

Is Japan Heading Towards Deflation Again?



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From this issue of *Japan SPOTLIGHT*, we will be publishing Japan's major economic indicators, and will also be publishing a column on the key indicators among them. The first indicator that we have picked for this new series is the Consumer Price Index (CPI), which measures to what extent Japan has escaped from the deflation that has long tormented it.

What Is the CPI?

The CPI aggregates the prices of goods and services that households purchase. How much the average Japanese household spends on goods and services, such as food and rent, as a percentage of total consumption is principally derived from the "Family Income and Expenditure Survey", and by fixing the consumption weight at a certain standard one can observe how expenditures on consumption fluctuate.

There are three main indices. The first is the "All items" index which aggregates the goods and services that households purchase. The second is the "All items, less fresh food" which excludes fresh food that is affected by non-economic factors such as the weather. The third is "All items, less food (less alcoholic beverages) and energy" which excludes food and crude oil, the majority of which is dependent on overseas imports.

From a monetary policy perspective, "All items, less fresh food" is closely monitored. In its "Outlook for Economic Activity and Prices", the Bank of Japan (BOJ) publishes the outlook for the CPI ("All items, less fresh food") projected by its Policy Committee members. In contrast, "All items, less food (less alcoholic beverages) and energy" is closer

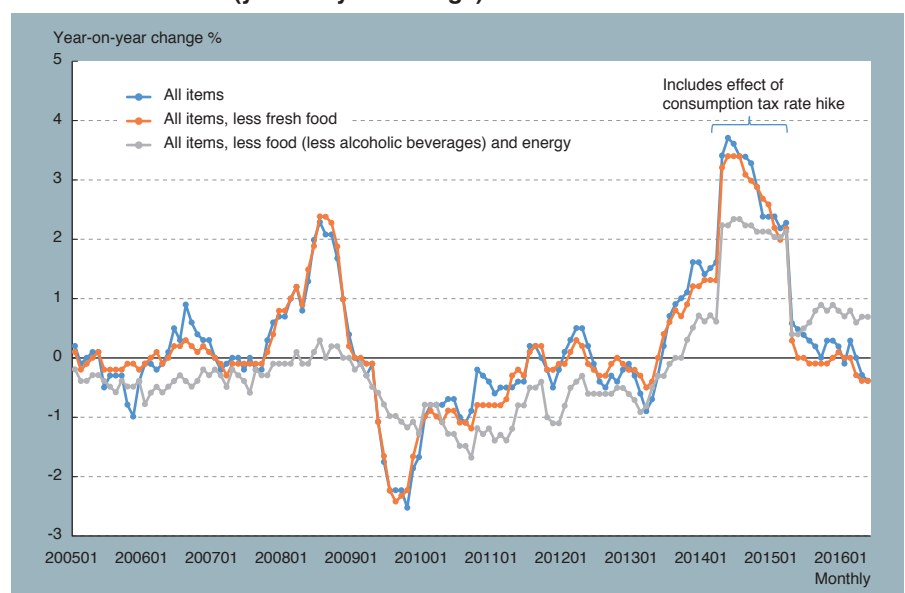
to the Core Personal Consumption Expenditure (PCE) inflation which the Federal Reserve Board of the United States uses to monitor the economic situation.

CPI Negative Range Expanding

The rate of increase in the CPI for "All items, less fresh food" turned positive in June 2013 (*Chart 1*). The increase steadily expanded to 1.3% in March 2014, just before the consumption tax rate was raised to 8%. On April 4, 2013, the BOJ began its "Quantitative and Qualitative Monetary Easing" with a target CPI increase of 2%, and this policy seemed as if it was taking effect smoothly. But in April 2015, when the impact of the consumption rate hike had faded, the rate of increase slowed to 0.3%, and since

CHART 1

Trend in CPI (year-on-year change)



Source: Consumer Price Index, Statistics Bureau, Ministry of Internal Affairs and Communications

March 2016 it has been in negative territory and its range seems to be expanding. There are also more people now wondering whether “Abenomics” has reached its limit.

However, it is appropriate to view the rise in inflation rate for “All items, less fresh food” between 2013 and 2014 as being amplified by the yen’s depreciation and the rise in energy-related prices such as crude oil, both of which took place around the time of the monetary easing. The boosting effect was subsequently toned down on the back of a sharp fall in crude oil prices, and most recently this has become a source of downward pressure.

The rate of increase of the CPI for “All items, less food (less alcoholic beverages) and energy” was slow until 2014, but it is still maintaining a gradual rise at around 0.6% to 0.7%. The extent and repercussions of the impact of the yen’s appreciation since early 2016 will be the key to determining whether the Japanese economy will once again fall into deflation or not.

2015 to Become Reference Year

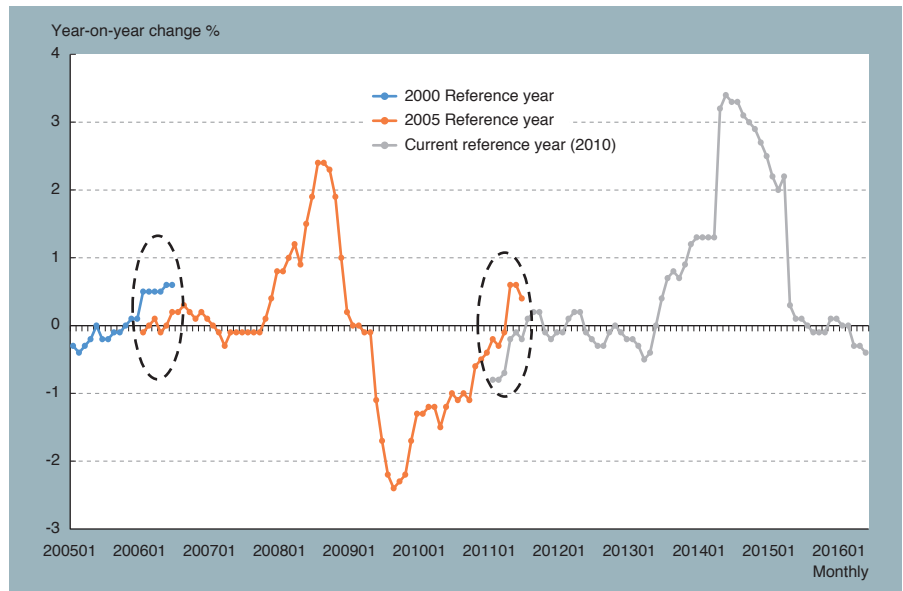
In calculating the CPI, goods and services that are highly important to households are chosen. The degree of importance of items for households changes over time. So does the weight of consumption. Thus the goods and services as well as the weight of consumption undergo a review once every five years. This is what is called the change in the reference year.

The reference year changes to 2015 from the CPI for July 2016 that will be published in August 2016. The number of items used in the calculations is 585 – 33 items such as soy milk and hearing aids have been added, while 32 items such as lunch for children, thermometers, and Electronic Toll Collection (ETC) system tools have been taken off.

The CPI reflecting the revision to the reference year will be calculated for periods after January 2015, and the rate of increase in the CPI under the new reference year will be available for the period after January 2016. On the other hand, the rate of increase in the CPI has already been calculated and published under the 2010 reference year. This means that two kinds of rate of increase in

CHART 2

Rate of rise in consumer prices with revisions to reference year



Source: Consumer Price Index, Statistics Bureau, Ministry of Internal Affairs and Communications

prices exist for the same month.

In the summer of 2006 when the revision of the reference year to 2005 was implemented, the revision also impacted the assessment of monetary policy. Back then, the rate of increase in the CPI (“All items, less fresh food”) under the 2000 reference year showed that Japan was slowly exiting deflation, and the BOJ lifted the zero-interest rate policy in July 2006. But under the 2005 reference year which was published from August 2006, the rate of increase for the CPI (“All items, less fresh food”) dropped to 0% and the BOJ was criticized for being too quick to end its monetary easing (Chart 2).

We will be looking closely at what the rate of increase for the CPI will look like with the 2015 reference year when the publications begin in August 2016.

Note: This article and the charts with the major economic indicators are based on publicly available information as of July 13, 2016. JS

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ECONOMIC INDICATORS FOR JAPAN

Calendar year, Quarter and Month	Real GDP		Nominal GDP		IIP rate of increase over previous year/term (month) (%)	CPI (All items, less fresh food) rate of increase over previous year/ the same term (month) of the previous year (%)
	Amount (trillion yen)	Rate of increase over previous year/term (%)	Amount (trillion yen)	Rate of increase over previous year/term (%)		
2007	523.7	2.2	513.0	1.2	2.8	0.0
2008	518.2	-1.0	501.2	-2.3	-3.4	1.5
2009	489.6	-5.5	471.1	-6.0	-21.9	-1.3
2010	512.7	4.7	482.7	2.4	15.6	-1.0
2011	510.3	-0.5	471.6	-2.3	-2.8	-0.3
2012	519.2	1.7	475.3	0.8	0.6	-0.1
2013	526.3	1.4	479.1	0.8	-0.8	0.4
2014	526.1	0.0	486.9	1.6	2.1	2.6
2015	528.9	0.5	499.2	2.5	-1.2	0.5
2015/3rd Qtr.	530.2	0.5	501.0	0.6	-1.0	-0.1
4th Qtr.	527.9	-0.4	499.7	-0.3	0.1	0.0
2016/1st Qtr.	530.6	0.5	503.6	0.8	-1.0	-0.1
2nd Qtr.	530.8	0.0	504.7	0.2	0.2	-0.4
2016/Jan.	—	—	—	—	2.5	0.0
Feb.	—	—	—	—	-5.2	0.0
Mar.	—	—	—	—	3.8	-0.3
Apr.	—	—	—	—	0.5	-0.3
May	—	—	—	—	-2.6	-0.4
Jun.	—	—	—	—	2.3	-0.5
Sources	"SNA (National Accounts of Japan)", Cabinet Office				"Indices of Industrial Production", Ministry of Economy, Trade and Industry	"Consumer Price Index", Statistics Bureau, Ministry of Internal Affairs and Communications

Calendar year, Quarter and Month	Foreign Trade Statistics									
	Exports amount (trillion yen)	Exports rate of increase over previous year/ the same term (month) of the previous year (%)	Imports amount (trillion yen)	Imports rate of increase over previous year/ the same term (month) of the previous year (%)	Exports amount to US (trillion yen)	Exports to US rate of increase over previous year/ the same term (month) of the previous year (%)	Imports amount from US (trillion yen)	Imports from US rate of increase over previous year/ the same term (month) of the previous year (%)	Exports amount to EU (trillion yen)	Exports to EU rate of increase over previous year/ the same term (month) of the previous year (%)
2007	83.9	11.5	73.1	8.6	16.9	-0.2	8.3	5.5	12.4	13.6
2008	81.0	-3.5	79.0	8.0	14.2	-15.9	8.0	-3.7	11.4	-7.8
2009	54.2	-33.1	51.5	-34.8	8.7	-38.6	5.5	-31.4	6.7	-41.0
2010	67.4	24.4	60.8	18.0	10.4	18.8	5.9	7.2	7.6	12.8
2011	65.5	-2.7	68.1	12.1	10.0	-3.4	5.9	0.3	7.6	0.0
2012	63.7	-2.7	70.7	3.8	11.2	11.7	6.1	2.5	6.5	-14.7
2013	69.8	9.5	81.2	14.9	12.9	15.6	6.8	12.0	7.0	7.7
2014	73.1	4.8	85.9	5.7	13.6	5.6	7.5	10.7	7.6	8.4
2015	75.6	3.4	78.4	-8.7	15.2	11.5	8.1	6.9	8.0	5.3
2015/3rd Qtr.	19.0	3.7	19.9	-5.9	3.8	13.5	2.0	4.5	2.0	5.1
4th Qtr.	18.9	-4.6	19.0	-13.9	3.9	1.5	1.9	-1.0	2.1	5.8
2016/1st Qtr.	17.5	-7.9	17.2	-15.7	3.7	-3.5	1.8	-9.4	2.1	6.0
2nd Qtr.	17.0	-9.5	15.5	-18.8	3.4	-9.6	1.8	-14.7	1.9	1.9
2016/Jan.	5.4	-12.9	6.0	-17.8	1.1	-5.3	0.6	-10.0	0.6	-3.7
Feb.	5.7	-4.0	5.5	-14.2	1.2	0.2	0.6	5.1	0.7	9.3
Mar.	6.5	-6.8	5.7	-14.9	1.3	-5.1	0.6	-20.0	0.8	12.1
Apr.	5.9	-10.1	5.1	-23.3	1.2	-11.8	0.6	-18.1	0.7	9.9
May	5.1	-11.3	5.1	-13.7	1.0	-10.7	0.6	-8.5	0.6	-4.0
Jun.	6.0	-7.4	5.3	-18.8	1.2	-6.5	0.6	-17.1	0.7	-0.4
Sources	"Trade Statistics of Japan", Ministry of Finance									

Calendar year, Quarter and Month	Cash salary amount rate of increase over previous year/ the same term (month) of the previous year (%)	Active job openings-to-applicants ratio (time(s))	Unemployment rate (%)	M2 rate of increase over previous year/ the same term (month) of the previous year (%)	Balance of payments		Yen/\$ rate (averaged during the term)
					Trade balance (trillion yen)	Current balance (trillion yen)	
2007	-1.0	1.04	3.9	1.6	14.2	24.9	117.8
2008	-0.3	0.88	4.0	2.1	5.8	14.9	103.3
2009	-3.9	0.47	5.1	2.7	5.4	13.6	93.5
2010	0.5	0.52	5.1	2.8	9.5	19.4	87.8
2011	-0.2	0.65	4.6	2.7	-0.3	10.4	79.8
2012	-0.9	0.80	4.3	2.5	-4.3	4.8	79.8
2013	-0.4	0.93	4.0	3.6	-8.8	4.5	97.6
2014	0.4	1.09	3.6	3.4	-10.5	3.9	105.8
2015	0.1	1.20	3.4	3.7	-0.6	16.4	121.0
2015/3rd Qtr.	0.5	1.22	3.4	4.0	-0.3	4.9	122.2
4th Qtr.	0.2	1.26	3.3	3.4	0.1	3.4	121.5
2016/1st Qtr.	0.7	1.29	3.2	3.2	0.9	6.0	115.4
2nd Qtr.	0.5	1.36	3.2	3.4	1.5	4.7	108.1
2016/Jan.	0.0	1.28	3.2	3.2	-0.4	0.6	118.2
Feb.	0.7	1.28	3.3	3.2	0.4	2.4	115.0
Mar.	1.5	1.30	3.2	3.2	0.9	3.0	113.1
Apr.	0.0	1.34	3.2	3.4	0.7	1.9	109.7
May	-0.1	1.36	3.2	3.4	0.0	1.8	109.2
Jun.	1.3	1.37	3.1	3.4	0.8	1.0	105.4
Sources	"Monthly Labour Survey", Ministry of Health, Labour and Welfare	"Employment Referrals for General Workers", Ministry of Health, Labour and Welfare	"Labour Force Survey", Statistics Bureau, Ministry of Internal Affairs and Communications	"Money Stock", Bank of Japan	"Balance of Payments", Ministry of Finance		Bank of Japan

Calendar year, Quarter and Month	Foreign Trade Statistics									
	Imports amount from EU (trillion yen)	Imports from EU rate of increase over previous year/ the same term (month) of the previous year (%)	Exports amount to Asia (excluding China) (trillion yen)	Exports to Asia (excluding China) rate of increase over previous year/ the same term (month) of the previous year (%)	Imports amount from Asia (excluding China) (trillion yen)	Imports from Asia (excluding China) rate of increase over previous year/ the same term (month) of the previous year (%)	Exports amount to China (trillion yen)	Exports to China rate of increase over previous year/ the same term (month) of the previous year (%)	Imports amount from China (trillion yen)	Imports from China rate of increase over previous year/ the same term (month) of the previous year (%)
2007	7.7	10.2	27.6	10.3	16.5	6.1	12.8	18.9	15.0	9.1
2008	7.3	-4.8	27.0	-2.0	17.2	4.1	12.9	0.9	14.8	-1.4
2009	5.5	-24.3	19.1	-29.3	11.6	-32.8	10.2	-21.0	11.4	-22.9
2010	5.8	5.5	24.7	29.5	14.1	22.0	13.1	27.8	13.4	17.3
2011	6.4	10.1	23.8	-3.9	15.7	11.7	12.9	-1.4	14.6	9.2
2012	6.6	3.6	23.3	-1.8	16.3	3.3	11.5	-10.8	15.0	2.7
2013	7.6	15.2	25.2	8.1	18.3	12.6	12.6	9.7	17.7	17.4
2014	8.2	6.8	26.1	3.5	19.4	6.2	13.4	6.0	19.2	8.6
2015	8.6	5.6	27.1	3.7	18.9	-2.6	13.2	-1.2	19.4	1.3
2015/3rd Qtr.	2.2	10.3	6.8	3.8	4.7	-0.1	3.4	-1.4	5.1	9.0
4th Qtr.	2.3	13.3	6.5	-8.0	4.6	-9.6	3.4	-6.8	4.9	-6.5
2016/1st Qtr.	2.1	5.2	6.0	-13.1	4.3	-14.4	2.9	-7.1	4.5	-7.5
2nd Qtr.	1.9	-5.5	6.0	-11.9	3.8	-17.2	3.0	-10.8	4.0	-13.0
2016/Jan.	0.7	6.1	1.9	-17.9	1.5	-17.3	0.9	-17.4	1.7	-6.0
Feb.	0.7	14.3	1.9	-10.6	1.4	-10.7	0.9	5.1	1.3	-20.7
Mar.	0.7	-3.6	2.2	-11.0	1.4	-14.7	1.1	-7.1	1.5	6.4
Apr.	0.6	-8.3	2.0	-12.8	1.2	-21.6	1.0	-7.7	1.3	-16.7
May	0.7	-1.5	1.9	-12.1	1.3	-11.5	0.9	-14.9	1.3	-9.7
Jun.	0.7	-6.6	2.1	-10.9	1.3	-17.8	1.0	-10.0	1.4	-12.4
Sources	"Trade Statistics of Japan", Ministry of Finance									