
Mizuho Economic Outlook & Analysis

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Background of the slowdown in inbound tourism consumption per person and its future outlook

< Summary >

- ◆ Since the latter half of 2015, the slowdown in inbound tourism consumption has been accelerating. A breakdown of factors shows that while the number of inbound tourists to Japan remains firm, growth in expenditure per person has clearly slowed down.
- ◆ Growth in shopping expenditure per person has slowed particularly among tourists from China and the NIEs, which can be explained by (1) the pause in the yen's depreciation, and (2) the fading impact of policy measures such as the expansion of tax-free items and the relaxation of visa requirements.
- ◆ Looking forward, even though the slowdown in inbound tourism consumption may come to a halt by virtue of new policy effects, we do not expect strong growth. To raise the expenditure per person, it will be necessary to boost the consumption of services in addition to shopping.

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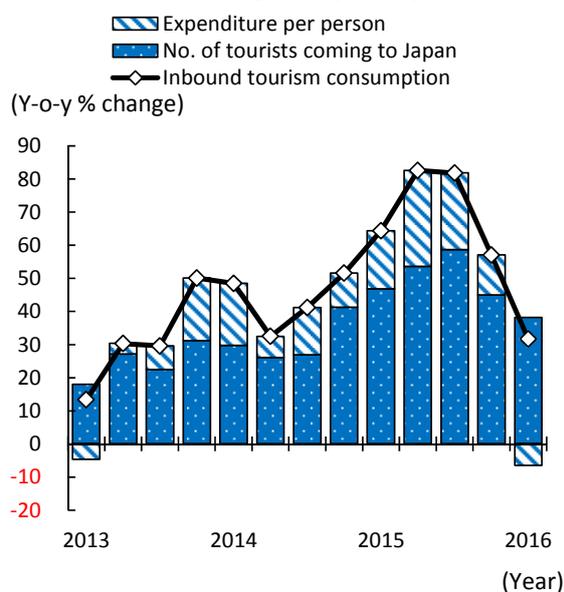
1. A sharp slowdown of inbound tourism consumption

Bearish views are emerging on inbound tourism consumption, which has served to underpin Japan’s economic growth. The ongoing appreciation of the Japanese yen reflecting the destabilization of the global financial markets, and the economic slowdown in China, which boasts the greatest number of tourists visiting Japan, are weighing down inbound tourism consumption, leading to concerns that it may be difficult to maintain the pace of inbound tourism consumption growth achieved thus far.

Looking at the trend of inbound tourism consumption, its growth rate in the Jan-Mar quarter of 2016 remained high at +30% y-o-y. Nonetheless, if we compare this with the growth rate of +80% y-o-y recorded in mid-2015, we cannot deny the slowdown of inbound tourism consumption. Hence we conducted a factor analysis of the value of inbound tourism consumption (**Chart 1**). The chart shows that the growth in the number of inbound tourists is still firm despite a slight slowdown. On the other hand, growth in expenditure per person on a year-on-year basis is clearly slowing down, falling into negative territory during the Jan-Mar quarter of 2016 for the first time in 12 quarters. Thus we can conclude that the recent sharp decline of inbound tourism consumption stems primarily from the fall in expenditure per person.

In view of these circumstances, for the purpose of the expansion of inbound tourist consumption, it is important to promote the expansion of expenditure per person in addition to boosting the number of tourists. In this report, we seek to analyze the background of the current stagnation of inbound tourism consumption growth by focusing on expenditure per person (details of the analysis on the number of inbound tourists can be found in Ichikawa & Tadaide [2016]) and suggest possible remedies. Note that unless otherwise noted, we used the travel consumption amount derived by multiplying the “average expenditure per person” by the

Chart 1: Breakdown of inbound tourism consumption (value)



Source: Made by MHRI based on the Japan Tourism Agency, *Consumption Trend Survey for Foreigners Visiting Japan*, and the Japan National Tourism Organization (JNTO).

“purchase rate” and not the “trip consumption value” or “total trip expenditure per person” announced by the Japan Tourist Agency due to data constraints.¹

2. A significant decline of shopping expenditure per person

First of all, if we divide expenditure per person into shopping and services (**Chart 2**), the chart reveals a sharp decline of shopping expenditure per person growth since the latter half of 2015. On the other hand, there has been no major fluctuation in the area of services, whose consumption value has remained almost unchanged compared with shopping.

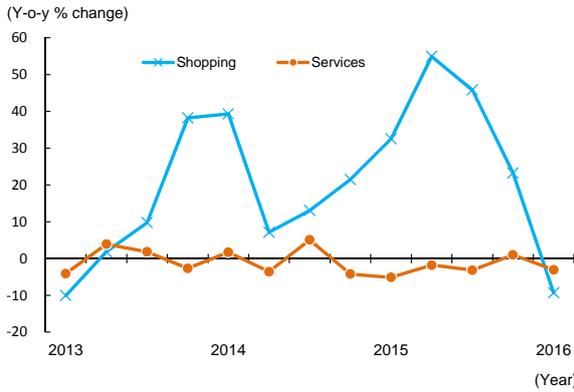
Next, we looked at the breakdown of expenditure per person by category and by nationality (**Chart 3**). In the case of China, over 50% of expenditure per person is shopping, an overwhelming share compared with other countries and regions. For the US, Europe and Australia, services account for a majority of expenditure per person, and the ratio of shopping is relatively small. While the NIEs and ASEAN countries (which are defined as the five countries of Thailand, Malaysia, Indonesia, Philippines and Vietnam in this report) are positioned as somewhere in-between these countries/regions, their shopping expenditure per person is considered to have a great impact on the overall shopping expenditure per person, given their high share in the number of inbound tourists to Japan.

In fact, if we look at the contribution to shopping expenditure per person by country/region (**Chart 4**), since the latter half of 2015 the main factor behind the slowdown of shopping expenditure per person has been the decline of China and the NIEs. It should be noted that the contribution of ASEAN countries is quite small and their overall impact is limited.

Chart 5 depicts the trend of expenditure per person of tourists from China and the NIEs. The chart reveals that the shopping expenditure per person of tourists from China and the NIEs increased significantly toward mid-2015, but has been falling significantly since the Jul-Sep quarter of 2015.

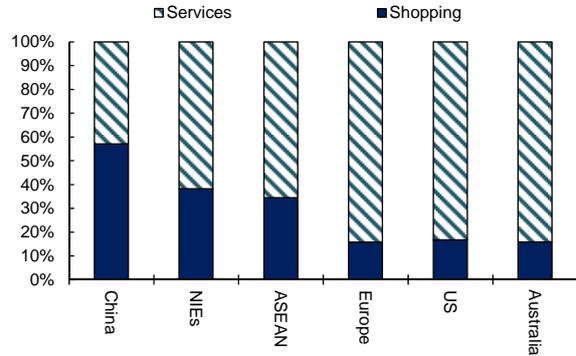
¹ Trip expenditure per person announced by the Japan Tourism Agency is estimated by adding the tourist’s spending (which does not include the cost of the package tour itself) during the stay in Japan to the cost of participating in the package tour, which is allocated to such items as “accommodation,” “restaurant, fast food, café, etc.,” “transportation” and “entertainment.” The derived value is then multiplied by the number of foreign tourists visiting Japan to calculate the total trip expenditure amount. A breakdown of the quarterly “shopping expenditure” has been available since the Jan-Mar quarter of 2014. In this report, we tried to analyze the development of inbound tourism consumption for as long a period as possible by estimating the trip expenditure per person by multiplying the average expenditure by purchaser (for example, confectioneries), which is investigated by the products purchased, by the purchase rate for each product.

Chart 2: Expenditure per person by item



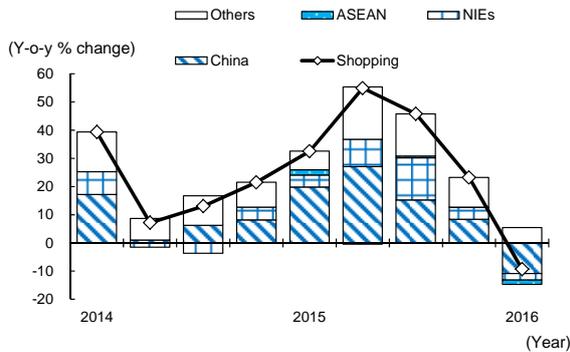
Note: Services represents the total of “accommodation,” “entertainment,” “restaurant, fast food, café, etc.,” “transportation” and “other spending.”
 Source: Made by MHRI based on the Japan Tourism Agency, *Consumption Trend Survey for Foreigners Visiting Japan*, and the Japan National Tourism Organization (JNTO).

Chart 3: Expenditure per person by main visitors’ countries



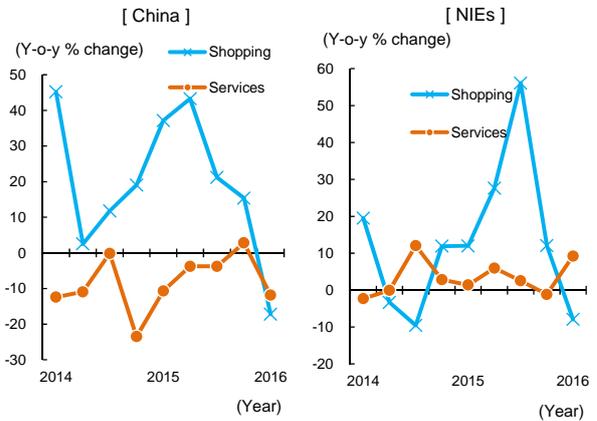
Notes: 1. The graph is created based on the data of trip expenditure per person in 2015 compiled by the Japan Tourism Agency.
 2. Services represents the total of items other than shopping (accommodation, restaurant, fast food and café, etc., entertainment, transportation and other spending).
 3. Europe represents the weighted average value of the UK, Germany, France, Italy and Spain.
 Source: Made by MHRI based on the Japan Tourism Agency, *Consumption Trend Survey for Foreigners Visiting Japan*.

Chart 4: Contribution of shopping expenditure per person by country/region



Note: ASEAN data only from 2015 due to data constraints.
 Source: Made by MHRI based on the Japan Tourism Agency, *Consumption Trend Survey for Foreigners Visiting Japan*, and the Japan National Tourism Organization (JNTO).

Chart 5: Expenditure per person of tourists from China and the NIEs



Note: Services represents the total of “accommodation,” “entertainment,” “restaurant, fast food, café, etc.,” “transportation” and “other spending.”
 Source: Made by MHRI based on the Japan Tourism Agency, *Consumption Trend Survey for Foreigners Visiting Japan*, and the Japan National Tourism Organization (JNTO).

3. The halt in the yen's depreciation and fading policy effects are among the background factors

Then, what lies behind the fall of the growth rate of shopping expenditure per person since the second half of 2015? In search of the answer, we conducted a panel data analysis to seek the determining factors of shopping expenditure per person (details of the analysis can be found in the supplementary discussion in the original report in Japanese²). As a result, (1) real exchange rates, (2) policy to expand tax-free items from October 2014,³ and (3) policy to relax multiple-entry visa requirements were shown to be statistically significant as explanatory variables of shopping expenditure per person. In other words, if the local currency of a tourist strengthens against the Japanese yen, it has the effect of pushing up the shopping expenditure per person. Also, the expansion of tax-free items since October 2014 and the relaxation of multiple-entry visas appear to have supported the increase in shopping expenditure per person.

However, these supporting factors may be fading. The first reason is the pause in the yen's depreciation. Looking at the real exchange rate of the Japanese yen against the currencies of China and the NIEs (**Chart 6**), the weakening trend of real exchange rates (yen depreciation and local currencies appreciation) in countries and regions other than Hong Kong came to a pause in mid-2015. In the Jan-Mar quarter of 2016, real exchange rates rose in all the target countries/regions, with the yen appreciating and local currencies depreciating, reducing the relative inexpensiveness at the time of shopping in Japan.

The second reason may be the slackening of the push-up effect of expanding the tax-free items. To confirm this hypothesis, we would need to track the total sales value of the new tax-free items all around Japan. But due to statistical constraints, we looked at the sales value of the new tax-free items in the statistics covering the purchase of tax-free items by foreign tourists at department stores. Department stores are considered to be the business category that receives the largest benefit from inbound tourism consumption growth,⁴ and we believe that department store sales statistics are a prominent indicator of the overall picture. If we look at **Chart 7**, the growth rate of newly-added tax-free item sales peaked from October 2015, suggesting the possibility that the loss of policy effects

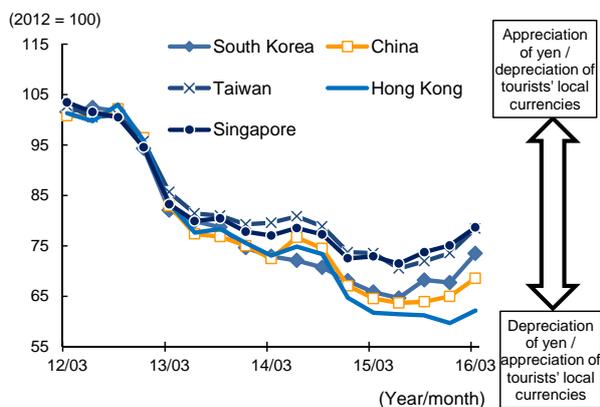
² <http://www.mizuho-ri.co.jp/publication/research/pdf/insight/jp160623.pdf>

³ While consumables such as foodstuffs, beverages, drugs and cosmetics were excluded from the scope of tax-free items in the past, after October 1, 2014, if the total purchase of such consumables is between 5,000 and 500,000 yen per day at the same store, they are subject to tax-free shopping.

⁴ Looking at the *Consumption Trend Survey for Foreigners Visiting Japan* for 2015 compiled by the Japan Tourism Agency, the ratio of respondents who answered that they purchased at department stores accounts for 60.3%, following "duty free shop at the airport" at 61.8%.

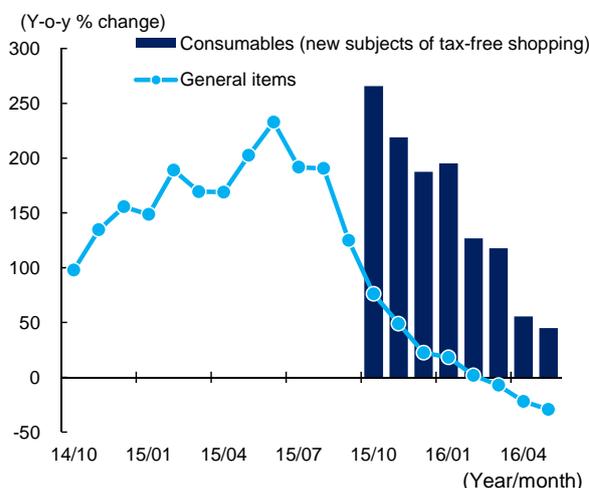
led to a decline in shopping expenditure per person of tourists from China and the NIEs.⁵

Chart 6: Real exchange rates (against the Japanese yen)



Source: Made by MHRI based on CEIC Data.

Chart 7: Purchase of tax-free items by foreign tourists at department stores



Note: The figure is not adjusted for the number of stores.
Source: Made by MHRI based on the Japan Department Stores Association.

As for Chinese tourists, the fading push-up effect from the relaxation of multiple-entry visas may have had an impact on their shopping expenditure. The Japanese government introduced a multiple-entry visa (one that does not require visitors to stay overnight in Okinawa Prefecture or one of the three prefectures in the Tohoku region) targeting high income Chinese tourists. Implementation of this policy may have led to a larger share of high income tourists with little experience of visiting Japan. Intuitively, with more high income earners visiting Japan, the higher the shopping expenditure per person will be. Here, we confirmed the expenditure per person by the number of visits to Japan. **Chart 8** depicts expenditure per person of Chinese tourists by number of visits to Japan. Statistical constraints do not permit us to divide the expenditure by shopping and consumption of services. But as we saw in **Chart 3**, since shopping accounts for a higher share of expenditure in the case of Chinese tourists relative to tourists from other countries and regions, we can infer that the trend of expenditure per person is greatly affected by the trend of shopping expenditure. As we focus on the movement of expenditure per person of tourists with little experience of visiting Japan (one to three times), the growth rate of expenditure rises substantially after the visa relaxation compared with tourists with more experience (over four times). This suggests that as a result of the rise in share of wealthy tourists coming to Japan after the

⁵ The growth rate of the purchase unit price disclosed in the purchase of tax-free items by foreign tourists at department stores has also slowed since the latter half of 2015 and is now hovering in negative territory on a year-on-year basis.

visa relaxation, trip expenditure per person was pushed up. However, in the Jan-Mar quarter of 2016, which is one year after the visa relaxation, expenditure per person of tourists who have come to Japan one to three times declined sharply, showing that the impact of the visa relaxation had run its course.

4. Shrinking growth potential of shopping expenditure per person

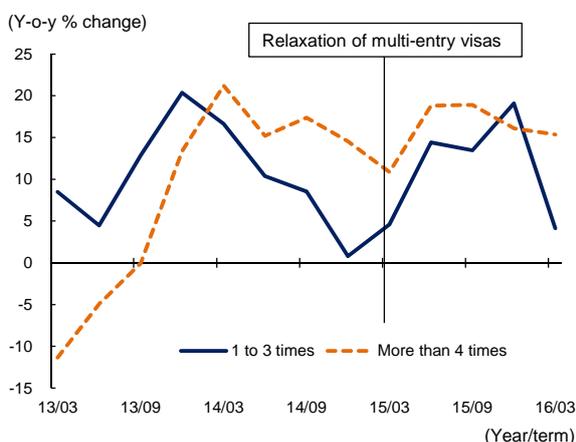
Then, how should we view the outlook of the shopping expenditure per person in the future? Although there is a possibility that the decreasing trend will come to a halt, we cannot expect a significant rise of the growth rate.

In order to boost expenditure per person, a new policy effect is expected to be one factor that might exert a positive impact on spending. Beginning from May 1, 2016, the minimum purchase amount for tax-free shopping was reduced to 5,000 yen for both general items and consumable items (before the revision, the minimum purchase amount was over 10,000 yen and 5,000 yen, respectively). This means that folk craft goods and traditional crafts with low unit prices, previously outside the scope of tax-free shopping, have newly become subject to tax-free shopping. Furthermore, for

Chinese tourists, the Japanese government announced in the Ministerial Council on the Promotion of Japan as a Tourism-Oriented Country held in May 2016 that it will relax the visa requirement⁶ by the summer of this year⁷ in the “2016 Action Program toward the Realization of Japan as a Tourism-Oriented Country.”

By virtue of such a new policy effect, we can expect the slowdown in shopping expenditure per person to gradually ease. But compared with other policies adopted in the past, such as expanding the tax-free items and relaxing visa requirements mentioned

Chart 8: Trip expenditure per person by number of visits



Note: Since the data fluctuate substantially, we calculated the year-on-year changes of the moving average of the past four quarters.

Source: Made by MHRI based on the Japan Tourism Agency, *Consumption Trend Survey for Foreigners Visiting Japan*.

⁶ This includes expanding the multi-entry visa targets, such as commercial and academic purposes, extending the period of validity to a maximum 10 years, and simplifying the visa application process for certain types of college students.

⁷ It should be noted that visa requirements are scheduled to be relaxed also for tourists from India and Russia, albeit we omit a detailed explanation.

earlier, this new policy measure lacks strength and is not expected to lift the shopping expenditure per person as strongly as in mid-2015. Furthermore, if the lower minimum purchase amount for tax-free items results in shifting the majority of demand to items with lower unit prices, shopping expenditure per person may even decline. As for the relaxation in visa requirements for Chinese tourists, unlike the previous visa relaxation targeting high income earners, the revision this time is not expected to relax the income restriction and therefore may have less effect in buoying the shopping expenditure per person.

Also, the Chinese government has implemented measures to restrict the outflow of personal spending by tourists shopping overseas. For example, in April this year, China raised the tariff rate on luxury goods such as expensive watches, alcohol and cosmetics. Beginning in June, the Chinese government has begun to tax or confiscate items if the quantity purchased overseas exceeds a “reasonable standard” for an individual, thereby strengthening the restriction on bringing in items purchased overseas by Chinese tourists. Since we cannot deny the possibility that the Chinese government might continue to beef up such measures, it is highly unlikely that the shopping expenditure per person of Chinese tourists will continue growing at the same pace as in the past.

Attention should also be paid to the trends of foreign exchange rates. As explained earlier, our panel analysis revealed that real exchange rates affect the shopping expenditure per person. Should the UK’s exit from the EU and the weakening of the Chinese yuan heighten uncertainty in the global financial markets, it may trigger a sharp yen appreciation from the current level. In this case, the relative expensiveness of Japanese goods for tourists coming to Japan will rise and exert downward pressures on the shopping expenditures per person.

5. Increasing the consumption of services is the key to boosting expenditure per person

As mentioned above, shopping expenditure per person is no longer expected to be buoyed by the widely known bulk-buying of Chinese tourists. Even though the decline in the shopping expenditure growth rate may be mitigated by policy effects, such policy effects alone cannot continue to fuel the shopping expenditure on a sustainable basis, given that the expansion of tax-free items and the relaxation of visa requirements cannot be maintained indefinitely from a medium-term perspective. In addition, since shopping expenditures are affected by fluctuations in the foreign exchange rates, increasing the dependency on shopping may make expenditure per person even more unstable.

In light of such circumstances, it is imperative to boost expenditure per person by

increasing the services expenditure other than shopping on a medium-term basis, because services expenditure is less susceptible to the changes in foreign exchange rates and policy effects relative to shopping expenditure. In fact, although we also conducted a panel data analysis on services expenditure as we did in Chapter 3, such coefficients as foreign exchange rates and policy effects did not prove to be statistically significant. As pointed out in a preceding study,⁸ services expenditure on accommodation and dining, among others, may be driven more by other factors such as higher brand recognition of Japan's indigenous tourism resources (such as Japanese cuisine and hot springs). More specifically, by enhancing the reputation (brand value) of Japanese tourism through promotional campaigns by the Japanese public and private sectors, and through word of mouth among tourists visiting Japan, we can expect to stimulate the consumption of services of subsequent foreign tourists and create additional demand due to the spread of a new and better reputation.

Furthermore, from a medium-term perspective, the income level of visitors' countries may affect services expenditure per person. **Chart 9** shows the medium-term relationship between expenditure per person and income level by type of spending based on the data of 20 countries.⁹ The chart reveals that unlike shopping expenditure, services expenditures such as food and beverages and lodging tends to increase along with the income level. This may be attributable to the fact that as the income level rises along with economic development, differences in the quality of local goods and Japanese goods gradually become smaller, and this makes shopping in Japan less attractive and shifts the purpose of tourism from shopping to cultural experience. If we actually look at the purpose of tourists' visits by country in **Chart 10**, while the main purpose of Chinese tourists coming to Japan is shopping, tourists from the NIEs, the US, Europe and Australia are more interested in experiencing Japanese cuisine and tend to prefer spending more money on services than goods.¹⁰

Despite the current slowdown, our view over the medium-term remains unchanged that China's income level will rise in the future and its economic structure will shift to one driven by personal consumption and the service industry through an increase of the middle class and wealthy populations. Although its economic structure will not be comparable to the US, Europe and Australia, it is expected to transform gradually into

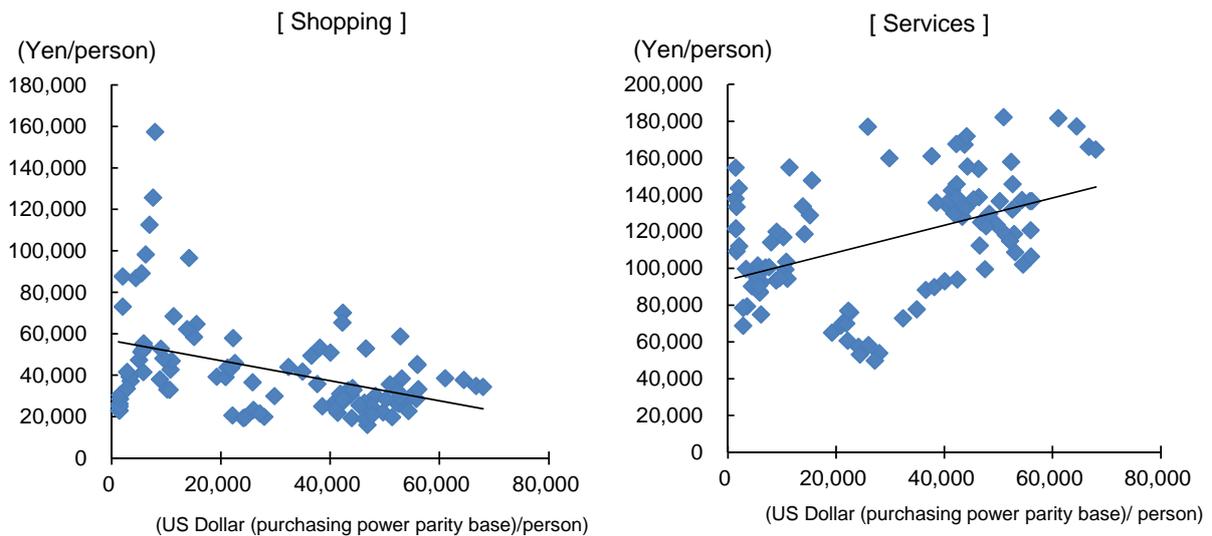
⁸ Refer to Osada, Ojima, Kurachi, Miura, and Kawamoto (2015).

⁹ China, South Korea, Taiwan, Hong Kong, Singapore, Thailand, Malaysia, India, Russia, Australia, the US, Canada, France, Germany, the UK, Spain, Indonesia, Italy, Philippines and Vietnam.

¹⁰ It should be mentioned that for ASEAN, despite its low income level, people from this area are highly interested in Japanese cuisine, and thus there seems to be room to expand the consumption of services. The current services expenditure is also growing with the exception of Thailand. In the future, this area carries the possibility of becoming a primary inbound tourism consumption target after China.

the structure seen in the NIEs countries. While bulk-buying by Chinese tourists has served as a jump starter for inbound tourism consumption in Japan in recent years, it will be essential to capture the consumption of services, which is expected to expand at a gradual but stable pace in the future.

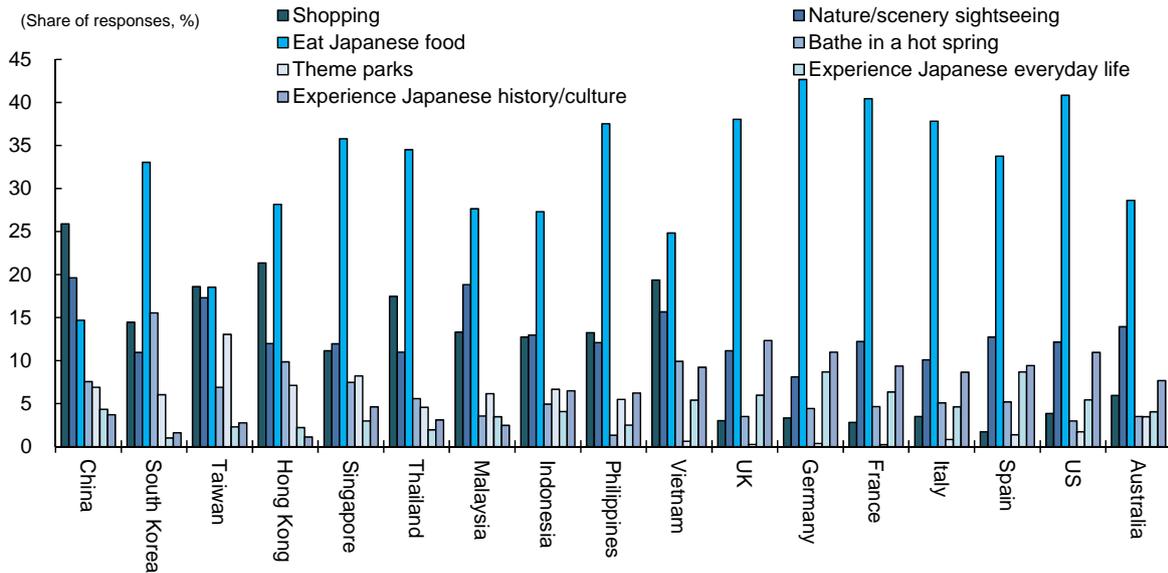
Chart 9: Trip expenditure per person and income level



- Notes: 1. Trip expenditure per person by item has been converted into real value using the consumer price index.
 2. The figure represents trip expenditure per person compiled by the Japan Tourism Agency.
 3. The graphs are created using unbalanced panel data tracked in 20 countries/regions from calendar years 2010 through 2015.
 4. Services represents the total of “accommodation,” “entertainment,” “restaurant, fast food, café, etc.,” “transportation” and “other spending.”

Source: Made by MHRI based on the Japan Tourism Agency, *Consumption Trend Survey for Foreigners Visiting Japan*, the Ministry of Internal Affairs and Communication, *Consumer Price Index*, and the IMF.

Chart 10: Main purposes of tourists coming to Japan



Note: The figure represents the ratio of responses to the question “which were you looking forward to the most?” (single response) in 2015.

Source: Made by MHRl based on the Japan Tourism Agency, *Consumption Trend Survey for Foreigners Visiting Japan*.

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