

Global Watch

February 2010

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This is an abstract of our monthly reports on the Japanese Economy. The information and the views contained herein are subject to change without notice.



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§Japanese Economy

1. Overview of the economy

The economy is continuing to show improvement, but there are signs of a weakening of momentum in some sectors.

By Shinichiro Kobayashi, Senior Economist

The Japanese economy is continuing to show improvement. However, the level of economic activity is still relatively low, and signs have begun to emerge of a weakening of the momentum of the pace of improvement.

The initial quick estimates of real GDP growth in the October-to-December quarter (scheduled to be announced on February 15) are expected to show positive growth over the previous quarter, as in the previous quarter, and there is a possibility that the rate of growth may rise. As exports continue to perform robustly, the external sector is expected to continue to be the overall driving force for growth. However, there is a strong possibility that domestic demand may rise for the first time in seven quarters, since personal consumption is expected to hold firm, and capital investment is believed likely to begin to show positive growth.

Production activity in the manufacturing sector is maintaining an upward trend, and the index of mining and manufacturing production in December rose 2.2% over the previous month, the 10th consecutive month-to-month increase. As a result, production in the October-to-December quarter posted a gain of 4.6% over the previous quarter, the third consecutive quarter of firm growth in this indicator. Exports, which are the driver of these increases, are continuing to hold steady. Real exports in December were up 2.8% month to month and grew at a faster pace than production as a whole. By industry, both production and exports were strong in the electronic parts and devices industry, supported by the bottoming out in the worldwide semiconductor industry. The information and telecommunications industry, which includes flat-panel-display (FPD) TVs, also reported robust sales in Japan and overseas, and general machinery, along with certain other industries, has finally begun to bottom out, led principally by external demand.

Consumer spending is also showing a favorable performance, led by consumer durables. For example, in January, the number of new automobile registrations stood at 42.8% above the level of the same period a year earlier, and sales of FPD TVs posted a year-on-year gain of 69.3%, thus both continuing to show high rates of expansion in unit sales. Moreover, according to the October-to-December household expenditure survey, consumption expenditures in real

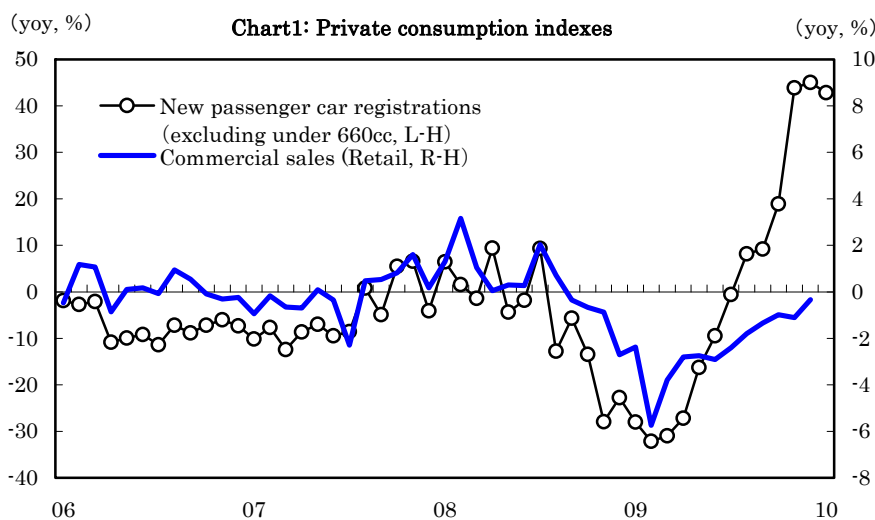
terms (by households with two or more persons) rose for the third consecutive quarter, especially outlays for automobile-related and education/entertainment related goods and services. In the October-to-December quarter, these real consumption expenditures were up 1.8% from the previous quarter, and the margin of increase is expanding. Also, the unemployment rate in November moved upward slightly to 5.2%, but then declined to 5.1% in December. These data suggest that, while the economic environment remains harsh, a substantial worsening of conditions seems to have been avoided. In addition, the number of new housing starts (on a seasonally adjusted basis) in December rose for the fourth consecutive month, to approximately 819,000, suggesting that trend toward improvement is growing stronger.

On the other hand, the momentum of improvement in the economy as a whole seems to be showing signs of weakening. The forecast index for manufacturing production calls for a 1.3% month-to-month increase in January, thus holding firm, but a slight increase of only 0.3% is forecast for February, suggesting the possibility that actual results may show a decline. In addition, the pace of expansion in automobile exports is weakening according to the most-recent data. These and other indicators suggest that in some industries the movement toward restocking of inventories in overseas markets may have run its course. The export environment is not unfavorable, as the United States and China are still reporting steady economic recovery, but the momentum of expansion in exports seems to be gradually weakening.

Additionally, the income environment in Japan continues to be harsh. Total cash earnings in December showed a continued substantial decline of 6.1% compared with the same period of the previous year. Although nonscheduled salary payments were at about the same level as for a year earlier, the decrease in year-end bonuses was the principal reason for the decline. As a result, the divergence between movements in income and consumption is increasing. Amid these conditions, consumer psychology is deteriorating, and in December the index of consumer attitudes declined for the second consecutive month. If consumer psychology continues to deteriorate, there is concern that this may have an impact on consumer spending.

Thus far, the positive effects of government policies and the rebound following the sudden decline in the economy last year have accelerated the pace of improvement in the economy. However, the portion of the impetus toward improvement coming from the rebound cannot continue indefinitely. There is a possibility that the rebound effect may wear off as the end of the fiscal year approaches.

(2010.2.8)



Source: Japan Automobile Dealers Association, Ministry of Economy, Trade and Industry

2. Topic of the month

Consumers becoming more thrift-conscious

By Shinichiro Kobayashi, Senior Economist

Although sales of eco-cars, FPD TVs, and other big-ticket consumer durables are holding strong and consumer spending overall remains firm, there are signs of a diversity of underlying trends. These include the recent closing of some stores by long-established department stores. Since incomes are declining, the amount of money that households can allocate for consumer spending is limited as long as they do not increase their borrowings or sell financial assets. Under these circumstances, consumers are prone to become more thrift-conscious. The effects of this are especially apparent in the decline in the number of persons patronizing restaurants and service establishments and the rates of utilization of these outlets. In addition, spending per customer has continued to decline unchecked.

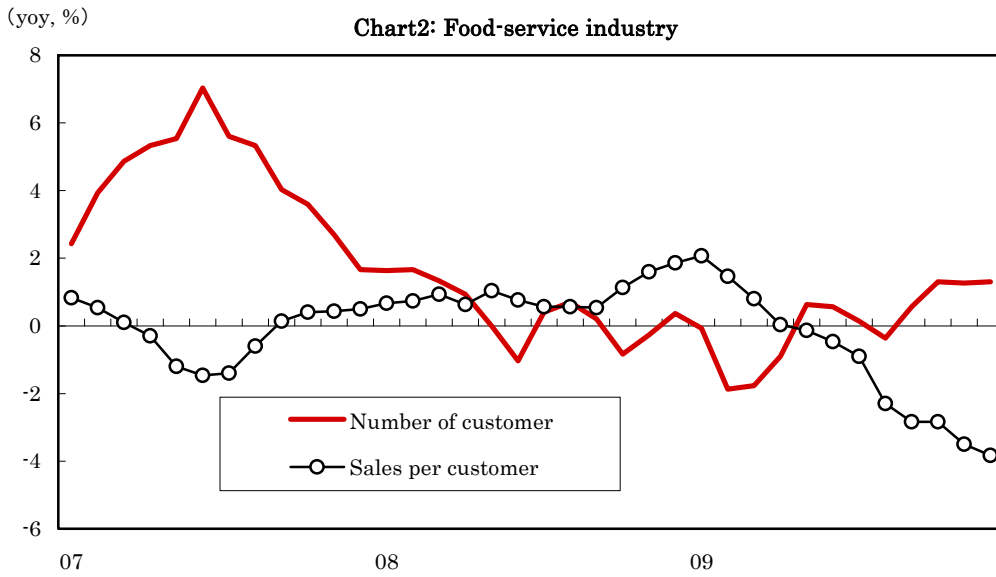
Chart 2 shows trends compared with the previous year in the number of customers of restaurants and similar establishments (adjusted for changes in the number of such outlets) and the average expenditure per customer. Recently, there has been a suggestion of an upward trend in the number of people eating out, but the expenditure per customer has continued to decline. Chart 3 shows the utilization rates of inns and other establishments in the accommodations business as well as the total spending per capita of customers of these

establishments. Since 2007, the rate of utilization has declined sharply, and, since 2008, average expenditure per customer has begun to drop, indicating that conditions are severe both in terms of the number of visitors and the amount they spend. In addition, average spending by customers eating out has decreased to about 93% of the peak level, while average spending on accommodations has fallen to about 75% of the peak level. (Average spending for nightly accommodations in the early 1990s was 1,000 yen recently, this has dropped to 16,000yen.)

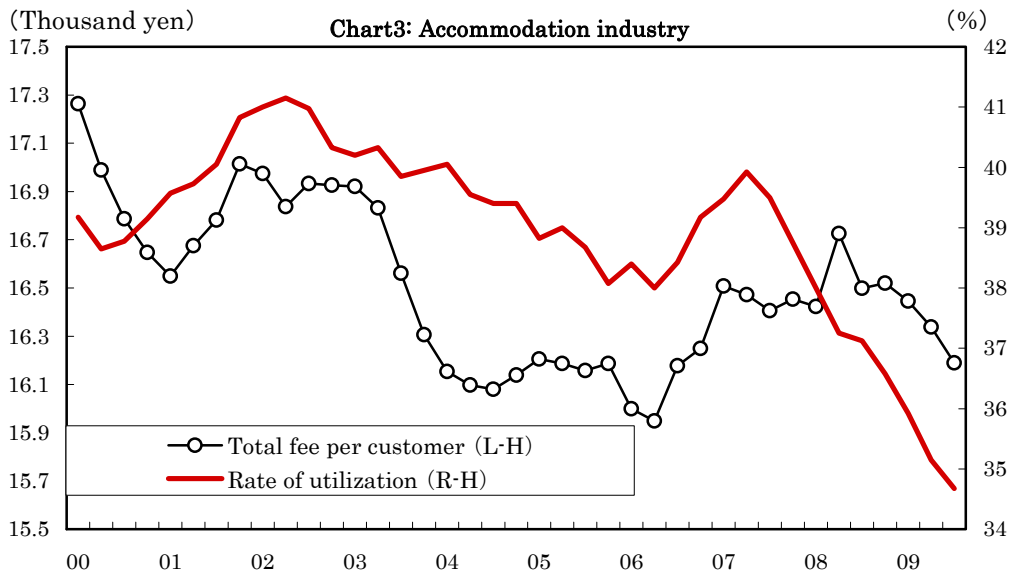
The growing thrift-consciousness of consumers is likely to have an effect on the average expenditure per customer in such cases as the following: (1) when prices of similar goods and services decline, (2) when consumers show a stronger preference for lower-value-added goods and services, and (3) when consumers buy a smaller number of goods and services per capita. In case (1), this means that the drop in demand is bringing a decline in prices. In case (2), consumers experience a growing preference for lower-priced goods and services. In other words, consumers substitute lower-priced goods for the more-expensive ones they bought before. In case (3), in the restaurant industry, for example, consumers now tend to buy three items per meal, compared with four items previously. In the accommodations industry, consumers forego the option of purchasing additional goods and services at inns and hotels.

The income environment is expected to remain harsh for the time being. Accordingly, there is concern that the level of spending per customer may continue to decline.

(2010.2.8)



Note: The number of customers is adjusted along with the change in number of outlets.
 Figures are the three month backward moving average.
 Source: Japan Foodservice Association



Note: Total fee per customer is the total expenditures per guests.
 Figures are the four-quarter backward moving average.
 Source: Japan Ryokan & Hotel Association