

Monthly Report of Prospects for Japan's Economy

October 2022

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 September 2022 issue of the original Japanese version.

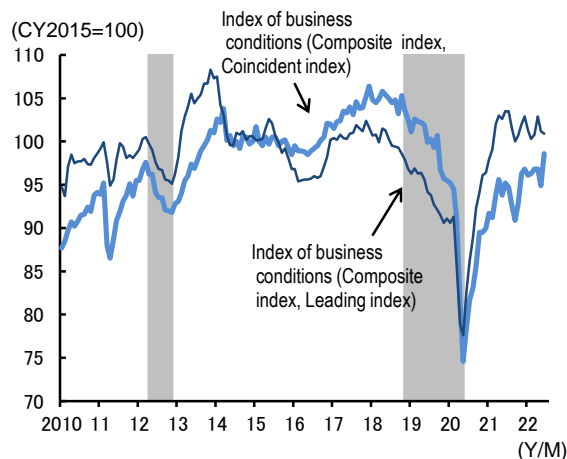
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The General Situation – The economy is picking up

Figure 1-1 Economic Activity

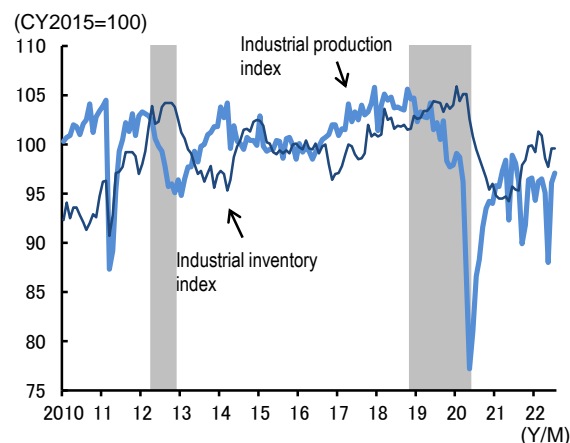
Regarding indices of business sentiment, coincident indices are rising, while leading indices are moving back and forth.



Source: The Cabinet Office.

Figure 1-2 The Corporate Sector

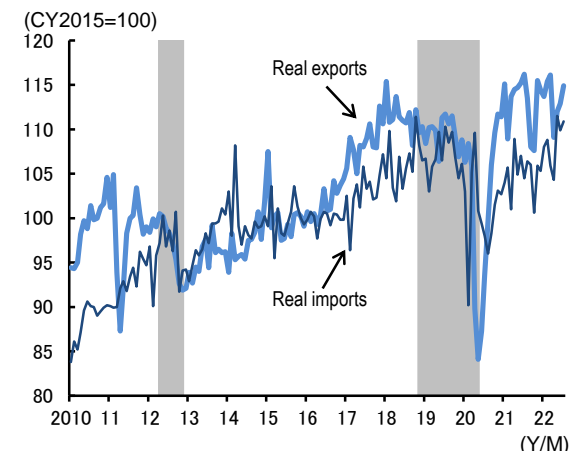
Industrial production is increasing, mainly in the automobile and general-purpose/commercial machinery sectors.



Source: The Ministry of Economy, Trade and Industry.

Figure 1-3 Overseas Demand

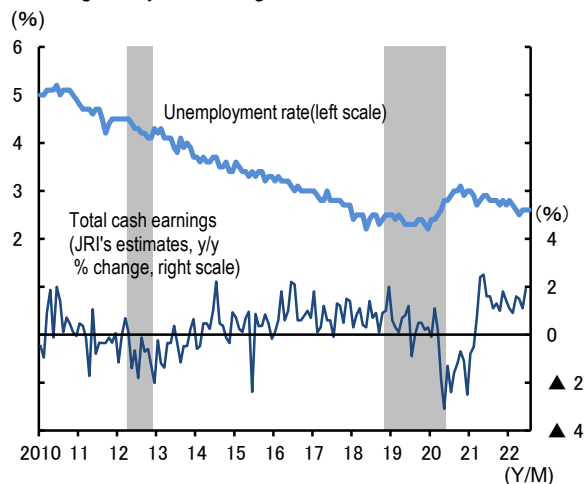
Exports to the EU, China, etc. are rising and imports remain high.



Source: The Bank of Japan.

Figure 1-4 Employment and Income

The unemployment rate is unchanged and nominal wages are rising mainly due to fringe benefits.

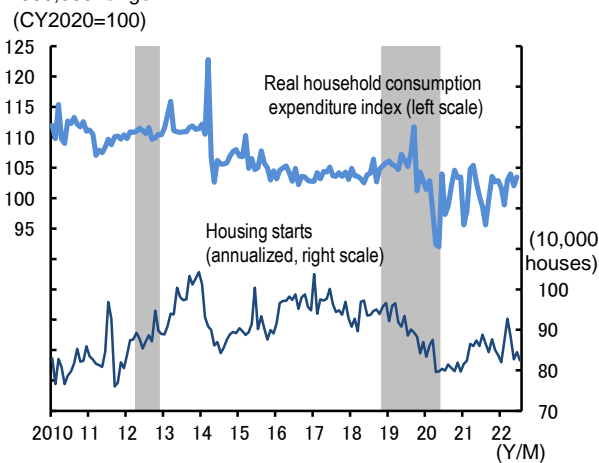


Source: The Ministry of Internal Affairs and Communications, The Ministry of Health, Labor and Welfare.

* The shaded area indicates the recession phase.

Figure 1-5 The Household Sector

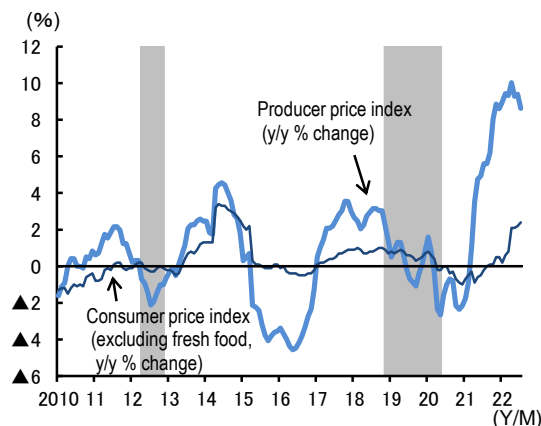
Real consumption is recovering as opportunities to go out increase, and housing starts are hovering in the low-800,000 range.



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

Corporate price inflation is running high at more than 8%, and consumer prices were over 2% higher than a year earlier for the fourth consecutive month.



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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The economy is picking up as personal consumption rebounds

◆ Positive growth continued in the April-June quarter

Real GDP in April-June grew from the previous quarter at an annualized rate of 3.5%, marking the third consecutive quarter of positive growth. On the demand side, the easing of activity restrictions spurred personal consumption, with food service, accommodation, and other services the main beneficiaries of the recovery. Public-sector demand increased for the first time in three quarters as the bulk of last fiscal year's supplementary budget began to be spent, chiefly on "national land resilience," i.e., infrastructure investment.

◆ Exports and production are both on the rise

Real exports increased in July for the third month in a row. By region, shipments to the U.S. declined, while those to Europe, China, and other Asian countries continued their ascent.

With supply constraints easing, the Industrial Production Index rose for the second

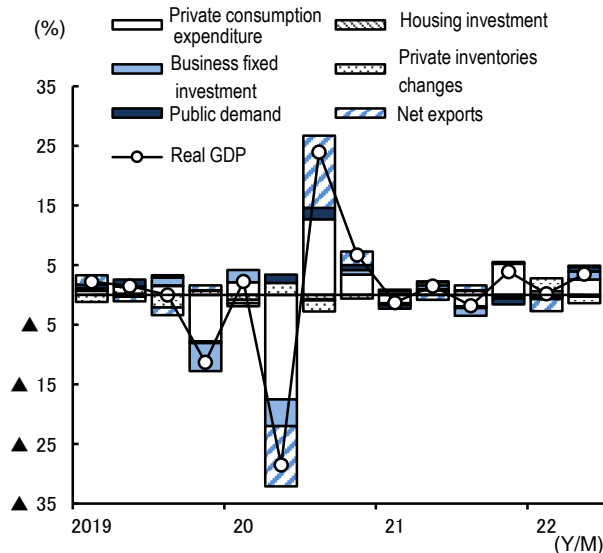
consecutive month in July, up 1.0% from the previous month. Capital goods-related industries, such as automobiles and general-purpose/commercial machinery, boosted the overall figure. Near-future production plans indicate continued increased output in August (+5.5% month-on-month (MoM)) and September (+0.8% MoM).

However, there is a risk that plans will be revised downward due to the COVID flare-up in Japan and the world economic slowdown, which is especially pronounced in the U.S. and Europe. In particular, production of electronic components/devices could decline as a consequence of flagging smartphone sales across the globe.

◆ The personal consumption recovery pauses

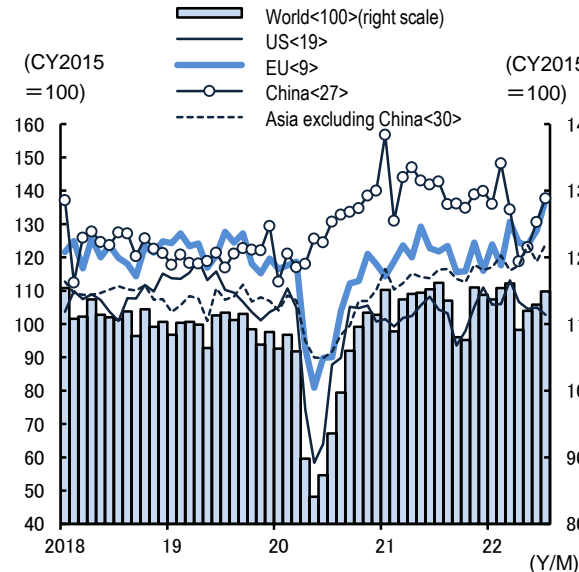
In July, the Real Consumption Activity Index (adjusted for the travel balance) dipped 0.4%, the first month-on-month (MoM) decline in five months. The COVID resurgence in Japan weighed on consumption, especially of services.

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



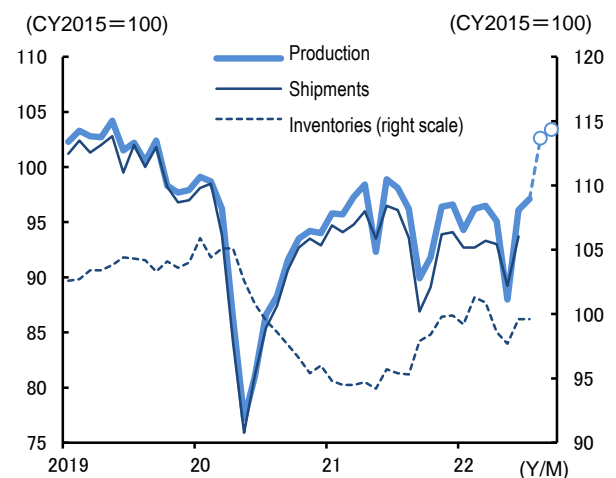
Source: The Japan Research Institute, Ltd. based on data of The Cabinet Office.

Figure 2-2 Real Exports
<seasonally adjusted>



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

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.

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Goods exports are rising, but inbound demand still needs time to fully recover

◆ Transportation machinery exports have picked up

Looking at real exports by category, exports of transportation machinery, capital goods, etc. increased as the problem of shortages of components from China abated.

Looking ahead, exports are expected to continue to see moderate growth. While overseas economies look set to slow down, there is some potential for increases, mainly in the automobile industry, where order backlogs have been building due to supply constraints. According to the Bank of Japan's Tankan DI for the overseas supply-demand balance for manufactured goods, excess demand is expected to continue.

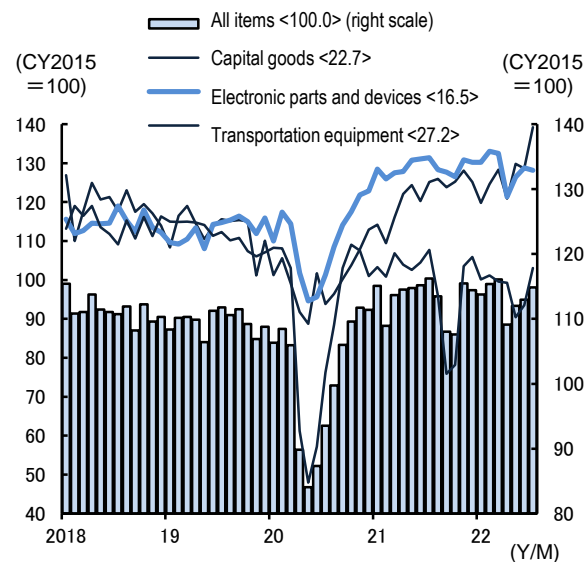
◆ Inbound demand is weak

In July, the number of foreign visitors to Japan was 145,000, down 90% from the pre-COVID level, and just 20% of the government's cap on arrivals. In response to

this situation, the government raised the daily entry limit from 20,000 to 50,000 people on September 7, and also eased waterfront measures, including exempting triple-vaccinated visitors from testing negative before their departure for Japan.

However, tourists still require visas and have to be on package tours. Since most foreign visitors to Japan before the COVID pandemic made their own travel arrangements, removal of the ban on individual travel is indispensable for a full-fledged recovery in inbound tourism.

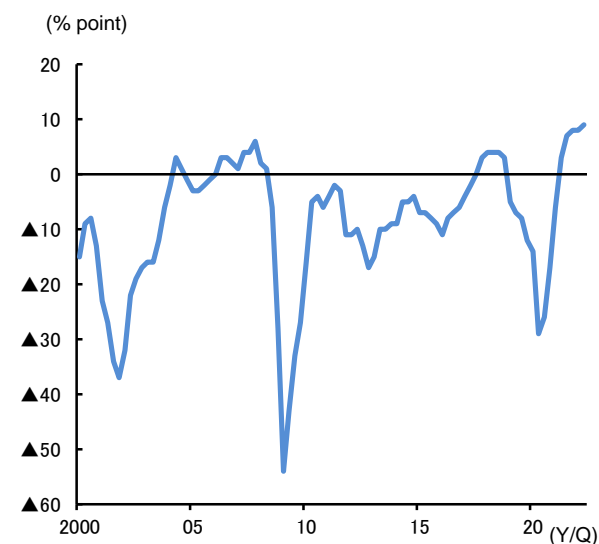
Figure 3-1 Real Exports by Item
<seasonally adjusted>



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 CY2021.

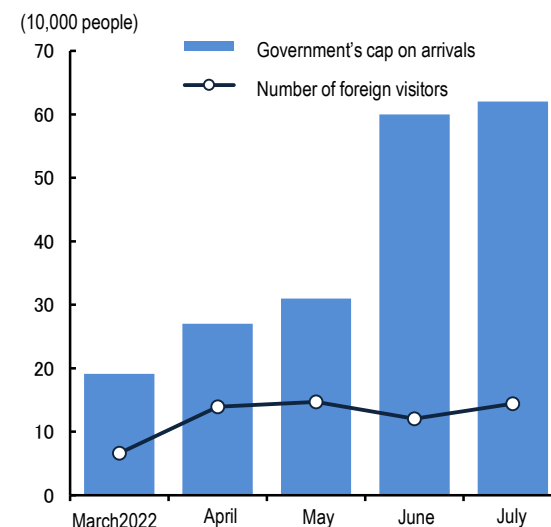
Figure 3-2 DI for Overseas Supply and Demand Conditions for Products



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

Note: The latest figures are forecasts based on June 2022 Tankan Survey.

Figure 3-3 Upper limit on the Number of Visitors to Japan and the Number of Foreign Visitors



Source: The Japan Research Institute, Ltd. based on data of the Japan National Tourism Organization, various media reports.

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High corporate earnings are supporting capital investment

◆ Corporate earnings are increasing

According to the Financial Statements Statistics of Corporations, ordinary profit for all industries in April-June rose by 5.5% from the previous quarter, meaning that profits have climbed for three quarters in succession. The ordinary profit to net sales ratio was 7%, the highest level ever. By industry, the manufacturing sector saw its profits rise for the fourth consecutive quarter. Although sales declined due to stalled production activities caused by supply chain disruptions, nonoperating income such as dividends boosted profits. Meanwhile, the non-manufacturing sector, driven by a recovery in personal consumption due to the easing of activity restrictions, also earned higher profits, mainly from accommodation/food services and lifestyle-related services.

Looking ahead, the pace of profit growth will be lower than in the previous fiscal year due to higher costs associated with rising resource prices and the depreciation of the yen, but companies will absorb the cost increases to a certain extent through

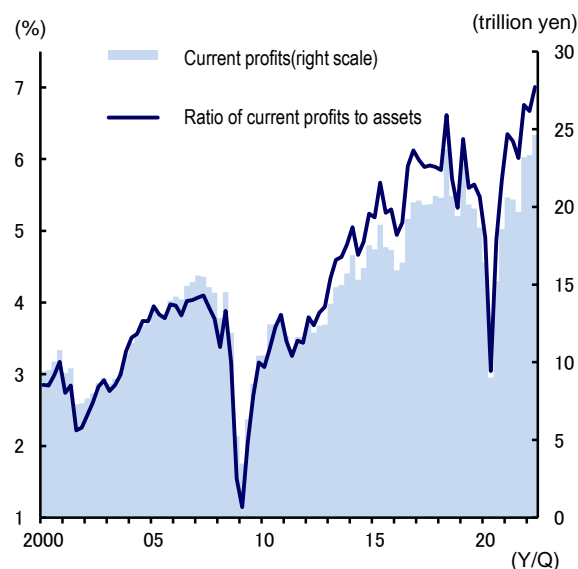
improved efficiency. Corporate earnings are expected to remain at high levels against a backdrop of normalization of economic activity and recovery of production.

◆ Capital investment is picking up

According to the Financial Statements Statistics of Corporations, capital investment in April-June increased by 3.9% from the previous quarter, marking the first rise in two quarters.

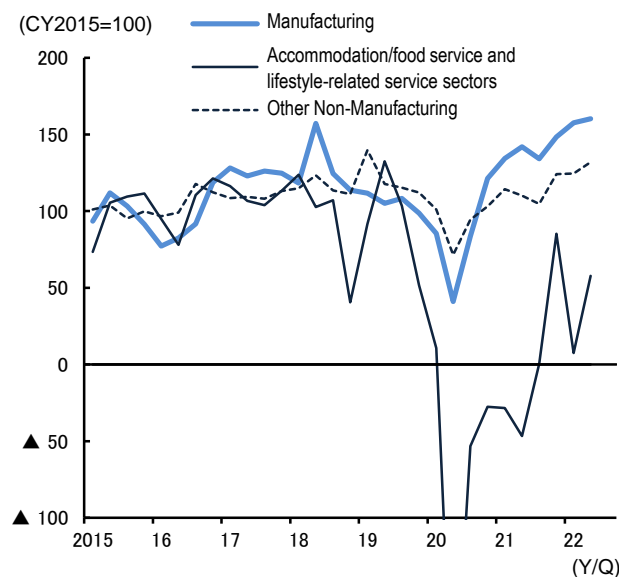
And going forward, capital investment is expected to continue to recover, supported by high corporate earnings. Both machinery orders and construction orders, leading indicators of capital investment, are on the rise, as companies maintain a proactive investment stance.

Figure 4-1 Current Profit and Ratio of Current Profits to Assets
<seasonally adjusted>



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

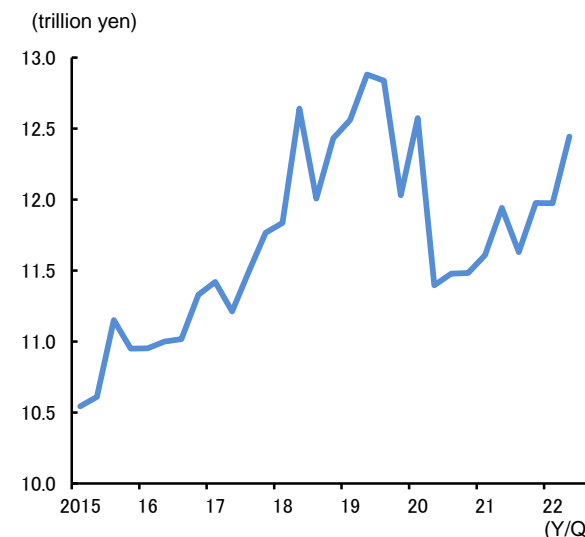
Figure 4-2 Current Profits of Japanese Corporations by Type



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
<all industries, 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.

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High prices are putting downward pressure on real wages

◆ Personnel shortages are gradually becoming more apparent

The employment environment has improved slightly as the economy picks up. The number of workers has increased moderately since early spring. The unemployment rate has declined slightly since early spring to 2.6%. The number of job openings is slowly increasing, while the number of job seekers remains flat, and labor shortages are gradually becoming more noticeable.

Looking ahead, the number of workers is unlikely to rise rapidly due to lingering uncertainty over the domestic infection situation and overseas economies, but is still expected to increase moderately on the back of the recovery in services consumption.

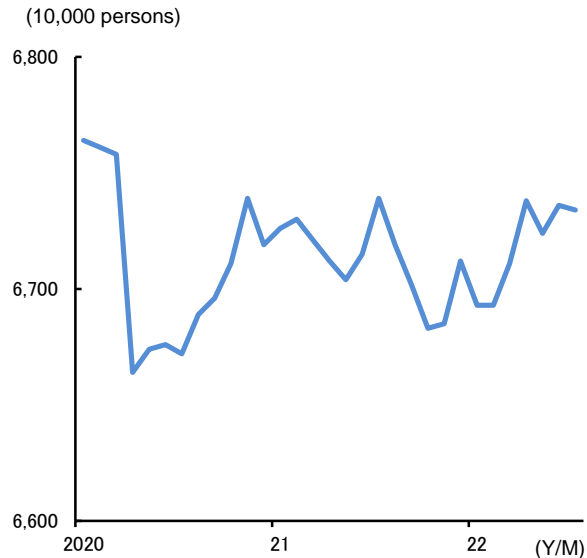
◆ Real wage growth rate has turned negative

Total cash payrolls in July increased 2.5% year on year (YoY), staying in positive territory. This was mainly due to an increase in bonuses at some major companies

following restraint last year. Real wages, however, declined 0.6% YoY due to the downward pressure of rising prices. Although the rates of wage increases awarded this spring were higher than last year due to the widespread basic wage hikes, this was largely a reaction to the tepid wage growth of the previous year, so while the trend is upward, the pace is weak.

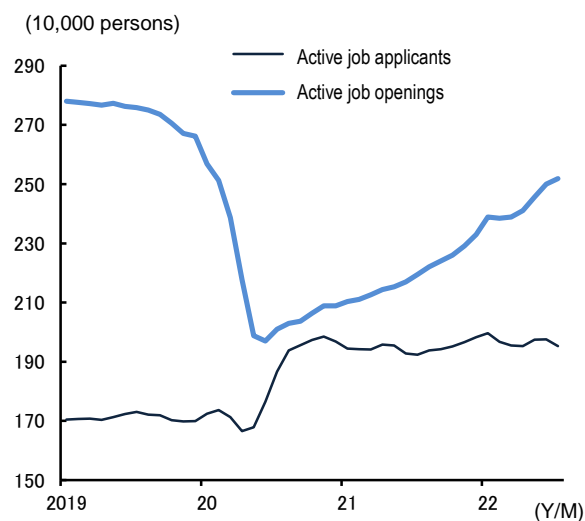
Looking ahead, nominal wages are expected to continue to rise moderately against a backdrop of 1) a growing sense of labor shortages, 2) increases in minimum wages, and 3) moves to reflect higher prices in basic wage hikes. However, given the strong sense of uncertainty about the outlook for the domestic and overseas economies, and the expectation that companies will remain cautious when setting wages, the conclusion drawn would be that wage increases will not outstrip price rises.

Figure 5-1 Number of Employees
<seasonally adjusted>



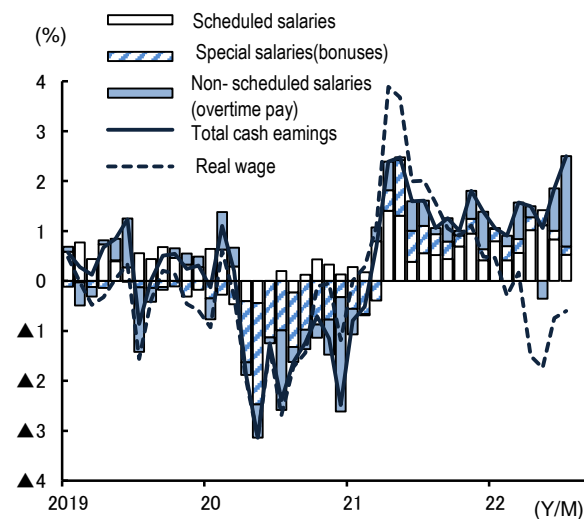
Source: The Japan Research Institute, Ltd. based on data of The Ministry of Internal Affairs and Communications.

Figure 5-2 Active Job Openings and
Active Job Applicants



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

Figure 5-3 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.

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The negative impact on consumption of the COVID flare-up is modest

◆ Full-scale resumption of travel subsidies is being delayed due to the infection resurgence

Although the recovery in services consumption has slowed due to the nationwide COVID rebound during the summer, a decline similar to that seen in previous waves of infection has been avoided. Travel spending has risen, propelled by the “prefectural residents discount” program, which provides subsidies for travel within one’s own prefecture, and the “regional block discount” program, which extends the subsidies to travel to neighboring prefectures.

However, due to the suspension of some subsidies and the postponement of the introduction of a nationwide subsidy program, consumption has not recovered to the extent anticipated when measures aimed at stimulating demand were first introduced.

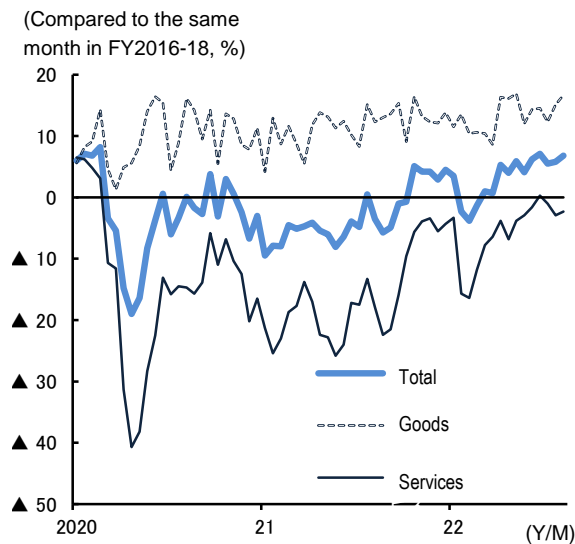
As for goods consumption, although the view that prices are going to keep rising has spurred some people to rush to department stores to purchase luxury items,

automobile sales have stalled. Deliveries have been delayed due to prolonged supply chain turmoil caused by lockdowns and summer power shortages in China.

◆ Services consumption will return to normal soon

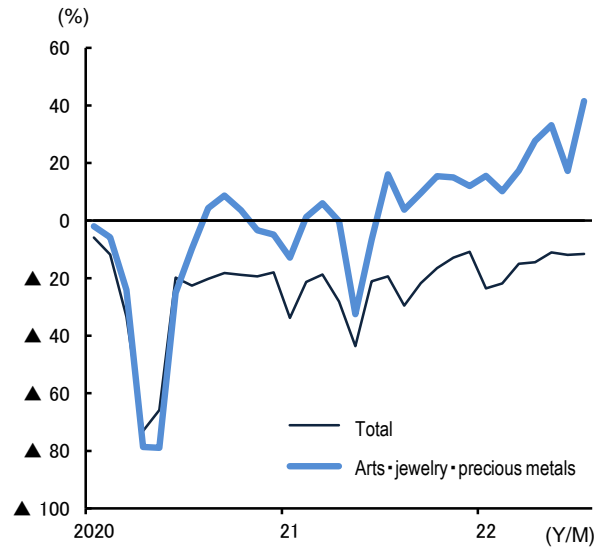
New infections have topped out recently. If the pandemic continues heading into the end phase, the recovery in personal consumption, especially of services, is expected to become clearer. However, rising prices, particularly those of food, energy, and other daily necessities, will increase the burden on households. Although excess savings are expected to offset the negative impact of higher prices, attention needs to be paid to the risk of the consumption recovery being derailed by thrifty spending habits among consumers.

Figure 6-1 Domestic Household Consumption
<JCB consumption now>



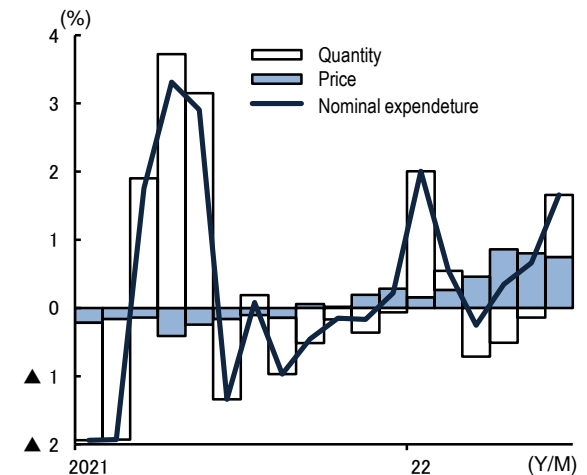
Source: The Japan Research Institute, Ltd. based on data of JCB consumption Now, Google.

Figure 6-2 Department Store Sales
<compared to the same month in 2018>



Source: The Japan Research Institute, Ltd. based on data of Japan Department Stores Association.

Figure 6-3 Description of Change in Household Expenditures



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

Note: Households of 2 or more people.

Topic: The labor shortage in the logistics sector is becoming more serious

◆ The personnel shortage is being driven by both supply and demand factors

With labor shortages becoming more apparent across the economy, the logistics sector is experiencing an increasingly serious shortage of personnel. According to the Bank of Japan's Tankan survey of employment, labor shortages in transportation and postal services have expanded since the end of last year, second only to hotel accommodation, food service, and personal services, whose demand is rapidly recovering following the slump caused by the COVID pandemic.

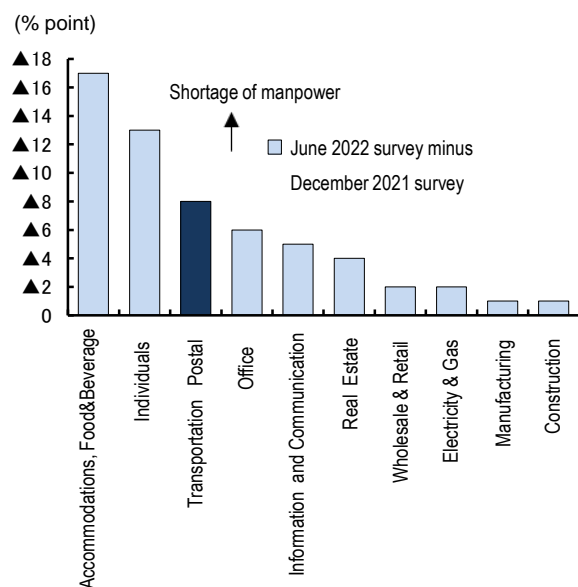
The shortages can be attributed to both supply- and demand-side factors. On the demand side, the rapid expansion of the online market during the pandemic led to a significant increase in parcel traffic. On the supply side, stagnant growth in the number of people wishing to work in the logistics sector can be pointed to as a factor. For example, the Ministry of Land, Infrastructure, Transport and Tourism (MLIT) has highlighted the harsh nature of the work, including low wages and long working hours,

as a reason for the labor shortage. Indeed, overtime hours in the transportation and postal services sector are much longer than in other industries.

◆ Tasks are to improve the working environment and introduce labor-saving measures

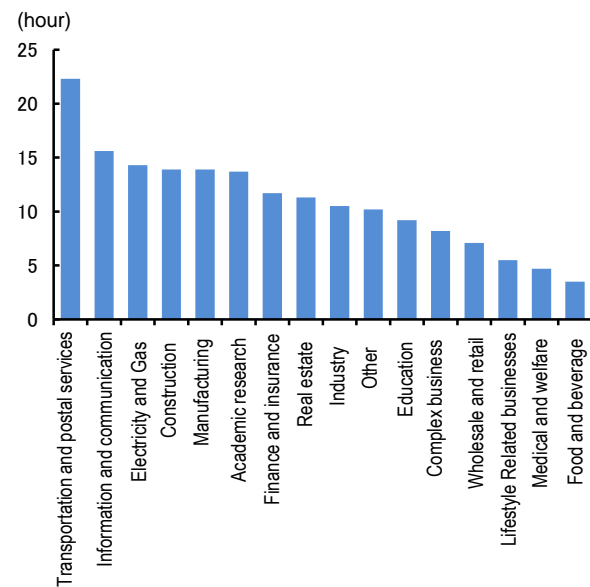
The personnel shortage in the logistics sector is likely to intensify in the future. The number of deliveries per employee is expected to continue to increase, which may lead to even longer working hours. To address the labor shortage, there is an urgent need to improve the pay and conditions of employees and introduce labor-saving measures. However, Japan lags behind other countries in moves to automate deliveries using robots, with such initiatives limited to demonstration experiments and deliveries to remote islands. It is vital to further improve the working environment to treat employees better and save on labor through measures such as deregulation.

Figure 7-1 Change in DI for Employment Headcount



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

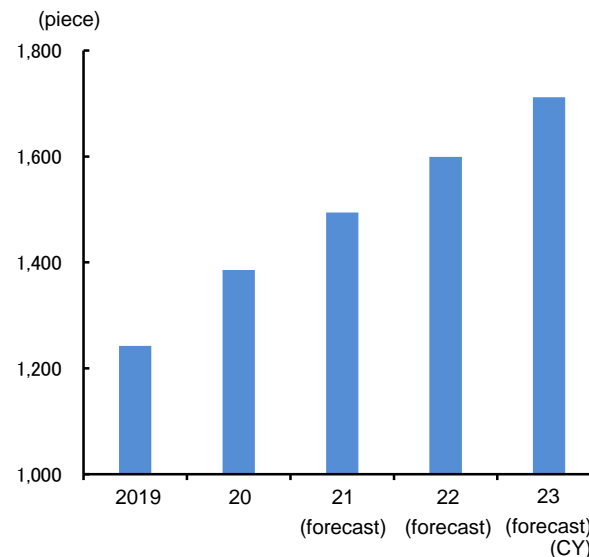
Figure 7-2 Overtime Working Hours by Industry



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

Note: Prescribed monthly working hours in FY2021. Office size is 5 or more employees.

Figure 7-3 Number of Deliveries per Employee



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

Note: Projected figures for FY21 and beyond.

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Prospects for Japan's Economy - Projected Real GDP Change; 1.9% for FY2022 and 1.4% for FY2023

◆ High growth will be sustained for the time being, driven by capital investment and exports

(1) The Japanese government's second quarterly estimate (QE) for the April-June quarter saw the real GDP growth rate revised upward to an annualized +3.5% compared with the previous quarter (or +0.9% compared with the previous quarter) from the first QE figures (+2.2% and +0.5%). By demand category, capital investment was revised upward, as were personal consumption and government spending, though by small margins in the case of the latter two. It has become clear that the domestic economy is picking up.

(2) Looking ahead, the Japanese economy is expected to recover moderately, led by domestic demand. After slowing in the July-September quarter in response to soaring COVID infections, personal consumption is expected to exhibit a clear recovery in October-December and beyond. Although rising energy and food prices will weigh heavily on household purchasing power, household savings accumulated during the COVID pandemic and government measures to ease the pain of higher prices will support personal consumption. Capital investment is expected to continue bouncing back thanks to strong corporate earnings. Investment demand is growing as companies resume investments postponed during the pandemic and take steps to accelerate decarbonization and digitalization. In the manufacturing sector, investment is centered on expanding capacity to supply electronic materials (chemicals sector) and components for electric vehicles (electrical machinery sector). In the non-manufacturing sector, there are numerous redevelopment projects in the Tokyo metropolitan area and new construction projects for logistics facilities.

(3) On the other hand, exports are expected to grow only moderately. Compounding the slowdown in overseas economies, continued lockdowns in some Chinese cities are also acting as a drag on exports.

(4) The growth rate for FY2022 is expected to be strongly positive at +1.9% as the economy rebounds from the COVID pandemic slump. In FY2023, growth is expected to cool to +1.4%, a pace that will still exceed the potential growth rate. However, factors such as the slowdown in overseas economies will weigh on GDP, and recovery to the pre-COVID peak (April-June 2019) is set to be delayed to FY2024.

Figure 8 Projections for GDP Growth and Main Indicators of Japan (as of September 8, 2022)

| | (seasonally adjusted, annualized % changes from the previous quarter) | | | | | | | | | (% changes from the previous fiscal year) | | |
|---|---|---------|--------------|--------|--------|--------|--------|--------|--------|---|--------------|---------|
| | CY2022 | | | | CY2023 | | | | CY2024 | FY2021 | FY2022 | FY2023 |
| | 1~3 | 4~6 | 7~9 | 10~12 | 1~3 | 4~6 | 7~9 | 10~12 | 1~3 | (Actual) | (Projection) | |
| | (Actual) | | (Projection) | | | | | | | | | |
| Real GDP | 0.2 | 3.5 | 1.1 | 2.2 | 1.8 | 1.4 | 1.1 | 0.9 | 0.9 | 2.3 | 1.9 | 1.4 |
| Private Consumption Expenditure | 1.2 | 4.8 | 0.8 | 2.4 | 1.8 | 1.2 | 1.0 | 0.8 | 0.8 | 2.6 | 3.0 | 1.3 |
| Housing Investment | ▲ 5.6 | ▲ 7.3 | 3.4 | 1.8 | 1.8 | 1.8 | 0.2 | 0.0 | ▲ 0.1 | ▲ 1.6 | ▲ 3.0 | 1.2 |
| Business Fixed Investment | ▲ 0.5 | 8.3 | 4.0 | 3.6 | 3.4 | 2.8 | 2.4 | 2.2 | 2.2 | 0.6 | 3.1 | 2.9 |
| Private Inventories (percentage points contribution) | (2.2) | (▲ 1.1) | (▲ 0.4) | (0.0) | (0.0) | (0.0) | (0.0) | (0.0) | (0.0) | (0.1) | (0.0) | (▲ 0.0) |
| Government Consumption Expenditure | 1.6 | 2.8 | 0.5 | 0.5 | 0.4 | 0.4 | 0.2 | 0.2 | 0.2 | 2.0 | 1.3 | 0.3 |
| Public Investment | ▲ 12.3 | 3.8 | 3.4 | 2.8 | 2.0 | 1.4 | 0.8 | 0.2 | 0.2 | ▲ 7.5 | ▲ 2.6 | 1.4 |
| Net Exports (percentage points contribution) | (▲ 1.7) | (0.4) | (0.0) | (0.0) | (0.0) | (0.0) | (0.0) | (0.0) | (0.0) | (0.0) | (▲ 0.2) | (▲ 0.0) |
| Exports of Goods and Services | 3.6 | 3.7 | 1.8 | 1.6 | 1.6 | 1.4 | 1.4 | 1.2 | 1.2 | 12.5 | 2.6 | 1.5 |
| Imports of Goods and Services | 14.8 | 2.7 | 0.6 | 2.8 | 2.8 | 2.4 | 2.0 | 2.0 | 2.0 | 7.2 | 3.6 | 1.3 |
| (Ref.) Domestic Private Demand (percentage points contribution) | (2.6) | (2.5) | (0.7) | (2.0) | (1.6) | (1.2) | (1.0) | (0.8) | (0.8) | (1.5) | (2.1) | (1.2) |
| (Ref.) Public Demand (percentage points contribution) | (▲ 0.4) | (0.8) | (0.3) | (0.2) | (0.2) | (0.2) | (0.1) | (0.1) | (0.1) | (▲ 0.0) | (0.1) | (0.1) |

| | (% 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 GDP | 0.2 | 1.2 | 2.2 | 2.8 | 3.0 | 2.8 | 2.5 | 1.9 | 1.7 | 1.3 | 2.3 | 2.2 |
| GDP deflator | ▲ 0.5 | ▲ 0.3 | 0.1 | 0.9 | 0.7 | 1.0 | 0.9 | 0.6 | 0.6 | ▲ 1.0 | 0.4 | 0.8 |
| Consumer Price Index (excluding fresh food) | 0.6 | 2.1 | 2.6 | 3.0 | 2.5 | 1.8 | 1.4 | 0.8 | 0.7 | 5.7 | 2.5 | 1.2 |
| Unemployment Rate (%) | 2.7 | 2.6 | 2.5 | 2.5 | 2.5 | 2.5 | 2.4 | 2.4 | 1.0 | 2.8 | 2.5 | 2.4 |
| Exchange Rates (JY/US\$) | 116 | 130 | 136 | 140 | 138 | 137 | 136 | 134 | 133 | 112 | 136 | 135 |
| Import Price of Crude Oil (US\$/barrel) | 85 | 109 | 107 | 103 | 104 | 101 | 100 | 99 | 98 | 76 | 106 | 100 |

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.