

FY2012 and FY2013 Economic Outlook

REVISED
To reflect the
2nd QE for the
Jan-Mar Qtr
of 2012

June 2012

Key points of Mizuho Research Institute's (MHRI) outlook on the economy in FY2012 and FY2013 reflecting *The Second Preliminary Quarterly Estimates of GDP (2nd QE)* of Japan for the Jan-Mar quarter of 2012

<The US Economy >

◆ Weak growth due to household balance sheet adjustment and fiscal austerity

2012: +2.0% (previous forecast +2.0%)
2013: +1.3% (previous forecast +1.3%)

<The Eurozone Economy >

◆ Fiscal austerity will drag down growth. Uncertainties regarding the sovereign debt crisis will linger

2012: -0.2% (previous forecast -0.1%)
2013: +0.7% (previous forecast +0.7%)

<The Asian Economy >

◆ Slowdown mainly among export-driven countries.

2012: +6.5% (previous forecast +6.6%)
2013: +6.3% (previous forecast +6.5%)

<The Japanese Economy >

◆ FY2012: +2.1% (previous forecast +2.0%)

Domestic demand-led growth, driven mainly by the twin pillars of reconstruction-related demand and eco-car subsidies

◆ FY2013: +1.3% (previous forecast +1.3%)

Slow-down due to peak-out of reconstruction demand
Surge of demand prior to tax hike will push up growth in the second half of the fiscal year

This English-language translation is based upon the outlook in Japanese released on June 8, 2012. This publication is compiled solely for the purpose of providing readers with information and is in no way meant to encourage readers to buy or sell financial instruments. Although this publication is compiled on the basis of sources which MHRI believes to be reliable and correct, MHRI does not warrant its accuracy and certainty. Readers are requested to exercise their own judgment in the use of this publication. Please also note that the contents of this publication may be subject to change without prior notice.

I. The current state of the Japanese economy

Growth was revised up sharply in the 2nd QE for the Jan-Mar quarter of 2012

The *Second Preliminary Quarterly Estimates of GDP* (“2nd QE”) for the Jan-Mar quarter of 2012 released by the Cabinet Office on June 8, 2012 revealed an upward revision of Japan’s real GDP growth in the Jan-Mar quarter to +1.2 % q-o-q (+4.7% p.a.) from +1.0% q-o-q (+4.1% p.a.) in the *First Preliminary Quarterly Estimates of GDP* (“1st QE”) (Chart 1). The overall picture remains unchanged that growth was driven mainly by personal consumption and public demand.

Looking closer at each of the components of demand, capital investment was revised upward from -3.9% q-o-q to -2.1% q-o-q, reflecting data releases such as the *Financial Statements Statistics of Corporations by Industry*. In contrast, the contribution by private-sector inventory investment to quarterly real GDP growth was revised down from +0.4% pt to +0.3% pt. Turning to other components of domestic private demand, both personal consumption (+1.1% q-o-q → +1.2% q-o-q) and housing investment (-1.6% q-o-q → -1.5% q-o-q) were subject to slight upward revisions. As a result, the contribution by domestic private demand to quarterly real GDP growth was revised up to +0.7% pt from +0.5% pt.

As for public demand, government consumption remained unchanged from the 1st QE at +0.7% q-o-q, while public investment was subject to a downward revision (+5.4% q-o-q → +3.8% q-o-q). The contribution by public demand to quarterly real GDP growth dipped slightly to +0.3% pt from +0.4% pt. The contribution by domestic demand – combining both private and public demand – was revised to +1.0% pt (+0.9% pt in the 1st QE).

[Chart 1: The 2nd QE of the Jan-Mar quarter of 2012]

	(Q-o-q % change)					2012 Jan-Mar	1st QE Jan-Mar
	2011 Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec	2012 Jan-Mar		
Domestic gross expenditure	-2.0	-0.4	1.9	0.0	1.2	1.0	
(Q-o-q change, p.a.)	-7.7	-1.7	7.8	0.1	4.7	4.1	
Domestic demand	-1.8	0.6	1.1	0.7	1.0	0.9	
	(-1.8)	(0.6)	(1.1)	(0.7)	(1.0)	(0.9)	
Private demand	-2.2	0.1	1.5	0.9	0.9	0.6	
	(-1.6)	(0.1)	(1.1)	(0.7)	(0.7)	(0.5)	
Consumption	-1.5	0.6	1.1	0.7	1.2	1.1	
Housing investment	1.6	-3.1	4.8	0.1	-1.5	-1.6	
Capital investment	-0.3	-0.3	0.1	5.2	-2.1	-3.9	
Inventory investment	(-0.7)	(-0.1)	(0.3)	(-0.4)	(0.3)	(0.4)	
Public demand	-0.5	1.9	0.0	0.1	1.3	1.5	
	(-0.1)	(0.5)	(0.0)	(0.0)	(0.3)	(0.4)	
Government final consumption	0.3	0.7	0.2	0.4	0.7	0.7	
Public investment	-4.1	7.3	-1.0	-0.8	3.8	5.4	
Net exports of goods & services	(-0.2)	(-1.0)	(0.8)	(-0.7)	(0.1)	(0.1)	
Exports	-0.4	-6.3	8.7	-3.7	3.0	2.9	
Imports	1.2	0.2	3.5	0.9	1.9	1.9	

Note: The figures in parentheses indicate the contributions to gross domestic expenditures.

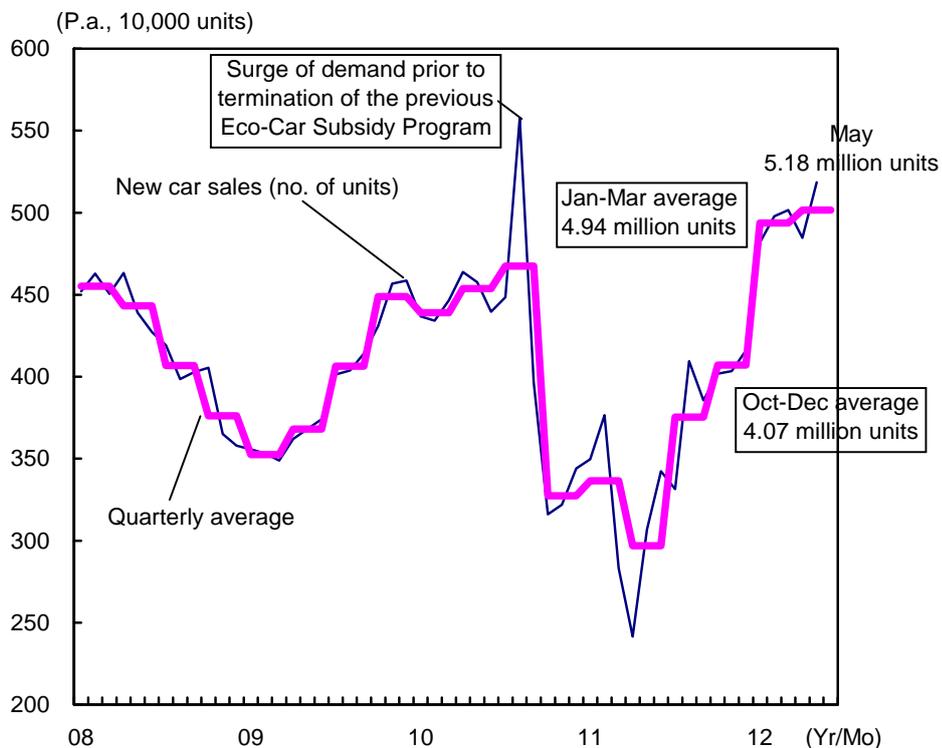
Source: Cabinet Office, *Preliminary Quarterly Estimates of GDP*.

Growth forecast to slow down to +1% p.a. level in Apr-Jun qtr

Turning to external demand, exports (+2.9% q-o-q → +3.0% q-o-q) were revised upward, while imports (+1.9% q-o-q) remained unchanged. As a result, the contribution by external demand to quarterly real GDP growth (+0.1% pt) remained unchanged.

In the Apr-Jun quarter of 2012, Japan's real GDP growth should remain in positive territory, given the ongoing expansion of public demand due to reconstruction works related to the Great East Japan Earthquake. However, despite the strong growth of car sales backed by the government's eco-car subsidy program, a slowdown from the Jan-Mar quarter is inevitable. Together with the recent softening of exports (**Chart 2**), we expect the pace of real GDP growth to slow down to the +1% level on an annualized basis in the Apr-Jun quarter of 2012.

[Chart 2: New car sales]



Note: Seasonal-adjustments by MHRI.

Source: Made by MHRI based upon releases by Japan Automobile Dealers Association.

II. Forecast on the Japanese economy in FY2012 and FY2013

The economy will remain on recovery track due to reconstruction demand.

FY2012 real GDP growth: +2.1%

In FY2012, the Japanese economy should continue to follow a recovery driven mainly by domestic demand backed by the twin pillars of reconstruction-related demand and the eco-car subsidy program. In contrast, external demand may not be expected to serve as the driver of growth, judging from the softening of exports stemming from the weak recovery of the overseas economies.

Orders for reconstruction-related public works are expected to rise sharply over the summer months, providing reasons to believe that public investment (on a works-in-progress basis) will continue to grow throughout FY2012. Personal consumption should also remain on firm footing backed by the gradual recovery of labor market conditions. Furthermore, considering that capital investment is also expected to remain on a gradual uptrend reflecting the improvement of corporate earnings, domestic private demand should remain on firm footing for the time being.

However, it looks likely that the eco-car subsidy program will expire in July as the budget outlay for the subsidies are depleted. Given the inevitable fall of car sales immediately after the expiration, personal consumption may weaken temporarily from the summer to early autumn. In 2013, a further US economic slowdown due to factors such as fiscal tightening is forecast to serve as a negative impact upon Japan's exports and production. Even though reconstruction-related demand should serve as underlying support, the Japanese economy should gradually slow down in the second half of the fiscal year.

On a fiscal year basis, the rate of real GDP growth should rise to 2.1% in FY2012 (MHRI outlook in May: +2.0%) as a result of the rise of public demand accompanying reconstruction from the Great East Japan Earthquake and the gradual expansion of domestic private-sector demand.

Reconstruction-related demand will peak out.

FY2013 growth will slow down to +1.3%

In FY2013, reconstruction-related demand is forecast to peak out, leading to the decline of public investment. The Japanese economy is expected to enter a "soft patch" in the first half of FY2013. Note that the Japanese economy risks falling into a recession during this period, depending upon overseas economic trends.

In the second half of FY2013, the last-minute rush of demand prior to the consumption tax hike should serve to push up domestic demand. The consumption tax hike bill currently debated in Diet proposes to raise the consumption tax from 5% to 8% in April 2014. In the run-up to the tax hike, the last-minute demand in forms such as personal consumption and housing investment should push up the rate of economic growth in the second half of FY2013.

On a fiscal year basis, the pace of real GDP growth is forecast to slow down

The greatest risk is the escalation of the eurozone debt crisis and appreciation of the yen

from FY2012 to +1.3% in FY2013 (MHRI outlook in May: +1.3%).

As explained above, the Japanese economy is forecast to remain on a gradual recovery track throughout FY2012 and FY2013 despite a temporary slowdown in the first half of FY2013. The greatest risk to this outlook is an overseas economic downturn and appreciation of the yen.

The financial markets are turning risk averse, given the rise of concerns regarding the political turmoil in Greece and the deterioration of financial conditions of Spanish banking institutions. MHRI's economic outlook is based upon the assumption that a Greek exit from the eurozone will be averted through a compromise between the Greek government and the EU subsequent to the re-election on June 17th – for example in the form of an easing of the target for reduction of the fiscal deficit. However, in the event negotiations between Greece and the EU head into difficulties, thus leading to the prolongation of the turmoil, there are the risks of a global stock market fall and strengthening of the yen. Moreover, the possibility of an abrupt departure of Greece from the eurozone may not be ruled out altogether. An overseas economic slowdown and yen appreciation due to the escalation of the eurozone debt crisis will serve as a negative factor upon the Japanese economy through the fall of exports and deterioration of corporate earnings and consumer confidence.

The prolonged suspension of Japan's nuclear power plants will serve as a negative factor upon domestic demand

On the domestic side, the shortage of electrical power may be cited as a risk factor. This summer, the areas outside those served by the Tohoku Electrical Power Co., Inc and the Tokyo Electric Power Company (TEPCO) are required to cut electrical power usage by 5~15%. In particular, in the event the Ohi Nuclear Power Plant (Reactors No. 3 and 4) remain shut down, the areas served by the Kansai Electric Power Co. (KEPCO) would have to reduce electrical power usage by more than 15%, serving as constraints upon production activity and consumption over the summer months. Furthermore, in the event all of Japan's nuclear power plants remain suspended, fuel costs for thermal electrical power generation would increase by approximately JPY3 trillion from the level before the earthquake disaster, leading to the deterioration of Japan's trade balance. If the move to raise electrical power charges currently limited to TEPCO spreads to other electrical power companies as well, there are concerns that it will gradually have a negative impact upon personal consumption and capital investment.

[Chart 3: Outlook on the Japanese economy]

		FY2010	FY2011	FY2012	FY2013	2012				2013				2014
						Jan-Mar	Apr-Jun	Jul-Aug	Oct-Dec	Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec	Jan-Mar
GDP (real)	Q-o-q % ch	3.2	-0.0	2.1	1.3	1.2	0.4	0.3	0.3	0.1	0.2	0.4	0.7	0.9
	Q-o-q % ch p.a.	--	--	--	--	4.7	1.6	1.1	1.1	0.5	0.8	1.6	2.7	3.5
Domestic demand	Q-o-q % ch	2.4	1.0	2.1	1.2	1.0	0.4	0.3	0.1	0.2	0.1	0.3	0.7	0.9
Private sector demand	Q-o-q % ch	3.0	0.6	2.0	1.3	0.9	0.3	0.2	0.0	0.2	0.1	0.4	0.8	1.1
Personal consumption	Q-o-q % ch	1.5	1.1	1.5	1.1	1.2	0.1	0.0	-0.4	0.1	0.1	0.2	0.9	2.0
Housing investment	Q-o-q % ch	2.4	3.6	2.3	7.8	-1.5	0.4	1.4	1.9	-0.6	2.4	4.6	6.0	-8.0
Capital investment	Q-o-q % ch	3.5	0.9	3.3	2.0	-2.1	1.2	0.8	0.8	0.4	0.4	0.5	0.4	0.5
Inventory investment	Q-o-q contribution, % pt	0.8	-0.4	0.2	-0.2	0.3	0.0	-0.0	0.0	0.1	-0.1	-0.0	-0.1	-0.2
Public sector demand	Q-o-q % ch	0.5	2.1	2.3	0.8	1.3	0.6	0.5	0.4	0.2	0.1	0.2	0.2	0.0
Government consumption	Q-o-q % ch	2.3	1.8	1.4	1.2	0.7	0.2	0.3	0.3	0.1	0.2	0.5	0.5	0.2
Public investment	Q-o-q % ch	-6.7	3.1	6.6	-1.2	3.8	2.5	1.5	0.8	0.7	-0.2	-1.4	-1.3	-0.6
External demand	Q-o-q contribution, % pt	0.8	-1.0	-0.1	0.1	0.1	-0.0	-0.0	0.2	-0.0	0.0	0.0	-0.0	-0.0
Exports	Q-o-q % ch	17.2	-1.4	5.4	2.4	3.0	2.0	0.7	0.9	-0.1	0.6	0.8	0.9	0.9
Imports	Q-o-q % ch	12.0	5.3	5.3	1.6	1.9	2.1	0.7	-0.3	0.2	0.3	0.5	0.9	1.0
GDP (nominal)	Q-o-q % ch	1.1	-2.0	1.7	1.4	1.2	0.1	0.5	0.1	0.4	-0.1	0.7	0.4	1.0
GDP deflator	Y-o-y % ch	-2.0	-2.0	-0.4	0.0	-1.3	-1.0	-0.5	-0.3	0.1	0.0	0.2	0.1	0.0
Domestic demand deflator	Y-o-y % ch	-1.2	-0.7	-0.4	-0.5	-0.4	-0.5	-0.6	-0.4	-0.3	-0.6	-0.5	-0.5	-0.5

Source: Made by MHRI based upon Cabinet Office, *Preliminary Quarterly Estimates of GDP*.

		FY2010	FY2011	FY2012	FY2013	2012				2013				2014
						Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec	Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec	Jan-Mar
Industrial production	Q-o-q % ch	9.3	-1.0	3.8	1.8	1.3	0.3	0.9	0.7	-0.1	0.0	0.8	0.8	0.7
Ordinary profits	Y-o-y % ch	39.0	-2.0	10.5	4.9	14.1	21.0	14.7	7.4	1.9	2.1	3.8	6.1	7.5
Nominal labor compensation	Y-o-y % ch	0.5	0.1	0.4	0.6	-0.0	0.2	0.4	0.6	0.4	0.6	0.6	0.6	0.6
Unemployment rate	%	5.0	4.5	4.4	4.2	4.5	4.5	4.4	4.3	4.3	4.3	4.2	4.1	4.1
New housing starts	P.a., 10,000 units	81.9	84.1	88.3	95.5	86.2	87.2	87.9	90.1	87.5	91.7	97.0	100.3	92.0
Current account balance	P.a., JPY tril	16.7	7.9	9.7	13.7	7.1	7.3	9.4	10.6	11.1	11.3	14.2	14.5	14.9
Domestic corporate goods prices	Y-o-y % ch	0.7	1.7	-1.1	-0.4	0.5	-0.7	-1.3	-1.0	-1.2	-1.0	-0.4	-0.3	-0.0
Consumer prices	Y-o-y % ch	-0.8	0.0	-0.2	-0.2	0.1	-0.0	-0.3	-0.1	-0.2	-0.4	-0.2	-0.1	-0.0
Uncollateralized overnight call rate	%	0.06	0.08	0~0.10	0~0.10	0.08	0~0.10	0~0.10	0~0.10	0~0.10	0~0.10	0~0.10	0~0.10	0~0.10
Yield on newly-issued 10-yr JGBs	%	1.13	1.05	0.95	0.99	0.97	0.90	0.95	1.00	0.95	0.95	0.95	1.00	1.05
Nikkei average	JPY	9,961	9,181	9,500	9,500	9,274	9,100	9,400	9,700	9,400	9,200	9,300	9,600	9,800
Exchange rate	JPY/USD	86.0	79.0	79.0	80.0	79.3	80.0	78.0	80.0	79.0	79.0	79.0	81.0	82.0
Crude oil price (WTI nearest term contract)	USD/bbl	84.0	97.0	90.0	82.0	103.0	94.0	86.0	92.0	88.0	85.0	81.0	81.0	82.0

Notes: 1. The readings above may differ from public releases because the rates of change are calculated based upon actual results.

2. Ordinary profits are based upon the *Financial Statements Statistics of Corporations by Industry* (ex finance & insurance, and production, transmission and distribution of electricity services).

3. Consumer prices exclude fresh food (2010 base).

4. Quarterly data on the unemployment rate, new housing starts and current account balance are seasonally-adjusted.

5. Of the finance-relate indices, the uncollateralized overnight call rate refers to the rate at the end of term and all others are averages during the relevant terms.

Sources: Made by MHRI based upon Cabinet Office, *Preliminary Quarterly Estimates of GDP*, Ministry of Economy, Trade and Industry, *Indices of Industrial Production*, Ministry of Finance, *Financial Statements, Statistics of Corporations by Industry, Quarterly*, Ministry of Internal Affairs and Communications, *Labor Force Survey, Consumer Price Index*, Ministry of Land, Infrastructure, Transport and Tourism, *Current Survey on Construction Statistics*, Bank of Japan, *Balance of Payments, Corporate Goods Price Index, Financial and Economic Statistics Monthly, Foreign Exchange Rates*, Japan Bond Trading Co., Ltd., *Latest Daily JGB Rates*, Nikkei Inc. and Bloomberg.

[Chart 4: Outlook on the US economy]

	2012				2013				2011	2012	2013
	Jan-Mar (Actual)	Apr-Jun	Jul-Sep	Oct-Dec	Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec	(Actual)	(Actual)	(Actual)
GDP (q-o-q % ch, p.a.)	1.9	1.7	1.8	1.5	1.0	1.1	1.0	1.0	1.7	2.0	1.3
Personal consumption (q-o-q % ch, p.a.)	2.7	2.4	2.1	2.0	1.0	1.9	1.9	1.8	2.2	2.2	1.7
Housing investment (q-o-q % ch, p.a.)	19.4	5.0	5.0	5.0	5.0	5.0	5.0	5.0	-1.3	9.1	5.0
Capital investment (q-o-q % ch, p.a.)	1.9	5.0	7.3	7.0	6.0	5.5	5.0	5.0	8.8	6.2	6.0
Inventory investment (USD billion p.a.)	0.2	-0.1	0.0	-0.1	0.4	0.0	0.0	0.0	-0.2	0.1	0.1
Government spending (q-o-q % ch, p.a.)	-3.9	-3.0	-3.0	-3.0	-5.4	-5.4	-5.4	-5.4	-2.1	-3.0	-4.5
Net exports (USD billion p.a.)	-411.9	-409.3	-407.3	-407.6	-403.9	-403.1	-402.3	-401.4	-413.6	-409.0	-402.7
Exports (q-o-q % ch, p.a.)	7.2	5.5	3.5	3.0	2.0	2.0	2.0	2.0	6.7	4.8	2.6
Imports (q-o-q % ch, p.a.)	6.1	4.0	2.5	2.5	1.0	1.5	1.5	1.5	4.9	3.7	1.8
Domestic final demand (q-o-q % ch, p.a.)	1.7	1.7	1.7	1.6	0.5	1.0	1.0	1.0	1.8	1.7	1.1
Unemployment rate (%)	8.3	8.2	8.2	8.1	8.1	8.2	8.2	8.2	9.0	8.2	8.2
PCE deflator (y-o-y % ch)	2.3	1.7	1.6	1.7	1.6	1.7	1.7	1.8	2.5	1.8	1.7
Core PCE deflator ex food and energy (y-o-y % ch)	1.9	1.8	1.8	2.0	1.9	2.1	2.1	2.1	1.4	1.9	2.0

Sources: US Department of Commerce, US Department of Labor, MHRI.

[Chart 5: Outlook on the Eurozone economy]

	2011	2012	2013	2011		2012		2013	
	(Actual)	(Forecast)	(Forecast)	1H	2H	1H	2H	1H	2H
				(Forecast)	(Forecast)	(Forecast)	(Forecast)	(Forecast)	(Forecast)
Real GDP	1.5	-0.2	0.7	1.9	0.1	-0.5	0.1	0.7	1.2
Y-o-y % ch of 4th qtr of each year (% ch o-y-a for half year terms)	0.7	0.0	0.6	2.0	1.0	-0.2	-0.2	0.4	0.9
Private-sector consumption	0.2	-0.3	0.7	-0.2	-0.3	-0.6	0.3	0.8	0.8
Government consumption	-0.3	-0.9	-1.1	-0.3	-0.7	-0.4	-1.8	-1.0	-0.7
Fixed capital formation	1.6	-1.5	1.6	2.9	-1.1	-2.9	0.9	1.7	2.2
External demand (contribution)	1.0	0.9	0.2	0.9	1.4	1.2	-0.1	0.1	0.4
Exports	6.3	2.8	3.4	5.6	3.4	2.2	3.5	2.8	4.4
Imports	4.1	0.8	3.3	3.7	0.2	-0.6	4.0	2.7	3.8
Inventories, balancing items (contribution)	0.2	-0.5	0.1	0.7	-0.8	-0.7	0.3	0.1	0.0
Domestic demand	0.6	-1.2	0.5	1.1	-1.3	-1.8	0.1	0.6	0.8
Consumer prices	2.7	2.2	1.4	2.6	2.8	2.5	2.0	1.4	1.4
Core inflation rate	1.4	1.6	1.5	1.4	1.5	1.6	1.6	1.5	1.4

Notes: 1. Calendar-year data refer to the y-o-y % ch. Half-year term figures refer to the % change from the previous term (p.a.) for GDP, and the % change from the previous year for consumer prices. The shaded columns are forecasts.

2. Growth rate adjusted for operating days.

Sources: Eurostat, MHRI.

[Chart 6: Outlook on the Asian economies]

(%)

	2010	2011	2012		2013	
				Previous		Previous
Asia	9.2	7.5	6.5	6.6	6.3	6.5
China	10.4	9.2	8.3	8.5	8.2	8.4
NIEs	8.4	4.0	2.4	2.4	1.9	1.9
South Korea	6.3	3.6	2.8	2.8	2.2	2.2
Taiwan	10.7	4.0	2.3	2.3	2.2	2.2
Hong Kong	7.1	5.0	1.9	1.9	0.8	0.8
Singapore	14.8	4.9	1.5	1.5	0.5	0.5
ASEAN5	7.0	4.4	5.1	4.7	4.3	4.5
Indonesia	6.2	6.5	6.1	6.1	5.4	5.4
Thailand	7.8	0.1	4.5	3.8	3.2	3.8
Malaysia	7.2	5.1	3.8	3.5	2.9	2.9
Philippines	7.6	3.7	4.9	3.6	3.2	3.5
Vietnam	6.8	5.9	5.1	5.1	5.4	5.4
India	8.2	7.5	5.9	6.0	5.7	5.8

Notes: 1. Real GDP growth rate (y-o-y ch). The shaded columns are forecasts.
 2. Averages are calculated by the 2010 GDP share (PPP basis) by the IMF.
 3. The figures in the "previous" column are forecasts in MHRl's *FY2012 and FY2013 Economic Outlook* (May 18, 2012).
 Sources: Statistical data of relevant countries, MHRl.

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