



The Japan Report

EY Consulting Japan

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Economy

Q1 economic results were mixed. GDP fell 1.0%, a drop of 3.9% at an annualized rate as a renewed COVID-19 state of emergency led to a reduction in consumer spending. The Coincident Index (CI) and Industrial Production (IPI) continued to recover in the first quarter; CI rising 3.2% and IPI rising 2%. Japan's exports rose 16.1% annually in March, mainly driven by exports to China. However, the Q1 balance of trade surplus saw a significant drop (-72%) as exports declined 1% while imports rose 7%.

COVID-19

After a spike in January, new COVID-19 cases declined rapidly until a second spike necessitated extensions of states of emergencies in several prefectures. Increased restrictions on dining out and alcohol consumption in Tokyo and Osaka have proved successful in reducing cases. Vaccinations have started in earnest. By 7 June 2021, 13.85 million people have been vaccinated and it appears the fourth wave is over.

Geopolitics and trade

The Upper House passed Digital Reform Bills on 12 May. One of these bills establishes a digital agency. The new governmental agency will be responsible for standardizing 17 different core systems used among the governmental agencies, including one for social security. It will promote the digitization of administrative works and raise the effectiveness of government services.

Politics

On 11 May, the House of Representatives passed amendments to the Referendum Law, which stipulates the procedures for revising the constitution. The House of Councilors plans to pass the proposed amendments by 16 June, the end of the current Diet session. The proposed amendments to the constitution aim to improve the ease of voting, adding train stations and commercial facilities as polling stations.

Olympics

Rising COVID-19 cases are causing public concern. Only a minority of the Japanese citizens support the Olympics to go ahead. Nonetheless, the Japanese government says the Olympics will proceed. COVID-19 vaccinations are ramping up now. Hopefully, this will alleviate some of the widespread public concern, and we can experience a great TOKYO 2020.

1 COVID-19

The third state of emergency was extended to 20 June which has had the desired effect with case numbers dropping rapidly. Daily vaccination rates now hitting 0.7 million.

Source: "Japan to Approve Moderna Vaccine as Soon as May 21, Yomiuri Says", Bloomberg, <https://www.bloomberg.com/news/articles/2021-05-01/japan-to-approve-moderna-vaccine-as-soon-as-may-21-yomiuri-says>, accessed 1 May 2021; "Coronavirus (COVID-19): 'Open Data'", The Ministry of Health, Labour and Welfare, <https://www.mhlw.go.jp/stf/covid-19/open-data.html>, accessed 3 June 2021; "COVID-19 vaccines", Prime Minister's Office of Japan, <https://www.kantei.go.jp/jp/headline/kansensho/vaccine.html>, accessed 3 June 2021.

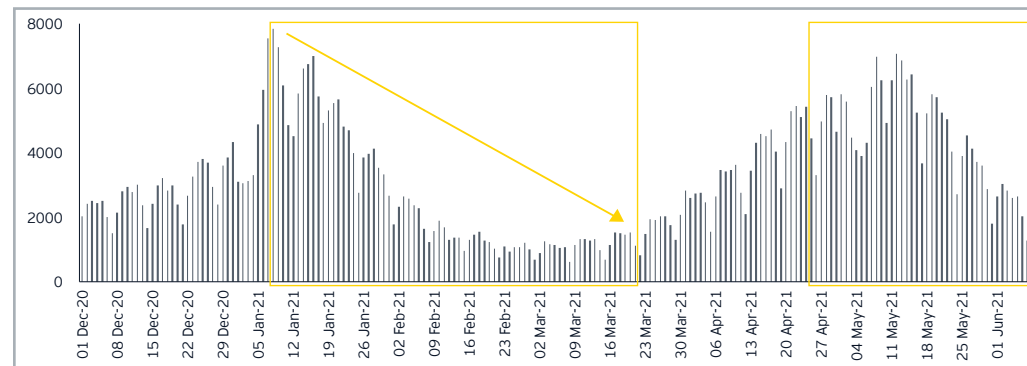
1. Update on COVID-19 - state of emergency

- On 25 April 2021, the government declared a state of emergency (SOE) in Tokyo, Osaka, and surrounding areas originally to 11 May. This has subsequently extended to 20 June. On 10 June 2021, the government plans to withdraw the anti-corona measures it had taken in Gunma, Ishikawa and Kumamoto prefectures.
- In the fourth wave of the COVID-19, more cluster infections occurred at offices and schools than in the previous waves. Even under the third state of emergency, the government did not require schools to close nor companies to enforce the work-from-home policy. During previous COVID-19 waves, infections mainly occurred in hospitals, restaurants, and bars. As a result stricter anti-virus measures were introduced. The government prohibited restaurants and bars from serving alcohol, offering karaoke services, and opening after 8pm. Non-compliance can result in a fine of up to 300,000 yen.
- These measures have had the desired effect and as of 7 June the number of new COVID-19 cases has dropped to 1,273, and it appears the fourth wave is over.

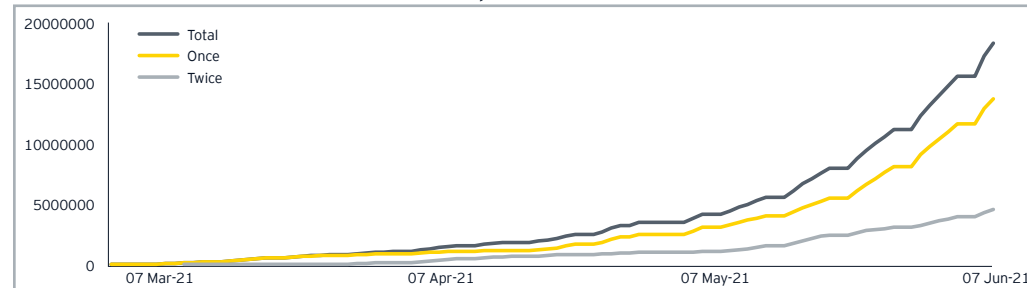
2. Schedule of Vaccination for COVID-19

- Vaccinations to healthcare workers began on 17 February and to those over 65 years old on 12 April. Vaccines now becoming available to citizens in many prefectures. By 7 June, roughly 10.97% (13.75million) of the total population has been vaccinated at least once.

The number of new COVID-19 cases (Yellow indicates under the SOE)



The number of vaccines administered in Japan



2 Politics, economic policy and Olympic update

Steady steps toward constitutional reform and digitalization.

Source: "The Referendum Law", Nikkei, <https://www.nikkei.com/article/DGXZQOUA051BB0V00C21A5000000/>, accessed 3 June 2021; "Quantum technologies", Nikkei, <https://www.nikkei.com/article/DGKKZ071581360U1A500C2TJC000/>, accessed 3 June 2021; "The establishment of a digital agency", Nikkei, <https://www.nikkei.com/article/DGXZQOUA064BB0W1A400C2000000/>, accessed 3 June 2021; "RCEP", Nikkei, <https://www.nikkei.com/article/DGXZQOUA27E3L0X20C21A4000000/>, accessed 3 June 2021; "The research fund guideline published by the Japanese government", Nikkei, <https://www.nikkei.com/article/DGXZQODE241540U1A420C2000000/>, accessed 3 June 2021; "Anti-Olympic petition", Nikkei, <https://www.nikkei.com/article/DGXZQOUE214T30R20C21A5000000/>, accessed 3 June 2021.

Movement toward constitutional reform

On 11 May, the House of Representatives passed amendments to the Referendum Law, which stipulates the procedures to revise the Constitution. The House of Councilors plans to pass the proposed amendments by 16 June, the end of the current Diet session. The proposed amendments aim to improve the ease of voting, adding train stations and commercial facilities as polling stations. In revising the Constitution, the Diet is likely to discuss the position of the Self-Defense Forces.

Industrial policy for the utilization of quantum technology

On 9 March 2021, the supercomputer Fugaku started its operation. It has been used for COVID-19 countermeasures and is expected to be used commercially.

The government will launch a joint research project on quantum technology for information processing and communications with approximately 50 Japanese companies by the end of May. Japan is leading in quantum communication and cryptography technology, areas directly related to national security. The public and private sectors are working together to accelerate the practical application of this technology.

Japan to promote digitization, enhancing cybersecurity and privacy

The House of Councilors passed the Digital Reform Bills on 12 May, one of which establishes a digital agency. The new governmental agency will be responsible for standardizing 17 different core systems used among the governmental agencies, including one for social security. It will promote the digitization of administrative works and raise the effectiveness of government services.

Foreign affairs and security

Japan is strengthening economic ties with countries in the Asia Pacific. On 28 April, the Regional Comprehensive Economic Partnership Agreement (RCEP), the first free trade agreement between Japan, China, South Korea and 12 other countries, was approved by the Japanese Diet. It has been approved by China and Singapore as well. RCEP is expected to enter into force by the end of this year.

From a national security perspective, the Japanese government will require researchers to declare their relations with foreign companies to prevent technology theft when they receive public funding. The government is concerned that artificial intelligence (AI) and quantum technology may be stolen and diverted for military use in other countries. The US and Japan have cooperated in biotechnology, AI, and quantum technology. The US fears that a third country may steal its technologies through Japan. The Japanese government aims to enhance the protection of R&D information, secure the research environments, and further promote international research alliances.

Tokyo Olympics and Paralympics

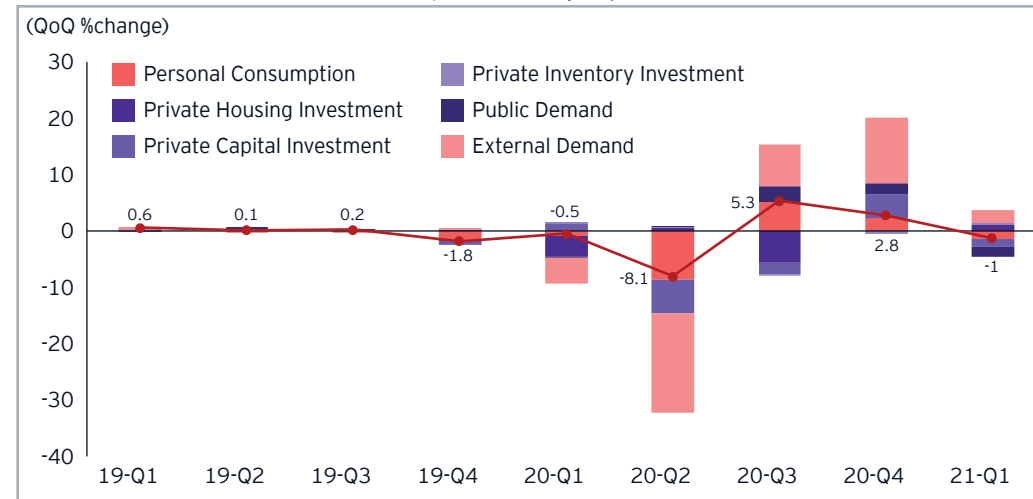
The Japanese Olympic Committee is preparing to hold the games without an audience. Citizens have negative opinions about organizing the Olympics during the COVID-19 pandemic – a signature campaign asking to cancel the Olympics collected 300,000 signatures in four days. Some local governments have canceled pre-camps due to the difficulty in setting up their medical system. President Bach of the International Olympic Committee (IOC) had planned to visit Japan on 17 May, but he postponed the visit due to the extension of the third state of emergency. The Tokyo and Japanese governments and the IOC keep pushing to have the games, while many Japanese citizens cannot stop worrying about a possible spread of the COVID-19 and the risk of healthcare collapsing.

3 Macroeconomic trends

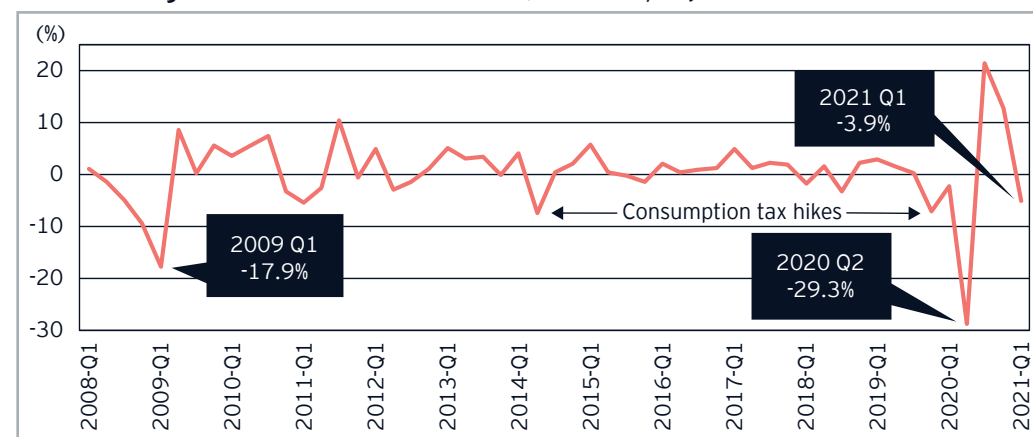
Japan's GDP decreased 1.0% in Q1 2021 compared to Q4 of 2020. The decline in Japan's GDP in FY2020 was 4.6%, the largest decline in the postwar period.

- Japan's GDP decreased 1.0% in Q1 compared to Q4 in real terms. The annualized growth rate of -3.9% is below the 16.6% growth rate in Q4 of 2020. The reason for this decline is the state of emergency that lasted from 8 January to 21 March 2021. Private consumption, especially services, including eating out, has fallen.
- The GDP growth rate in FY2020 was -4.6%, the largest decline in the postwar period. It is the first contraction since FY2008 when the economic growth was -3.6% due to the global financial crisis in that year.

Contribution to real GDP (% , %pt seasonally adjusted basis)



Real GDP growth rate (QoQ Annualized, seasonally adjusted basis)



Source: "GDP", Cabinet Office, <https://www.esri.cao.go.jp/sna/menu.html>, accessed 8 June 2021, "GDP", NHK, <https://www3.nhk.or.jp/news/html/20210518/k10013036691000.html>, accessed 3 June 2021, "GDP", Nikkei, <https://www.nikkei.com/article/DGXZQQUA178DKOX10C21A5000000/>, accessed 3 June 2021

The economic situation

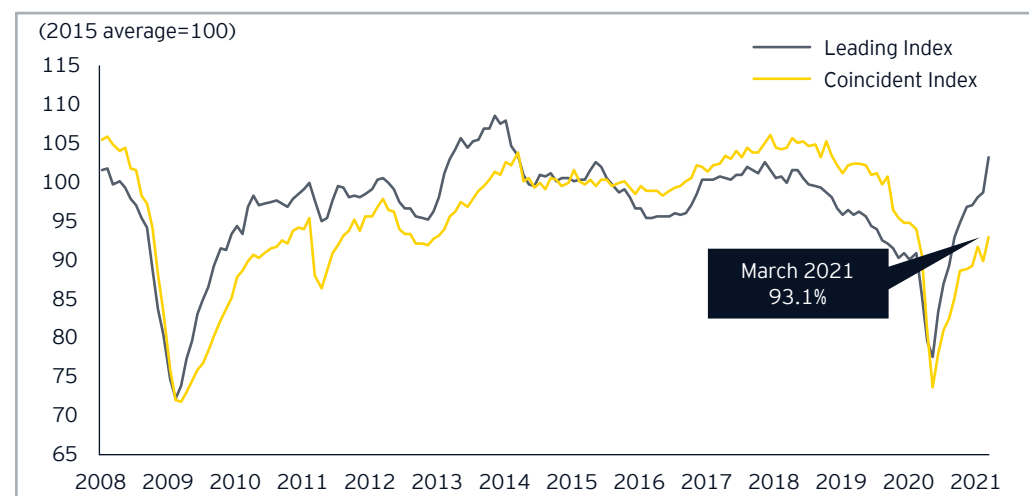
Business conditions and industrial production

The Coincident Index (CI) and Industrial Production (IPI) have continued to recover in the Q1 of 2021.

The coincident index of business conditions has improved. It rose 3.2 points from the previous month in March to 93.1.

The industrial production index in March rose 2.0% from the previous month to 97.7. According to the Manufacturing Production Forecast Survey, which surveys the production plans of major companies, April is expected to show continued recoveries with a month-on-month increase of 8.4%, while May is expected to show a month-on-month decline of -4.3%.

CI* Coincident Index of business conditions

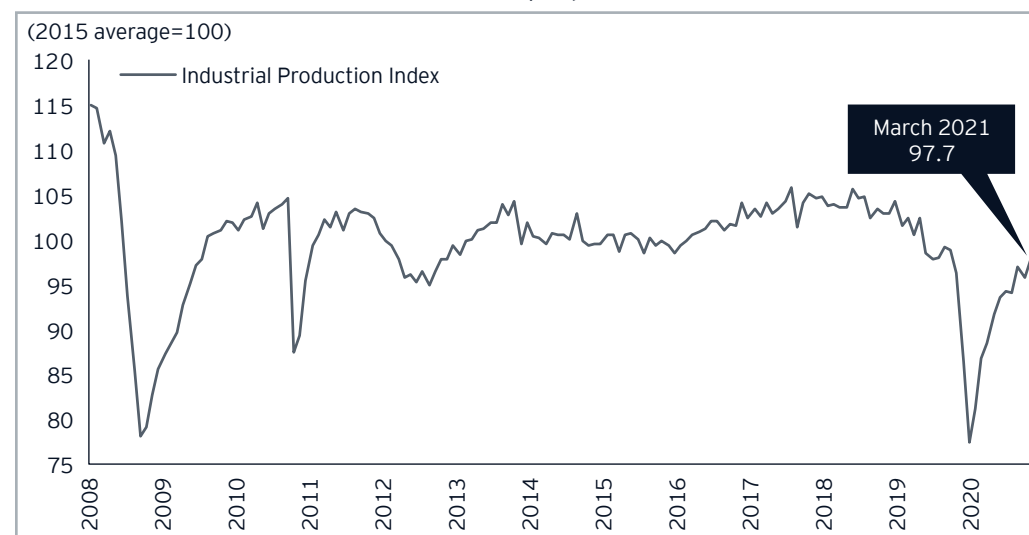


* The Composite Indexes (CI) mainly aim to measure the tempo and the volume of economic fluctuations. They compose the quantitative changes in indicators such as factory output, employment and retail sales data that are sensitive to business cycle movements.

* Leading Index tends to precede the coincident CI by a few months. It is used to forecast changes in the direction of the economy in the upcoming months.

Source: "The coincident index of business conditions", Cabinet Office, <https://www.esri.cao.go.jp/jp/stat/di/di.html>, accessed 3 June 2021

Industrial Production Index (seasonally adjusted)



Source: "The industrial production index", Ministry of Economy, Trade and Industry, <https://www.meti.go.jp/statistics/tyo/iip/index.html>, accessed 3 June 2021, Ministry of Economy, Trade and Industry

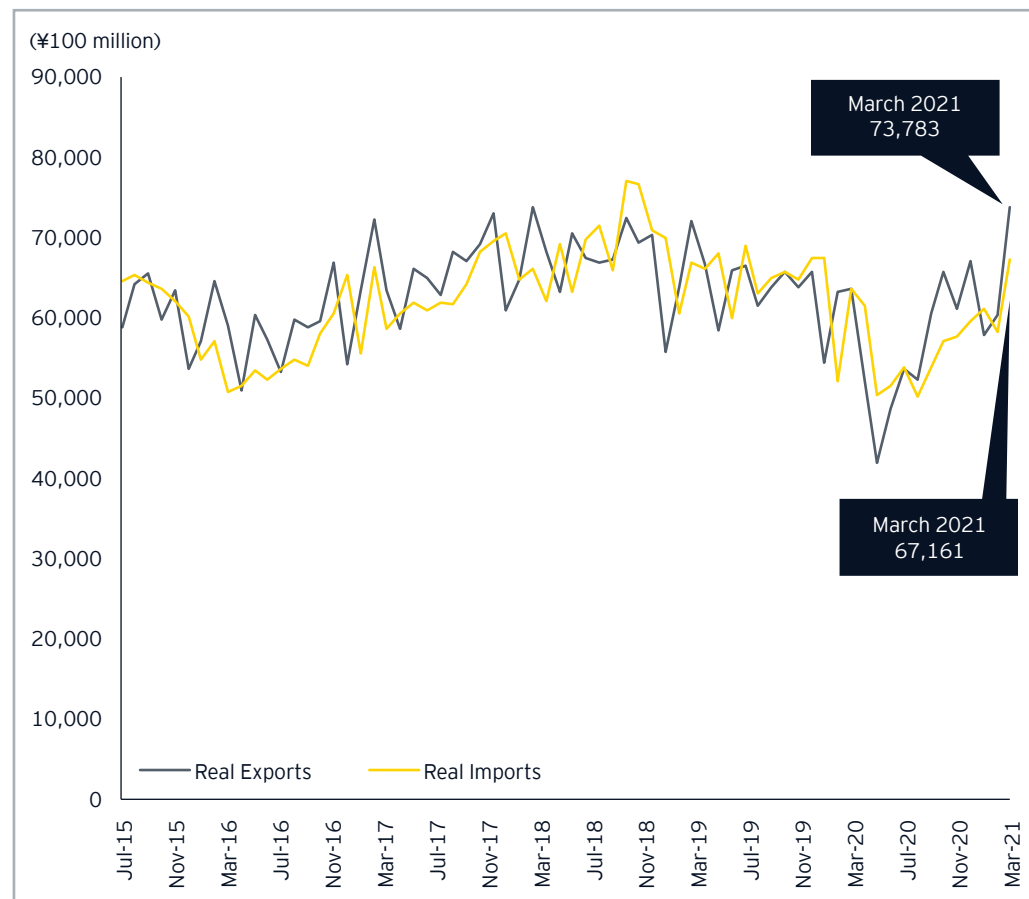
The economic situation

Foreign trade

Japan's exports rose 16.1% annualized in Q1, mainly driven by exports to China. The balance of trade surplus dropped 72% as exports declined 1% while imports rose 7% this quarter.

- ▶ Japan exports rose 16.1% on an annual basis in March 2021. Total exports between April 2020 to March 2021 have fallen 8.4% compared to exports between April 2019 and March 2020.
- ▶ Exports in Q1 of 2021 declined 1% compared to Q4 in 2020. Imports rose 7%, which contributed to a decline of the trade surplus by 72% compared to Q4 of 2020.
- ▶ Imports increased in Q1 of 2021 because the drop in consumer spending was more than offset by a recovery in industrial production. Exports to China fell 332.3 billion yen while exports to the rest of the world rose 142.4 billion yen, resulting in a decline in total exports of 189.9 billion yen in Q1.

Export/Import



Source: "Export/Import", Ministry of Finance, <https://www.customs.go.jp/toukei/info/>, accessed 3 June 2021

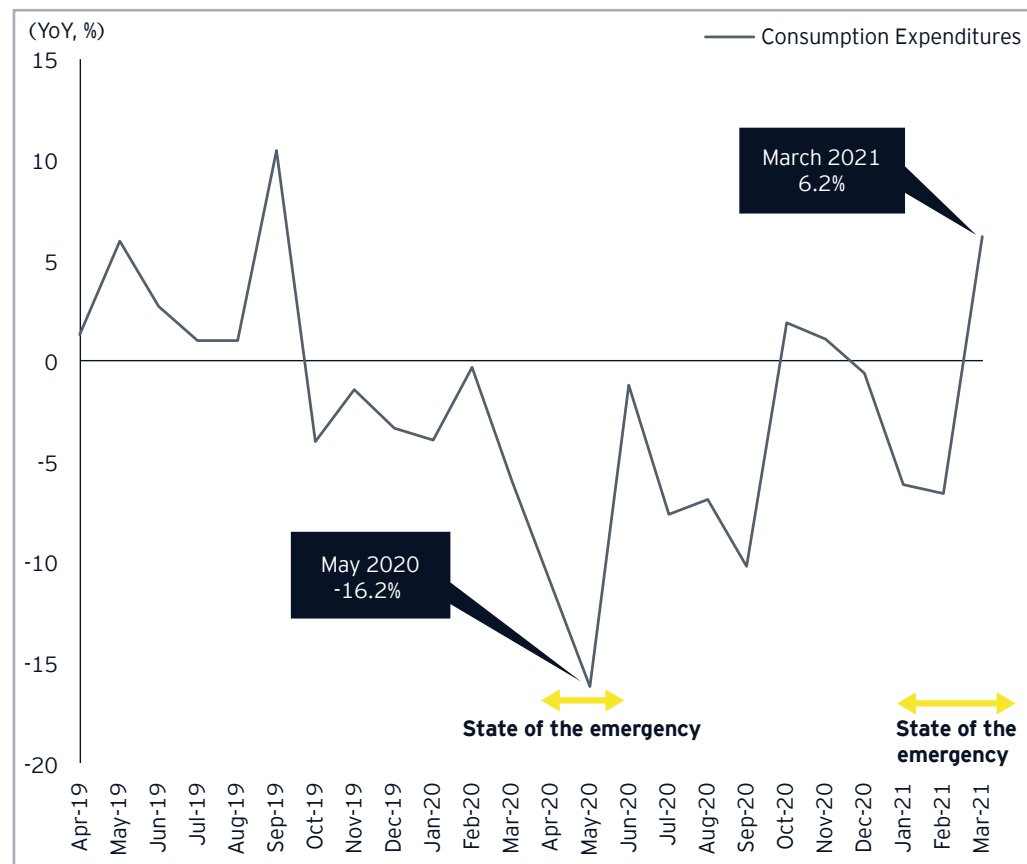
The economic situation

Consumption

Household spending rose in March 2021 to 6.2% in real terms YoY, the first increase in four months.

- ▶ In March 2021, the average household consumption expenditure rose 6.2% YoY. This rise was relative to a strong decline in consumption in March 2020, when the number of COVID-19 cases surged, and the government asked people to stay home. Therefore, this improvement doesn't show an actual improvement in daily life compared to March 2020.
- ▶ The previous year saw increased spending on maintenance and repair of residential facilities, tuition fees, durable goods for education and entertainment, electricity, water and sewage charges, insurance and medical services and clothing. In terms of individual items, increases in personal computers, televisions, Internet connection fees and accommodation fees pushed up the figures.
- ▶ On the other hand, automobile-related expenses decreased. Food prices remained unchanged. Among individual items, rice, instant noodles and toilet paper, which consumers hoarded last year, decreased.

Consumption expenditure (real, two-or-more-person households)



Source: "Consumption expenditure", Ministry of Internal Affairs and Communications, <https://www.stat.go.jp/data/kakei/sokuhou/tsuki/index.html>, accessed 3 June 2021

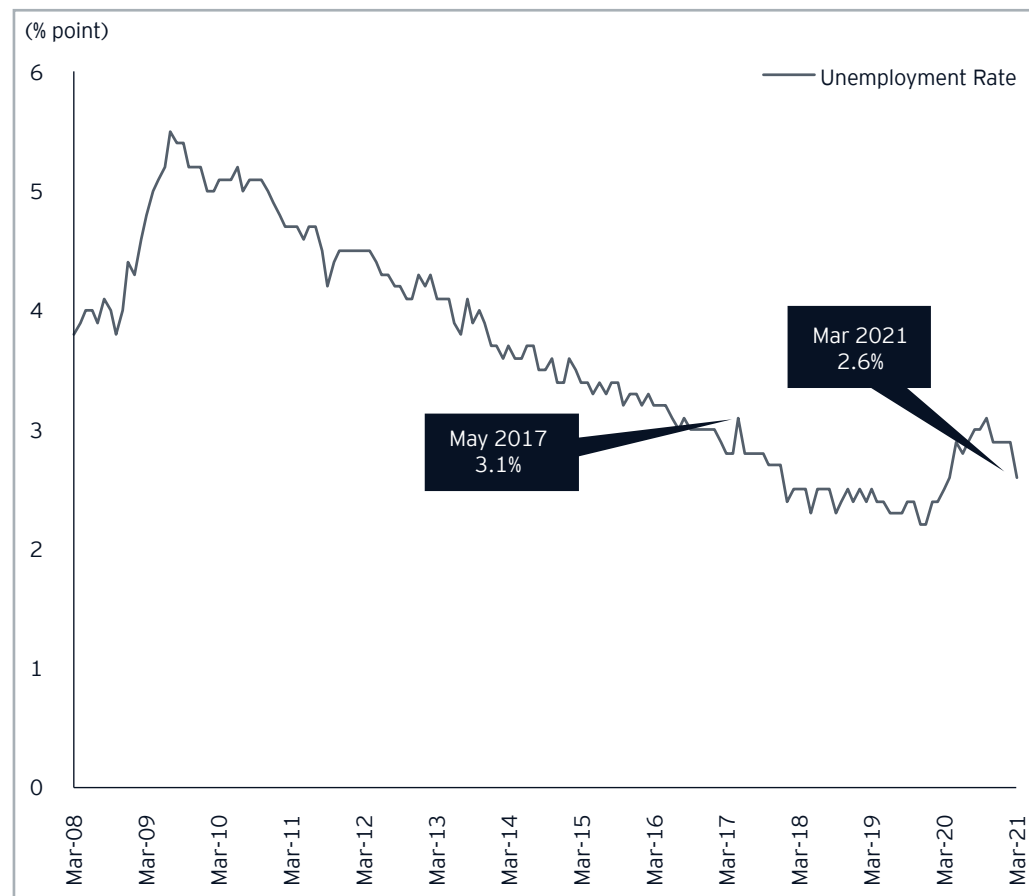
The economic situation

Employment

The unemployment rate fell by 0.2% in Q1 compared Q4 last year. Recovery in IT, education, and medical services contribute to this decline.

- ▶ The unemployment rate fell by 0.2% Q1 compared to Q4. The number of people employed in accommodation and restaurant services has decreased while it has increased in IT, education and medical services. The number of persons who were let go by their employers decreased while the number of persons looking for a job has increased in quarter.

Unemployment rate (seasonally adjusted)



Source: "Labour Force Survey", The Ministry of Internal Affairs and Communications, Statistic Bureau of Japan, <https://www.stat.go.jp/data/roudou/index.html>, accessed 3 June 2021

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