

Sustained Strong Corporate Profits Point to Increasing Employment and Capital Expenditures

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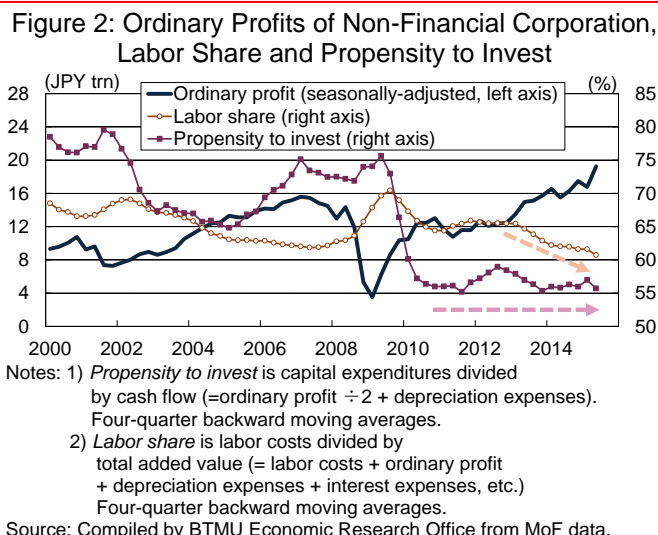
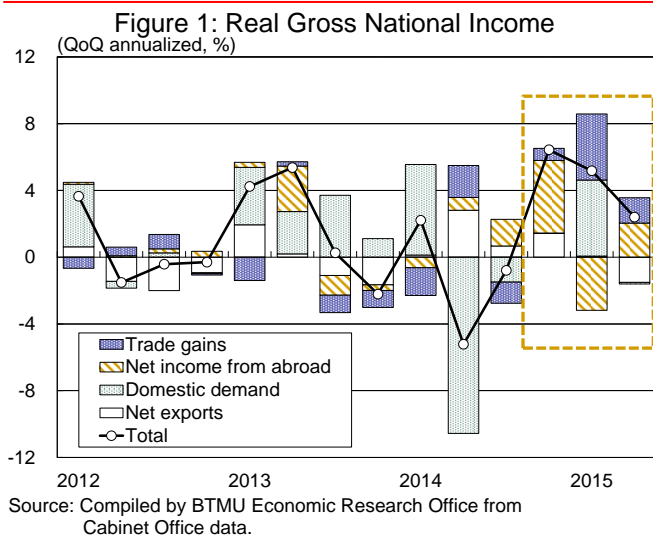
The Bank of Tokyo-Mitsubishi UFJ, Ltd.
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1. The Real Economy

Japan's real GDP slipped by an annualized -1.2% QoQ in Apr-Jun, the first contraction in three quarters. Looking from demand side, the result showed that the economic recovery had stagnated temporarily. On the other hand, however, incomes have continued to rise. Real gross national income, which shows the trend of incomes for the country as a whole, gained an annualized +2.4% QoQ in Apr-Jun, the third straight quarter of expansion (Figure 1). While net exports weighed on income as exports weakened, trade gains were a boosting factor as international commodity markets slumped. Also, net income from abroad contributed to increase in income, reflecting improving gains from overseas investments due to the weaker JPY trend.

Rising national income is largely being manifested as higher corporate profits. Ordinary profits of non-financial corporation stood at approximately JPY20 trillion in Apr-Jun (adjusted for seasonality), up JPY 2 trillion on-quarter and a record high (Figure 2). On the other hand, the labor share—which reflects the portion of added value generated by companies paid to employees as labor cost—continues to fall slowly. Moreover, although propensity to invest—which shows the ratio of cash flow used for capital expenditures—has bottomed, it remains well below the strong level prior to the collapse of Lehman Brothers. Companies appear to have great capacity for boosting demand by recirculating their profits domestically through job creation and wage hike as well as expansion of capital expenditures.

Tight labor supply-demand and a diminishing sense of surplus capital stock are encouraging companies to recirculate their sizeable profits domestically. As the funds of companies circulate within Japan, the country's economy should become stronger and more stable. This scenario appears highly probable, with the highest current fiscal year capital expenditure plans among large companies in nine years as well as the biggest wage hikes in this year's spring wage negotiations in 17 years.



2. Monetary Policy and Financial Markets

(1) MONETARY POLICY & LONG-TERM YIELDS

At its September 14-15 Monetary Policy meeting, the Bank of Japan agreed to hold current monetary policy intact. BoJ Governor Haruhiko Kuroda, at the post-meeting press conference, commented that price trend is picking up steadily in terms of the supply-demand gap, wage trend, and corporate pricing behaviors. The BoJ started releasing CPI(excluding fresh foods and energy) in its *Monthly Report of Recent Economic and Financial Developments* in July, and its growth rate extended by +0.8% YoY in the most recent July (Figure 3). Looking at the breakdown of the data, prices are rising gradually not only for goods more sensitive to the JPY's weakening, but also for services. Prolonged weak oil prices and the contraction in Japan's real GDP in Apr-Jun have stoked expectations of further monetary easing among some investors, but the BoJ feels that its 2% price stability target may be achieved in 1H 2016 and has rejected further monetary easing for now.

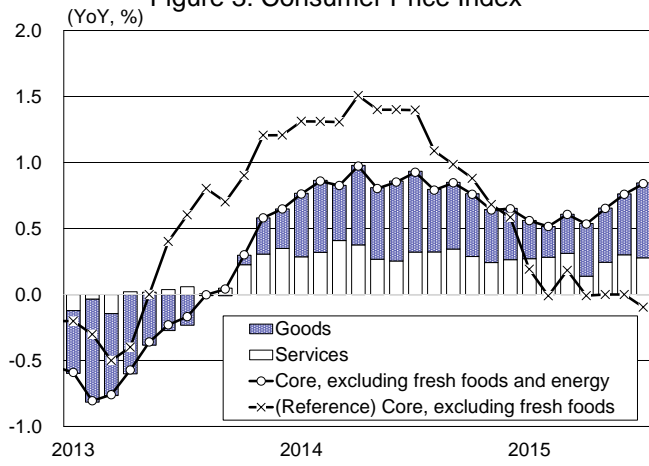
The 10Yr JGB yield has been at around the higher 0.3% recently because bonds were apt to be bought amidst stock market volatility due to concerns about the outlook for China's economy.

(2) EXCHANGE RATES

The JPY has remained in the lower USD/JPY 120 range of late amidst JPY buying due to heightening risk-aversion moves by investors and the BoJ's deferral of further monetary easing. USD/JPY has been in step with stock prices since around the start of the fiscal year but has been comparatively stable since August, even as stock prices have plunged and remain volatile.

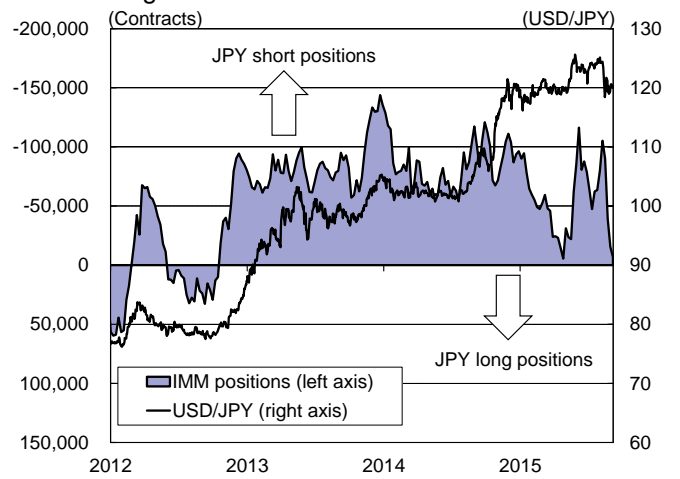
Looking at non-commercial investors' JPY/USD futures net positions in currency options market, net JPY selling position has prevailed since 2013 but recently selling and buying have been roughly neck-and-neck (Figure 4). While there is less risk that reversals of JPY selling positions will cause the JPY to strengthen versus the USD, this could be a sign that the market does not expect the JPY to weaken much more even as a US rate hike nears.

Figure 3: Consumer Price Index



Note: Excluding direct impact of consumption tax hike.
Source: Compiled by BTMU Economic Research Office from MIC data.

Figure 4: IMM Position and USD/JPY



Source: Compiled by BTMU Economic Research Office from Bloomberg.

MAIN ECONOMIC AND FINANCIAL INDICATORS (JAPAN)

1. Main Economic Indicators

As of Oct. 14, 2015

	Fiscal 2013	Fiscal 2014	2014	2015		2015				
			4Q	1Q	2Q	MAY	JUN	JUL	AUG	SEP
Real GDP Growth Rate <% changes from previous period at SA annual rate>	2.1	-0.9	1.3 (-1.0)	4.5 (-0.8)	-1.2 (0.8)	***	***	***	***	***
Index of All Industries Activity	2.2	-1.1	0.6 (-1.1)	1.1 (-1.2)	-0.3 (1.3)	-0.9 (-0.2)	0.5 (2.2)	0.2 (1.7)		
Industrial Production Index	3.2	-0.4	0.8 (-1.5)	1.5 (-2.1)	-1.4 (-0.5)	-2.1 (-3.9)	1.1 (2.3)	-0.8 (0.0)	-0.5 (0.2)	
Production										
Shipments	2.9	-1.1	0.9 (-1.9)	1.7 (-2.4)	-2.4 (-0.3)	-1.9 (-3.2)	0.6 (1.8)	-0.4 (-0.8)	-0.5 (0.8)	
Inventory	-1.2	6.2	0.9 (6.2)	1.0 (6.2)	1.1 (4.0)	-0.8 (3.9)	1.5 (4.0)	-0.8 (2.7)	0.4 (2.2)	
Inventory/Shipments Ratio (2010=100)	106.3	112.0	113.8 [104.6]	112.3 [103.1]	114.0 [108.7]	115.4 [108.5]	113.5 [112.0]	112.2 [110.2]	119.1 [117.9]	[111.5]
Domestic Corporate Goods Price Index	1.9	2.8	-1.3 (2.4)	-1.6 (0.5)	0.3 (-2.2)	0.2 (-2.2)	-0.2 (-2.4)	-0.3 (-3.1)	-0.6 (-3.6)	-0.5 (-3.9)
Consumer Price Index(SA, total, excl.fresh foods)	0.8	2.8	-0.1 (2.7)	-0.7 (2.1)	0.6 (0.1)	0.0 (0.1)	0.1 (0.1)	0.0 (0.0)	0.0 (-0.1)	
Index of Capacity Utilization (2010=100)	100.0	100.6	100.7 [100.2]	101.7 [104.7]	97.6 [101.2]	96.4 [101.9]	97.1 [99.4]	96.9 [98.8]		[100.3]
Machinery Orders(Private Demand, Excl.Electric Power and Ship building)	11.5	0.8	0.7 (-2.6)	6.3 (3.3)	2.9 (12.4)	0.6 (19.3)	-7.9 (16.6)	-3.6 (2.8)	-5.7 (-3.5)	
Manufacturing	10.2	7.0	2.4 (8.6)	2.3 (5.2)	12.1 (27.5)	9.9 (44.6)	-14.0 (25.0)	-5.3 (3.8)	-3.2 (4.5)	
Non-manufacturing Excl.Electric Power & Ship building	12.1	-3.3	-1.1 (-9.6)	8.5 (1.4)	-1.7 (2.3)	-4.0 (2.5)	0.6 (10.4)	-6.0 (1.8)	-6.1 (-9.5)	
Shipments of Capital Goods (Excl.Transport Equipment)	5.5	4.3	2.7 (5.0)	1.2 (-1.1)	-2.1 (2.5)	-1.4 (-0.4)	2.0 (4.7)	0.7 (0.4)	-5.8 (0.4)	
Construction Orders	20.1	8.2								
Private	14.2	4.8								
Public	31.2	22.9								
Public Works Contracts	17.7	-0.3								
Housing Starts 10,000 units at Annual Rate, SA	98.7 (10.6)	88.0 (-10.8)	86.8 (-13.8)	89.8 (-5.4)	95.8 (7.6)	91.1 (5.8)	103.3 (16.3)	91.4 (7.4)	93.1 (8.8)	
Total floor	(9.9)	(-15.2)	(-19.3)	(-9.0)	(4.2)	(3.5)	(11.5)	(4.6)	(3.4)	
Sales at Retailers	2.9	-1.2								
Real Consumption Expenditures of Households over 2 persons (SA)	0.9	-5.1	1.7 (-3.4)	1.4 (-6.5)	-3.2 (0.5)	2.4 (4.8)	-3.0 (-2.0)	0.6 (-0.2)	2.5 (2.9)	
Propensity to Consume (SA,%)	75.5	74.2	74.5 [75.1]	74.6 [78.3]	73.7 [73.6]	74.3 [71.3]	73.7 [74.8]	71.4 [75.0]	74.3 [73.6]	[75.1]
Overtime Hours Worked (All Industries, 5 employees or more)	4.8	2.0	0.1 (0.9)	0.3 (-0.6)	-0.9 (-1.6)	-0.3 (-1.7)	0.6 (-0.8)	-0.2 (-0.7)	-1.0 (-0.8)	
Total Cash Earnings (Regular Employees Only; All Industries, 5 employees or more)	-0.2	0.5								
Employment Index(Regular Employees Only;All Industries, 5 employees or more) (Change over the M/Q/Y)	45	77	76	90	96	95	97	96	87	
Ratio of Job Offers to Applicants (SA,Times)	0.97	1.11	1.12 [1.01]	1.15 [1.05]	1.18 [1.09]	1.19 [1.09]	1.19 [1.10]	1.21 [1.10]	1.23 [1.10]	[1.10]
Unemployment Rate (SA,%)	3.9	3.5	3.5	3.5	3.3	3.3	3.4	3.3	3.4	
Economy Watcher Survey (Judgment of the present condition D.I.%)	54.0	46.6	43.6 [53.6]	49.3 [55.2]	52.6 [44.8]	53.3 [45.1]	51.0 [47.7]	51.6 [51.3]	49.3 [47.4]	47.5 [47.4]
Bankruptcies (Number of cases)	10,536 (-10.0)	9,543 (-9.4)	2,222 (-13.5)	2,272 (-7.6)	2,296 (-12.1)	724 (-13.1)	824 (-4.7)	787 (-10.7)	632 (-13.0)	673 (-18.6)

(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 Oct. 14, 2015

	Fiscal	Fiscal	2014	2015		2015				
	2013	2014	4Q	1Q	2Q	MAY	JUN	JUL	AUG	SEP
Customs Clearance (Exports in Yen Terms)	10.8	5.4	(9.1)	(9.0)	(6.7)	(2.4)	(9.5)	(7.6)	(3.1)	
Value	10.2	3.9	(6.6)	(5.0)	(7.3)	(6.4)	(9.5)	(8.4)	(7.5)	
Volumes	0.6	1.3	(2.4)	(3.8)	(-0.6)	(-3.8)	(0.0)	(-0.7)	(-4.1)	
Imports (In Yen terms)	17.4	-0.9	(1.2)	(-9.3)	(-5.1)	(-8.6)	(-2.9)	(-3.1)	(-3.1)	
Value	14.6	1.2	(4.9)	(-5.1)	(-3.1)	(-3.5)	(-1.5)	(-0.2)	(-2.4)	
Volumes	2.3	-2.1	(-3.5)	(-4.6)	(-2.2)	(-5.3)	(-1.4)	(-2.9)	(-0.7)	
Current Account (100 mil. yen)	14,715	79,309	15,124	44,177	37,637	18,660	5,615	18,086	16,531	
Goods (100 mil. yen)	-110,187	-65,659	-17,782	-3,311	-678	-480	1,156	-1,080	-3,261	
Services (100 mil. yen)	-34,448	-27,482	-6,656	-2,801	-6,266	881	-1,878	-1,836	578	
Financial Account (100 mil. yen)	-17,549	133,088	22,468	63,894	46,954	33,759	4,156	9,170	19,384	
Gold & Foreign Exchange Reserves (\$1mil.)	1,279,346	1,245,316	1,260,548	1,245,316	1,242,935	1,245,755	1,242,935	1,242,316	1,244,150	1,248,936
Exchange Rate (¥/\$)	100.23	109.92	114.56	119.07	121.35	120.74	123.75	123.23	123.23	120.22

3. Financial Market Indicators

	Fiscal	Fiscal	2014	2015		2015				
	2013	2014	4Q	1Q	2Q	MAY	JUN	JUL	AUG	SEP
Uncollateralized Overnight Call Rates	0.073	0.068	0.064	0.073	0.067	0.069	0.072	0.074	0.076	0.073
			[0.072]	[0.074]	[0.067]	[0.068]	[0.067]	[0.066]	[0.069]	[0.066]
Euro Yen TIBOR (3 Months)	0.223	0.194	0.184	0.171	0.169	0.169	0.169	0.169	0.169	0.169
			[0.220]	[0.215]	[0.211]	[0.210]	[0.210]	[0.210]	[0.210]	[0.210]
Newly Issued Japanese Government Bonds Yields (10 Years)	0.640	0.400	0.330	0.400	0.455	0.390	0.455	0.410	0.380	0.350
			[0.735]	[0.640]	[0.565]	[0.570]	[0.565]	[0.530]	[0.490]	[0.525]
Average Contracted Interest Rates on Loans and Discounts(City Banks) (% changes from previous period)	1.077	1.006	1.025	1.006	0.987	1.003	0.987	0.982	0.980	
			(-0.023)	(-0.019)	(-0.019)	(-0.004)	(-0.016)	(-0.005)	(-0.002)	
The Nikkei Stock Average (TSE 225 Issues)	14,828	19,207	17,451	19,207	20,236	20,563	20,236	20,585	18,890	17,388
			[16,291]	[14,828]	[15,162]	[14,632]	[15,162]	[15,621]	[15,425]	[16,174]
M2(Average)	(3.9)	(3.3)	(3.5)	(3.5)	(3.9)	(4.1)	(3.9)	(4.0)	(4.2)	(3.8)
Broadly-defined Liquidity(Average)	(3.7)	(3.3)	(3.5)	(3.5)	(4.3)	(4.5)	(4.5)	(4.6)	(4.7)	(4.2)
Principal Figures of Financial Institutions										
Loans and Discount (Average)	Banks & Shinkin	(2.0)	(2.4)	(2.5)	(2.5)	(2.5)	(2.5)	(2.6)	(2.7)	(2.6)
	Banks	(2.3)	(2.5)	(2.7)	(2.6)	(2.6)	(2.6)	(2.5)	(2.7)	(2.8)
	City Banks etc.	(1.7)	(1.4)	(1.7)	(1.4)	(1.4)	(1.3)	(1.2)	(1.4)	(1.7)
	Regional Banks	(3.3)	(3.8)	(3.8)	(4.0)	(4.0)	(4.1)	(3.9)	(4.0)	(3.8)
	Regional Banks II	(1.4)	(2.9)	(3.1)	(3.1)	(3.1)	(3.0)	(3.2)	(3.4)	(3.4)
	Shinkin	(0.3)	(1.4)	(1.5)	(1.6)	(1.9)	(1.9)	(1.9)	(2.0)	(2.1)
Deposits and CDs (Average)	Total(3 Business Condition)	(3.8)	(3.3)	(3.8)	(3.9)	(4.3)	(4.6)	(4.3)	(4.3)	(4.5)
	City Banks	(3.7)	(3.4)	(4.4)	(4.7)	(5.4)	(6.0)	(5.3)	(5.5)	(5.8)
	Regional Banks	(4.3)	(3.3)	(3.2)	(3.1)	(3.3)	(3.5)	(3.4)	(3.4)	(3.3)
	Regional Banks II	(2.5)	(3.1)	(3.3)	(3.1)	(2.9)	(2.9)	(2.9)	(2.8)	(2.6)

(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.

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