

Corporations' business results remain strong, yet there is a risk of downward pressure in the future

YUMIKO HISHIKI
YUUSUKE YOKOTA
ECONOMIC RESEARCH OFFICE

12 OCTOBER 2018

MUFG Bank, Ltd.
A member of MUFG, a global financial group

(ORIGINAL JAPANESE VERSION RELEASED ON 21 SEPTEMBER 2018)

1. The Real Economy

Corporations' business results remain strong. According to Financial Statements Statistics of Corporations, sales of all industries (excluding finance and insurance) grew by 5.1% YoY in the April-June 2018 quarter, increasing for the seventh consecutive quarter. Ordinary profits rose by 17.9% YoY, accelerating for the first time in five quarters and recording the eighth consecutive quarter of growth with a record-high level of profits (Chart 1). Analysis of the factors for the year-on-year change in ordinary profits reveals that this strong growth was brought about by an increase in sales – reflecting robust domestic and external demand – and the contribution from non-operating revenue and expenses turning positive due to a rise in dividends from overseas subsidiaries and such, despite downward pressures such as an increase in personnel expenses owing to the labour shortage. In addition, corporations are strengthening their attitudes toward investment on the back of this “increase in profits associated with business growth”, and real capital expenditure rose by 12.8% QoQ annualised (on a GDP basis) in the April-June quarter.

That being said, it is important to cautiously monitor the sustainability of the current profit environment. Looking at the World Economic Climate included in the World Economic Survey (WES), a questionnaire study of economic experts around the world such as research institutes and financial institutions conducted by the Ifo Institute in Germany, the index of “economic expectations for the next six months” dropped considerably, falling to its lowest level since the October-December 2011 quarter, which was when the European debt crisis hit (Chart 2). Contrary to the robust growth of the global economy at present, the extent of the slump in the forecast indicates the high level of caution regarding trade friction and the potential size of its impact. As this index is based on a questionnaire, it may fluctuate depending on the direction of future policies. However, considering the correlation between the index and Japan's exports up until now, it is important to be sufficiently cautious regarding the risk that the worsening trade friction will put downward pressure on corporate profits through future deterioration of the export environment, and also bring about negative impacts on the increasing trend of capital expenditure.

Chart 1: Ordinary Profits of Non-Financial Corporations

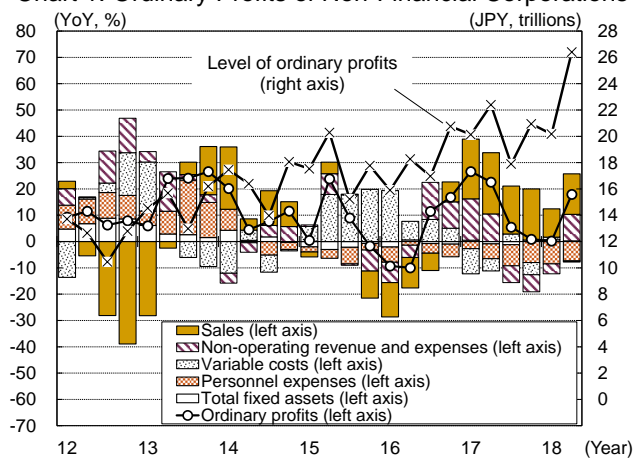
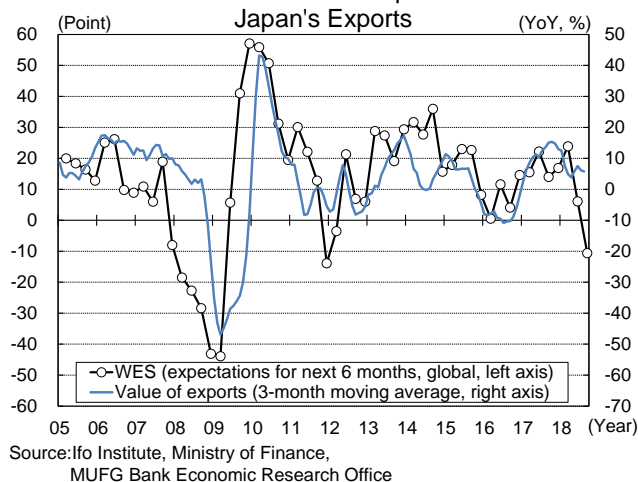


Chart 2: WES Economic Expectations and Japan's Exports



2. Prices and Financial Markets

The Bank of Japan (BoJ) decided to maintain its current monetary policy at its Monetary Policy Meeting on 18th-19th September. The focus of attention this time was on how the BoJ would evaluate the market reaction after it announced the “Strengthening the Framework for Continuous Powerful Monetary Easing” in July. Regarding this point, Governor Kuroda said “trading often tapers in the summer which means it is difficult to evaluate, so an assessment of the current situation would be too hasty” at the press conference after the meeting. Nevertheless, he touched on the BoJ’s Bond Market Survey in August, where responses that bond market functioning “has improved” exceeded “has decreased” for the first time in three years, saying “trading on the bond market has become more active than before and is fluctuating more than before”.

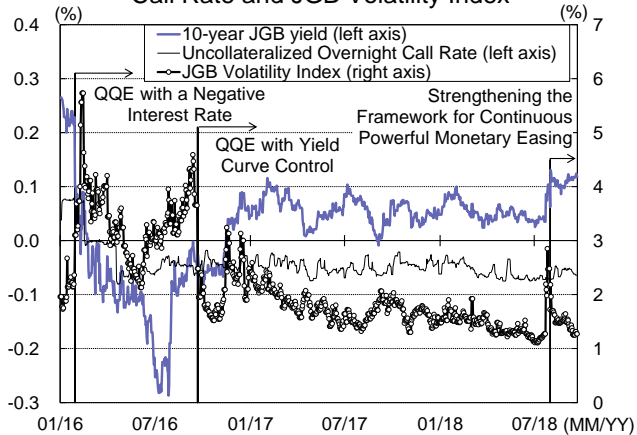
Looking back at financial markets during this time, 10-year Japanese government bond (JGB) yields were at around 0.05% before the Monetary Policy Meeting in July, yet they are now rising and are slightly above 0.1% (Chart 3). In addition, the uncollateralized overnight call rate averaged -0.057% during August’s reserve maintenance period (16th August – 15th September), during which time the Benchmark Ratio for the Macro Add-On Balance was raised. This was slightly higher than July’s average of -0.065%¹. The JGB Volatility Index for 10-year JGBs also rose sharply from the end of July, when the speculation about policy changes began, until early August (however, in mid-September it had almost returned to the previous level before the sharp rise). It appears that market functionality is recovering to a limited extent.

That being said, some market participants still expect a monetary policy adjustment to occur by the end of 2019 (Chart 4). The reason for this is the majority of market participants seem to believe the BoJ’s actions to address side effects, such as impacts on the bond market and financial intermediary functions, are insufficient with regards to the BoJ’s monetary policy decision in July. With a rise in the possibility of small, additional changes to monetary policy aimed at further improving market functionality, it is important to keep an eye on analysis in Financial System Reports and market trends.

While interest rates are rising in the US owing to its robust economy, the JPY is currently around JPY 112 to the USD. Even with temporary changes in the situation overseas, the overall trend of the JPY is expected to remain at its current level of depreciation due to the difference in US and Japanese monetary policy.

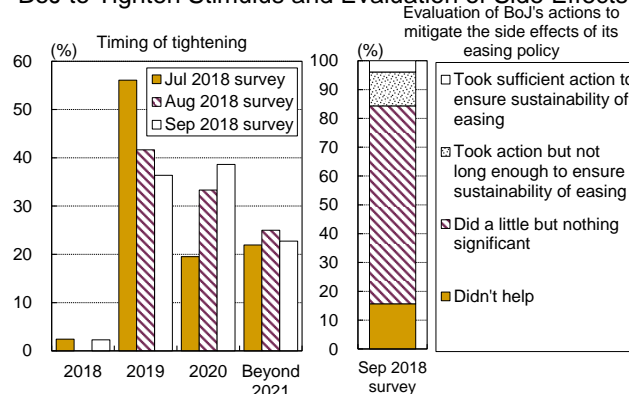
¹ Bank of Japan Current Account Balances are divided into three tiers: Basic Balances, to which an interest rate of 0.1% is applied; Macro Add-On Balances, to which a zero interest rate is applied; and Policy-Rate Balances, to which a negative interest rate is applied. Financial institutions with a Policy Rate Balance have an incentive to lend to other financial institutions in financial markets when interest rates exceed -0.1%. On the other hand, financial institutions with an unused allowance in their Macro Add-On Balance are encouraged to borrow with a negative interest rate within the limits of this allowance. If Policy Rate Balances decrease and Macro Add-On Balances increase due to an increase in the Benchmark Ratio of Macro Add-On Balances, theoretically this would put upward pressure on market rates owing to an increase in borrowing and a decrease in lending.

Chart 3: 10-Year JGB Yield, Uncollateralized Overnight Call Rate and JGB Volatility Index



Source: Bloomberg, MUFG Bank Economic Research Office

Chart 4: Market Expectations regarding the Timing for BoJ to Tighten Stimulus and Evaluation of Side Effects



Note: "Timing of tightening" is the question asked regarding the timing of stimulus to economists who expect the BoJ to tighten stimulus at its next policy change
Source: Bloomberg, MUFG Bank Economic Research Office

(Translated by Elizabeth Foster)

MAIN ECONOMIC AND FINANCIAL INDICATORS (JAPAN)

1. Main Economic Indicators

As of Sep. 21, 2018

	Fiscal	Fiscal	2017	2018		2018				
	2016	2017	4Q	1Q	2Q	APR	MAY	JUN	JUL	AUG
Real GDP Growth Rate <% changes from previous period at SA annual rate>	1.2	1.6	0.9 (2.0)	-0.9 (1.0)	3.0 (1.3)	***	***	***	***	***
Index of All Industries Activity	0.6	1.8	0.7 (1.8)	-0.5 (1.3)	0.9 (1.0)	1.0 (1.4)	0.1 (1.6)	-0.8 (0.2)		
Industrial Production Index	1.0	4.1	1.6 (4.6)	-1.3 (2.4)	1.3 (1.9)	0.5 (2.6)	-0.2 (4.2)	-1.8 (-0.9)	-0.2 (2.2)	
Production										
Shipments	0.8	3.3	0.8 (3.1)	-1.1 (1.5)	1.9 (2.2)	1.6 (3.6)	-1.6 (3.3)	0.3 (-0.2)	-2.0 (1.2)	
Inventory	-4.0	3.9	2.2 (1.9)	3.4 (3.9)	-1.9 (2.4)	-0.6 (1.7)	0.6 (2.5)	-1.9 (2.4)	-0.2 (2.8)	
Inventory/Shipments Ratio (2010=100)	112.9	112.4	112.1 [109.7]	114.9 [111.1]	114.7 [111.8]	113.8 [113.1]	113.9 [111.7]	116.5 [110.7]	117.0 [112.4]	110.1 [110.1]
Domestic Corporate Goods Price Index	-2.4	2.7	0.9 (3.3)	0.6 (2.5)	0.6 (2.4)	0.3 (2.0)	0.5 (2.6)	0.3 (2.8)	0.4 (3.0)	0.0 (3.0)
Consumer Price Index(SA, total, excl.fresh foods)	-0.2	0.7	0.4 (0.9)	-0.1 (0.9)	0.4 (0.7)	-0.1 (0.7)	0.0 (0.7)	0.1 (0.8)	0.1 (0.8)	0.3 (0.9)
Index of Capacity Utilization (2010=100)	98.6	101.7	102.7 [100.1]	101.0 [100.1]	102.0 [101.8]	104.2 [103.5]	102.0 [100.3]	99.8 [101.7]	99.2 [100.6]	102.5 [102.5]
Machinery Orders(Private Demand, Excl.Electric Power and Ship building)	0.5	-0.8	0.3 (0.0)	3.3 (0.2)	2.2 (8.0)	10.1 (9.6)	-3.7 (16.5)	-8.8 (0.3)	11.0 (13.9)	
Manufacturing	-4.6	9.2	3.5 (13.3)	2.5 (10.6)	5.5 (17.8)	22.7 (23.5)	1.3 (26.2)	-15.9 (6.6)	11.8 (21.2)	
Non-manufacturing Excl.Electric Power & Ship building	4.3	-7.8	-2.1 (-9.7)	3.4 (-6.9)	-0.4 (0.3)	0.4 (-1.1)	0.2 (8.4)	-7.0 (-4.6)	10.9 (7.7)	
Shipments of Capital Goods (Excl.Transport Equipment)	1.4	6.2	3.1 (7.2)	-0.5 (7.0)	0.5 (4.2)	2.5 (9.5)	-4.6 (3.8)	-1.1 (0.0)	-0.7 (5.4)	
Construction Orders	4.0	0.7								
Private	5.1	0.6								
Public	8.4	-5.4								
Public Works Contracts	4.1	-4.3								
Housing Starts 10,000 units at Annual Rate, SA Total floor	97.4 (5.8) (4.1)	94.6 (-2.8) (-3.7)	94.8 (-2.4) (-3.2)	89.2 (-8.0) (-9.2)	96.8 (-1.8) (-3.6)	99.2 (0.3) (-2.1)	99.6 (1.3) (0.1)	91.5 (-7.1) (-8.9)	95.8 (-0.7) (-1.6)	
Sales at Retailers	-0.2	1.9								
Real Consumption Expenditures of Households over 2 persons (SA)	-1.6	0.4	-0.6 (0.5)	1.1 (0.6)	-1.4 (-1.3)	-1.6 (-1.3)	-0.2 (-1.4)	2.9 (-1.2)	-1.1 (0.4)	
Propensity to Consume (SA, %)	72.1	71.7	71.3 [71.8]	71.4 [73.0]	69.4 [74.6]	70.2 [73.1]	72.3 [77.0]	66.1 [73.8]	69.9 [70.3]	70.3 [70.3]
Overtime Hours Worked (All Industries, 5 employees or more)	-0.7	0.4	0.3 (1.2)	-1.1 (-1.2)	1.6 (0.6)	0.4 (0.0)	1.3 (0.9)	-0.3 (0.9)	-3.1 (-1.8)	
Total Cash Earnings (Regular Employees Only; All Industries, 5 employees or more)	0.4	0.7								
Employment Index(Regular Employees Only;All Industries, 5 employees or more) (Change over the M/Q/Y)	103	105	133	25	6	13	7	0	-11	
Ratio of Job Offers to Applicants (SA, Times)	1.39	1.54	1.57 [1.41]	1.59 [1.44]	1.60 [1.49]	1.59 [1.47]	1.60 [1.49]	1.62 [1.50]	1.63 [1.51]	1.52 [1.52]
Unemployment Rate (SA, %)	3.0	2.7	2.7	2.5	2.4	2.5	2.2	2.4	2.5	
Economy Watcher Survey (Judgment of the present condition D.I.%)	46.4	50.5	53.3 [49.8]	49.1 [48.7]	48.1 [49.2]	49.0 [48.5]	47.1 [49.1]	48.1 [50.0]	46.6 [49.9]	48.7 [50.0]
Bankruptcies (Number of cases)	8,381 (-3.5)	8,367 (-0.2)	2,106 (1.0)	2,041 (-1.8)	2,107 (-3.7)	650 (-4.4)	767 (-4.4)	690 (-2.3)	702 (-1.7)	694 (8.6)

(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 Sep. 21, 2018

	Fiscal	Fiscal	2017			2018			2018		
	2016	2017	4Q	1Q	2Q	APR	MAY	JUN	JUL	AUG	
Customs Clearance (Exports in Yen Terms)	-3.5	10.8	(13.0)	(4.9)	(7.5)	(7.8)	(8.1)	(6.7)	(3.9)	(6.6)	
Value	-6.0	5.5	(7.9)	(0.8)	(1.8)	(0.5)	(1.5)	(3.4)	(3.0)	(5.4)	
Volumes	2.7	5.0	(4.8)	(4.1)	(5.6)	(7.2)	(6.4)	(3.2)	(0.9)	(1.1)	
Imports (In Yen terms)	-10.2	13.7	(17.0)	(7.5)	(7.5)	(6.0)	(14.1)	(2.6)	(14.6)	(15.4)	
Value	-10.0	8.8	(10.9)	(3.6)	(6.1)	(3.8)	(7.0)	(7.5)	(10.2)	(10.5)	
Volumes	-0.2	4.4	(5.5)	(3.7)	(1.4)	(2.1)	(6.6)	(-4.5)	(4.1)	(4.5)	
Current Account (100 mil. yen)	210,188	218,127	43,257	58,821	49,589	18,451	19,383	11,756	20,097		
Goods (100 mil. yen)	57,851	45,936	11,527	7,246	10,904	5,738	-3,038	8,205	-10		
Services (100 mil. yen)	-13,813	-5,378	-1,975	2,127	-6,343	-5,015	423	-1,751	-1,744		
Financial Account (100 mil. yen)	247,407	196,174	30,753	75,622	43,667	4,254	33,208	6,206	-8,319		
Gold & Foreign Exchange Reserves (\$1mil.)	1,230,330	1,268,287	1,264,283	1,268,287	1,258,748	1,256,018	1,254,477	1,258,748	1,256,276	1,259,305	
Exchange Rate (¥/\$)	108.37	110.80	112.95	108.20	109.05	107.43	109.69	110.03	111.37	111.06	

3. Financial Market Indicators

	Fiscal	Fiscal	2017			2018			2018		
	2016	2017	4Q	1Q	2Q	APR	MAY	JUN	JUL	AUG	
Uncollateralized Overnight Call Rates	-0.045	-0.050	-0.042	-0.048	-0.065	-0.063	-0.061	-0.071	-0.070	-0.059	
			[-0.043]	[-0.042]	[-0.054]	[-0.054]	[-0.053]	[-0.056]	[-0.054]	-0.049	
Euro Yen TIBOR (3 Months)	0.057	0.065	0.063	0.078	0.084	0.097	0.078	0.078	0.091	0.091	
			[0.056]	[0.056]	[0.056]	[0.056]	[0.056]	[0.056]	[0.075]	[0.056]	
Newly Issued Japanese Government Bonds Yields (10 Years)	0.065	0.045	0.045	0.045	0.030	0.050	0.030	0.030	0.060	0.110	
			[0.040]	[0.065]	[0.075]	[0.015]	[0.040]	[0.075]	0.075	[0.010]	
Average Contracted Interest Rates on Loans and Discounts(City Banks) (% changes from previous period)	0.847	0.817	0.828	0.817	0.789	0.793	0.794	0.789	0.788		
			(-0.003)	(-0.011)	(-0.028)	(-0.024)	(0.001)	(-0.005)	(-0.001)		
The Nikkei Stock Average (TSE 225 Issues)	18,909	21,454	22,765	21,454	22,305	22,468	22,202	22,305	22,554	22,865	
			[19,114]	[18,909]	[20,033]	[19,197]	[19,651]	[20,033]	[19,925]	[19,646]	
M2(Average)	(3.6)	(3.7)	(3.9)	(3.2)	(3.1)	(3.2)	(3.2)	(3.1)	(2.9)	(2.9)	
Broadly-defined Liquidity(Average)	(1.9)	(3.1)	(3.3)	(2.6)	(2.5)	(2.5)	(2.5)	(2.5)	(2.3)	(2.2)	
Principal Figures of Financial Institutions											
Loans and Discount (Average)	Banks & Shinkin	(2.4)	(2.8)	(2.6)	(2.1)	(2.0)	(2.0)	(1.9)	(2.1)	(2.0)	(2.2)
	Banks	(2.4)	(2.8)	(2.6)	(2.1)	(2.0)	(2.0)	(1.9)	(2.1)	(2.0)	(2.2)
	City Banks etc.	(1.2)	(2.0)	(1.7)	(0.7)	(0.5)	(0.5)	(0.3)	(0.6)	(0.3)	(0.7)
	Regional Banks	(3.5)	(3.6)	(3.6)	(3.5)	(4.1)	(3.6)	(4.4)	(4.5)	(4.5)	(4.5)
	Regional Banks II	(3.1)	(3.0)	(3.0)	(2.8)	(0.6)	(2.7)	(-0.5)	(-0.4)	(-0.5)	(-0.5)
	Shinkin	(2.3)	(2.7)	(2.6)	(2.5)	(2.3)	(2.3)	(2.3)	(2.2)	(2.2)	
Deposits and CDs (Average)	Total(3 Business Condition)	(3.8)	(4.2)	(4.3)	(3.5)	(3.8)	(3.8)	(3.8)	(3.8)	(3.7)	
	City Banks	(5.5)	(5.9)	(6.1)	(4.9)	(5.2)	(5.3)	(5.1)	(5.3)	(5.4)	
	Regional Banks	(2.3)	(2.5)	(2.5)	(2.2)	(2.8)	(2.3)	(3.2)	(3.0)	(3.0)	
	Regional Banks II	(2.1)	(2.1)	(2.0)	(1.6)	(-0.2)	(1.7)	(-1.1)	(-1.1)	(-1.2)	

(Notes)

Newly Issued Japanese Government Bonds Yields and 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.

For further details, please contact the Economic Research Office, MUFG Bank

Managing Director, Yasuhiro Ishimaru Tel: +81-(0)3-3240-3204

Written by Yumiko Hishiki < yumiko_4_hishiki@mufg.jp >

Yuusuke Yokota < yuusuke_yokota@mufg.jp >

This report is intended for information purposes only and shall not be construed as solicitation to take any action such as purchasing/selling/investing financial market products. In taking any action, each reader is requested to act on the basis of his or her own judgment. This report is based on information believed to be reliable, but we do not guarantee its accuracy. The contents of the report may be revised without advance notice. Also, this report is a literary work protected by the copyright act. No part of this report may be reproduced in any form without express statement of its source. This report is also available for viewing online.

