

REVISED
to reflect the
2nd QE for the
Jan-Mar Qtr
of 2016

FY2016, FY2017 Economic Outlook

- Even though the postponement of the consumption tax hike has eased uncertainties, the slowdown of the overseas economies will serve as a drag upon the Japanese economy -

June 8, 2016

Mizuho Research Institute

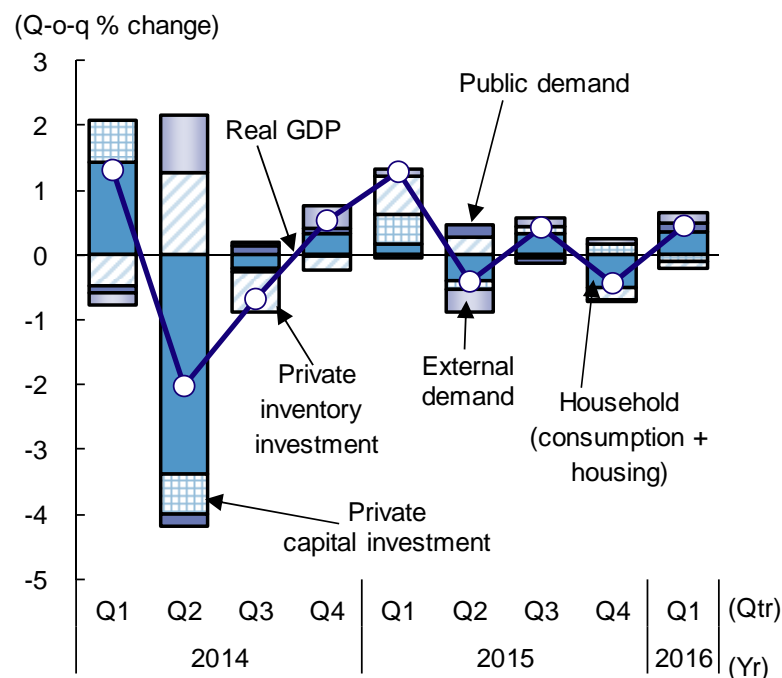
The Japanese economy: the economy is forecast to lack strength due to the slowdown of overseas economies
For the time being, Japan's economic recovery will depend upon public demand

- ❑ The *Second Preliminary Quarterly Estimates of GDP* (“2nd QE) for the Jan-Mar quarter of 2016 revealed a slight upward revision of Japan’s real GDP from the *First Preliminary Quarterly Estimates of GDP* (“1st QE). Even so, the overall state of the economy remains unchanged that the pace of growth is flat when averaged out with the decline in the Oct-Dec quarter of 2015.
- ❑ Japan’s economic growth will likely lack strength in FY2016, as the overseas economic slowdown and the strong yen are expected to weigh down upon growth. However, the economy should continue to grow at a pace of +0.6%, above the potential rate of growth (estimated to be around +0.2% to +0.3%), since the external malaise is not as serious to cause a loss of momentum of the Japanese economy and that the acceleration of public investment and economic stimulus measures (scheduled in the autumn season of 2016) should serve as underpinnings.
- ❑ In FY2017, the pace of economic growth is forecast to rise to +1.0% as the economic stimulus measure in the previous year kick in, and the overseas economies (mainly the developed economies (DM)) gradually pick up.
- ❑ In FY2016 and FY2017, the contribution ratio by public demand to real GDP growth should rise sharply (FY2015: approximately 21%, FY2016: approximately 67%, FY2017: approximately 44%). This means that public demand should supplement the slow recovery of private-sector and external demand.
- ❑ Given the fall of crude oil prices, the year-on-year (y-o-y) change of the core CPI should trend close to 0% until around the end of 2016. From then onward, the y-o-y change of energy prices should rise to positive territory, lifting the core inflation rate to nearly 1% (excluding the impact of the consumption tax hike) toward the latter half of the forecast horizon. The underlying trend in inflation excluding the impact of energy prices should gradually improve.

1. The 2nd QE for the Jan-Mar quarter of 2016: despite an upward revision, the Japanese economy is still in a soft patch

- The 2nd QE for the Jan-Mar quarter of 2016 revealed a slight upward revision of Japan's real GDP to +0.5% q-o-q (+1.9% p.a.) from the 1st QE (-1.7% p.a.).
 - In contrast to the downward revision of public investment, capital investment and inventory investment were revised upward.
 - ✓ As in the 1st QE, confirmation of the firmness of capital investment in the 2nd QE was a positive factor. Even so, since overall GDP growth was more or less flat when averaged out with the decline (-1.8% p.a.) in the Oct-Dec quarter, our view remains unchanged that the Japanese economy remained in a soft patch.

[GDP in the Jan-Mar quarter of 2016 (2nd QE)]



Source: Made by Mizuho Research Institute (MHRI) based upon Cabinet Office, *National Accounts of Japan*.

	2015				(Q-o-q % change)	
	Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec	2016 Jan-Mar	1st QE Jan-Mar
Gross domestic production	1.3	-0.4	0.4	-0.4	0.5	0.4
(Q-o-q change, p.a.)	5.2	-1.7	1.7	-1.8	1.9	1.7
(Y-o-y change)	-1.0	0.7	1.8	0.7	0.1	-0.0
Domestic demand	1.2	-0.1	0.3	-0.5	0.3	0.2
(Contributions)	(1.2)	(-0.1)	(0.3)	(-0.5)	(0.3)	(0.2)
Private demand	1.6	-0.4	0.5	-0.6	0.2	0.1
(Contributions)	(1.2)	(-0.3)	(0.4)	(-0.5)	(0.2)	(0.1)
Personal consumption	0.2	-0.8	0.5	-0.8	0.6	0.5
Housing investment	2.1	2.2	1.7	-1.0	-0.7	-0.8
Capital investment	3.2	-1.2	0.8	1.3	-0.7	-1.4
Inventory investment	(0.6)	(0.3)	(-0.1)	(-0.2)	(-0.1)	(-0.0)
Public demand	-0.2	0.8	-0.3	-0.1	0.5	0.6
(Contributions)	(-0.0)	(0.2)	(-0.1)	(-0.0)	(0.1)	(0.2)
Government consumption	0.3	0.4	0.2	0.7	0.7	0.7
Public investment	-2.3	2.8	-2.4	-3.6	-0.7	0.3
Net exports of goods & services	(0.1)	(-0.4)	(0.1)	(0.1)	(0.2)	(0.2)
Exports	2.2	-4.8	2.6	-0.8	0.6	0.6
Imports	1.5	-2.5	1.7	-1.1	-0.4	-0.5
Nominal GDP	2.0	-0.2	0.8	-0.2	0.6	0.5
GDP deflator (y-o-y change)	3.2	1.4	1.8	1.5	0.9	0.9

Note: The figures in parentheses indicate the contributions to gross domestic production.
Source: Made by MHRI based upon Cabinet Office, *National Accounts of Japan*.

2. Outlook on the Japanese economy: revisions to FY2016 and FY2017 growth, reflecting the postponement of the consumption tax hike

- Considering that Japan has opted to postpone its consumption tax hike again, we have revised down our forecast on FY2016 growth to +0.6% (which would have been 0.9% if the tax hike were implemented as scheduled). On the other hand, we have revised upward our forecast on growth in FY2017 to +1.0% (which would have been 0.2% if the tax hike were implemented as scheduled).
 - In FY2016, the pace of growth will fall by approximately 0.3% pt due to the absence of a rush of demand.
 - In FY2017, the downward pressures (around 0.7% pt to 0.8% pt) will ease since there would be no backlash to the rush of demand and that there would be no additional household burdens.

[Outlook on the Japanese economy]

CY		Actual		Including impact of the tax hike postponement		Excluding impact of the tax hike postponement	
		2014	2015	2016	2017	2016	2017
Real GDP	Q-o-q % ch	-0.9	0.8	0.6	1.0	0.9	0.2
Domestic demand	Q-o-q % ch	-1.5	0.7	0.6	0.9	1.0	0.1
Private sector demand	Q-o-q % ch	-1.9	0.7	0.2	0.7	0.8	-0.3
Personal consumption	Q-o-q % ch	-2.9	-0.2	0.7	1.0	1.3	-0.6
Housing investment	Q-o-q % ch	-11.7	2.4	0.7	-1.5	3.2	-6.6
Capital investment	Q-o-q % ch	0.1	2.0	1.2	1.8	1.5	0.6
Inventory investment	Q-o-q contribution, % pt	0.6	0.3	-0.4	-0.3	-0.4	0.2
Public sector demand	Q-o-q % ch	-0.3	0.6	1.8	1.6	1.7	1.1
Government consumption	Q-o-q % ch	0.1	1.5	1.6	1.7	1.6	1.4
Public investment	Q-o-q % ch	-2.6	-2.7	2.6	1.6	2.1	0.2
External demand	Q-o-q contribution, % pt	0.6	0.1	0.0	0.0	-0.1	0.1
Exports	Q-o-q % ch	7.9	0.4	1.1	2.8	1.0	2.7
Imports	Q-o-q % ch	3.4	-0.1	0.9	2.5	1.6	2.1

Notes: Figures in the shaded areas are forecasts.

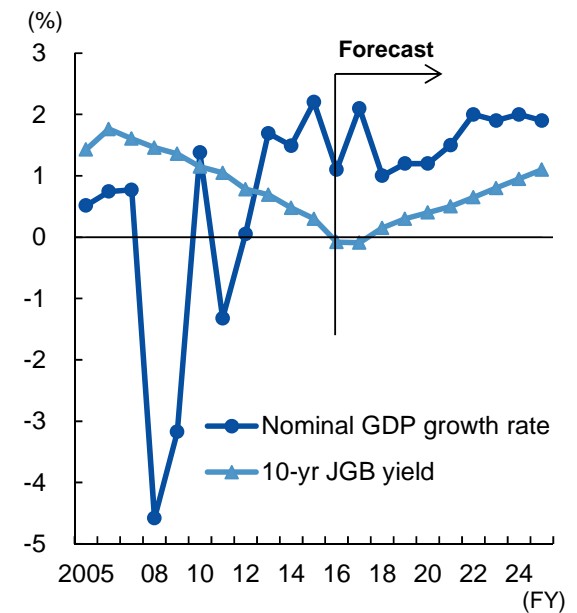
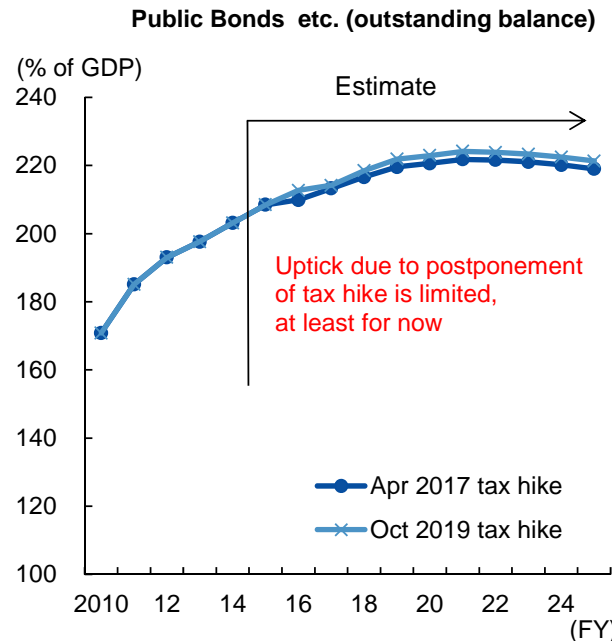
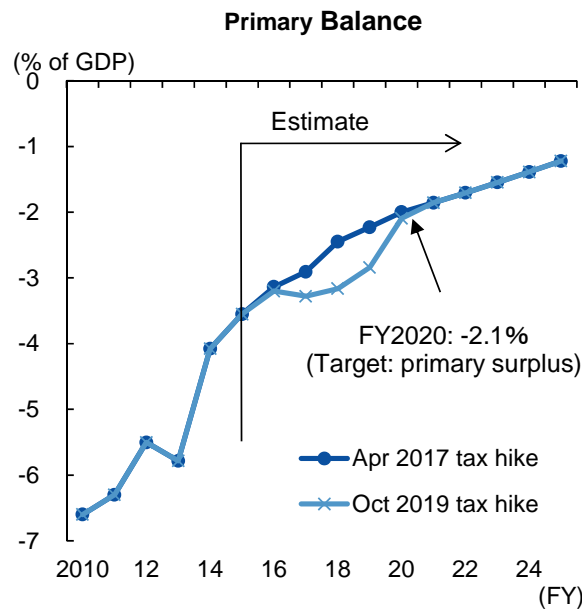
Source: Made by MHRI based upon Cabinet Office, *Preliminary Quarterly Estimates of GDP*.

The Japanese economy: even though the postponement of the tax hike will be a setback for fiscal rehabilitation, it will not lead directly to the rise of concerns regarding fiscal collapse

- ❑ The primary balance will fall by approximately JPY4 trillion (slightly less than 1% of GDP) due to the postponement of the scheduled consumption tax hike.
- ❑ According to MHRI's outlook on the economy over the mid-term, it is possible to curb the rise of the outstanding balance of public bonds etc. The current conditions do not necessarily raise alarms over fiscal conditions.
 - ✓ Even so, note that this is based upon the premise that nominal interest rates will remain below the rate of GDP growth in nominal terms due to the continuation of monetary easing. The collapse of this premise may lead to the rise of interest rates and the deterioration of public bonds outstanding.

[The impact of the tax hike postponement upon fiscal conditions]

[(Reference) Nominal GDP and nominal interest rate (10-yr JGB yield)]



Notes: The outstanding balance of public bonds etc. refers to the "securities other than equities (debt)" in the central government's general account.
Source: Made by MHRI based upon Cabinet Office, *National Accounts of Japan*, Ministry of Finance materials.

Japan: growth will depend upon public demand for the time being due to factors such as the slowdown of the overseas economies

- FY2016: even though the Japanese economy should gradually return to a recovery path, uncertainties will persist due to the slowdown of the overseas economies.
 - The Japanese economy is forecast to grow +0.6% in FY2016, slowing down from +0.8% in FY2015. Even so, the growth rate should remain above the potential rate of growth (estimated to be around +0.2% to +0.3%), as the acceleration of public investment and economic stimulus measures (scheduled in the autumn season of 2016) serve as underpinnings.
- FY2017: the pace of economic growth is forecast to rise to +1.0% as the economic stimulus measure in the previous year kick in, and the overseas economies – driven mainly by the developed market (DM) economies – gradually pick up.

[Outlook on the Japanese economy]

		2014	2015	2016	2017	2015		2016				2017				2018
		FY				Jul-Sep	Oct-Dec	Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec	Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec	Jan-Mar
GDP (real)	Q-o-q % ch	-0.9	0.8	0.6	1.0	0.4	-0.4	0.5	0.1	0.2	0.2	0.2	0.3	0.2	0.3	0.3
	Q-o-q % ch p.a.	--	--	--	--	1.7	-1.8	1.9	0.4	0.9	0.8	0.6	1.3	0.8	1.0	1.3
Domestic demand	Q-o-q % ch	-1.5	0.7	0.6	0.9	0.3	-0.5	0.3	0.2	0.3	0.2	0.2	0.3	0.1	0.2	0.3
Private sector demand	Q-o-q % ch	-1.9	0.7	0.2	0.7	0.5	-0.6	0.2	0.1	0.1	0.2	0.1	0.1	0.2	0.2	0.3
Personal consumption	Q-o-q % ch	-2.9	-0.2	0.7	1.0	0.5	-0.8	0.6	0.2	0.3	0.2	0.3	0.3	0.3	0.3	0.3
Housing investment	Q-o-q % ch	-11.7	2.4	1.6	-1.5	1.7	-1.0	-0.7	2.2	0.8	-0.6	-0.6	-0.7	-0.4	0.2	-0.0
Capital investment	Q-o-q % ch	0.1	2.0	1.2	1.8	0.8	1.3	-0.7	0.1	0.5	0.5	0.4	0.4	0.5	0.5	0.4
Inventory investment	Q-o-q contribution, % pt	0.6	0.3	-0.4	-0.3	-0.1	-0.2	-0.1	-0.1	-0.2	0.0	-0.1	-0.1	-0.1	-0.0	0.0
Public sector demand	Q-o-q % ch	-0.3	0.6	1.8	1.6	-0.3	-0.1	0.5	0.5	0.7	0.4	0.4	0.8	0.1	0.1	0.4
Government consumption	Q-o-q % ch	0.1	1.5	1.6	1.7	0.2	0.7	0.7	0.2	0.3	0.3	0.2	0.5	0.5	0.5	0.4
Public investment	Q-o-q % ch	-2.6	-2.7	2.6	1.6	-2.4	-3.6	-0.7	2.1	2.6	1.1	1.2	1.9	-1.5	-1.6	0.2
External demand	Q-o-q contribution, % pt	0.6	0.1	0.0	0.0	0.1	0.1	0.2	-0.1	-0.0	-0.0	-0.0	0.0	0.1	0.0	0.0
Exports	Q-o-q % ch	7.9	0.4	1.1	2.8	2.6	-0.8	0.6	-0.4	0.5	0.4	0.5	0.7	0.9	0.9	0.9
Imports	Q-o-q % ch	3.4	-0.1	0.9	2.5	1.7	-1.1	-0.4	0.3	0.7	0.7	0.6	0.6	0.6	0.7	0.7
GDP (nominal)	Q-o-q % ch	1.5	2.2	1.1	2.0	0.8	-0.2	0.6	-0.4	1.0	0.3	0.0	0.2	1.4	0.7	-0.2
GDP deflator	Y-o-y % ch	2.4	1.4	0.4	1.0	1.8	1.5	0.9	0.3	0.6	0.5	0.3	0.6	1.1	1.4	1.0
Domestic demand deflator	Y-o-y % ch	2.1	-0.2	-0.1	0.9	-0.1	-0.2	-0.5	-0.5	-0.5	0.0	0.5	0.9	1.0	0.9	0.8

Notes: Figures in the shaded areas are forecasts.

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

Japan: the y-o-y % change of the core CPI will trend around 0% in the second half of 2016

[Outlook on the Japanese economy (major economic indicators)]

		2014	2015	2016	2017	2015		2016				2017				2018
		FY				Jul-Sep	Oct-Dec	Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec	Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec	Jan-Mar
Industrial production	Q-o-q % ch	-0.5	-1.0	0.6	2.6	-1.0	0.1	-1.0	0.2	1.0	0.9	0.6	0.6	0.5	0.5	0.7
Ordinary profits	Y-o-y % ch	5.1	3.5	-4.9	5.9	8.5	-3.1	-9.6	-6.2	-2.4	-4.7	-5.7	-0.0	4.2	7.6	13.0
Nominal compensation of employees	Y-o-y % ch	1.9	1.7	1.8	2.0	1.7	1.9	2.5	1.9	1.8	1.9	1.7	1.8	1.9	2.1	2.0
Unemployment rate	%	3.5	3.3	3.2	3.1	3.4	3.3	3.2	3.2	3.2	3.2	3.1	3.1	3.1	3.0	3.0
New housing starts	P.a., 10,000 units	88.0	92.1	92.5	90.7	91.7	86.8	94.7	95.3	93.4	91.4	89.6	90.1	90.6	91.3	90.7
Current account balance	P.a., JPY tril	8.7	18.0	17.8	19.5	15.9	19.2	19.8	18.6	17.8	17.4	15.5	16.8	20.0	20.6	17.7
Domestic corporate goods prices	Y-o-y % ch	2.7	-3.2	-2.0	1.3	-3.7	-3.7	-3.4	-3.9	-2.9	-1.5	0.4	0.8	1.0	1.7	1.6
Consumer prices (ex fresh food)	Y-o-y % ch	2.8	-0.0	0.1	1.1	-0.1	0.0	-0.1	-0.4	-0.2	0.2	0.9	1.2	1.2	1.0	0.8
Consumer prices (ex fresh food, ex consumption tax)	Y-o-y % ch	0.8	-0.0	0.1	1.1	-0.1	0.0	-0.1	-0.4	-0.2	0.2	0.9	1.2	1.2	1.0	0.8
Consumer prices (ex food (ex alcohol) and energy, ex consumption tax)	Y-o-y % ch	0.6	0.7	0.3	0.7	0.8	0.8	0.7	0.5	0.2	0.2	0.4	0.7	0.8	0.8	0.6
Uncollateralized overnight call rate	%	0.02	-0.00	-0.05	-0.05	0.01	0.04	-0.00	-0.05	-0.05	-0.05	-0.05	-0.05	-0.05	-0.05	-0.05
Yield on newly-issued 10-yr JGBs	%	0.48	0.30	-0.10	-0.09	0.39	0.31	0.06	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.05
Nikkei average	JPY	16,273	18,841	16,500	17,800	19,412	19,053	16,849	16,600	16,200	16,500	16,800	17,200	17,500	18,000	18,500
Exchange rate	JPY/USD	110	120	107	111	122	121	115	109	105	106	108	109	110	112	113
Crude oil price (WTI nearest term contract)	USD/bbl	81	45	47	47	47	42	34	46	48	48	45	45	47	48	49

- Notes: 1. Figures in the shaded areas are forecasts. 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* (all industries) (ex finance & insurance, and production, transmission and distribution of electricity).
3. Quarterly data on the unemployment rate, new housing starts and current account balance are seasonally-adjusted.
4. Of the finance-related indices, the uncollateralized overnight call rate refers to the rate at the end of term, the yield on newly-issued 10-yr JGBs refers to the average of the end-of-month rates during the relevant 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.

3. The global economy: downside risks will linger despite forecasts of a DM-led recovery

- The rate of growth in the forecast area should pick up toward 2017, downside risks will linger mainly among the EM economies.
 - 2016: our outlook on growth with respect to the US, Eurozone, Indian, Australian and Brazilian economies have been revised upward from our outlook as of May, reflecting the revision of growth in the Jan-Mar quarter.
 - 2017: outlooks on the Japanese, Indian and Brazilian economies have been revised upward. The revision of the Japanese economy stems from the shift in timing of the consumption tax hike.

[Outlook on the global economy]

Calendar year	(Y-o-y % change)					(Y-o-y % change)		(% point)	
	2013 (Actual)	2014 (Actual)	2015 (Actual)	2016 (Forecast)	2017 (Forecast)	2016 (Forecast as of May)	2017	2016 (Breadth of change from May)	2017
Total of forecast area	3.3	3.5	3.2	3.3	3.7	3.2	3.7	0.1	—
Japan, US, Eurozone	0.8	1.5	1.9	1.5	1.8	1.4	1.7	0.1	0.1
US	1.5	2.4	2.4	1.8	2.3	1.6	2.3	0.2	—
Eurozone	-0.3	0.9	1.7	1.5	1.4	1.4	1.4	0.1	—
Japan	1.4	-0.0	0.5	0.5	0.9	0.5	0.6	—	0.3
Asia	6.4	6.3	6.1	6.0	6.0	6.0	6.0	—	—
China	7.7	7.3	6.9	6.6	6.5	6.6	6.5	—	—
NIEs	2.9	3.4	1.9	1.8	2.2	1.8	2.2	—	—
ASEAN5	5.0	4.6	4.8	4.6	4.5	4.6	4.5	—	—
India	6.3	7.0	7.2	7.7	7.7	7.5	7.5	0.2	0.2
Australia	2.0	2.7	2.5	2.7	2.5	2.6	2.5	0.1	—
Brazil	3.0	0.1	-3.8	-3.4	0.8	-3.5	0.6	0.1	0.2
Russia	1.3	0.7	-3.7	-1.2	1.0	-1.2	1.0	—	—
Japan (FY)	2.0	-0.9	0.8	0.6	1.0	0.9	0.2	-0.3	0.8
Crude oil price (WTI, USD/bbl)	98	93	49	44	46	44	46	—	—

Note: The total of the forecast area is calculated upon the 2013 GDP share (PPP) by the IMF.

Sources: Made by MHRI based upon International Monetary Fund (IMF) and statistics of relevant countries and regions.

(Reference) Key political events

	2016		2017		2018	
US	Nov	Presidential election			Feb	FRB Chair Yellen's term of office ends
					Nov	Mid-term presidential elections
Europe	Jun	UK referendum on whether it will stay in or leave the EU	Mar	General election (the Netherlands)	H1	General election (Italy)
			Apr-May	Presidential election (France)		
			Jun	Legislative election (France)		
			Sep	General election (Germany)		
Japan	Jul	Upper House election			Apr	BOJ Governor Kuroda's term of office ends
					Sep	LDP general election
					Dec*	Lower House members' term of office end
Asia	Sep*	Upper house & lower house elections (Australia)	This year	Election of Legislative Council President (Hong Kong)	May	Legislative election (Malaysia)
	Autumn	6th Plenary Session of the CPC Central Committee (China)	Dec*	Presidential election (South Korea)	Autumn	3rd Plenary Session of the CPC Central Committee (China)
	This year	Communist Party Congress (Vietnam)	Autumn	19th National Congress of the Communist Party of China (China)	This year	Upper house election (India)
	This year	Upper house election (India)			This year	Legislative election (Cambodia)
	This year	Legislative Council election (Hong Kong)				
Others	May	G7 Summit Meeting (Japan)			Mar	Presidential election (Russia)
	Aug	Brazil summer Olympic Games			Oct	Presidential election (Brazil)
	Sep	G20 Summit Meeting (China)				
	Sep	Lower house election (Russia)				* = approximate date

Source: Made by MHRI.

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