

For Immediate Release

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**Issuance of the FY2017 - 2020 “Japanese Economy Outlook”
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- Japanese Economy Outlook: Positive output gap is not the goal, more stimulus will be required to achieve the price stability: (Summary) -

Highlights:

- Nominal GDP growth rate for second quarter of 2017 is above 4% (annualized rate), nominal GDP growth rate became larger than real GDP one.
- But the real consumption is still below theoretical amount based on income and wealth effect by 2 trillion yen. There are some market participants who advocate the reverse of expansionary macroeconomic policy. However it is too early to do so because the Japan's inflation rate is still far below from 2% target.
- Non-traditional monetary policy tends to let yield curve flatter, but the expansionary monetary policy may contribute to the higher GDP and asset prices. Corporation is likely to be financial deficit once price target will be achieved.
- We believe that expansionary macroeconomic policy is still essential for Japanese economy. In order to achieve 2% inflation target, the government may need to take expansionary fiscal policy and postpone and/or freeze of consumption tax hike scheduled in Oct, 2019.

1. 2017-Q2 GDP expanded due to accommodative fiscal and monetary policy, but the consumption is still weak compared with its theoretical amount

Japan's 2017-Q2 GDP data draw attention because the nominal GDP grew at 1.1% (4.6% on annualized rate) from previous quarter, it was above real GDP growth rate. Real consumption grew at 0.9% from previous quarter, but its amount is still below than theoretical amount based on income and wealth effect by 2 trillion yen. We still believe that consumption is weak and it is too early to implement consumption tax hike.

2. Output improvement is not enough to increase prices, corporate and household are still in financial surplus

The positive output gap may improve further, inflation and expected inflation is staying about 0.5%, still far from the 2% price target. The general government's deficit improved rapidly. Corporations and households are still reluctant to increase fixed investment and consumption. The pace of government fiscal re-balancing may be too fast. This suggests that the government should increase fiscal expenditure.

3. Accommodative monetary policy with inflation targeting may support real economy

Some economists imply that the expansionary monetary policy with aggressive stance is likely to improve real economy and asset price market. The lending by financial sector is hard to increase because the corporations are financial surplus. If the current solid economy will continue, then the corporations will turn to be financial deficit and the lending is likely to increase. The difficulties of price increase are common among Japan, the US and Europe, still the corporations in overseas are not necessary financial surplus.

4. Future Outlook to FY2020: Upward revision in growth outlook and downward revision in prices

We extend our economic and price outlook to FY2020. We upward revise in growth outlook and downward revise in price outlook. Positive output gap is likely to improve further but it is unlikely to warrant price stability. Current low interest rates may provide good opportunity for government and the central bank to implement policy mix, further accommodative monetary and fiscal policy.

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