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Apr-Jun 2013 First Preliminary GDP Estimate

Undershot expectations but not unfavorable

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Summary

- The first preliminary estimate of Apr-Jun 2013 real GDP (Cabinet Office) posted an advance of 0.6% q/q, annualized at +2.6%, the third quarterly positive growth in a row but short of market expectations (+0.9%; annualized at +3.6%). Behind this was a q/q slide in capex despite expectations of a turnaround, as well as a significant negative contribution of inventories.

- Domestic demand saw the third positive contribution to q/q GDP growth in a row (+0.5 percentage points), while foreign demand saw the second positive contribution in a row (+0.2 points). Real GDP continues to grow supported by balanced domestic and foreign demand. In addition, as the major factor pulling down real GDP was a slide in inventories, the lower-than-expected growth was not as bad as at first glance. Nevertheless, the Apr-Jun GDP result holds the key to determine whether the consumption tax will be raised as planned. We expect the hike to occur as scheduled.

- The ongoing uptrend in GDP is likely to continue in Jul-Sep and beyond. Although risk of a downswing in the Chinese economy warrants monitoring, exports are likely to maintain an uptrend, supported by improvement in overseas economies, centering on the US, and given that benefits from a weaker yen since end-2012 will materialize. The improvement in corporate earnings driven by higher exports should have positive effects on household income, supporting personal consumption. Although capex has stagnated, higher earnings and improved sentiment should give rise to capex. We anticipate the economy gradually gaining momentum in FY13, supported by such a cyclical recovery and other factors including (1) public investment accelerating again reflecting execution of the FY12 supplementary budget, and (2) personal consumption and housing investment seeing forward-loaded demand emerging toward end-FY13, prior to the expected tax hike in April 2014.

Positive contribution of domestic and foreign demand vs. negative contribution of inventories

The first preliminary estimate of Apr-Jun 2013 real GDP (Cabinet Office) posted an advance of 0.6% q/q, annualized at +2.6%, the third quarterly positive growth in a row but short of market expectations (+0.9%; annualized at +3.6%). Behind the shortfall was a q/q slide in capex despite expectations of a turnaround, as well as a significant negative contribution of inventories to GDP growth. Meanwhile, domestic demand saw the third positive contribution to q/q GDP growth in a row (+0.5 percentage points), while foreign demand saw the second positive contribution in a row (+0.2 points). In other words, real GDP continues to grow supported by well-balanced domestic and foreign demand. In addition, as the major factor pulling down real GDP was a slide in inventories, the lower-than-expected Apr-Jun growth was not as bad as at first glance. Nevertheless, the Apr-Jun GDP result holds the key to determine whether the consumption tax will be raised as planned. We expect the hike to be implemented as scheduled.

The GDP deflator increased q/q (+0.1%) for the first time in five quarters, showing signs of a bottoming out, although it declined y/y (–0.3%) for the 15th consecutive quarter. The q/q rise reflects higher import prices triggered by a weaker yen, as well as q/q gains in housing investment, capex, and public investment deflators, accompanying higher construction material prices due to firm construction demand. Nominal GDP increased (+0.7% q/q; annualized at +2.9%) for the third consecutive quarter.

Housing investment, capex, and inventories undershot expectations

Personal consumption increased 0.8% q/q, a rise for the third quarter in a row. It saw a broad-based gain, regardless of type of goods/services. The improved consumer sentiment accompanying higher stock prices has been a major factor driving consumption. At the same time, real employee compensation increased 0.4%, the second q/q gain in a row, helping push up consumption as well.

Housing investment had been steady, supported by ongoing lower housing loan rates and reconstruction demand, but it declined 0.2% q/q, the first slide in five quarters. However, it does not warrant an overly pessimistic view, because the number of housing starts, a leading indicator of housing investment, has been on a steady uptrend.

Capex declined 0.1% q/q, the sixth quarterly slide in a row. Although the decline was minor, it was expected to post the first gain in six quarters, and is thus negative. Although the Bank of Japan’s Tankan survey of corporate sentiment and other statistics showed that sentiment on capex began to signal a turnaround, actual capex fell short.

Public investment increased 1.8% q/q, the sixth consecutive quarterly gain. While the investment level has been high, the pace of growth slowed somewhat. However, it regained momentum, accompanying execution of the FY12 supplementary budget.

Exports increased 3.0% q/q, the second quarterly gain in a row. As effects of the weaker yen since end-2012 have begun to emerge with a time lag, exports have grown steadily. Exports to the EU have been sluggish. However, those to Asian trading partners began to firm up and those to the US have been steady, driving overall exports. Along with improved exports and domestic demand, imports also increased, by 1.5%, the second quarterly advance in a row. However, the smaller gain in imports was offset by a larger gain in exports, and foreign demand (net exports) made a positive contribution of 0.2 points to GDP growth.

Positive growth likely in Jul-Sep 2013 and beyond

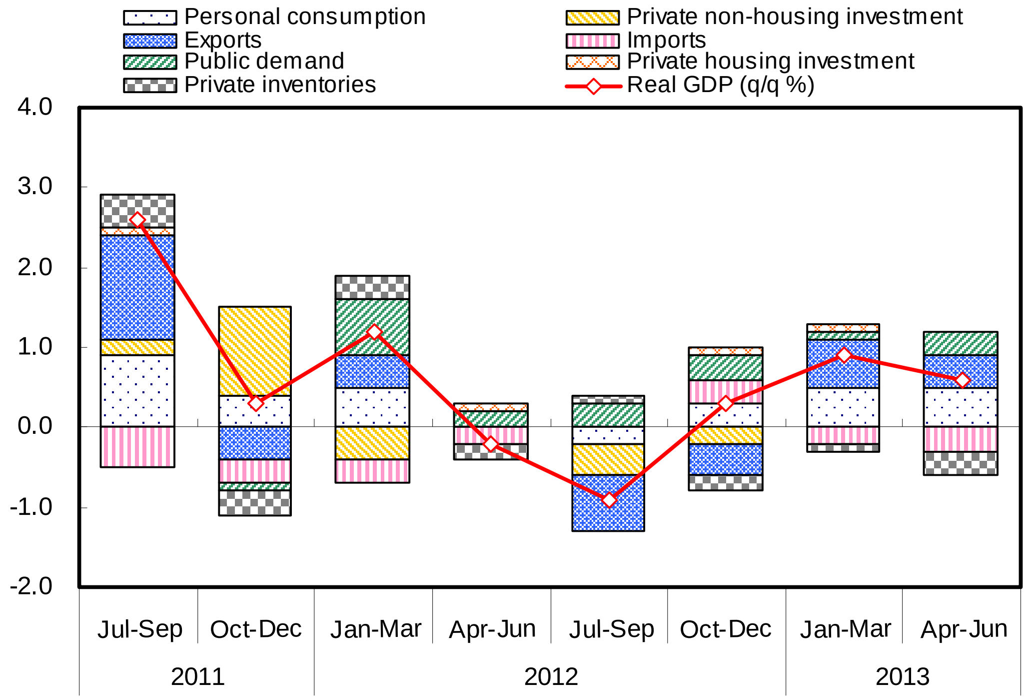
The ongoing uptrend in GDP is likely to continue in Jul-Sep and beyond. Although risk of a downswing in Chinese economy warrants monitoring, exports are likely to maintain an uptrend via improvement in overseas economies, centering on the US, and benefits from a weaker yen since end-2012 starting to materialize. At the same time, the improvement in corporate earnings driven by higher exports should have positive effects on the environment surrounding household income, supporting personal consumption. Although capex has stagnated, higher corporate earnings and improved corporate sentiment should give rise to capex going forward. We anticipate the economy gaining momentum in FY13, supported by such a cyclical recovery and other factors including (1) public investment accelerating again reflecting execution of the FY12 supplementary budget, and (2) personal consumption and housing investment seeing forward-loaded demand emerging toward end-FY13, prior to the expected tax hike in April 2014.

First Preliminary Apr-Jun 2013 GDP (chain linked) **Chart 1**

		2012			2013	
		Apr-Jun	Jul-Sep	Oct-Dec	Jan-Mar	Apr-Jun
Real GDP	Q/q %	-0.2	-0.9	0.3	0.9	0.6
Annualized	Q/q %	-0.9	-3.6	1.0	3.8	2.6
Personal consumption	Q/q %	0.1	-0.4	0.5	0.8	0.8
Private housing investment	Q/q %	2.1	1.6	3.6	1.9	-0.2
Private non-housing investment	Q/q %	-0.3	-3.2	-1.4	-0.2	-0.1
Change in private inventories (contribution to real GDP growth)	Q/q % pts	-0.2	0.1	-0.2	-0.1	-0.3
Government consumption	Q/q %	0.0	0.4	0.6	0.1	0.8
Public investment	Q/q %	5.1	3.5	3.0	1.1	1.8
Exports of goods and services	Q/q %	-0.2	-4.5	-2.7	4.0	3.0
Imports of goods and services	Q/q %	1.3	-0.0	-2.0	1.0	1.5
Domestic demand (contribution to real GDP growth)	Q/q % pts	0.0	-0.2	0.3	0.5	0.5
Foreign demand (contribution to real GDP growth)	Q/q % pts	-0.2	-0.7	-0.1	0.4	0.2
Nominal GDP	Q/q %	-0.8	-0.9	0.1	0.6	0.7
Annualized	Q/q %	-3.3	-3.4	0.4	2.5	2.9
GDP deflator	Y/y %	-1.0	-0.8	-0.7	-1.1	-0.3

Source: Cabinet Office; compiled by DIR.
Note: Due to rounding, contributions do not necessarily conform to calculations based on figures shown.

Contribution to Real GDP (q/q %; % pt) **Chart 2**



Source: Cabinet Office; compiled by DIR.