

Japan: Market Insights

February 2024

Economic growth and inflation outlook

Growth and inflation to ease in 2024

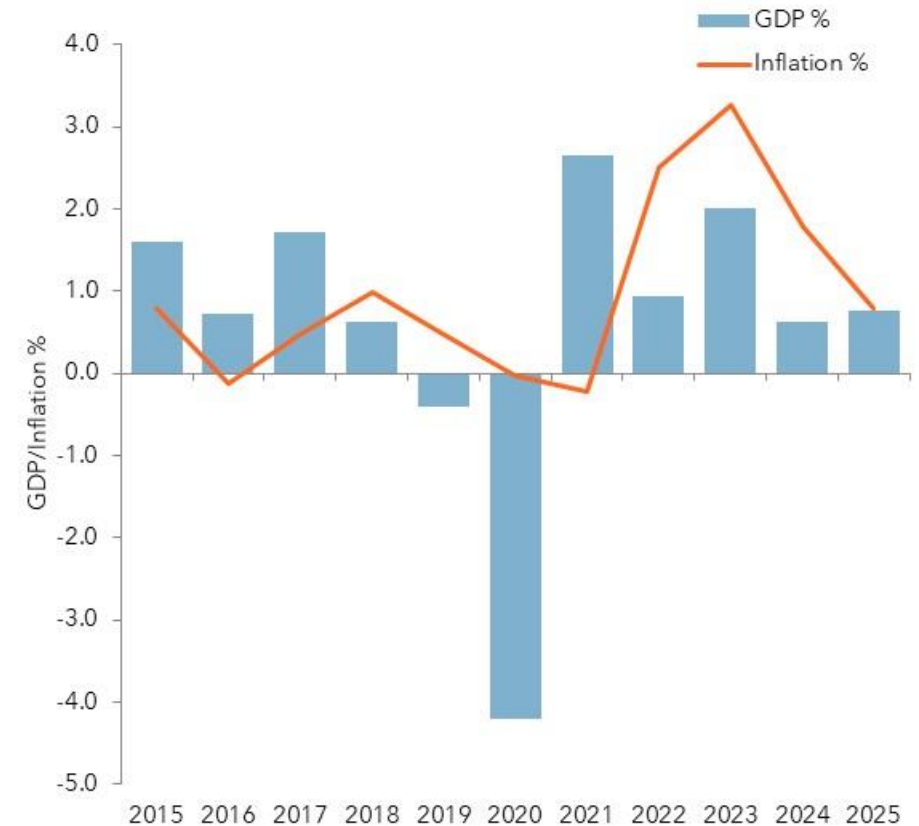
Japan's growth in GDP (gross domestic product) strengthened from 0.9% to 2.0% in 2023, and yet the economy was essentially stagnant in the final quarter. A fading of pent-up consumer spending and a loss of economic momentum in export markets is expected to see growth slip back to just 0.6% in 2024.

Spending remains weak among Japanese consumers, as real incomes are still negative, having failed to keep pace with inflation. In time, the strain from the dip in real incomes will ease, and this will pave the way for consumption to recover. Helped by labor shortages and robust corporate earnings, the *Spring Negotiation* is pointing toward wage rises similar to, or modestly higher than in 2023. Rising wages alongside moderating inflation should ease some of the real income burden on consumers. But any immediate recovery in consumer spending will be dampened by the continued erosion of post-pandemic pent-up demand.

Exports were generally weak during the final quarter of 2023. While demand for capital goods from Asia and the U.S. should be supportive in 2024, credit constraints combined with an easing of pent-up demand for motor vehicles will ensure only gradual gains for Japanese exports. In general, exports are likely to be sluggish throughout 2024.

Inflation advanced from 2.5% to 3.3% in 2023. As the effects of past price rises increasingly fade from the calculations, Oxford Economics expects inflation to slip to 1.8% in 2024 and then further to 0.8% in 2025.

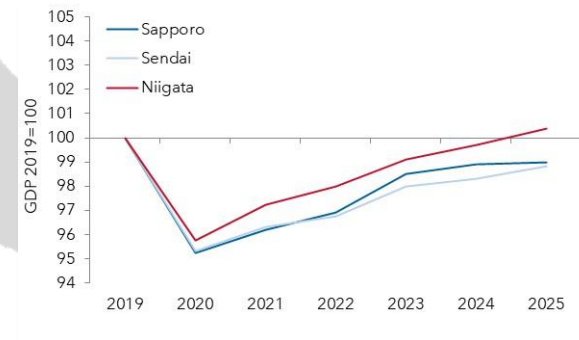
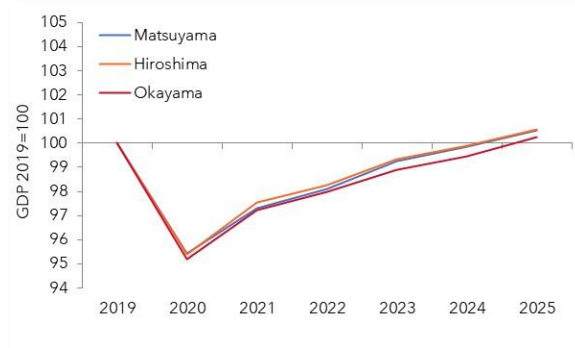
Economic growth and inflation



Economic outlook for Japan's key cities

Aside from Tokyo and Nagoya, growth prospects are generally weak

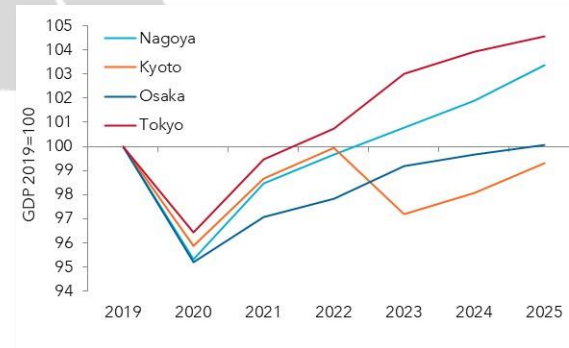
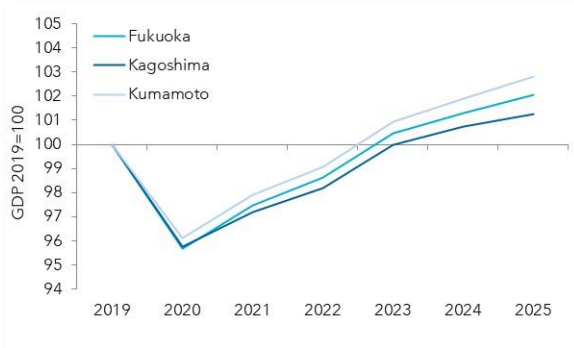
There has and is likely to be little material difference in the performance of these three cities' economies. All saw their gross domestic product (GDP) contract by almost 5% in 2020. Recovery has been slow. A return to 2019 levels of activity is not expected until 2025. Prospects are slightly weaker for Okayama's economy.



Recovery has been slow in northern Japan. By 2025, GDP in Sapporo and Sendai is still expected to be around 1% less than it was in 2019. Niigata should perform a little better, with GDP finally moving above pre-pandemic levels in 2025. But its economy may be only 0.4% larger.

All three cities' economies contracted by around 4% in 2020.

While all saw activity moved above 2019 levels in 2023, Kumamoto had the slightly stronger recovery. And it should lead the way through 2025, with GDP 3% larger than in 2019. Kagoshima will trail with an economy just 1% bigger by 2025.



Tokyo's economy led the recovery, with activity restored by 2022. By 2025, its GDP should be 5% larger than in 2019. The prospects for Nagoya are also encouraging, with 3.4% expansion expected.

In contrast, Osaka's economy may finally recover in 2025. Kyoto, having suffered a reversal in 2023, may still be more than 1% from recovery in 2025.

Japan's air travel market

Domestic air travel demand recovery has stalled

Almost 81 million passengers flew on domestic air services within Japan in 2019. By 2021, demand had dropped by more than 60% to just over 30 million.

Real progress towards recovery was made during 2022. At the start of the year, passenger numbers were still 47% below their pre-pandemic level. By the end of the year, the deficit had been cut to just 7%.

Since then, the market has found it difficult to secure a full return of domestic passengers. Throughout 2023, their numbers have remained below 2019 levels, with little sign of the gap narrowing. Despite rising by 34% year-over-year, domestic travel in 2023 was still 7% away from a full recovery. Demand growth is also losing momentum, with the pace of expansion slowing to 7% in November and to just 3% in December.

One encouraging sign of normality returning to the market, however, is that seasonal patterns in demand appear to have been largely restored.

International demand still a long way from recovery

Because of the overhang of restrictions on travel, the recovery in international demand has been much slower.

During 2021, international passenger numbers fell to just 7% of their pre-pandemic level. By the start of 2022, they were still down by around 90%, although the year ahead was characterized by a steady recovery. This left demand 43% below 2019 by December.

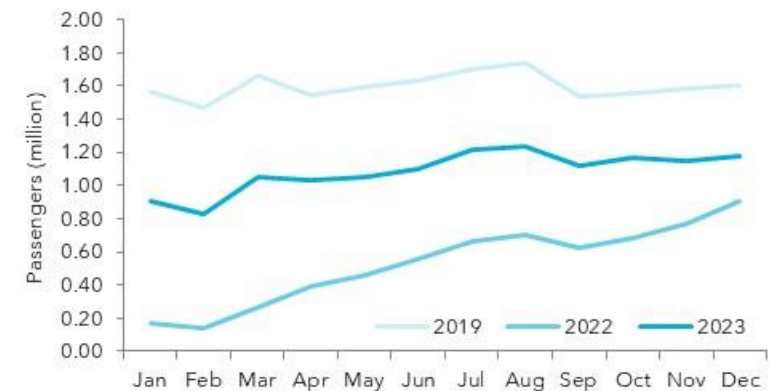
Progress towards recovery was much slower during 2023, despite demand more than doubling year-over-year (YoY). By December 2023, international air travel was still more than a quarter lower than in the same month in 2019. And the pace of YoY growth slowed markedly during the year, slipping to 30% by December.

Preliminary numbers from ANA show YoY growth continuing at around 30% at the start of 2024.

Domestic airline passengers



International airline passengers



Recovery in airline capacity

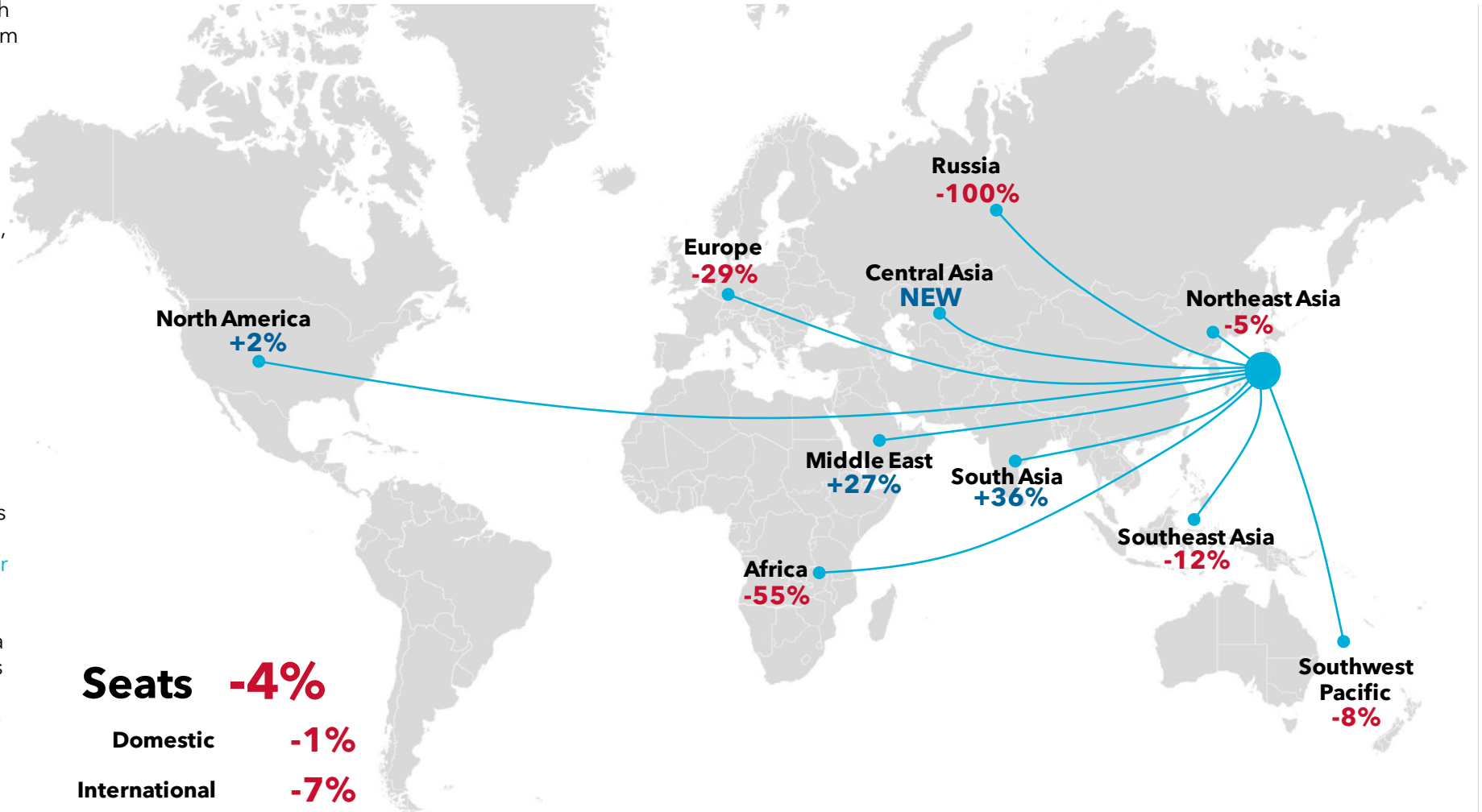
Airline capacity is below pre-pandemic levels in many markets

Domestic airline capacity in February 2024 was just **1%** lower in Japan than in the same month in **2019**. International capacity was further from recovery at **7%** lower, although airline seats were already some way above pre-pandemic levels in three regions.

South Asia has seen the biggest post-pandemic expansion in capacity, with airlines offering **36%** more seats. While there have been modest increases to India and Sri Lanka, growth has been driven largely by new connections to Bangladesh and Nepal.

Capacity to the Middle East is also more than **one quarter** higher than in 2019. This reflects strong growth to Turkey. In addition to its existing **daily** Tokyo Narita-Istanbul service, Turkish Airlines has added a **daily** flight from Haneda, whilst also linking Istanbul to Osaka with **four** weekly flights.

European capacity is still almost **30%** below its 2019 level. Seats to Finland, France Germany and the Netherlands are between **one quarter** and **one third** lower. Capacity shortfalls are even bigger to Belgium, Denmark and Italy, while flights have yet to be restored to Austria and Spain. But there are only **12%** fewer seats on offer to the U.K., while Poland and Switzerland can boast more non-stop seats to Japan than before the pandemic.



Growth in domestic air capacity

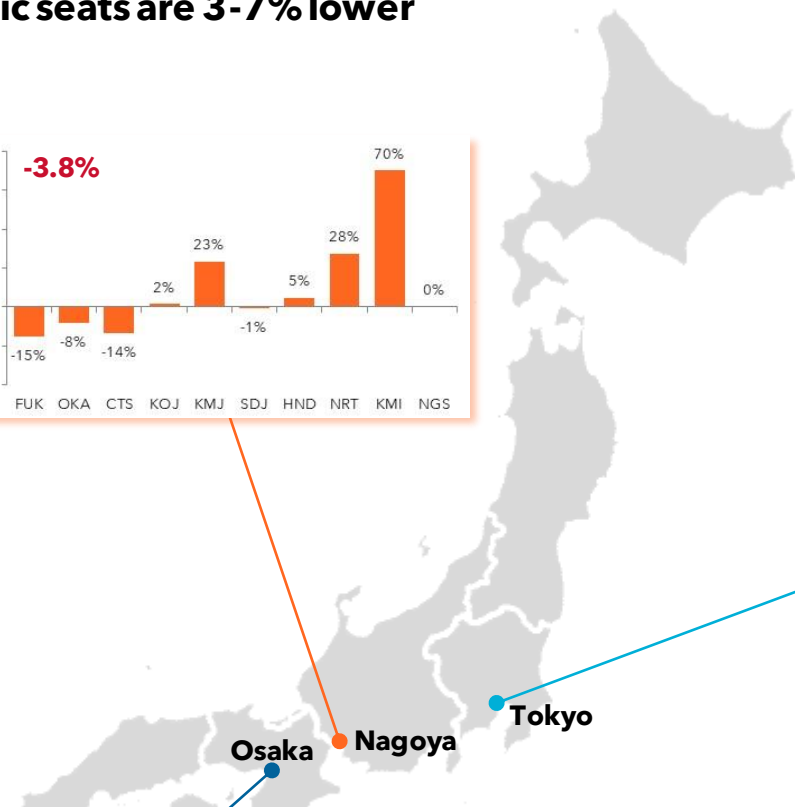
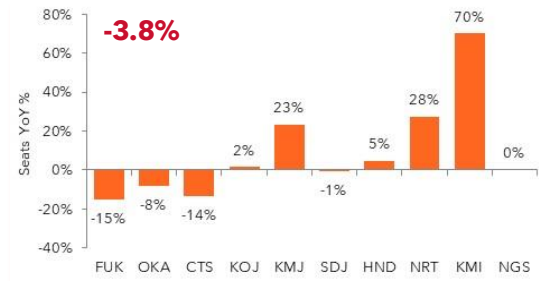
Across Japan's three largest markets, domestic seats are 3-7% lower

Domestic seat capacity across three of Japan's largest markets was down by 4% year-over-year (YoY) in February 2024. While seats from Tokyo (Haneda and Narita airports) and Nagoya (Chubu Centrair and Komaki) were 3-4% lower, Osaka (Itami and Kansai airports) recorded a deeper 7% decrease.

Among the airports most served from Tokyo, Osaka Itami (ITM), Kagoshima (KOJ) and Hiroshima (HIJ) have seen seat numbers decrease by around 10%. But capacity has increased slightly Kumamoto (KMJ) and Nagasaki (NGS), whilst remaining stable to Sapporo (CTS), Naha (OKA) and Osaka Kansai (KIX) airports.

The 4% decline in seats at Nagoya was driven by capacity cuts in the city's three largest domestic markets: Fukuoka, Naha and Sapporo. In contrast, capacity to some other leading markets - and Miyazaki (KMI) most notably - has seen some strong YoY increases.

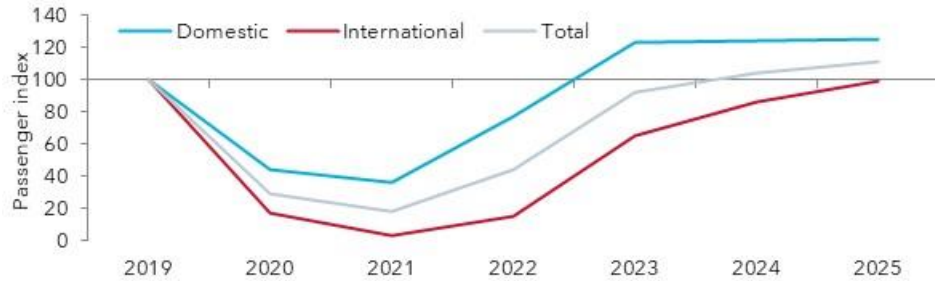
Seats fell YoY in February in most of the top domestic markets served from Osaka. Capacity to Kagoshima slumped by 28%. But there are now 10% more seats on flights to Fukuoka.



Air travel outlook

International recovery 2-3 years behind domestic

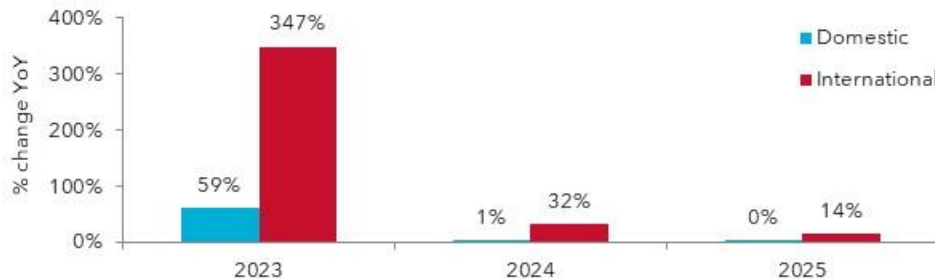
Air travel 2019=100



After falling to just 36% of their normal level in 2021, domestic passengers finally moved back above their pre-pandemic level in 2023, with strong growth pushing them 23% higher. But it seems the rebound in domestic demand will go no further.

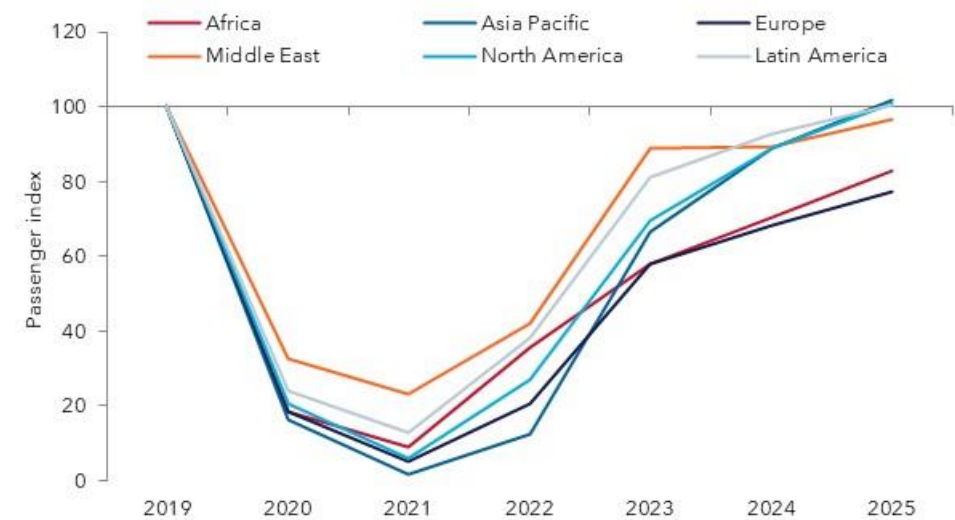
While the return of international demand had started a year later, full recovery may occur two or even three years after the restoration of domestic travel. By 2025, Tourism Economics believes international demand could still be just short of a full recovery. While passenger numbers surged by 347% in 2023, the recovery seems likely to rapidly lose momentum. Domestic travel will fair even worse, recording virtually no growth in 2024 and 2025.

Year-over-year growth in air travel: 2023-2025



Asia Pacific leading recovery in international air travel

Air travel by region 2019=100



Asia Pacific is Japan's dominant international air travel market, accounting for more than 80% of overseas trips. Demand in this market was hit harder than in any other region. After a slow start to its recovery, Asia Pacific should join Latin and North America as the first regions to see a full recovery in air travel to/from Japan in 2025. At this point, Africa and Europe should still be a long way from recovery.

The Middle East, which had been the region least impacted by the pandemic, had seemed poised for a full recovery in 2023 or 2024. However, the restoration of air travel demand now seems unlikely by 2025.

Airfares in 2023-2025

Average ticket prices in 2023

Short-haul fares lower year-over-year and vs 2019

The first half of 2023 had featured some strong year-over-year (YoY) movements in average ticket prices (ATPs) for short-haul travel, but this still left pricing below 2019 levels.

The situation changed dramatically in the second half, with fares lower in every month through November. This pushed ATPs **one quarter lower** than in 2019.



Long-haul fares much higher than in 2019

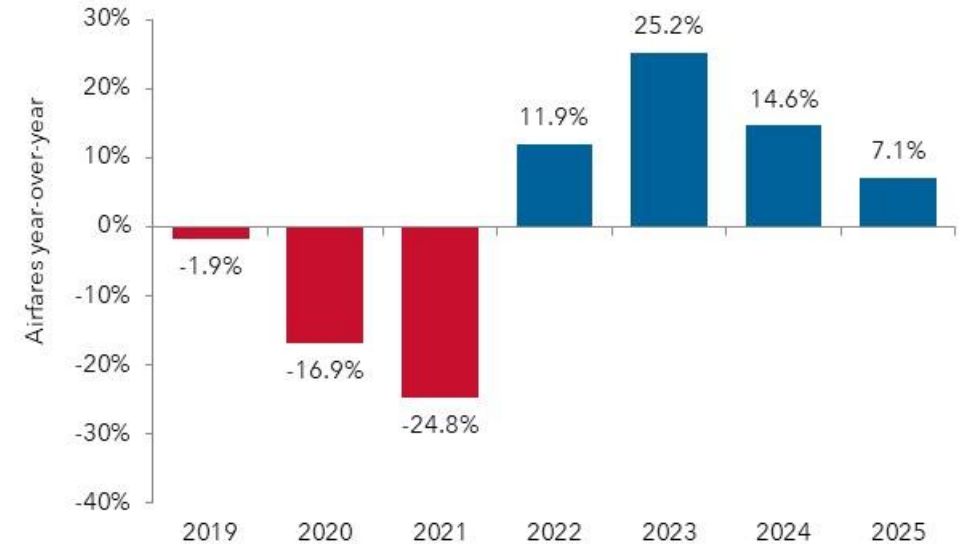
In contrast to short-haul fares, pricing for long-haul flights was weaker YoY during the first eight months of 2023, with only modest rises thereafter. On average, fares were **3%** lower during the 11-month period.

Due to some strong increases in **2020** and **2021**, ATPs were above pre-pandemic levels throughout 2023, averaging **19%** higher. However, this figure had eased to **11%** by November.



Outlook through 2025

Airfares year-over-year inflation

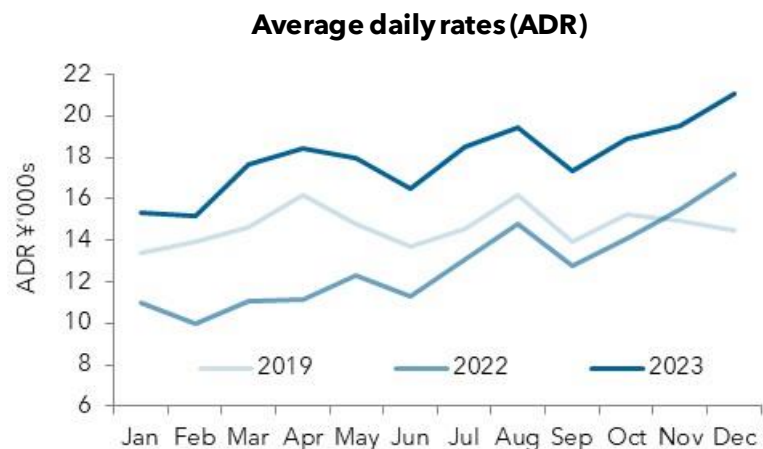


According to IATA data, Japanese airfares dipped by **2%** in 2019. The market then endured two years of steeply falling ticket prices, with fares dropping by **one quarter** in **2021** alone.

Airfares rebounded with a **12%** increase in **2022**. Following Japan's full reopening, travel's recovery drove airfares **25%** higher in **2023**. While inflation should ease in **2024**, IATA still forecasts a further **15%** rise in airfares, easing to **7%** in **2025**. At this stage, airfares may still only be **7%** higher than they were in 2019.

Hotel activity in the Japanese market

Strong rate recovery outpaces occupancy



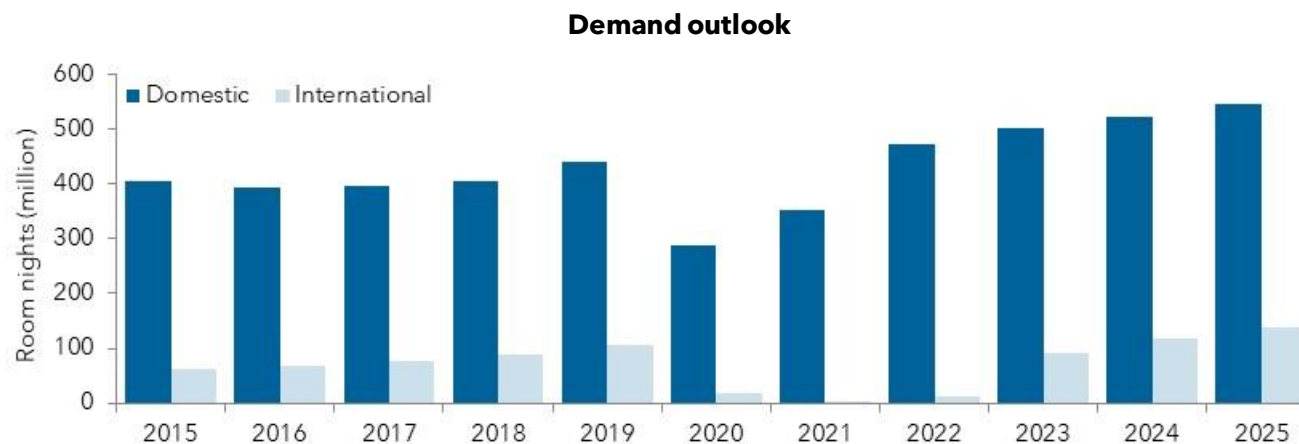
Source: BCD analysis of STR data, February 2024

Hotel occupancy made real progress in its recovery during 2022, starting the year at 44% and ending it above 75%. However, it remained below 2019 levels throughout 2023, averaging 74.2% for the year, compared to 82.3% in the pre-pandemic period. By December, occupancy was still around six-points from a full recovery, and it had dipped lower year-over-year.

The performance of average daily rates (ADRs) has been quite different. Even though occupancy had not recovered, by the end of 2022, ADRs had moved 19% higher than in December 2019. Room rates moved even higher during 2023, rising on average by 37% year-over-year (YoY) and to 23% above 2019. By the end of 2023, rate inflation had eased a little, but ADRs were still up 23% YoY.

Total hotel room nights decreased by 44% in 2020. Domestic guests, who had previously accounted for more than 80% of demand, saw room nights move back 7% above pre-pandemic levels in 2022. A full recovery in international demand is expected in 2024 and should herald some strong growth. By 2025, room nights from international travelers should be one-third higher than in 2019, overtaking the one-quarter expansion by domestic travelers.

Total demand for hotel rooms in Japan is expected to rise by 8% in 2024 and 7% in 2025.



Source: Tourism Economics, February 2024

Hotel rates in key cities

Tokyo bucked the trend of falling room rates during 2023

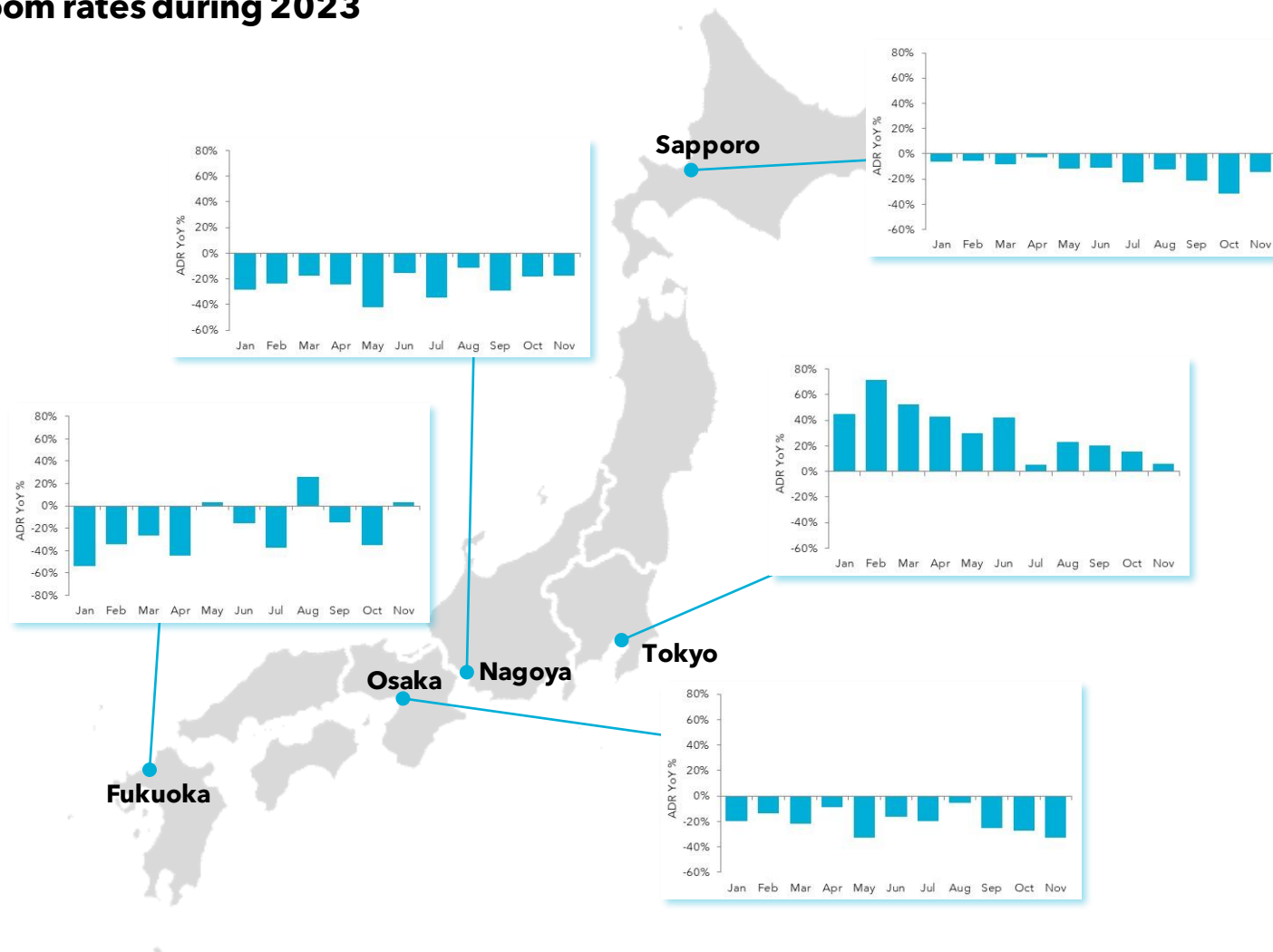
Corporate travelers saw average daily rates (ADR) for hotel accommodation in most of Japan's largest cities decrease year-over-year (YoY) throughout 2023.

The clear exception is **Tokyo**, where ADRs have been increasing quite steeply ever since the middle of 2022. However, the pace of rate inflation moderated during 2023, easing from a peak of **70%** in February down to just **6%** in November. This slowdown is an inevitable result of the numbers cycling over some big increases in the previous year.

Among other cities, **Sapporo's** hotels saw price decreases deepen as 2023 progressed, moving from January's **-6%** to **-14%** by November.

Osaka has seen a similar pattern: Decreases deepened from **20%** at the start of the year to **33%** by November 2023.

The situation is more varied elsewhere. **Fukuoka** saw a mix of price rises and falls during 2023, ending the period with November's **3%** rise. While prices fell throughout 2023 in **Nagoya**, the level of decrease ranged between **11%** and **42%**, depending on the month. After two months below 20%, there are tentative signs of rate deflation easing.



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