

“Jan-Mar 2014 First Preliminary GDP Estimates Upswing in Capex”

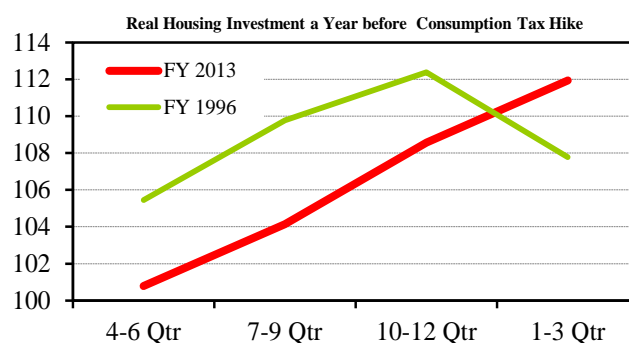
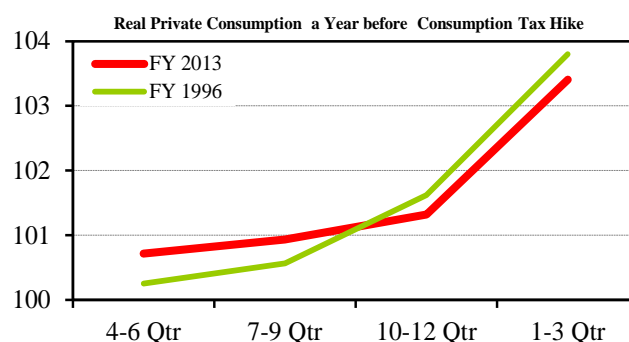
First Preliminary Jan. – Mar. GDP Estimates

On May 15, the Cabinet Office released Jan.-Mar. 2014 first preliminary GDP estimates. The q-o-q real GDP growth rate was +5.9% annualised. It was well above the market consensus (Bloomberg median) of +4.2% annualised which already had reflected high economic growth of rush demand ahead of the consumption tax hike. The reason of this upswing was due to much more-than-expected strength of capex which rose 4.9% q-o-q (+21.0% annualized) against the market consensus of +2.1% q-o-q. The private consumption was +2.1% q-o-q (+8.5% annualized) which was in line with market expectations.

Capex achieved positive growth for the fourth consecutive quarters. Its annualized growth rate remained subdued in single digit for three consecutive quarters since Apr.-Jun. 2013 which was slower than other capital expenditure related statistics such as machinery orders. In general, capex tend to lag behind real core machinery orders (excl. ships and electric power companies) by one to two quarters. I assume, therefore, that for this occasion, capex spent a longer than expected latent period and was finally been reflected in the GDP.

Comparing impact of the rush demand of FY 2013 with FY 1996 which was a year before previous consumption tax hike, there seemed to be no big difference on the private consumption growth rate. For FY 2013, however, due to the weaker yen and higher stock market supported by aggressive monetary and fiscal stimulation, consumer expenditure became active which created some pre-consumption on demand in the first half of the year. Comparing quarterly trend of real private consumption of FY 2013 with FY 1996, former outperformed in the first half but underperformed in the latter half.

Another characteristics this time was that impact of the rush demand before and after the consumption tax hike to the private housing investment was not so eminent compared to that of FY 1996. Probably this was partly due to the introduction of special tax measures from FY 2014 which in some cases were more attractive to purchase house



(Note) Both charts were drawn based on previous year's Jan.-Mar. quarter to be 100
(Source) SMAM, based on the Cabinet Office data



after the consumption tax hike.

This time, the growth rate of private housing investment adding latest figure (+12.9% annualized) and that of Oct.-Dec. 2013 (+18.2% annualized) exceeded that of the first half of the year during which delivery of house was possible ahead of the consumption tax hike.

As to net export, both export and import increased substantially. (exports + 26.3%, imports + 27.7% both q-o-q annualized). Compared to Oct.-Dec. 2013 quarter, the export increased much more than the import which improved the net export substantially from negative 2.2 ppt to negative 1.1 ppt although the attribution to the real GDP growth rate was minus for three consecutive quarters. This was a surprise to me as there was no evidence on the net export improvement from trade statistics. I assume this was due to the special factor caused by the introduction of new standards for international balance of payment statistics. Meanwhile, the growth rate of government consumption turned negative -1.5 % q-o-q annualized) after seven quarters due to the end of the first round of fiscal policy stimulation.

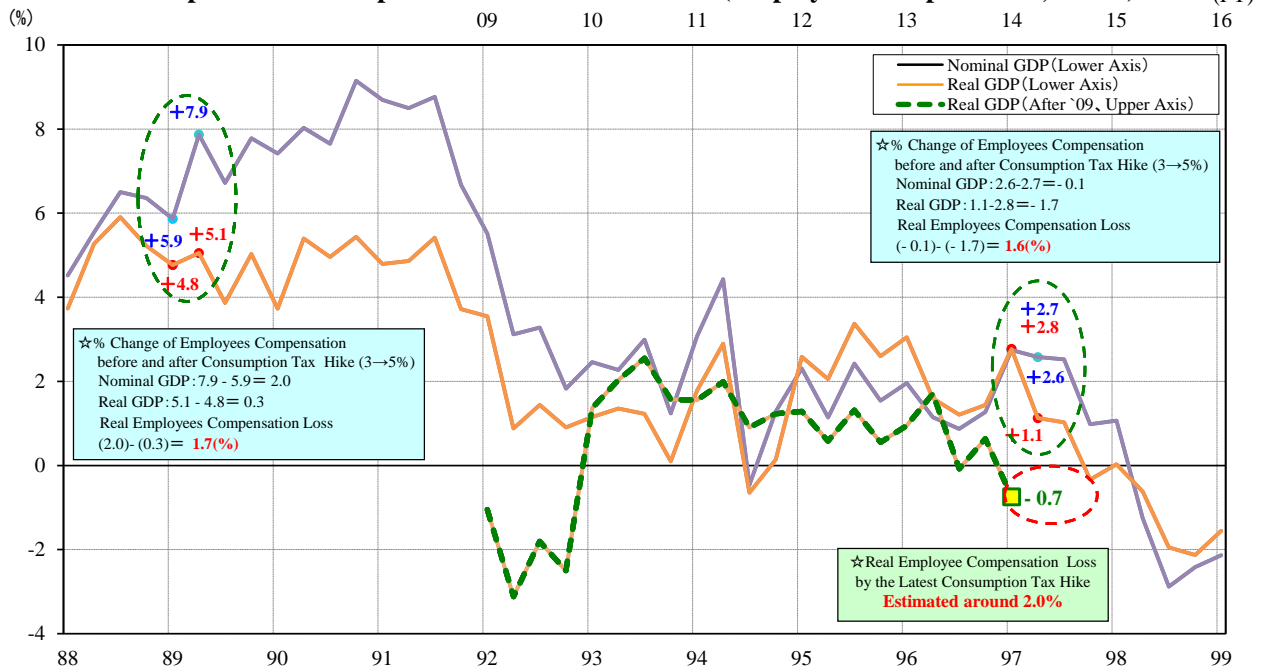
Future Outlook & Focus

It is estimated that the domestic economy will show a substantially negative growth in Apr.-Jun quarter due to subsequent pull-back of rush demand before the consumption tax hike. After Jul.-Sep. quarter it is expected to gradually recover if external shock, considerably detrimental to the economy, will not happen.

There are some uncertain factors over the economic growth recovery. One of which is the unsatisfactory growth of employees compensation. The real employees compensation was +2.8% q-o-q in the quarter of Jan.-Mar. 1997 which was just before the previous consumption tax hike. It contracted in the quarter of Apr.-Jun. after the consumption tax hike (3%→5%), however, maintained positive growth rate of +1.1% q-o-q.

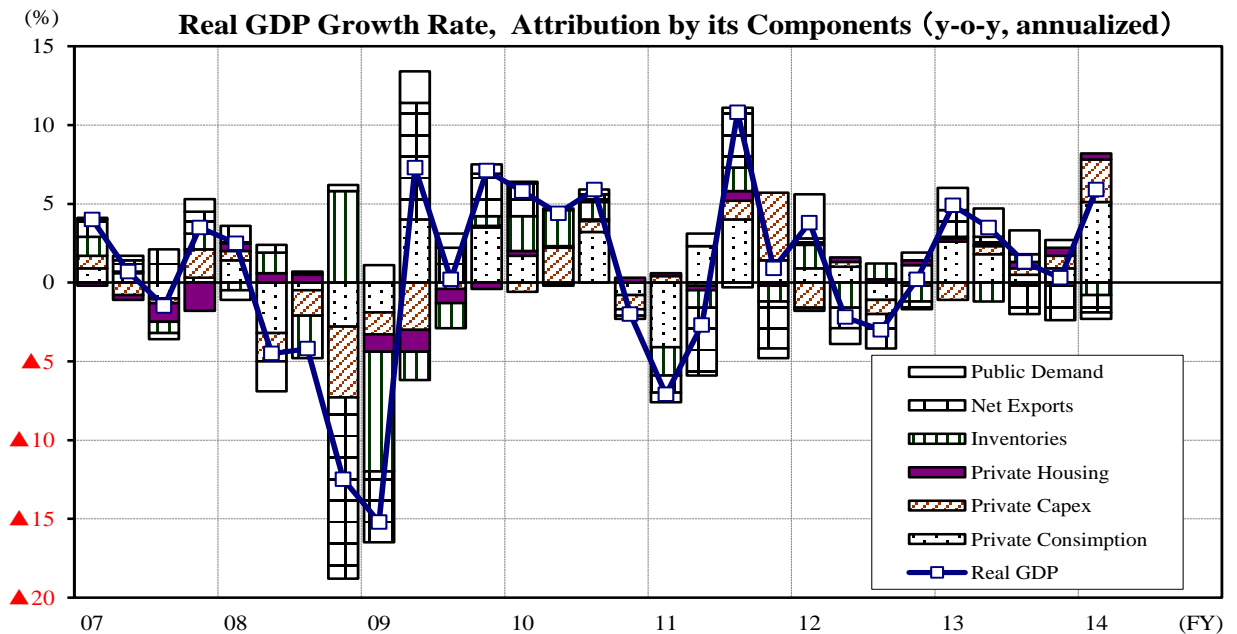
On the other hand, the growth rate of the quarter of Jan.-Mar. 2014 was negative 0.7% q-o-q. Tax hike this time (5%→8%) was estimated to push down the growth rate by 2% or so. The wage hike after the annual spring wage negotiation is supposedly a little bit above 2% which is not enough to boost employees compensation growth positive. I can not help but think that the income environment this year will be worse than that of FY 1997. In order to maintain favorable consumer sentiment, it is hoped that the corporations should endeavor to maintain the momentum of wage hike as well as the government to maintain its economic stimulus policy going forward.

Impact of Consumption Tax Hike to Real GDP (Employees Compensation, Y-o-Y)



(Note) 1. Horizon of data is from Jan-Mar 1988 to Jan-Mar 1999 (Lower Axis), from Jan-Mar 2009 to Jan-Mar 2014 (Upper Axis)
 2. Since data of real employees compensation was not available till 1993, SMAM calculated it by dividing nominal employees compensation by consumer price index (All Items)
 (Source) SMAM, based on the Cabinet Office and the Ministry of Internal Affairs & Communications data.

Real GDP Growth Rate, Attribution by its Components (y-o-y, annualized)



(Note) Horizon of data is from Jan-Mar 2007 to Jan-Mar 2014 (First preliminary announcement)
 (Source) SMAM, based on the Cabinet Office data

◇ **Real GDP Growth Rate, Attribution by its Components** (% , annualized)

Year. Months of Qtr	12.10-12	13.1-3	13.4-6	13.7-9	13.10-12	14.1-3	
Real GDP	+0.2	+4.9	+3.5	+1.3	+0.3	+5.9	
Attribution	Private Consumption	+1.1	+2.6	+1.8	+0.5	+0.9	+5.1
	Private Capex	▲0.2	▲1.1	+0.5	+0.4	+0.8	+2.7
	Private Housing	+0.3	+0.2	+0.1	+0.4	+0.5	+0.4
	Inventories	▲1.0	+0.1	▲1.2	+0.5	▲0.2	▲0.8
	Net Exports	▲0.5	+1.7	+0.5	▲2.0	▲2.2	▲1.1
	Public Demand	+0.5	+1.4	+1.8	+1.5	+0.5	▲0.4

(Source) SMAM, based on the Cabinet Office data

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