Euler Hermes Economic Research

Country Report

Japan

Short-term gain, long-term pain

General Information

GDP	USD4601.5bn (World ranking 3, World Bank 2014)
Population	127.1mn (World ranking 10, World Bank 2014)
Form of state	Parliamentary government with a Constitutional Monarchy
Head of government	Shinzo ABE
Next elections	2016, legislative (House of Councilors)

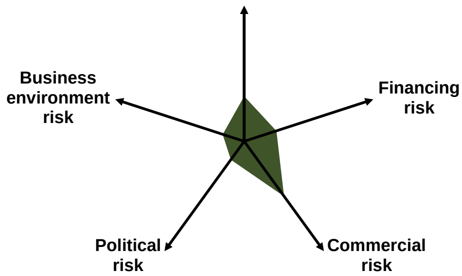
Strengths

- Current account surplus
- Low public external debt
- Good geographical location
- Innovative industries and high quality products
- High savings rate

Weaknesses

- Vulnerable to natural disaster
- Ageing population
- Huge public debt and large public deficit
- Highly dependent on energy imports

Country Rating A1



Source: Euler Hermes

Trade Structure

By destination/origin (% of total)

Exports		Rank		Imports
United States	19%	1	22%	China
China	18%	2	9%	United States
Korea, Republic of	7%	3	6%	Australia
Taiwan	6%	4	6%	Saudi Arabia
Hong Kong	6%	5	5%	United Arab Emirates

By product (% of total)

Exports		Rank		Imports
Road vehicles	21%	1	19%	Petroleum, petroleum products and
Electrical machinery, apparatus and	12%	2	10%	Gas, natural and manufactured
Specialised machinery	6%	3	7%	Electrical machinery, apparatus and
Other industrial machinery and parts	6%	4	5%	Telecommunication and sound
Iron and steel	5%	5	4%	Metalliferous ores and metal scrap

Source: UNCTAD

Economic Overview

Gradual pick-up in activity, stabilizing insolvencies

GDP growth is set to improve gradually in 2016 (+0.7%) and 2017 (+1%) supported by accommodating policies. Financing conditions are supportive of ultra-loose monetary policy. The fiscal stance is becoming more relaxed with new rounds of stimulus expected this year (1pp of GDP at least) and another postponement of the sales tax (from April 2017 to October 2019). Domestic demand will be the main growth driver in the short run. In particular, private consumption will pick up speed, benefiting from improving purchasing power, more favorable fiscal environment and rising confidence as the sales tax has been delayed. Investment is set to increase but as slow pace due to weak profits growth in H1 2016, strong JPY undermining price competitiveness and weak new export orders. After seven consecutive years of decline, insolvencies will stabilize in 2016 and increase slightly in 2017 (+3%).

External position is solid but is hindered by low external demand

Japan has a net creditor position with a net international investment position of JPY339tn in 2015. Moreover, the country exhibits a solid current account surplus underpinned by large investment revenues and reduced trade deficit thanks to low oil prices. Low external demand and higher yen hinder the short term outlook with lower exports revenues expected this year. The current account surplus will decrease close to 3% GDP in 2016.

Policies: high public debt and low progress on reforms are the main concerns

Public debt is set to increase to 251% GDP in 2017 (248% GDP in 2015). The government decided to slow the pace of "fiscal consolidation" again, postponing the sales tax rise and adding further stimulus to the economy. Although the size is critical (the highest among advanced economies), the debt ownership structure (non-resident holding of Government debt is about 9 percent) and the low-interest rate insulate the Japanese economy from a financial shock in the short-run. However, a clear plan to reduce the debt will be needed to ensure the medium term outlook. On the monetary front, the ultra-loose stance will be maintained and probably extended as stronger JPY and further deflationary pressures undermine growth. Furthermore, in order to put growth on a sustainable pace, less reliant on stimulus, the authorities will also need to move quicker on reforms especially on labor market flexibility and TPP ratification.

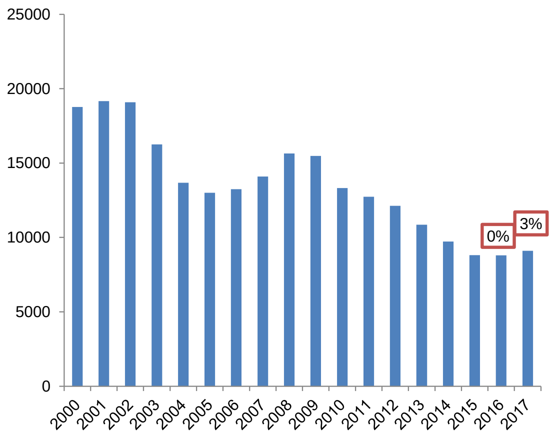
Key economic forecasts (fiscal year)

	2014	2015	2016f	2017f
GDP growth (% change)	-0.1	0.5	0.7	1.0
Inflation (%, year average)	2.7	0.8	0.2	1.0
Fiscal balance (% of GDP)*	-6.2	-5.2	-5.3	-4.9
Public debt (% of GDP)*	249.1	248.1	250.0	251.5
Current account (% of GDP)	0.6	3.3	2.9	2.5
External debt (% of GDP)	67.6	71.1	71.6	72.0

* Fiscal indicators includes: Central Government, Local Government and Social Security Funds

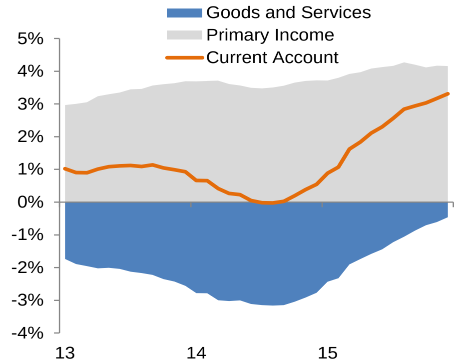
Sources: IMF, Euler Hermes

Figure 1 – Insolvencies (number and growth rate)



Sources: national sources, Euler Hermes

Figure 2 – Current account and selected sub-components (% GDP)



Sources: IHS, Euler Hermes

View all Euler Hermes Economic Research online
http://www.eulerhermes.com

Contact Euler Hermes Economic Research Team
research@eulerhermes.com

Last review: 2016-06-06
Country Risk Analyst:
Mahamoud Islam
mahamoud.islam@eulerhermes.com