

## 【NEWS RELEASE】

August 14, 2019  
SMBC Nikko Securities Inc.

**Quarterly Economy Outlook for FY 2019-2020**

August 14, 2019 (JST), “SMBC NIKKO Japan Economic Outlook for FY 2019-2020” has been released, responding to the first preliminary of GDP (April-June 2019 period).

**See Domestic Recovery Despite Trade War, Tax Hike**

- ◆ Real GDP: +0.9% in FY19 and +0.9% in FY20
- ◆ Nominal GDP: +0.9% in FY19 and +1.3% in FY20


**Summary****• GDP growth outlook**

We revise our outlook to reflect the first preliminary Apr-Jun 2019 GDP data. We forecast real GDP growth of 0.9% YoY in FY19 and 0.9% in FY20, an upward revision of 0.1ppt versus our previous outlook for FY19 (10 June), largely to reflect strong capex and housing investment of late.

**• Current state of the economy**

Apr-Jun 2019 real GDP growth (annualized basis) was up 1.8% QoQ, for a third straight quarter of growth. Drivers of domestic demand like private consumption, capex, and public sector outlays are strong, and the downtrend in exports—the largest drag on the domestic economy—has faded, largely owing to a pause in the semiconductor-related correction. The global semiconductor correction reflected declining demand for IT end products (like cell phones and servers), and the upturn in end product demand has now fed through to components like semiconductors. In the past three months global semiconductor sales have rebounded and semiconductor prices have bottomed as well. This suggests the domestic production correction led by the high-tech field should fade from here.

That said, the external climate still includes many threats such as escalating US-China trade tension and the strong yen. Also, Japan has a consumption tax hike set for 1 Oct. In this light, Japan's economy will likely continue to face domestic troubles and external threats.

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## • **Risk**

Rather than continued escalation of US-China trade tensions, we expect the parties will work toward an agreement. We think the US's unveiling of a fourth round of tariffs on China on 1 Aug was prompted by a perceived failure of China to live up to its agreement to purchase US farm imports. While this might represent a misreading of the data by the US, it suggests the Trump administration's decisions are being influenced by the upcoming 2020 presidential race. Still, the fourth round of tariffs would cover about 40% of consumer goods, and so would likely have a negative impact on the Christmas shopping season if enacted. This suggests further hikes to tariffs ahead of year-end will be difficult.

Meanwhile, China lacks effective ways to retaliate against the US. Indeed, any intensification of the trade war will only accelerate the ongoing trend of firms moving operations outside of China, accelerating the hollowing out of industry there. If Trump is reelected this situation will only get more serious. China's best option would be to come to an agreement with the US and get it to lower tariffs, thus avoiding a hollowing out of its industry.

Both the US and China have room to compromise. It makes sense for the US to get China to resume farm product purchases and to avoid widening the scope of tariffed products. This would be positive both for the US Christmas shopping season and for Trump's reelection prospects. China, meanwhile, had been purchasing US farm products from the start of the year, so resuming such purchases would be easy. It could moreover lay the groundwork for a quid pro quo by the US. We therefore expect US-China trade talks to move toward an agreement from here, rather than intensified conflict.

As for Japan's consumption tax hike, this time around we expect no major front loading of demand nor any significant drop off after the hike. Such trends occur mainly for durable goods, but in the case of autos, nearly 90% of the additional costs from the consumption tax hike will be offset by automobile tax cuts, so we expect no significant demand rush. For housing investment, meanwhile, policies such as longer mortgage tax reduction periods and expanded housing subsidies will make it more beneficial to purchase housing after the tax hike, so we expect no significant demand rush here either.

## • **Outlook for the economy**

We expect the upturn in the semiconductor cycle will drive a cyclical recovery for Japan's economy. As for the trade war, both the US and China have room to compromise, so we expect they will work towards a breakthrough. We expect the consumption tax hike this Oct will bring no major demand rush or drop off. Even if the economy does turn down, the government could unveil further stimulus measures or additional BOJ stimulus at the extraordinary Diet session this autumn. We expect Japan's economy will not fall into recession but rather will enjoy a sustained mild recovery with nearly 1% growth.

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## Quarterly forecasts for Japanese economy

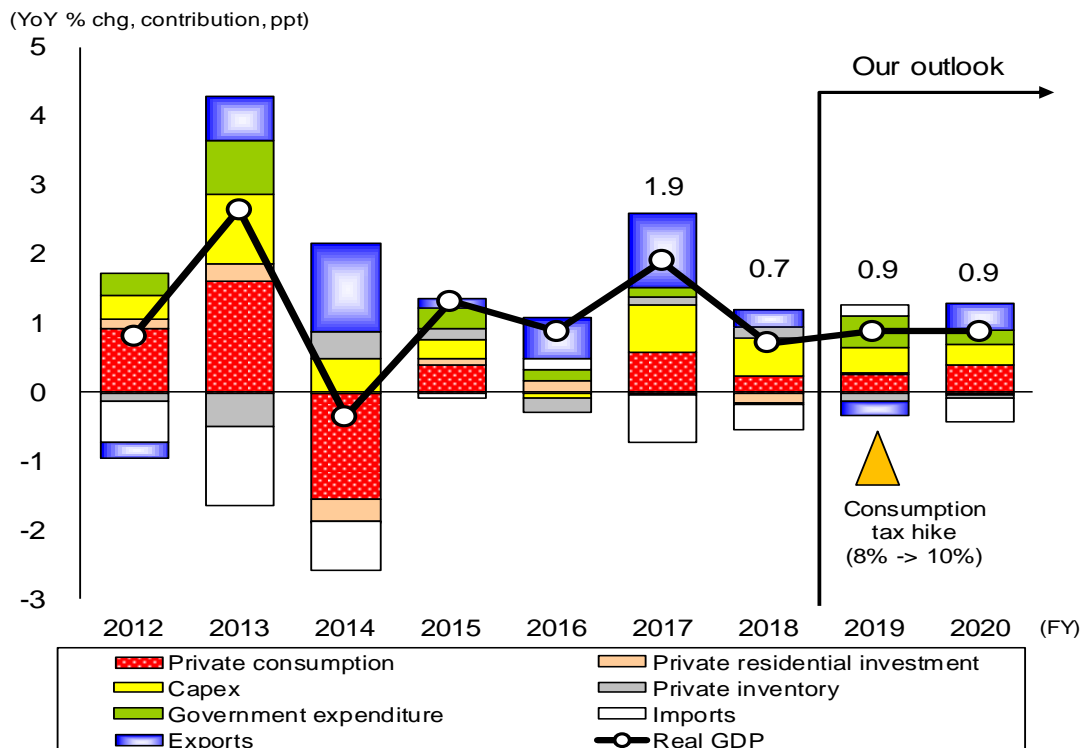
	2018				2019				2020				2021	FY18	FY19	FY20	Comparison with previous forecasts (as at 10 Jun 2018)	
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q				FY19	FY20
Real GDP growth (QoQ)	-0.1	0.4	-0.5	0.4	0.7	0.4	-0.6	0.5	0.0	0.3	0.5	0.0	0.6					
(annual rate)	-0.3	1.6	-1.9	1.6	2.8	1.8	-2.3	1.8	0.1	1.1	2.0	0.0	2.2	0.7	0.9	0.9	0.1	0.0
Domestic demand, contribution (QoQ)	-0.2	0.4	-0.3	0.8	0.3	0.7	-1.1	1.0	0.1	0.3	0.4	-0.1	0.5	0.7	0.9	0.9	0.1	0.0
Private consumption (QoQ)	-0.1	0.4	-0.1	0.4	0.1	0.6	-1.6	1.5	-0.3	0.1	0.3	-0.5	0.5	0.5	0.5	0.7	-0.4	0.3
Capex (QoQ)	-2.5	-1.9	0.8	1.3	0.6	0.2	0.0	-1.5	-0.5	-0.5	0.5	0.5	0.5	-4.4	0.6	-0.9	1.4	0.2
Residential investment (QoQ)	1.0	2.5	-2.6	2.7	0.4	1.5	-0.5	0.0	0.5	0.5	0.8	0.5	0.5	3.5	2.3	1.7	0.6	-0.1
Public investment (QoQ)	-1.0	-1.2	-1.8	-1.3	1.4	1.0	0.8	0.5	0.0	-0.2	-0.5	-0.5	-0.5	-4.0	2.1	-0.1	-1.0	-0.6
Foreign demand, contribution (QoQ)	0.1	0.0	-0.2	-0.4	0.4	-0.3	0.5	-0.5	0.0	0.0	0.1	0.1	0.1	0.0	0.0	0.0	0.0	0.0
Exports (QoQ)	1.0	0.8	-2.1	1.2	-2.0	-0.1	0.0	0.0	0.3	0.5	0.8	0.8	0.8	1.5	-1.2	2.4	0.6	-0.4
Imports (QoQ)	0.6	0.8	-1.2	3.6	-4.3	1.6	-3.0	3.0	0.5	0.5	0.5	0.5	0.5	2.1	-1.0	1.9	0.3	0.2
Nominal GDP growth (QoQ)	-0.1	0.2	-0.4	0.4	1.0	0.4	-1.1	0.9	-0.3	0.6	0.7	0.3	0.5	0.5	0.9	1.3	0.2	-0.2
Industrial production (QoQ)	-0.9	0.8	-0.7	1.3	-2.5	0.6	0.3	2.5	-2.0	0.0	2.0	1.0	1.0	0.2	0.1	2.1	-2.0	0.0
Trade balance (Y tn, SAAR)	4.3	3.4	0.4	-2.3	2.8	0.6	3.6	-3.3	-2.5	-2.5	-2.1	-1.3	-0.4	1.1	-0.4	-1.6	-1.4	-2.9
Unemployment rate (%)	2.5	2.4	2.4	2.4	2.4	2.4	2.4	2.4	2.4	2.3	2.3	2.3	2.3	2.4	2.4	2.3	0.0	0.0
Core CPI (YoY)	0.9	0.8	0.9	0.9	0.8	0.8	0.5	1.5	1.7	1.7	1.8	0.7	0.7	0.8	1.1	1.2	0.6	0.3
(Ex effects of consumption tax hike)	0.9	0.8	0.9	0.9	0.8	0.8	0.5	0.5	0.7	0.7	0.8	0.7	0.7	0.8	0.6	0.7	0.6	0.3
IOER (Eop)	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	0.0	0.0
YCC 10y JGB yields target (Eop)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
US real GDP growth (QoQ annualized)	2.5	3.5	2.9	1.1	3.1	2.1	2.3	2.2	2.1	2.1	2.1	2.1	2.1	2.7	2.2	2.1	-0.2	-0.1
US unemployment rate (%)	4.1	3.9	3.8	3.8	3.9	3.6	3.6	3.6	3.6	3.5	3.5	3.4	3.4	3.9	3.6	3.4	0.0	0.0
US core CPI (YoY)	1.9	2.2	2.2	2.2	2.1	2.1	2.1	2.2	2.2	2.3	2.3	2.3	2.3	2.2	2.2	2.3	0.0	0.0
Fed rate (Eop)	1.625	1.875	2.125	2.375	2.375	2.375	1.875	1.625	1.625	1.625	1.875	1.875	1.875	2.375	1.625	1.875	-0.30	-0.20

Assumptions: Forex rate (annual mean): JPY108.9/USD in FY19 and JPY113.3/USD in FY20; Crude oil price (WTI annual mean): USD57.9/bbl in FY19 and USD58.9/bbl in FY20.

Notes: 1) US GDP on a calendar basis, US unemployment rate is the average for the period, and FF rate at end of year. 2) Actual figures from Cabinet Office (CAO), MIC, METI, BOJ. Forecasts by SMBC NIKKO.

Sources: CAO; Ministry of Economy, Trade and Industry (METI); Ministry of Internal Affairs and Communications (MIC); Bank of Japan (BOJ); SMBC NIKKO forecasts

## Outlook for Real GDP growth



Sources: CAO, SMBC NIKKO forecasts

## APPENDIX

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