

AT A GLANCE | Japan

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Transition to ‘With-COVID’ Society and Economic Outlook

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Two Years Behind U.S. Normalization

The Japanese government significantly eased border measures in October 2022 and began a clear shift toward fostering an economy and society that effectively coexist with COVID-19 (hereafter referred to as the “with-COVID” policy). On January 20, 2023, Prime Minister Fumio Kishida announced that the government would consider changing the classification of the novel coronavirus to Class 5, the same classification used for seasonal influenza, as early as this spring. In the future, the government will drastically revise its coronavirus measures, including public support for medical institutions and patients.

Many countries, including Japan, have been locked in a trade-off between quarantine measures and economic activity. Several U.S. states were among the first to remove testing requirements in 2021, and some European countries followed suit. Even China, which seems to have been the most adamant about a zero-COVID strategy, effectively switched in December 2022. Japan will make a full-fledged transition to the with-COVID policy, the slowest among major developed countries. Although lagging behind in laps, the shift to the with-COVID approach is a boost to the economy given the trade-off.

The questions that now arise are how much the pace of economic recovery will accelerate, and how the move to the with-COVID policy will affect other economic events. This report considers the institutional changes in the full-fledged transition to the with-COVID policy, the current environment surrounding households, and its relationship to economic schedules.

Key Points of Japanese Case for ‘With-COVID’

The transition to the with-COVID system will begin in earnest in the spring, but the key point is that the transition period has been pushed back to the spring. In other words, it does not mean an immediate transition from setting a preparatory period for municipalities and medical institutions. This means that even if a full-fledged economic recovery occurs, it will start in early spring.

Of course, the “eighth wave” of infections underlying the current changes has something to do with this as well. The decision to delay the transition appears to have been driven by fears that the winter shift to the with-COVID system could lead to a further increase in the number of cases and put more strain on healthcare providers.

According to media reports, the authorities are considering changing the classification under the Infectious Diseases Act from the current two or more categories of “novel influenza and other infectious diseases” to Class 5 starting in the spring. If it becomes Class 5, patients will no longer have to wait seven days in principle for infected patients and five days in principle for close contacts, and will be transferred to regular medical care. Once the waiting list is eliminated, economic activity, including human flows, will no longer be hampered by the spread of the coronavirus. In addition, the government will not be able to declare a state of emergency even if the disease spreads, so a sharp economic slowdown is likely to be avoided.

From the perspective of medical resources, it will be possible to see patients outside of fever clinics, and they will be seen at general medical institutions. The burden on certain medical institutions is expected to decrease. At the same time, public costs—such as medical expenses for treatment and hospitalization and

the addition of medical fees to medical institutions that accept patients with fever—are expected to be gradually reduced.

Overall, although the timing has been pushed back to the spring, there will be no longer be a waiting period related to the risk of contracting the disease, and health resources will be normalized. In other words, impediments to economic activity should be seen as largely eliminated.

On a slightly more granular note, however, the impact on mask-wearing and the associated consumption of face-to-face services may remain. Japan will continue to require people to wear masks only if they have fever or other symptoms that could spread the infection to others, or if they are elderly or have underlying medical conditions that require prevention.

The government already said in May 2022 that outdoor mask-wearing was not required. While there are caveats, such as the presence or absence of conversation, the government has gradually reduced the need to wear masks. However, many people in Japan still maintain the custom of mask-wearing. While not legally binding, the voluntary practice of wearing masks could remain in place. The recovery in consumption of face-to-face services such as eating and drinking may be limited, if not self-restrained.

Current Environment Surrounding Household Finances

As noted above, while there are some other points to keep in mind, the main scenario of a full-fledged transition to the with-COVID policy and an economic recovery beginning in the spring are consistent. On the other hand, other than attention to with-COVID itself, the changing environment surrounding household finances has become something to watch.

As we have previously pointed out in this report, consumer confidence has continued to deteriorate recently (Figure 1). Rising food and energy prices, which have not occurred in the past 20 to 30 years, have significantly increased household inflation expectations (Figure 2). Against this backdrop, consumer confidence remains weak, and even with a full-fledged shift to the with-COVID system, the recovery in consumption may be slow.

In this case, the so-called surplus savings will likely remain (Figure 3). Although there are various methods for estimating surplus savings and the results need to be viewed with a wide range of approaches in mind, there is no doubt that surplus savings are accumulating as the propensity to consume has been curbed through the pandemic. While surplus savings have been seen by some as a source of room for increased consumption, it seems increasingly likely that spending will remain subdued as excess savings are used to fight inflation.

Figure 1: Consumer Sentiment Index



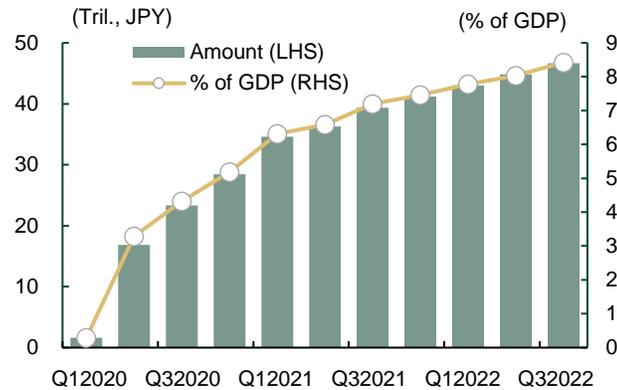
Source: CAO

Figure 2: Expected Inflation of Households (expected prices in one year)



Source: Bank of Japan

Figure 3: Estimation of Surplus Savings



Source: CAO

An Economic Schedule Packed With Important Events

There will be a flurry of economic events in the spring, which will coincide with the start of a full-fledged transition to the with-COVID approach.

In February, as analyzed in this report last week, indicators will be released for the spring wage negotiations. Candidates for the Bank of Japan’s (BOJ) executive vice governor position are also expected to be submitted to the Diet. Expectations for a policy correction at the March 9-10 Monetary Policy Meeting have been smoldering among some market participants. A new deputy governor will take office on March 20. In addition, the BOJ will close its Proper Loan Program for small and medium-sized enterprises at the end of March.

A new governor will take office on April 9 and the first Monetary Policy Meeting under the new regime will be held on April 27-28. As has been reported in the past, there may be a review of the joint statement between the government and the BOJ. Around this time, companies and organizations will report their decisions regarding the wage negotiations. A preliminary report on the Japanese Trade Union Confederation is usually released in mid-May.

The full-fledged transition to the with-COVID policy, which overlaps with that schedule, could affect the three things noted below.

First, the BOJ’s contingency operations during the pandemic period are expected to be completed on time. The plan, which has been in line with the government’s goal to help companies raise funds, will come to an end in line with the full-scale transition to the with-COVID approach.

Second, and overlapping with the first, there will be growing momentum to change the monetary policy framework. The transition from a pandemic to a “peacetime” approach can occur not only with respect to infectious disease law, but also with respect to monetary policy. Among other things, the “[f]or the time being, the government will closely monitor the impact of the novel coronavirus disease and work to support the cash flow of companies and maintain the stability of financial markets, and if necessary, it will not hesitate to take additional monetary easing measures. The policy rate is expected to remain at or below the current level of short- and long-term interest rates” section of the statement, which also relates to the current forward guidance of the policy rate, may be amended.

Third, it has an impact on business sentiment. Even companies that could not tolerate wage increases during the pandemic may find themselves more willing to raise wages if they see a near-term improvement in corporate earnings.

There are many aspects of quarantine measures in relation to the coronavirus that cannot be discussed simply with respect to economic activity. Inflation, household sentiment and consumption trends also need to be closely monitored. However, in relation to the economic schedule, the change in approach could be one of the symbolic catalysts representing a turning point of the Japanese economy amid many important events.

Economic Outlook: 2022-2024 Forecast

Figure 1: Forecasts for Economic Growth, Inflation, and Unemployment Rates

		2022			2023				2024				2021	2022	2023	2024
		Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4				
US	Real GDP	-0.6	3.2	2.9	-0.2	0.3	0.7	0.8	1.4	1.6	1.6	1.8	5.9	2.1	0.6	1.2
	Inflation	5.0	4.9	4.7	4.9	4.7	4.2	3.6	3.2	3.0	2.8	2.6	3.3	5.0	4.4	2.9
	Unemployment	3.6	3.6	3.6	4.5	4.8	5.0	5.0	5.0	5.0	4.9	4.9	5.4	3.7	4.8	5.0
Euro Area	Real GDP	0.8	0.3	-0.2	-0.2	0.4	0.3	0.0	0.1	0.5	0.4	0.3	5.3	3.4	0.5	1.0
	Inflation	8.0	9.1	10.3	8.9	7.2	5.7	4.2	3.8	3.2	2.5	2.2	2.6	8.6	6.5	2.9
	Unemployment	6.7	6.7	6.7	6.9	7.1	7.1	7.2	7.4	7.4	7.3	7.2	7.7	6.7	7.1	7.3
Japan	Real GDP	4.5	-0.8	3.6	2.4	1.5	0.9	0.9	0.9	0.8	0.8	0.7	1.7	1.5	1.8	0.9
	Inflation	2.1	2.7	3.8	3.1	2.4	2.0	1.8	2.7	3.0	2.9	2.2	-0.2	2.3	2.3	2.7
	Unemployment	2.6	2.5	2.5	2.5	2.4	2.4	2.4	2.3	2.3	2.3	2.3	2.8	2.6	2.4	2.3
China	Real GDP	0.4	3.9	2.9	2.6	7.6	5.5	7.0	7.1	5.8	5.2	4.9	8.1	3.0	5.8	5.7
	Inflation	2.2	2.8	1.8	2.1	2.2	2.0	2.0	2.1	2.2	2.1	2.0	0.8	1.7	2.1	2.1
	Unemployment	5.8	5.4	5.6	5.5	5.4	5.1	4.9	4.9	4.9	5.0	5.0	5.1	5.1	5.2	5.0

Real GDP growth is in QoQ annualized for U.S. and Japan, QoQ for euro area and YoY for China and India. Inflation rate is in YoY%. Inflation rate is YoY, % of core index (ex. fresh food) for Japan, YoY % of PCE deflator for U.S., and total YoY% for the rest.

Figure 2: Forecast for Rates

Interest rate		2022	2023				2024				2022	2023	2024
		Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
US	Policy rate	4.25 ~ 4.50	4.75 ~ 5.00	4.75 ~ 5.00	4.75 ~ 5.00	4.50 ~ 4.75	4.25 ~ 4.50	4.00 ~ 4.25	3.75 ~ 4.00	3.50 ~ 3.75	4.25 ~ 4.50	4.50 ~ 4.75	3.50 ~ 3.75
	2yr	4.20	4.30	4.30	4.20	4.00	4.00	3.70	3.50	3.20	4.20	4.00	3.20
	10yr	3.60	3.60	3.50	3.40	3.40	3.30	3.30	3.20	3.20	3.60	3.40	3.20
Germany	Policy rate	2.50	3.50	3.75	3.75	3.50	3.25	3.25	3.00	3.00	2.50	3.50	3.00
	Deposit rate	2.00	3.00	3.25	3.25	3.00	2.75	2.75	2.50	2.50	2.00	3.00	2.50
	2yr	2.50	3.10	3.20	3.10	2.90	2.70	2.50	2.40	2.30	2.50	2.90	2.30
Japan	Policy rate	-0.10	-0.10	-0.10	-0.10	-0.10	0.10	0.10	0.10	0.10	-0.10	-0.10	0.10
	2yr	0.00	0.00	0.10	0.15	0.20	0.30	0.30	0.30	0.30	0.00	0.20	0.30
	10yr	0.50	0.50	0.75	0.75	0.75	0.90	0.90	0.90	0.90	0.50	0.75	0.90
China	Policy rate	2.75	2.65	2.65	2.65	2.65	2.65	2.65	2.75	2.75	2.75	2.65	2.75
	2yr	2.39	2.35	2.40	2.55	2.60	2.62	2.65	2.70	2.75	2.39	2.60	2.75
	10yr	2.83	2.85	2.80	2.85	2.90	2.92	2.95	3.00	3.05	2.83	2.90	3.05

Figure 3: Forecast for FX and Oil Price

		2022	2023				2024				2022	2023	2024
		Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
USD/JPY	Range	130.58 ~ 151.95	120.00 ~ 138.00	118.00 ~ 136.00	118.00 ~ 136.00	116.00 ~ 134.00	113.00 ~ 131.00	113.00 ~ 131.00	110.00 ~ 128.00	110.00 ~ 128.00	113.47 ~ 151.95	116.00 ~ 138.00	110.00 ~ 131.00
	End of quarter	131.12	130.00	128.00	128.00	126.00	123.00	123.00	120.00	120.00	131.12	126.00	120.00
EUR/USD	Range	0.9633 ~ 1.0735	1.0806 ~ 1.1200	1.0300 ~ 1.1300	1.0100 ~ 1.1100	0.9800 ~ 1.0800	0.9600 ~ 1.0600	1.0000 ~ 1.1000	1.0300 ~ 1.1300	1.0200 ~ 1.1200	0.9536 ~ 1.1495	0.9800 ~ 1.1300	0.9600 ~ 1.1300
	End of quarter	1.0705	1.0700	1.0800	1.0500	1.0300	1.0200	1.0500	1.0800	1.0700	1.0705	1.0300	1.0700
EUR/JPY	Range	138.81 ~ 148.40	124.40 ~ 150.00	128.00 ~ 148.00	125.00 ~ 145.00	120.00 ~ 140.00	115.00 ~ 135.00	120.00 ~ 138.00	120.00 ~ 138.00	120.00 ~ 138.00	124.40 ~ 150.00	120.00 ~ 150.00	115.00 ~ 138.00
	End of quarter	140.41	139.10	138.24	134.40	129.78	125.46	129.15	129.60	128.40	140.41	129.78	128.40
Crude Oil Prices (WTI)		82.64	88.00	85.50	88.30	94.15	98.30	85.00	82.50	84.15	98.74	88.99	87.49

※ Crude oil prices are averages for each period. Source: SMBC.

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