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Jul-Sep 2014 1st Preliminary GDP Estimate

Negative growth completely outside expectations

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Summary

- The real GDP growth rate for Jul-Sep 2014 (1st preliminary est) declined by -1.6% q/q annualized (-0.4% q/q), recording negative growth for the second consecutive period. Not only did performance fall below market consensus (+2.2% q/q annualized and +0.5% q/q), it fell below the lower level of the outlook, recording minus growth completely outside expectations. Factors behind the major decline in real GDP include anemic growth in personal consumption and a decline in capex despite previous expectations of growth. Private sector inventories also contributed to the major decline.

- Personal consumption was up +0.4% q/q, the first time it has recorded growth in two quarters. Considering the major drop experienced during the Apr-Jun period due to reactionary decline, growth in the Jul-Sep period was slight, a sign that recovery is lagging. A comeback was seen in some areas, including semi-durables (+3.5% q/q) and non-durables (+2.0% q/q), but improvements were slight considering the steep declines both of these areas suffered in the previous period. Meanwhile, in addition to the lagging recovery in the area of services (-0.0% q/q), durables continued their downward spiral (-4.5%) after having experienced major declines last period, thereby helping to push overall figures downward.

- Results for the period showed minus growth outside previous expectations and confirmed that the Japanese economy is experiencing stagnation. However, moderate growth is expected to continue during the Oct-Dec period and beyond. Improvements were seen in real employee compensation during the Jul-Sep period (+0.7% q/q), meaning there is a steady undertone in overall conditions influencing households, including employment and income. Although recovery in personal consumption has been lagging since the reactionary decline earlier this year, a comeback is seen in the near future.

Real GDP falls below consensus; second consecutive quarter of minus growth

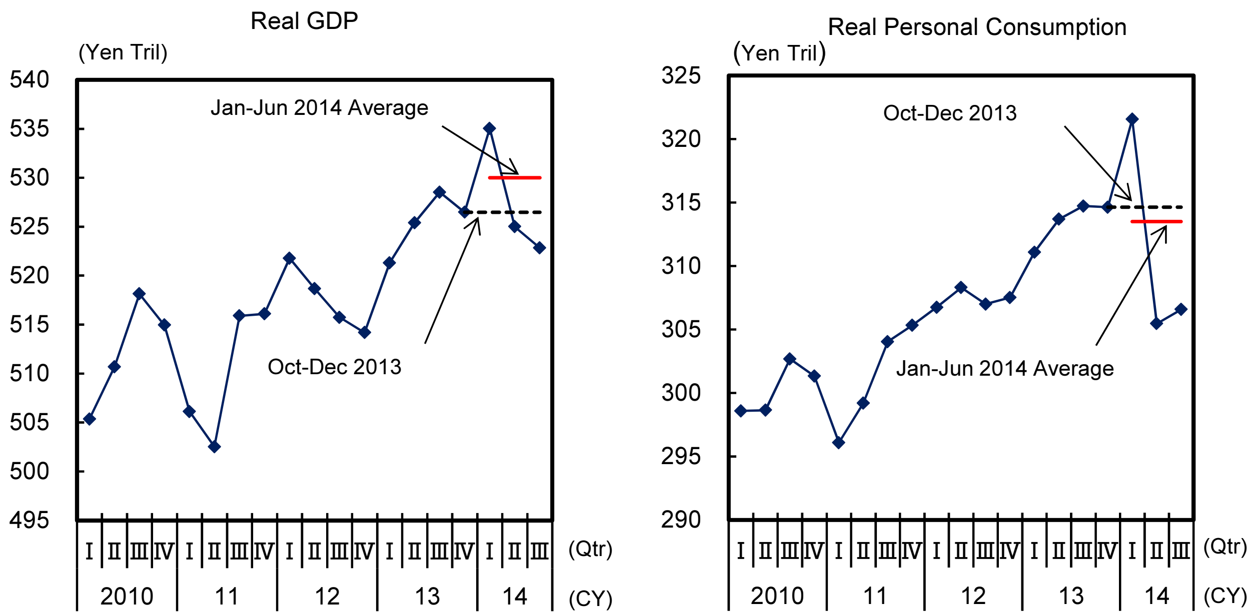
The real GDP growth rate for Jul-Sep 2014 (1st preliminary est) declined by -1.6% q/q annualized (-0.4% q/q), recording negative growth for the second consecutive period. Not only did performance fall below market consensus (+2.2% q/q annualized and +0.5% q/q), it fell below the lower level of the outlook, recording minus growth completely outside expectations. Factors behind the major decline in real GDP include anemic growth in personal consumption and a decline in capex despite previous expectations of growth. Private sector inventories also contributed to the major decline.

Slow recovery in personal consumption; capex falls below expectations

Performance by demand component shows personal consumption up +0.4% q/q, the first time it has recorded growth in two quarters. Considering the major drop experienced during the Apr-Jun period due to reactionary decline, growth in the Jul-Sep period was slight, a sign that recovery is lagging. A comeback was seen in some areas, including semi-durables (+3.5% q/q) and non-durables (+2.0% q/q), but improvements were slight considering the steep declines both of these areas suffered in the previous period. Meanwhile, in addition to the lagging recovery in the area of services (-0.0% q/q), durables continued their downward spiral (-4.5%) after having experienced major declines last period, thereby helping to push overall figures downward.

Housing investment declined for the second consecutive quarter at -6.7% q/q, while personal consumption showed some signs of a comeback, however slight, after the reactionary decline experienced in the previous quarter. Housing investment continued its downward spiral after the reactionary decline experienced in the previous period. New housing starts showed signs of bottoming out early on in the Jul-Sep period, but housing investment still reported a continued decline on a GDP basis, which is reported on an accrual basis.

Status of Recovery from Reactionary Decline After Consumption Tax Increase **Chart 1**



Source: Cabinet Office; compiled by DIR.

Capex fell by -0.2% in comparison with the previous quarter representing its second consecutive period of declines. The coincident index for capex, shipments of capital goods, showed signs of a comeback early on in the Jul-Sep period, hence opinions were that a shift into a growth period was coming up in the future. Instead, there was minus growth completely outside expectations. Until now production has continued to stagnate, and declining operating rates, along with the deteriorating earnings environment, have put the brakes on capex.

Public investment was up by +2.2% q/q, the second consecutive quarter of growth. As the effects of past budgetary measures fall away, public investment begins to slow down as it did during last term. However, front-loading the FY2013 and FY2014 budgets has brought public investment back up to past levels.

Exports grew for the first time in two quarters at +1.3% q/q. While exports to the US and EU have been slow, Asia has been growing, thereby pushing overall figures up. Imports also moved into a growth trend due to the comeback in domestic demand, winning +0.8% q/q. The extent of contribution from overseas demand (net exports) grew only slightly at +0.1%pt q/q.

The GDP deflator declined for the first time in two quarters at -0.3% q/q. The domestic demand deflator grew for the fifth consecutive quarter at +0.1% q/q, but the GDP deflator was pushed down somewhat by the import deflator (a deduction item), which experienced major growth at +3.5% q/q. The GDP deflator declined for the second consecutive quarter at +2.1% y/y, though its growth rate was higher than last period. Meanwhile, nominal GDP declined for the second quarter in a row at -3.0% q/q annualized (-0.8% q/q).

2014 Jul-Sep GDP (1st Preliminary Estimate) **Chart 2**

		2013		2014		
		Jul-Sep	Oct-Dec	Jan-Mar	Apr-Jun	Jul-Sep
Real GDP	Q/q %	0.6	-0.4	1.6	-1.9	-0.4
Annualized	Q/q %	2.4	-1.6	6.7	-7.3	-1.6
Personal consumption	Q/q %	0.3	-0.0	2.2	-5.0	0.4
Private housing investment	Q/q %	4.3	2.2	2.3	-10.0	-6.7
Private non-housing investment	Q/q %	0.7	0.8	7.5	-4.8	-0.2
Change in private inventories (contribution to real GDP growth)	Q/q % pts	0.3	-0.1	-0.5	1.2	-0.6
Government consumption	Q/q %	0.1	0.2	-0.2	-0.0	0.3
Public investment	Q/q %	5.7	1.7	-2.0	0.3	2.2
Exports of goods and services	Q/q %	-0.6	0.2	6.4	-0.5	1.3
Imports of goods and services	Q/q %	1.8	3.7	6.2	-5.4	0.8
Domestic demand (contribution to real GDP growth)	Q/q % pts	1.0	0.2	1.8	-2.9	-0.5
Foreign demand (contribution to real GDP growth)	Q/q % pts	-0.4	-0.6	-0.2	1.0	0.1
Nominal GDP	Q/q %	0.4	0.1	1.5	-0.1	-0.8
Annualized	Q/q %	1.6	0.5	6.3	-0.4	-3.0
GDP deflator	Y/y %	-0.4	-0.4	-0.1	2.0	2.1

Source: Cabinet Office; compiled by DIR.

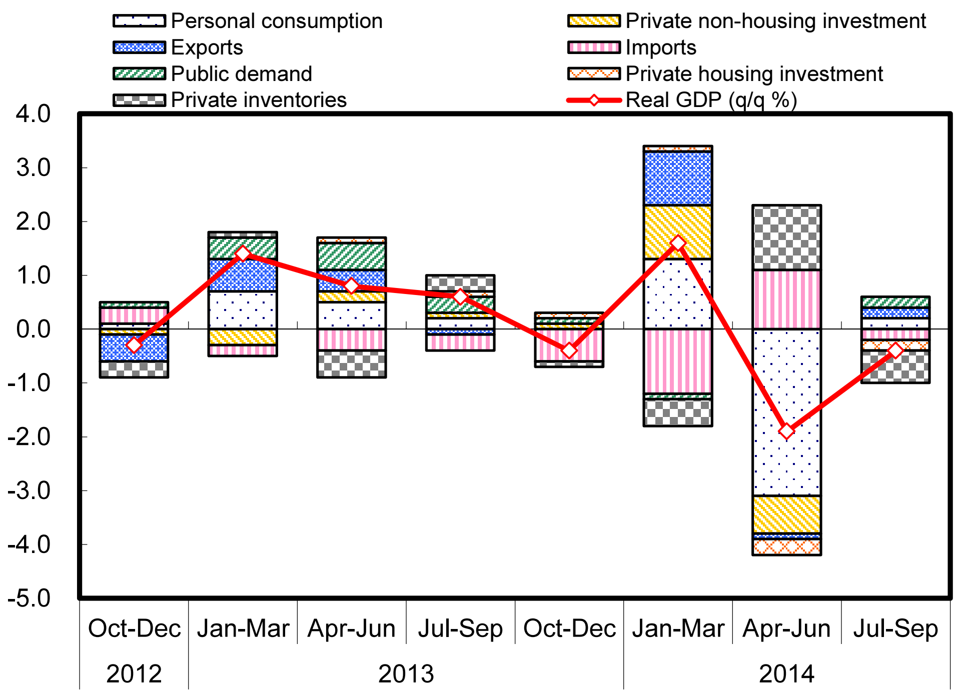
Notes: 1) Due to rounding, contributions do not necessarily conform to calculations based on figures shown.
2) Q/q figures seasonally adjusted basis.

Japan's economy to achieve a gradual comeback in the future

Results for the period showed minus growth outside previous expectations and confirmed that the Japanese economy is experiencing stagnation. However, moderate growth is expected to continue during the Oct-Dec period and beyond.

As can be seen in the improvements in real employee compensation during the Jul-Sep period (+0.7% q/q), conditions influencing households, including employment and income, reflect a steady undertone. Although recovery in personal consumption has been lagging since the reactionary decline earlier this year, a comeback is seen in the near future. As for the Oct-Dec period, chances are good that growth will be achieved for the first time in two quarters due to upward pressure from monthly carryover (carryover as seen in the aggregate index for consumption will give a push of +0.5%). Meanwhile, housing investment, which has continued to suffer from the effects of the reactionary decline, is expected to move steadily toward recovery now that housing starts, a leading indicator, appear to be making a comeback. As for capex, a recovery is expected which will bring activity back to a growth trend. In addition to continued improvement in machinery orders, another leading indicator, the BOJ Tankan indicates that capex activities are reflecting a steady undertone. Operating rates remain at a low level in the manufacturing industries and hence there is still some hesitance regarding increases in capacity, but underlying strength is expected to continue centering on replacement investment. As for exports, moderate growth is seen as overseas economies gradually recover. However, there has been an increasing sense recently that overseas economies are slowing down, so there is increasing risk that recovery may experience a slowdown. This situation will require close monitoring. Slowdowns are already being seen in both the EU economy and in the emerging economies of Asia centering on China. Possibilities are high that exports to these regions will continue to be sluggish for some time. However, the US continues to experience a steady recovery, and overall, exports are not expected to lose momentum.

Contribution to Real GDP (% pt; seasonally adjusted basis)
Chart 3



Source: Cabinet Office; compiled by DIR.