

Monthly Report of Prospects for Japan's Economy

September 2021

Macro Economic Research Center
Economics Department



The Japan Research Institute, Limited

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

This report is the revised English version of the August 2021 issue of the original Japanese version.

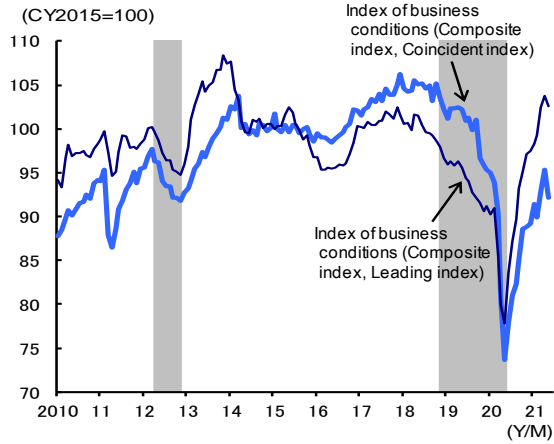
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The General Situation – Economic Activity Picked up, While the Recovery Was Lackluster in Some Areas

Figure 1-1 Economic Activity

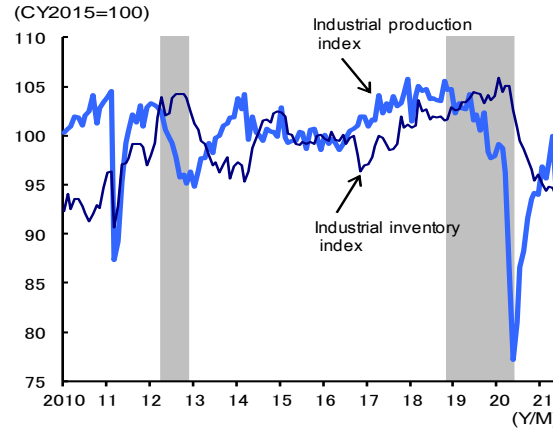
Both the CI leading index and the CI coincident index declined slightly in reaction to the rapid increases.



Source: The Cabinet Office.

Figure 1-2 The Corporate Sector

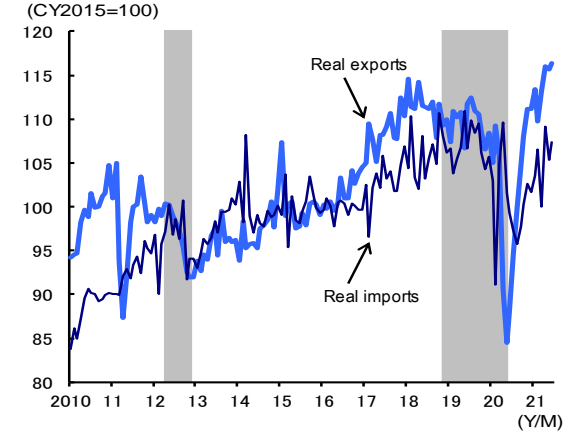
Industrial production remained on an increasing trend on the back of the recovery of the automotive industry.



Source: The Ministry of Economy, Trade and Industry.

Figure 1-3 Overseas Demand

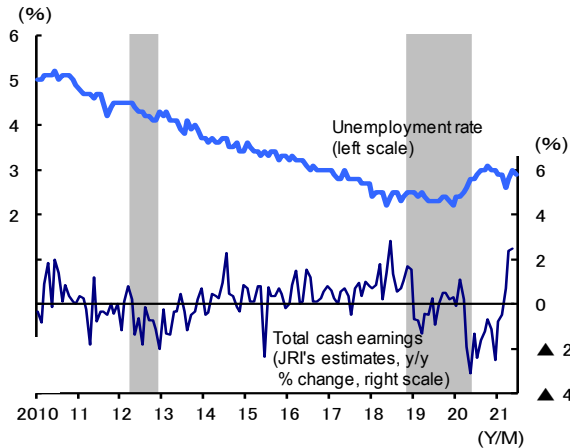
Both exports and imports are on a rising trend, albeit with fluctuations.



Source: The Bank of Japan.

Figure 1-4 Employment and Income

The unemployment rate remained at around 3%. Nominal wages turned positive on a year-on-year basis.

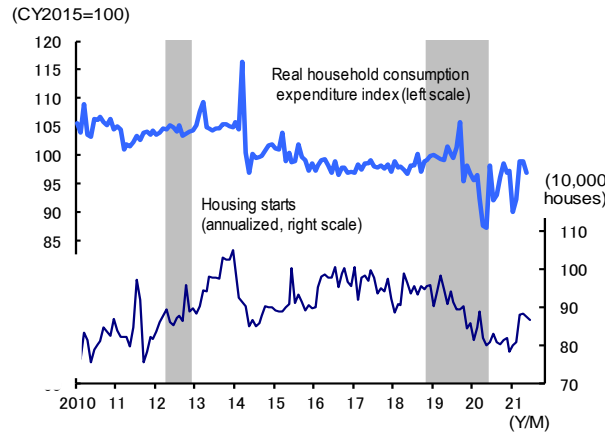


Source: The Ministry of Internal Affairs and Communications, The Ministry of Health, Labor and Welfare.

* The shaded area indicates the recession phase.

Figure 1-5 The Household Sector

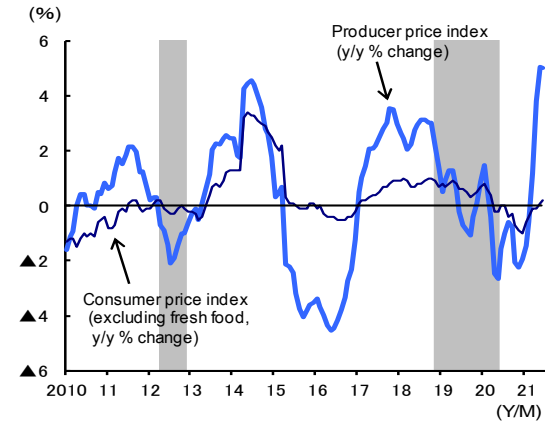
Real consumption saw some ups and downs due to restrictions on activity. Housing starts have rebounded slightly.



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

Figure 1-6 Prices

Producer prices increased mainly for petroleum products. Consumer prices turned positive year on year.



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

Production and Exports Remained Firm, While Personal Consumption Saw Some Ups and Downs

◆ Industrial Production is on a Rising Trend

The Industrial Production Index for June 2021 increased by 6.5% from the previous month, up for the first time in two months. By industry, production continued to increase for production machinery and electronic components and devices for which external demand remained robust. In addition, production of automobiles rapidly recovered as the effects of fires at a semiconductor plant in Japan ran their course.

Looking at the future production plan, while production is expected to decrease by 1.1% month-over-month in July, it is expected to increase by 1.7% month-over-month in August. Although the outlook for automobile production remains highly uncertain due to a prolonged global semiconductor shortage and sluggish parts supplies in Southeast Asia due to the impact of COVID-19, production activity will likely remain robust for the manufacturing industry on the whole.

◆ Exports Remained Firm

While real exports in June declined by 0.6% from the previous month, down for the

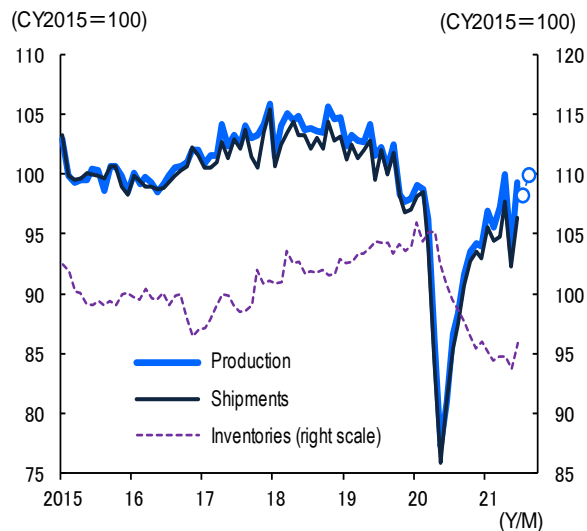
first time in four months, they were above the level from two months ago, and thus, exports were judged to have remained on a rising trend. By region, exports to Europe decreased in reaction to the significant rise that occurred in the previous month, while those to the United States remained robust.

◆ Personal Consumption Saw Some Ups and Downs

Japan's Real Consumption Activity Index (travel balance adjusted) for May 2021 declined by 3.7% from the previous month, down for the second consecutive month. Service consumption plunged as the third state of emergency declaration exerted downward pressure on the industry.

Meanwhile, the Consumer Confidence Index in June and July 2021 rose for two straight months. Consumption rebounded slightly from June on the back of the temporary easing of activity restrictions and progress made in the COVID-19 vaccine rollout.

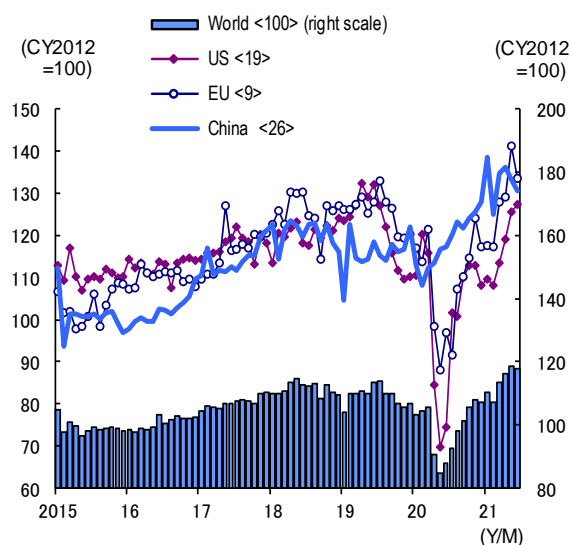
Figure 2-1 Industrial Production Index
<seasonally adjusted>



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 July and August 2021 based on the production forecast index.

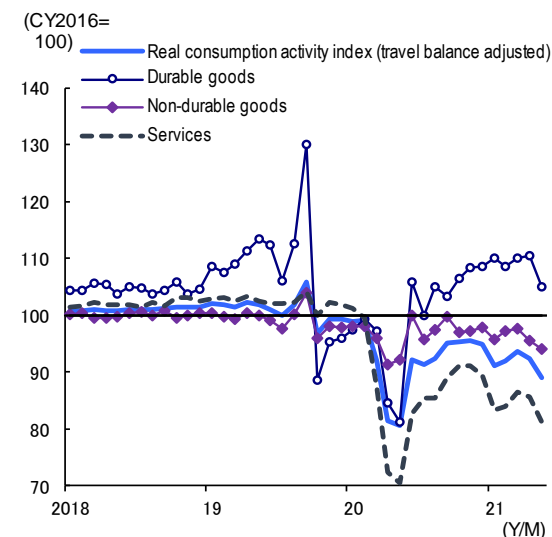
Figure 2-2 Real Exports by Destination
<seasonally adjusted>



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 CY2020.

Figure 2-3 Real Consumption Activity Index
<seasonally adjusted>



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

Exports of Goods Remained on a Recovery Trend

◆ Exports Were Led by Electronic Parts and Capital Goods

Goods exports are on a rising trend on the whole. By item, an increase in shipments of electronic parts and devices was prominent, while shipments of capital goods also continued to increase. Looking at capital goods exports by region, the increasing trend has been accelerating for shipments to the United States and the EU, where economic activity has resumed, in addition to shipments to China, where the recovery in economic activity has been firm.

As for future prospects, exports will likely remain strong, underpinned by the recovery of overseas economies. By item, shipments of electronic parts and devices as well as capital goods are expected to remain as the driving force on the back of initiatives by governments around the world to promote the spread of electric vehicles (EVs) and the domestic production of semiconductors, on top of increased demand for 5G-related products and a recovery in global demand for capital investment. Meanwhile, for transportation machinery, production expansion has been hindered by the prolonged supply shortage of semiconductor components,

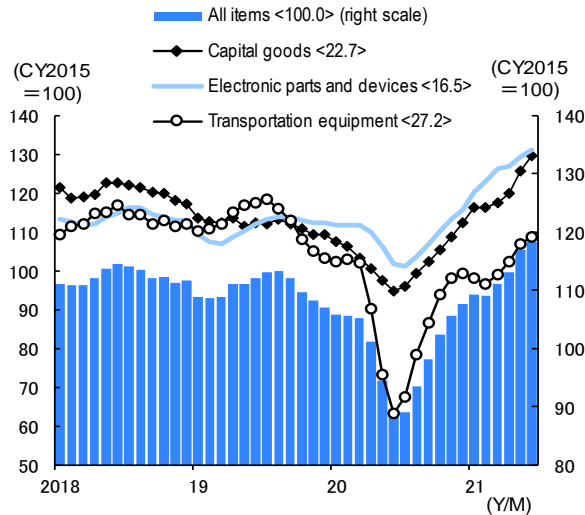
necessitating the elimination of supply constraints in order to achieve sustainable growth in exports.

◆ Demand Related to Inbound Tourism Has Remained Virtually Nonexistent

Amid restrictions on overseas travel around the world, the number of tourists visiting Japan has declined significantly.

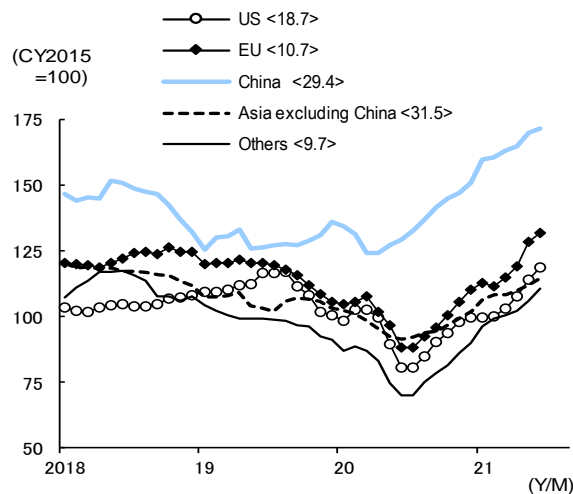
It is difficult for the Japanese government to ease entry restrictions for tourists until COVID-19 infections settle down both in Japan and overseas. Given this situation, a recovery in demand related to inbound tourism cannot be expected for the foreseeable future. The International Civil Aviation Organization (ICAO) predicts that the number of passengers around the world at the end of 2021 will recover to only around 50% of the level prior to the COVID-19 outbreak. In Japan, given the current situation surrounding COVID-19 vaccinations, recovery in the movement of people across national borders may be slower than in other developed countries.

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



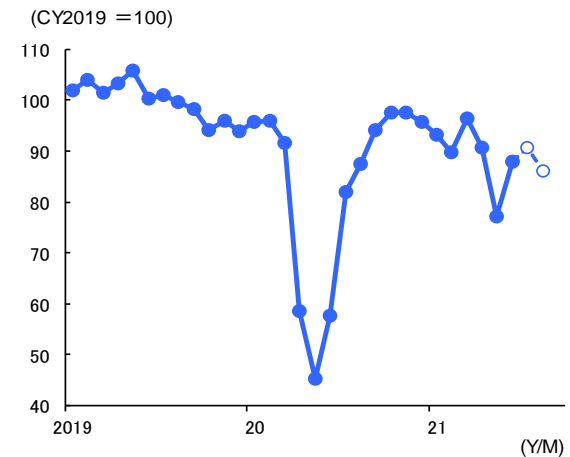
Source: The Japan Research Institute, Ltd. based on data of The Ministry of Finance, The Bank of Japan.
Note: 1. 3-month moving averages.
2. Figures in the angled brackets show the shares in total nominal exports in CY2020.

Figure 3-2 Real Exports of Capital Goods by Country or Area
<seasonally adjusted>



Source: The Japan Research Institute, Ltd. based on data of The Ministry of Finance, The Bank of Japan.
Note: 1. 3-month moving averages.
2. Figures in the angled brackets show the shares in total nominal exports of capital goods in CY2020.

Figure 3-3 Production Index for Transportation Equipment
<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 index are forecasts based on the method of the METI.

Corporate Earnings Have Been Polarized, While Business Fixed Investment Is Expected to Rebound

◆ Corporate Earnings Have Become Polarized

According to the Financial Statements Statistics of Corporations by Industry, current profits of the manufacturing industry for the January-March 2021 quarter increased 12.5% from the previous quarter, remaining on a rising trend on the back of the recovery in exports. On the other hand, in the nonmanufacturing sector, while current profits on the whole increased from the previous quarter, the accommodation and food services industries, which have been greatly impacted by the COVID-19 pandemic, continued to record further losses. For the April-June 2021 quarter, while exports continued to expand, domestic consumption remained sluggish due to the effects of the state of emergency declaration. As a result, corporate earnings appear to have remained polarized.

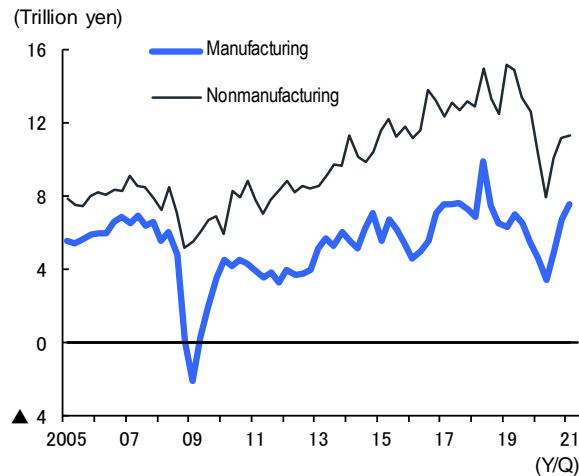
Recently, a rise in raw material prices due to a recovery in global production activities has been a factor in the decline in profits in the manufacturing industry. However, it is judged that the trend of growing profits in the manufacturing sector is unlikely to end since the decline in profits due to higher raw material prices is

expected to amount to only about 30% of the increase in profits resulting from increased exports.

◆ Companies Have Resumed Capital Investment

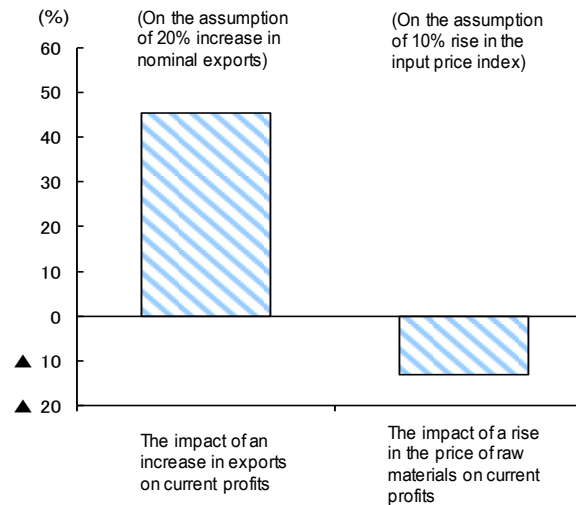
Capital expenditure for the January-March 2021 quarter decreased 0.7% from the previous quarter on an industry-wide basis, down for the fourth consecutive quarter. However, there have been moves to resume postponed investment activities, mainly in the manufacturing industry, where improvement in the earnings environment has been prominent. According to the Bank of Japan's June 2021 Tankan Survey, capital expenditure plans (large enterprises, industry-wide basis) for fiscal 2021 are 12.3% higher than actual results of the previous year, with the prospect of a recovery in the level of investment to pre-COVID-19 outbreak values. However, corporate investment stance varies among industries, and companies are expected to remain cautious with regard to capital investment in industries such as accommodation and food services and personal services.

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



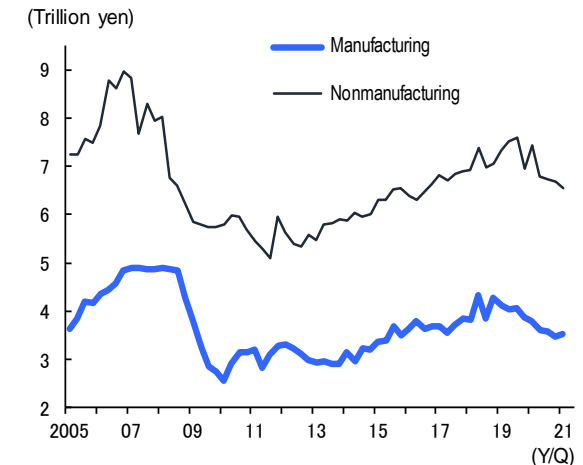
Source: The Japan Research Institute, Ltd. based on the data of The Ministry of Finance.
Note: All industries except for financial services and insurance.

Figure 4-2 Impact of Exports and Prices on Current Profits <FY2021>



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

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.

The Recovery in Employment and Income Conditions Will Be Delayed Due to the Effects of Restrictions on Activities

◆ Employment Conditions Saw Some Ups and Downs

The unemployment rate in June 2021 was 2.9%, down for the first time in three months. Looking at a breakdown in the numbers by industry, the accommodation and food services industries increased year on year for the first time in 18 months. There is an ongoing trend of maintaining employment due to concerns about labor shortages over the medium- to long-term, in addition to the use of employment adjustment subsidies.

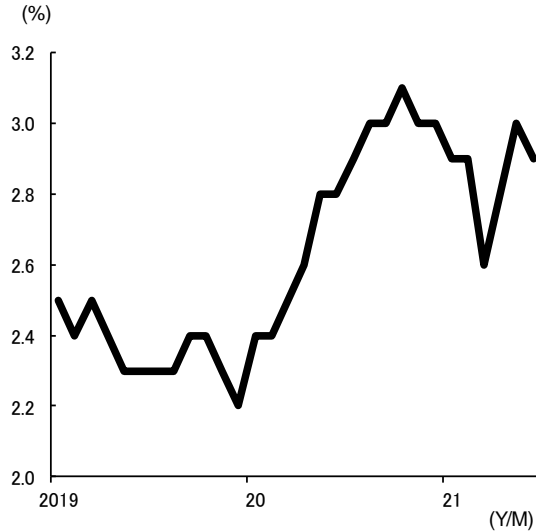
However, as a result of reinforcement of activity restrictions after July, it is inevitable that employment in food services and other industries will decline to a certain extent. Amid this situation, the Japanese government has set a policy to maintain special treatment such as raising the upper limit of employment adjustment subsidies until the end of this year. While it is unlikely that the numbers of unemployed will increase rapidly, it is expected to take some time before employment conditions recover in earnest.

◆ The Lower Rate of Part-time Workers Boosted Average Wages

Total cash earnings (on the basis of common business establishments) in May 2021 rose 2.5% year-on-year, recording a year-on-year increase for the third consecutive month. This is a high growth rate in recent years, particularly for scheduled salaries. However, the increase was attributable primarily to the fact that average wages were boosted by a lower rate of part-time workers paid low-wages due to the effects of the COVID-19 pandemic; the actual pay situation has been sluggish.

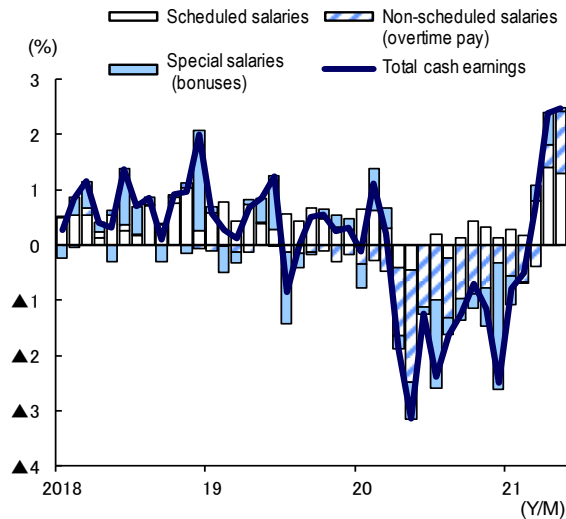
Meanwhile, this year's summer bonuses were reported to be sluggish, mainly at large companies. This is because the impact of deteriorated earnings in the previous fiscal year due to the COVID-19 pandemic was fully reflected in this year's summer bonuses at many large companies. Owing to the decline in special salaries (bonuses), it is difficult to expect that overall wages will improve in earnest for the foreseeable future.

Figure 5-1 Unemployment Rate
<seasonally adjusted>



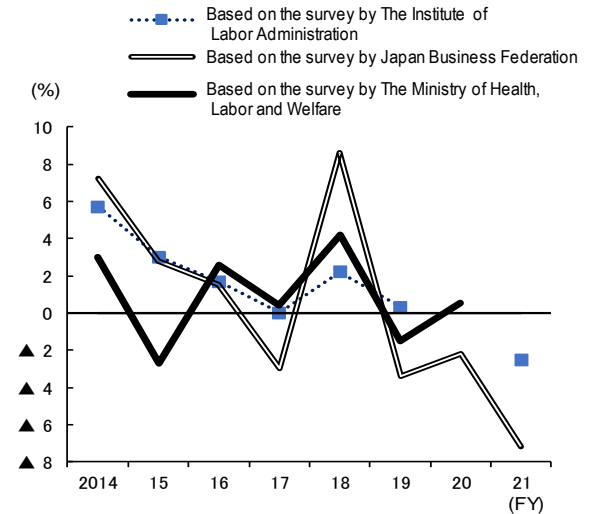
Source: The Japan Research Institute, Ltd. based on data of The Ministry of Internal Affairs and Communications.

Figure 5-2 Contributions to Change Rate of Nominal Wages
<year-on-year % change>



Source: The Japan Research Institute, Ltd. based on data of The Ministry of Health, Labor and Welfare.
Note: On the basis of common business establishments.

Figure 5-3 Summer Bonuses
<year-on-year % change>



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

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Personal Consumption is Expected to Visibly Recover with Progress in the COVID-19 Vaccine Rollout

◆ Personal Consumption Saw Some Ups and Downs Due to Restrictions on Activities

Consumption has been up and down due to the repeated easing and reinforcement of restrictions on activities. Consumption based on credit card settlements decreased from early May through early June but picked up slightly thereafter as the number of people visiting commercial facilities recovered.

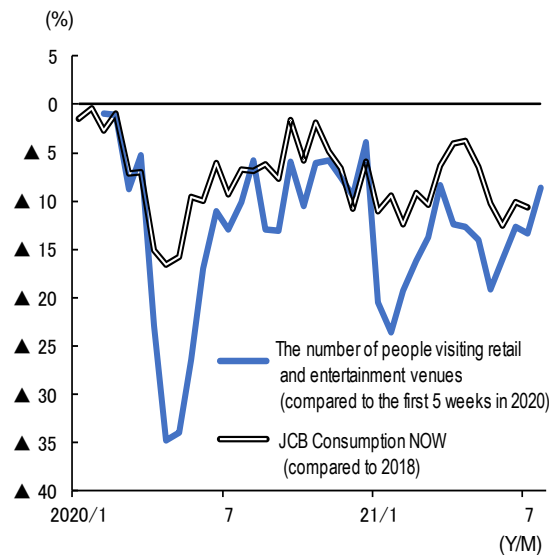
Recently, progress has been made in the COVID-19 vaccine rollout, which is the key to normalizing consumption activities. If the vaccination rate of 1 million doses per day can be maintained, 70% of the population will be vaccinated with two doses by the end of November—enough to achieve herd immunity for Japan. COVID-19 related savings, or money which has not been spent on household expenses due to self-restraint in consumption activities, are estimated to have accumulated to about 400,000 yen on average for working households and 500,000 yen for retired

households. Given this situation, it is predicted that the recovery in consumption will become clear as so-called “revenge spending” becomes apparent with the progress in the COVID-19 vaccine rollout.

◆ Housing Investment Saw Signs of a Recovery

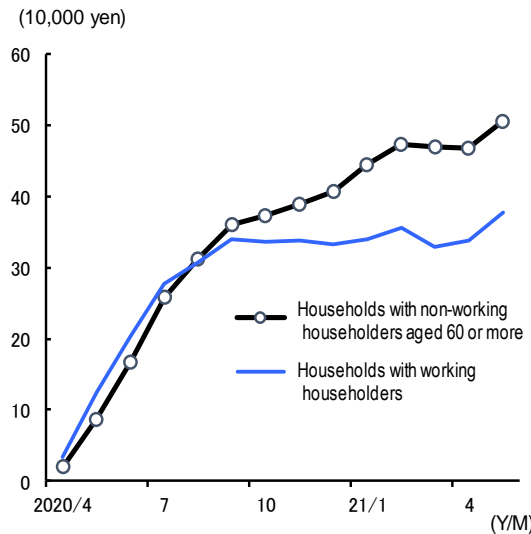
The number of housing starts (seasonally adjusted annual rate) for the April-June 2021 period stood at 870,000, showing signs of a recovery from the low level of around 800,000 since the spring of 2020. As low interest rates and housing loan tax breaks continued, construction work, which had been suspended due to the effects of COVID-19, resumed. However, the rise in the prices of newly-built houses due to the increases in material prices and labor costs has affected the rise in the prices of used condominiums. After pent-up demand settles in the future, the higher prices will likely put downward pressure on demand.

Figure 6-1 Consumption Based on Credit Card Settlements <compared to the same month in 2018>



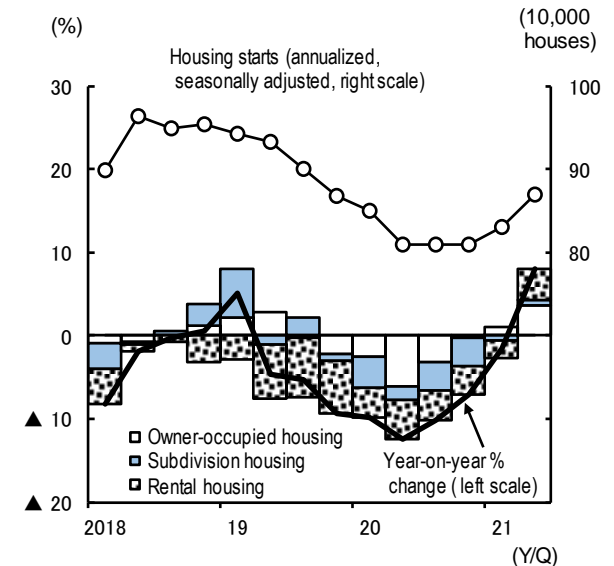
Source: The Japan Research Institute, Ltd. based on data of JCB Consumption NOW, Google.

Figure 6-2 COVID-19 Related Savings per Household by Type



Source: The Japan Research Institute, Ltd. based on data of The Ministry of Internal Affairs and Communications. Note: Households with 2 or more household members.

Figure 6-3 Change in Housing Starts



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

Topic: Downward Pressure on Consumption from the State of Emergency Declaration Has Diminished

◆ The State of Emergency Declaration Was Reissued and Extended in July

Since the beginning of July, the Japanese government issued and extended the state of emergency declaration along with priority preventive measures to control the spread of COVID-19. Due to these measures to restrict activities, the recovery in personal consumption has been delayed. However, the decline in consumption is expected to be limited compared to previous activity restriction periods for the following reasons.

First, the number of regions and areas covered by the latest activity restrictions is smaller than in the past, as is the number of restaurants and bars that have been closed.

Second, the deterrent to economic activity resulting from activity restrictions has been declining. The decline in consumption per household tends to decrease with the issuance of every activity restriction. The decline in the number of people out and about on the street also tends to diminish. On the supply side, some restaurants and

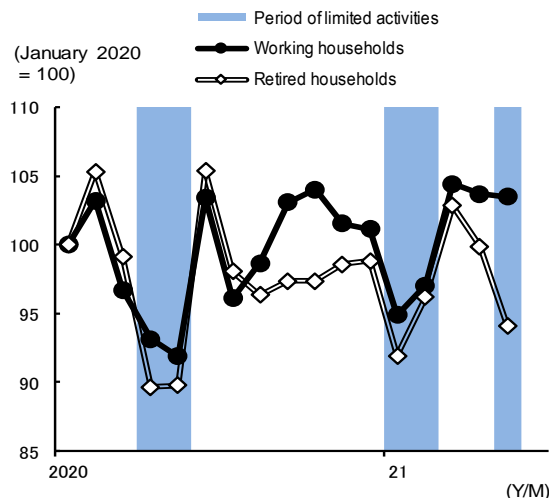
bars do not comply with activity restriction requests.

◆ Consumption Among Retired Households Will Also Recover in Early Autumn

By household type, consumption by working households is relatively strong. Stay-at-home demand, such as online content and gardening-related products, is growing. Service consumption is also improving, albeit with fluctuations due to activity restrictions. In addition to the popularity of camping among people seeking to avoid overcrowding, the resumption of sporting events with admission restrictions has also contributed to the increase in spending.

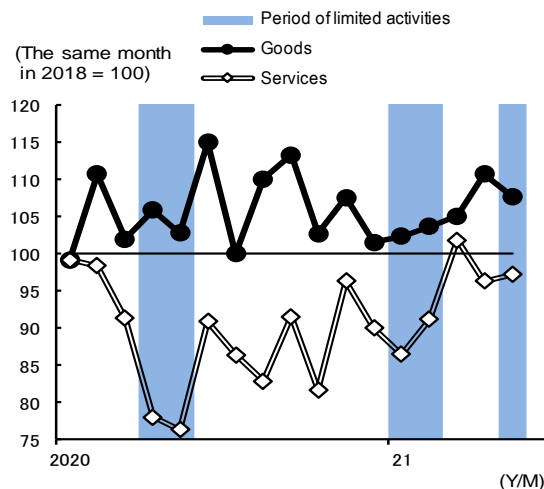
On the other hand, retired households remain cautious concerning infection, and service consumption has been sluggish. However, vaccination rates are rising, particularly among the elderly, and a clear recovery in consumption is expected in early autumn, when the trend will spread to younger generations.

Figure 7-1 Nominal Consumption Value per Household by Type <seasonally adjusted>



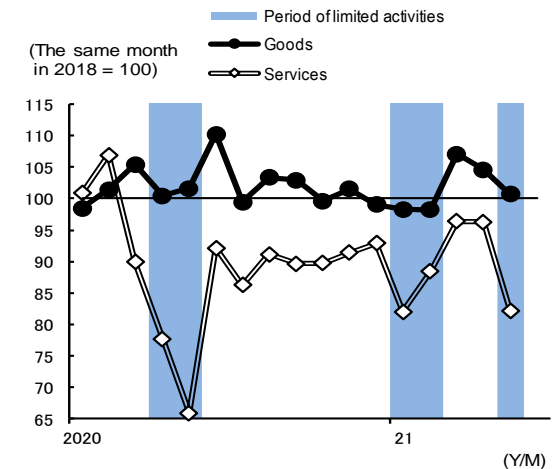
Source: The Japan Research Institute, Ltd. based on data of The Ministry of Internal Affairs and Communications.
 Note: 1. Households with 2 or more household members.
 2. Retired households indicate households with non-working householders aged 60 or more.

Figure 7-2 Nominal Consumption Value in Working Households <compared to CY2018>



Source: The Japan Research Institute, Ltd. based on data of The Ministry of Internal Affairs and Communications.
 Note: Households with 2 or more household members.

Figure 7-3 Nominal Consumption Value in Retired Households <compared to CY2018>



Source: The Japan Research Institute, Ltd. based on data of The Ministry of Internal Affairs and Communications.
 Note: 1. Households with 2 or more household members.
 2. Retired households indicate households with non-working householders aged 60 or more.

Prospects for Japan's Economy - Projected Real GDP Change; 3.7% for FY2021 and 2.5% for FY2022

◆ Pace of Economic Recovery Will Accelerate through the Second Half of FY2021

(1) Japan's real GDP for the April–June 2021 period was +1.3% on an annualized quarter-on-quarter change basis (up 0.3% from the preceding quarter), achieving positive growth for the first time in two quarters driven by an increase in exports and capital investment. However, as a third state of emergency was declared in Tokyo and Osaka Prefecture and it weighed on personal consumption, Japan could not fully recover from the decline recorded in the January–March 2021 period. The Japanese economy remains stagnant.

(2) In future economic prospects, an increase in exports driven by the recovery in overseas economies will likely underpin the Japanese economy, as activity restrictions have been eased mainly in the United States and Europe in line with progress in the COVID-19 vaccine rollout. Capital investment is also expected to continue to pick up in Japan as a result of moves to resume investment, particularly in the manufacturing sector, which has seen a marked recovery in corporate earnings.

(3) Meanwhile, consumer spending will likely remain sluggish for the time being as the state of emergency was issued once again in Tokyo and other prefectures in July and August. As the highly contagious Delta variant is rampant at present, it remains to be seen whether the COVID-19 pandemic can be brought under control. However, it is unlikely that personal consumption will start to decline again in the July–September 2021 period, given the progress in COVID-19 vaccine rollout among the elderly and the fact that the effect of restricting the movement of people has weakened due to the repeated states of emergency. After autumn, it is forecast that the pace of the recovery in consumption will accelerate and the economy will be boosted as people other than the elderly are vaccinated, which is expected to curb the number of new cases.

(4) After the beginning of FY2022, it is anticipated that consumer spending will be mostly normalized and that the pace of economic recovery will return to an average speed. As a result, quarterly growth is expected to slow significantly.

(5) As a result, Japan's growth rate for FY2021 is expected to be +3.7%, which is not sufficient to fully recover from the decline recorded in FY2020 (–4.5%). However, the growth rate for FY2022 is anticipated to be +2.5%, and Japan will likely achieve high positive growth for two years in a row. It is forecast that Japan's GDP will recover to the peak level prior to the outbreak of COVID-19 (July–September 2019 period) in the April–June 2022 period.

◆ Prices Rose for the Second Consecutive Month

(6) In June 2021, core CPI increased 0.2% year-on-year, up for the second consecutive month, reflecting the rise in energy prices. Excluding the effects of the rise in energy prices, however, core CPI dropped 0.3% year-on-year, down for three straight months, against the backdrop of a decline in communications costs reflecting lower mobile phone charges, among other factors.

As for the future outlook, while energy prices are expected to continue increasing, strong downward pressure will be exerted on general prices from the viewpoint of supply and demand, and communications costs are anticipated to continue in a decline. Consequently, CPI excluding fresh food and energy will likely hover around zero for the time being.

Figure 9 Projections for GDP Growth and Main Indicators of Japan (as of August 16, 2021)

	(seasonally adjusted, annualized % changes from the previous quarter)											(% changes from the previous fiscal year)		
	CY2020		CY2021				CY2022				CY2023	FY2020	FY2021	FY2022
	7~9	10~12	1~3	4~6	7~9	10~12	1~3	4~6	7~9	10~12	1~3			
	(Actual)		(Actual)	(Projection)	(Projection)	(Projection)	(Projection)	(Projection)	(Projection)	(Projection)	(Projection)	(Actual)	(Projection)	(Projection)
Real GDP	22.8	11.9	▲ 3.7	1.3	2.8	5.2	5.1	1.3	1.1	1.0	1.0	▲ 4.5	3.7	2.5
Private Consumption Expenditure	22.1	9.4	▲ 4.0	3.4	1.7	6.5	6.8	0.7	0.7	0.9	0.9	▲ 5.9	3.9	2.6
Housing Investment	▲ 21.0	0.1	3.8	8.6	3.5	0.6	2.8	2.0	0.7	0.2	0.0	▲ 7.2	2.3	1.5
Business Fixed Investment	▲ 8.0	18.3	▲ 4.9	7.0	3.8	5.4	5.4	3.9	3.0	2.5	2.5	▲ 6.8	4.2	3.9
Private Inventories (percentage points contribution)	(▲ 0.8)	(▲ 2.0)	(1.7)	(▲ 0.7)	(0.2)	(0.2)	(0.0)	(0.0)	(0.0)	(0.0)	(0.0)	(▲ 0.2)	(▲ 0.1)	(0.0)
Government Consumption Expenditure	11.5	7.6	▲ 6.7	2.0	1.9	1.4	1.8	0.7	0.7	0.4	0.4	3.3	1.4	1.0
Public Investment	2.6	4.0	▲ 4.0	▲ 5.7	1.2	1.8	0.8	0.0	▲ 1.0	▲ 0.6	0.0	4.2	▲ 1.1	0.1
Net Exports (percentage points contribution)	(11.2)	(4.2)	(▲ 0.9)	(▲ 1.3)	(0.5)	(0.2)	(0.1)	(0.1)	(0.1)	(0.0)	(0.0)	(▲ 0.6)	(0.7)	(0.1)
Exports of Goods and Services	32.6	55.8	9.8	12.3	5.7	5.7	4.9	4.6	4.6	4.1	4.1	▲ 10.4	14.6	4.8
Imports of Goods and Services	▲ 29.0	20.8	16.8	21.9	2.9	4.3	4.3	4.0	4.0	3.8	3.8	▲ 6.8	9.8	4.0
(Ref.) Domestic Private Demand (percentage points contribution)	(7.9)	(5.5)	(▲ 1.2)	(2.5)	(1.9)	(4.6)	(4.6)	(1.1)	(0.9)	(0.9)	(0.9)	(▲ 4.7)	(2.7)	(2.1)
(Ref.) Public Demand (percentage points contribution)	(2.6)	(1.8)	(▲ 1.6)	(0.1)	(0.5)	(0.4)	(0.4)	(0.1)	(0.1)	(0.1)	(0.1)	(0.9)	(0.2)	(0.2)

	(% changes from the same quarter of the previous year)											(% changes from the previous fiscal year)		
	7~9	10~12	1~3	4~6	7~9	10~12	1~3	4~6	7~9	10~12	1~3			
Nominal GDP	▲ 4.5	▲ 0.8	▲ 1.4	6.7	2.0	1.1	4.0	4.1	3.9	2.4	1.2	▲ 3.9	3.4	2.9
GDP deflator	1.2	0.2	▲ 0.1	▲ 0.7	▲ 0.9	▲ 0.1	0.4	0.5	0.7	0.3	0.1	0.6	▲ 0.3	0.4
Consumer Price Index (excluding fresh food)	▲ 0.2	▲ 0.9	▲ 0.4	0.0	0.3	1.0	0.7	0.9	0.5	0.4	0.3	▲ 0.4	0.5	0.5
Unemployment Rate (%)	3.0	3.1	2.8	2.9	3.1	3.1	3.1	3.0	2.9	2.9	2.8	2.9	3.0	2.9
Exchange Rates (JY/US\$)	106	104	106	109	111	111	112	113	112	112	113	106	111	113
Import Price of Crude Oil (US\$/barrel)	41	44	55	67	76	73	70	68	69	68	68	43	71	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.