

### Postponement of Consumption Tax Hike and its Impact to Japanese Equity

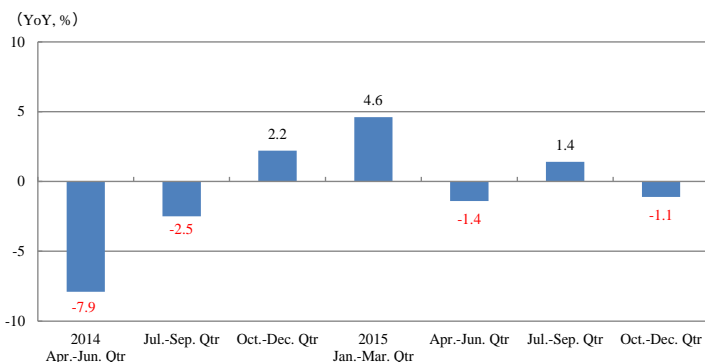
- While, news on postponement of consumption tax hike are reported frequently, speculation is reinforced that PM Abe would make a final decision on the tax hike around end of May when the G7 Summit will be held.
- However, if the tax hike is postponed, PM Abe has to show the path to achieve fiscal consolidation target, as financial situations are severe.
- Rise in the Japanese stock market on economic measures and the tax hike postponement depends on whether they will expand future demand and corporate earnings.

**While, news on postponement of consumption tax hike are reported frequently, speculation is reinforced that PM Abe would make a final decision on the tax hike around end of May when the G7 Summit will be held**

Lately, many articles on postponement of consumption tax hike are reported on various newspapers. At G20 Finance Ministers and Central Bank Governors Meeting held in February, participating nations agreed to implement flexible fiscal policy and Japan is to host G7 Ise-Shima Summit on 26<sup>th</sup> and 27<sup>th</sup> of May, 2016. Postponement of consumption tax hike has become more likely, as the G7 Summit looks like a good opportunity to appeal for international cooperation by fiscal stimulus.

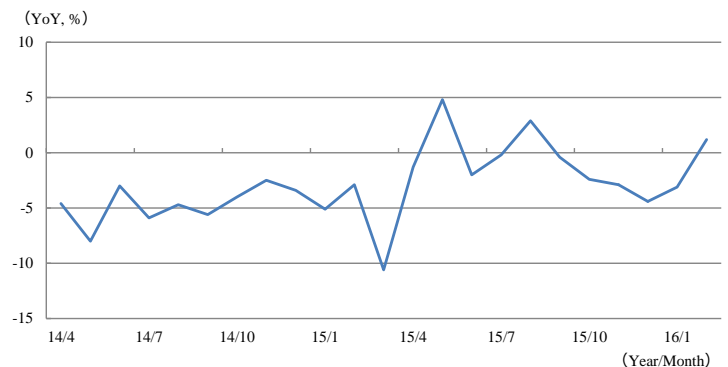
The Japanese government is expected to i) release economic measures by drafting up “Japan - Promoting Dynamic Engagement of All Citizens Plan” in May, ii) compile supplemental budget draft (to be submitted at autumn extraordinary Diet session) as a source of the economic measures, iii) decide whether to raise the tax or not and scale of the stimulus package. The International Finance and Economic Assessment, a preparatory meeting for the G7 Ise-Shima Summit, is taking place until May and Jan.-Mar. first preliminary real GDP figure will be announced on 18<sup>th</sup> May, as well. More and more experts expect PM Abe to decide around end of May to put off the consumption tax hike or not.

"Chart 1: Real GDP Growth Rate of Japan"



(Note) Data period is from April-June Quarter, 2014 to October-December Quarter, 2015.  
(Source) SMAM, based on Bloomberg L. P. data.

"Chart 2: Real Consumer Spending of Japan"



(Note) Data period is from April 2014 to February 2016.  
(Source) SMAM, based on Bloomberg L. P. data.

### **However, if the tax hike is postponed, explanation on the path to achieve fiscal consolidation target is necessary, as financial situations are severe**

It appears that another consumption tax hike scheduled in April 2017 will be a difficult choice for the Abe administration, as growth of real GDP growth rate (Chart 1) and real consumer spending (Chart 2) in Japan has been weak since the consumption tax hike in April 2014. Therefore, it is quite likely that combination of postponement of consumption tax hike and economic measures based on source of tax revenue increase without depending on additional government bond issuance will be implemented.

However, financial situations in Japan are severe. Based on estimation by International Monetary Fund (IMF), general government gross debt per GDP of Japan is likely to reach 248% by the end of year 2016. This is much worse than 207% of Greece and the worst amongst major countries. In the case of postponement of consumption tax hike, Japanese government needs to explain how fiscal consolidation target set by itself can be achieved in a concrete manner. If not, Abe's administration will lose credibility of both domestic and overseas parties concerned on the country's sustainability of finance.

### **Rise in the Japanese stock market on economic measures and the tax hike postponement depends on whether they will expand future demand and corporate earnings**

Japanese equities are likely to perform well for a while, underpinned by expectation of the economic measures and postponement of consumption tax hike. According to various news and reports, issuance of "Premium gift vouchers" and vouchers for child-care-support services aiming at stimulating consumption have been discussed by the government. If the stimulus package can provide new growth opportunities to corporations and contribute to create sustainable demand, full-fledged rise in stock price can be expected. If failed to do so, stocks will be sold in disappointment.

In general, growth in future cash flow generated by corporations and earnings are considered to be factors for the stock price to rise. It must be noted that future cash flow and earnings will not necessarily grow by postponing consumption tax hike. Therefore, stock prices will possibly not rise by simply postponing consumption tax. With this in mind, it is necessary to assume the case of "stock prices rising with expectation on economic measures and postponement of consumption tax hike, but falling when they are announced", as financial proverb goes "Buy on the rumor, sell on the fact".

**\* Please note that this report is a translation of Japanese report written on 1<sup>st</sup> April, 2016.**

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