The Japanese Economy In 1994

Prospects for fiscal 1994

The Japanese economy entered a recessionary phase in April 1991 and severe conditions have continued since. During this period, the slump has spread to almost every sector, from manufacturing to private consumption. Considering that the longest postwar recession until now lasted 36 months and that non-manufacturing sectors were comparatively stable following the oil crises and strong yen slowdowns, the gravity of this recession is readily apparent.

Among manufacturing industries, increased semiconductor exports, in conjunction with the increased demand for personal computers in the U.S., has been the principal factor in demand that has already begun to rebound. In the automotive sector, however, passenger vehicle substitution demand has lagged due to insufficient amounts of disposable income, and the demand for trucks is slack due to sluggish private construction.

As a result of the stronger yen, a reduced competitive edge due to overseas manufacturers' quality enhancements, and increased local manufacturing in Europe and the U.S., exports of fully assembled vehicles are also declining. While home appliances have experienced steady replacement purchases for white goods, the audio-visual equipment slowdown continues. Air conditioners are also in a deep freeze due to the chilly summer of 1993. In the area of industrial machinery, in conjunction with the manufacturing industry's freeze on investment in facilities and equipment, machine tool production has declined sharply.

Looking at individual consumption, sales of reasonably priced housing subdivisions under ¥50 million have trended favorably due to lower interest rates and increased financing from the Housing Loan Corporation. As far as new housing starts are concerned, demand for single homes and subdivided lots has already rebounded. However, worsening corporate results have led to increasingly severe employment and income conditions, and because consumption cooled, fiscal year 1992's underlying negative growth trend in department store and supermarket profits has continued.

Since 1992, investment in plants and equipment has dropped below the previous year's levels in almost all sectors. A February 1994 survey of facilities investments conducted by the Industrial Bank of Japan shows a forecasted 5.6% drop in fiscal 1993 and planned cuts of 6.1% in 1994. With the exception of the increases predicted for electric power companies, for whom investment in expanded supply capacity corresponding to medium- to long-term supply and demand is indispensable, rail companies who are struggling to relieve congestion, and the communications sector, which is focusing investments on digital capabilities for mobile telecommunications, there was an across the board decline.

Although stimulus packages, the largest in monetary terms, have been implemented several times, the inevitable feeling is that they have been ineffective in spurring the economy, particularly with regard to the efficacy of public sector investments. One major obstacle is that increases in public construction starts through the economic stimulus packages have not been able to compensate for declining private demand. Additionally, because the content of the construction work has shifted in emphasis to sewerage, parks, and other quality of life projects, materials consumption has declined in scale. Thirdly, we should note that large scale projects involving hundreds of millions of yen have run their course and construction has tended to be smaller in scale.

With slackening demand, the market has softened in almost every industrial sector. Previous aggressive investment in boosted capacity in the pulp and petrochemicals sectors has led to a particularly serious gap in supply and demand. Moreover, the yen's rise has become a negative factor in corporate results, resulting in declining exports and worsening profitability. Although companies have made efforts to cut costs they have been unable to shrink personnel costs and overhead, giving rise to forecasts that key corporations' (approximately 160 companies) ordinary profits will decline by about 40 percent.

Regarding individual consumption in fiscal 1994, income and inhabitant's tax cuts are predicted to have limited effect, and with no improvement in income and employment, a downswing is predicted. In terms of private investment in plant and equipment as well, there is strong overcapacity in every sector due to long-term, stagnant demand adding force to those who argue that the slump will continue. In addition, it is doubtful that there will be an upturn in exports as it is believed that the yen will continue to strengthen unless a reduction in the trade surplus can be achieved. For this reason demand in key industrial sectors will not rebound until the latter half of 1994 and it is thought that the business climate will not start toward an overall recovery until fiscal 1995.

It is forecast that demand for automobiles will begin to recover around summer 1994. For home appliances as well, in addition to an expected rebound for air conditioners, in the area of white goods refrigerators and washing machines are showing signs of a recovery. However, because VTRs, color TVs, and other audio-visual equipment sales continue to stagnate, reflecting broadly increased consumption during the domestic demand growth phase, and because of the continued shift to local production overseas there is a great likelihood that the demand recovery phase will be delayed until fiscal 1995 or later. As no upturn in demand for machinery, plant investments, or construction is expected, the forecast is that a demand rebound is not likely until 1995. This also holds for material industry trends which are dependent upon assembly industry trends, plant investment, or construction demand trends, and the forecast is that demand will probably not recover until the latter half of 1994, in 1995, or later.

In this recession, particular notice should be paid to the maturation of the car markets, existing household appliances, and other consumer durables that have been the motor force of Japanese industry until now. Due to the decline in the younger population over the mid-term along with road, parking facility, and other infrastructure restrictions in major cities, it is forecast that the automobile maturation trend will continue, with a focus on substitution purchase demand. Furthermore, in addition to the continuing shift to overseas production, the stronger yen has led to a decline in competitive superiority and it is forecast that fully-assembled vehicle exports will trend downward.

The home appliance sector has not produced any new growth products in the 1990s either, while hit products that propelled demand have matured. Moreover, with the stronger yen products with no capacity for price shifts have led to broadly worsening export profitability, resulting in a conspicuous shift to overseas production of VTRs, air conditioners, and other goods. This maturation of domestic demand in the consumer durables industry and decreased domestic production due to declining exports has as a natural consequence led to declining production volumes in the materials industry. As such, it is predicted that demand recovery will be extremely slack in most industrial sectors.

As can be seen, existing key industries have insufficient capability to drive the economy. In order to maintain the most stable growth amid predicted conditions of a sluggish economic recovery process, the crucial issue is how best to actualize demand hidden below the surface. For example, because the younger baby boomers will be forming families in the mid-1990s expectations are that there will be new demand for housing acquisitions. Moreover, as approximately 40% of current housing is more than 20 years old, about 70% of urban housing does not meet government housing inspection standards. As such, there is already a considerable amount of latent demand for home reconstruction. For new industry sectors as well there is expectation for future growth in the mobile telecommunications field, such as car and portable phones, and areas in which Japan possesses technological superiority, such as environmental equipment.

In the midst of the major trend toward maturation of demand for consumer durables in this recession, stocks that were accumulated during domestic demand growth phases are being adjusted. Also, the lengthening recession and strong yen's advance have the inherent possibility of bursting the favorable spiral cycle brought on by competitive strength in the assembly and materials industries.

As such, we can say that Japanese industry as a whole faces structural changes and can move in two directions: develop operations in new technologies and products in areas where there is great latent demand and future growth is expected, or develop overseas markets, focusing on Asia, where demand can be foreseen for existing technologies and products. JJTI

(Fujiyama Kazuho, economist)

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Notes: 1. Years are calendar year unless specified.
2. The fiscal year is from April to March.
3. Figures and tables provided by the IBJ unless specified.

Industrial and Economic Outlook