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Japan's Economy: Monthly Outlook (May 2023)

Economic outlook revised; Japan's economy gains in stability with increase in positive factors

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Summary

- In light of the announcement of the Jan-Mar 2023 GDP 1st preliminary results, we have revised our economic outlook. We now see growth in Japan's real GDP at +1.5% in FY2023, and +1.2% in FY2024 (on a calendar year basis we expect +1.3% in 2023 and +1.4% in 2024). We expect Japan's economy to continue recovering despite the economic slowdown in the global economy, with underlying support from the normalization of economic activity, a major increase in wages in the spring wage negotiations, and accommodative fiscal and monetary policies. The major downside risk factors for Japan lie in the overseas economy, such as the increasing instability of banks in the US. This will require continued vigilance regarding the direction of the US economy for the time being.

- Japan's Consumer Price Index, all items less fresh food (core CPI) is expected to be +2.4% in FY2023, and +1.7% in FY2024. With the highest wage increase rate in thirty years expected in the spring wage negotiations, corporate price-setting is aggressive, and the forecast has been revised upward significantly because wages and prices have begun to rise cyclically

- The Bank of Japan is expected to maintain its current monetary policy framework throughout the period covered by this forecast. However, if the BOJ determines that the underlying inflation rate will increase toward 2%, accompanied by higher wages as the downside risks to the US economy and the results of the 2024 spring wage negotiations become known to some extent, it may decide to announce the results of its policy review and remove yield curve control of its current policy as early as the April 2024 Monetary Policy Meeting.

1. Positive Growth Seen Centering on Domestic Demand, but Vigilance Required Regarding Possible Worsening of Overseas Demand

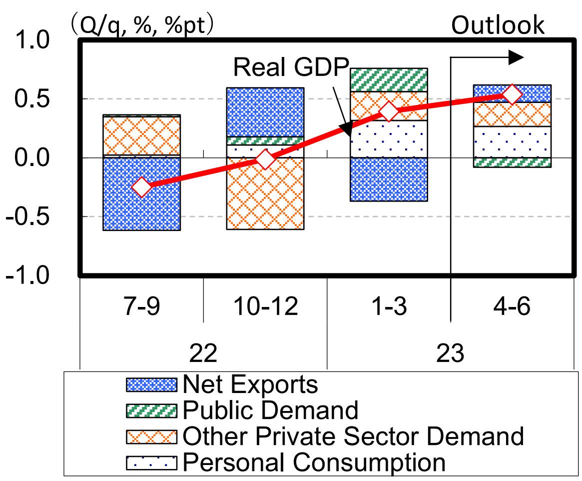
Jan-Mar period real GDP expected to achieve positive growth for first time in three quarters lead by domestic demand

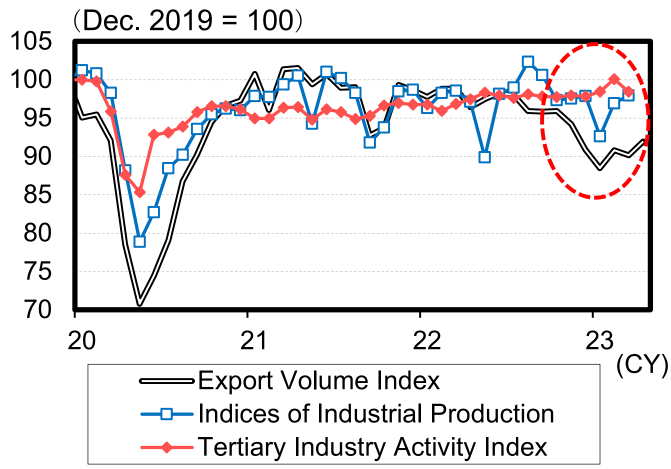
The real GDP growth rate for Jan-Mar 2023 recorded growth of +1.6% q/q annualized (+0.4% q/q), thereby achieving positive growth for the first time in three quarters (chart 1, left)[1]. Private sector demand, including personal consumption and capital expenditure grew overall, compensating for the major decline in exports associated with the slowdown in overseas economies (Chart 1, right). In addition, consumption by tourists visiting Japan (inbound demand), which is included in consumption of services, experienced major growth.

Looking at performance by demand component (Chart 1, left), in the area of private sector demand, all components achieved growth. As for public sector demand, government consumption declined slightly, while public investment grew. As for overseas demand, both exports and imports declined. Since the decline in exports exceeded that of imports, the contribution of net exports (overseas demand) shifted into the negative.

Personal consumption recorded its fourth consecutive quarter of growth at +0.6% despite continuing price highs. Although the government's comprehensive economic measures curbed electricity and city gas prices, the growth rate of the personal consumption deflator increased significantly from the previous period (when it was at +0.7%) to +1.1%. As a result, real employee compensation (in other words real wages as seen from a macro point of view) declined for the sixth consecutive quarter, falling below the level recorded in the Apr-Jun period of 2020 after the first declaration of a state of emergency. With this situation as a background, consumption has continued to recover despite declining incomes, funded by household savings that accumulated substantially after the spread of COVID-19.

Real GDP Growth Rate Results & Outlook (Left); Export Volume & Production, and Tertiary Industry Activity (Right) Chart 1





Source: Cabinet Office, Ministry of Economy, Trade and Industry; compiled by DIR.
Notes: Figures on both the left and right side of the chart are seasonally adjusted.

Real GDP in Apr-Jun 2023 expected to achieve positive growth for second consecutive quarter

Our outlook for the real GDP growth rate in the Apr-Jun period of 2023 sees growth of +2.2% q/q annualized. Though prices will continue to be high, personal consumption will continue to recover,

[1] See the DIR report by Keiji Kanda and Wakaba Kobayashi dated 17 May 2023, *Jan-Mar 2023 1st Preliminary GDP Estimate*.

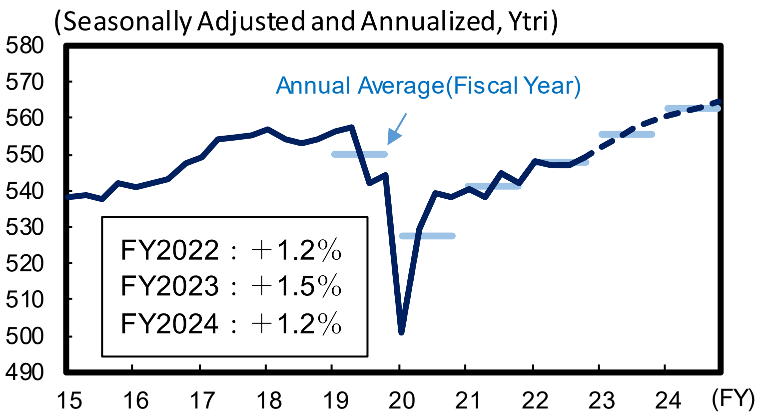
supported by the shift of COVID-19 to Category V Infectious Diseases under the Infectious Diseases Control Law, and the highest wage increases in thirty years in the spring wage negotiations of 2023. In addition, inbound consumption still has significant room for recovery, especially among Chinese visitors to Japan.

On the other hand, the outlook for the US economy is becoming increasingly uncertain, with a number of financial institutions having gone bankrupt in the months of March and May. While the inflation rate is on the way down, it is still significantly higher than the Fed's target of 2%. The growth rate in wages remains high, and there are possibilities of monetary tightening continuing in the long-term, as well as additional interest rate hikes. Meanwhile, the situation in Ukraine remains unpredictable. The European economy could still worsen, and further resource price highs could occur. We need to continue paying attention to the impact of a slowdown in overseas economies on the Japanese economy.

Economic outlook for Japan: domestic consumption should get a boost from economic normalization, but exports of goods are sluggish

Chart 2 illustrates the trend in Japan's real GDP according to our main scenario and our underlying assumptions based on the outlook for overseas economies. Our assumptions for the outlook for overseas economies is based on the latest predictions of our experts on the economies of each of the countries covered (as of May 23).

Outlook for Japan's Real GDP and Assumptions Regarding Overseas Economies **Chart 2**



US, Eurozone & China
Real GDP Growth Rate

US	2022 : +2.1% 2023 : +1.2% 2024 : +0.8%
Eurozone	2022 : +3.5% 2023 : +0.7% 2024 : +1.2%
China	2022 : +3.0% 2023 : +5.9% 2024 : +4.3%

Source: Produced by DIR based on data from Cabinet Office and various countries.
Note: The dashed line in the chart represents predicted values as estimated by DIR. Outlooks for the US, Eurozone and China are based on predictions by DIR's in-house expert.

We expect real GDP growth in 2023 to be +1.2% y/y in the US, +0.7% in the Eurozone, and +5.9% in China. Looking at performance by region, real GDP in the US for the Jan-Mar period of 2023 grew by +1.1% q/q annualized, representing a slowdown in comparison to the previous quarter which was at +2.6%. While housing investment, capital investment, and private inventories were dragged down by the tight financial environment, consumer spending, which accounts for 70% of GDP, accelerated and some resilience was seen. As for the future, a gradual slowdown in consumption and employment is expected, and there are concerns about downside risks to the economy associated with bank instability and high inflation. Our outlook for real GDP in 2023 was revised upwards by 0.1%pt in comparison to the March 9, 2023 report, *"Japan's Economic Outlook No. 216 Update"* (Japanese only, our previous outlook).

With this overseas economic outlook, Japan's real GDP growth rate under the main scenario is expected to be +1.5% y/y in FY2023 and +1.2% in FY2024 (+1.3% in 2023 and +1.4% in 2024 on a calendar year basis).

The outlook for the FY2023 growth rate has been revised downwards by 0.2%pt in comparison to our previous outlook. This is mainly due to a slower-than-expected recovery in exports to China with the sluggish recovery in demand for goods even after the elimination of the zero-COVID policy, and a more cautious outlook for exports to Europe and the US. Looking at the situation by component, semiconductor manufacturing equipment is stagnant with the demand for semiconductors for use in PCs and smartphones down. The outlook for capital expenditure was also revised downwards in association with the slow recovery in the export of goods. However, the view that economic recovery will continue even with high prices remains unchanged from the previous outlook. This is due to the normalization of economic activity and accommodative fiscal and monetary policies (chart 4).

The outlook for the FY2024 growth rate has been revised upwards by 0.2%pt in comparison to the previous outlook. However, when carryover from the previous year is removed, growth is expected to be slow at +0.6% y/y. Growth is likely to be moderate with an expected pause in the recovery of demand associated with economic normalization.

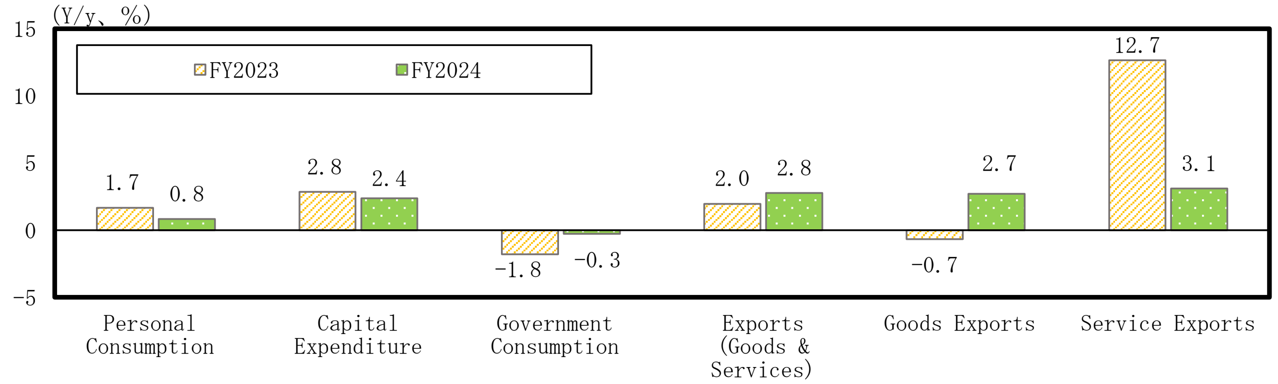
Major demand components are expected to perform as illustrated in Chart 3. While prices remain high, household savings, which accumulated substantially during the Corona crisis, and major wage increases in the spring wage negotiations will support a recovery in personal consumption. The elimination of the shortage of semiconductors is also expected to bring about pent-up demand for motor vehicles.

With the acceleration of domestic economic normalization, capex centering on the non-manufacturing industry should pick up, with a focus on investment in renewal and expansion of capacity. Support is also seen from investment in greening and digitalization. However, it is necessary to remain cautious with the possibility that the tendency to avoid investment in manufacturing may strengthen due to uncertainty regarding the US and European economies.

Government consumption is expected to decline through the end of 2023 as the boost from infectious disease control measures, such as testing programs and vaccinations, will gradually wear off. Thereafter, we expect consumption to return to the trend before the spread of infection, which was increasing mainly in medical and long-term care benefits spending amid the aging of the population.

Regarding exports, FY2023 goods exports are expected to suffer a decline in comparison to the previous year. While pent-up demand for motor vehicles is expected to appear around the middle of 2023 with the resolution of the semiconductor shortage, other goods will likely be severely affected by the slowdown in overseas economies until around autumn of 2023. On the other hand, in the area of service exports, inbound consumption centering on visitors from China is expected to recover significantly.

Outlook for Major Demand Components **Chart 3**



Source: Cabinet Office; compiled by DIR.

Japan's economy gains in stability with strengthening of positive factors

There are many factors bringing underlying support to Japan's economy centering on FY2023. These are as follows: (1) Recovery in consumption of services due to the shift of the classification of COVID-19 to Category V Infectious Diseases under the Infectious Diseases Control Law, (2) Households dipping into excess savings will mitigate the effects of high prices, (3) Further recovery of inbound consumption, (4) Recovery production in motor vehicles and elimination of order backlog in machinery orders due to resolution of supply constraints, (5) Steep wage increases in 2023 spring wage negotiations, (6) Continuation of accommodative fiscal and monetary policies, and (7) A pause in import inflation (Chart 4). Factor (5) has been added since our previous outlook (the March 9, 2023 report, *"Japan's Economic Outlook No. 216 Update"* (Japanese only), and as for (6), the possibility that Japan's monetary policy will change has actually decreased for the time being (see Chapter 2 for more details). These factors are providing increased stability for Japan's economy.

Consumption of domestic services according to GDP statistics, excluding inbound consumption, is estimated to have accounted for 54% of disposable income during the Jan-Mar period of 2023. This falls below the 57% recorded during the Jul-Sep period of 2019 before the increase in consumption tax and before the spread of COVID-19. If a recovery to that level is achieved, consumption of services would be boosted around 8 tril yen annualized. However, since goods consumption may stagnate in the process of service consumption recovery, the overall increase in consumption must be discounted, but for the time being, the shift of the classification of COVID-19 to Category V Infectious Diseases under the Infectious Diseases Control Law, and Nationwide Travel Support[2], are expected to support the recovery in service consumption.

[2] Nationwide Travel Support has been extended through June and will continue through July in some regions.

Seven Positive Factors for Japan's Economy — Chart 4

Factor	Comments
(1) Recovery in consumption of services due to the shift of the classification of COVID-19 to category Ⅴ Infectious Diseases under the Infectious Diseases Control Law	The ratio of disposable income accounted for by service consumption is still low. Consumption of services would grow to around 8 tril yen if it were to reach the level recorded during the Jul-Sep period of 2019.
(2) Households dipping into excess savings will mitigate the effects of high prices	Household savings, which has grown at a pace exceeding that recorded before the spread of COVID-19, was approximately 45 tril yen as of the end of March 2023 (this is the equivalent of 16% of consumer spending in 2022).
(3) Further recovery of inbound consumption	A full-fledged recovery in the number of tourists visiting from China is on the way after having continued to be sluggish. Inbound consumption is expected to grow by around 3 tril yen in 2023.
(4) Recovery production in motor vehicles and elimination of order backlog in machinery orders due to resolving of resolution of supply constraints	If pent-up demand for motor vehicles appears, demand will increase by around 1.7 tril yen from households alone.
(5) Steep wage increases in 2023 spring wage negotiations	The rate of wage increase including regular salary increase is expected to be at its highest level in thirty years.
(6) Continuation of accommodative fiscal and monetary policies	The BOJ is taking a serious view of the risk of an overly hasty monetary tightening if moves are made to quickly achieve the 2% price stability level, and therefore will continue yield curve control for the time being.
(7) A pause in import inflation	Resource prices may continue stable with the slowdown in the global economy, but resource prices still threaten to rise again if the Ukraine situation becomes increasingly tense.

Source: Produced by DIR.

High prices have put downward pressure on personal consumption through a decline in household purchasing power, but this has been mitigated by the approximately 45 tril yen in excess savings[3] that have accumulated at a faster pace since the pandemic (the amount at the end of March 2023 is equivalent to 16% of the amount of personal consumption in 2022). The fact that consumer spending has increased for four consecutive quarters despite a sharp decline in real employment compensation can be attributed to the fact that a portion of household savings was withdrawn and used to finance consumption.

The number of foreign visitors to Japan has surged since October 2022, immediately after the drastic relaxation of border control measures, recovering to 67% of what it was in April of 2019 in April 2023. However, the number of visitors from China, which reached around 10 million in 2019, has only recovered to 15% of that earlier figure. The pace of recovery is likely to pick up in the future with the increase in the number of regular flights between Japan and China, and the Chinese government's lifting of the restriction on group tours to Japan. We expect the number of Chinese tourists visiting Japan in 2023 to reach around 24 million (an increase of around 20 million in comparison with the previous year), and inbound consumption to total 4.1 tril yen (an increase of 3.2 tril yen in comparison with the previous year).

Domestic sales of new cars in April 2023 reached their highest point since April of 2021 (seasonally adjusted by DIR) due to the mitigation of the shortage in semiconductors for motor vehicles. However, pent-up demand, generated by the inability of supply to keep up with demand until now, is still at a high

[3] We consider the deviation from the trend in household savings seen in 2015-19 (excluding the Oct-Dec 2019 period, which was strongly affected by the consumption tax hike and natural disasters) to be "excess savings," and base our estimate on this assumption.

level, and is estimated to have reached approximately 630,000 units as of the end of April 2023, or approximately 1.7 tril yen in monetary terms. Recovery production of motor vehicles in order to handle pent-up demand (i.e. for the purpose of using up order backlog) is expected to be in full-gear by around summer of 2023[4], and is expected to boost not only the consumption of durables, but exports and capital expenditure (in the form of corporate purchasing of vehicles) as well.

Wage increase rate in spring wage negotiations may be raised to the 3% level in 2024

As mentioned above, the 2023 spring wage negotiations are expected to bring the highest rate of wage increases in 30 years. According to the results of the fifth round of responses released by the Japanese Trade Union Confederation on May 10, the weighted average wage increase rate (including regular salary increases) was 3.67%, and 3.35% for small and medium-sized companies with less than 300 employees.

The focus will be on whether the high rate of wage increases will continue in 2024 and beyond. We estimated the rate of wage increase in the spring wage negotiations by using corporate performance, labor supply and demand, the rate of increase in the consumer price index (CPI), and terms of trade (all of which are values for the previous year), which affect the rate of wage increase in the spring wage negotiations, as explanatory variables, and found that the rate of wage increase in the 2024 spring wage negotiations will be 3.2% (Chart 5 left). The reason for this is that the terms of trade are expected to improve in 2023, and the rate of CPI increase and the demand deficient unemployment rate are expected to remain at the same level as the previous year, while the rate of increase in sales is expected to contract.

The estimated rate of wage increase in the 2023 spring wage negotiations is 3.1%, and the actual rate is likely to land in the 3.6% range. One of the reasons why wage increases will be much higher than estimated is that the external labor market (job change market) is likely to become more active. If a situation occurs where wages are likely to rise due to job changes, even in Japan, where the internal labor market is well-developed, companies will be forced to be more aggressive in raising wages to prevent employees from leaving their jobs[5]. Such "defensive wage increases" are more likely to be implemented by small and medium-sized enterprises, which have serious labor shortages, than by large enterprises.

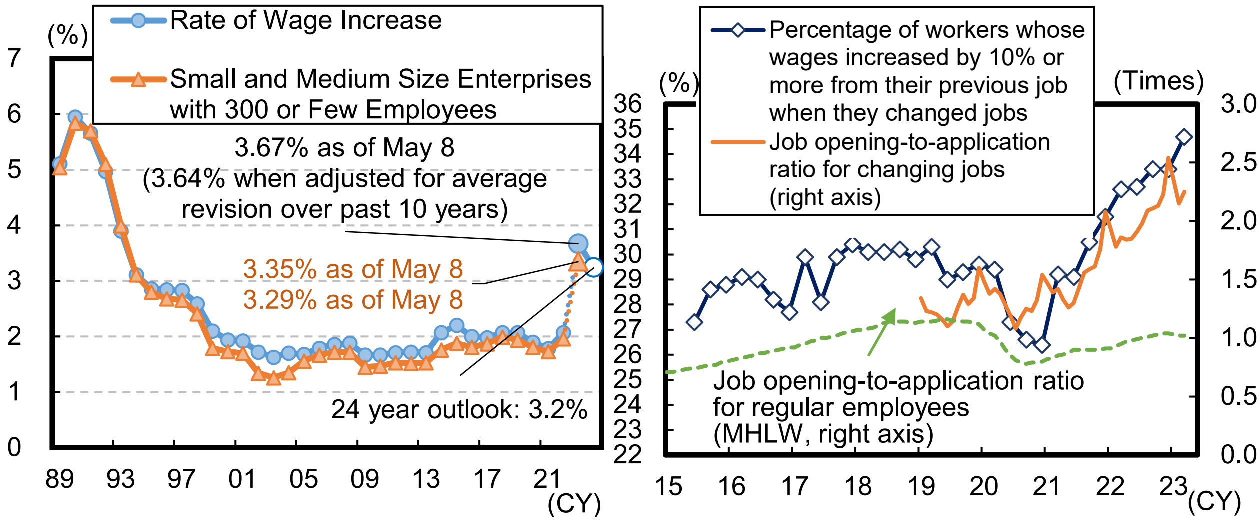
Chart 5 right shows job change market trends based on publicly available data from private job search support service companies. The job-change opening-to-application ratio has been rising rapidly since the beginning of 2022, exceeding 2x in August. While the number of persons seeking to change jobs has remained flat, the number of job openings has been on a steady increase since the middle of 2020. The most recent figures published by the Ministry of Health, Labor and Welfare show that the job opening-to-application ratio for regular employees is at the same level as before the expansion of the infection, indicating that the labor supply-demand balance in the job market is tightening noticeably. In addition, the percentage of job changers whose wages increased by 10% or more as a result of changing jobs rose rapidly from the second half of 2021 to the first half of 2022, reaching its highest level since the Apr-Jun period of 2002 in the Jan-Mar period of 2023.

[4] According to reports, Toyota Motor Corporation is also planning a high level of recovery production in the summer of 2023.

[5] Kakuho Furukawa, Yosuke Kido, and Yoshihiko Hogen (2023), "Labor Market of Regular Workers in Japan: A Perspective from Job Advertisement Data" (Bank of Japan Working Paper Series, No. 23-J-2 (Japanese only, translated by DIR.)), pointed out the following spillover channels through which an increase in wages offered in the job market boosts average wages for regular employees: (1) a channel in which firms raise wages in order to retain workers as it becomes easier for them to move to higher paying jobs (external effect), and (2) a channel in which firms raise wages for fairness consideration as newly hired workers are paid high wages within a firm (internal effect).

Although there is a possibility that the momentum for wage increases may wane in the future due to a decline in labor demand, especially in the manufacturing sector as overseas demand falters, if the economy continues to recover and the external labor market becomes more active, the wage increase rate in the 2024 spring wage negotiations will be in the 3% range, following the previous year's rate.

Trends in Rate of Wage Increase, Including Fixed Salary, in Spring wage Negotiations Announced by Japanese Trade Union Confederation (left), and Trends in Job Change Market (right) Chart 5



Source: Ministry of Internal Affairs and Communications, Ministry of Finance, Ministry of Health, Labour and Welfare, Bank of Japan, Japanese Trade Union Confederation, "2023 Spring Wage Negotiations, Results of Fifth Round of Responses" (May 10, 2023), "Wage Changes at the Time of Job Change" by Recruit Co., doda (Persol Career); compiled by DIR.

Notes: 1) The chart on the left shows the results of tabulating responses using the average wage method. Wage growth rate forecast for 2024 was created from an equation using the following explanatory variables: (1) sales growth rate, (2) CPI growth rate, (3) underemployment rate, (4) terms of trade (in log terms), (5) wage dummy variable, and (6) constant. (1) to (4) are the previous year's values. ((1) has a 10% significance level and (2) and (4) through (6) have a 1% significance level. The estimation period is 1976-2022, and the adjusted coefficient of determination is 0.92). For the wage increase rate as the explained variable, we used the Japanese Trade Union Confederation's actual data since 1989 and the Ministry of Health, Labour and Welfare's "Survey on Wage Increases and Other Conditions" through 1988. The wage increase rate for 2023 is based on the results of the Japanese Trade Union Confederation's most recent survey.

2) The left axis of the chart on the right shows the percentage of workers among the users of the job change support service (Recruit Agent) whose wages increased by 10% or more from their previous job when they changed jobs during the period April-June 2015. Job opening-to-application ratio for changing jobs on the right axis shows the number of mid-career job openings per one registered member on the doda (Persol Career) website from January 2019. The effective job opening-to-application ratio for regular employees is seasonally adjusted.

Risk factors from a global perspective: possibility that US may be entering serious recession remains a cautionary point

The main risk factor for Japan's economy is the situation overseas. Specifically, this includes the possibility that the US may be entering a serious recession, further tensions in Ukraine, and a significant adjustment in China's real estate market.

In particular, we need to pay attention to the near-term economic trends in the US. Chart 6 shows the (results of model calculation) of the impact on real GDP growth in each country and region, assuming a scenario in which the US experiences a strong credit contraction or a serious banking crisis due to prolonged monetary tightening or other factors.

If Risk Scenario (1) emerges, in which the lending policy of US banks is prolonged at the current level, the real GDP growth rate of the US will decline by 1.8% pt. Applied to the outlook for the 2024 growth rate, which means that the main scenario of +0.8% y/y will fall to -1.0% y/y. The impact on Japan's real GDP growth rate is also significant at -1.1% pt, and real GDP growth will decline from +1.4% y/y to +0.3% y/y. Furthermore, if Risk Scenario (2) emerges, in which US banks' lending attitudes become as severe as they were during the global financial crisis of 2008, the real GDP growth rates of Japan, the US, and Europe will all fall into significant negative growth.

Although Japan is in an environment where economic recovery is more likely to continue than in Europe and the US, we continue to be wary of a significant deterioration in overseas economies, particularly the US.

Influence on Real GDP Growth Rates Worldwide if US Economic Risk Scenario Emerges **Chart 6**

(%pt)

	Global Economy	Japan	US	China	Eurozone	Emerging Nations (Excluding China)
Risk Scenario Ⅰ ⇒Lending attitude of US banks prolonged at the current level	▲ 1.5	▲ 1.1	▲ 1.8	▲ 0.9	▲ 1.3	▲ 1.7
Risk Scenario Ⅱ ⇒US banks' lending attitudes become as severe as they were during the global financial crisis of 2008	▲ 4.0	▲ 3.0	▲ 5.0	▲ 2.3	▲ 3.6	▲ 4.5

Source: IMF, Haver Analytics; compiled by DIR.
Note: Estimates based on model calculation. See Chapter 5 of the DIR report dated 23 May 2023, *"Japan's Economic Outlook No. 217"* for details.

2. Outlook for Prices and Monetary Policy

Core CPI growth rate seen at +1.7% y/y in FY2024

The CPI, all items less fresh food (core CPI) is expected to increase by +2.4% y/y in FY2023, and +1.7% in FY2024, assuming the latest resource prices and exchange rates (Chart 7). The CPI, all items less fresh food and energy is expected to increase by around +1.5% in the Jan-Mar period of 2025, the last period included in this report's forecast range.

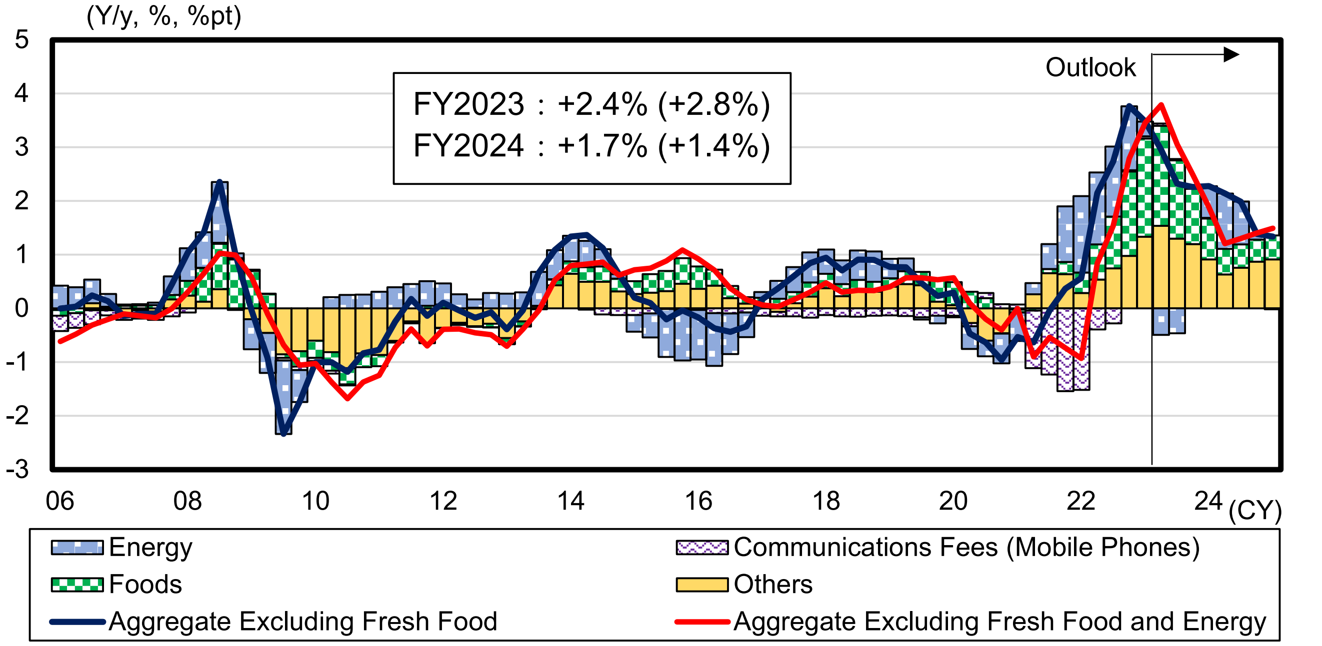
Price hikes in food and beverages, an especially broad category of components, are continuing to be carried out. According to the Teikoku Databank survey on price revision trends, the number of products for which there are plans to implement price increases in 2023 is expected to exceed 20,000 as of the end of April[6]. The rate of increase in price per time is also sustaining at a higher rate than in 2022.

Regarding energy, the seven major electric power companies, including Tokyo Electric Power Company, have announced price increases for regulated electricity rates for households effective June 1 (reflected in the CPI for July). The price increase for a standard household will be up to about 40%, although the increase has been reduced from the initial application, and will be a factor pushing up prices.

On the other hand, the government's additional price hike countermeasures include a "recommended business menu" to support consumers and businesses affected by high prices, including a reduction in the burden of LP gas rates. These policies are expected to push prices down to a certain degree in the future.

[6] For details, see Teikoku Databank, "Survey of Price Revision Trends of 195 Major Food Companies - May 2023" (April 28, 2023, Japanese only).

Outlook for CPI (Excluding Fresh Food for All Years – Figures in Parenthesis Exclude Both Fresh Food and Energy) **Chart 7**



Source: Ministry of Internal Affairs and Communications; compiled by DIR.
Note: Price outlook assuming resource prices and exchange rates at the time the chart was produced. Assumes that Nationwide Travel Support will be implemented from October 2022 through the end of June 2023, excluding the year-end, New Year holidays and long holidays, and that high energy price measures will be implemented through the end of September 2023 (energy bills for February-October will be reduced). The unit price of the Renewable energy power generation promotion levy in FY2023 is 1.40 yen/kwh.

Outlook for prices revised upwards due to more aggressive pricing behavior by corporations

With significant wage hikes expected in the spring wage negotiations, companies have recently become more aggressive in their pricing behavior, and wages and prices have begun to rise in a cyclical manner. Compared to the rapidly declining import price inflation rate, the decline in the core CPI growth rate will be smaller.

Corporate inflation expectations also appear to be rising. The BOJ Tankan five-year price outlook (enterprises of all sizes and all industries) rose to +2.0% y/y in September 2022 (+2.1% y/y in March 2023). This is the first time since March 2014, when the survey began, that it has reached 2%. In addition, prices of items with infrequent price revisions (sticky price items), which are closely related to firms' inflation expectations, have risen sharply since mid-2022[7]. Based on an analysis by the US Federal Reserve Bank of Atlanta, we estimate that the price growth rate of sticky price items in Japan rose to +2.8% in April 2023, the highest level in nearly 30 years[8].

In response to these changes in the environment surrounding prices, the price outlook has been raised from the previous forecast. The CPI inflation rate on an aggregate basis, excluding fresh food and energy, has been revised upward by 1.2% pt y/y in FY2023 and by 0.6% pt y/y in FY2024.

BOJ expected to continue current monetary easing policy framework for the time being

At the April 2023 Monetary Policy Meeting, the BOJ decided to maintain monetary easing through yield curve control (YCC), along with a review of its monetary policy operations to date.

[7] Since firms that provide goods and services with infrequent price revisions (sticky price items) set optimal prices by taking into account expected price changes until the next price revision, rising inflation expectations will encourage these firms to increase the scope of price increases. The relationship between price stickiness and expected inflation is demonstrated in the Calvo sticky price model.
[8] See Chapter 4 of our previous outlook for details on how sticky price item prices are estimated.

Based on our price outlook assumptions (Chart 7, above), underlying inflation will not reach 2% over the forecast period. Therefore, in our main scenario, we expect the current framework of monetary easing measures to remain in place, and the BOJ is unlikely to move to significantly revise its policy, including eliminating the YCC, until it releases the results of its review, which will take about one to one and a half years to complete.

However, if the BOJ determines that the underlying inflation rate will increase toward 2%, accompanied by higher wages, when the downside risks to the US economy and the results of the 2024 spring wage negotiations become known to some extent, it may decide to release the review and eliminate the YCC as early as at the April 2024 Monetary Policy Meeting.

Japan's Economic Outlook No. 217 (May 23, 2023) **Chart 8**

		2022			2023				2024				2025	FY2022 (CY)	FY2023 (CY)	FY2024 (CY)
		Apr-Jun	Jul-Sep	Oct-Dec	Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec	Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec	Jan-Mar			
Real GDP	Y tril; annualized	548.3	546.9	546.8	549.0	551.9	554.8	557.3	559.2	560.5	561.8	563.1	564.5	547.7	555.7	562.4
	Q/q %	1.1	-0.2	-0.0	0.4	0.5	0.5	0.5	0.3	0.2	0.2	0.2	0.2			
	Q/q %; annualized	4.7	-1.0	-0.1	1.6	2.2	2.1	1.8	1.3	1.0	0.9	0.9	1.0			
	Y/y %	1.8	1.6	0.4	1.3	0.5	1.5	1.9	1.9	1.6	1.3	1.0	1.0	1.2	1.5	1.2
														(1.0)	(1.3)	(1.4)
Private Consumption	Q/q %	1.7	0.0	0.2	0.6	0.5	0.5	0.4	0.2	0.2	0.2	0.2	0.2	2.4	1.7	0.8
Private Residential Investment	Q/q %	-1.8	-0.5	0.2	0.2	0.4	0.6	0.6	0.0	-0.2	-0.2	-0.2	-0.2	-4.4	1.3	-0.1
Private Non-Resi. Investment	Q/q %	2.1	1.5	-0.7	0.9	0.9	0.8	0.8	0.7	0.5	0.5	0.5	0.5	3.0	2.8	2.4
Government Consumption	Q/q %	0.7	0.0	0.2	-0.0	-0.5	-1.3	-0.9	0.2	0.2	0.2	0.2	0.2	1.1	-1.8	-0.3
Public investment	Q/q %	0.6	1.1	0.2	2.4	0.7	0.6	0.4	0.3	0.3	0.3	0.3	0.3	-2.6	3.6	1.3
Exports	Q/q %	1.5	2.5	2.0	-4.2	1.2	1.9	1.3	0.8	0.4	0.4	0.4	0.5	4.4	2.0	2.8
Imports	Q/q %	1.0	5.6	-0.0	-2.3	0.5	0.6	0.6	0.4	0.3	0.2	0.2	0.3	7.1	0.9	1.3
Nominal GDP	Q/q %; annualized	4.3	-3.1	4.3	7.1	5.2	2.8	2.9	3.4	1.9	1.2	1.2	1.4	1.9	4.0	2.1
GDP deflator	Y/y	-0.3	-0.4	1.2	2.0	2.8	3.3	2.5	1.5	1.1	1.1	0.9	0.6	0.7	2.5	0.9
Industrial production	Q/q	-2.7	5.9	-3.0	-1.8	4.6	1.9	0.6	-0.2	-0.0	0.2	0.3	0.3	-0.2	4.8	1.0
Core CPI	Y/y	2.1	2.7	3.8	3.5	3.0	2.3	2.3	2.3	2.1	2.0	1.4	1.3	3.0	2.4	1.7
Unemployment rate	%	2.6	2.6	2.5	2.6	2.6	2.6	2.5	2.5	2.5	2.4	2.4	2.4	2.6	2.5	2.4
Trade balance (goods, services)	Y tril; annualized	-14.8	-22.3	-20.6	-15.0	-12.7	-11.3	-10.9	-10.1	-10.1	-10.0	-9.9	-9.6	-18.1	-11.2	-9.8
Current account balance	Y tril; annualized	12.8	4.1	9.9	10.2	17.2	19.7	20.5	21.1	21.9	22.2	22.6	23.2	9.2	19.6	22.4
Major assumptions																
Crude oil price (WTI futures)	$/bbl	108.5	91.4	82.6	76.0	74.1	71.9	71.9	71.9	71.9	71.9	71.9	71.9	89.6	72.4	71.9
Exchange rate	Yen/$	129.6	138.4	141.4	132.3	136.6	138.7	138.7	138.7	138.7	138.7	138.7	138.7	135.4	138.2	138.7

Source: Compiled by DIR.

Note: GDP through Jan-Mar 2023: actual; thereafter: DIR estimates.