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Japan's Medium-term Economic Outlook (January 2021) (Summary)

Coronavirus Crisis Transforms Global Economy while Encouraging Environment-Friendly Industries

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Summary

- We revised our medium-term outlook for Japan's economy for the first time in approximately one year. In this report, we survey the global economy and Japan's economy and fiscal situation over the next ten years (2021-30), looking ahead to the post-corona era when the COVID-19 is no longer a threat to humankind. Furthermore, we will examine the economic significance and issues surrounding the goal to reach zero greenhouse gas emissions that Japan, the United States, Europe, and China are aiming for.
- We expect the growth rate of the global economy over the next 10 years to be at an average annualized rate of 3.5% assuming that the COVID-19 vaccine is disseminated between the middle of 2021 and 2023. In the first half of the forecast period, the economy is expected to exhibit growth on the high side at +3.9% due to the rebound from the downturn caused by the coronavirus crisis, while in addition, fiscal and monetary policy, as well as the relaxation of US-China trade friction, will also play a supporting role. In the latter half of the period the growth rate is expected to return to 3.1%, about the level of the potential growth rate, with fiscal consolidation and the normalization of monetary policy.
- Over the next ten years Japan's real GDP growth rate is expected to be at an average annualized rate of 1.4%. As is the case of the global economic outlook, the first half of the forecast period is expected to be on the high side at +1.8%. Then during the second half it is expected to decline to 1.0% due to the suspension of monetary easing and the acceleration of Japan's population decline. The effects of the coronavirus crisis on the potential growth rate are expected to be limited, with growth in investment especially promising in the areas of digitalization expected to speed up in the future, and environmentally friendly industries. At the

same time, the fiscal situation is expected to see a major deterioration due to the rapid growth experienced in the expense of responding to the coronavirus crisis. The primary balance (PB) in FY2025 will be -3.5% as a proportion of GDP, and it will be extremely difficult to achieve the fiscal consolidation target.

- The acceleration in global efforts towards becoming more environmentally friendly is not a temporary or short-term phenomenon. In fact, it should bring about fundamental structural changes in the mid to long-term. The "Green Growth Strategy" compiled in December 2020 is estimated to boost Japan's real GDP level by about 1.2% over the next 30 years. On the other hand, in the mid to long-term the marginal cost of reducing CO2 emissions is expected to grow, and hence there is a risk that the virtuous circle of the economy and the environment will cease to function. Carbon pricing, which the government will resume considering, will impact various industries differently, hence it will be necessary to keep abreast of the various arguments surrounding this question in the future.

Forecast Tables (as of Jan 2021)

(FY)	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030
Real GDP (Y/y %)	1.7	0.8	1.8	0.3	-0.3	-5.5	3.2	2.7	1.5	0.8	0.8	0.9	1.1	1.0	0.9	0.9
Private final consumption	0.7	-0.3	1.0	0.2	-0.9	-6.7	2.4	3.1	2.2	0.7	0.7	0.7	0.8	0.7	0.8	0.7
Private housing investment	3.1	4.3	-1.8	-4.9	2.5	-7.0	0.4	-0.9	-2.3	-1.6	-1.5	-1.7	-1.5	-0.3	-0.5	-1.2
Private capital investment	3.4	0.8	2.8	1.0	-0.6	-8.0	2.6	3.2	2.3	1.7	1.6	1.7	1.7	1.7	1.4	1.1
Government final consumption	2.2	0.9	0.3	1.1	2.0	2.5	1.5	1.4	0.7	0.9	0.9	0.9	1.0	0.9	1.0	1.1
Public fixed capital formation	-1.3	0.5	0.6	0.8	1.5	3.3	1.0	2.0	1.8	2.1	2.1	1.6	1.3	0.9	1.0	1.0
Export of goods and services	1.1	3.4	6.3	2.1	-2.6	-12.9	9.8	4.9	1.9	2.1	2.3	2.7	4.0	3.0	2.7	2.7
Import of goods and services	0.4	-0.5	3.8	2.8	-1.2	-7.0	2.5	3.6	4.1	1.9	2.1	2.5	3.2	2.8	2.5	2.4
Index of Industrial Production (Y/y %)	-0.8	0.8	2.9	0.2	-3.7	-10.0	6.7	3.5	1.8	1.0	1.1	1.2	1.4	1.3	1.2	1.1
Consumer Price Index (Y/y %)	0.2	0.0	0.7	0.7	0.6	-0.6	-0.1	0.1	0.8	0.9	0.9	0.8	0.8	0.9	0.9	1.0
O/N call rate (%)	0.1	0.0	0.0	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.1	0.3	0.5
Yield on 10-yr JGBs (%)	0.3	0.0	0.1	0.1	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.6	1.1	1.7
Y/\$	120.1	108.3	110.8	110.9	108.7	105.6	104.0	102.2	101.0	101.0	100.7	100.7	100.9	99.5	98.0	94.3
Y/EUR	132.5	118.8	129.7	128.4	120.8	123.4	126.0	126.6	127.2	128.0	128.7	128.4	128.2	126.8	125.5	121.1
No. employed (Y/y %)	0.5	1.0	1.4	1.7	0.8	-0.9	0.7	0.0	0.1	0.0	0.0	-0.2	-0.2	-0.3	-0.3	-0.4
Unemployment rate (%)	3.3	3.0	2.7	2.4	2.3	3.0	2.9	2.9	2.8	2.8	2.7	2.7	2.7	2.7	2.6	2.6
Household savings rate (%)	0.1	1.3	0.8	1.2	3.2	12.7	8.0	5.5	4.0	3.7	3.2	3.0	2.6	2.7	3.0	3.4
Central & local government																
Fiscal balance (% of nominal GDP)	-4.4	-4.3	-3.5	-3.1	-3.8	-16.0	-6.4	-5.5	-4.7	-4.6	-4.5	-4.2	-4.0	-3.9	-4.0	-4.3
Primary balance (% of nominal GDP)	-2.9	-2.9	-2.2	-1.9	-2.7	-14.8	-5.3	-4.4	-3.7	-3.6	-3.5	-3.2	-3.1	-3.0	-3.1	-3.3
Debt (% of nominal GDP)	182.9	185.7	186.1	189.2	190.0	215.3	215.0	214.9	215.5	217.3	218.7	219.7	220.1	220.3	220.7	221.3

Assumptions

World economic growth (PPP; Y/y %; CY)	3.4	3.3	3.8	3.5	2.8	-3.9	5.0	4.3	3.6	3.4	3.2	3.0	3.4	3.2	3.0	3.0
US (Y/y %; CY)	3.1	1.7	2.3	3.0	2.2	-3.7	3.6	3.3	2.2	2.1	1.9	1.5	2.0	1.9	1.8	1.7
Euro zone (Y/y %; CY)	1.9	1.8	2.7	1.9	1.3	-7.3	4.2	3.5	2.0	1.7	1.4	1.0	1.1	1.3	1.1	1.1
China (Y/y %; CY)	7.0	6.8	6.9	6.7	6.0	2.3	8.0	6.0	5.5	5.3	5.2	5.1	5.4	5.0	4.9	4.8
Oil price (WTI; \$/bbl)	45.0	47.9	53.7	62.8	54.9	41.0	49.0	50.0	55.0	59.0	62.0	64.0	69.0	72.0	75.0	77.0
Population (Y/y %)	-0.3	-0.1	0.0	-0.2	-0.2	-0.3	-0.4	-0.4	-0.4	-0.5	-0.5	-0.5	-0.5	-0.6	-0.6	-0.6

Source: Compiled by DIR.

Notes: 1) Through FY19: actual.

2) Fiscal balance: excl. the expenditures and the fiscal resources for the recovery and reconstruction measures.