

ECONOMIC RESEARCH – MARCH 2025

INVESTMENT INSIGHT

JAPAN



- ✓ **Strong Japanese economic recovery supported by rising exports**
- ✓ **First quarter of 2025 likely to be solid**

YIELD DIFFERENTIAL IN FAVOR OF THE YEN

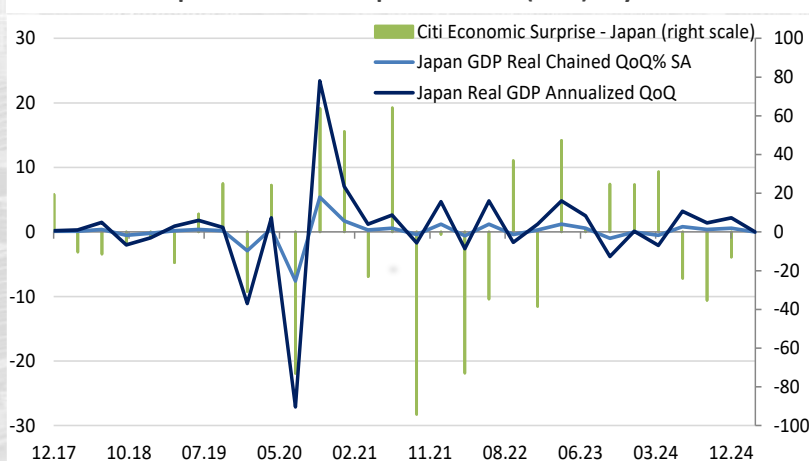
Robust Q4 growth supported by exports

After a period of sluggish performance, the Japanese economy displayed unexpected resilience and dynamism in the final quarter of 2024. This surprising upturn has now renewed optimism for a stronger-than-expected start to 2025. Japan's real GDP grew by a robust +0.7% on a seasonally adjusted basis, a rate double the consensus forecast of +0.3%. While this quarterly performance was strong, the broader picture for the year was more tempered. The Q4 results only managed to lift the year-on-year growth to a modest +0.1%, marking the lowest growth rate since the global pandemic began.

A deeper look into contributing factors

The most significant positive surprise came from net exports, which saw a considerable increase of +0.7%, surpassing the anticipated +0.4%. However, it is important to note that this boost was largely due to a sharper contraction in imports, driven by lower global energy prices, rather than a genuine surge in demand for Japanese goods. On the domestic front, household consumption remained limited at a modest +0.1% increase. This suggests that despite better-than-expected results, consumer sentiment remains cautious heading into 2025. The impact of wage increases negotiated in early 2024 was unfortunately offset by high inflation, which prevented any meaningful growth in real wages and thus continued to constrain domestic spending.

Japanese economic performance (GDP) in yen



Sources : Bloomberg, BBGI Group

Outlook for Q1 2025

The Japanese economy's reliance on external factors, such as international demand and foreign trade, remains a key vulnerability. The persistence of inflation is a significant headwind, as it is unlikely to allow for a substantial improvement in household purchasing power in early 2025, which will continue to suppress domestic demand. This is a critical challenge, as sustainable economic health depends on a strong domestic consumption base. Furthermore, the economy faces growing geopolitical risks, including the potential for new tariffs from major trading partners.

Anticipated U.S. demand

Expectations for the first quarter of 2025 suggest a temporary reprieve. Japanese exports are projected to benefit from a brief upturn in U.S. demand, as businesses preemptively order and take delivery of goods in anticipation of the aforementioned tariffs. This trend was already visible in January's data, with a remarkable +7.2% rise in exports, including a significant +21.8% jump in vehicle exports. However, a regional analysis of trade data highlights the fragility of this growth: the increase in U.S. demand was not replicated with other key partners, as trade with China and Europe declined by -6.2% and -15.1% respectively.

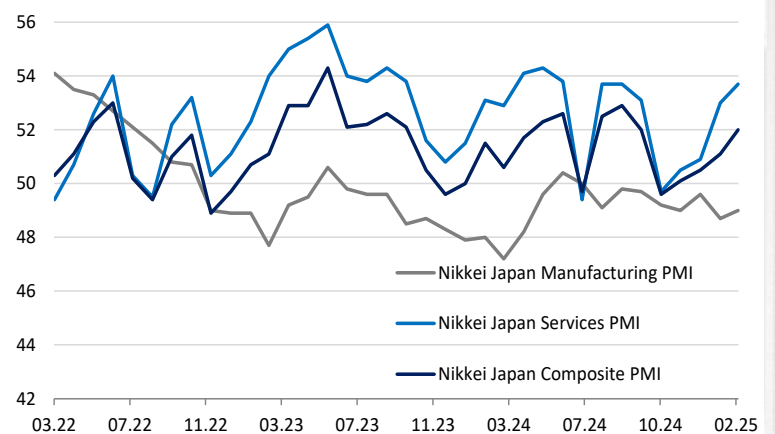
Emerging challenges and the trade balance

Despite the positive export figures, a dramatic increase in imports of IT and communications equipment, which surged by +16.7%, has shifted the trade balance into an unexpected deficit of \$18.2 billion. Given the mounting global trade risks, Japan must prepare for a potential reduction in exports if new trade barriers materialize. To maintain a positive trajectory and foster more resilient growth, it will be imperative for future economic policy to be supported by robust domestic consumption and targeted fiscal spending.

Looking ahead to Q2

In the short term, a substantial recovery in both international demand and domestic consumption is not foreseen. This leads to a moderate outlook for Q2 2025, following a Q1 that was largely sustained by temporary external factors. The economy's ability to pivot from an export-dependent model to one driven by internal strength will be the key to its long-term health. While the year's overall growth is expected to be around +1%, the underlying vulnerabilities remain and will require strategic policy responses.

PMI indicators (manufacturing, services, composite)



Sources : Bloomberg, BBGI Group

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