

A recovery is expected in both the semiconductor cycle and in Japanese exports

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1. The Real Economy

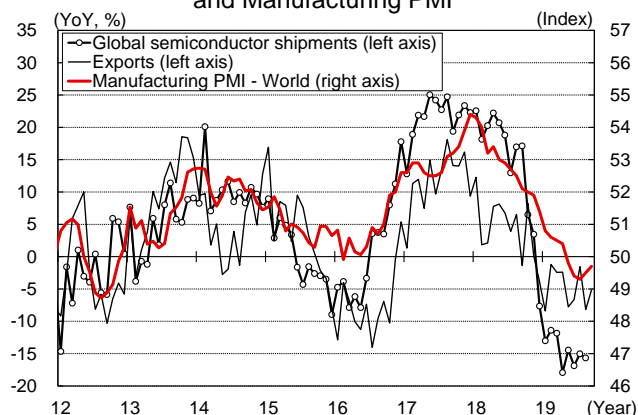
Japanese exports are showing some weakness as the global economy appears to be slowing further. Nevertheless, growth of Japanese exports is expected to stop falling in the future due to signs of a recovery in the global manufacturing and semiconductor sectors.

The manufacturing sector in Japan is deeply embedded in the global supply chain, so Japanese exports generally move with changes in global manufacturing (Chart 1). In around July this year, it seems global manufacturing PMI bottomed out for now, indicating the possibility that global production activities will start to recover. When it comes to answering the question of if the manufacturing sector will continue to recover worldwide into next year as it has been doing, the fact that the amount of global semiconductor shipments has stopped falling is significant as semiconductors form the initial stage of a wide range of industries. Following the prolonged boom, which started during the latter half of 2016 and continued into 2017, there was a long period of cyclical negative growth which has now unequivocally ended. This can be seen in the positive movements in Taiwan's electronic parts and components industry, which holds the position of the world's larger producer of semiconductors. There is large growth in fixed asset purchases, which precede production and shipments. This positive result indicates the semiconductor industry is likely to enter a phase of recovery (Chart 2). In addition, there is also a feeling that the business results and investment plans of the major corporations related to semiconductors are bottoming out. It is thought that semiconductors are being incorporated into a diverse range of machinery and equipment, such as electric household appliances, cars and production machinery, due to the digitalisation which has been taking place recently. It is possible that this can also be interpreted as preceding a recovery in the manufacturing sector as a whole.

While it is necessary to continue to remain cautious about downside risks to the global economy, such as the prolonged, escalated trade friction between the US and China, there is a possibility that Japanese exports will recover going forwards owing to the bottoming out of the global manufacturing sector, starting with the semiconductor industry. Although there are concerns at present that private consumption will soften due to the consumption tax rate hike in October, if a rise in exports – which have been weak up until now – were to occur, it would

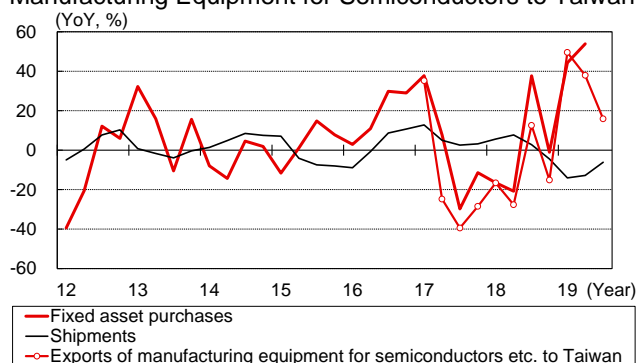
likely offer strong support to the Japanese economy as exports provide a significant contribution to overall growth.

Chart 1: Exports and Global Semiconductor Shipments and Manufacturing PMI



Source: Ministry of Finance, World Semiconductor Trade Statistics, Markit, MUFG Bank Economic Research Office

Chart 2: Fixed Asset Purchases and Shipments of Taiwan's Electronic Parts and Components, Exports of Manufacturing Equipment for Semiconductors to Taiwan



Note: Most recent shipments data is an average of July and August
Source: Taiwan Department of Statistics, Ministry of Finance, MUFG Bank Economic Research Office

2. Prices and Financial Markets

2.1 Monetary Policy

The Bank of Japan (BoJ) decided to maintain its policy rate at its monetary policy meeting in October, but it revised its forward guidance (Table 1). The Bank's view of the current situation is "although there had been no further increase in the possibility that the momentum toward achieving the price stability target would be lost, it was necessary to continue to pay close attention to the possibility". As a result, the Bank said it "expects short- and long-term interest rates to remain at their present or lower levels" and removed its mention of the period "at least through around spring 2020". Addressing this matter, Governor Kuroda stated "we made clear that our policy stance is we will carry out policies giving more consideration to the direction of easing", suggesting the continuation of long-term monetary easing and the possibility interest rates may be lowered further into negative territory in the future.

That being said, the BoJ is probably still some way off cutting interest rates further. In the attachment published alongside its statement, the Bank has factored in a temporary narrowing of the output gap within positive territory, yet it expressed that it expects the gap "to remain at around the current level on average" to discourage a rise in the market's expectations of further monetary easing, which are directly linked with the narrowing of the positive output gap in the near future. On the economic front, the scale of the impact of the national consumption tax rate hike remains within expectations and uncertainty sparked by politics and policies overseas has faded somewhat owing to a partial agreement between the US and China over trade and the UK and EU negotiators' approval of a EU withdrawal agreement bill and another extension of the Brexit deadline. Meanwhile, although the manufacturing industry remains soft, there appears to be signs of recovery within the semiconductor cycle both within and outside Japan. Furthermore, the US Federal Reserve Board (FRB) and the European Central Bank have started to insinuate they will be halting their additional monetary easing for the time being. Taking this into account, it is likely the BoJ will maintain its current easy policy for the time

being and will not decide to embark on large-scale monetary easing, such as lowering interest rates further into negative territory, provided there is no trigger, such as a large, sudden change in FX markets or the situation overseas.

2.2 Exchange Rates

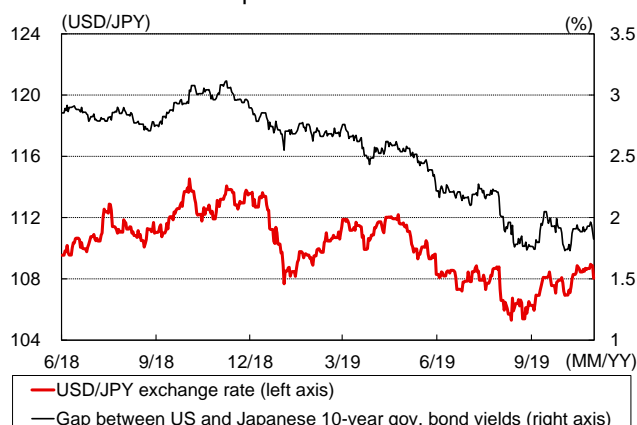
At the start of October, US interest rates rose as the excessive expectations of an interest rate cut were adjusted and the gap between US and Japanese interest rates expanded, resulting in the JPY trading at around JPY108 per USD (Chart 3). The FRB then decided to lower interest rates during its third meeting in a row, yet upward pressure on the JPY did not increase, even though there was no significant change in the BoJ's position. One of the factors behind the strong USD is the relatively robust growth of the US economy. In light of this, and the FRB's insinuation that it will stop lowering interest rates for the time being, the JPY is likely to continue to hover at its current levels and will not appreciate significantly.

Table 1: Key Points from October's Monetary Policy Meeting

Forward Guidance for Policy Rates	
Latest	The Bank expects short- and long-term interest rates to remain at their present or lower levels as long as it is necessary to pay close attention to the possibility that the momentum toward achieving the price stability target will be lost.
Previous	The Bank intends to maintain the current extremely low levels of short- and long-term interest rates for an extended period of time, at least through around spring 2020, taking into account uncertainties regarding economic activity and prices including developments in overseas economies and the effects of the scheduled consumption tax hike.
Assessment of the Momentum toward Achieving the Price Stability Target	
The output gap is likely to narrow temporarily within positive territory. However, throughout the projection period, it is expected to remain at around the current level on average with the economy continuing on an expanding trend.	
Medium- to long-term inflation expectations have been more or less unchanged on the whole, although they have shown somewhat different developments depending on indicators. As for the outlook, such expectations are likely to follow an increasing trend, with the output gap remaining positive.	

Source: Bank of Japan, MUFG Bank Economic Research Office

Chart 3: USD/JPY Exchange Rate and the Gap between US and Japanese 10-Year Gov. Bond Yields



Source: Bloomberg, MUFG Bank Economic Research Office

(Translated by Elizabeth Foster)

MAIN ECONOMIC AND FINANCIAL INDICATORS (JAPAN)

1. Main Economic Indicators

As of Nov. 1, 2019

	Fiscal	Fiscal	2018	2019		2019				
	2017	2018	4Q	1Q	2Q	MAY	JUN	JUL	AUG	SEP
Real GDP Growth Rate <% changes from previous period at SA annual rate>	1.9	0.7	1.8 (0.3)	2.2 (1.0)	1.3 (1.0)	***	***	***	***	***
Index of All Industries Activity	1.8	0.8	0.9 (1.4)	-0.5 (0.3)	0.5 (0.2)	0.4 (0.1)	-0.7 (-0.4)	0.2 (1.3)	0.0 (-0.5)	
Industrial Production Index	2.9	0.3	1.4 (1.3)	-2.5 (-1.7)	0.6 (-2.3)	2.0 (-2.1)	-3.3 (-3.8)	1.3 (0.7)	-1.2 (-4.7)	1.4 (1.1)
Production										
Shipments	2.2	0.2	1.0 (1.1)	-2.1 (-1.6)	1.0 (-2.7)	1.3 (-1.8)	-4.0 (-4.9)	2.7 (1.9)	-1.3 (-4.5)	1.3 (2.0)
Inventory	5.1	0.2	0.9 (1.7)	0.9 (0.2)	0.9 (3.0)	0.5 (1.5)	0.4 (3.0)	-0.2 (2.5)	-0.1 (2.6)	-1.6 (0.7)
Inventory/Shipments Ratio (2015=100)	101.9	105.0	105.6 [102.6]	105.9 [104.3]	106.9 [104.0]	106.4 [104.9]	109.8 [104.2]	107.5 [105.5]	110.5 [104.4]	107.9 [105.2]
Domestic Corporate Goods Price Index	2.7	2.2	0.1 (2.3)	-0.8 (0.9)	0.4 (0.6)	-0.1 (0.7)	-0.6 (-0.2)	0.0 (-0.6)	-0.3 (-0.9)	0.0 (-1.1)
Consumer Price Index(SA, total, excl.fresh foods)	0.7	0.8	0.4 (0.9)	-0.2 (0.8)	0.4 (0.8)	-0.1 (0.8)	-0.1 (0.6)	0.1 (0.6)	0.1 (0.5)	-0.1 (0.3)
Index of Capacity Utilization (2015=100)	102.7	102.5	104.7 [103.8]	100.5 [102.2]	102.4 [103.3]	103.9 [104.0]	101.2 [101.5]	102.3 [101.3]	99.3 [102.8]	
Machinery Orders(Private Demand, Excl.Electric Power and Ship building)	-0.8	2.8	-3.2 (2.0)	-3.2 (-2.5)	7.5 (4.1)	-7.8 (-3.7)	13.9 (12.5)	-6.6 (0.3)	-2.4 (-14.5)	
Manufacturing	9.2	3.8	-4.1 (-0.6)	-7.7 (-8.0)	2.5 (-8.5)	-7.4 (-10.5)	-1.7 (-7.1)	5.4 (-9.4)	-1.0 (-17.4)	
Non-manufacturing Excl.Electric Power & Ship building	-7.8	2.1	-1.9 (4.5)	-0.3 (1.8)	13.1 (15.9)	-9.0 (3.0)	30.5 (30.0)	-15.6 (10.2)	-8.0 (-12.1)	
Shipments of Capital Goods (Excl.Transport Equipment)	7.0	-0.3	1.6 (1.3)	-7.4 (-6.9)	2.5 (-6.6)	5.0 (-4.2)	-5.0 (-6.2)	0.2 (-3.2)	2.5 (-7.0)	8.6 (7.7)
Construction Orders	0.7	6.5								
Private	0.6	14.5								
Public	-5.4	-15.0								
Public Works Contracts	-4.3	1.1								
Housing Starts										
10,000 units at Annual Rate, SA	94.6	95.3	95.5	94.2	91.8	90.0	92.2	91.0	89.1	89.7
Total floor	(-2.8)	(0.7)	(0.6)	(5.1)	(-4.7)	(-8.7)	(0.3)	(-4.1)	(-7.1)	(-4.9)
Sales at Retailers	1.9	1.6								
Real Consumption Expenditures of Households over 2 persons (SA)	0.3	0.0	0.2 (1.1)	-0.2 (2.0)	0.6 (3.3)	5.5 (6.0)	-2.8 (2.7)	-0.9 (1.0)	2.4 (1.0)	
Propensity to Consume (SA, %)	71.7	69.2	68.6 [71.6]	69.8 [71.0]	67.5 [68.8]	71.6 [70.6]	64.2 [66.1]	71.5 [70.9]	70.2 [70.4]	[70.4]
Overtime Hours Worked (All Industries, 5 employees or more)	0.4	-1.7	0.0 (-2.6)	-0.7 (-2.1)	1.0 (-2.4)	1.0 (-2.9)	-0.3 (-2.7)	-0.8 (-0.9)	-1.6 (-2.0)	
Total Cash Earnings (Regular Employees Only; All Industries, 5 employees or more)	0.7	0.9								
Employment Index(Regular Employees Only;All Industries, 5 employees or more) (Change over the M/Q/Y)	99	1	-40	96	86	82	88	97	95	
Ratio of Job Offers to Applicants (SA, Times)	1.54	1.62	1.62 [1.56]	1.63 [1.59]	1.62 [1.61]	1.62 [1.61]	1.61 [1.61]	1.59 [1.62]	1.59 [1.63]	1.57 [1.63]
Unemployment Rate (SA, %)	2.7	2.4	2.4	2.4	2.4	2.4	2.3	2.2	2.2	2.4
Economy Watcher Survey (Judgment of the present condition D.I.%)	50.5	47.8	48.3 [52.3]	46.0 [49.5]	44.5 [48.7]	44.1 [47.9]	44.0 [48.8]	41.2 [47.1]	42.8 [48.7]	46.7 [48.3]
Bankruptcies (Number of cases)	8,367 (-0.2)	8,110 (-3.1)	2,070 (-1.7)	1,916 (-6.1)	2,074 (-1.6)	695 (-9.4)	734 (6.4)	802 (14.2)	678 (-2.3)	702 (13.0)

(Notes)

Unless otherwise indicated, tabulated figures and those in parentheses show % changes from previous quarter/month as applicable.

The figures in () indicate % changes from previous year.

[] show the comparable figure of the previous year.

2. Balance of Payments

As of Nov. 1, 2019

	Fiscal	Fiscal	2018	2019		2019				
	2017	2018	4Q	1Q	2Q	MAY	JUN	JUL	AUG	SEP
Customs Clearance (Exports in Yen Terms)	10.8	1.9	(1.3)	(-3.9)	(-5.6)	(-7.8)	(-6.6)	(-1.5)	(-8.2)	(-5.2)
Value	5.5	2.5	(2.8)	(1.2)	(0.7)	(1.2)	(-1.2)	(-3.1)	(-2.4)	(-2.9)
Volumes	5.0	-0.6	(-1.4)	(-5.0)	(-6.2)	(-8.9)	(-5.5)	(1.6)	(-6.0)	(-2.3)
Imports (In Yen terms)	13.7	7.2	(11.2)	(-2.0)	(-0.1)	(-1.4)	(-5.2)	(-1.1)	(-11.9)	(-1.5)
Value	8.9	5.7	(6.9)	(-0.2)	(0.0)	(-0.2)	(-2.0)	(-7.3)	(-6.2)	(-7.8)
Volumes	4.4	1.4	(4.0)	(-1.8)	(-0.1)	(-1.2)	(-3.2)	(6.7)	(-6.1)	(6.8)
Current Account (100 mil. yen)	221,749	192,434	26,018	59,541	45,676	16,501	12,549	19,999	21,577	
Goods (100 mil. yen)	45,396	6,963	-6,423	2,141	-16	-6,561	7,662	-745	509	
Services (100 mil. yen)	-4,567	-7,123	-3,066	3,561	-1,046	1,677	795	-2,299	233	
Financial Account (100 mil. yen)	206,805	212,310	27,016	88,169	65,220	31,913	38,471	9,170	16,299	
Gold & Foreign Exchange Reserves (\$1mil.)	1,268,287	1,291,813	1,270,975	1,291,813	1,322,279	1,307,975	1,322,279	1,316,452	1,331,583	1,322,581
Exchange Rate (¥/\$)	110.80	110.88	112.87	110.17	109.85	109.83	108.06	108.22	106.27	107.41

3. Financial Market Indicators

	Fiscal	Fiscal	2018	2019		2019					
	2017	2018	4Q	1Q	2Q	MAY	JUN	JUL	AUG	SEP	
Uncollateralized Overnight Call Rates	-0.050	-0.062	-0.066	-0.054	-0.060	-0.050	-0.063	-0.071	-0.046	-0.059	
			[-0.042]	[-0.048]	[-0.065]	[-0.061]	[-0.071]	[-0.070]	[-0.059]	-0.059	
Euro Yen TIBOR (3 Months)	0.065	0.062	0.050	0.037	0.049	0.049	0.049	0.049	0.009	0.009	
			[0.063]	[0.078]	[0.084]	[0.078]	[0.078]	[0.091]	[0.091]	[0.050]	
Newly Issued Japanese Government Bonds Yields (10 Years)	0.045	-0.095	-0.010	-0.095	-0.165	-0.095	-0.165	-0.160	-0.280	-0.215	
			[0.045]	[0.045]	[0.030]	[0.030]	[0.030]	[0.060]	0.110	[0.125]	
Average Contracted Interest Rates on Loans and Discounts(City Banks) (% changes from previous period)	0.817	0.751	0.759	0.751	0.749	0.753	0.749	0.747	0.746		
			(-0.016)	(-0.008)	(-0.002)	(0.002)	(-0.004)	(-0.002)	(-0.001)		
The Nikkei Stock Average (TSE 225 Issues)	21,454	21,206	20,015	21,206	21,276	20,601	21,276	21,522	20,704	21,756	
			[22,765]	[21,454]	[22,305]	[22,202]	[22,305]	[22,554]	[22,865]	[24,120]	
M2(Average)	(3.7)	(2.7)	(2.5)	(2.3)	(2.5)	(2.6)	(2.3)	(2.3)	(2.4)	(2.4)	
Broadly-defined Liquidity(Average)	(3.1)	(1.9)	(1.6)	(1.7)	(1.8)	(1.8)	(1.7)	(1.8)	(1.8)	(1.8)	
Principal Figures of Financial Institutions											
Loans and Discount (Average)	Banks & Shinkin	(2.8)	(2.2)	(2.2)	(2.3)	(2.4)	(2.6)	(2.3)	(2.3)	(2.1)	(2.0)
	Banks	(2.8)	(2.2)	(2.3)	(2.4)	(2.6)	(2.8)	(2.4)	(2.4)	(2.2)	(2.2)
	City Banks etc.	(2.0)	(1.0)	(1.2)	(1.6)	(2.4)	(2.8)	(2.3)	(2.5)	(2.1)	(2.1)
	Regional Banks	(3.6)	(4.3)	(4.3)	(4.1)	(5.1)	(4.9)	(4.6)	(4.4)	(4.3)	(4.3)
	Regional Banks II	(3.0)	(-0.4)	(-0.8)	(-0.8)	(-6.6)	(-5.6)	(-5.6)	(-5.7)	(-5.7)	(-5.7)
	Shinkin	(2.7)	(2.1)	(2.0)	(1.7)	(1.4)	(1.5)	(1.3)	(1.2)	(1.2)	(1.0)
Deposits and CDs (Average)	Total(3 Business Condition)	(4.2)	(3.4)	(3.2)	(3.1)	(2.5)	(2.6)	(2.3)	(2.1)	(2.3)	(2.5)
	City Banks	(5.9)	(4.9)	(4.6)	(4.7)	(3.5)	(3.7)	(3.1)	(2.7)	(3.1)	(3.4)
	Regional Banks	(2.5)	(2.7)	(2.6)	(2.3)	(3.4)	(3.2)	(3.1)	(3.1)	(3.1)	(3.1)
	Regional Banks II	(2.1)	(-1.3)	(-1.8)	(-2.0)	(-6.2)	(-5.2)	(-5.4)	(-5.4)	(-5.4)	(-5.5)

(Notes)

Newly Issued Japanese Government Bonds Yields and Interest rates are averages. The Nikkei Stock Average is as of month-end. Unless otherwise indicated, tabulated figures and those in parentheses show % changes from previous quarter/month as applicable. The figures in () indicate % changes from previous year. [] show the comparable figure of the previous year.

(Sources)

Cabinet Office, National Accounts, Machinery Orders; METI, Indices of Tertiary Industry Activity, Industrial Production, Current Survey of Commerce; MOF, Trade Statistics, Balance of Payments; MPMHAPT, Consumer Price Index, Family Income and Expenditure Survey, Labour Force Survey; MHLW, Monthly Labour Survey; Ministry of Land, Infrastructure, and Transport, Economic Construction Statistics; BOJ, Corporate Price Index, Financial and Economic Statistics Monthly, etc.

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