

Economic Report

Global Watch August 2016

1. Overview of the Japanese Economy: Remains Roughly Flat

By Shinichiro Kobayashi, Principal Economist

The economy remains roughly flat with some weaker trends seen previously retreating.

The real GDP in the April-June quarter was virtually unchanged (+0.2% at an annualized rate). Domestic demand continues to be firm, but, reflecting the weakness in exports, the contribution of the external sector is a somewhat large negative figure and tended to act as a drag on the overall economy. However, at present, the economy is thought likely to be firming up a foothold for improvement, and, going forward, there is a possibility that conditions in the economy may grow brighter.

First, industrial production, which had been weakening, has reached bottom. Industrial production in June (final figure) increased 2.3% over the previous months with gains in a wide range of industries, including comebacks in transportation equipment and other sectors. Since overseas demand for materials for smartphones and capital equipment is weak, we cannot rule out the risk of a downturn, but surveys of industrial production forecasts call for robust increases in July and August (2.4% and 2.3%, respectively), and there is a possibility of improvement going forward.

On the other hand, at present, capital investment and exports both lack strength. In the real GDP data for the April-June quarter, real private capital investment declined for the second consecutive quarter. However, the need for investments to maintain and replace existing equipment is thought likely to be strong, and, even though corporate performance is weakening at present, corporations still have ample cash on hand, and investment is not likely to continue on a declining trend. Real exports in the April-June quarter were weak, declining 1.5% from the previous quarter, but there are some positive movements that are gradually emerging, including production in expectation of a comeback in automobile exports, which have been stagnant.

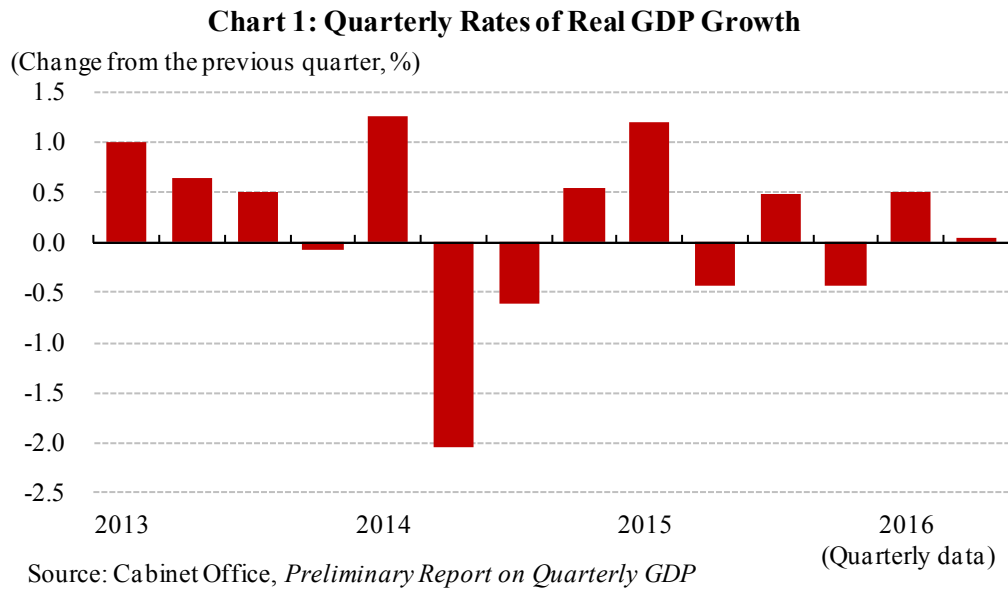
In the household sector, the supply and demand balance for labor remains tight, and the unemployment ratio in June declined to the lowest level since the previous low of 3.1% in July 1995. In addition, the ratio of job openings to job seekers rose to 1.37 in June, the highest level since August 1991. However, these favorable movements are just not bringing increases in wages. In June, total per capita cash compensation of workers (preliminary figure) increased 1.3% over the same month of the previous year, but this was because non-scheduled wage payments, including summer bonuses, rose 3.3% year on year, in part as a reaction to low payments in the

previous year. Regularly scheduled wages were up only 0.1%, suggesting the improvement in this indicator has paused.

Personal consumption remains virtually flat, reflecting the delayed recovery of consumer confidence and deep-rooted frugality among households. Real expenditures in the June Survey of Family Income and Expenditures (covering households of two or more persons, seasonally adjusted) declined 1.1% from the previous month, the second consecutive monthly decline. However, the consumer price index (comprehensive index, excluding fresh food) in June had declined to 0.5% below the same month of the previous year, suggesting this may provide a tailwind and give some impetus to consumer spending. In nominal terms, the improvement in total cash compensation has paused, but, in real terms, cash compensation in June was up year on year for the fifth consecutive month (rising 1.8% year on year).

Judging from the fact that wage increases during the spring labor offensive this year weakened and the deterioration in corporate performance, wages are forecast to remain virtually level for the time being. However, since the decline in natural resource prices and the drop in import prices due to the appreciation of the yen may continue, there is a strong possibility that consumer prices will continue to be below previous-year levels, and this is likely to be a factor supporting consumption due to the boosting effect on real incomes.

In addition, there are some positive trends, including the receding of the temporary gloomy mood surrounding future trends in overseas economies because of the bottoming out of commodity market prices, the view that the timing of increases in U.S. interest rates would be postponed, and the correction of the high value of the dollar. The confusion that followed the exit of the United Kingdom from the EU is gradually quieting down, and turmoil in international financial markets is receding, suggesting that the repercussions of the U.K.'s exit from the EU may be marginal. For these reasons, the forecast is for the world economy to show moderate recovery, and Japan's exports will improve gradually. Moreover, private capital investment may shift to a moderate rising trend and the supplementary budget for fiscal 2016 will give a positive boost to the economy through the end of the fiscal year. Although the rekindling of concerns about the slowdown in overseas economies and the risk of a downturn will remain, looking ahead, the movements toward improvement in the Japanese economy are expected to spread gradually. (2016.8.10)



2. Topic of the Month: Do the Olympics Boost Consumer Spending?

By Ruriko Toshida, Economist

The July 2020 Tokyo Olympics are now less than four years from now, and construction on the main stadium has begun. Construction demand is expected to reach a peak in 2018, but the positive impact of the games on consumer spending is thought likely to rise as 2020 approaches.

To confirm this, we investigated trends in retail sales (in nominal terms) around the month when the past three Summer Olympic Games were held (Chart 2).

First, in Greece, where the 2004 Summer Olympics were held, although we found that the Olympics boosted retail sales, then peaked four months prior to the Olympics, and followed a declining trend thereafter. After the Olympics, there was a reactionary decline and retail sales deteriorated.

At the time of the 2008 Olympics in Beijing, although consumption rose in the midst of China’s high economic growth, it peaked at the time the games were held and growth slowed thereafter. Subsequently, with the collapse of Lehman Brothers Holdings in September 2008 and the sudden downturn in the world economy, consumption was adversely affected, and the growth rate declined further.

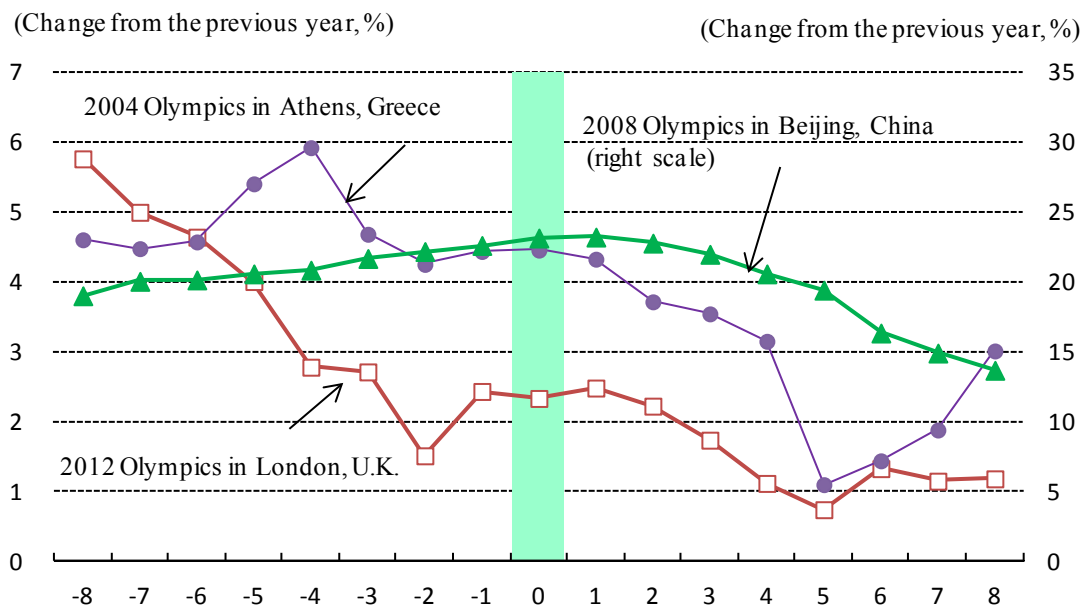
At the time of the London Olympics in 2012, along with the sudden decline in the rate of price increases, the growth rate of retail sales shrank. Retail sales showed a slight improvement at the time the games were held, but deteriorated thereafter.

As these data show, although the economic environment prevailing at the time played a role in influencing retail sales, in the midst of major trends, consumption received a slight boost during the month when the games were

held, but tended to stagnate thereafter.

In the case of the 2020 Tokyo Olympics, the games will take place after an increase in Japan's consumption tax in October 2019. Just as after the increase in the consumption tax in April 2014, consumer demand will likely show a surge prior to the tax hike, followed by a reactionary decline, and then there is a possibility that consumption may move into a prolonged slump. Under these circumstances, even if the holding of the Olympics gives a temporary boost to consumption, the positive effects will run their course in a short period of time and there is a possibility that, after the games, consumer spending may worsen. This points to the conclusion that we should not rely excessively on the Olympics to boost consumer spending. (2016.8.10)

Chart 2: Trends in Nominal Retail Sales before and after the Olympic Games



Notes:

1. When the games were held in two consecutive months, the longer of the two is defined as zero.
2. Three-month lagging moving averages
3. Data sources are the U.K. National Statistics Bureau, China Statistics Bureau, and Eurostat.

(Month when games were held = 0)

- This report is based on information believed to be reliable, but we do not guarantee its accuracy.
- This report is intended only for information and should not be construed as solicitation to take any action such as purchasing/selling/investing financial market products. In taking any action, each reader is requested to act on the basis of his or her own judgment.
- Use of this report is limited to "reproduction for personal use" or "quotation" as stipulated in the Copyright Law. For such use, please explicitly cite this report as the source of the information or quotation.
- Any use that exceeds the scope of "reproduction for personal use" or "quotation" requires explicit permission for such use from us prior to its use.