

Yen 4Sight

Highlights

- Indicators released this week provided further assurance that private consumption rebounded in Q4.
- Bonus payments helped labour income growth pickup further in December.
- But the Economy Watchers Survey and PMIs caution that the economy likely had a soft start to this year.
- The coming week brings the preliminary national accounts for Q4. We expect real GDP to have rebounded 0.5%Q/Q.

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Interest and exchange rate forecasts

End period	8 Feb	Q119	Q219	Q318
BoJ ONR %	-0.10	-0.10	-0.10	-0.10
10Y JGB %	-0.3	0.00	0.00	0.00
JPY/USD	110	109	110	108
JPY/EUR	125	125	126	123

Source: Bloomberg, BoJ and Daiwa Capital Markets Europe Ltd.

A decent end to 2018, but concerns about Q119

While many regional markets were closed for the Lunar New Year holiday, global sentiment soured somewhat in the past week as the likelihood of a quick US-China trade deal diminished against the backdrop of poor economic data and downgrades to GDP forecasts in Europe and Australia. That shift was reflected in a weakening of Japan's equity indices and a step down in 10Y JGB yields further below zero percent. And while Japan's data flow provided further assurance that a return to positive growth will be confirmed in the coming week's preliminary estimate of Q4 GDP, sentiment indicators again raised concerns about prospects for the current quarter.

Consumer spending lifts in December

A key focus ahead of the national accounts was the strength of consumer spending during the fourth quarter – expected to be a key driver of a rebound in overall activity. Helpfully, the BoJ released its December consumption activity index – a guide to private consumption spending bettered only by the less timely Cabinet Official Synthetic Consumption Index. The BoJ's index – which is constructed using both demand- and supply-side indicators – increased 0.5%M/M in real terms in December. And with the previous month's estimated decline halved to 0.3%M/M, this meant that annual growth improved to 1.3%Y/Y – the second best reading of 2018 – from an upwardly-revised 0.8%Y/Y in November.

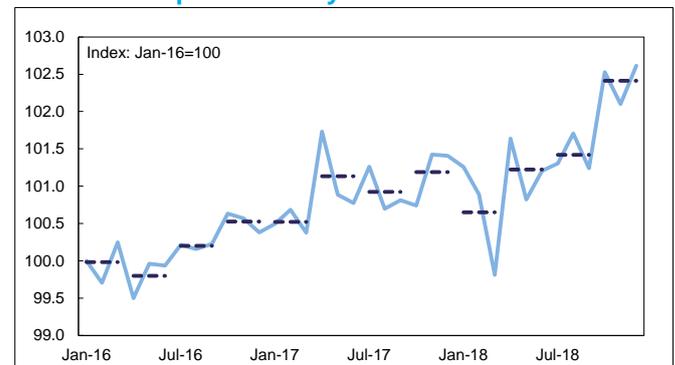
BoJ index suggests robust spending growth in Q4

Within the detail, a decline of just 0.1%M/M in spending on services was more than outweighed by a 1.8%M/M rebound in spending on durable goods, while spending on non-durable goods also rose a very solid 1.0%M/M. Meanwhile, the travel-adjusted real index – which conceptually aligns most closely with the national accounts measure of private consumption by removing the net spending of tourists – also rose 0.5%M/M in December following a smaller-than-previously-estimated 0.4%M/M decline in November. As a result, spending on this measure rose 1.0%Q/Q in Q4 – a result that clearly points to the likelihood of a healthy rebound in the national accounts measure of private consumption during the quarter.

Core household spending also up at end-2018

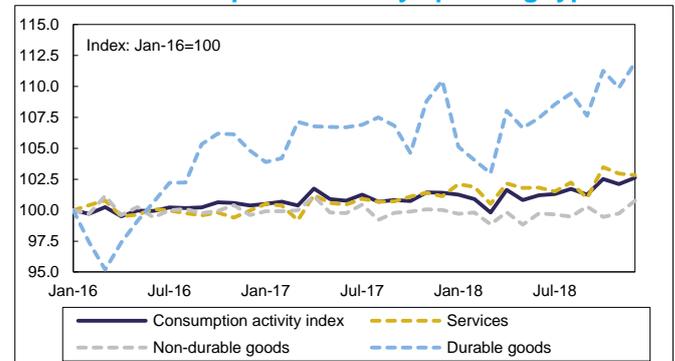
Further information on consumer spending was provided by MIC's household survey, although this has recently been a less reliable guide to the national accounts measure of private

BoJ consumption activity index*



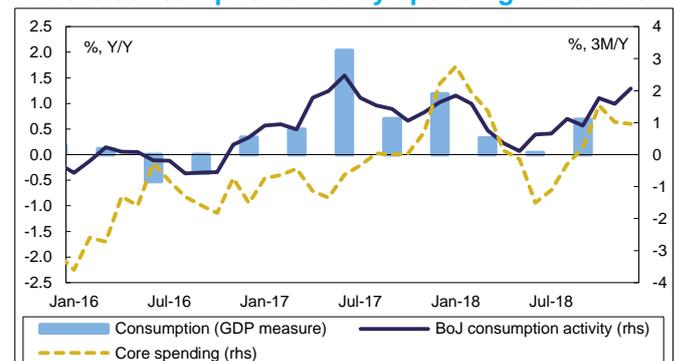
*Real terms and travel-adjusted. Source: BoJ and Daiwa Capital Markets Europe Ltd.

BoJ real consumption index by spending type



Source: BoJ and Daiwa Capital Markets Europe Ltd.

Private consumption and key spending indicators



Source: BoJ, MIC, Cabinet Office, Thomson Reuters and Daiwa Capital Markets Europe Ltd.



consumption. After adjusting for a discontinuity caused by changes undertaken to the survey last year, real spending amongst two-or-more person households fell 0.1%M/M. Even so, annual growth edged up to 0.1%Y/Y, the first positive reading since August. And while core spending – which excludes housing, auto sales and certain other expenditures – declined 1.2%Y/Y, it grew a little more than 1%Q/Q through Q4 – a result that is entirely consistent with the BoJ's own indicator.

Household incomes grow in December

Elsewhere in the survey, real disposable income for workers' households rose 2.1%Y/Y in December, marking the strongest outcome since June. In a similar vein, the MHLW's preliminary Monthly Labour Survey for December reported that growth in total labour cash earnings (per person) edged up 0.1ppt to 1.8%Y/Y. Taking a matched sample of respondents – to look through the impact of sampling changes – earnings growth was only slightly weaker at 1.7%Y/Y. And after allowing for a decline rate of inflation, real earnings growth increased to a six-month high of 1.4%Y/Y. As always, we caution that the preliminary results can be subject to substantial revision. But, at face value, the results suggest that consumer spending should continue to expand at a moderate pace in the near term.

Wage detail slightly less positive for inflation

Unfortunately for the BoJ, the survey detail suggested that the flow-through to inflation might be slightly weaker than suggested by the headline figures. The solid headline growth in incomes was due to bonus payments, up 2.7%Y/Y in December. Growth in contracted earnings fell back 0.5ppt to 0.8%Y/Y, with growth in scheduled earnings (i.e. ordinary time) slowing 0.4ppt to 0.9%Y/Y. The preliminary estimates indicated that scheduled earnings of part-time workers rose 2.5%Y/Y on a per hour basis, up 0.2ppt from November. But the equivalent rate for full-time workers slowed 0.4ppt to 1.0%Y/Y, a result that merely matched the average rate recorded last year.

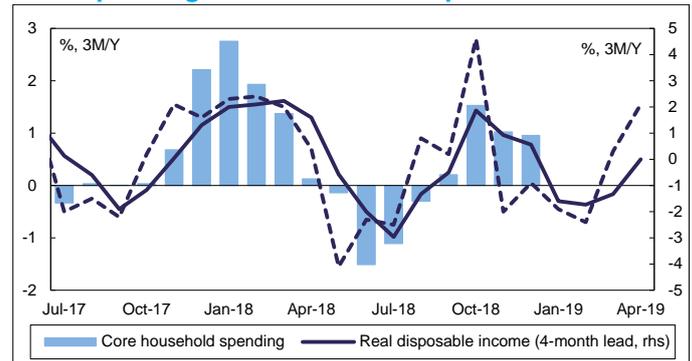
Hours worked fall back in December

Elsewhere in the survey, the number of regular employees rose 0.2%M/M in December – the third consecutive such increase – so that annual growth nudged up to 0.8%Y/Y. The preliminary estimates suggested that the number of full-time employees rose 0.5%Y/Y, up from no growth in November. However, if the pattern of past revisions holds, this finding is likely to be overturned when the final estimates are released. Meanwhile, after rising sharply over the previous two months – reflecting a rebound in activity in the wake of the natural disasters that struck through Q3 – aggregate hours worked (per person) were reported to have declined 3.2%M/M in December to be down 2.1%Y/Y.

Economy watchers report weaker conditions

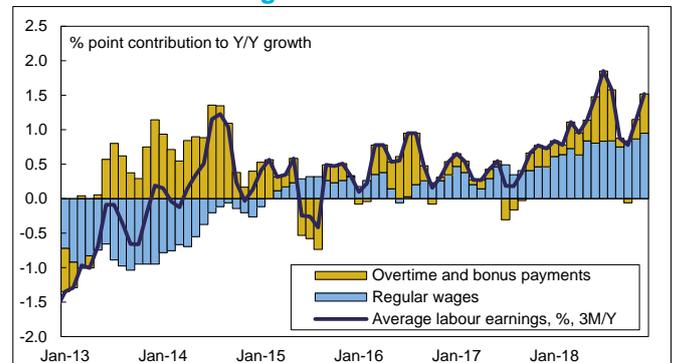
Of more contemporary interest – and concern – the Cabinet Office's Economy Watchers survey for January contained more worrying signs, likely reflecting increasing unease about the global economic outlook. In particular, the overall current conditions index fell to just 45.6 – the weakest outcome since July 2016 – following a December reading

Core spending and household disposable income*



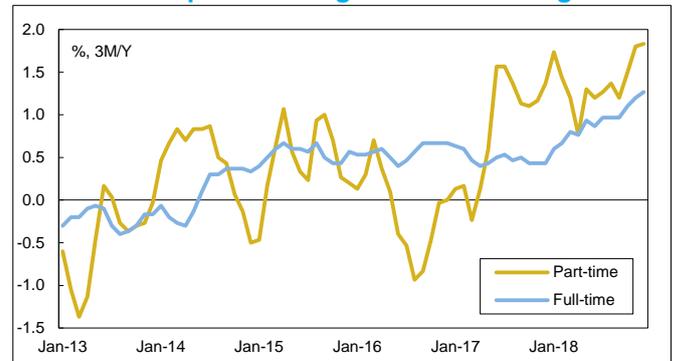
*Dashed dark blue line is Y/Y growth. Source: MIC, Bloomberg and Daiwa Capital Markets Europe Ltd.

Labour cash earnings



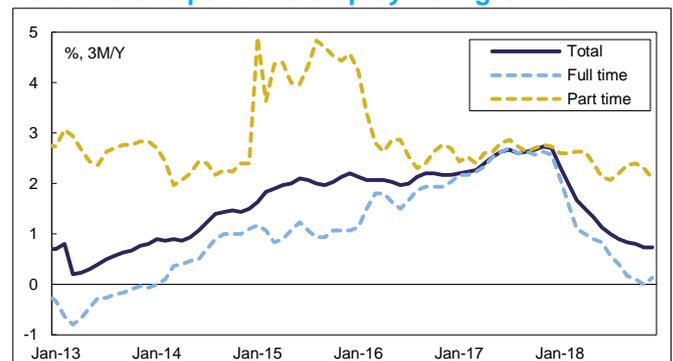
Source: MHLW, Thomson Reuters and Daiwa Capital Markets Europe Ltd.

Full-time and part-time regular cash earnings



Source: MHLW, Bloomberg and Daiwa Capital Markets Europe Ltd.

Full-time and part-time employment growth



Source: MHLW, Bloomberg and Daiwa Capital Markets Europe Ltd.

that was revised down 1.2pts to 46.8. The household-related index fell 2pts to 44.6, the weakest result since September 2016. But, after falling steeply in December, the business-related index rose 0.5pt to 46.6. The forward-looking indices were somewhat less discouraging, with the overall outlook index up 1.5pts to 49.4 – albeit from a downwardly-revised December and leaving it just below the Q4 average. The business-related index rose just 0.5pt to 46.8, which was still the second-weakest reading recorded in the last 2½ years.

Composite PMI also points to soft start to Q1

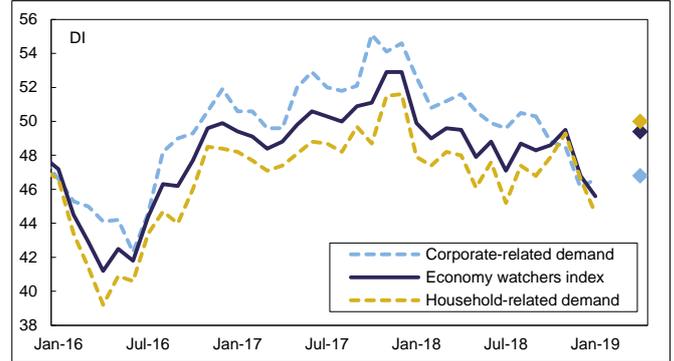
To some extent, the services PMIs offered comfort about the extent of any loss of momentum at the start of 2019. The headline activity index rose 0.6pt in January to 51.6, slightly above last year's average, while the new orders PMI edged up 0.1pt to 52.1. But given the scale of the deterioration in the manufacturing output PMI, the headline composite index fell 1.1pts to a four-month low of 50.9 – a result that tallies with the Economy Watchers' survey and Reuters Tankan to suggest a soft start to 2019. With respect to inflation, while the services input price PMI edged down to an eight-month low of 53.6, the output price index edged up to 52.3, the highest in six months. Similarly, the composite input price PMI fell 0.4pt to a fifteen-month low of 54.9. But the output price index rose 0.2pt to a three-month high of 52.2, a touch above the 2018 average to suggest no significant loss of underlying price pressure at the start of the year.

The week ahead in Japan and the US

Following Monday's holiday, the highlight of the coming week's Japanese economic diary will be Thursday's preliminary national accounts for Q4. After a disappointing 0.6%Q/Q contraction in Q3, our colleagues in Tokyo forecast a 0.5%Q/Q rebound in real GDP in Q4. Solid growth in private consumption, a rebound in business capex and a small positive contribution from inventories is expected to be partly offset by a further negative contribution from net exports and a small negative contribution from public spending. Ahead of the national accounts we will receive the Tertiary Industry Index for December on Tuesday and the January goods PPI on Wednesday. The final results of the December IP survey are due on Friday. In the bond market, the MoF will auction 5-year JGBs on Wednesday and 10-year IIBs on Friday.

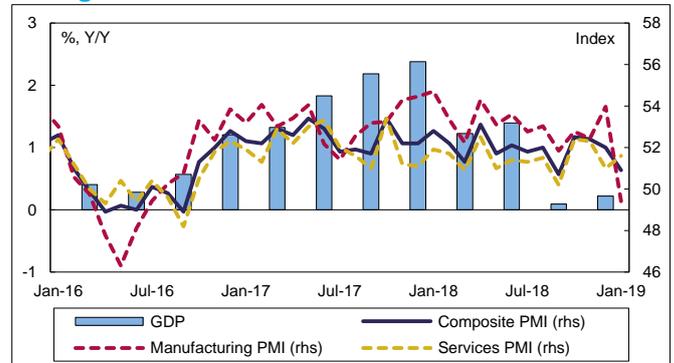
In the US the coming week's diary begins with the release on Monday of revisions to the CPI, which will include new quality adjustments for telecommunication services and new seasonal factors. The NFIB small business survey for January and JOLTS survey for December are due on Tuesday. Attention the following day will turn to the January CPI report, with the PPI report for last month due on Thursday. Also on Thursday we will finally receive the December retail sales report and November business inventory data, which will provide additional information ahead of the Q4 GDP report now scheduled for release at the end of this month. On Friday January IP data and February's New York Fed manufacturing survey will cast more light on the factory sector. That day will also see the release of the preliminary findings of the University of Michigan's consumer survey for February and import price data for January. The coming week's US Treasury auction schedule contains only bills.

Economy watchers survey



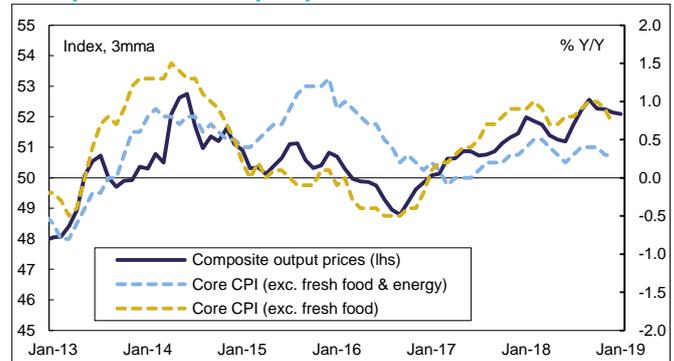
*Diamonds represent outlook indices, Source: Cabinet Office, Thomson Reuters and Daiwa Capital Markets Europe Ltd.

GDP growth and PMIs*



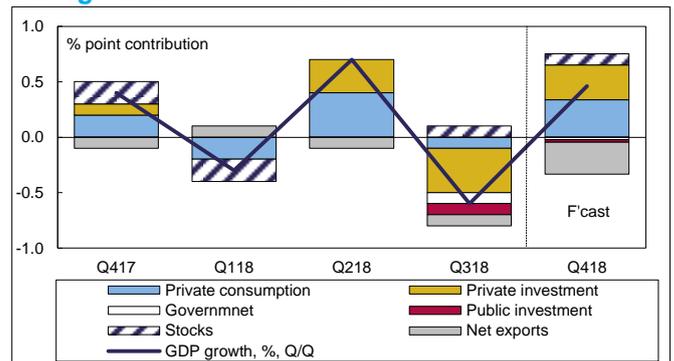
*Manufacturing PMI is output index, Q418 GDP figure is Daiwa forecast. Source: Markit, Cabinet Office, Thomson Reuters and Daiwa Capital Markets Europe Ltd.

Composite PMI output price index and core CPI



Source: Markit, MIC, Thomson Reuters and Daiwa Capital Markets Europe Ltd.

GDP growth and contributions



Source: Cabinet Office and Daiwa Securities

Economic calendar

Key data releases – February/March

04	05	06	07	08
MONETARY BASE Y/Y% DEC 4.8 JAN 4.7	10Y JGB AUCTION SERVICES PMI DEC 51.0 JAN 51.6 COMPOSITE PMI DEC 52.0 JAN 50.9		30Y JGB AUCTION 6M TB AUCTION BOJ CONSUMPTION ACTIVITY INDEX M/M% NOV -0.3 DEC 0.5 20-DAY TRADE - EXPORTS Y/Y% DEC -1.5 JAN -8.9 IMPORTS Y/Y% DEC 5.0 JAN -8.4	3M TB AUCTION AVERAGE WAGES Y/Y% NOV 1.7 DEC 1.8 HOUSEHOLD SPENDING Y/Y% NOV -0.6 DEC 0.1 ECONOMY WATCHERS SURVEY – CURRENT CONDITIONS DI DEC 46.8 JAN 45.6 FUTURE CONDITIONS DI DEC 47.9 JAN 49.4 BANK LENDING Y/Y% DEC 2.5 JAN 2.4 CURRENT ACCOUNT ¥TRN NOV 1.4 DEC 1.6
11	12	13	14	15
NATIONAL HOLIDAY – FOUNDATION DAY	TERTIARY ACTIVITY INDEX M/M% NOV -0.3 DEC -0.1 M3 MONEY SUPPLY Y/Y% DEC 2.1 JAN 2.1	5Y JGB AUCTION (APPROX ¥2.0TRN) GOODS PPI Y/Y% DEC 1.5 JAN 1.0	GDP Q/Q% Q3 -0.6 Q4 P 0.5	10Y JGBI AUCTION (APPROX ¥0.4TRN) 3M TB AUCTION (APPROX ¥4.34TRN) INDUSTRIAL PRODUCTION M/M% NOV -1.0 DEC F -0.1 CAPACITY UTILISATION M/M% NOV 1.0 DEC N/A
18	19	20	21	22
MACHINE ORDERS (DEC) DEPARTMENT STORE SALES* (JAN)	20Y JGB AUCTION 1Y TB AUCTION REUTERS TANKAN (FEB)	TRADE BALANCE (JAN) OVERSEAS VISITORS (JAN)	AUCTION FOR ENHANCED LIQUIDITY MANUFACTURING PMI (FEB P) ALL INDUSTRY ACTIVITY (DEC)	3M TB AUCTION NATIONAL CPI (JAN) AVERAGE WAGES (DEC F)
25	26	27	28	01
SERVICES PPI (JAN)	AUCTION FOR ENHANCED LIQUIDITY		2Y JGB AUCTION INDUSTRIAL PRODUCTION (JAN P) RETAIL SALES (JAN) HOUSING STARTS (JAN) CONSTRUCTION ORDERS (JAN)	3M TB AUCTION TOKYO CPI (FEB) UNEMPLOYMENT RATE (JAN) JOB-TO-APPLICANT RATIO (JAN) CAPITAL SPENDING SURVEY (Q4) CONSUMER CONFIDENCE (FEB) MANUFACTURING PMI (FEB F) VEHICLE SALES (FEB)

*Approximate date of release. Source: BoJ, MoF, Bloomberg, Thomson Reuters and Daiwa Capital Markets Europe Ltd.

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