

JAPAN

8

A LAGGING ECONOMIC RECOVERY

The Covid-19 pandemic did not hit the Japanese economy as hard as the other advanced countries. In 2020, GDP growth did not contract as much as in other places. Yet a slow vaccination rollout and the lack of confidence of economic agents are straining the momentum of Japan's recovery. After a strong performance in late 2020, the Japanese economy is lagging somewhat compared to the United States and Europe. Consumer confidence – a key ingredient for a robust economic recovery – is still low compared to pre-crisis levels. This atmosphere is dragging down private consumption and the dynamics of the tradeable services sector as well. The services industry is having a hard time swinging back into growth. In this persistently tough environment, inflation will continue to hold near 0%, far from the central bank's 2% target. Monetary policy will remain accommodating and unchanged in 2021 and 2022, even though the Bank of Japan might allow long-term sovereign rates to rise to the upper range of 0.25%.

A TIMID REBOUND

After reporting a relatively strong performance in Q4 2020 compared to the other advanced economies, Japan experienced a difficult H1 2021. Japanese GDP contracted by 1% in Q1 2021, and could decline slightly again in Q2. A real but timid rebound is expected as of Q3. Starting in 2022, the Japanese economy is expected to slow sharply as growth converges towards its potential, which is structurally low. All in all, full-year Japanese GDP is estimated at 2.2% in 2021, after contracting 4.7% in 2020, and then will accelerate to 3.3% in 2022. Japan, like the Eurozone, is expected to return to its pre-crisis levels in Q4 2021. In 2022, Japan will lag behind the other advanced countries (see chart 2). The main reason for Japan's current troubles is the slow pace of its vaccination campaign. Even though it has accelerated in recent weeks, the vaccination coverage rate is still low: about 20% of the population has received a first dose, compared to nearly 50% in the European Union. This lag is draining consumer confidence. After bottoming out in spring 2020, consumer confidence rebounded but still falls short of pre-pandemic levels. Moreover, it declined again in May. The Japanese are starting to worry about the opening of the Olympic Games in July as well. These factors do not augur well for a strong rebound in private consumption, which already declined in Q1 2021. The corporate situation is also tough. Although corporate investment is beginning to pick up, it is still relatively low compared to pre-crisis levels, and the most recent economic statistics are sending very mixed signals. Since the outbreak of the Covid-19 crisis, the purchasing managers index (PMI) for tradeable services has failed to rise above the 50 threshold, which separates economic expansion from contraction. In the manufacturing sector, there has been a net improvement in the economic situation, although manufacturing PMI declined in June to 51.5, from 53 in May. The Tankan index for Q2 2021 could improve but will remain deteriorated.

With inflation holding close to 0% despite the recovery, the Bank of Japan will continue to support the economy in 2021 and 2022. Recently, however, it did begin to cutback ETF-type securities purchases. The BOJ could reactivate these operations if market conditions were to deteriorate sharply.

Completed on 28 June 2021

Louis Boisset

louis.boisset@bnpparibas.com

GROWTH AND INFLATION (%)

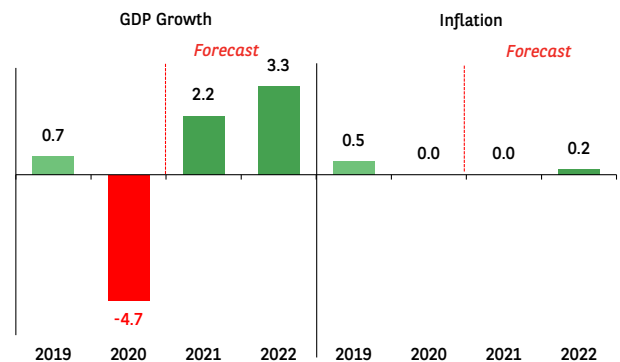


CHART 1

SOURCE: BNP PARIBAS GLOBAL MARKETS

GDP IN JAPAN, THE UNITED STATES AND THE EUROZONE (100= Q4 2019)

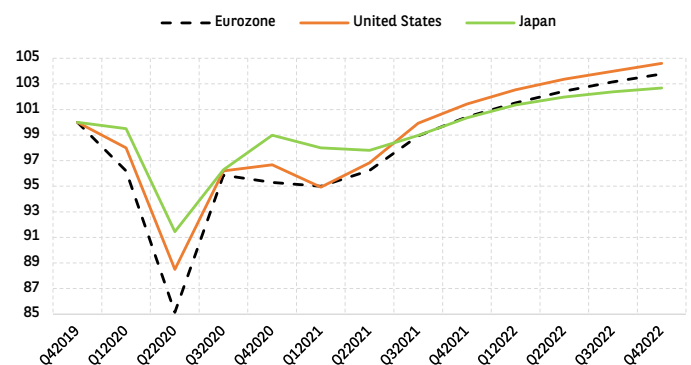


CHART 2

SOURCE: EUROSTAT, BNP PARIBAS GLOBAL MARKETS



BNP PARIBAS

The bank
for a changing
world