

Japan Economic Monthly

On the Heels of Abenomics Year One Results and Issues, Year Two Begins

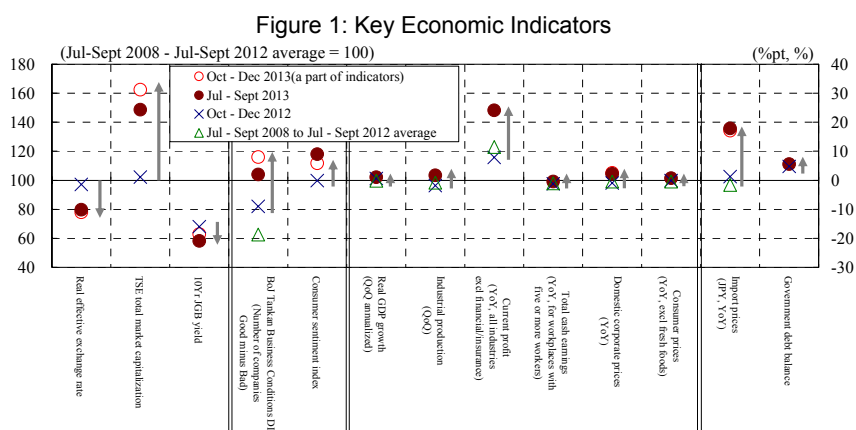
Economic Research Office
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1. The Real Economy

One year has passed since the launch of Prime Minister Shinzo Abe's second administration. Economic indicators now reflect the fruits of the first year of *Abenomics*, his economic policies. Beginning with the financial markets, which reacted positively to the policies from an early date, the JPY's real effective exchange rate (the weighted average of the JPY's value against the currencies of 43 trading partners adjusted for inflation) had fallen by 20% by Oct-Dec 2013, the market value of the Tokyo Stock Exchange was up by 59% on-year as of end-December (or JPY177 trillion), and the 10Yr JGB yield had declined by 0.06% points (Figure 1). Further, the Business Conditions DI in the BoJ's quarterly Tankan survey, which reflects corporate business sentiment, improved for four straight quarters, from -9% points in the December 2012 survey to +8% points in the December 2013 survey. Although the Consumer Confidence Index has dipped recently, it is higher than a year ago.

A number of economic indicators only show figures through Jul-Sept 2013, but real GDP growth continued to rise on-year for one year, from Oct-Dec 2012. Industrial production also started to expand in 2013. Corporate current profits in particular have improved strikingly. Current profit growth accelerated from +7.9% YoY in Oct-Dec 2012 to +24.1% YoY in Jul-Sept 2013 (for all industries excluding finance and insurance). On the other hand, total cash earning for household sector were still falling on-year (although they rose by +0.6% YoY in November, the first positive growth in five months). Some are still not enjoying the fruits of *Abenomics*.

Moreover, although domestic corporate goods prices and consumer prices have started to inch upward, import prices have been rising at a much faster pace (+17.1% YoY in Oct-Dec in JPY terms). The Government's handling of negative sides, including ballooning government debt burden, will be an issue for the second year of *Abenomics*.



Note: Right axis for BoJ Tankan Business Conditions DI and from Real GDP growth to Import prices.
 Source: Compiled by BTMU Economic Research Office from Bloomberg data, various materials.

2. Financial Markets

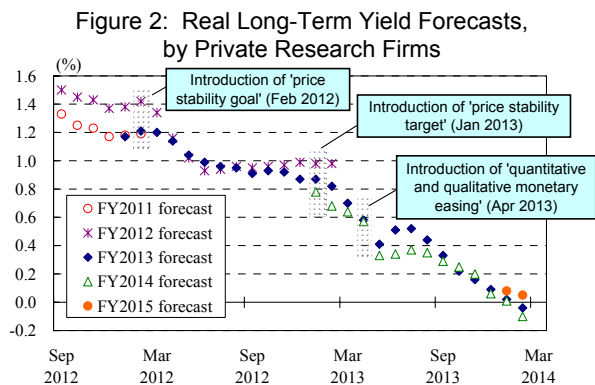
(1) Monetary Policy & Long-Term Yields

The BoJ agreed to maintain current monetary easing policy at the monthly Monetary Policy meeting January 21-22. The BoJ also made an interim assessment of the October *Outlook Report* at the meeting, re-iterating its view that *the year-on-year rate of increase in the consumer price index is likely to reach around 2 percent—the price stability target—toward the latter half of the forecast period (end-FY14 through FY15)*. The BoJ remains more bullish than the private sector inflation forecasts, but the massive quantitative monetary easing is clearly having an effect. The average of the real long-term yield forecasts (the 10Yr JGB yield minus ex-fresh food core inflation) by private sector has been declining with stronger monetary easing, to nearly zero recently (Figure 2). This shows that the BoJ has been successful at suppressing the nominal yield and rising inflation expectations. The BoJ is expected to ascertain the results of its operations while maintaining current policy. The 10Yr JGB yield rose together with the US yields through the end of last year, but has once again returned to the 0.6% level of late.

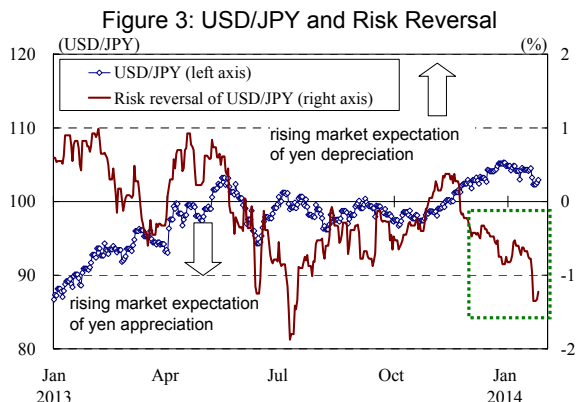
(2) Exchange Rates

USD/JPY has broken out of the upper JPY90 range, in which it had traded for several months, hitting the USD/JPY105 level at the end of 2013. Since the beginning of the year, the JPY has started to strengthen once again (Figure 3). This was blamed on the weakness of current employment statistics in the US in December as well as growing concerns about emerging market economies. However, risk reversal indicators, which reflect the direction of risk awareness among market participants, shows that concerns about the JPY strengthening had already begun to build by mid-December. The JPY had weakened quickly, and a correction was considered likely. There are still concerns about the JPY strengthening even

now. Although it seems unlikely that the JPY's weakening will stop anytime soon as the gap between US and Japan degrees of monetary easing widen, risk-averse buying of the JPY could occur amidst still-weak overseas economies. This possibility bears watching.



Note: 10Yr yield forecast (ESP Forecast survey) minus CPI (excl fresh foods) forecast (ESP Forecast survey, excl direct impact of FY14, FY15 consumption tax hikes).
 Source: Compiled by BTMU Economic Research Office from Japan Center for Economic Research materials.



Note: Risk reversal is call option implied volatility (25 delta, 1-month contract, annualized conversion value) minus put option implied volatility (same).
 Source: Compiled by BTMU Economic Research Office from Bloomberg data.

(Yasuhiro Ishimaru, Rei Tsuruta)

MAIN ECONOMIC AND FINANCIAL INDICATORS (JAPAN)

1. Main Economic Indicators

As of Mar. 4, 2014

	Fiscal 2011	Fiscal 2012	2013			2013				2014
			2Q	3Q	4Q	SEP	OCT	NOV	DEC	JAN
Real GDP Growth Rate <% changes from previous period at SA annual rate>	0.3	0.6	3.9 (1.2)	1.1 (2.3)	1.0 (2.7)	***	***	***	***	***
Index of All Industries Activity	0.3	0.1	1.0 (0.5)	0.6 (1.6)	0.2 (1.8)	0.5 (2.3)	-0.4 (1.7)	0.4 (1.8)	-0.1 (2.2)	
Industrial Production Index Production	-0.7	-2.9	1.5 (-3.1)	1.7 (2.3)	1.8 (5.7)	1.3 (5.1)	1.0 (5.4)	-0.1 (4.8)	0.9 (7.1)	4.0 (10.6)
Shipments	-1.5	-1.8	-1.9 (-3.5)	0.6 (1.6)	3.5 (6.4)	1.5 (4.6)	2.3 (6.3)	0.0 (6.6)	0.8 (6.3)	5.1 (9.0)
Inventory	12.1	-2.7	0.4 (-2.9)	1.2 (-3.5)	-2.5 (-4.3)	-0.2 (-3.5)	-0.3 (-3.8)	-1.8 (-5.1)	-0.5 (-4.3)	-0.9 (-3.7)
Inventory/Shipments Ratio (2010=100)	109.0	114.4	107.6 [111.5]	111.0 [116.4]	105.1 [117.7]	110.1 [118.5]	106.0 [117.7]	104.7 [117.7]	104.6 [117.7]	98.7 [113.2]
Domestic Corporate Goods Price Index	1.4	-1.1	0.7 (0.7)	0.8 (2.2)	0.2 (2.5)	0.2 (2.2)	-0.1 (2.5)	0.0 (2.6)	0.3 (2.5)	0.1 (2.4)
Consumer Price Index(SA, total, excl.fresh foods)	0.0	-0.2	0.7 (0.0)	0.4 (0.7)	0.3 (1.1)	0.0 (0.7)	0.2 (0.9)	0.2 (1.2)	-0.1 (1.2)	0.2 (1.3)
Index of Capacity Utilization (2010=100)	97.9	95.4	96.6 [99.6]	98.3 [95.1]	100.0 [93.1]	98.4 [91.9]	99.6 [93.0]	99.1 [92.3]	101.3 [94.0]	
Machinery Orders(Private Demand, Excl.Electric Power and Ship building)	6.2	-3.0	6.8 (6.4)	4.3 (9.6)	1.5 (13.3)	-2.1 (11.4)	0.6 (17.8)	9.3 (16.6)	-15.7 (6.7)	
Manufacturing	5.9	-10.1	5.6 (-4.2)	9.8 (8.2)	0.6 (14.8)	4.1 (17.3)	-0.2 (21.9)	6.0 (18.9)	-17.3 (5.5)	
Non-manufacturing Excl.Electric Power & Ship building	6.6	2.8	12.5 (14.1)	-4.1 (10.4)	7.5 (12.4)	-7.0 (8.0)	11.5 (15.1)	8.1 (15.1)	-17.2 (7.6)	
Shipments of Capital Goods (Excl.Transport Equipment)	6.7	-6.0	-0.2 (-5.4)	0.4 (0.3)	5.7 (10.8)	-1.5 (0.7)	9.3 (14.8)	-3.2 (10.4)	0.8 (7.6)	14.9 (22.9)
Construction Orders	7.1	2.4								
Private	3.7	2.6								
Public	22.7	5.3								
Public Works Contracts	-0.5	10.3								
Housing Starts 10,000 units at Annual Rate, SA	84.1 (2.7)	89.3 (6.2)	98.3 (11.8)	100.4 (13.5)	102.6 (12.9)	102.8 (19.4)	103.0 (7.1)	103.7 (14.1)	105.5 (18.0)	98.7 (12.3)
Total floor	(2.5)	(4.8)	(11.6)	(13.0)	(13.8)	(18.1)	(9.4)	(15.2)	(17.1)	(10.5)
Sales at Retailers	0.8	0.3								
Real Consumption Expenditures of Households over 2 persons (SA)	-1.2	1.6	-1.9 (-0.2)	-0.3 (0.7)	-0.2 (0.6)	1.0 (3.7)	0.3 (0.9)	-0.2 (0.2)	-0.4 (0.7)	1.6 (1.1)
Propensity to Consume (SA,%)	73.3	74.8	74.0 [74.4]	74.8 [74.1]	74.6 [74.5]	75.6 [74.1]	75.3 [74.2]	74.9 [74.9]	75.0 [75.1]	75.9 [76.1]
Overtime Hours Worked (All Industries, 5 employees or more)	0.8	-0.3	2.7 (1.0)	0.1 (4.0)	1.6 (6.0)	-0.5 (3.9)	1.2 (5.8)	1.2 (6.7)	-0.1 (5.6)	
Total Cash Earnings (Regular Employees Only; All Industries, 5 employees or more)	-0.3	-0.7								
Employment Index(Regular Employees Only;All Industries, 5 employees or more) (Change over the M/Q/Y)	52	107	33 138	43 131	49 133	46	46	53	48	
Ratio of Job Offers to Applicants (SA,Times)	0.68	0.82	0.90 [0.80]	0.95 [0.81]	1.01 [0.82]	0.96 [0.81]	0.98 [0.82]	1.01 [0.82]	1.03 [0.83]	1.04 [0.84]
Unemployment Rate (SA,%)	4.5	5.0	4.0	4.0	3.9	4.0	4.0	3.9	3.7	3.7
Economy Watcher Survey (Judgment of the present condition D.I,%)	44.9	46.3	55.1 [47.3]	52.1 [43.0]	53.7 [41.6]	52.8 [41.2]	51.8 [39.0]	53.5 [40.0]	55.7 [45.8]	54.7 [49.5]
Bankruptcies (Number of cases)	12,707 (-2.7)	11,719 (-7.7)	2,841 (-9.1)	2,664 (-8.8)	2,571 (-11.0)	820 (-11.9)	959 (-7.3)	862 (-10.5)	750 (-15.7)	864 (-7.4)

(Notes)

Unless otherwise indicated, tabulated figures and those in parentheses show % changes from previous quarter/month as applicable.

The figures in () indicate % changes from previous year.

[] show the comparable figure of the previous year.

2. Balance of Payments

As of Mar. 4, 2014

	Fiscal	Fiscal	2013			2013					2014
	2011	2012	2Q	3Q	4Q	SEP	OCT	NOV	DEC	JAN	
Customs Clearance(Exports in Yen Terms)	-3.7	-2.1	(7.1)	(12.7)	(17.4)	(11.5)	(18.6)	(18.4)	(15.3)	(9.5)	
Value	1.7	4.0	(10.5)	(12.1)	(12.5)	(13.6)	(13.6)	(11.5)	(12.4)	(9.7)	
Volumes	-5.3	-5.8	(-3.1)	(0.6)	(4.3)	(-1.8)	(4.4)	(6.2)	(2.5)	(-0.2)	
Imports(In Yen terms)	11.6	3.5	(10.4)	(17.5)	(24.0)	(16.6)	(26.2)	(21.2)	(24.7)	(25.1)	
Value	9.2	2.5	(12.2)	(18.1)	(17.8)	(19.1)	(18.7)	(15.4)	(19.1)	(15.7)	
Volumes	2.2	1.0	(-1.5)	(-0.5)	(5.4)	(-2.1)	(6.4)	(5.0)	(4.7)	(8.0)	
Current Balance(100 mil. yen)	76,180	43,536	17,287	13,523	-13,593	5,948	-1,279	-5,928	-6,386		
Trade Balance(100 mil. yen)	-34,698	-68,921	-19,624	-27,452	-35,588	-8,870	-10,919	-12,543	-12,126		
Services(100 mil. yen)	-18,265	-25,417	-3,334	-4,116	-6,561	-922	-3,137	-1,100	-2,324		
Capital and Financial Accounts(100 mil. yen)	29,618	-49,201	23,052	-7,458	28,777	1,631	4,073	6,443	18,261		
Gold & Foreign Exchange Reserves(\$1mil.)	1,288,703	1,254,356	1,238,713	1,273,446	1,266,815	1,273,446	1,276,751	1,275,352	1,266,815	1,277,058	
Exchange Rate(US\$)	79.05	83.08	98.74	98.94	100.45	99.24	97.85	100.03	103.46	103.94	

3. Financial Market Indicators

	Fiscal	Fiscal	2013			2013					2014
	2011	2012	2Q	3Q	4Q	SEP	OCT	NOV	DEC	JAN	
Uncollateralized Overnight Call Rates	0.077	0.083	0.073 [0.078]	0.073 [0.085]	0.072 [0.084]	0.072 [0.085]	0.070 [0.085]	0.073 [0.085]	0.074 [0.082]	0.073 [0.083]	
Euro Yen TIBOR (3 Months)	0.331	0.312	0.228 [0.333]	0.228 [0.327]	0.220 [0.318]	0.228 [0.327]	0.221 [0.326]	0.220 [0.318]	0.220 [0.308]	0.220 [0.292]	
Newly Issued Japanese Government Bonds Yields (10 Years)	1.050	0.760	0.772 [0.848]	0.732 [0.780]	0.642 [0.757]	0.680 [0.765]	0.590 [0.775]	0.600 [0.700]	0.735 [0.795]	0.620 [0.740]	
Average Contracted Interest Rates on Loans and Discounts(City Banks) (% changes from previous period)	1.269	1.184	1.153 (-0.031)	1.125 (-0.028)	1.102 (-0.023)	1.125 (-0.014)	1.124 (-0.001)	1.114 (-0.010)	1.102 (-0.012)	1.096 (-0.006)	
The Nikkei Stock Average (TSE 225 Issues)	10,084	12,398	13,677 [9,007]	14,456 [8,870]	16,291 [10,395]	14,456 [8,870]	14,328 [8,928]	15,662 [9,446]	16,291 [10,395]	14,915 [11,139]	
M2(Average)	(2.9)	(2.5)	(3.5)	(3.8)	(4.2)	(3.9)	(4.1)	(4.4)	(4.3)	(4.4)	
Broadly-defined Liquidity(Average)	(0.2)	(0.5)	(2.6)	(3.5)	(4.4)	(3.8)	(4.2)	(4.5)	(4.5)	(4.4)	
Principal Figures of Financial Institutions											
Loans and Discount (Average)	Banks & Shinkin		(-0.1)	(0.9)	(1.8)	(2.0)	(2.2)	(2.0)	(2.2)	(2.3)	(2.3)
	Banks		(-0.1)	(1.1)	(2.1)	(2.3)	(2.4)	(2.2)	(2.3)	(2.4)	(2.5)
	City Banks etc.		(-1.8)	(-0.2)	(1.6)	(1.9)	(1.8)	(1.9)	(1.7)	(1.8)	(1.8)
	Regional Banks		(1.9)	(2.9)	(3.2)	(3.2)	(3.3)	(3.1)	(3.1)	(3.3)	(3.4)
	Regional Banks II		(1.1)	(0.8)	(0.6)	(0.7)	(2.0)	(0.9)	(1.9)	(2.0)	(2.1)
Shinkin		(-0.5)	(-0.7)	(-0.2)	(0.1)	(0.5)	(0.1)	(0.4)	(0.5)	(0.6)	
Deposits and CDs (Average)	Total(3 Business Condition)		(2.7)	(2.2)	(3.8)	(3.8)	(3.9)	(3.8)	(3.9)	(4.0)	(3.8)
	City Banks		(1.9)	(1.8)	(4.1)	(3.7)	(3.7)	(3.5)	(3.7)	(3.7)	(3.8)
	Regional Banks		(3.7)	(2.8)	(4.0)	(4.5)	(4.5)	(4.6)	(4.4)	(4.6)	(4.4)
	Regional Banks II		(2.8)	(1.8)	(1.5)	(2.1)	(3.2)	(2.6)	(3.1)	(3.3)	(3.3)

(Notes)

Interest rates are averages. The Nikkei Stock Average is as of month-end.

Unless otherwise indicated, tabulated figures and those in parentheses show % changes from previous quarter/month as applicable.

The figures in () indicate % changes from previous year.

[] show the comparable figure of the previous year.

(Sources)

Cabinet Office, National Accounts, Machinery Orders; METI, Indices of Tertiary Industry Activity, Industrial Production, Current Survey of Commerce; MOF, Trade Statistics, Balance of Payments; MPMHAPT, Consumer Price Index, Family Income and Expenditure Survey, Labour Force Survey; MHLW, Monthly Labour Survey; Ministry of Land, Infrastructure, and Transport, Economic Construction Statistics; BOJ, Corporate Price Index, Financial and Economic Statistics Monthly, etc.

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