Think Tanks Cautious on 1996 Economy

By Sakamoto Sakae

Last December most of Japan's think tanks released their forecasts for Japan's economy in 1996. Without question, the most "authoritative" was the government's, noted for being the most off the mark for the past several years. Because the government forecast [compiled through joint discussions between the Economic Planning Agency (responsible for overall economic policy), the Ministry of Finance (in charge of public finance policies), and the Ministry of International Trade and Industry (responsible for industrial policy)] calls for higher growth than think tanks affiliated with bank and securities companies predict, the general view is that the government's latest rosy forecast will, as usual, be off target. Economists lapse into a loss of confidence if their predictions err twice or three times and usually make conservative forecasts, but hopes are that this year the government's bullish outlook on the economy will be correct.

Calm has finally returned to the foreign exchange market following last year's sudden high yen.

GOJ sees 2.5% growth

The Japanese government's economic forecast, a prerequisite to the drafting of the fiscal 1996 (April 1996–March 1997) budget, calls for real GDP of 2.5% in 1996. In the government's view, public works spending will pull the economy in the first half of the year, from April to September, and in the latter half, from October to March 1997, private demand will be sparked by the dual forces of private sector capital investments and private consumption, yielding an autonomous recovery. Domestic demand will contribute 2.7% to the growth rate, compared to -0.2% external demand, for a domestically driven economy not likely to incite overseas trade friction. Unemployment will be slightly high at 3.1% (but low compared to levels in other countries). However, with wholesale prices 0.1% higher and consumer prices up 0.5% from 1995, a rise in the rate of inflation indicates that the economy will begin to ease out of deflation and turn in an adequate performance.

How do overseas "authorities" view Japan's economy?

According to an economic forecast released by the Organization for Economic Cooperation and Development (OECD) in mid-December 1995, Japan's real GDP will grow 2.0% in 1996 and 2.7% in 1997. The OECD forecast is for the calendar year and consequently lower than the government's forecast, which is for the fiscal year, in view of the fact that the Japanese economy is entering a recovery phase. Parenthetically, since the OECD's economic forecast predicts 2.7% growth in the U.S. and 2.4% in Germany in 1996, Japan will have the lowest expansion rate among the three leading economic powers. The OECD report cites slumping consumer confidence due to employment instability and worsening results at financial institutions brought on by declining commercial property prices as underlying risks for Japan's economic decline, questioning whether growth will actually amount to 2.0%.

NRI cautiously predicts 1.0%

Compared to the government's predicted growth rate of 2.5% for 1996 (its initial 1995 forecast of 2.8% was modified to 1.2% when the 1996 forecast was released in December 1995), Nomura Research Institute, a Nomura Securities affiliate, released an extremely cautious forecast, calling for 1.0% growth (with a revised forecast of 0.8% for 1995). They see the economy bolstered in the first half of fiscal 1996 by increased public works spending under the economic stimulus package announced in fiscal 1995. But, as overseas economies are expected to decelerate during the second half of 1996 continuing weak external demand will dilute the effects of economic stimuli. Autonomous expansion of private domestic demand (capital investment, private consumption, and others) will be vital, but because structural problems in the economy have not been addressed a burst of new growth will require time. NRI's scenario remains dubious about an autonomous recovery.

Nikko Securities affiliate Nikko Research Center (NRC) is more optimistic than NRI, calling for 1.5% growth in 1996, up from 0.7% in 1995. But the figure is still lower than the government forecast. The main points cited by NRC are: an upturn in corporate profits due to corrections in the strong yen-weak dollar situation, signs of incipient economic expansion yielded by increased shipments of consumer durables and telecommunications investments, and the possibility that the worst case scenario, deflation, will be avoided. But it predicts that the pace of economic recovery will be moderate as smaller businesses' profits will remain stagnant and the pressure of employment and equipment investment adjustment will curb final demand for the time being.

NRC predicts that, although profits will rebound at large corporations, midsize and smaller companies will continue to face a tough business climate. Large companies have begun to show signs of revising capital spending plans upward as profits have rebounded, but smaller companies have become even more cautious about new investments; progress in restructuring efforts has yielded an upturn in profits at major corporations, while smaller subcontractors have been deprived of profit opportunities because large companies' requests for price cuts and manufacturing that has been shifted overseas have resulted in shrinking amounts of work. In NRC's view, large corporations are the only ones for whom better days have returned while, as the burden of restructuring has shifted to their shoulders, smaller firms have not been able to rally.

Telecommunications investments notable

Some think tanks have released forecasts that are nearly as optimistic as the government's. Research Institute on the National Economy (RINE), noted for announcing bullish economic forecasts, predicts 2.3% growth (1.1% for 1995), or about the same level as the government's forecast. The gist is that Japan's economy will differ greatly in the first and second halves of 1996, with the first half marked by a comparatively slow upturn, but an increasingly quick recovery in the second half. RINE offers two reasons for the accelerated upswing in the second half. First, Japan's economy will clearly take on a new form with the shift to an "information society," with increased investment in various types of information technology. And, the benefits of last September's added financial relief (the 0.5% official discount rate) will begin to be felt and the drop in general commodity prices will ease, offering an opportunity to halt stock deflation.

Similarly, Sumitomo–Life Research, Inc. predicts real growth of 2.3% (1.0% in 1995), focusing on telecommunications investments and predicting that capital outlays in this area will spur private sector spending. According to Sumitomo, increased public sector demand will shrink the gap between supply and demand, resulting in improvements in cash flows, and stepped–up investments related to information technology are expected to lead to more growth in private sector capital spending than in fiscal 1995. From the perspective of an increasing need to boost white collar employees' productivity, there is an inherent possibility that explosive growth will be seen in telecommunications spending in 1996.

Exchange rate at ¥103?

The exchange rate (¥79 to the dollar at the highest mark in April and ¥102 to the dollar as of mid-December) stifled the economy as it was on the verge of a resurgence in 1995 and the Bank of Tokyo, which has forecasting expertise in this area, predicts an average 1996 rate of ¥103.50 to the dollar (compared to a projected average rate of ¥95.63 to the dollar in 1995 and an actual ¥99.39 to the dollar in 1994). Further, the current surplus, tracked because it is linked to exchange rates, is projected to shrink to $88.8 billion, down from $105.7 billion in 1995, dropping below 2% of GDP to 1.9%.

Mitsubishi Bank, set to merge with the Bank of Tokyo in spring 1996, also predicts that for the immediate future the exchange rate will continue at ¥100–110 to the dollar in the first half. It says an exchange rate slightly above ¥100 to the dollar seems suitable, noting that the yen's purchasing power parity based on export prices for July–September 1995 is around ¥100. Mitsubishi offers the following rationale: the slowdown in the U.S. economy will lead to a gradual shrinking of the current deficit and Japan's trade surplus will gradually decline as manufacturing sites are increasingly shifted overseas and product imports pick up. However, Mitsubishi believes that, in view of Japan's export dependency and the twin deficits of the U.S., residually structural strong yen-weak dollar strains will continue over the medium to long term. JJTI

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