December 5, 2024

Bank of Japan

Economic Activity, Prices, and Monetary Policy in Japan

Speech at a Meeting with Local Leaders in Hiroshima

NAKAMURA Toyoaki

Member of the Policy Board

(English translation based on the Japanese original)

I. Economic Developments at Home and Abroad

I will begin my speech by talking about recent developments in and the outlook for overseas economies.

Overseas economies have grown moderately on the whole, although uncertainties surrounding these economies have continued to be high, such as a delay in the recovery of the European and Chinese economies, and the prolonged situation in Ukraine and the Middle East (Chart 1). The U.S. economy, despite the impact of successive policy interest rate hikes, has been firm, mainly due to resilient private consumption, and is increasingly expected to make a soft landing. However, the economy has also shown some signs of deceleration, such as declining trends in the number of job openings and the consumer confidence index, and a significant rise in credit card delinquency rates. Moreover, attention should be paid to the risk of a resurgence of inflation as a result of, for example, future economic developments and policy conduct. European economies have kept slowing moderately due to the continued impact of factors such as successive policy interest rate hikes in the past. There is concern over economic recovery being delayed in Europe due not only to the economic stagnation in Germany -- which has seen a decline in industrial strength and an increase in downward pressure on wages -- but also to chronic labor issues in European economies. The pace of recovery in the Chinese economy has slowed, reflecting an increase in households' thriftiness. The increase is mainly due to (1) prolonged sluggishness in the real estate market, (2) intensified price competition, (3) the high youth unemployment rate, and (4) people's concerns over future wages and their post-retirement years. I believe that further deterioration in the Chinese economy will be avoided through expansion in fiscal spending and monetary easing. However, as adjustment pressure in the real estate and labor markets remains, there is concern over a lower economic growth rate in the future, due to intensified price competition brought about by higher supply capacity and to growing trade friction.

Let me move on to recent developments in Japan's economic activity and prices. The economy has recovered moderately, although some weakness has been seen in part. In the corporate sector, goods exports have been more or less flat. Meanwhile, services exports have continued to increase at a pace almost surpassing the record high, given an increase in inbound tourism demand reflecting factors such as a higher number of foreign visitors. Industrial production has been more or less flat. Corporate profits have been on an improving trend. Business fixed investment has also been increasing moderately, due to growing demand for investment such as efficiency-improving investment and investments associated with digital transformation (DX) and green transformation (GX). That said, with aggregate demand remaining below aggregate supply, some of the business fixed investment plans may be postponed, and thus future developments warrant attention. With respect to the household sector, the income situation has improved moderately, as seen in the year-on-year wage growth continuing to be in the range of 2.5-3.0 percent. However, I am closely monitoring future developments in wage growth, as there seems to be a polarization between (1) growth-oriented firms -- large and medium-sized ones as well as some small ones -- making "virtuous" wage hikes and (2) the majority of small firms -- whose recovery of earning power has trailed behind -- making "defensive" wage hikes. Private consumption has been lacking momentum, mainly due to the impact of price rises and households' thriftiness. Turning to prices, the year-on-year rate of increase in the consumer price index (CPI) for all items excluding fresh food has been in the range of 2.0-2.5 percent recently, as services prices have continued to rise moderately, reflecting factors such as wage increases, although the effects of a pass-through to consumer prices of cost increases led by the past rise in import prices have waned.

As for the outlook, the Bank of Japan's October 2024 *Outlook for Economic Activity and Prices* (Outlook Report) forecasts that Japan's economy is likely to keep growing at a pace above its potential growth rate, with overseas economies continuing to grow moderately and as a virtuous cycle from income to spending gradually intensifies against the background of factors such as accommodative financial conditions (Chart 2). However, because I am not yet confident in the sustainability of wage hikes, my projection for real GDP growth rates for fiscal 2024 to 2026 is lower than the medians of the Policy Board members' forecasts presented in the October Outlook Report. My projection is based on factors such as the following: (1) private consumption that reflects an intensified thriftiness among households; (2) the possible postponement of implementing business fixed investment plans; and (3) mounting international competition triggered by the slowdown in overseas economies, particularly China. In the October Outlook Report, the median of the Policy Board members' forecasts for the year-on-year rate of increase in the CPI for all items excluding fresh food is around 2.5 percent for fiscal 2024, and around 2 percent for fiscal 2025 and 2026. However, in my view, the rate may not reach 2 percent in fiscal 2025 and thereafter.

II. Conduct of Monetary Policy in Line with the State of the Economy's Return to a Growth Path

The purpose of the Bank of Japan's monetary policy is to achieve the 2 percent price stability target in a sustainable and stable manner, thereby contributing to the sound development of the national economy. Factors such as U.S. monetary policy and developments in overseas economies and exchange rates impact economic activity and prices in Japan, and thus require consideration. However, I believe what is essential in the conduct of monetary policy is to contribute to improvement in Japan's economic fundamentals from a medium- to long-term perspective in line with the state of the economy's recovery, as the economy faces low profitability due to changes in demographics and the industrial structure. Keeping this view in mind and drawing from my own experience, I will overview topics such as the changes in Japan's industrial structure from a somewhat long-term perspective.

A. Changes in Japan's Industrial Structure and the State of Economic Recovery

During the Showa era's post-war period of rapid economic growth in Japan, export industries quickly flourished in a weak yen environment by realizing high performance, high quality, and low prices via a business model of mass production and vertical integration. Household income also continued to experience rapid growth. Meanwhile, as firms pursued greater production efficiency, the system of lifetime employment and seniority-based wages took shape. Trade friction subsequently broke out between Japan and the United States, while the yen began to appreciate rapidly following the 1985 Plaza Accord. This led firms, especially large ones, to actively expand their overseas sites.

As Japan entered the Heisei era in 1989, even under a strong yen, it seemed as if the bubble economy offset the downturn in export industries. However, as advances in IT drove greater digitalization and globalization, business models involving a horizontal division of labor proved increasingly superior. In this situation, the international competitiveness of Japan,[1] which globally ranked first until 1992, gradually declined because Japanese firms trailed behind in restructuring their business portfolios (Chart 3). Corporate earnings deteriorated, due in part to the collapse of the bubble economy in early 1992 and the financial system crisis. These developments prompted large firms with high productivity to actively invest overseas and relocate their supply chains to China, Southeast Asia, and other countries and regions, in pursuit of lower costs and higher growth. On the other hand, in Japan, large firms reformed their cost structures, by, for example, closing factories, downsizing, restraining investment, encouraging voluntary retirement, and cutting wages. The trends of cutting costs and restraining investment also spilled over to small firms, which faced dwindling orders as well as intensified price competition. As a result, despite an aging and declining population, the issue of labor shortages did not surface (Chart 4). Employment was prioritized over wages, and firms made little headway with restructuring their business portfolios to strengthen their ability to create added value. Under these circumstances, intensified price competition led to lower growth and profitability for domestic industries, and Japan's economy fell into deflation in which it was difficult for wages and prices to rise. The ensuing three decades of an economy oriented toward contraction, characterized by a deflationary mindset and cost-cutting, gave rise to a persistent vicious cycle in which the output gap fell into negative territory. Firms in Japan grew more cautious in their wage- and price-setting behavior, falling behind in terms of business fixed investment and digitalization. Thriftiness among households also seemed to take root. Looking at trends in the trade balance, Japan's terms of trade have deteriorated, due to lower exports of industrial products and higher imports of goods such as mineral fuels, and this has propelled a decline in firms' profitability (Chart 5). Moreover, Japan's wage levels, even those of large firms, is low compared to the Group of Seven (G7) countries and major Asian economies (Chart 6), and private consumption is lacking momentum. However, bold monetary easing and flexible fiscal policies have helped to bring about a situation where the economy is no longer in deflation.

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[1] The *IMD World Competitiveness Booklet* published by the International Institute for Management Development (IMD) shows that Japan ranked first in international competitiveness until 1992, but is now ranked quite low, in 38th place.

Furthermore, the rise in global inflation and the yen's depreciation after the onset of the COVID-19 pandemic gave rise to inflation in Japan as well, sparked by a rise in import prices. Firms, large ones in particular, have achieved stronger earning power due to their implementation of business portfolio restructuring. That is why in 2024, Japan saw its highest wage growth in 33 years, stock prices that exceeded the level of the bubble economy, and business fixed investment totaling more than 100 trillion yen. Such vigorous business activities have yielded initial signs of a significant shift toward "a growth-oriented economy driven by wage increases and investment" that is capable of keeping up with inflation. Regulatory reforms that had been sluggish have also begun to move ahead. That being said, real GDP has recently experienced quarter-on-quarter increases and decreases, and it is still too early to judge whether the economy is on a stable growth path.

B. Conduct of Monetary Policy in Line with the State of Economic Recovery

Since the recovery phase from the pandemic, labor shortages have grown more acute, fueling greater mobility in employment and wage hikes. Structural issues remain, however, including weak demand and supply-side constraints -- both due to the aging and declining population -- and low profitability of the industrial structure. As the recovery in investment has trailed behind for small firms in particular, I personally do not yet have confidence in the sustainability of the wage hikes. Achieving the 2 percent price stability target in a sustainable and stable manner will require changes to Japan's economic structure so that it will inspire confidence in the economy's expected return to a growth path driven by the stronger earning power of firms. I should note that this will take a considerable amount of time. However, there are already initial signs of a significant shift toward "a growth-oriented economy driven by wage increases and investment" that is capable of keeping up with inflation. To ensure that this shift maintains momentum and does not subside, I think it is now vital for the Bank to examine a wide range of data and cautiously adjust the degree of monetary accommodation to reflect the state of economic recovery.

Specifically, I would like to carefully confirm the state of Japan's economic recovery with reference to a wide range of data and anecdotal information, including (1) whether the level of earning power of small firms, for which recovery has trailed behind, is higher than before the pandemic, (2) whether firms are able to pass on costs to prices at a higher rate, (3) whether progress is made in stepping up business fixed investment as well as wages and bonus payments, (4) whether more small firms are making virtuous wage hikes, (5) whether households' thriftiness has improved, and (6) whether Japan's exports have become more competitive. I will return to these points later, along with a discussion of the structural issues facing Japan.

III. Toward Sustainable Economic Growth that Overcomes Structural Issues

I would now like to share my personal views from a medium- to long-term perspective on the "dynamism" of firms, employment, and households needed to achieve sustainable growth in Japan's economy, which is facing structural issues.

A. Improving Japanese Firms' Earning Power and Capacity for Raising Wages

As discussed so far, employment was prioritized over wages in Japan. This hindered business metabolism, generated delays in productivity gains, and led to stagnant wages. Following the 2008 Global Financial Crisis, many large firms shifted the focus of their management from reforming their cost structures to restructuring their business portfolios, thereby strengthening earning power. To secure human capital,[2] I think large and medium-sized firms that have boosted productivity will strengthen their mid-career hiring by offering higher wages than those of existing employees, and they will continue to raise wages at high rates to bridge the gap between the wages of existing employees and wages formed in the labor market.

Labor shortages among large firms spur the movement of labor from small firms to large firms, creating employment dynamism (Chart 7). Developments in the following components of nominal wage growth show positive signs: the inflation rate (maintenance of living standards), the labor productivity growth rate (fruits of productivity gains), and changes in labor share (capacity for raising wages) (Chart 8). Nonetheless, I believe that the benefits of restructuring at large firms have not yet sufficiently spilled over to small and medium-sized firms. According to the *Financial Statements Statistics of Corporations by Industry, Annually*, for fiscal 2023, operating profits per employee among medium-sized firms was around 40 percent of that of large firms, and only around 10 percent among small firms (micro firms

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2 "Human capital" is a term coined to express the idea that human resources are valuable for corporate management.

excluded). Personnel expenses per employee among medium-sized firms was around 70 percent of that of large firms, and around half among small firms (micro firms excluded). In terms of per-employee operating profits, business fixed investment, and personnel expenses by firm size, for large and medium-sized firms, operating profits per employee -- an indicator of earning power -- grew significantly compared with the pre-pandemic period of fiscal 2018. It appears that these firms are implementing virtuous wage hikes, which are accompanied by productivity gains achieved through active business fixed investment (Chart 9). Meanwhile, the earning power of small firms (micro firms excluded) is still on its way to recovery from the pandemic and remains below pre-pandemic levels. These firms are also taking a wait-and-see approach to fixed investment, and many seem to have raised wages as a defensive step that aims at retaining employees and is not accompanied by productivity gains. This trend was unchanged in the July-September 2024 *Financial Statements Statistics of Corporations by Industry, Quarterly*. Furthermore, at the October 2024 meeting of the general managers of the Bank's branches, there were many reports that small firms had raised wages as a defensive step to retain employees.

A March 2024 follow-up survey on the Price Negotiation Promotion Month organized by the Small and Medium Enterprise Agency found that the proportion of small firms that engaged in price negotiations was 59 percent, only a slight increase from the previous survey. The rate of passing on costs to prices was 46 percent -- largely unchanged from the previous survey, and the rate of passing on labor costs was 40 percent. These figures suggest that there has been a polarization between firms that have been able to pass on costs to prices, while others remain unable to do so. If the recovery in small firms' earning power does not progress while they continue to raise wages at high rates, they could theoretically start operating at a loss within several years. This indicates their lack of capacity for raising wages. A June 2024 survey by the Japan Chamber of Commerce and Industry found that only 30 percent of small firms had implemented virtuous wage hikes, while 44 percent had raised wages as a defensive step, and 26 percent reported being undecided or having no plans to raise wages. Thus, there is still a long way to go before sustainable and structural wage hikes are achieved.

With a view to securing funds for raising wages, economic growth and improvement in corporate profits are important. In terms of corporate earnings of listed firms for the first half of fiscal 2024, according to media reports, those of nonmanufacturers increased for four consecutive years, led by the finance and shipping industries. However, among manufacturers, firms in the automobile and steel industries in particular, earnings decreased for the first time in four years, mainly due to the slowdown in China and other overseas economies and to intensified price competition. Japan's trade balance deficit continued in October, making it the fourth consecutive month; consequently, the nominal GDP growth rate for the July-September quarter remained low at a 0.5 percent quarterly increase. However, many listed firms have been conducting business portfolio restructuring that strengthens the earning power of core businesses. I am closely monitoring the progress in this restructuring, and hope that its benefits will spill over to small firms.

Japan's economy is expected to head toward a growth path, albeit at a moderate pace, mainly led by growth-oriented large, medium-sized, and small firms. The Bank will gradually adjust its monetary policy accordingly. In response, small firms will need to move away from closed innovation, which relies on in-house expertise, and hasten structural reforms to step up the scale of their businesses, in order to reinforce the management resources necessary for growth-oriented business development. From this perspective, I am also paying attention to developments that feed into greater earning power, such as those in business fixed investment and exports, as well as mergers and acquisitions (M&As) and third-party business succession (Chart 10).

B. Improving the Dynamism of Firms and Employment to Make Industries Highly Profitable

If firms improve their capacity for innovation to make Japan's industrial structure highly profitable and enhance export competitiveness, these firms will be able to capture growth in overseas markets to a greater extent. This, in turn, will generate sustainable demand for business fixed investment in Japan and promote industrial clusters. Such moves are expected to spill over across small and medium-sized firms. Research and development (R&D) expenses -- which are critical in terms of boosting the declining international competitiveness I mentioned earlier -- were sluggish, amounting to 200.7 billion U.S. dollars in Japan in 2022, reflecting stagnation in its economic growth. In comparison, R&D expenses for the United States and China increased in line with their economic growth, standing at 923.2 billion U.S.

dollars and 811.8 billion dollars, respectively. One reason for this sluggishness in Japan's R&D expenses is that, due to the historical background I explained earlier, the innovation required of advanced economies has stagnated in Japan, forcing firms to face price competition with emerging economies and to cut costs. For example, while software investment has grown 11-fold in the United States since 1990, it has barely grown in Japan over the same period, indicating a widening disparity between the two (Chart 11). In addition to expanding business performance, it is important for advanced economies to play a leading role in making active investment in R&D, human capital, and digitalization to accelerate future growth, while providing greater value through generating innovation. I expect reforms to the industrial structure to progress through continued expansion in investment, including firms' actions currently underway to foster and develop leading industries and strengthen human capital development.

It is also vital to support the development of small and medium-sized firms and startups that aspire to expand overseas. Many large firms started out as so-called unicorns and then grew rapidly. From 2011 to 2021, about 30 percent of medium-sized firms in the United States and Europe grew into large firms, but this proportion in Japan was only about 10 percent, suggesting the weakening growth potential of small and medium-sized firms in Japan that form the backbone of domestic economic activity and investment. Compared with the 1990s, while large firms' operating profits per employee grew 2.4-fold and those of medium-sized firms grew 1.9-fold, profits of small firms remained flat (Chart 9). Increasingly acute labor shortages are also a major supply-side constraint. Furthermore, there are concerns that, if firms face delays in productivity gains due to the postponement of business fixed investment, they may move supply chains offshore. Therefore, my hope is to see growth in the following two types of firms especially: medium-sized firms aiming to grow into large firms, and small firms aiming to reach annual sales of 10 billion yen. This is also in line with the policy laid out by the Japanese government.

In addition, compared with the 1990s, large firms' labor costs per employee increased 1.1-fold, while those for small and medium-sized firms remained flat (Chart 9). As wages represent employee value, firms need to continue with their strenuous efforts to improve their earning power and implement virtuous wage hikes, thereby enhancing employee value.

Investment in human resource development, including reskilling efforts, is important in enhancing employee value. If firms find it difficult to do this on their own, one option is to entrust the management of the businesses to their best owners.[3] Nowadays, employees themselves must also make efforts to enhance their own value, and it is natural for employees to consider changing jobs as an option, if they are unable to enhance their value at their current employment. Therefore, I believe that the key to sustainable wage increases is how growth-oriented small and medium-sized firms implement structural reforms to step up the scale of their businesses.

Admiration for growth-oriented firms will be inspired through the growth of small firms into medium-sized firms, the growth of medium-sized firms into large firms, and the rapid expansion of startups into unicorns, especially unicorns that use new technologies to generate new markets. I believe that this will draw both funds and talent to these firms, creating a growth spiral that reinforces the dynamism of firms and employment characterized by continuing rises in wage levels (Chart 12). Through such developments, I hope to see a virtuous cycle of growth and profit sharing.

In addition, the growth of small firms -- whose employees account for about 70 percent of the total workforce in Japan -- is indispensable to raising wage levels nationwide, revitalizing the attractiveness of regions struggling with population outflows, and improving job satisfaction. I expect regional financial institutions familiar with the situation in their respective regions and their client firms to play their part in supporting them by reinforcing their earning power through a strengthening of cooperation with support organizations, such as the Organization for Small & Medium Enterprises and Regional Innovation, the National Center for Industrial Property Information and Training (INPIT),[4] university research centers, and consulting firms. Regional financial institutions should also provide in-depth business

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[3] The "Practical Guidelines for Group Governance Systems" issued by the Ministry of Economy, Trade and Industry on June 28, 2019, highlights the importance of focusing on which company is the best owner to realize the potential of each business, when optimizing the business portfolio of the group firm as a whole, by identifying and strengthening core businesses, while also streamlining non-core businesses.

[4] INPIT is an institution that offers various services such as providing information on intellectual property rights, including patents, and other support services for users of the system of industrial property rights.

matching for M&As and third-party business succession, and other value-added services. These efforts in turn would propel the structural reforms to step up the scale of the small firms' businesses and thereby strengthen their earning power. I look forward to the strengthening of support activities dedicated to improving corporate dynamism.

C. Improving Household Dynamism to Mitigate Concerns about the Future

As Japan's industrial structure relies on imports for most of its resources for production inputs, coupled with today's globalized supply chains, the country's economic structure is therefore susceptible to global inflation. The latest figure for the year-on-year rate of increase in scheduled cash earnings per employee is in the range of 2.5-3.0 percent, reflecting the highest wage increase rate in 33 years (Chart 13). Meanwhile, over the same period, the working age population in Japan has decreased by about 10 percent, while the number of pensioners has increased 2.4-fold. Furthermore, pensioners, whose income replacement ratio is about 60 percent relative to their past wages, now account for around 30 percent of the overall population, resulting in a heavy social burden for the working age population. As a result, the social structure has characteristics of overall sluggishness in households' purchasing power and their tendency toward thriftiness.

As Japan's economic structure is subject to low profitability, to dispel concerns about the future, it is essential for growth-oriented large and medium-sized firms, as well as some small ones, to take the lead in driving overall economic growth, and for virtuous wage hikes to spread to the majority of small firms that employ a sizable proportion of the country's workforce. However, the current wage level in Japan is low compared with other major economies. Japan also faces structural issues such as higher hourly cash earnings not leading to higher disposable income, due to the heavier social burden and the so-called annual income barrier. The latter refers to the fact that households' secondary earners or seniors try to adjust their working hours so that their income stays under the ceiling for tax exemption. Meanwhile, Japan's income structure is heavily dependent on employee compensation, which accounts for more than 90 percent of households' disposable income. To alleviate households' concerns about the future, efforts to diversify their earning power are necessary, as in the case with the United States, where employee compensation accounts for about 70 percent of disposable income, with dividend and interest income accounting for about 20 percent (Chart 14). With the launch of the new Nippon Individual Savings Account (NISA) program, households have started to diversify their income sources, enabling them to earn more income not only through better business performance at the firm where they work, but also through greater returns from their investments that reflect the growth of listed firms (Chart 15). Sustained wage increases and higher wages accompanied by job changes, coupled with investment that focuses on the long term, on regular contributions, and on risk diversification, will lead to improved household dynamism, thereby strengthening households' earning power. The hope is that this will feed into improvement in households' consumption patterns (Chart 16).

The Bank of Japan will continue to conduct monetary policy as appropriate to support firms' management efforts, enhance the dynamism of firms, employment, and households, and guide the economy's return to a growth path.

Thank you.

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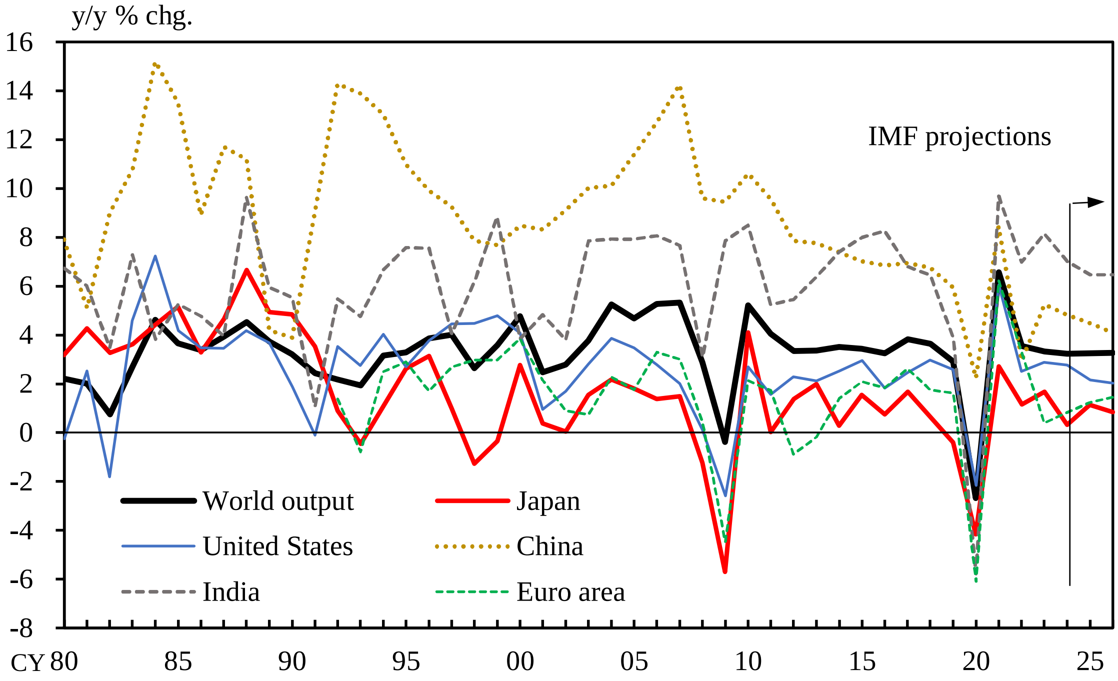
Chart 1

IMF Projections in the *World Economic Outlook* (October 2024)



Source: IMF.

Chart 2

Forecasts of the Majority of the Policy Board Members

y/y % chg.

	Real GDP	CPI (all items less fresh food)	(Reference) CPI (all items less fresh food and energy)
Fiscal 2024	+0.5 to +0.7 [+0.6]	+2.4 to +2.5 [+2.5]	+1.9 to +2.1 [+2.0]
Forecasts made in July 2024	+0.5 to +0.7 [+0.6]	+2.5 to +2.6 [+2.5]	+1.8 to +2.0 [+1.9]
Fiscal 2025	+1.0 to +1.2 [+1.1]	+1.7 to +2.1 [+1.9]	+1.8 to +2.0 [+1.9]
Forecasts made in July 2024	+0.9 to +1.1 [+1.0]	+2.0 to +2.3 [+2.1]	+1.8 to +2.0 [+1.9]
Fiscal 2026	+0.8 to +1.1 [+1.0]	+1.8 to +2.0 [+1.9]	+1.9 to +2.2 [+2.1]
Forecasts made in July 2024	+0.8 to +1.0 [+1.0]	+1.8 to +2.0 [+1.9]	+1.9 to +2.2 [+2.1]

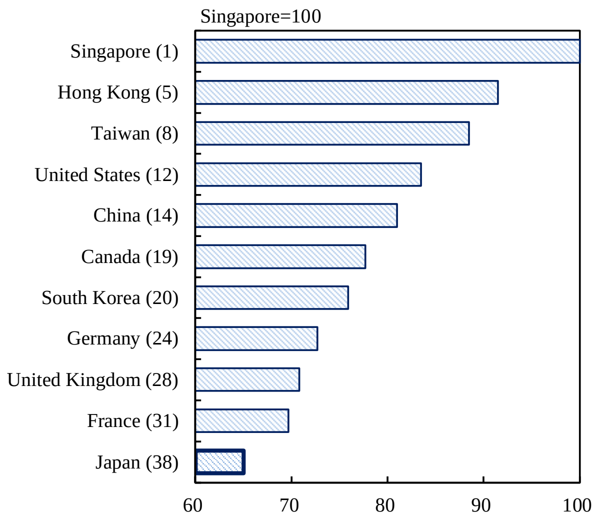
Notes: 1. Figures in brackets indicate the medians of the Policy Board members' forecasts (point estimates).
2. The forecasts of the majority of the Policy Board members are constructed as follows: each Policy Board member's forecast takes the form of a point estimate -- namely, the figure to which they attach the highest probability of realization. These forecasts are then shown as a range, with the highest figure and the lowest figure excluded. The range does not indicate the forecast errors.
3. Each Policy Board member makes their forecasts taking into account the effects of past policy decisions and with reference to views incorporated in financial markets regarding the future conduct of policy.

Source: Bank of Japan.

Chart 3

IMD World Competitiveness Ranking

Overall Score for 2024



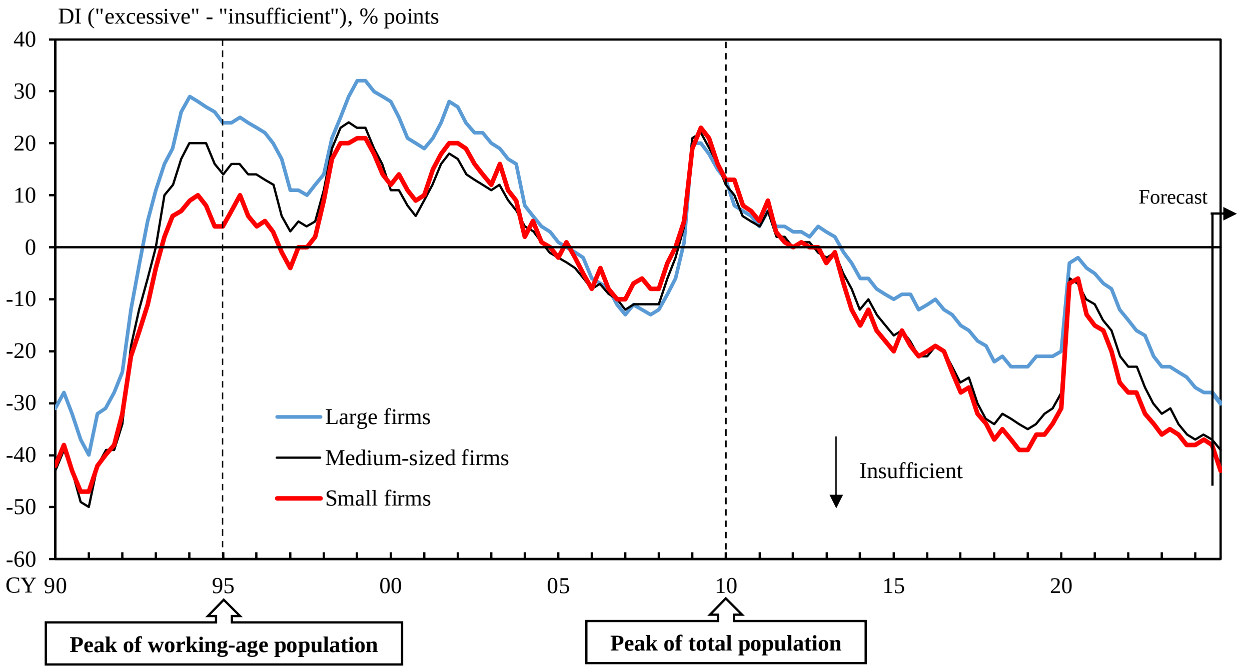
Japan's Ranking

Notes: 1. In the left panel, figures in parentheses indicate the ranking of the economy out of all 67 economies analyzed.
2. In the right panel, there is a discontinuity in the data for 1997 due to a change in the survey framework.

Source: IMD, "World Competitiveness Ranking 2024."

Chart 4

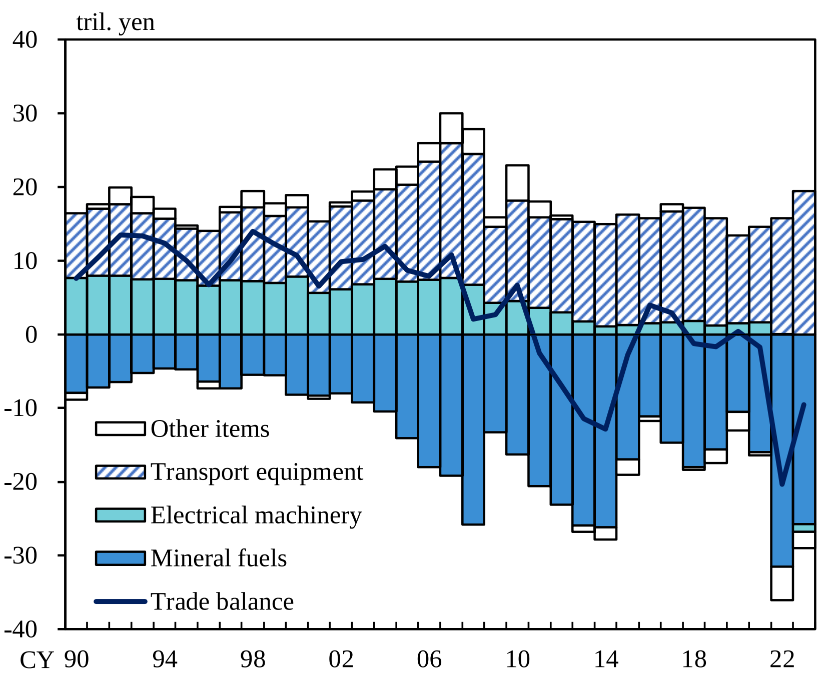
Diffusion Index (DI) for Employment Conditions



Note: Figures are for all industries, excluding financial institutions.
Source: Bank of Japan.

Chart 5

Nominal Trade Balance

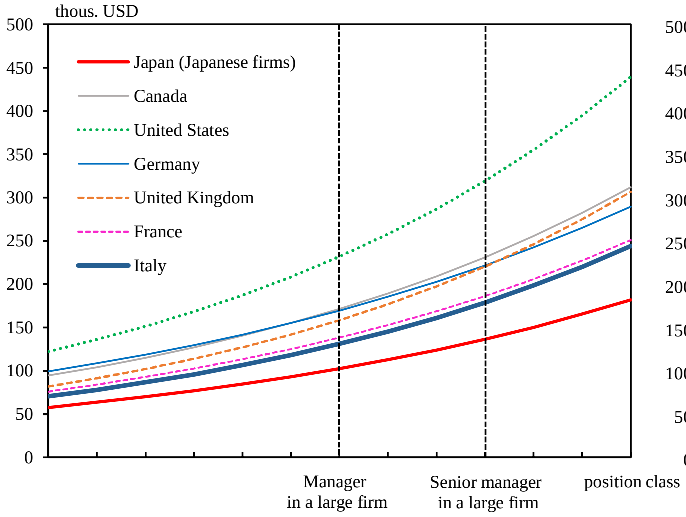


Source: Ministry of Finance.

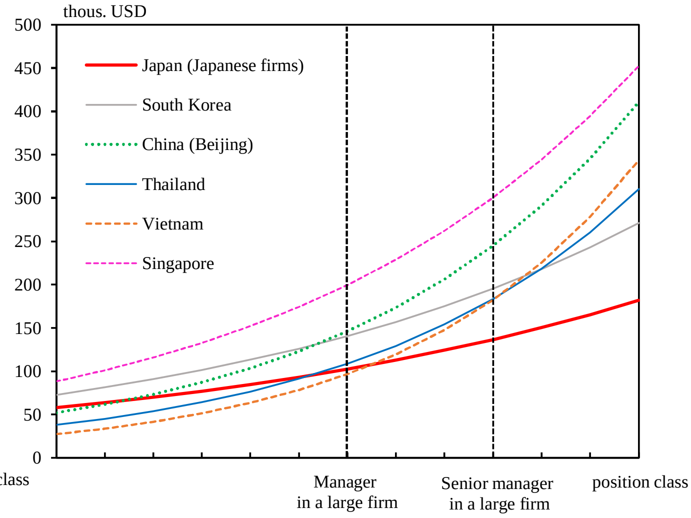
Chart 6

Annual Pay Comparison (as of 2024)

G7 Countries



Asian Economies



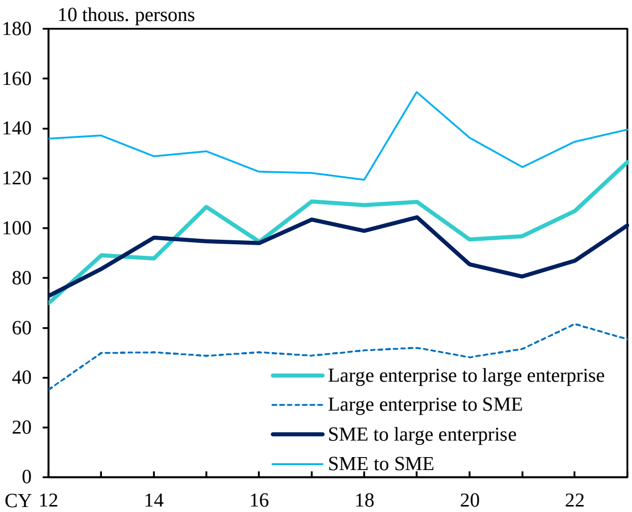
Notes: 1. The horizontal axis shows the level of the position class as defined by Mercer. Position classes below the executive level at large firms are shown in this chart. The further to the right, the higher the position class.
2. Figures include incentives paid for 100 percent achievement of performance targets and are the medians for each position class.

Source: Mercer, *2024 Total Remuneration Survey*.

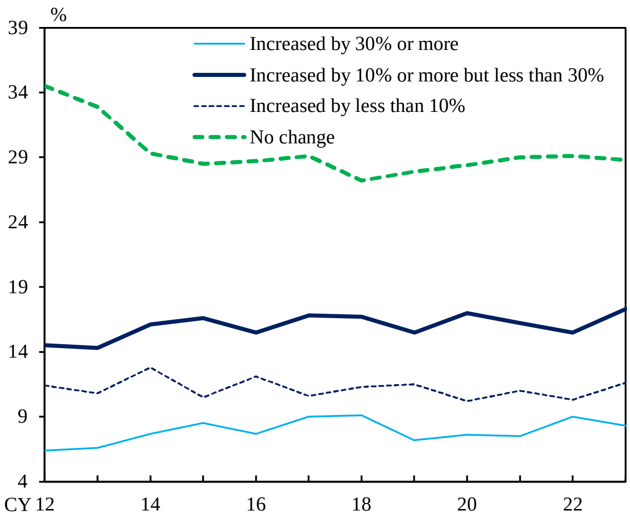
Chart 7

Labor Mobility and Wages

Number of Job Changers by Size of Enterprise



Share of Workers Who Experienced a Wage Increase after a Job Change



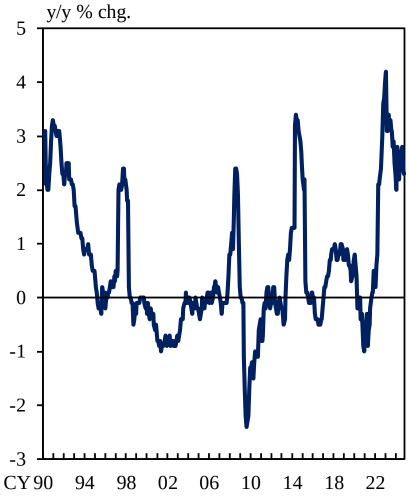
Note: In the left panel, small and medium-sized enterprises (SMEs) are enterprises with 5-299 employees. Large enterprises are those with 300 employees or more.

Source: Ministry of Health, Labour and Welfare.

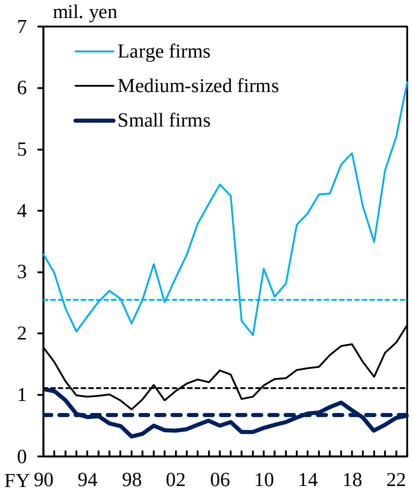
Chart 8

Three Indicators That Show Signs of Wage Increases

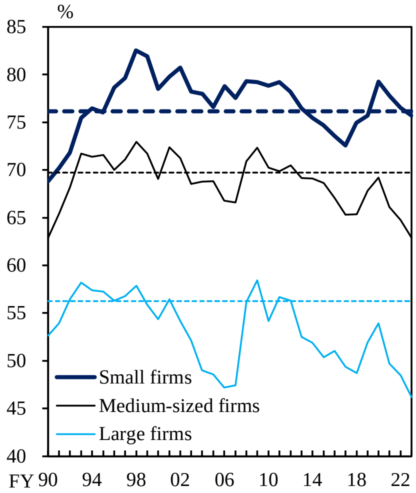
Prices



Operating Profits per Employee



Labor Share



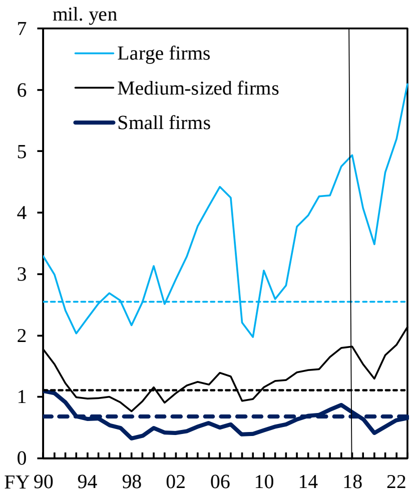
Notes: 1. Figures for prices are the CPI (all items less fresh food). Figures for operating profits per employee and labor share are based on the *Financial Statements Statistics of Corporations by Industry, Annually*, and exclude the finance and insurance industries. Large firms are commercial corporations with capital of 1 billion yen or more. Medium-sized firms are commercial corporations with capital of 100 million yen or more but less than 1 billion yen. Small firms are commercial corporations with capital of 10 million yen or more but less than 100 million yen. The dotted lines show the average values for the 1990s.
2. Labor share = personnel expenses / (operating profits + personnel expenses + depreciation expenses).

Sources: Ministry of Finance; Ministry of Internal Affairs and Communications.

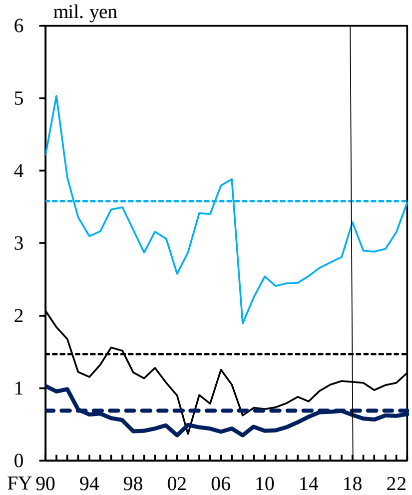
Chart 9

Recovery Status of Small and Medium-Sized Firms

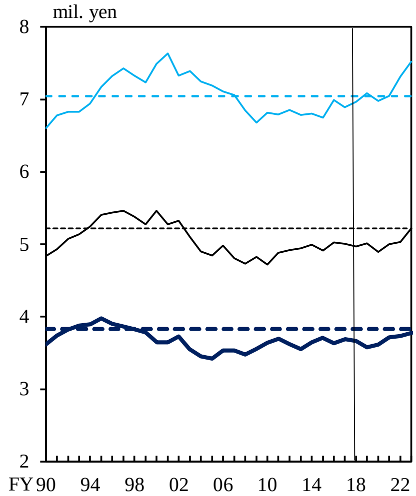
Operating Profits per Employee



Fixed Investment per Employee



Personnel Expenses per Employee



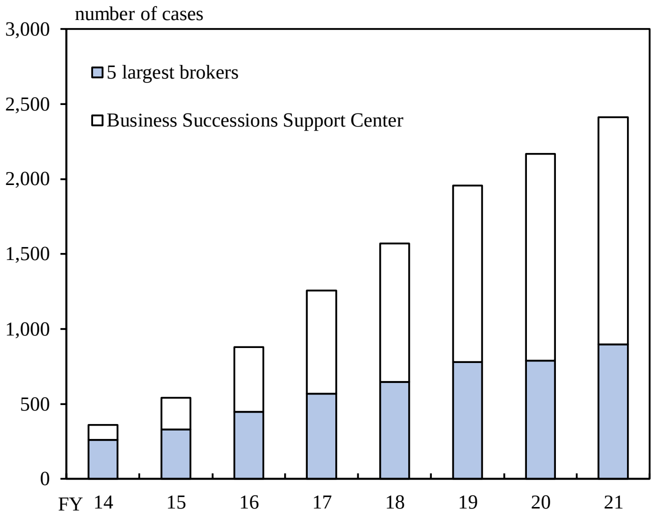
Notes: 1. Figures are based on the *Financial Statements Statistics of Corporations by Industry, Annually*, and exclude the finance and insurance industries. Large firms are commercial corporations with capital of 1 billion yen or more. Medium-sized firms are commercial corporations with capital of 100 million yen or more but less than 1 billion yen. Small firms are commercial corporations with capital of 10 million yen or more but less than 100 million yen. The dotted lines show the average values for the 1990s.
2. Personnel expenses include salaries and wages, bonuses, and welfare expenses.

Source: Ministry of Finance.

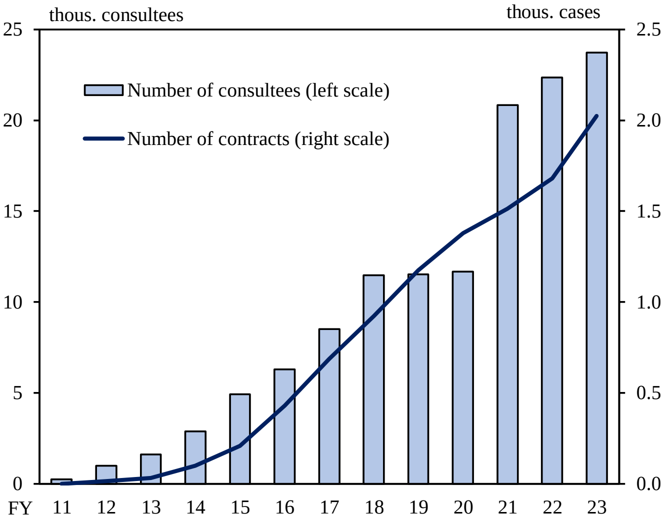
Chart 10

Progress in Structural Reforms by Small Firms

M&A Cases



Number of Business Successions



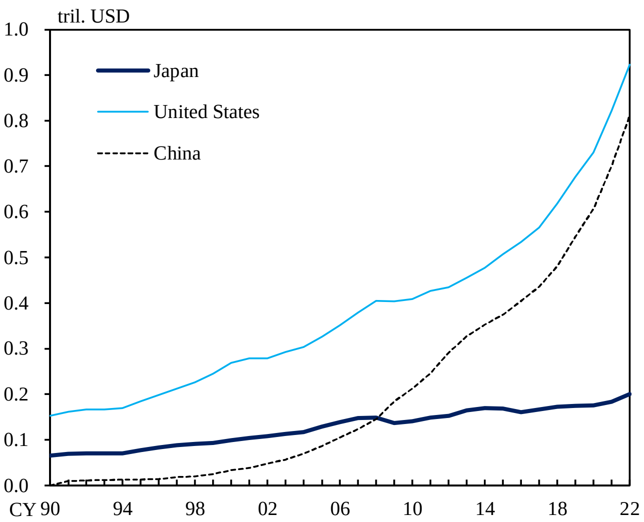
Notes: 1. The left panel is based on data from the report regarding the promotion of M&As among small firms released by the Small and Medium Enterprise Agency on June 21, 2022.
2. The right panel shows the number of consultees and the number of contracts concluded at the Business Successions Support Center.

Source: Small and Medium Enterprise Agency.

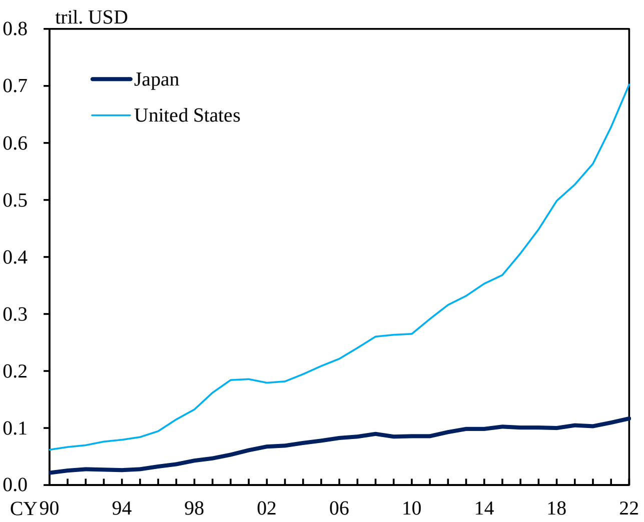
Chart 11

Investment in Innovation

R&D



Software Investment



Note: Figures are based on nominal values denominated in U.S. dollars.

Source: OECD.

Chart 12

Dynamism of Firms and Employment

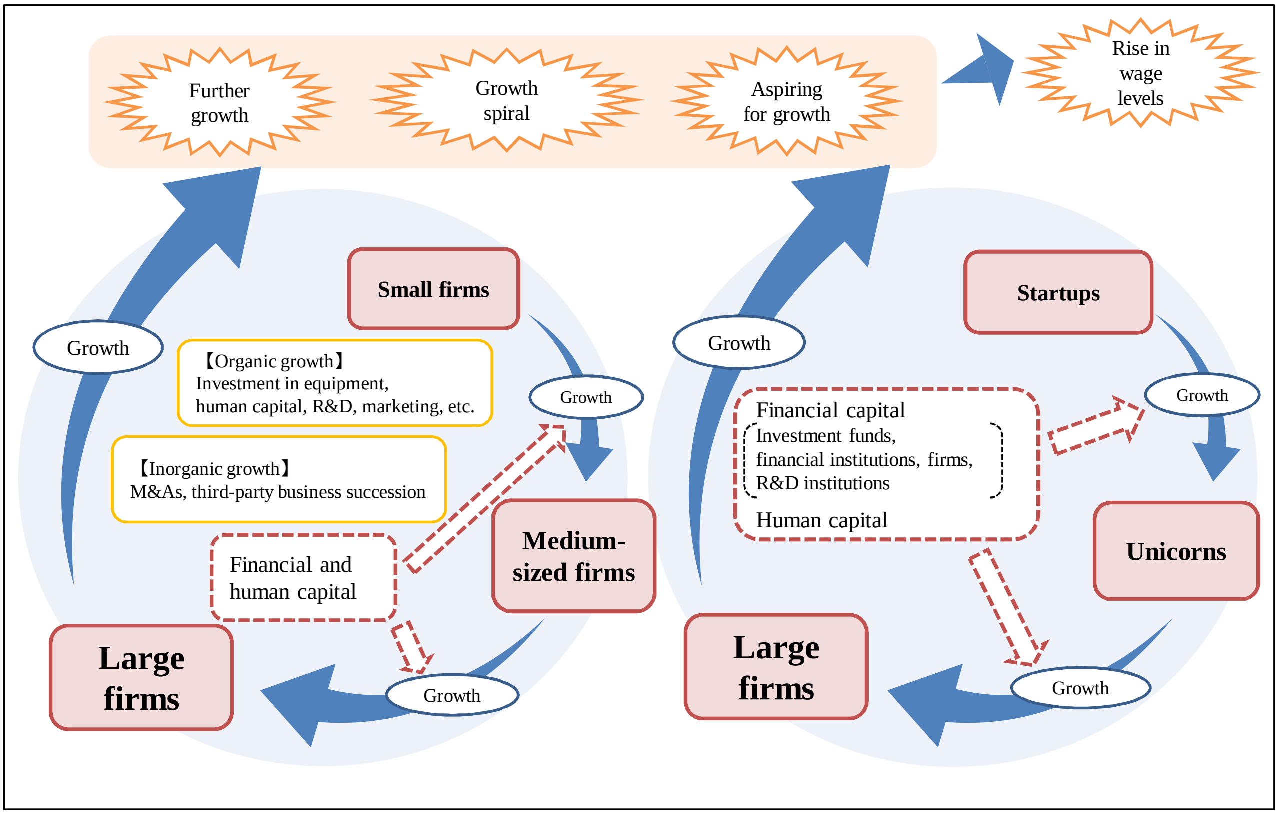
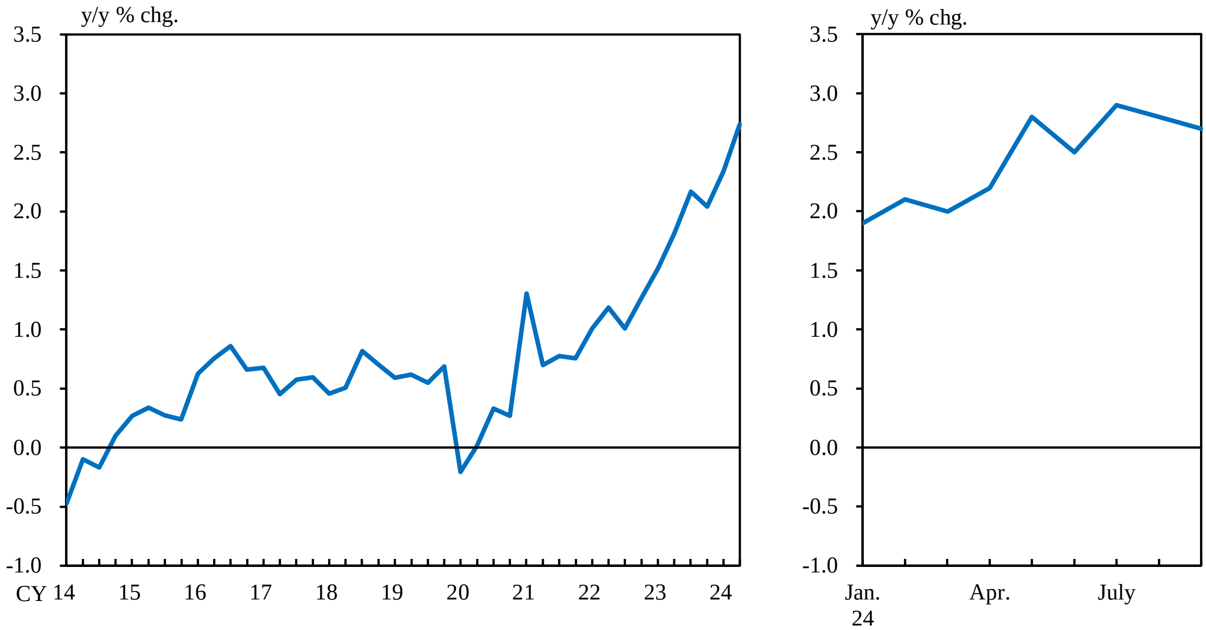


Chart 13

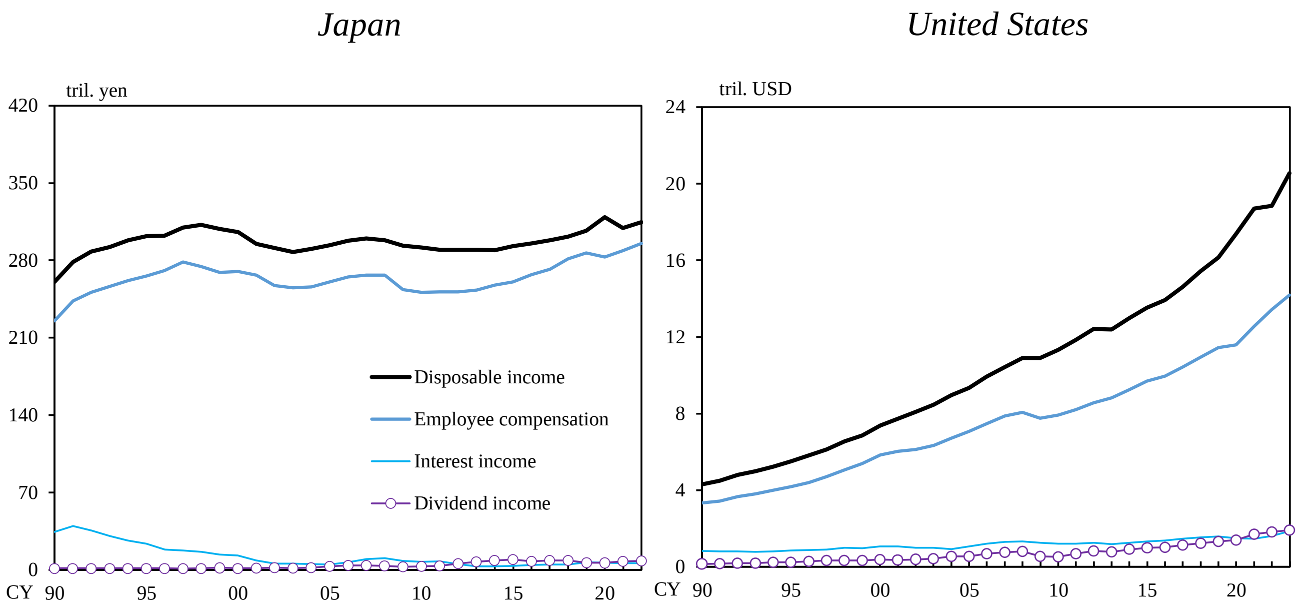
Scheduled Cash Earnings



Notes: 1. In the left panel, Q1=March-May, Q2=June-August, Q3=September-November, Q4=December-February.
2. Figures from fiscal 2016 onward are based on continuing observations following the sample revisions.

Source: Ministry of Health, Labour and Welfare.

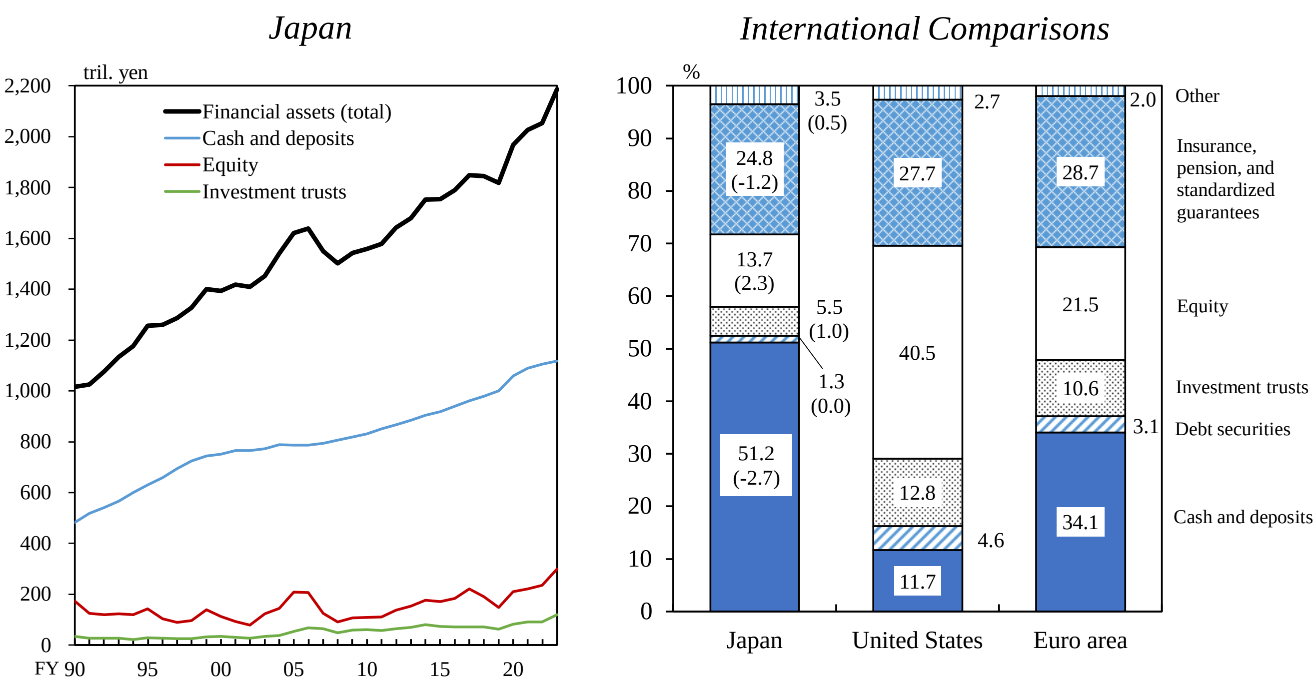
Household Disposable Income



Note: Figures for Japan before 1994 are calculated using year-on-year changes in each item based on the benchmark year of 2000.

Sources: Cabinet Office; U.S. Bureau of Economic Analysis (BEA).

Household Financial Assets



Note: In the right panel, figures are as of end-March 2024. Figures for the United States and the euro area are based on "Flow of Funds: Overview of Japan, the United States, and the Euro area," released by the Bank's Research and Statistics Department on August 30, 2024. Figures for Japan in parentheses indicate changes from the previous fiscal year (% points).

Source: Bank of Japan.

Dynamism of Households