Annual Report on the Japanese Economy and Public Finance 2018
(Report by Minister of State for Economic and Fiscal Policy)

— White Paper: Toward The Economy of Society 5.0 —
Summary

August 2018
Cabinet Office, Government of Japan
Chapter 1: Current State of Economic Recovery and Challenges ............................................. p.2

Chapter 2: Human Capital and Work Styles in the Era of the 100-year Life ............................................. p.6

Chapter 3: Changes in Economic Activities toward "Society 5.0" ................................................................. p.9

This material has been tentatively prepared to explain the "Annual Report on the Japanese Economy and Public Finance". For quotations and other purposes, please refer to the text of the "Annual Report on the Japanese Economy and Public Finance".
Since the end of 2012, the Japanese economy has been in a moderate recovery, approaching the longest recovery period after WW II.

In the 2000s, the economy recovered amid deflation. In the current recovery phase, **deflation faded** and corporate earnings **increased in broader sectors and all firm size**. Employment conditions are steadily improving. The **GDP gap has turned positive**. Raising the potential growth rate is the next critical challenge.
With robust service spending, private consumption is picking up. Large room for increase in internet consumption remains, in particular, among elder users.

Private consumption is picking up. Service consumption is especially robust, reflecting structural changes, such as the increased communication spending along with the diffusion of mobile phones, and the growth of spending on food services driven by increased single-person and double-income households.

Fewer elderly households shop on the internet. But, focusing only on the elderly households who online, the amount of their online spending is almost the same as those of younger households.

For clothing, furniture, home appliances, online shoppers tend to buy lower-priced goods.
Profitability of firms facing labor shortage tend to be high, though some suffer from a labor shortage. Improvement of productivity is a key challenge to address.

1-3. Trend and Challenges of Corporate Sector: Addressing Labor Shortage

Firms facing labor shortage tend to earn more profits, but some sectors are forced to limit workload owing to labor shortage.

Firms facing severe labor shortage need to increase productivity. More active investment in human capital of employees and for labor saving to raise productivity is crucial.
1-4. Challenges to Overcome Deflation and Revive the Economy: Trend of Prices and Wages

Amid a moderate rise in prices, continued wage increases are needed to overcome deflation and revive the economy.

1. Trend of prices

Prices are moderately increasing. International comparison shows little difference in prices of goods while **service prices increase slower in Japan, reflecting lower wage growth.**

![Graph showing trend of prices and GDP gap](image)

(1) Consumer prices and GDP gap

(Y/Y, %)

- Excluding fresh foods and energy
- Positive both in consumer prices and GDP gap


Note: Wages in (2) represent non-farm average of hourly pays.

2. Trend of wages

**Improved profitability and higher productivity** are likely to deliver base wage hike.

As the prospect of future business climate influences attitudes of companies toward wage increase, **improving their long-term prospects is also crucial.**

![Graph showing trend of wages](image)

2013 2014 2015 2016 2017 2018

Goods Services Wages

<table>
<thead>
<tr>
<th>Goods</th>
<th>Services</th>
<th>Wages</th>
</tr>
</thead>
<tbody>
<tr>
<td>Japan</td>
<td>USA</td>
<td>Euro zone</td>
</tr>
<tr>
<td>Japan</td>
<td>USA</td>
<td>Euro zone</td>
</tr>
<tr>
<td>Japan</td>
<td>USA</td>
<td>Euro zone</td>
</tr>
</tbody>
</table>

(2) Prices and wages: International Comparison

(2017: Y/Y, %)

Large differences in wages and service prices between Japan and US

(3) Analysis on factors which could raise probability of base wage increase

More profit, higher productivity, and labor shortage could lead to higher probability of base wage increase.

![Graph showing analysis on factors](image)

| Factor | (%)
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Pay more bonus instead</td>
<td>64.7</td>
</tr>
<tr>
<td>Poor business performance</td>
<td>50.6</td>
</tr>
<tr>
<td>Difficulty in pay cuts in future downturn</td>
<td>22.9</td>
</tr>
<tr>
<td>Attitudes of sector / competitors</td>
<td>13.9</td>
</tr>
<tr>
<td>Prices and other economic conditions</td>
<td>10.6</td>
</tr>
<tr>
<td>Loss of price competitiveness</td>
<td>8.4</td>
</tr>
<tr>
<td>No demand from unions</td>
<td>1.4</td>
</tr>
</tbody>
</table>

Source: Cabinet Office, "Attitude Survey of Companies on Work Style and Education & Training".