

Abenomics and the Outlook for the Japanese Economy

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FPCJ Press Briefing

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■ Three Arrows of Abenomics

1. Bold monetary policy
2. Flexible fiscal policy
3. Growth strategy to encourage private investment

■ Quantitative and Qualitative Monetary Easing (QQE)

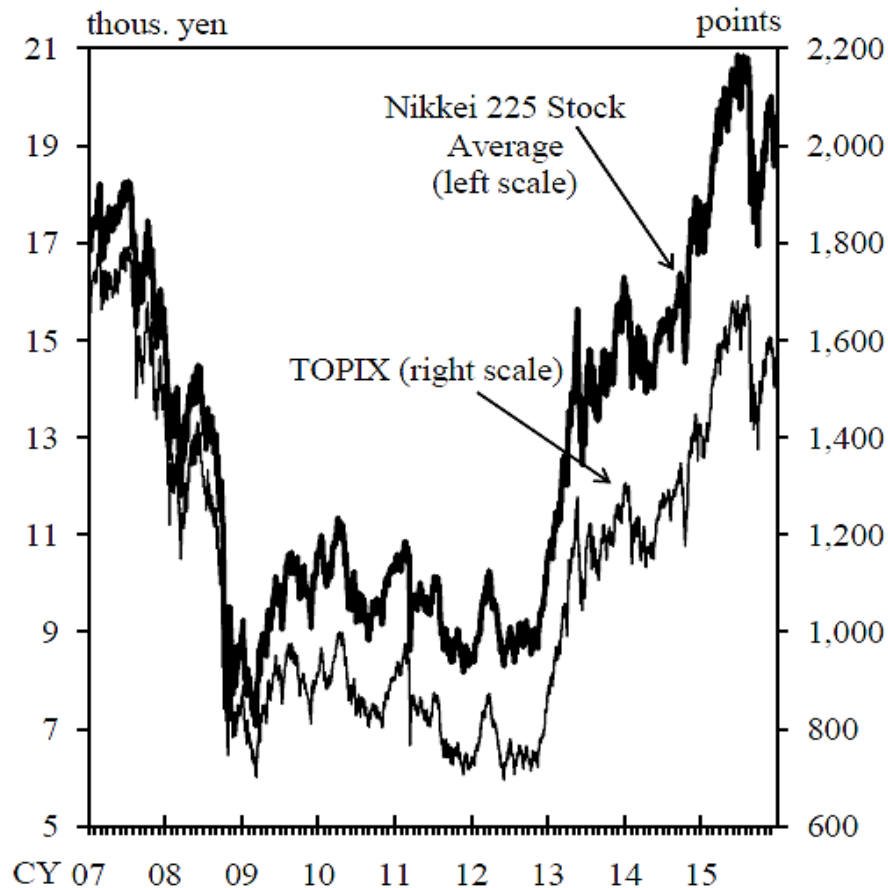
1. To achieve 2% inflation target in 2 years
2. To increase monetary base
3. To increase the purchase of long-term JGB

■ BoJ has decided to introduce negative interest rates on excess reserve, as massive purchase of JGB approaching the limit of market capacity.

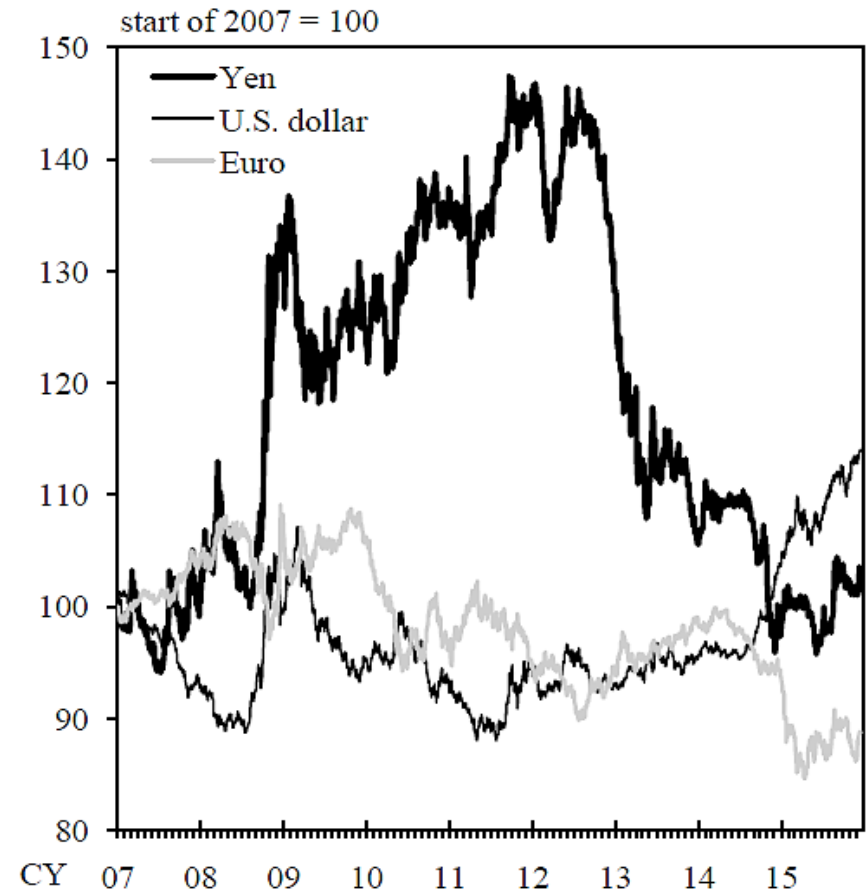
Achievements (1)

- QQE affected asset prices dramatically, higher stock prices and a weaker yen.

(1) Japanese Stock Prices



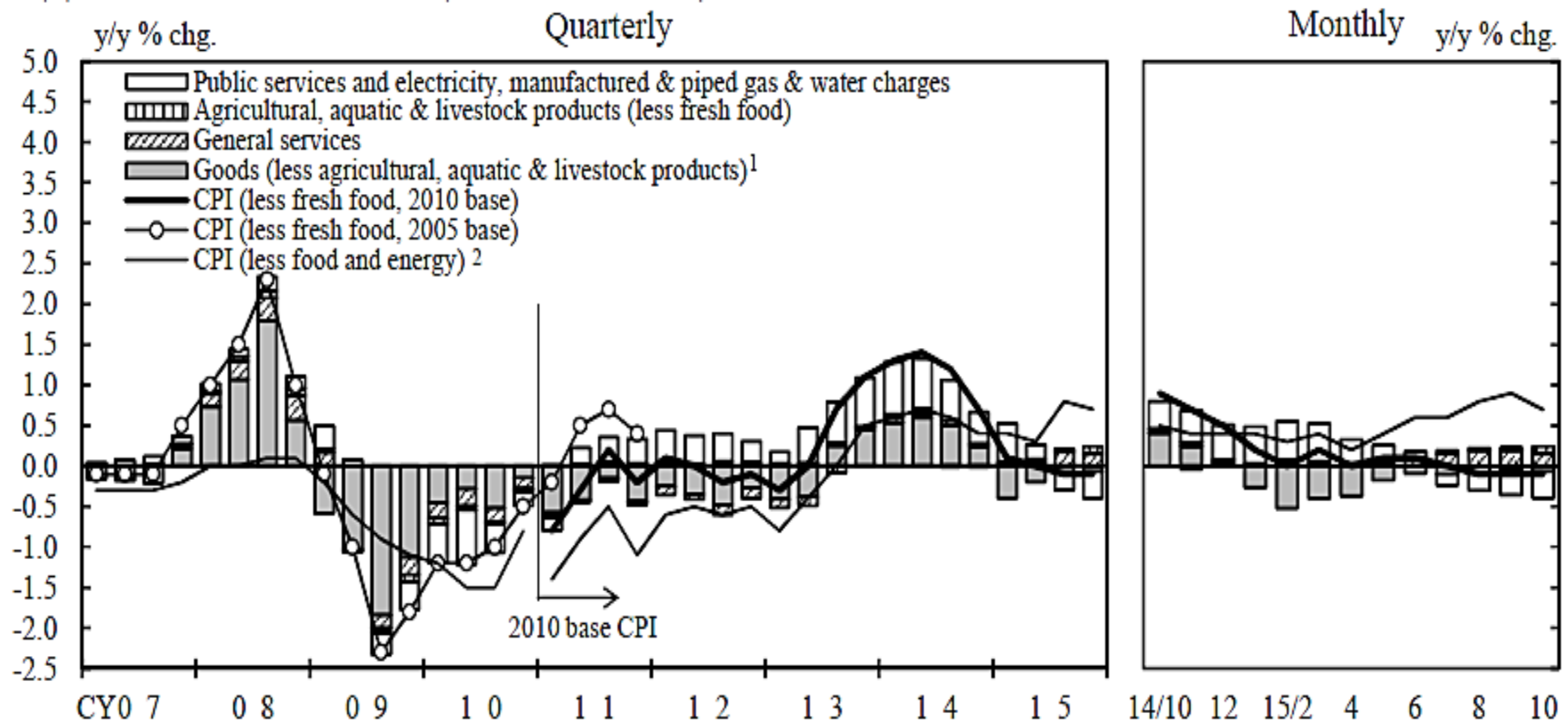
(2) Nominal Effective Exchange Rates



Achievements (2)

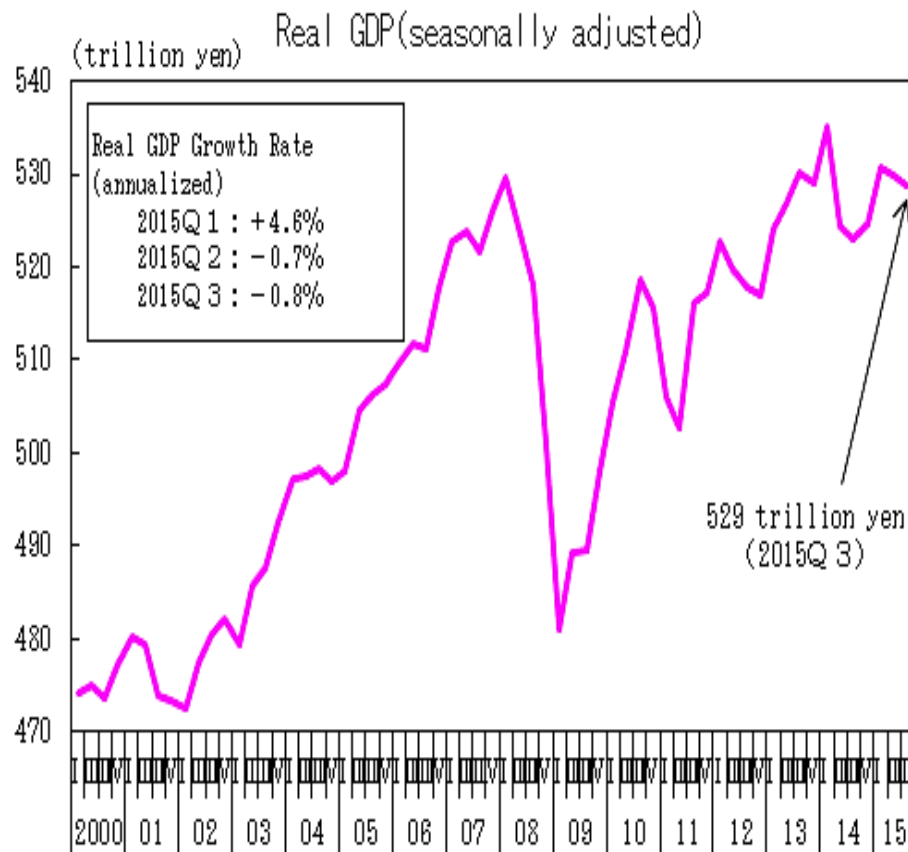
- CPI inflation rate has turned positive. Though core CPI came down to around zero, core CPI ex energy rose to + 1% year on year. But 2% target seems still far away.

(CPI inflation rate, % change year on year)

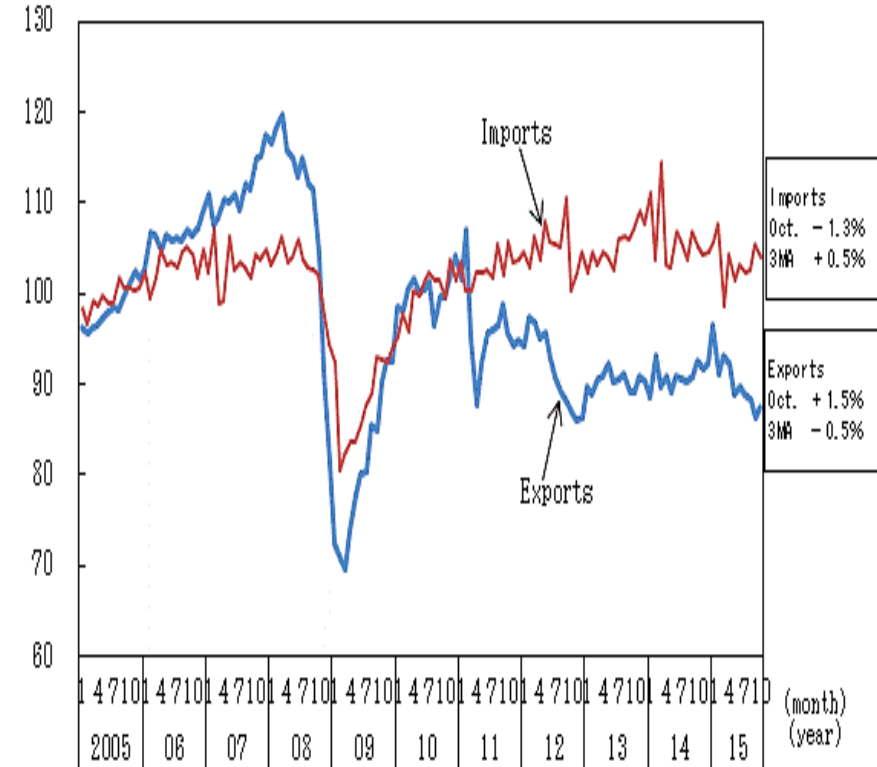


Disappointments (1)

- Overall growth remains slow. No visible acceleration seen.
- Despite substantial depreciation of yen, exports remain surprisingly weak.

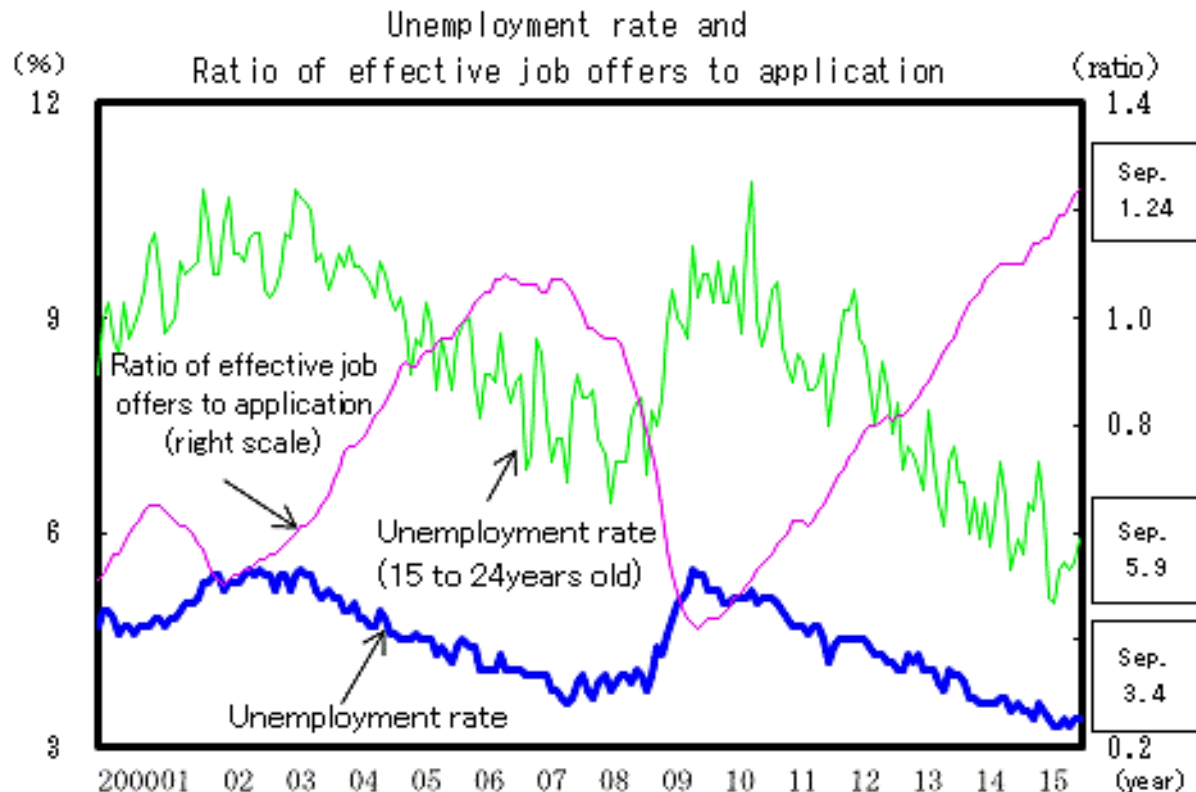


Exports and Imports Volume Index Trend (seasonally adjusted) (2010 = 100)



Surprise

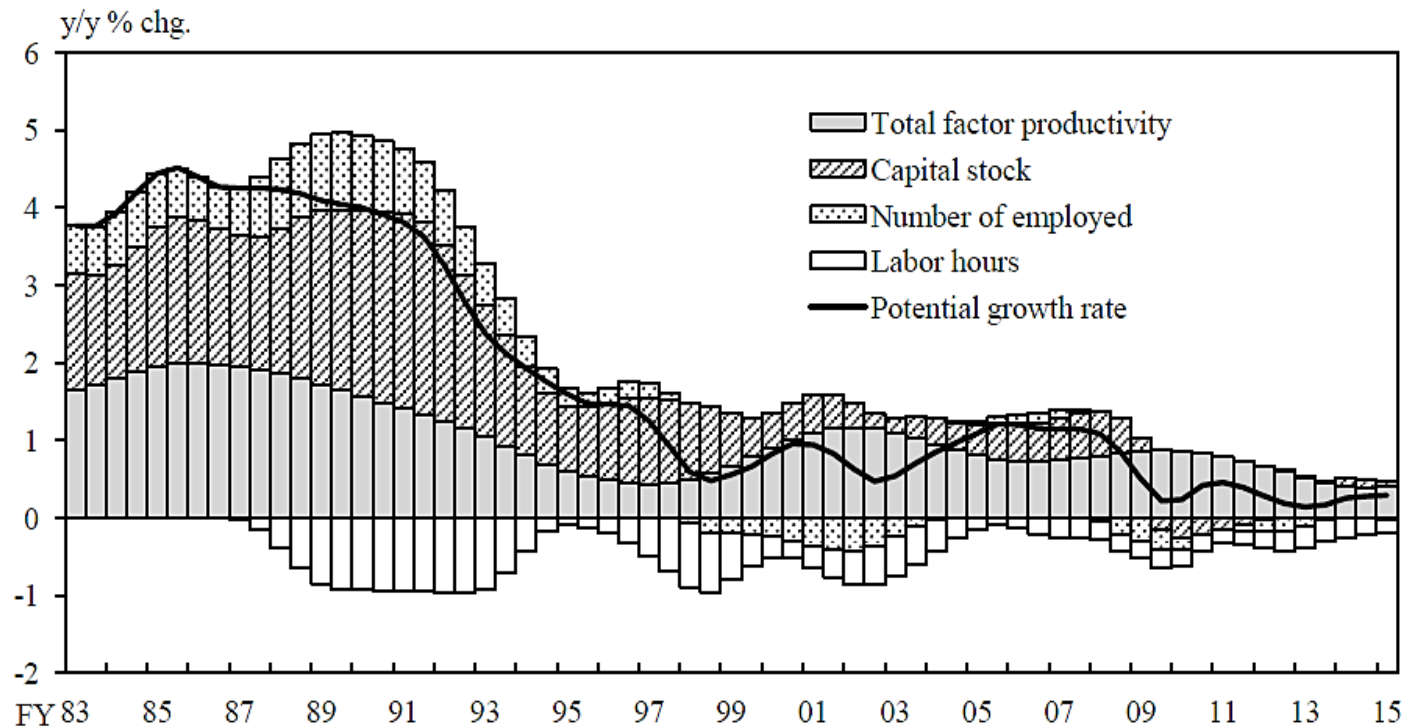
- Even with slow growth, unemployment rate has come down below 3.5%, suggesting the realization of “full employment”.
- This is largely due to the decrease in labor force reflecting rapid ageing of population.



Disappointment (2)

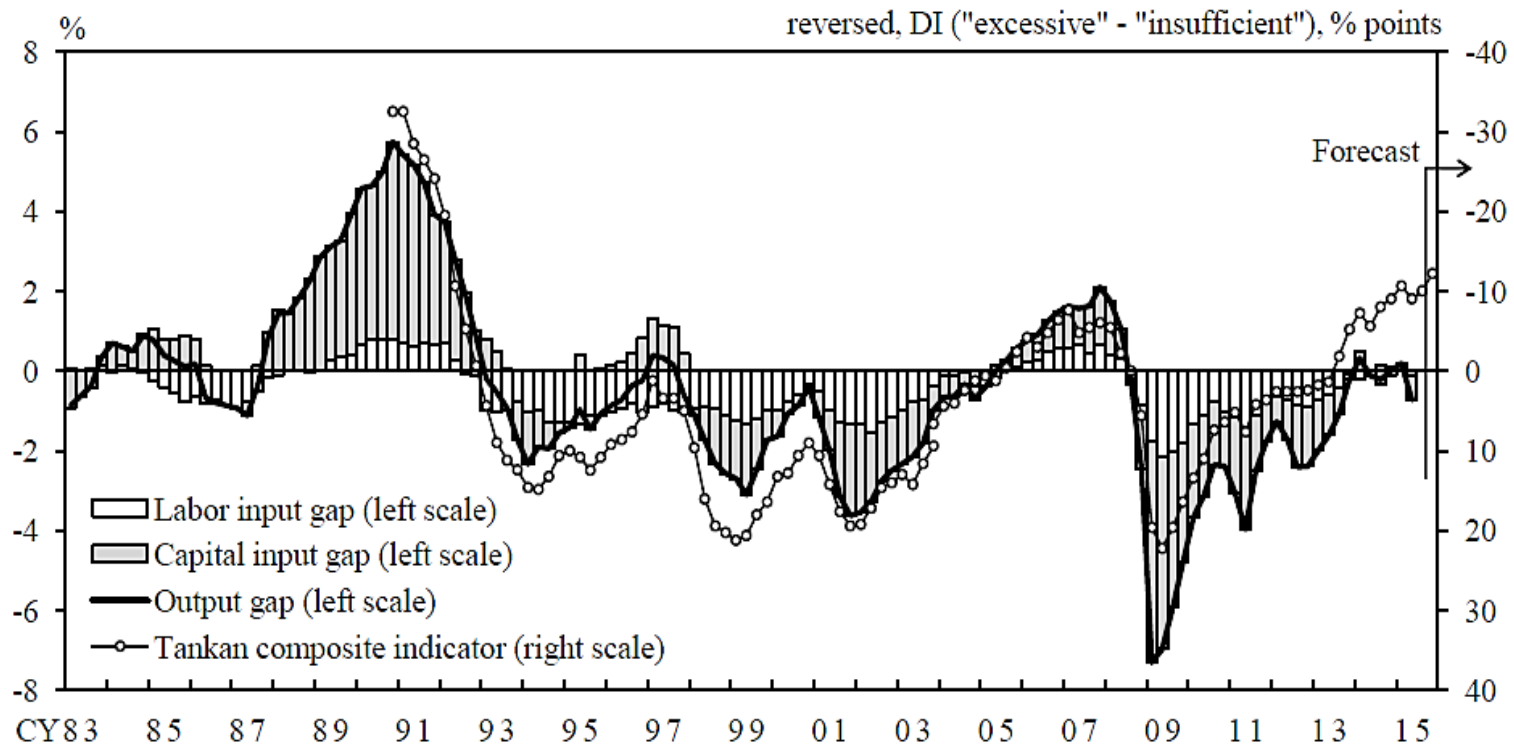
- Tighter labor market coupled with slow growth suggests lower productivity growth.
- Potential growth of the Japanese economy seems lower than 0.5%. Results of growth strategy not seen.

(potential growth rate estimated by BoJ)



- The escape from deflation may not be due to the success of Abenomics, but due to slower potential growth.
- Estimated output gap remained around zero even in the negative growth period in 2014. 2015 as well.

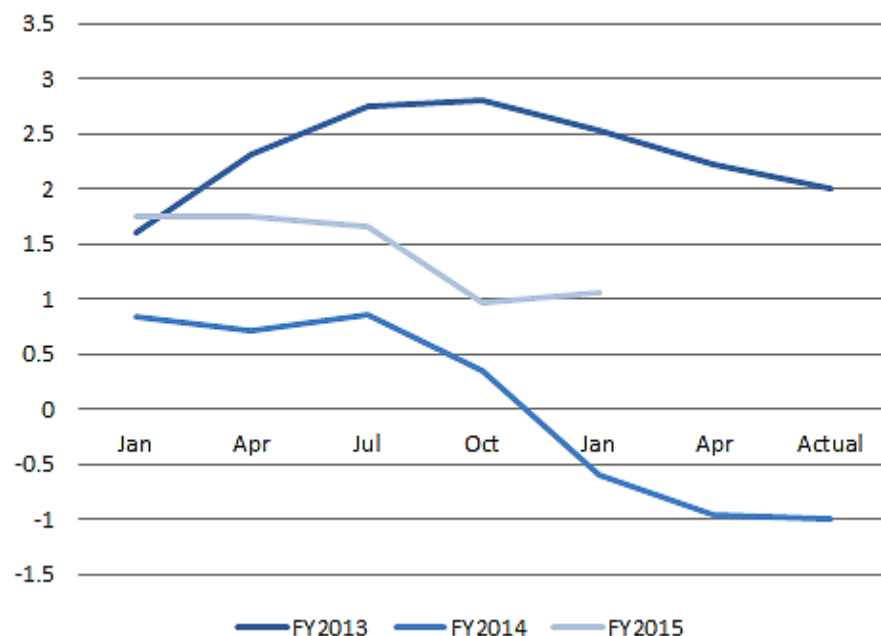
(output gap estimated by BoJ)



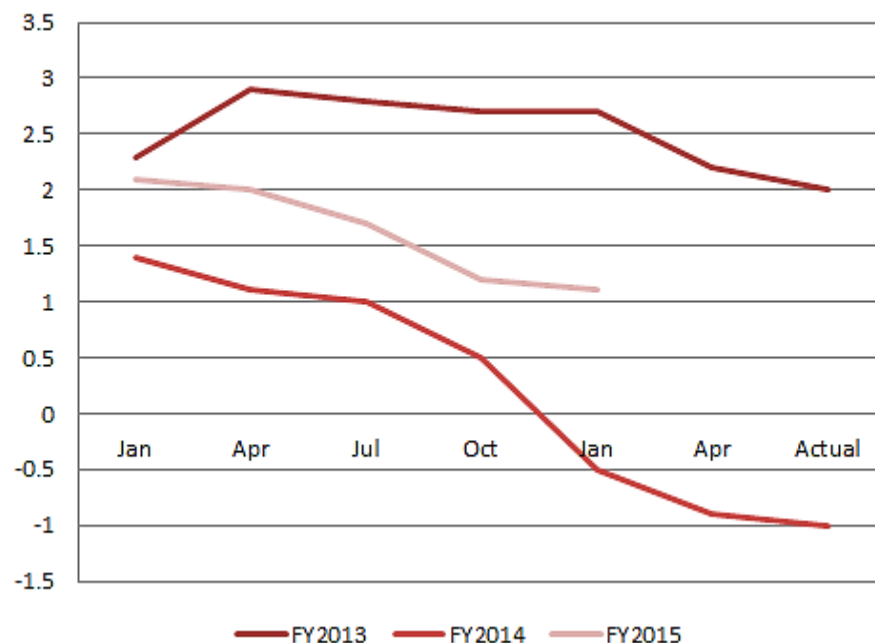
Current State of the Economy (1)

- Growth forecasts for FY2014 and FY2015 are revised down substantially.
- They are often attributed to tax hike(for FY2014), and China shock(for FY2015). But, aren't they simply reflections of very low potential growth?

Growth Forecasts by Private Institutions (%)

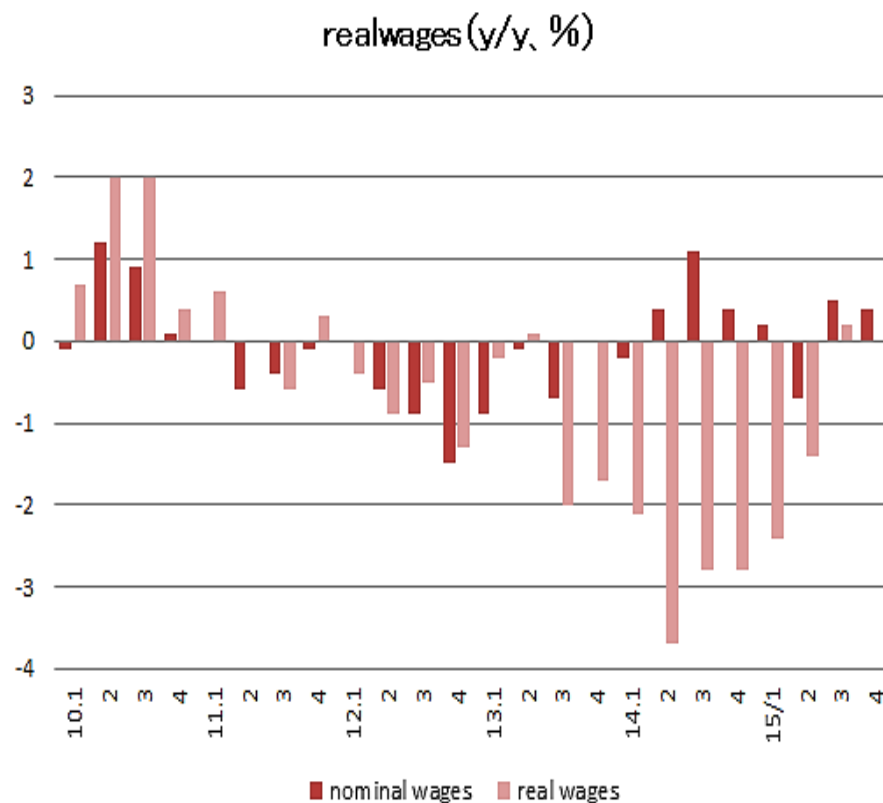
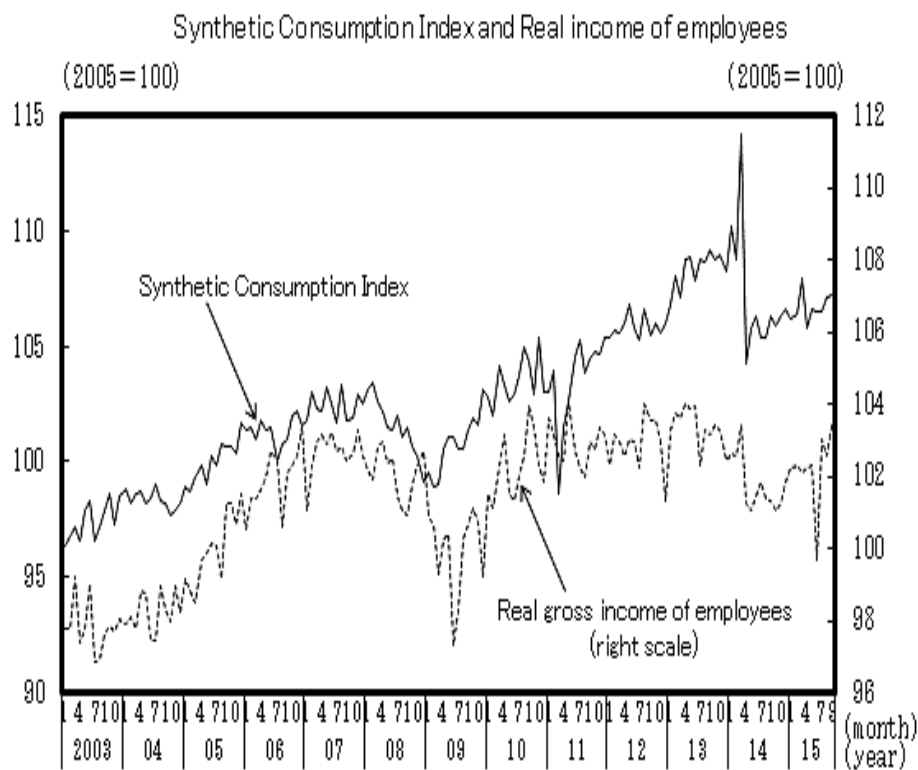


Growth Forecast by BOJ (%)



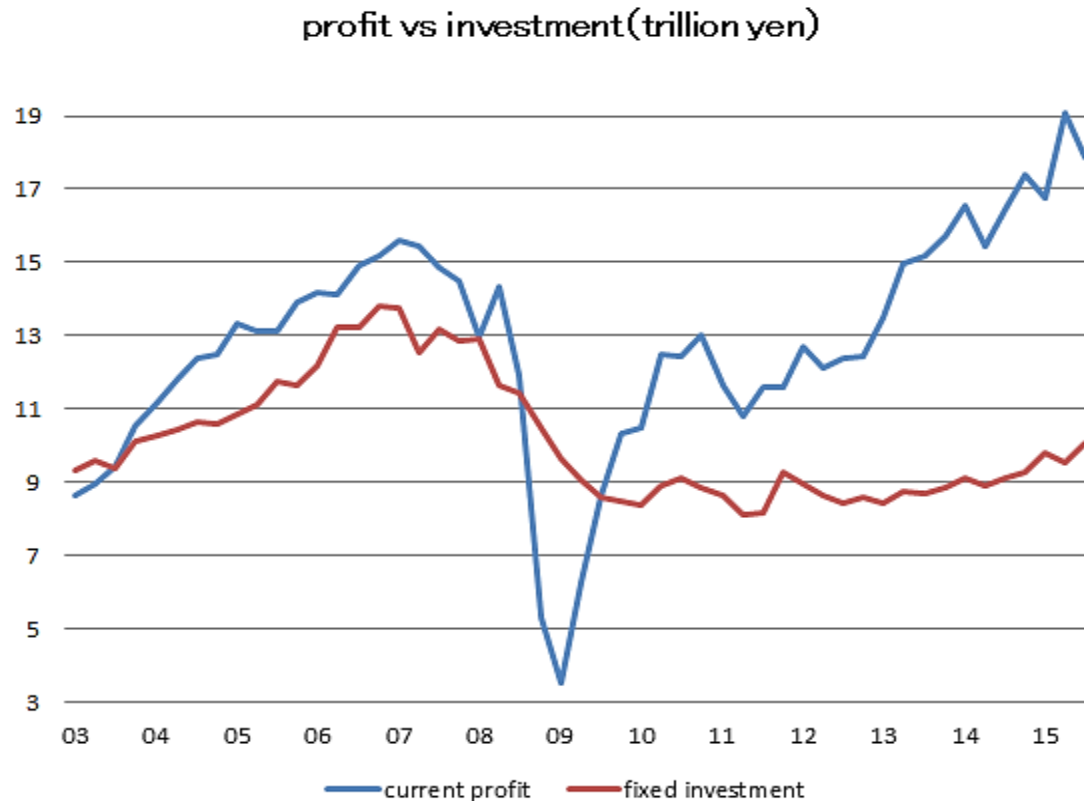
Current State of the Economy (2)

- Consumer spending remains lackluster reflecting weak real wage. While wage increase remains slow relative to corporate earnings, a weaker yen squeezes real income.
- But, real wages started to increase recently, thanks to cheaper oil.



Current State of the Economy (3)

- Corporate earnings improved substantially, owing to a weaker yen and cheaper oil. But, the increase in business investment remains surprisingly modest.
- Abe administration urges businessmen to increase investment as well as wages.



Forecasts for FY2016(1): Growth

- The Japanese economy will likely continue moderate economic growth during FY2016. Temporary surge in private consumption before Apr. 2017 consumption tax hike.
- But, 1.5% growth may be a little too optimistic.
 1. World economic growth will remain lackluster.
 2. Corporate earnings will remain good, but will not increase much.
 3. As wage base-up in 2017 may be lower than in 2016, real wage increase will be very modest.

(real GDP growth forecasts, y/y%)

	FY2015	FY2016	FY2017
Government	1.2	1.7	N.A.
Bank of Japan	1.1	1.5	0.3
Private Institutions	1.1	1.4	0.1

Forecasts for FY2016(2): Inflation

- Core CPI inflation rate, currently around zero, will likely pick up, as negative contribution of energy prices will decrease.
- CPI ex food and energy rose 0.8% y/y in last December.
- But, given very modest increase in wages, average core CPI inflation rate in FY2016 will unlikely exceed 1%, much lower than BoJ's 2% inflation target.
- Many forecasters assume crude oil price be 40–50 dollars/barrel. If current oil price around 30 dollars continues, CPI inflation rate may well go down further.

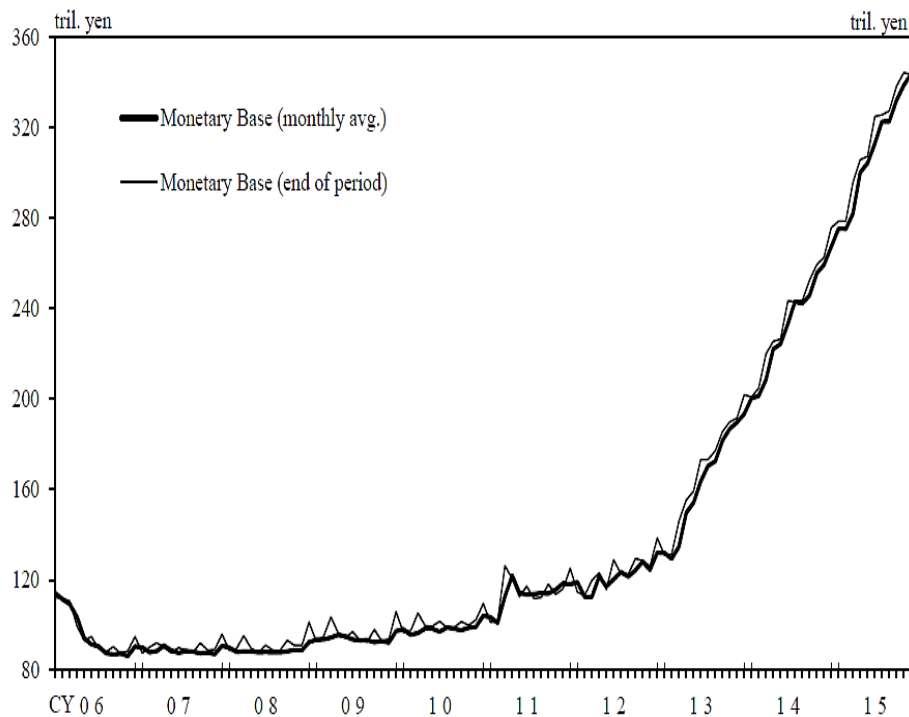
(core CPI inflation forecasts, y/y%)

	FY2015	FY2016	FY2017
Government	0.4	1.2	N.A.
Bank of Japan	0.1	0.8	1.8
Private Institutions	0.1	0.8	1.1

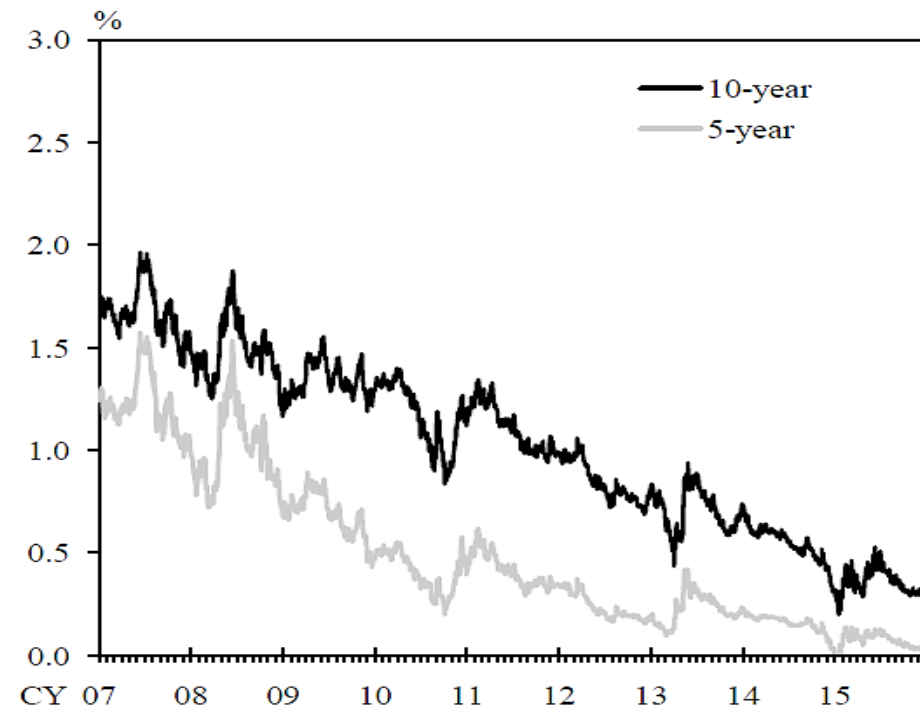
Risks (1)

- Bank of Japan is increasing monetary base by means of massive purchase of JGB, 10 trillion yen per month.
- Long-term interest rates remain extremely low because of BoJ purchase. But, what happens if BoJ stop buying JGB after achieving 2% inflation target?

(monetary base)



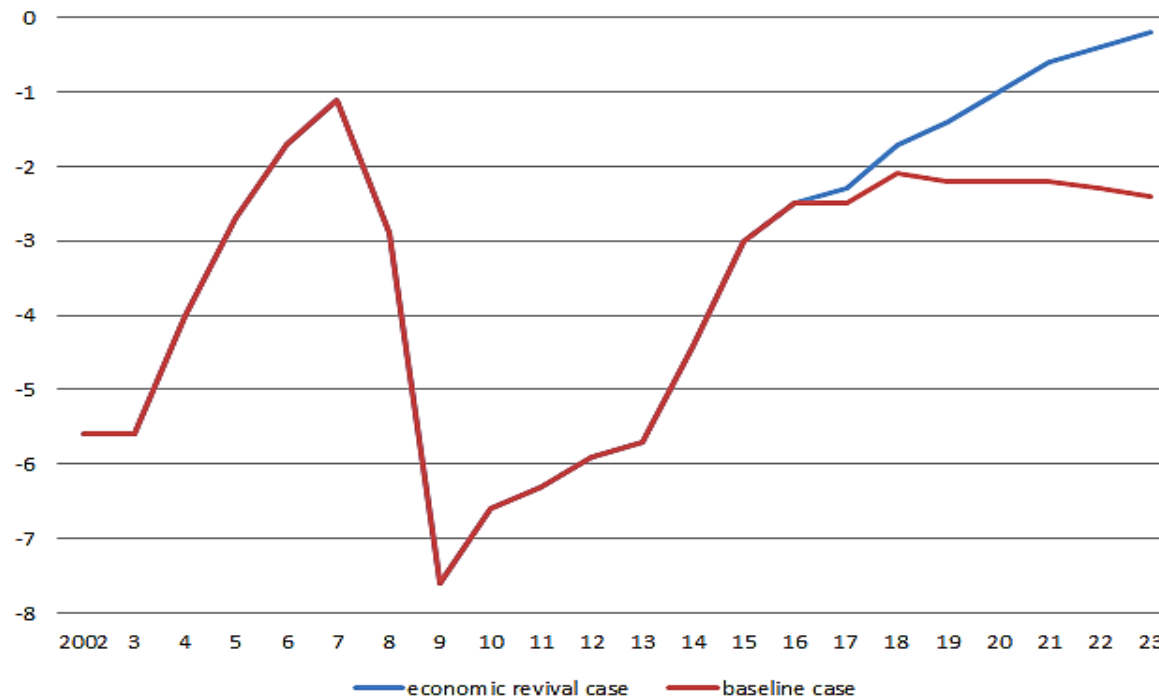
(JGB yields)

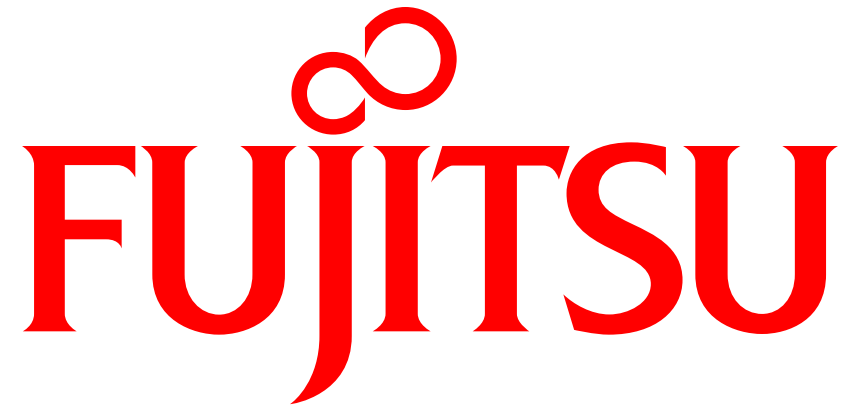


Risks (2)

- Japan's public debt/nominal GDP ratio exceeds 200%, higher than that of Greece!
- Abe administration commits to achieve positive primary budget balance in 2020. But, the assumption of the plan is incredibly optimistic (3% nominal and 2% real growth).

【projection of primary budget balance, % of nominal GDP】





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