FY2024 New Year Economic Outlook

Dilemmas lurking in the last mile

December 25, 2023

Mizuho Research & Technologies, Ltd.

Key points of our outlook

- The global economy in 2024 is expected to slow due to an economic downturn in China and high interest rates in Europe and the United States. Global growth will continue to be weighed down in 2025 by prolonged adjustments in China's real estate sector, but the year will likely see the global economy moderately recover as the US and European economies gradually pick up steam with continued lower interest rates, while ASEAN and other economies will bounce back driven by external demand from developed countries.
- Economic activities in the US will return to normal as inflation rapidly falls, with the easing of pressures on the labor market and supply chains (supply constraints). The need for excessive monetary tightening and the accompanying downward pressure on the economy will diminish. Given the impact of the tight monetary policy, the US economy is likely to slow but avoid negative growth in 2024, getting on track for a moderate recovery in 2025.
- Europe's economy will fall into recession fueled by the growing impact of monetary tightening from the end of 2023 through the first half of 2024. The European Central Bank (ECB) will begin to cut interest rates in the first half of 2024, with the pace of rate cuts expected to be moderate due to concerns about wage inflation. European economic growth will likely be weak in the lower 0% range in 2023 and 2024, picking up in 2025 with further rate cuts and lower inflation.
- China's economic slowdown will further accelerate in 2023 and 2024 amid prolonged adjustments in its real estate sector, with growth inevitably weakened by the government's cautious stance toward massive stimulus packages involving large deficits. The newly industrialized economies (NIEs) will recover in 2024 due to the semiconductor cycle's turnaround, while the Association of Southeast Asian Nations (ASEAN) will see its economy move forward, driven by policy rate cuts and rising external demand.
- The Japanese economy will likely advance at a moderate pace in FY2024 with a pause in the recovery of service spending and inbound tourism demand through the easing of coronavirus concerns, compounded by the softening of overseas economies and sluggish growth in real employee compensation. The growth rate in FY2025 is likely to slow toward the potential growth rate with personal consumption lacking strength and the pace of recovery led by external demand remaining moderate.
- In financial markets, the US Federal Reserve's interest rate cuts and the Bank of Japan's (BOJ) policy changes will narrow the gap between domestic and foreign interest rates, and the yen is expected to gradually strengthen to the upper 120-yen per dollar range through the end of 2024. The BOJ will lift negative interest rates and remove the yield curve control (YCC) in the April-June quarter of 2024, and is likely to maintain its zero interest rate policy as the upward momentum of wages and prices falters.

Outlook on the global economy: Moderate recovery after the slowdown in 2024

Outlook on the global economy

(Y-o-y % change) (%pt)

	2022	2023 (Outlook)	2024 (Outlook)	2025 (Outlook)	2023 (Compared with Sept.)	2024 (Compared with Sept.)
Global real GDP growth	3.3	3.0	2.8	2.9	0.1	0.3
Japan, US, Europe	2.5	1.5	0.9	1.5	0.2	0.6
US	1.9	2.4	1.2	1.5	0.4	1.1
Eurozone	3.4	0.4	0.4	1.5	-	0.1
UK	4.1	0.4	0.7	1.8	0.2	0.1
Japan	1.0	2.0	1.0	1.0	0.1	0.2
Asia	4.1	5.0	4.7	4.4	0.2	0.2
China	3.0	5.2	4.6	4.2	0.4	0.2
NIEs	2.2	1.4	2.1	1.7	-0.1	0.2
ASEAN5	5.9	4.6	4.5	4.6	-0.1	0.1
India	6.7	6.7	6.1	6.0	-	-0.1
Australia	3.7	1.9	1.8	1.7	0.1	-
Japan (FY)	1.5	1.6	1.1	0.7	-0.2	0.3

Economic slowdown in 2024 due to high interest rates in the US and Europe and China's sagging economy. Moderate recovery in 2025 led primarily by the US, Europe, and ASEAN.

Easing supply constraints (labor and goods shortages) and slowing inflation. Employment and incomes remain resilient despite the growing impact of monetary tightening. The growth rate rises in 2025.

High interest rates exert downward pressure on aggregate demand. Negative growth from late 2023 through early 2024, with recovery in 2025.

Prolonged adjustments in the real estate sector and continuing sluggish consumer confidence. Cautious stance on massive stimulus measures. The projected growth rate remains slow.

Fading pent-up demand. Global manufacturers move forward at a tepid pace. Slowing growth momentum.

Note: The figures in shaded areas are forecasts. The global growth rate is calculated based on GDP share (PPP) from the IMF.
Source: Compiled by MHRT based on IMF data and the statistics of relevant countries and regions.

Key issues and assessments of the major economies

US	**Factors behind slowing inflation and the depth of economic slowdown**	◆ Inflation will slow more than expected due to the easing of labor and goods shortages (supply constraints). ◆ Slowing inflation will reduce the need for excessive monetary tightening and downward pressure on the economy. ◆ Employment and incomes are unlikely to worsen significantly despite the growing impact of monetary tightening (demand suppression). ◆ Negative growth will be avoided in 2024 while heading toward a growth recession.
Europe	**Outlook for wages and prices, and the timing of rate cuts**	◆ Inflation will continue to slow with a pause on passing on energy costs and a faltering economy. ◆ Wages are likely to top out, but labor bargaining through spring 2024 should be watched closely. ◆ The ECB is expected to cut interest rates in the April-June 2024 quarter after confirming slowing wage growth.
Emerging economies	**China's slumping real estate sector, and the timing of Asia's economic recovery**	◆ Infrastructure investment will prop up China's economy, but growth will slow in 2024 and beyond due to weak consumer confidence and adjustments in the real estate sector. A shrinking population, tighter domestic governance, escalating US-China tensions, and other structural factors will also exert downward pressure on growth. ◆ NIEs and ASEAN will experience economic downturns in the first half of 2024, with recovery likely to take hold from mid-2024 when external demand is expected to pick up and monetary tightening lifted. India will continue to enjoy growth driven by overseas and government infrastructure investments.
Japan	**Prospects for wages and prices**	◆ Annual spring wage negotiations in 2024 will bring pay raises higher than the previous year to maintain a high level, but real wages will continue to post a year-on-year decline through the first half of 2024. Personal consumption will lack strength, and the supply-demand gap will not be bridged until the second half of 2024. ◆ With little expectation of prices being pushed up from the demand side, small and midsize enterprises (SMEs) will become cautious about raising wages. Both nominal wages and consumer prices will slow to a +1% range year-on-year increase in FY2025. (The momentum to achieve the 2% inflation target is unlikely to be maintained.)
Financial markets	**Impact of monetary policy changes in Japan and the US**	◆ Japan's long-term interest rates are expected to be in the lower 1% range, reflecting the BOJ's shift to monetary tightening. ◆ The US long-term interest rates will rise close to 4%, before declining to the upper 3% range. ◆ The yen is expected to strengthen to the upper 120-yen per dollar range on the back of the shrinking gap in interest rates between Japan and the US. ◆ US stocks are likely to continue rising across the board, while Japanese stocks will fall through mid-2024 on the back of a stronger yen.

Source: Compiled by MHRT.

(1) US: Slowing economy, avoiding negative growth, and heading toward a growth recession

- Real GDP growth is forecast at +1.2% in 2024 and +1.5% in 2025.
  - The overall macro supply capacity has recently improved as businesses boosted production facilities, and immigrants and prime-age workers expanded the labor supply. Labor and goods shortages (supply constraints) have been eased, and inflation has steadily decelerated.
  - Interest rate hikes will exert a marked impact primarily on the corporate sector through mid-2024. Companies will become less willing to hire workers, but immigrants and prime-age workers will flow into recession-proof "rock-solid" industries, such as healthcare and government services, preventing a deterioration in employment conditions.
  - The Federal Reserve is expected to cautiously cut interest rates in the April-June 2024 quarter and onward to prevent a resurgence of inflationary pressures.

Outlook on the US economy

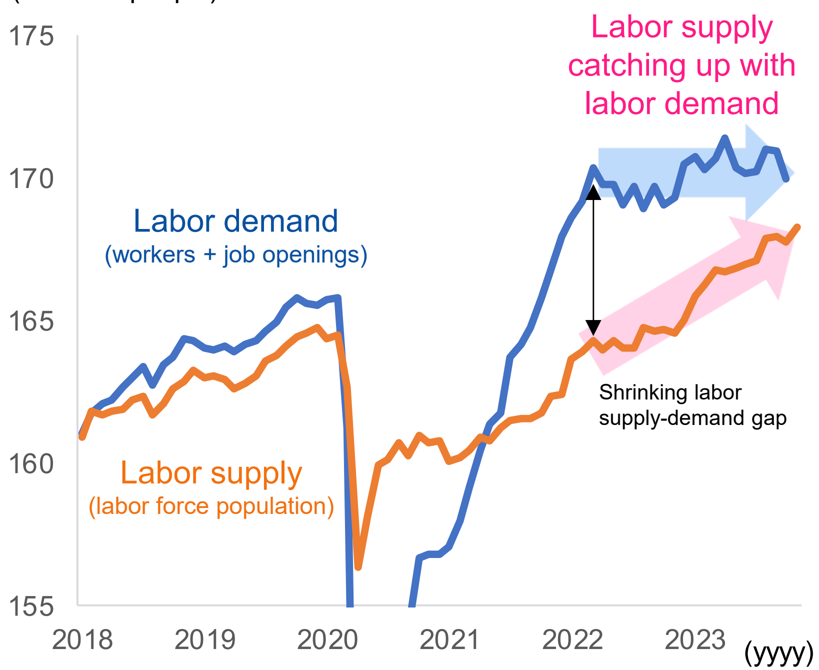
		2022	2023	2024	2025	2023				2024				2025			
			(Outlook)			Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec	Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec	Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec
GDP (real)	Q-o-q % ch p.a.	1.9	2.4	1.2	1.5	2.2	2.1	5.2	1.0	0.5	0.2	0.6	1.4	2.0	2.2	1.5	1.5
Personal consumption	Q-o-q % ch p.a.	2.5	2.2	1.3	1.9	3.8	0.8	3.6	1.7	0.7	0.4	1.0	1.8	2.4	2.3	2.1	2.1
Housing investment	Q-o-q % ch p.a.	-9.0	-11	1.8	5.9	-5.3	-2.2	6.2	0.4	0.2	0.2	4.8	6.1	6.8	6.5	6.5	5.8
Capital investment	Q-o-q % ch p.a.	5.2	4.2	0.5	1.4	5.7	7.4	1.3	0.0	-0.6	-1.0	0.8	1.5	1.4	1.7	1.7	2.8
Inventory investment	Q-o-q contribution p.a. %pt	0.0	-0.2	0.1	0.3	-2.2	0.0	1.4	0.2	0.1	0.0	0.1	0.2	0.5	0.5	0.1	0.0
Government consumption	Q-o-q % ch p.a.	-0.9	3.7	0.9	0.1	4.8	3.3	5.5	0.0	0.0	0.0	0.0	0.1	0.1	0.1	0.1	0.1
Net exports	Q-o-q contribution p.a. %pt	0.0	0.1	-0.3	-0.6	0.6	0.0	-0.0	-0.4	-0.1	-0.0	-0.5	-0.6	-0.7	-0.5	-0.6	-0.6
Exports	Q-o-q % ch p.a.	7.0	2.4	0.4	0.7	6.8	-9.3	6.0	0.4	0.4	0.4	0.4	0.4	0.9	0.9	0.9	1.2
Imports	Q-o-q % ch p.a.	8.6	-1.5	1.6	4.1	1.3	-7.6	5.2	2.7	0.7	0.3	3.8	4.0	5.0	3.6	4.6	4.9
Unemployment rate	%	3.6	3.7	4.2	4.0	3.5	3.6	3.7	3.8	4.1	4.3	4.2	4.1	4.1	4.0	4.0	4.0
PCE deflator	Y-o-y % ch	6.5	3.8	2.6	2.3	5.0	3.9	3.4	3.1	2.7	2.6	2.5	2.4	2.3	2.3	2.3	2.2
Core, excl. food and energy	Y-o-y % ch	5.2	4.2	2.5	2.3	4.8	4.6	3.9	3.4	2.8	2.5	2.5	2.4	2.4	2.3	2.3	2.2

Note: The figures in shaded areas are forecasts by MHRT.
Source: Compiled by MHRT based on data from the US Department of Commerce and the US Department of Labor.

US: Labor supply catching up with labor demand; immigrants and prime-age workers easing labor shortages

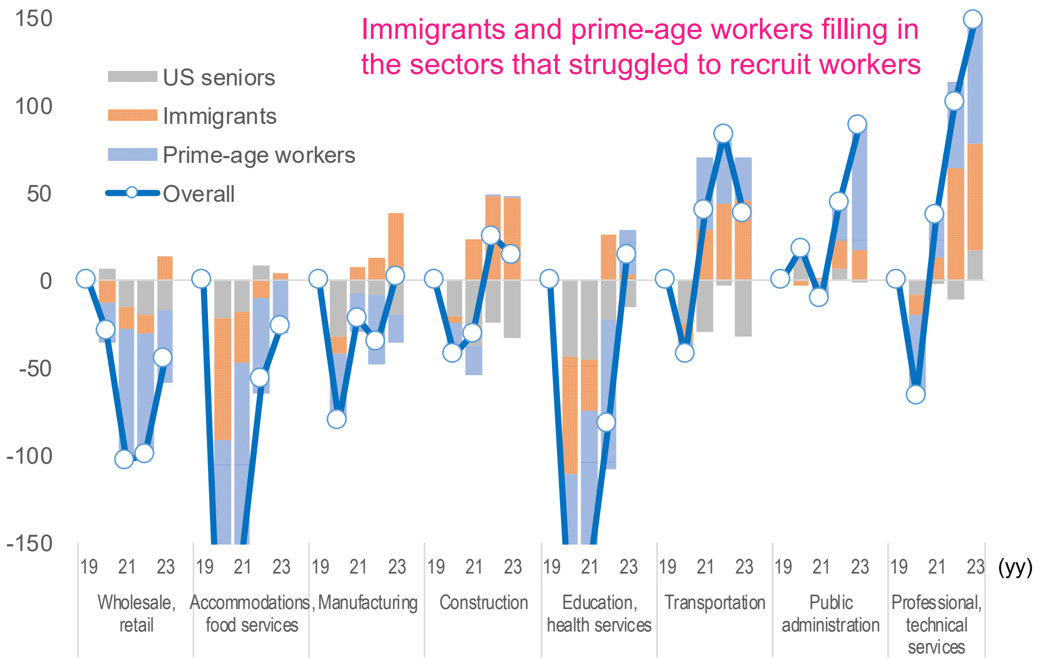
- Labor supply is on a recovery trend as it catches up with labor demand.
- While the senior group retired early after the pandemic, a growing number of immigrants and prime-age workers are joining the labor force to fill the void.
  - Immigration growth is being driven by the influx of migrants after President Joe Biden took office. However, a Republican candidate with a negative stance on immigration winning in the 2024 presidential election could see a decline in the influx of migrants and the return of labor shortages.
  - The increase in prime-age workers is attributed to female workers returning to work after having left their jobs for childrearing during the coronavirus pandemic as well as a rising number of highly educated workers with high labor participation rates.

Labor supply-demand gap



Source: Compiled by MHRT based on data from the US Department of Labor.

Workers by industry (cumulative changes since 2019)

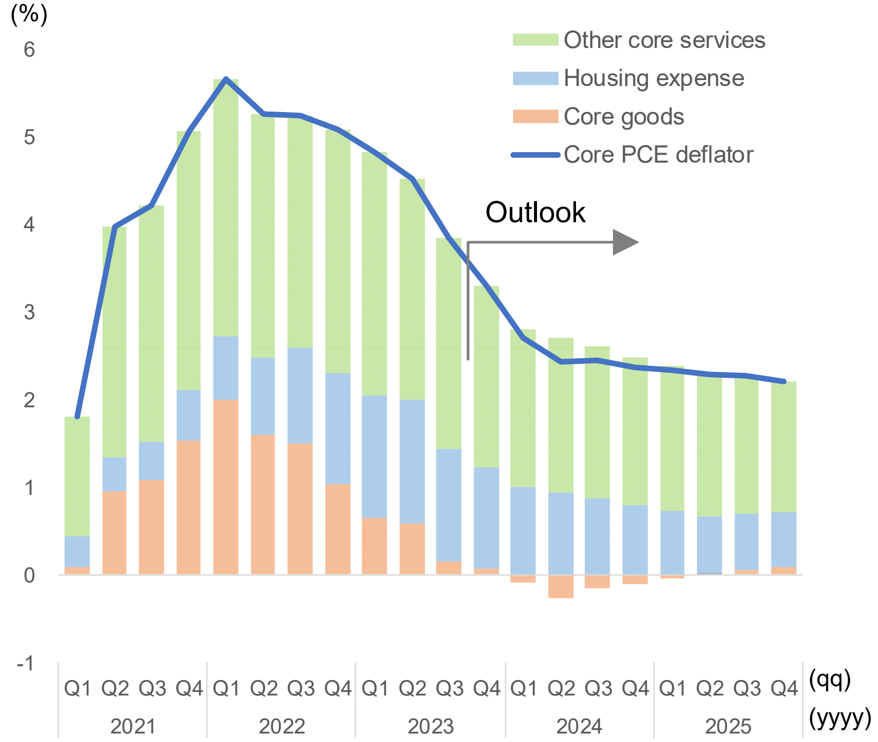


Note: Based on data in October of each year.
Source: Compiled by MHRT based on data from the US Department of Commerce.

US: Federal Reserve rate cuts starting in April-June 2024

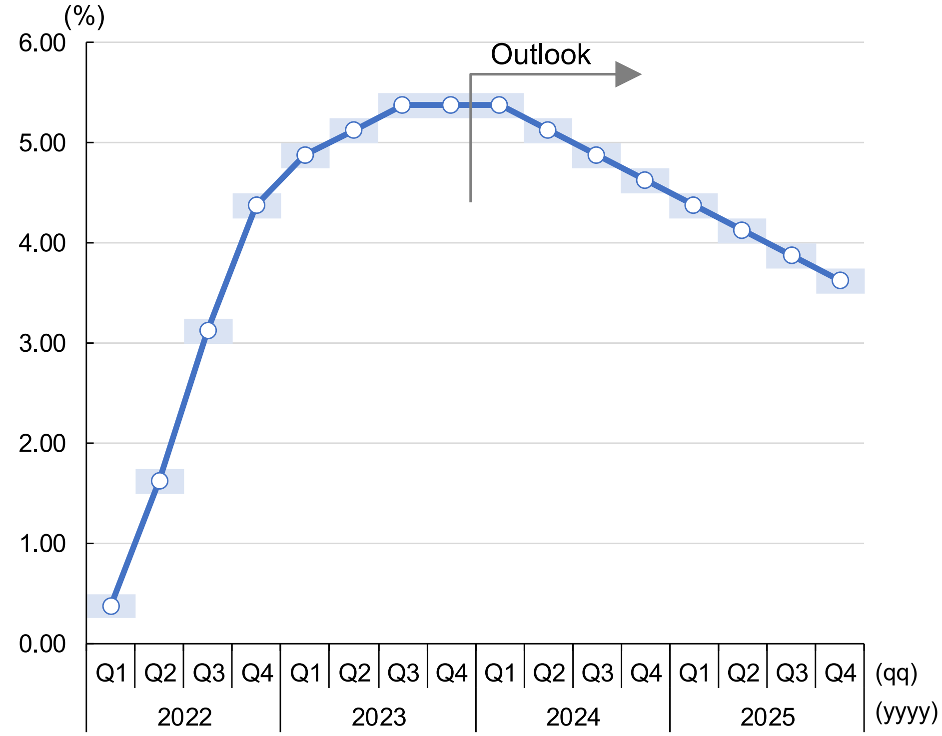
- Inflation is likely to slow steadily through the April-June 2024 period.
  - In the July-September 2024 quarter and beyond, goods prices will stabilize as the effects of easing supply constraints subside, while wages and service prices will decelerate at a rather moderate pace; on the whole, the decline in inflation will become smaller.
  - The core personal consumption expenditure (PCE) deflator will gradually slow to 2.4% at the end of 2024 and 2.2% at the end of 2025.
- The Federal Reserve is expected to begin cutting interest rates in the April-June 2024 period. Afterwards, rate cuts will likely continue at a modest and gradual pace.

Core PCE deflator outlook



Source: Compiled by MHRT based on data from the US Department of Commerce.

Monetary policy outlook



Source: Compiled by MHRT based on data from the Federal Reserve.

(2) Eurozone: Slight recession through early 2024; recovery beginning in late 2024

- Real GDP growth is forecast at +0.4% in both 2023 and 2024.
  - The eurozone economy will continue to experience a slight recession through early 2024 due to the impact of interest rate hikes and slowdown in overseas economies.
- Real GDP growth in 2025 is projected at +1.5%.
  - The eurozone economy will pick up from the second half of 2024, when inflation will likely subside and the ECB cuts interest rates.

Outlook on the Eurozone economy

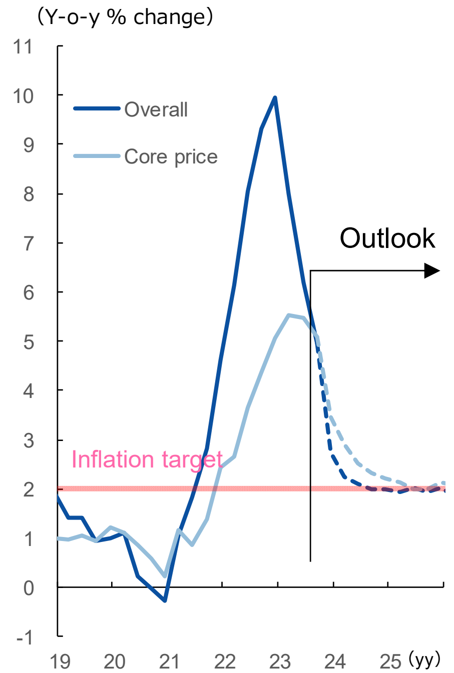
		2022	2023	2024	2025	2022				2023				2024				2025			
			(Outlook)			Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec	Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec	Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec	Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec
GDP (real)	Q-o-q % ch	3.4	0.4	0.4	1.5	0.7	0.8	0.5	-0.1	0.1	0.1	-0.1	-0.2	-0.1	0.3	0.4	0.5	0.4	0.3	0.2	0.2
Domestic demand	Q-o-q % ch	3.5	0.2	0.4	1.3	-0.0	0.7	1.0	-0.5	-0.6	0.8	-0.1	-0.2	-0.0	0.3	0.3	0.4	0.3	0.3	0.2	0.2
Personal consumption	Q-o-q % ch	4.2	0.5	0.6	1.3	-0.0	0.8	1.3	-0.8	0.0	0.0	0.3	-0.0	0.1	0.2	0.3	0.4	0.4	0.4	0.3	0.2
Gross fixed capital formation	Q-o-q % ch	2.6	0.7	-0.4	1.2	-0.5	0.5	1.3	-0.4	0.4	-0.1	0.0	-0.3	-0.3	-0.0	0.1	0.3	0.4	0.4	0.2	0.3
Government consumption	Q-o-q % ch	1.6	0.0	-0.2	0.3	0.4	-0.1	-0.1	0.5	-0.5	0.2	0.3	-0.3	-0.2	0.0	0.0	0.1	0.1	0.1	0.1	0.1
Inventory investment	QoQ contribution, %pt	0.3	-0.2	0.2	0.2	-0.1	0.2	0.1	-0.1	-0.5	0.7	-0.3	-0.1	-0.0	0.2	0.2	0.1	-0.0	-0.0	-0.0	-0.0
External demand	QoQ contribution, %pt	-0.0	0.3	-0.0	0.2	0.8	0.2	-0.5	0.4	0.6	-0.6	-0.0	0.0	-0.0	0.1	0.1	0.1	0.1	0.0	0.0	0.0
Exports	Q-o-q % ch	7.2	-0.8	-0.6	1.2	1.6	2.0	1.2	-0.3	-0.3	-1.1	-1.1	-0.1	0.0	0.2	0.3	0.4	0.4	0.3	0.2	0.2
Imports	Q-o-q % ch	7.9	-1.4	-0.5	0.8	0.1	1.8	2.4	-1.1	-1.6	0.0	-1.2	-0.2	0.0	0.0	0.1	0.2	0.2	0.3	0.2	0.2
CPI	Y-o-y % ch	8.4	5.4	2.1	2.0	6.1	8.0	9.3	10.0	8.0	6.2	5.0	2.7	2.2	2.1	2.0	2.0	1.9	2.0	1.9	2.0
Core, excl. food and energy	Y-o-y % ch	3.9	4.9	2.5	2.1	2.7	3.7	4.4	5.1	5.5	5.5	5.1	3.5	2.9	2.5	2.3	2.2	2.1	2.0	2.0	2.1

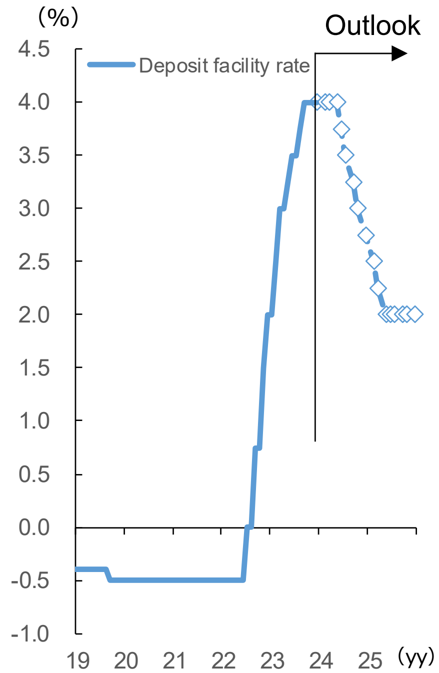
Note: The figures in shaded areas are forecasts by MHRT.
Source: Compiled by MHRT based on data from Eurostat.

Eurozone: ECB rate cuts starting in April-June 2024; minor impact of reducing PEPP reinvestments

- The ECB kept interest rates unchanged in October for the first time in 11 meetings of its Governing Council and held its policy rate steady at 4.0% in the following meeting in December.
  - With inflation clearly slowing, the ECB's next move is likely a rate cut. The timing is expected to be in the April-June 2024 period, when inflation will approach 2% and the outcomes of spring labor bargaining will be reported.
  - At the December meeting, the ECB decided to reduce reinvestments in bond buying under the pandemic emergency purchase programme (PEPP) to an average of 7.5 billion euros per month starting in the second half of 2024. With the portfolio gradually reduced, the impact on Italy's government bond yields is likely to be negligible, up about a mere 0.1 percentage points.

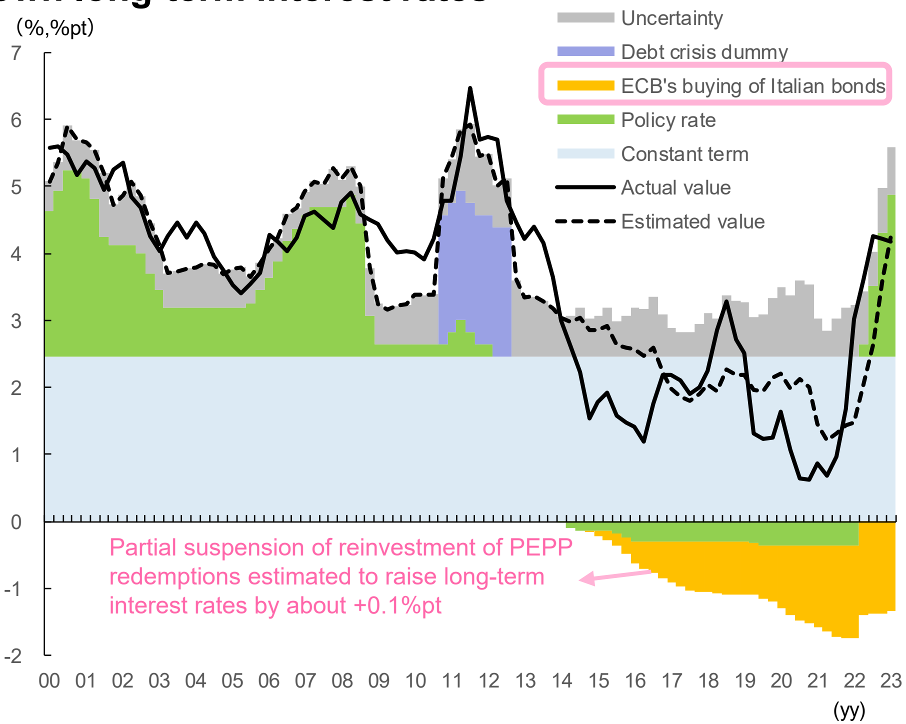
Eurozone: Inflation and policy rate outlook





Source: Compiled by MHRT based on data from Eurostat and the European Central Bank.

Italy: Effects of ECB bond purchases on pushing down long-term interest rates



Source: Compiled by MHRT based on data from Eurostat, the European Central Bank, Refinitiv, and other sources.

(3) Emerging economies: China facing a slowdown, NIEs and ASEAN recovering from mid-2024 or later, and India enjoying solid growth

- China's infrastructure investment will shore up the economy, but the country will experience an economic slowdown in 2024 and beyond on the back of prolonged adjustments in the real estate sector and sluggish consumer confidence. Economic growth will remain tepid due to the government's cautious stance on massive stimulus packages and downward pressures from its population decline and other structural factors.
- NIEs and ASEAN economies will weaken due to slumping external demand and monetary tightening, with recovery likely to pick up in mid-2024 or later.
  - NIEs will see growth rise in 2024 with improvements in their semiconductor cycles. ASEAN's recovery will be pushed back to 2025 due to its low reliance on semiconductors.
- India will continue to face inflationary pressure, but will maintain strong domestic demand supported by increasing overseas investment and the government's infrastructure spending.
  - Investment-driven growth is expected to continue through strong policy support.

Outlook on the emerging economies

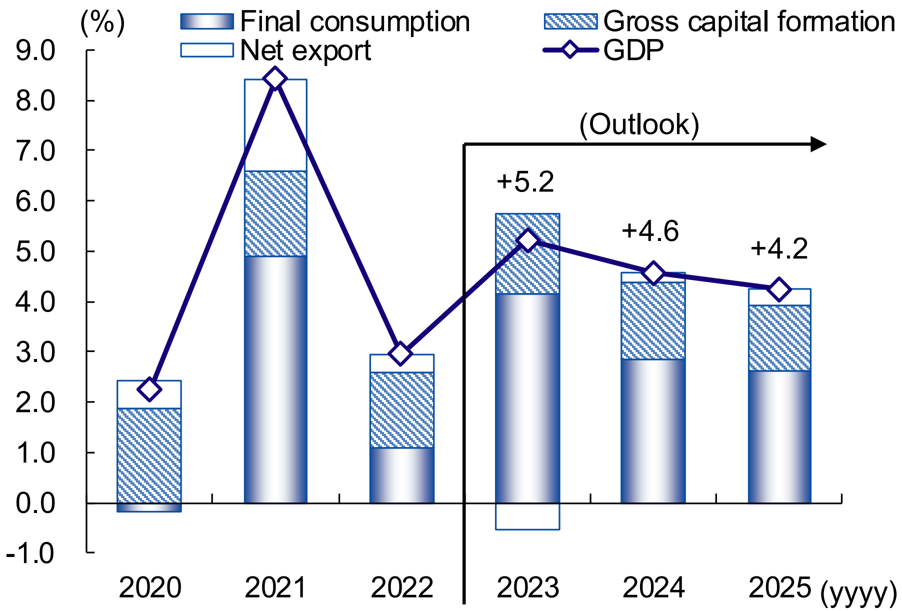
	2021	2022	2023 (Outloook)	2024	2025	2021 Jul-Sep	2021 Oct-Dec	2022 Jan-Mar	2022 Apr-Jun	2022 Jul-Sep	2022 Oct-Dec	2023 Jan-Mar	2023 Apr-Jun	2023 Jul-Sep
Asia	7.4	4.1	5.0	4.7	4.4	-	-	-	-	-	-	-	-	-
China	8.4	3.0	5.2	4.6	4.2	5.2	4.3	4.8	0.4	3.9	2.9	4.5	6.3	4.9
NIEs	5.7	2.2	1.4	2.1	1.7	-	-	-	-	-	-	-	-	-
South Korea	4.3	2.6	1.3	1.9	1.7	4.1	4.3	3.1	2.9	3.2	1.4	0.9	0.9	1.4
Taiwan	6.6	2.6	1.0	2.4	1.7	4.2	5.1	3.8	3.5	4.0	-0.7	-3.5	1.4	2.3
Hong Kong	6.4	-3.5	3.3	2.4	2.0	5.5	4.7	-3.9	-1.2	-4.6	-4.1	2.9	1.5	4.1
Singapore	8.9	3.6	1.3	2.1	1.9	8.7	6.6	4.0	4.5	4.0	2.1	0.5	0.5	1.1
ASEAN5	3.4	5.9	4.6	4.5	4.6	-	-	-	-	-	-	-	-	-
Indonesia	3.7	5.3	5.0	4.3	4.6	3.5	5.0	5.0	5.5	5.7	5.0	5.0	5.2	4.9
Thailand	1.5	2.6	2.9	3.6	2.7	-0.2	1.9	2.2	2.5	4.6	1.4	2.6	1.8	1.5
Malaysia	3.3	8.7	4.4	3.9	4.0	-4.2	3.6	4.8	8.8	14.1	7.1	5.6	2.9	3.3
Philippines	5.7	7.6	5.1	5.3	5.3	7.0	7.9	8.0	7.5	7.7	7.1	6.4	4.3	5.9
Vietnam	2.6	8.0	4.9	6.3	6.7	-6.0	5.2	5.1	7.8	13.7	5.9	3.3	4.1	5.3
India	8.9	6.7	6.7	6.1	6.0	9.1	5.2	4.0	13.1	6.2	4.5	6.1	7.8	7.6
Australia	5.2	3.7	1.9	1.8	1.7	4.6	5.0	3.6	3.9	5.7	2.7	2.3	1.8	2.5
Ref. NIEs+ASEAN5	4.3	4.5	3.4	3.6	3.6	-	-	-	-	-	-	-	-	-
Ref. Asia, excl. China	6.3	5.4	4.9	4.7	4.7	-	-	-	-	-	-	-	-	-

Note: Real GDP growth rates (y-o-y, %) and the figures in shaded areas are forecasts. The averages are calculated using IMF's GDP shares (based on purchasing power parity).
Source: Compiled by MHRT based on the statistics of relevant countries and regions, and data from the International Monetary Fund and other sources.

China: Infrastructure investment driven by additional government bonds propping up the economy, but projected growth remaining slow

- GDP growth is projected at +5.2% in 2023 and +4.6% in 2024.
  - Growth will be on the upswing driven by the issuance of an additional 1 trillion yuan of government bonds (0.8% to GDP ratio) aimed primarily at supporting recovery from natural disasters in October 2023 and the expansion of infrastructure investment.
  - However, the projected growth will remain slow due to prolonged adjustments in the real estate sector and slumping consumer confidence.
- GDP growth in 2025 is forecast at +4.2%, with the projected growth expected to remain weak.
  - Growth will remain under downward pressure from structural factors, such as population decline, tighter domestic governance, US-China tensions, in addition to prolonged adjustments in the real estate sector.
  - Fiscal measures to shore up the economy are expected, but massive stimulus packages involving a substantial increase in deficits are unlikely to be introduced.

Real GDP growth (contribution by demand component)



Source: Compiled by MHRT based on data from the National Bureau of Statistics of China and CEIC.

Overview of China's economic outlook

Factors behind China's stalling economic recovery
- Vicious cycle of slumping real estate sales and stagnant prices
- Personal consumption weakened by sluggish consumer confidence

Background of continued slow growth
- Downward pressure from structural factors including population decline, domestic governance, and US-China tensions
- Cautious about massive stimulus packages involving the expansion of deficits

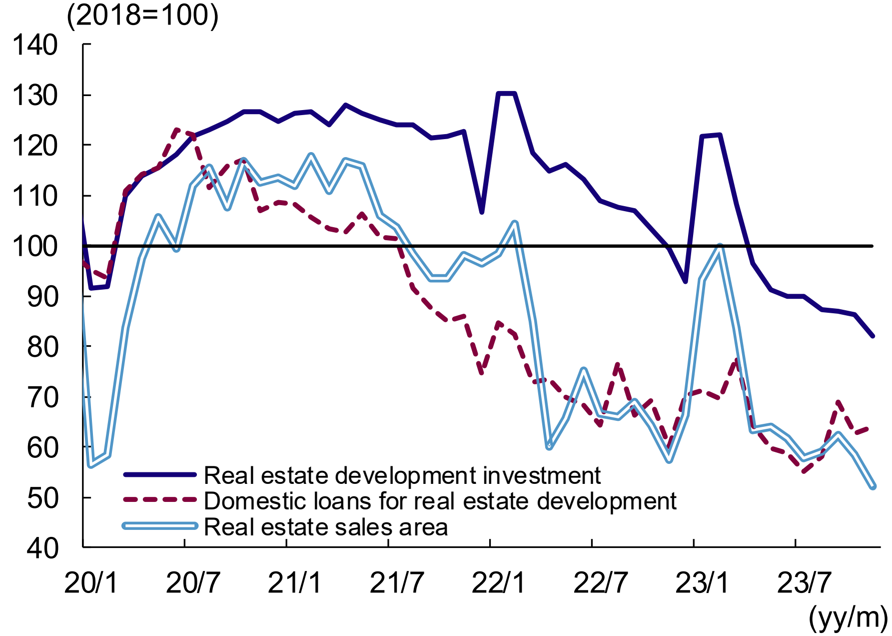
Impact of increasing government bond issuance and infrastructure investment
- Expanding infrastructure investment creating hidden debt in local financing platforms
- The banking sector remaining stable even with potential non-performing loans factored in

Source: Compiled by MHRT.

China: Real estate sector remaining sluggish; housing inventory adjustments completed in 2025 or later

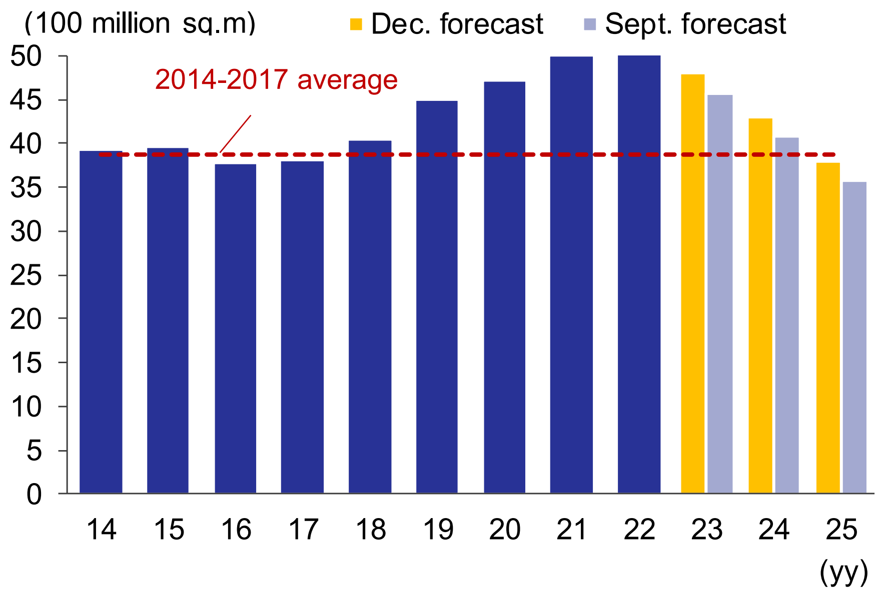
- Real estate sales and investments have gone from bad to worse. The measures introduced in August to stimulate actual demand have lost their effectiveness and recovery remains lackluster.
  - Domestic loans for real estate development have also been sluggish, with developers continuing to face fund shortages and pre-sold homes yet to be completed and delivered to their owners. These problems continue to dampen people's willingness to buy residential property.
- Housing inventory adjustments have been protracted as the sales slump persists, acting as a drag on China's economic recovery for years to come.
  - China's recent residential housing sales have averaged 940 million square meters per year, falling below the level of potential demand (1 to 1.3 billion square meters). Slumping sales have slowed the pace of housing inventory adjustments, which are likely to be completed in 2025 or later.

Real estate sales, lending, and investment



Note: Seasonally adjusted by MHRT.
Source: Compiled by MHRT based on data from the National Bureau of Statistics of China and CEIC.

Inventory of homes sold as of the year-end (estimated in 2023 and beyond)

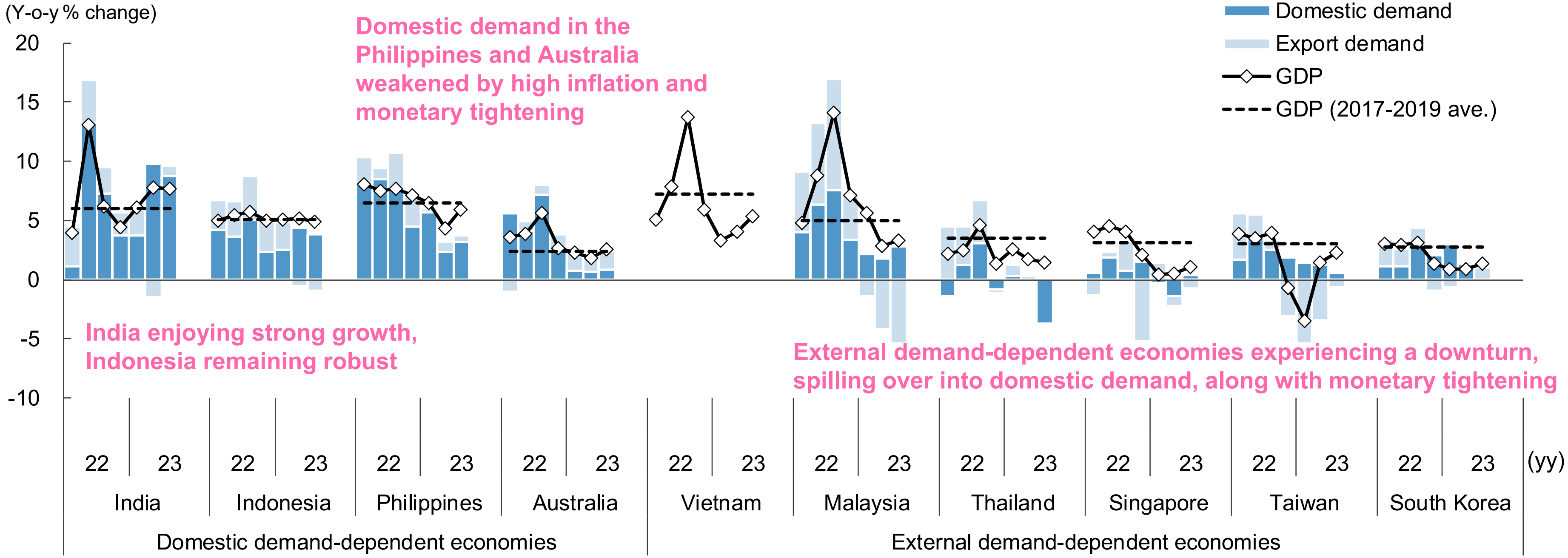


Note: Housing inventory = constructed areas + completed inventory - completed areas - reserved sales areas. The figures in 2023 and afterwards are calculated by adding newly constructed areas (annualized cumulative January-November 2023 total) to the previous year's housing inventory and subtracting demand (annualized cumulative January-November 2023 total sales areas of 940 million square meters and potential demand of 1.2 billion square meters in 2024-2025).
Source: Compiled by MHRT based on data from the National Bureau of Statistics of China and CEIC.

Asia: Slow recovery with continued monetary tightening and sluggish external demand

- Countries dependent on external demand continue to face an economic downturn.
  - Exports are showing signs of picking up, but not leading to a full-fledged recovery.
  - The impact of sluggish external demand has spilled over into employment and incomes in export-related sectors, and the combination with past monetary tightening has also weakened domestic demand.
- Polarization of domestic demand-dependent economies.
  - India and Indonesia see economic growth driven by domestic demand as inflations fall to their respective target levels.
  - In the Philippines and Australia, persistently high inflation and monetary tightening have resulted in a downturn in domestic demand.

Real GDP growth in Asian countries and regions

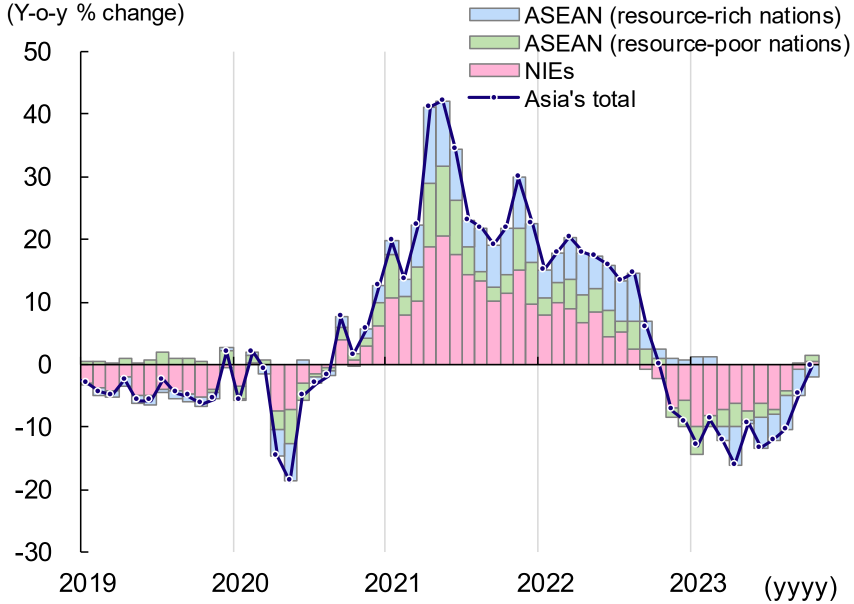


Source: Compiled by MHRT based on the GDP statistics of relevant countries and regions.

Asia: Semiconductor cycle picking up; full-fledged export recovery expected in mid-2024 or later

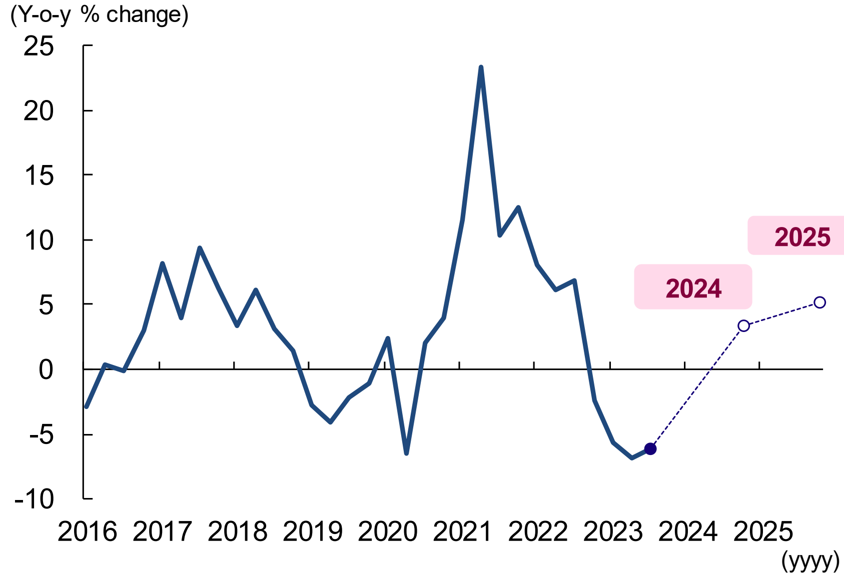
- Exports of emerging Asian economies (NIEs and ASEAN combined) have recovered to almost the same level as the previous year.
  - The recent rise in exports has been led by NIEs, with South Korea and Taiwan overcoming a major slump in semiconductors and IT products.
  - Resource-rich ASEAN economies have bottomed out year-on-year, but the pace of recovery remains slow
- NIEs' exports are picking up mainly to the US and China, but are expected to weaken again with the anticipated economic slowdown in the two countries.
  - Exports are rebounding with the US and China – both major demand engines – making progress in inventory adjustments, but exports from emerging Asian economies are likely to falter again in the first half of 2024 as the US economy is expected to slow. A full-fledge export recovery is projected in mid-2024 or later when the US economy bounces back.

Exports of emerging Asian economies (customs basis)



Note: ASEAN (resource-poor nations) refers to Thailand, Vietnam, and the Philippines, and ASEAN (resource-rich nations) represents Indonesia and Malaysia
Source: Compiled by MHRT based on the statistics of relevant countries and regions.

Real export projections for major NIEs and ASEAN economies



Note: The projections for South Korea, Taiwan, Singapore, Indonesia, Thailand, Malaysia, and the Philippines are estimated using key economic indicators, semiconductor sales, market indicators, and other data, and calculating the weighted average based on purchasing power parity.
Source: Compiled by MHRT based on the statistics of relevant countries and regions.

(4) Japan: Slow improvement in real wages, headwinds from slowing overseas economies, and moderate recovery

- Real GDP growth in FY2023 is estimated at +1.6% year-on-year, with negative growth in the July-September quarter due to weak domestic demand. The second half of the fiscal year will see personal consumption remain stagnant with rising prices and sluggish economic recovery with exports facing headwinds from overseas economic slowdown mainly in the US and Europe.
- Growth in FY2024 is projected at +1.1% year-on-year. While exports will pick up in the second half of the fiscal year in response to recoveries in overseas economies and the semiconductor market, service consumption and inbound tourism demand boosted by the easing of coronavirus concerns will come to a halt, and the rebound of automobile production driven by easing supply constraints will level off.
- Growth in FY2025 is forecast at +0.7% year-on-year. Personal consumption will lack strength due to sluggish growth in real employee compensation, and the growth rate is likely to slow toward the potential growth rate.

Outlook on the Japanese economy

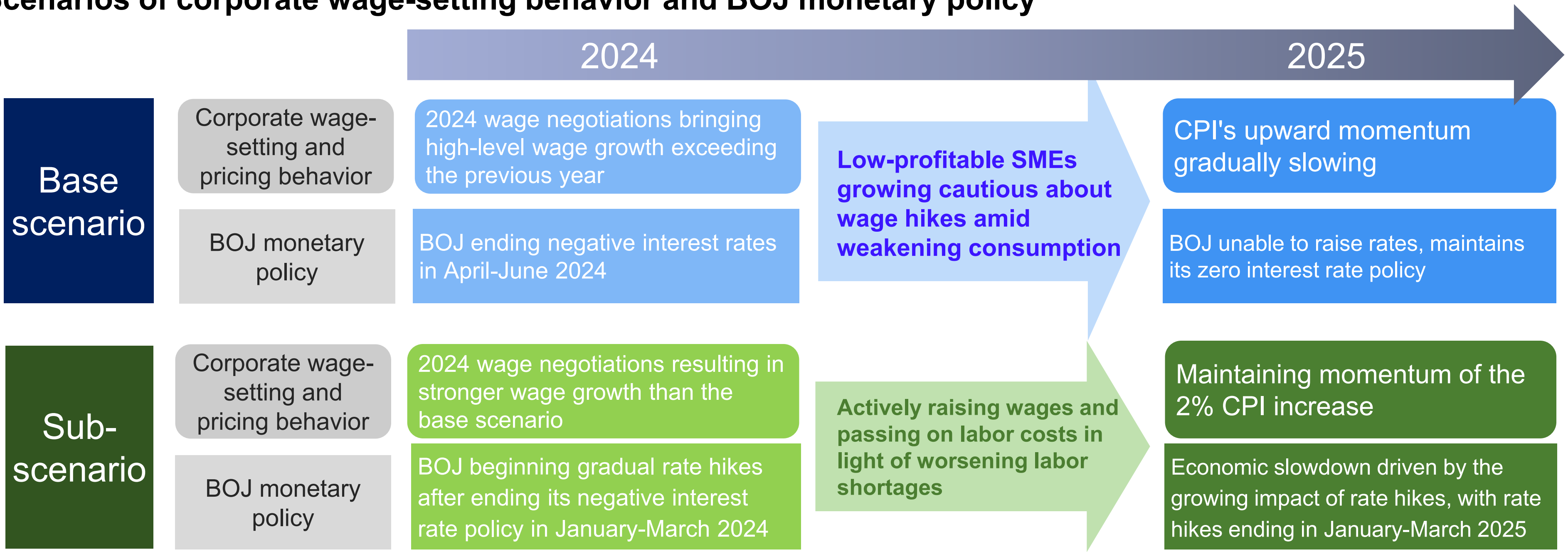
		2022	2023	2024	2025	2023				2024				2025				2026
		FY	(Outlook)			Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec	Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec	Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec	Jan-Mar
GDP (real)	Q-o-q % ch	1.5	1.6	1.1	0.7	1.2	0.9	-0.7	0.3	0.3	0.4	0.4	0.4	0.2	0.1	0.2	0.1	0.2
	Q-o-q % ch p.a.	—	—	—	—	5.0	3.6	-2.9	1.3	1.2	1.4	1.6	1.6	0.9	0.2	0.7	0.4	0.7
Domestic demand	Q-o-q % ch	2.0	0.2	1.1	0.7	1.6	-0.7	-0.6	0.3	0.4	0.4	0.4	0.3	0.2	0.1	0.2	0.2	0.2
Private-sector demand	Q-o-q % ch	2.7	-0.1	1.1	0.6	1.9	-1.0	-0.9	0.3	0.4	0.4	0.4	0.3	0.2	0.0	0.2	0.2	0.1
Personal consumption	Q-o-q % ch	2.7	0.1	1.0	0.5	0.9	-0.6	-0.2	0.1	0.3	0.3	0.4	0.2	0.1	0.1	0.1	0.1	0.1
Housing investment	Q-o-q % ch	-3.4	1.9	-0.3	-1.0	0.3	1.7	-0.5	-0.3	0.1	0.1	-0.1	-0.2	-0.2	-0.3	-0.3	-0.3	-0.2
Capital investment	Q-o-q % ch	3.4	0.1	1.7	2.1	1.8	-1.3	-0.4	0.7	0.6	0.1	0.5	0.7	0.6	0.5	0.5	0.5	0.6
Inventory investment	Q-o-q contribution, %pt	(0.1)	-0.2	0.0	(-0.1)	(0.7)	(-0.3)	(-0.5)	(0.0)	(0.0)	(0.1)	(0.0)	(0.0)	(-0.0)	(-0.1)	(0.0)	(0.0)	(-0.0)
Public-sector demand	Q-o-q % ch	-0.1	1.0	1.0	0.9	0.5	0.1	0.1	0.2	0.2	0.2	0.4	0.4	0.3	0.1	0.3	0.3	0.3
Government consumption	Q-o-q % ch	1.4	0.8	1.1	1.1	0.2	-0.1	0.3	0.2	0.2	0.2	0.3	0.3	0.3	0.3	0.3	0.3	0.3
Public investment	Q-o-q % ch	-6.1	2.7	0.9	0.3	1.9	1.5	-0.8	0.3	0.3	-0.2	0.6	0.5	0.3	-0.7	0.3	0.3	0.3
External demand	Q-o-q contribution, %pt	(-0.5)	(1.4)	(0.0)	(0.0)	(-0.4)	(1.6)	(-0.1)	(0.1)	(-0.1)	(-0.0)	(0.0)	(0.1)	(0.0)	(0.0)	(0.0)	(-0.1)	(-0.0)
Exports	Q-o-q % ch	4.7	2.8	1.3	2.7	-3.6	3.8	0.4	0.2	0.0	0.1	0.3	0.8	1.0	0.6	0.7	0.3	0.7
Imports	Q-o-q % ch	7.1	-3.1	1.1	2.4	-1.5	-3.3	0.8	-0.1	0.3	0.2	0.2	0.5	0.7	0.6	0.7	0.7	0.6
GDP (nominal)	Q-o-q % ch	2.3	5.3	2.5	1.7	2.2	2.6	-0.0	0.3	0.2	0.8	1.1	0.8	0.3	0.4	0.2	0.2	0.3
GDP deflator	Y-o-y % ch	0.9	3.6	1.3	0.9	2.3	3.8	5.3	3.3	2.2	1.0	1.1	1.6	1.6	1.6	0.8	0.5	0.7
Domestic demand deflator	Y-o-y % ch	3.2	2.3	1.1	0.8	3.2	2.7	2.6	2.0	1.9	1.3	1.1	0.9	0.8	0.9	0.8	0.8	0.8

Note: The figures in shaded areas are forecasts.
Source: Compiled by MHRT based on the Cabinet Office, *Quarterly Estimates of GDP*.

Japan: Businesses cautious about sustained wage hikes and cost pass-through; CPI's upward momentum gradually slowing

- [Base scenario] Annual spring wage negotiations in 2024 will produce higher-level results than the previous year, but low-profitable SMEs will gradually grow cautious about raising wages in FY2025 as personal consumption lacks strength. The consumer price index (CPI) will slowly lose upward momentum, with the core CPI falling below 2% in FY2025. The BOJ will maintain its zero interest rate policy after ending negative rates in April-June 2024.
- [Sub-scenario] The 2024 wage negotiations will result in stronger wage growth than the base scenario. Sustained wage hikes and pass-through of labor costs (norm changes in wages and pricing behavior) will continue in light of worsening labor shortages, thereby achieving the momentum for a CPI uncrease of 2%. The BOJ will raise interest rates in phases after ending negative rates in January-March 2024, and will stop rate hikes at a policy rate of 1% in January-March 2025 in response to an economic slowdown.

Scenarios of corporate wage-setting behavior and BOJ monetary policy



Source: Compiled by MHRT.

Japan: 2024 wage negotiations producing year-on-year growth; SMEs under pressure to hike wages

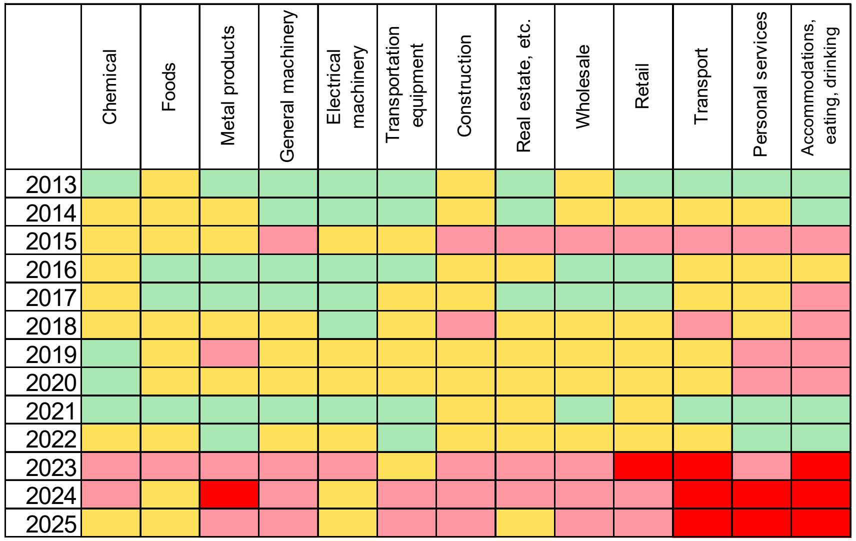
- Labor unions plan to strongly push for wage hikes in the FY2024 wage negotiations.
  - Japan's largest union, RENGO, revised its plan to push for pay raises of at least 5%, expressing a stronger demand than in 2023. All industrial unions will also press for higher wages.
- SMEs are under strong pressure to hike wages.
  - A heat map of wage hike pressure on SMEs based on labor supply and demand by industry, wage gaps with large companies, and past inflation rates illustrates that the pressure to hike wages is particularly strong in personal consumption-related industries (personal services, accommodations, and eating and drinking services) that face tight labor supply and demand as well as the transport industry, where the wage gap with large companies is widening.

Plans to demand higher wages in the 2024 wage negotiations

2023 wage negotiations	**2024 wage negotiations**
RENGO	
About 5% (wage hikes including periodic pay raises)	**At least 5%** (wage hikes including periodic pay raises)
Japan Council of Metalworkers' Unions (JWA, JEIU, etc.)	
Monthly pay hike of at least 6,000 yen (base pay)	**Monthly pay hike of at least 10,000 yen** (base pay)
UA ZENSEN (retail, restaurant, leisure industries, etc.)	
Seeking about 6% (wage hikes including periodic pay raises)	**Setting a 6% target** (wage hikes including periodic pay raises)
All Japan Federation of Transport Workers' Unions (trucking, etc.)	
Monthly pay hikes of 13,700 yen (wage hikes including periodic pay raises)	**Monthly pay hikes of 15,000 yen** (wage hikes including periodic pay raises)

Source: Compiled by MHRT based on data from RENGO and relevant media reports.

Heat map of wage hike pressure on SMEs



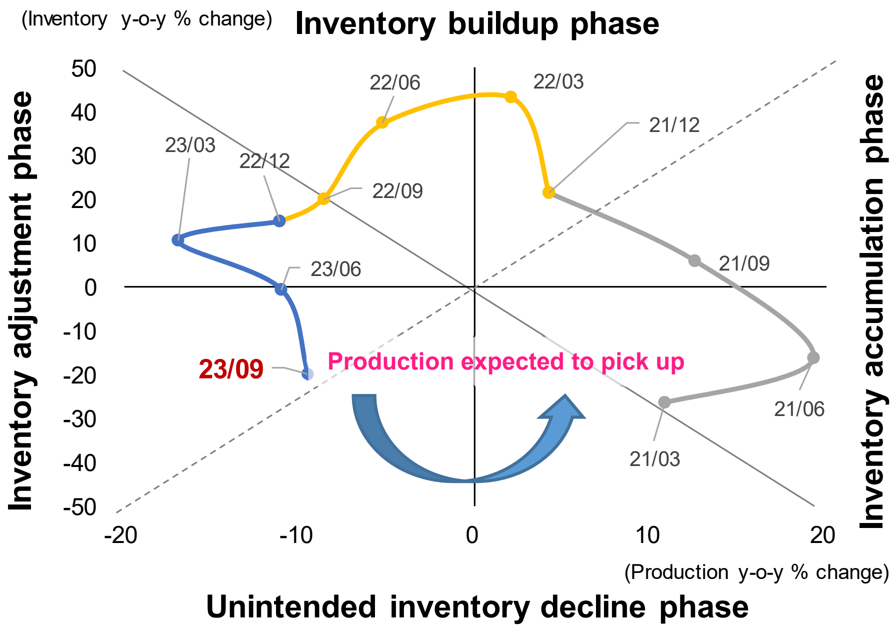
Note: Red represents extra-high pressure, pink high pressure, yellow medium pressure, and green low pressure. Based on labor supply and demand (Tankan, diffusion index (DI) for employment conditions), the wage gap between large companies and SMEs, and inflation rates. The heat map assumes the wage gap will remain unchanged from the current level, and the employment conditions DI will expand toward "insufficient" by 1 percentage point each year. Inflation rates are forecast by MHRT.

Source: Compiled by MHRT based on data from the Ministry of Finance, Ministry of Internal Affairs and Communications, and Bank of Japan.

Japan: Capital investment rising moderately in FY2024; downward pressure driven by ongoing supply constraints

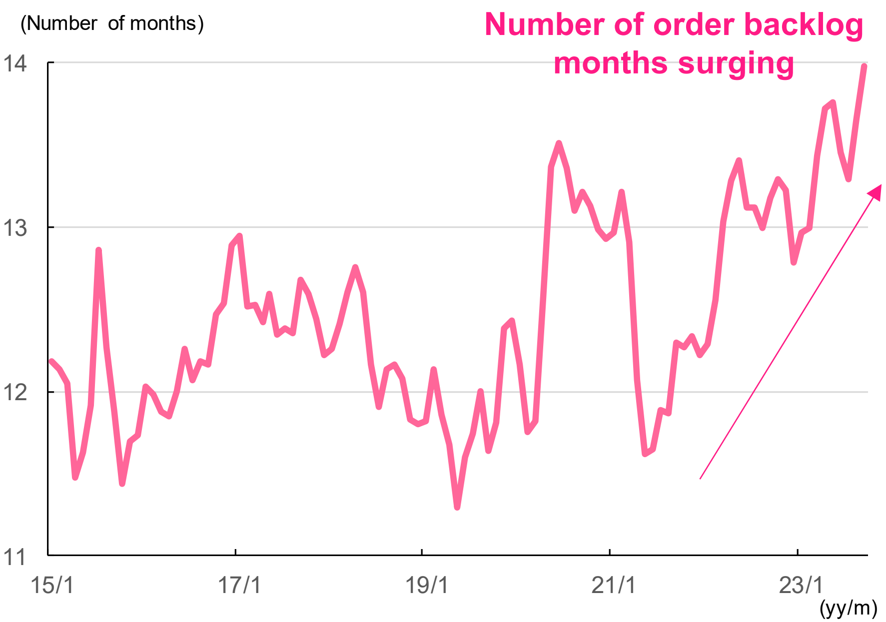
- Capital investment will pick up moderately from the second half of FY2023 through FY2024, accompanied by rebounding demand and easing of rising costs.
  - In terms of (1) insufficient demand, the semiconductor-related industry will enter the final phase of inventory adjustments, likely paving the way for recovering in FY2024. In addition, improving terms of trade between businesses are expected to ease the issue of (2) rising costs.
  - However, supply constraints will likely extend the months of machinery order backlogs (period required to eliminate order backlogs). Downward pressure driven by supply constraints, mainly (3) labor shortages, is expected to remain through FY2024.
  - Real capital investment is projected to mark a moderate increase of +0.1% in FY2023 and +1.7% in FY2024.

Inventory cycle of electronic component and device industries



Source: Compiled by MHRT based on the Ministry of Economy, Trade and Industry, *Indices of Industrial Production*.

Number of months of machinery order backlogs



Note: Backlog months = order backlogs at the end of month divided by average sales in the previous three months.
Source: Compiled by MHRT based on the Cabinet Office, *Machinery Orders*.

(5) Financial markets: BOJ’s tightening of its monetary policy triggering higher yen interest rates, a stronger yen, and lower stock prices; US stocks and interest rates rising

- The BOJ will implement the triple lifting of negative interest rates, yield curve control (YCC), and monetary base expansion policy in the April-June 2024 quarter. Japan’s long-term interest rates are likely to be in the lower 1% range after the BOJ ends its negative interest rate policy.
- US long-term interest rates will rise close to 4% from the second half of 2024 through the first half of 2025, then retreat to the upper 3% range. In terms of the dollar-yen exchange rate, the yen is expected to strengthen to the upper 120-yen per dollar range on the back of the narrowing gap in interest rates between Japan and the US.
- US stocks are projected to generally maintain an upward trend, though they may temporarily falter toward mid-2024. Japanese stocks are expected to decline through mid-2024 on the back of a stronger yen, before rallying in the second half of 2024 and beyond.

Outlook on financial markets

		2022	2023	2024	2025	2023				2024				2025				2026
		FY	FY	FY	FY	Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec	Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec	Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec	Jan-Mar
Japan																		
Interest rate on the policy rate balance	(End-of-period value, %)	- 0.10	- 0.10	0.00	0.00	- 0.10	- 0.10	- 0.10	- 0.10	- 0.10	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Newly issued JGBs	(10-year, %)	0.29	0.35 to 1.00	0.90 to 1.50	0.75 to 1.30	0.44	0.42	0.60	0.50 to 1.00	0.65 to 1.10	1.00 to 1.50	1.00 to 1.50	0.90 to 1.40	0.90 to 1.40	0.90 to 1.40	0.80 to 1.30	0.80 to 1.30	0.75 to 1.25
Nikkei Stock Average	(JPY)	27,272	27,427 to 35,000	28,000 to 35,900	30,500 to 38,900	27,291	30,469	32,517	30,400 to 34,000	29,800 to 35,000	28,000 to 33,000	29,000 to 34,000	30,000 to 35,000	30,100 to 35,900	30,500 to 36,700	31,100 to 37,300	31,800 to 38,200	32,300 to 38,900
US																		
Federal Funds Rate (lower end)	(End-of-period value, %)	4.75	5.25	4.25	3.25	4.75	5.00	5.25	5.25	5.25	5.00	4.75	4.50	4.25	4.00	3.75	3.50	3.25
Newly issued government bonds	(10-year, %)	3.37	3.31 to 5.05	3.35 to 4.30	3.45 to 4.35	3.65	3.59	4.14	3.65 to 5.05	3.50 to 4.60	3.35 to 4.15	3.50 to 4.20	3.55 to 4.25	3.60 to 4.30	3.65 to 4.35	3.60 to 4.30	3.50 to 4.20	3.45 to 4.15
Dow Jones Average	(USD)	32,549	30,800 to 39,000	33,200 to 40,800	35,600 to 43,400	33,219	33,643	34,669	32,300 to 38,000	33,300 to 39,000	33,200 to 38,400	33,800 to 39,200	34,600 to 40,200	35,200 to 40,800	35,600 to 41,200	36,200 to 42,000	36,900 to 42,700	37,400 to 43,400
Eurozone																		
ECB deposit facility rate	(End-of-period value, %)	3.00	4.00	2.25	2.00	3.00	3.50	4.00	4.00	4.00	3.75	3.25	2.75	2.25	2.00	2.00	2.00	2.00
German government bonds	(10-year, %)	1.73	1.80 to 3.00	1.80 to 2.80	2.15 to 2.90	2.34	2.37	2.59	1.80 to 3.00	1.80 to 3.00	1.80 to 2.65	1.90 to 2.70	2.05 to 2.75	2.10 to 2.80	2.15 to 2.85	2.15 to 2.85	2.20 to 2.90	2.20 to 2.90
Exchange rates																		
USD/JPY	(JPY/USD)	135	130 to 152	120 to 148	122 to 136	132	138	145	140 to 152	134 to 148	131 to 143	125 to 137	120 to 132	123 to 135	122 to 134	123 to 135	124 to 136	124 to 136
EUR/USD	(USD/EUR)	1.04	1.04 to 1.13	0.96 to 1.19	1.04 to 1.21	1.07	1.09	1.09	1.04 to 1.12	1.00 to 1.12	0.98 to 1.10	0.96 to 1.08	0.99 to 1.11	1.02 to 1.14	1.04 to 1.16	1.06 to 1.18	1.07 to 1.19	1.09 to 1.21

Source: Compiled by MHRT based on data from Bloomberg.