

【NEWS RELEASE】

February 18, 2022
SMBC Nikko Securities Inc.

Quarterly Economic Outlook for FY2021-2022

February 18, 2022(JST), “SMBC NIKKO Japan Economic Outlook for FY2021-2022” has been released, responding to the first preliminary of GDP (October-December 2021 period)

Bumpy Road to Normal, But Getting There

- ◆ Real GDP: FY21 +2.4%, FY22 +3.2%
- ◆ Nominal GDP: FY21 +1.7%, FY22 +4.9%

Summary• **GDP growth outlook**

We revise our economic outlook in light of the first preliminary Oct-Dec 2021 GDP data. We forecast real GDP growth of +2.4% YoY in FY21 and +3.2% in FY22. We lower our FY22 forecast by 0.8ppt from our previous forecast (8 December). We cut our forecast for public investment to reflect lower consumption amid quasi-lockdown measures in Jan-Mar. We still expect economic growth to pick up in FY22.

- **Interest rate forecasts**

Real GDP growth in Oct-Dec was +5.4% QoQ annualized, recovering from -2.7% in Jul-Sep. This reflects the lifting of economic restrictions and easing of supply constraints. The Japanese economy has been stop-and-go due to CV19 variants.

CV19 infections: The number of new positive cases has peaked. That said, a seventh wave of infections is expected, so we think the government needs to deploy booster shots quickly. Booster vaccinations are highly effective in preventing hospitalization, at around 90%, so we expect risk of medical collapse to diminish, and we also anticipate fewer reasons for economic restrictions. In addition, Covid-19 is classified as a type-II infectious disease, the same as SARS, which had a fatality rate of 10-15%. Meanwhile the fatality rate for Omicron is only around 0.2%, nearly the same as type-V influenza (around 0.1%). If Covid-19 can be treated in general hospitals as with influenza, this should spur the economy to normalize.

Private consumption: Disposable incomes and consumer sentiment have already recovered to pre-CV19 levels, and excess savings among households have reached Y45tn. One-off and recurring purchasing power is sufficient and there is major potential for a recovery. We expect gradual normalization in light of weaker virulence, booster shots, potential changes in infectious disease classification, ample household purchasing power, and economic policy measures.

Inflation/inflation: We expect core CPI to reach around +1.7% in April due to higher global resource prices and yen depreciation. We forecast average growth of around +1.2% in FY22. We expect real incomes to decline by around Y3.4tn, but with wage growth and benefits likely to boost incomes by Y7.6tn and excess savings of Y45tn, we think consumption is unlikely to fall short.

In addition, the BOJ is likely to curb rises in long-term and real interest rates if inflation is around +0.5% at present. This could encourage yen depreciation, causing the Y/\$ rate to weaken to around Y120/\$.

- **US inflation and rate hikes**

Inflation is up in the US for the first time in 40 years. We see two possible mismatches behind this: 1) labor supply-demand, and 2) energy policy. If there are mismatches, it will take time to resolve them, and it could take longer for inflation to abate.

The Fed's rate hike projection to 2.5% looks reasonable based on the natural real yield and savings rate. The Fed does not expect rate hikes to send the economy into recession. It is aiming for a soft landing - a sustainable economy (potential GDP) with full employment and average inflation at 2%.

In terms of potential GDP, the real growth rate is around 2% and the nominal growth rate is around 4%, so economic growth should be stable. A nominal GDP growth rate of 4% would boost S&500 EPS by around 15%, prompting a rise in share prices.

Risks include a pickup in inflation due to stronger-than-expected crude oil prices and more rate hikes.

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Quarterly forecasts for Japanese economy

	《Actual》→《Forecasts》												《A》→《F》 (Unit:%)			Comparison with previous forecasts (as at 8 Dec 2021)			
	2020				2021				2022				2023	FY20	FY21	FY22	FY21	FY22	
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q						
Real GDP growth (QoQ)	0.4	-7.9	5.3	1.8	-0.5	0.6	-0.7	1.3	-0.4	2.1	0.7	0.5	0.5						
(annual rate)	1.8	-28.2	23.0	7.5	-2.1	2.4	-2.7	5.4	-1.5	8.5	2.9	2.1	2.1	-4.5	2.4	3.2	0.0	-0.8	
Domestic demand, contribution (QoQ)	0.6	-5.2	2.7	1.1	-0.4	0.7	-0.8	1.1	-0.5	2.0	0.8	0.6	0.6	-3.9	2.3	3.2	-0.2	-0.8	
Private consumption (QoQ)	0.8	-8.6	5.3	1.6	-0.8	0.7	-0.9	2.7	-1.6	3.0	0.7	0.5	0.5	-5.4	2.4	3.8	0.3	-0.7	
Capex (QoQ)	-4.9	-0.1	-4.7	-0.1	0.9	1.0	-1.6	-0.9	-0.5	0.0	0.0	0.2	0.2	-7.8	-1.3	-1.1	-0.1	-0.9	
Residential investment (QoQ)	2.7	-6.9	-0.4	1.2	0.4	2.0	-2.4	0.4	1.0	1.5	1.0	1.0	1.0	-7.5	1.4	3.4	-0.7	-0.4	
Public investment (QoQ)	-1.0	3.8	1.0	2.0	-1.6	-3.3	-3.0	-3.3	-1.0	-0.3	1.5	0.8	0.8	5.2	-7.3	-1.8	-3.2	-3.0	
Foreign demand, contribution (QoQ)	-0.2	-2.7	2.6	0.8	-0.1	-0.1	0.1	0.2	0.2	0.0	-0.1	-0.1	-0.1	-0.6	0.1	0.0	0.1	0.0	
Exports (QoQ)	-4.6	-17.8	8.7	10.7	2.2	3.1	-0.3	1.0	2.0	1.5	1.0	0.5	0.5	-10.5	13.0	4.6	1.3	0.0	
Imports (QoQ)	-3.6	-1.6	-7.0	5.5	3.0	3.8	-0.9	-0.3	1.0	1.5	1.5	0.8	0.8	-6.7	6.3	3.6	-0.8	-0.3	
Nominal GDP growth (QoQ)	0.7	-7.4	5.1	1.3	-0.4	0.2	-1.0	0.5	2.0	2.2	0.9	0.7	0.7	-3.9	1.7	4.9	-0.6	-0.2	
Industrial production (YoY)	-4.7	-20.7	-12.7	-4.2	-1.5	19.9	5.9	1.2	2.3	4.2	10.4	11.4	8.8	-9.9	6.9	8.7	1.6	1.7	
Trade balance (Y tn, SAAR)	1.2	-10.1	3.0	8.0	3.7	-0.4	-3.7	-5.3	-5.6	-5.8	-6.6	-7.1	-7.6	1.1	-3.8	-6.8	-0.6	-2.8	
Unemployment rate (%)	2.4	2.7	3.0	3.0	2.8	2.9	2.8	2.7	2.7	2.6	2.6	2.5	2.5	2.9	2.8	2.6	0.0	0.1	
Core CPI (YoY)	0.7	0.2	-0.3	-0.9	-0.5	-0.9	0.0	0.4	0.5	1.6	1.5	1.0	0.6	-0.5	-0.0	1.2	-0.6	-0.2	
(Ex effects of consumption tax hike)	-0.3	-0.8	-1.3	-0.9	-0.5	-0.9	0.0	0.4	0.5	1.6	1.5	1.0	0.6	-1.0	-0.0	1.2	-0.6	-0.2	
IOER (Eop)	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	0.0	0.0	
YCC 10y JGB yields target (Eop)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
US real GDP growth (QoQ annualized)	-5.1	-31.2	33.8	4.5	6.3	6.7	2.3	6.9	1.7	3.8	3.0	2.5	2.4	-3.4	5.7	3.6	0.1	-0.7	
US unemployment rate (%)	3.8	13.0	8.8	6.8	6.2	5.9	5.1	4.2	4.1	4.0	3.8	3.8	3.8	8.1	5.4	3.9	0.0	-0.2	
US core CPI (YoY)	2.2	1.3	1.7	1.6	1.4	3.7	4.1	5.0	4.4	4.2	4.0	3.8	3.5	1.7	3.6	4.1	0.1	-0.1	
Fed rate (Eop)	0.125	0.125	0.125	0.125	0.125	0.125	0.125	0.125	0.375	0.875	1.125	1.375	1.625	0.125	0.125	1.375	0.00	1.00	

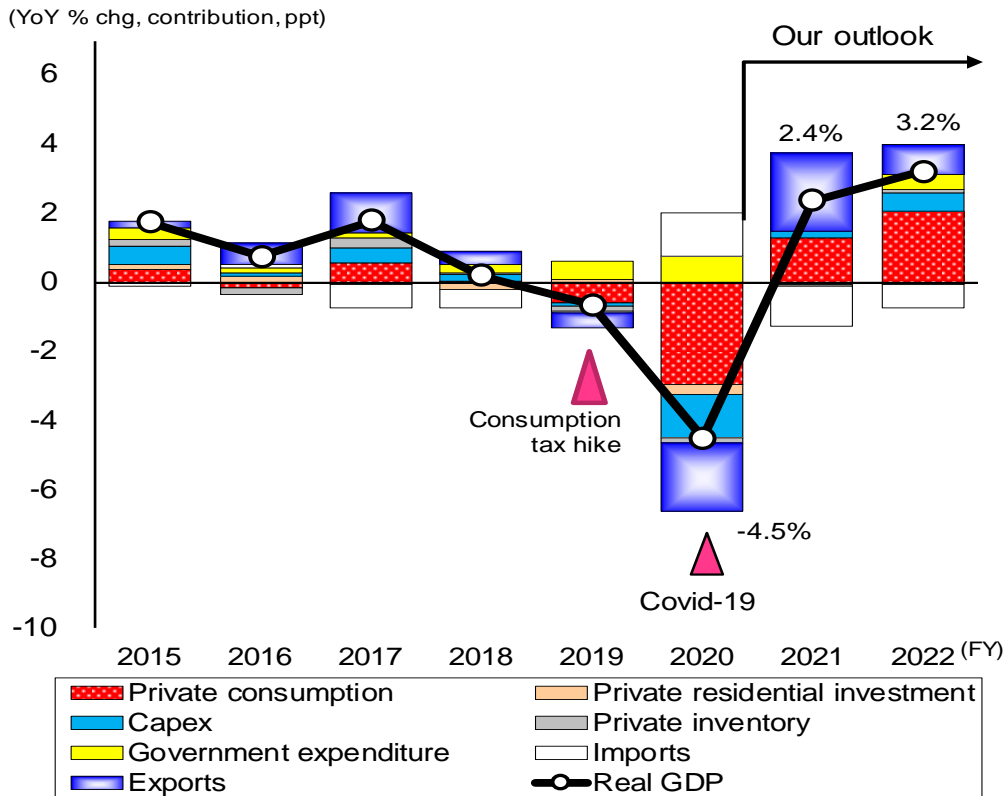
Assumptions: Forex rate (annual mean): Y112/\$ in FY21 and Y120/\$ in FY22.

Crude oil price (WTI annual mean): \$72.6/bbl in FY21 and \$97.5/bbl in FY22.

Notes: US GDP on a calendar basis, US unemployment rate is the average for the period, FF rate is at end of year.

Sources: Cabinet Office, Ministry of Internal Affairs and Communications, Ministry of Economy, Trade and Industry, and Bank of Japan, SMBC NIKKO estimates

Outlook for real GDP growth



Sources: Cabinet Office, SMBC NIKKO estimates

APPENDIX

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