

ROBUST GROWTH UNDER LOW INFLATIONARY PRESSURE

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The U.S.: Still Going Strong

The U.S.'s real GDP increased at an annual rate of 4.5 percent in the first quarter of 1999, which is decent enough, although slightly lower than the 6.0 percent in the fourth quarter of 1998. The major contributors to this growth were personal consumption and fixed investment. Real personal consumption expenditures increased 6.7 percent, compared to the 5.0 percent increase in previous quarter. As these indices show, the U.S. economy remains robust and the corporate earnings outlook is improving. Now, notwithstanding last year's expectations, the U.S. GDP is going to grow around 3.5~3.6% in 1999.

Consumer spending will remain strong throughout this year, though moderated from its recent pace. Slow job growth, declining income growth and higher energy costs will drain some consumer purchasing power and contribute to the moderation. But the overall consumption volume, which usually lags behind GDP growth by couple of quarters, will post one of its strongest figures since the mid 1990's.

The corporate earnings outlook is also becoming more and more optimistic, as the negative factors associated with the global crisis recede. The S&P 500 operating EPS (Earnings Per Share) is expected to rise 8.0~8.5% to \$47.5~\$48.00 for 1999. Meanwhile, inflation should remain subdued, though higher energy prices are about to show up in headline inflation data. The CPI will be up 2.2~2.3% during 1999, up from 1.6% last year, mainly because of the higher oil prices. For the U.S. economy, robust growth under low inflationary pressure will go on for a while.

Japan: Standing at the Crossroads

Japan's housing investment has started recovering, and public works orders are increasing considerably. Meanwhile, industrial production has stopped decreasing. Apparently, these current changes in the economic situation seem to have stopped a further deterioration in corporate and consumer sentiments. However, business fixed investment has been declining, and the recovery in private consumption continues to be weak as a whole. Corporate profits remain weak, and employment and household income conditions continue to deteriorate.

As for the outlook, with the progress in inventory adjustment gradually paving the way for a recovery in production, the government's policy measures and monetary easing by the Bank of Japan will underpin the economy. However, the corporate restructuring process is one of the key factors which will determine Japan's economic outlook in the near future. Faced with declining profits, major firms have started full-scale restructuring. Although such corporate restructuring is expected to improve productivity and create an environment for smooth structural reforms in the intermediate term, it may, in the short run, reduce fixed investment and discourage household expenditure. Needless to say, restructuring will prove to be helpful for profitability, but until excess capacity is reduced one cannot expect that the return on capital will rise. Such circumstances mean that an immediate, self-sustained recovery in private demand will not be easily achieved. The Japanese economy and financial markets are standing at the crossroads. **VIP**