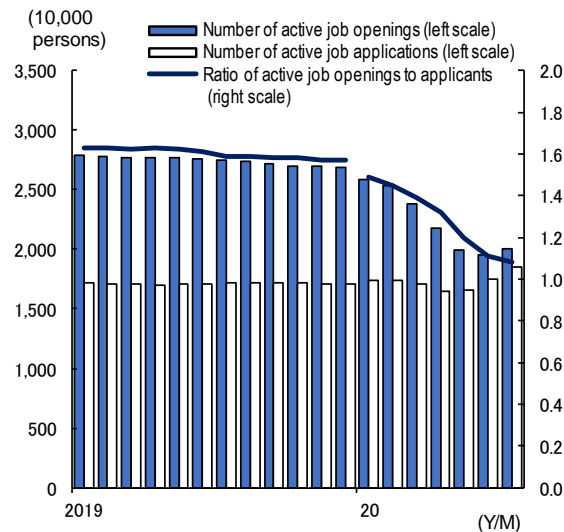
While the number of workers has diminished by 760,000 on a year-on-year basis, which is around 1% of the total number of workers, a sense of excessive workforce among enterprises has risen rapidly as sales decline. It is inevitable that more

companies will move toward cutting back on employment in the future as they become more aware of the prolonged impact of the novel coronavirus. Judging from the correlation with the employment conditions DI in the BOJ Tankan Survey, the unemployment rate will likely rise to nearly 4% at least, its highest level since 2013, by the end of the year.

◆ Total Cash Earnings Saw a Decline

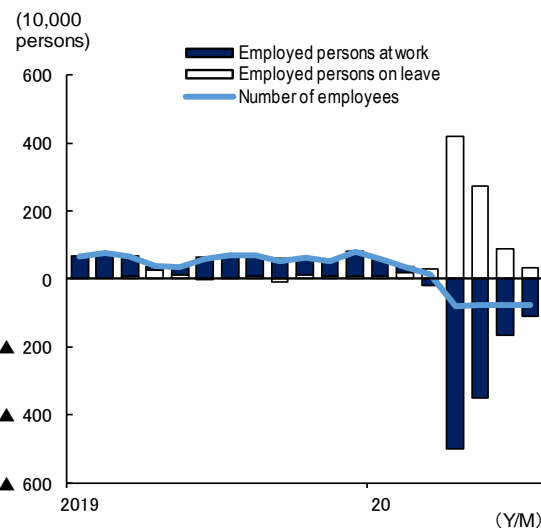
The novel coronavirus has also had ripple effects on wages. Total cash earnings in June plunged 1.7% year-on-year, recording a year-on-year decline for the third consecutive month. Against the backdrop of a decline in overtime due to sluggish economic activity, non-scheduled salaries (overtime pay) declined significantly. In addition, special salaries (bonuses) also saw a decrease reflecting the deterioration of the corporate earnings environment. It is also anticipated that downward pressure on scheduled salaries will increase going forward.

Figure 5-1 Ratio of Active Job Openings to Applicants
<seasonally adjusted>



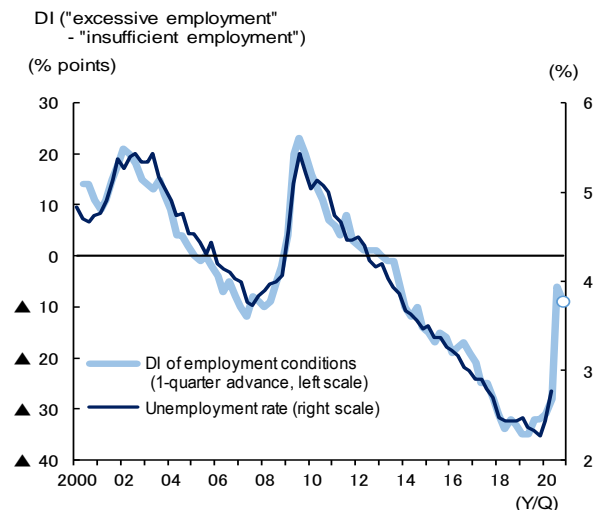
Source: The Japan Research Institute, Ltd. based on data of The Ministry of Health, Labor and Welfare.

Figure 5-2 Number of Employees by Type <difference from a year earlier>



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

Figure 5-3 Tankan DI of Employment Conditions and Unemployment Rate



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

Note: The latest figure of the DI is a forecast.

Rebound in Private Consumption Seems to Have Paused

◆ Recovery of Consumption Remains at Standstill

While private consumption had been picking up for some time following the lifting of the state of emergency, the recovery has leveled off since the beginning of the summer as pent-up demand subsequent to the self-restraint period has run its course and the number of new coronavirus cases started to increase once again. Retail sales in July fell 2.8% year-on-year, showing an accelerated decline compared with the previous month (down 1.3% year-on-year). In addition, the consumer confidence index began to decline again in August, indicating a lull in the improvement of consumer sentiment.

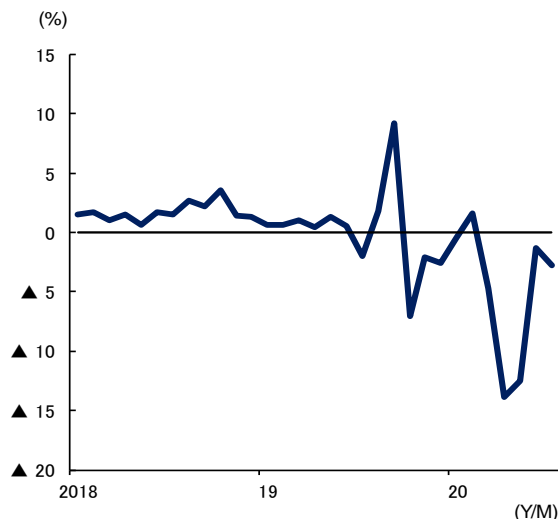
Given the above, the pace of recovery in personal consumption is expected to remain moderate. This is due primarily to the lingering tendency toward self-restraint. The number of people at retail and entertainment facilities remains about 90% of that before the outbreak of the novel coronavirus, which indicates that it will take some time for consumption activities involving outings to be normalized. In addition, the

deterioration of employment and income conditions, such as the rise in the unemployment rate, is anticipated to exert downward pressure on the recovery of consumption. Based on such circumstances, private spending is highly likely to remain at a level below before the outbreak of the novel coronavirus even through FY2021.

◆ Housing Investment Is Expected to Continue Declining for the Foreseeable Future

The environment surrounding the housing market will likely remain harsh due to voluntary restraint on outings and the worsening employment and income environment. Taking into account the correlation between the housing DI in the Economy Watchers Survey and the number of housing starts, the number of housing starts is expected to temporarily drop to around 600,000-700,000 on an annualized basis in the second half of the year.

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



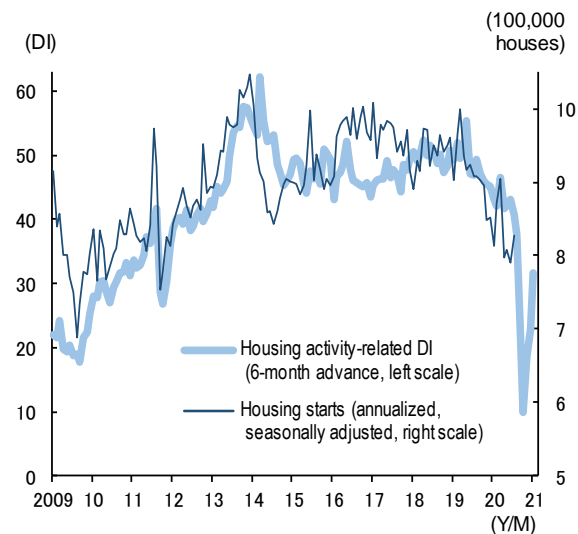
Source: The Japan Research Institute, Ltd. based on data of The Ministry of Economy, Trade and Industry.

Figure 6-2 Consumer Confidence Index
<seasonally adjusted>



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

Figure 6-3 Economy Watchers Survey
and Housing Starts



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

Topic: Consumption Behavior Changes amid the Outbreak of the Novel Coronavirus

◆ More Hours at Home Has Changed Consumption Trends

Since the outbreak of the novel coronavirus, household consumption behavior has changed significantly due to an increase in the amount of time people spend at home. Specifically, the following two changes can be pointed out.

First, the shift from brick-and-mortar stores to online stores is accelerating. Since March, when the novel coronavirus was recognized as a global pandemic, the percentage of households which use online shops has risen from around 40% to nearly 50%. The shift to online services has also expanded into services consumption, with more businesses, such as gyms and restaurants, offering services or taking orders online.

The second is the rise of nesting consumption. Looking at household spending after the outbreak of the novel coronavirus by item, spending increased on items,

such as study desks, chairs, and game software, that enhance the work and living environments at home. On the other hand, sales of business suits and cosmetics fell sharply due to a decline in opportunities to go out.

◆ Changes Will Likely Persist Even After the Spread of the Novel Coronavirus Settles down

The increase in the number of hours people spend at home reflects the increased use of teleworking. Since telework reduces office expenses and improves the work-life balance of employees, there are a considerable number of companies that intend to continue using telework even after the spread of the novel coronavirus settles down. The change in consumption behavior is expected to continue, as it is unlikely that the amount of time people spend at home will decrease to the level before the outbreak of the novel coronavirus, given the establishment of teleworking.

Figure 7-1 Number of Hours People Spend at Home
<on a nationwide basis>

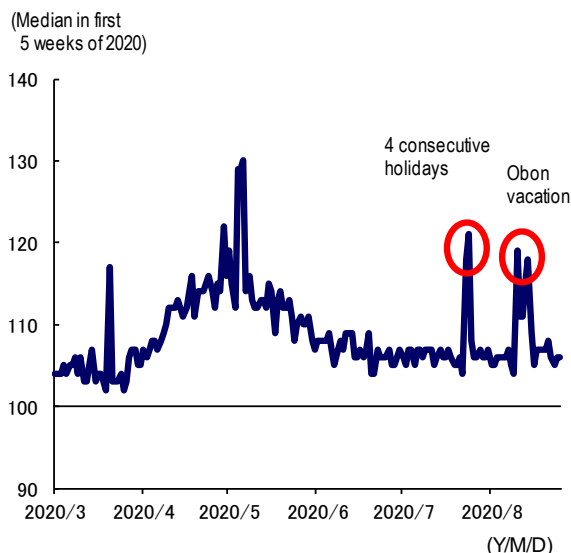


Figure 7-2 Percentage of Households which Use Online Shops
<seasonally adjusted>

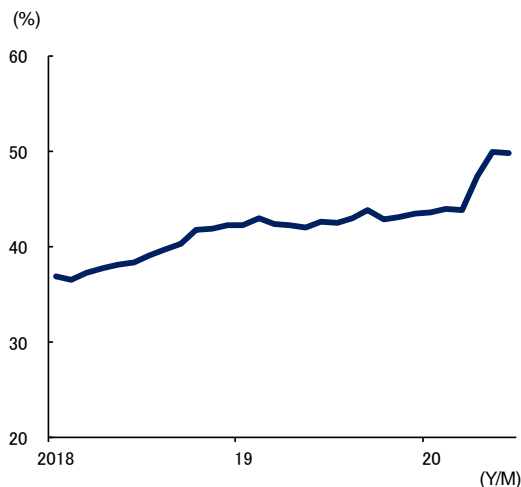
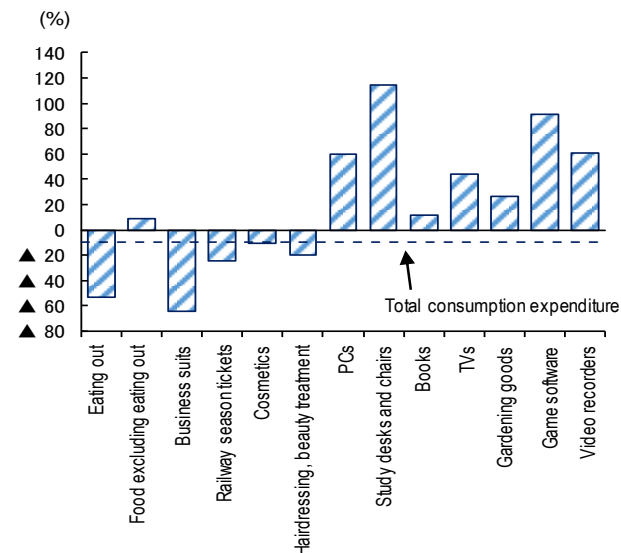


Figure 7-3 Consumption Expenditure by Item
<year-on-year % change>



Prospects for Japan's Economy - Projected Real GDP Change; -5.4% for FY2020 and 3.4% for FY2021

◆ Japan Will See a Negative Growth Rate of Minus 5.4% for FY2020 and Will Not Return to Its Pre-coronavirus Growth Level Until After 2022

- (1) According to the Second Preliminary Quarterly Estimates of GDP (2nd QE), Japan's real GDP growth rate for the April-June 2020 period was -28.1% on an annualized quarter-on-quarter change basis (down 7.9% from the preceding quarter), virtually unchanged from the First Preliminary Quarterly Estimates of GDP (1st QE) (-27.8% on an annualized quarter-on-quarter change basis; down 7.8% from the preceding quarter). Looking at the revisions by demand item, however, inventory investment has been revised upward significantly, indicating that corporate inventories are increasing due to a sharp drop in demand. In addition, capital investment has been revised downward, showing a sharp decline in the economy due to the impact of the novel coronavirus.
- (2) Looking ahead, the level of economic activity since summer has been on a recovery trend due to the lifting of the state of emergency, and the growth rate in the July-September period is likely to be positive, with an annual growth rate of over 10%. However, the pace of economic recovery is expected to remain moderate, as the number of coronavirus infections started to increase once again, recovering around 40% of the decline in GDP that occurred in the first half of the year.
- (3) By demand item, trade activities related to exports will likely take time to rebound, as the resumption of economic activity remains slow in various countries. In addition, demand related to inbound tourism will remain virtually nonexistent for the time being due to ongoing border restrictions in an effort to avoid another wave of coronavirus.
- (4) Meanwhile, in terms of domestic demand, the recovery of personal consumption is expected to be hampered by deteriorating employment income conditions, on top of the lingering tendency toward self-restraint. The unemployment rate is likely to rise

to close to 4% at least by the end of the year, as companies are increasingly feeling employment surpluses due to the effects of declining demand. It is projected that personal consumption will remain below the level before the outbreak of the novel coronavirus for a long period of time, as downward pressure on wages, especially winter bonuses, is expected to intensify against the backdrop of deteriorating corporate earnings.

- (5) Due to the foregoing, Japan will likely see negative growth for FY2020 at a rate of minus 5.4%. While the growth rate for FY2021 is expected to turn positive at +3.4%, the pace of recovery will be slow, and it is forecast that economic activity will not recover to the level before the outbreak of the novel coronavirus until after 2022.

◆ Prices Have Been Declining

- (6) In July, core CPI (excluding the impact of the increase in the consumption tax rate and the provision of free education) diminished 0.3% year-on-year, unchanged from the previous month. While the resumption of weekend and holiday discounts on expressways tolls contributed to the decline, downward pressure from falling energy prices decreased.

As for the future outlook, downward pressure on prices from the viewpoint of supply and demand will likely intensify. Furthermore, as the trend of falling energy prices will likely continue for the foreseeable future, reflecting the year-on-year decline in crude oil prices, the decline in core CPI is expected to expand once again toward year-end.

Figure 9 Projections for GDP Growth and Main Indicators of Japan (as of September 8, 2020)

	(seasonally adjusted, annualised % changes from the previous quarter)									(% changes from the previous fiscal year)		
	CY2020				CY2021				CY2022	FY2019	FY2020	FY2021
	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 GDP	▲ 2.3	▲ 28.1	16.9	6.7	3.3	1.6	2.8	▲ 0.0	1.0	0.0	▲ 5.4	3.4
Private Consumption Expenditure	▲ 2.8	▲ 28.2	18.9	3.5	3.1	1.7	2.4	0.8	1.2	▲ 0.5	▲ 6.0	3.2
Housing Investment	▲ 15.0	▲ 2.0	▲ 24.8	▲ 7.5	28.2	14.9	7.4	6.9	4.2	0.6	▲ 8.9	8.2
Business Fixed Investment	7.0	▲ 17.5	▲ 1.8	16.2	2.8	2.3	2.3	1.8	1.8	▲ 0.3	▲ 3.9	3.6
Private Inventories (percentage points contribution)	(▲ 0.3)	(1.4)	(▲ 0.7)	(▲ 0.2)	(0.0)	(0.0)	(0.0)	(0.0)	(0.0)	(▲ 0.1)	(0.1)	(▲ 0.1)
Government Consumption Expenditure	0.1	▲ 2.3	4.8	2.5	0.0	0.2	3.5	▲ 2.3	0.4	2.3	1.0	1.0
Public Investment	▲ 1.8	4.6	2.8	4.9	▲ 1.0	▲ 2.1	▲ 0.4	0.6	0.8	3.3	2.5	0.0
Net Exports (percentage points contribution)	(▲ 0.9)	(▲ 10.9)	(6.3)	(2.1)	(0.8)	(0.1)	(0.2)	(▲ 0.4)	(▲ 0.1)	(▲ 0.2)	(▲ 1.6)	(0.7)
Exports of Goods and Services	▲ 19.9	▲ 56.0	26.2	23.7	17.2	9.5	6.1	▲ 0.2	2.0	▲ 2.6	▲ 15.2	10.9
Imports of Goods and Services	▲ 15.6	▲ 1.9	▲ 16.4	8.9	12.1	8.6	4.7	2.4	2.8	▲ 1.5	▲ 6.1	5.7
(Ref.) Domestic Private Demand (percentage points contribution)	(▲ 1.4)	(▲ 19.2)	(8.5)	(4.0)	(2.8)	(1.7)	(1.9)	(0.9)	(1.1)	(▲ 0.4)	(▲ 4.1)	(2.5)
(Ref.) Public Demand (percentage points contribution)	(▲ 0.0)	(▲ 0.3)	(1.2)	(0.8)	(▲ 0.1)	(▲ 0.1)	(0.7)	(▲ 0.5)	(0.1)	(0.6)	(0.3)	(0.2)

	(% changes from the same quarter of the previous year)									(% changes from the previous fiscal year)		
Nominal GDP	▲ 0.9	▲ 8.7	▲ 5.9	▲ 3.3	▲ 2.1	6.5	3.3	1.9	1.5	0.8	▲ 5.0	3.2
GDP deflator	0.9	1.3	0.7	0.0	▲ 0.2	▲ 0.6	▲ 0.3	0.0	0.1	0.8	0.4	▲ 0.2
Consumer Price Index (excluding fresh food)	0.6	▲ 0.1	0.1	▲ 0.8	▲ 0.7	0.1	0.0	0.7	0.6	0.6	▲ 0.4	0.3
(excluding fresh food, consumption tax, education free of charge)	0.2	▲ 0.4	▲ 0.2	▲ 0.7	▲ 0.6	0.1	0.0	0.7	0.6	0.4	▲ 0.5	0.3
Unemployment Rate (%)	2.4	2.8	3.2	3.8	3.9	3.7	3.5	3.4	3.3	2.3	3.4	3.5
Exchange Rates (JY/US\$)	109	108	106	106	107	108	108	108	108	109	107	108
Import Price of Crude Oil (US\$/barrel)	68	31	42	47	48	50	54	60	62	68	41	57

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.