

Global Watch

April 2010

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The information and the views contained herein are subject to change
without notice.



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§Japanese Economy

1. Overview of the economy

After entering the new fiscal year, the pace of improvement in the economy is slowing.

By Shinichiro Kobayashi, Senior Economist

The trend toward improvement in Japan's economy is continuing. There are signs that the bottoming out in corporate capital investment and the employment and income environments, where conditions had been stagnant, is becoming more broad-based. However, thus far, the momentum of improvement has been relatively strong, partly because of reactions to previous declines, but is now forecast to weaken gradually going forward.

According to the Bank of Japan's Tankan survey (Short-Term Survey of Enterprises in Japan) for March, which was released on April 1, the diffusion index (DI) measuring sentiment regarding economic conditions among large corporations in the manufacturing sector posted an improvement of 11 points from the previous quarter. The DI rose to -14 (the number of "favorable" responses minus "unfavorable" responses), the fourth consecutive quarterly improvement. Factors supporting this improvement in sentiment are the continuing increase in exports and the upward trend in industrial production because of the progress toward inventory adjustments and the positive effects of government economic policies. The outlook is for the pace of improvement in sentiment to become more gradual as the additional boost provided by government policies for the automobile and other industries begins to weaken and the rise in raw material prices brings a deterioration in the terms of trade, mainly in the basic materials industries. Nevertheless, the trend toward improvement in sentiment is expected to continue because of the increase in exports and other factors. In addition, the DI measuring views of economic conditions among large corporations in the non-manufacturing sector in the latest Tankan showed an improvement of seven points over the previous quarter. Although the margin of improvement is not as large as in the manufacturing sector, sentiment regarding economic conditions is continuing to improve.

Sentiment among small and medium-sized enterprises (SMEs) in the manufacturing sector also posted marked improvement, and view of economic conditions among SMEs in the non-manufacturing sector showed moderate improvement. However, in part because SMEs are more dependent on domestic demand, they show more deep-rooted cautionary attitudes, and the expectations in both the manufacturing and non-manufacturing sectors are for

deterioration going forward.

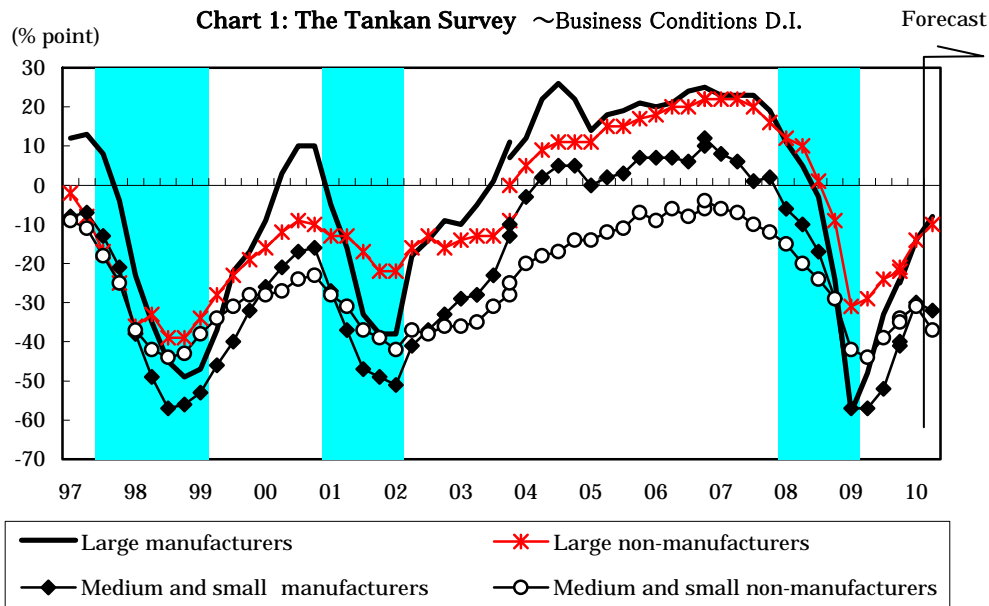
While employment conditions are harsh, improvement is continuing now that the worst phase of the downturn has passed. The peak rate of unemployment, which was 5.6%, was recorded last July, and, as of January and February this year, the unemployment rate had dropped to 4.9%. In addition, total cash compensation of workers on a per-capita basis in February was 0.6% below the same month of the previous year, but the margin of decline is shrinking. Although scheduled wages remain below those of the previous year, nonscheduled compensation is rising, mainly in the manufacturing sector, and this improvement is contributing to the shrinkage in the overall margin of decline in wages.

Personal consumption is holding firm. According to the February Survey of Households, real consumption (for households of two-or-more persons) was down a substantial 1.6% from the level of the previous month. However, there is a possibility that this decline may have been due to the sampling methods. Commerce (retail) sales in February and new automobile registrations in March continued to be strong. Although employment and income conditions are showing improvement, this appears to be due to the boost provided by the positive effects of government policies.

On the other hand, mining and manufacturing production in February declined 0.9% from the previous month, the first drop in a year, because of decreases in the production of transportation equipment, information and telecommunications equipment, and other industries. This suggests that production, which had been on a robust upward trend, has paused temporarily. According to the production forecast survey, output is expected to rise 1.4% in March, and then decline again by a marginal 0.1% in April. Although production will remain on an upward trend, the pace is expected to become more moderate. However, real exports in February were 1.1% over those of the previous month, for their 12th consecutive monthly rise. This and other factors indicate that exports are continuing on a robust trend. Therefore, there appears to be little reason for concern at present that production will lose momentum.

The movement toward improvement in the economy is expected to continue, but unlike the previous fiscal year, the momentum of improvement will probably weaken gradually. Consumer spending, in particular, is continuing to be strong for the time being because of the positive impact of government policies, but in the latter half of this fiscal year, the effects of these policies will run their course, and the risk of a sudden decline in consumption will remain.

(2010.4.8)



Note: Shaded areas indicate the recession periods according to the Cabinet Office, except the latest bottom, which is our own estimate. Due to revision, data are not comparable before and after March 2004, March 2007 and March 2010.

Source: Bank of Japan

2. Topic of the month

The level of business plans according to the Bank of Japan's Tankan survey

By Shinichiro Kobayashi, Senior Economist

The Bank of Japan's Tankan survey for March clarified corporate capital investment plans for fiscal 2010 (ending March 31, 2011). According to the survey, capital spending will be reduced marginally, with large corporations in the manufacturing sector lowering capital investments by 1.0% from the previous fiscal year, and large non-manufacturing enterprises cutting investment spending by 2.4%. Since capital investment plans among large corporations tend to be understated in March, there is a possibility that growth in capital investment in fiscal 2010 may be positive. In addition, according to GDP statistics, private capital investment has already reached bottom on a nominal basis.

In general, the Tankan reviews rates of growth of items contained in corporate business plans, including capital investment in most cases; however, it presents both actual amounts of capital investment and planned amounts, thus making it possible to see the actual

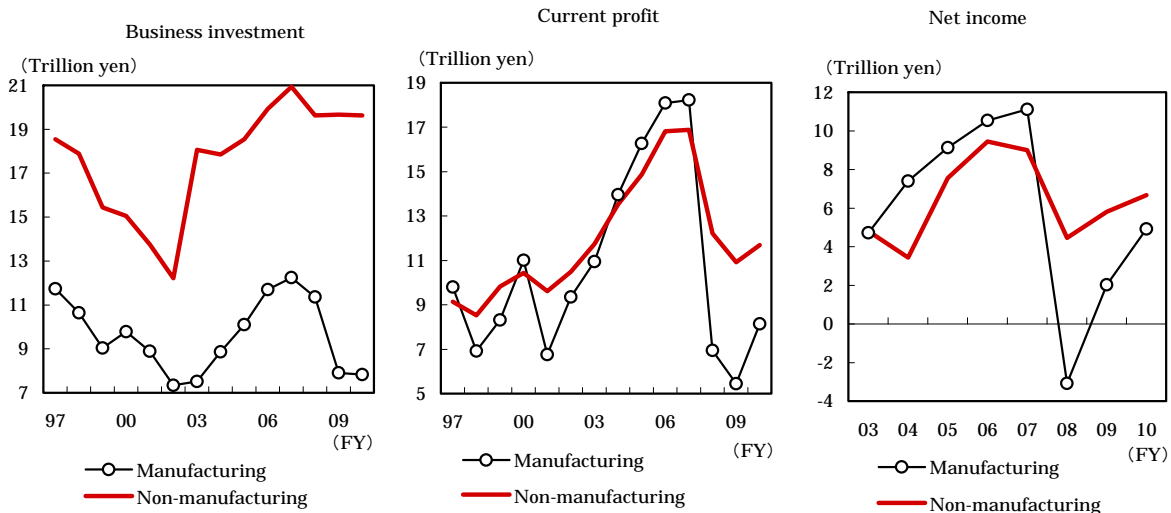
levels. According to the Tankan, in the manufacturing sector, the level of capital investment plans in fiscal 2010 will be only 63.1% of the previous peak level. On the other hand, capital investment in the non-manufacturing sector will be 93.7% of the previous peak, indicating that non-manufacturing companies are maintaining a relatively high level of capital investment (Refer to the chart.).

Similarly, according to the Tankan, plans for ordinary profit of large corporations in fiscal 2010 show a sharp recovery of 49.3% over the previous fiscal year in manufacturing, but the actual level of ordinary profit will be only 44.6% of the previous peak. On the other hand, plans for ordinary profit of non-manufacturing companies call for a small increase of 7.1% over the previous year; however, since the decline during fiscal 2008 in this sector was relatively small, ordinary profit in fiscal 2010 is expected to recover to 69.3% of the previous peak. In addition, according to corporate plans, net income in the manufacturing sector will only recover to 44.3% of the previous peak, but ordinary profit in the non-manufacturing sector will recover to 70.5% of the previous peak.

As these comments suggest, even small increases in monetary terms will appear to be sharp increases in percentage growth terms when the figures for the previous year, which are the points of comparison, are low. Since many of the figures being used for the comparisons date from the period following the collapse of Lehman Brothers Holdings, some caution is in order when using these statistics.

(2010.4.8)

Chart2: Annual projections based on the Tankan Survey



Note1: All Figures are those of large enterprises'. Data of FY2009 are estimated amount, and those of FY2010 are the planned amount as of March 2010 survey.

Note2: Due to revision of the companies surveyed, the continuity of the data is not maintained.

Note3: Business investment includes land purchase, but excludes software investment.

Source: Bank of Japan