

The pace of investment growth by companies is accelerating, especially M&As and foreign investment

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1. The Real Economy

Growth of ordinary profits across all industries (excluding the financial and insurance industries) rose to 26.6% year-on-year (YoY) in Q1, accelerating for the third consecutive quarter and surpassing the historic high recorded in Q4 2016 (Chart 1). Analysis of the data reveals that an increase in “sales” due to a recovery in both Japanese and foreign economies contributed to the increase in ordinary profits. An improvement in non-operating revenue and expenses – including exchange gains and losses as well as dividends received from overseas subsidiaries – also boosted the growth of ordinary profits. There was some downward pressure on profits from a rise in variable costs due to an increase in oil prices as well as labour costs, but this was absorbed. Looking at FY2016, there was a marked slowdown in the first half of the year owing to yen appreciation, but profits regained momentum in the latter half of the year and grew 10.0% YoY.

What effect did the business environment mentioned above have on business activities in FY2016? Looking at the condition of businesses’ financing and investment from changes in the balance sheet, on the liabilities and equity side, there was a continued increase in net assets and debts against a backdrop of robust corporate earnings (Table 1). As for debts, while short-term borrowings declined, corporate bond issuance increased sharply owing to low interest rates after the introduction of negative interest rates by the Bank of Japan (BoJ). This suggests that the trend in corporate financing has shifted from short-term to long-term. Turning to assets, there was a significant acceleration in “investment and other assets”, including foreign and domestic M&As as well as overseas investment. Meanwhile “tangible fixed assets” (domestic capital investment) also increased moderately. Looking at corporations as a whole, they are expanding their domestic and foreign M&As and overseas investment whilst maintaining real investment in domestic businesses at a certain level by adding external funds to the high level of cash flow. Looking forward, it appears that businesses’ profits will become more robust due to an increase in domestic and foreign demand and their positive investment behaviour will continue.

Chart 1: Ordinary Profits of Corporations
(excluding Financial and Insurance)

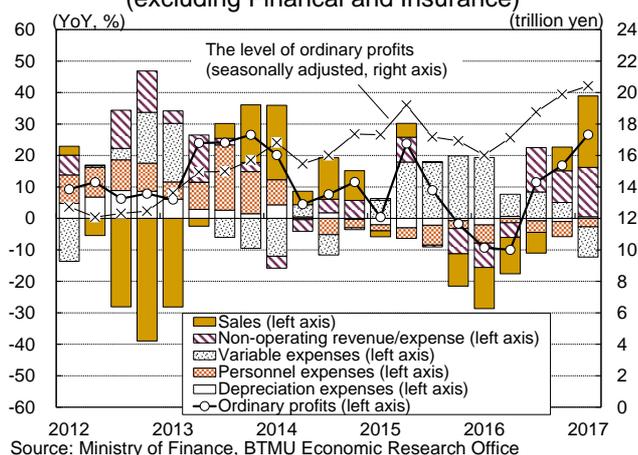


Table 1: Balance Sheet of Corporations
(excluding Financial and Insurance)

	(Change in JPY, trillions)					
	11 Mar→ 12 Mar	12 Mar→ 13 Mar	13 Mar→ 14 Mar	14 Mar→ 15 Mar	15 Mar→ 16 Mar	16 Mar→ 17 Mar
Investment						
Liquid assets	+6	-26	+17	+56	+21	-7
Cash and deposits	-3	-4	+4	+18	+10	+8
Bills and accounts receivable	+9	-18	+7	+12	+0	-4
Inventories	-2	-2	+1	+10	+1	-4
Securities	-0	-0	-0	-1	-2	-1
Other liquid assets	+1	-3	+6	+17	+12	-6
Fixed assets	-19	+2	+9	+38	+29	+39
Tangible fixed assets	-28	-4	-10	+18	+5	+3
Intangible fixed assets	+1	+1	-3	+1	+0	+3
Investment and other assets	+8	+5	+21	+20	+23	+33
Total assets	-13	-24	+25	+94	+50	+32
Financing						
Liquid liabilities	+12	-40	+10	+28	+14	-17
Bills and accounts payable	+12	-16	+3	+7	-6	-4
Short-term borrowings	-9	-11	+4	+4	+7	-11
Other liquid liabilities	+9	-13	+4	+17	+14	-2
Fixed liabilities	-12	-4	-9	+9	+3	+21
Bonds	-4	+0	-0	+1	+0	+8
Long-term borrowings	-9	-4	-7	+7	+5	+10
Other fixed liabilities	+2	-1	-1	+2	-2	+3
Net assets	-14	+20	+24	+58	+32	+27
Liabilities and net assets	-13	-24	+25	+94	+50	+32

Note: Subjects of the survey are corporations (excluding finance and insurance) with capital of over JPY 10 million

Source: Ministry of Finance Japan, BTMU Economic Research Office

2. Financial Markets

(1) Monetary Policy

The Bank of Japan decided to maintain its current monetary policy at the Monetary Policy Meeting on 15th – 16th June. At a press conference after the meeting, when asked about an exit strategy from monetary easing, a topic which is gathering increasing attention, Governor Haruhiko Kuroda did not change his existing stance as his response indicates: "it's inappropriate to say now specifically how we will exit our monetary policy." On the other hand, regarding the impact of an exit strategy on the BoJ treasury, he went on to say that "central banks can continuously generate seigniorage (profit from issuing currency), thereby maintaining revenue in the long term".

In the Financial Results for FY2016 published by the BoJ this month, operating profits increased from JPY 762.6 billion the previous financial year to JPY 1.952 trillion (Chart 2). A large factor in this increase was a reduction in the amount of "FX losses". However, regarding JGBs, which make up a large portion of the BoJ's assets, there was a decrease in "profits from JGBs" ("interest on JGBs" plus the "write-down of JGBs", the latter being the loss incurred by JGBs purchased at higher prices than the face values). This decrease is because of a rise in the purchase of JGBs at higher prices than the face values due to the introduction of the negative interest rate policy as part of the BoJ's quantitative easing, as well as a fall in JGB yields. This suggests that if the negative interest rate policy continues, even if the balance of JGBs held by the BoJ increases, seigniorage may not necessarily increase.

On 10th May, in a statement made at the Committee on Financial Affairs at the House of Representatives, Mr Kuroda said "we will consider it as a future possibility," when asked about releasing calculations regarding the effect on the BoJ's balance sheet if monetary stimuli were to be withdrawn. When the BoJ actually takes steps towards an exit strategy, it will be required to release information which will shed light on the future of monetary policy in order to avoid rattling the markets. Moreover, it is preferable if this information includes preliminary calculations of BoJ revenue in the future.

(2) Long-Term Yields and Exchange Rate

The USD/JPY rate has been moving in tandem with the difference in Japanese and US real interest rates (Chart 3). Since the 10-year JGB yield has moved within a narrow range of around 0.05% and inflation expectations have remained almost unchanged in Japan, the USD/JPY rate mainly reflects fluctuations in US interest rates and inflation expectations. Looking forwards, based on the forecast that the BoJ will maintain its current monetary policy; it appears the JPY will continue to be affected by the situation in the US.

Chart 2: Breakdown of Bank of Japan's Operating Profit

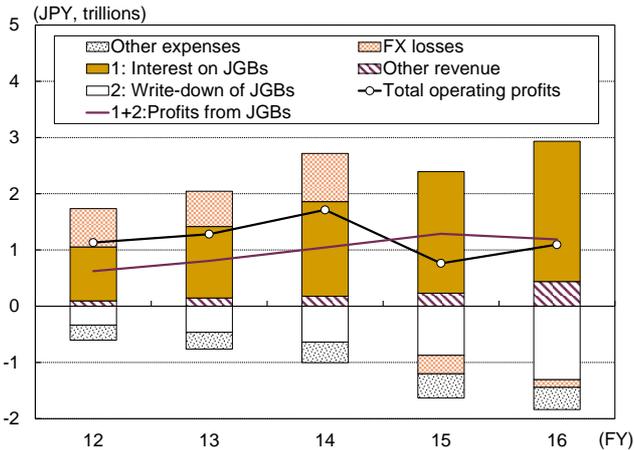
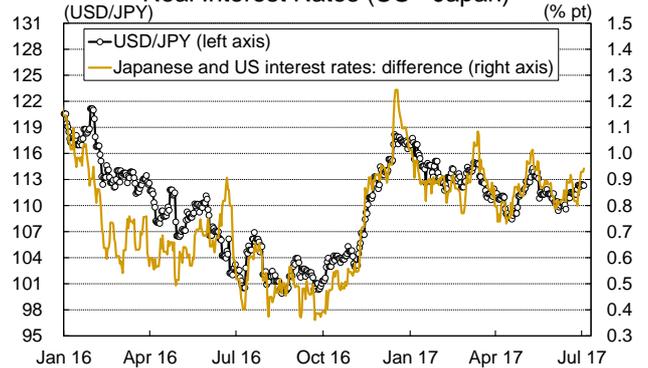


Chart 3: USD/JPY and the Difference in Real Interest Rates (US - Japan)



Note: "Real interest rate" refers to the yield of 10-year government bond - break-even inflation rate.
Source: Bloomberg data, BTMU Economic Research Office

(Translated by Elizabeth Foster)

MAIN ECONOMIC AND FINANCIAL INDICATORS (JAPAN)

1. Main Economic Indicators

As of June. 23, 2017

	Fiscal	Fiscal	2016		2017	2017				
	2015	2016	3Q	4Q	1Q	JAN	FEB	MAR	APR	MAY
Real GDP Growth Rate <% changes from previous period at SA annual rate>	1.2	1.2	1.0 (1.1)	1.4 (1.6)	1.0 (1.3)	***	***	***	***	***
Index of All Industries Activity	0.9	0.6	0.6 (0.7)	0.4 (1.1)	-0.1 (0.8)	-0.4 (1.3)	0.6 (0.0)	-0.7 (1.0)	2.1 (1.9)	
Industrial Production Index	-0.9	1.1	1.6 (0.4)	1.8 (2.1)	0.2 (3.8)	-2.1 (3.2)	3.2 (4.7)	-1.9 (3.5)	4.0 (5.7)	
Production										
Shipments	-1.1	0.8	1.0 (-0.5)	2.4 (1.8)	-0.1 (3.7)	-1.1 (4.2)	1.4 (3.7)	-0.8 (3.5)	2.7 (4.9)	
Inventory	1.1	-4.0	-2.2 (-2.7)	-2.4 (-5.3)	2.2 (-4.0)	0.1 (-5.0)	0.7 (-3.9)	1.5 (-4.0)	1.5 (-1.1)	
Inventory/Shipments Ratio (2010=100)	114.9	112.9	114.3 [114.7]	109.7 [114.9]	111.5 [116.8]	111.6 [117.5]	111.3 [115.3]	111.5 [117.5]	114.7 [115.9]	116.7 [116.7]
Domestic Corporate Goods Price Index	-3.3	-2.3	-0.3 (-3.8)	0.4 (-2.1)	1.6 (1.0)	0.6 (0.5)	0.3 (1.1)	0.2 (1.4)	0.2 (2.1)	0.0 (2.1)
Consumer Price Index(SA, total, excl.fresh foods)	0.0	-0.2	-0.2 (-0.5)	0.2 (-0.3)	-0.1 (0.2)	0.3 (0.1)	0.0 (0.2)	0.0 (0.2)	0.0 (0.3)	
Index of Capacity Utilization (2010=100)	98.0	98.6	98.0 [97.6]	100.1 [97.9]	99.8 [96.1]	98.3 [96.4]	101.4 [95.4]	99.8 [96.4]	104.1 [96.4]	95.9 [95.9]
Machinery Orders(Private Demand, Excl.Electric Power and Ship building)	4.1	0.5	5.5 (6.5)	0.3 (3.6)	-1.4 (-1.0)	-3.2 (-8.2)	1.5 (5.6)	1.4 (-0.7)	-3.1 (2.7)	
Manufacturing	6.2	-4.6	1.9 (-0.5)	2.7 (3.5)	-4.2 (-6.8)	-10.8 (-22.0)	6.0 (9.5)	0.6 (-4.9)	2.5 (9.8)	
Non-manufacturing Excl.Electric Power & Ship building	2.5	4.3	6.2 (11.8)	-1.0 (3.3)	0.0 (3.1)	0.7 (5.7)	1.8 (2.7)	-3.9 (2.2)	-5.0 (-2.1)	
Shipments of Capital Goods (Excl.Transport Equipment)	-2.2	1.5	1.3 (0.7)	2.4 (4.7)	-2.4 (3.1)	-2.3 (4.4)	1.7 (4.0)	-4.4 (1.6)	6.5 (4.2)	
Construction Orders	-0.9	4.0								
Private	7.9	5.1								
Public	-15.6	8.4								
Public Works Contracts	-3.8	4.1								
Housing Starts 10,000 units at Annual Rate, SA	92.1 (4.6)	97.4 (5.8)	97.9 (7.1)	95.3 (7.9)	97.5 (3.5)	100.1 (12.8)	94.0 (-2.6)	98.4 (0.2)	100.4 (1.9)	
Total floor	(2.1)	(4.1)	(5.1)	(5.3)	(3.3)	(14.5)	(-2.5)	(-2.0)	(3.0)	
Sales at Retailers	0.8	-0.2								
Real Consumption Expenditures of Households over 2 persons (SA)	-1.2	-1.6	-0.4 (-2.4)	-0.9 (-0.7)	0.8 (-2.0)	0.5 (-1.2)	2.5 (-3.8)	-2.0 (-1.3)	0.5 (-1.4)	
Propensity to Consume (SA, %)	73.6	72.1	70.7 [73.6]	71.8 [73.0]	73.1 [72.6]	71.0 [72.3]	75.4 [74.0]	72.8 [71.6]	73.1 [74.2]	74.7 [74.7]
Overtime Hours Worked (All Industries, 5 employees or more)	-1.3	-0.7	-0.2 (-1.5)	0.1 (-1.2)	1.5 (1.2)	2.0 (0.7)	0.1 (1.5)	0.1 (1.5)	-0.9 (0.6)	
Total Cash Earnings (Regular Employees Only; All Industries, 5 employees or more)	0.2	0.4								
Employment Index(Regular Employees Only;All Industries, 5 employees or more) (Change over the M/Q/Y)	98	103	102	105	112	109	113	114	127	
Ratio of Job Offers to Applicants (SA, Times)	1.23	1.39	1.37 [1.22]	1.41 [1.26]	1.44 [1.29]	1.43 [1.29]	1.43 [1.29]	1.45 [1.31]	1.48 [1.33]	1.35 [1.35]
Unemployment Rate (SA, %)	3.3	3.0	3.0	3.1	2.9	3.0	2.8	2.8	2.8	
Economy Watcher Survey (Judgment of the present condition D.I.%)	48.8	46.4	45.2 [49.5]	48.7 [47.7]	49.2 [45.6]	48.6 [46.6]	48.5 [44.6]	50.6 [45.4]	50.4 [43.5]	50.1 [43.0]
Bankruptcies (Number of cases)	8,684 (-9.0)	8,381 (-3.5)	2,087 (-0.2)	2,086 (-3.1)	2,079 (-3.0)	605 (-10.4)	688 (-4.8)	786 (5.4)	680 (-2.2)	802 (19.5)

(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 June. 23, 2017

	Fiscal	Fiscal	2016		2017	2017				
	2015	2016	3Q	4Q	1Q	JAN	FEB	MAR	APR	MAY
Customs Clearance (Exports in Yen Terms)	-0.7	-3.5	(-10.2)	(-1.9)	(8.5)	(1.3)	(11.3)	(12.0)	(7.4)	(14.9)
Value	2.0	-5.8	(-11.1)	(-6.3)	(3.1)	(1.6)	(2.8)	(5.0)	(3.2)	(6.9)
Volumes	-2.7	2.4	(1.0)	(4.7)	(5.1)	(-0.3)	(8.3)	(6.6)	(4.1)	(7.5)
Imports (In Yen terms)	-10.2	-10.2	(-19.3)	(-9.3)	(8.6)	(8.4)	(1.3)	(15.9)	(15.2)	(17.8)
Value	-8.4	-10.7	(-18.8)	(-10.7)	(6.2)	(2.0)	(5.8)	(11.3)	(9.7)	(11.8)
Volumes	-1.9	0.5	(-0.7)	(1.6)	(2.2)	(6.3)	(-4.3)	(4.2)	(5.0)	(5.4)
Current Account (100 mil. yen)	178,618	201,990	57,743	40,876	57,869	655	28,136	29,077	19,519	
Goods (100 mil. yen)	3,296	57,654	14,860	17,146	10,889	-8,534	10,768	8,655	5,536	
Services (100 mil. yen)	-13,527	-15,058	-3,470	-5,520	-1,192	-2,357	-639	1,804	-2,947	
Financial Account (100 mil. yen)	238,492	249,526	104,960	22,119	52,650	-15,351	17,752	50,249	10,705	
Gold & Foreign Exchange Reserves (\$1mil.)	1,262,099	1,230,330	1,260,145	1,216,903	1,230,330	1,231,573	1,232,340	1,230,330	1,242,295	1,251,868
Exchange Rate (¥/\$)	120.13	108.37	102.40	109.32	113.60	114.73	113.06	113.01	110.06	112.21

3. Financial Market Indicators

	Fiscal	Fiscal	2016		2017	2017					
	2015	2016	3Q	4Q	1Q	JAN	FEB	MAR	APR	MAY	
Uncollateralized Overnight Call Rates	0.063	-0.045	-0.046 [0.074]	-0.043 [0.076]	-0.042 [0.035]	-0.045 [0.074]	-0.038 [0.033]	-0.042 [-0.003]	-0.054 [-0.037]	-0.053 -0.059	
Euro Yen TIBOR (3 Months)	0.157	0.057	0.057 [0.169]	0.056 [0.169]	0.056 [0.122]	0.056 [0.169]	0.056 [0.098]	0.056 [0.098]	0.056 [0.060]	0.056 [0.060]	
Newly Issued Japanese Government Bonds Yields (10 Years)	-0.050	0.065	-0.085 [0.350]	0.040 [0.270]	0.065 [-0.050]	0.085 [0.095]	0.050 [-0.065]	0.065 [-0.050]	0.015 -0.085	0.040 [-0.120]	
Average Contracted Interest Rates on Loans and Discounts(City Banks) (% changes from previous period)	0.924	0.847	0.865 (-0.021)	0.853 (-0.012)	0.847 (-0.006)	0.855 (0.002)	0.852 (-0.003)	0.847 (-0.005)	0.850 (0.003)		
The Nikkei Stock Average (TSE 225 Issues)	16,759	18,909	16,450 [17,388]	19,114 [19,034]	18,909 [16,759]	19,041 [17,518]	19,119 [16,027]	18,909 [16,759]	19,197 [16,666]	19,651 [17,235]	
M2(Average)	(3.5)	(3.6)	(3.3)	(3.8)	(4.1)	(4.0)	(4.1)	(4.2)	(4.0)	(3.9)	
Broadly-defined Liquidity(Average)	(3.7)	(1.8)	(1.4)	(1.6)	(2.2)	(2.0)	(2.3)	(2.4)	(2.6)	(2.8)	
Principal Figures of Financial Institutions											
Loans and Discount (Average)	Banks & Shinkin	(2.4)	(2.4)	(2.1)	(2.5)	(2.8)	(2.5)	(2.8)	(3.0)	(3.0)	(3.2)
	Banks	(2.5)	(2.4)	(2.1)	(2.5)	(2.8)	(2.6)	(2.9)	(3.0)	(3.0)	(3.3)
	City Banks etc.	(1.2)	(1.2)	(0.7)	(1.4)	(2.0)	(1.7)	(2.1)	(2.3)	(2.4)	(2.9)
	Regional Banks	(3.7)	(3.5)	(3.5)	(3.6)	(3.6)	(3.5)	(3.6)	(3.8)	(3.6)	(3.9)
	Regional Banks II	(3.2)	(3.1)	(2.9)	(3.1)	(3.2)	(3.1)	(3.2)	(3.2)	(2.9)	(3.0)
	Shinkin	(2.2)	(2.3)	(2.3)	(2.3)	(2.5)	(2.3)	(2.5)	(2.6)	(2.8)	(2.9)
Deposits and CDs (Average)	Total(3 Business Condition)	(3.7)	(3.8)	(3.4)	(4.2)	(4.5)	(4.5)	(4.4)	(4.7)	(4.4)	(4.5)
	City Banks	(4.5)	(5.5)	(4.8)	(6.0)	(6.4)	(6.4)	(6.1)	(6.6)	(6.4)	(6.3)
	Regional Banks	(3.0)	(2.3)	(2.2)	(2.3)	(2.7)	(2.6)	(2.7)	(2.7)	(2.5)	(2.6)
	Regional Banks II	(2.5)	(2.1)	(1.9)	(2.2)	(2.4)	(2.3)	(2.4)	(2.5)	(2.2)	(2.5)

(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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