

New targets set in the “new economic policy package”

TOORU KANAHORI
YUUSUKE YOKOTA
ECONOMIC RESEARCH OFFICE

9 JANUARY 2018

(ORIGINAL JAPANESE VERSION RELEASED ON 22 DECEMBER 2017)

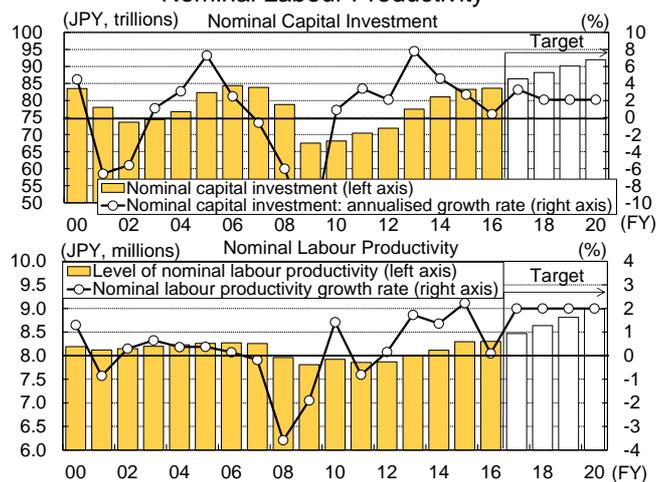
The Bank of Tokyo-Mitsubishi UFJ, Ltd.
A member of MUFG, a global financial group

1. The Real Economy

On 8th December, the Cabinet approved a new economic policy package which consists of two pillars: a productivity revolution and a human resource development revolution. The productivity revolution aims to boost companies' vitality by lowering the corporate tax burden in real terms for those who increase wages and make innovative investments. It also includes structural reforms in line with Society 5.0, such as creating regulatory sandbox frames. Furthermore, the Cabinet raised three new items as targets: a 10% increase from FY2016 in the amount of capital investment by FY2020, a 3% rise in wages from FY2018 and a doubling of the labour productivity growth rate from the FY2011-FY2015 average of 0.9% to 2.0%.

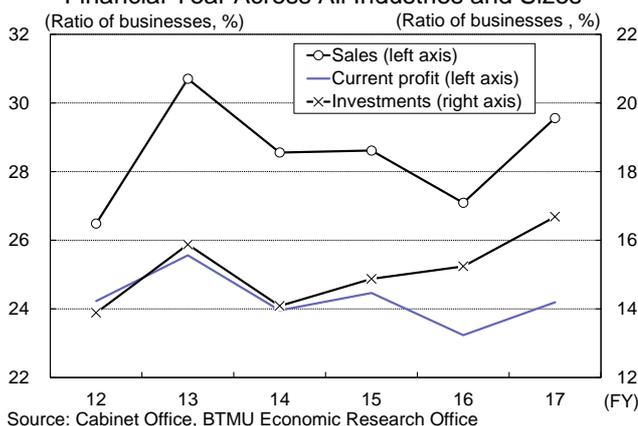
First, in order to achieve a 10% rise in capital investment, it will be necessary to increase nominal capital investment by a yearly average of 2.4%, but considering the yearly average was 3.9% between the FY2013 to FY2016 period since Abenomics was introduced, this target is not much higher (Chart 1). The Business Outlook Survey forecast for FY2018 showed an increase in the ratio of companies who answered “will rise” to the question of “which of the following will increase next fiscal year compared to this fiscal year” in each of the three areas (sales, current profit and investments), which suggests companies are taking a positive view of the future business climate (Chart 2). Based on the fact that capital investment appears to have entered a cyclical phase of expansion, it is reasonably likely that the 10% rise will be achieved. Second, there has been a significant recovery of corporate earnings, a gradual rise in prices and an escalation of the labour shortage as well as an upward trend for hiring regular employees. In light of these factors, the bar is set fairly high for achieving a 3% rise in wages, yet the foundation for this is said to be firming up. On the other hand, looking at the nominal labour productivity growth rate published by the Japan Productivity Center, only FY2015 has exceeded the 2% mark since FY1996 and, by extension, it will be difficult to double the labour productivity growth rate. Nevertheless, such an ambitious target reveals the strong will of the government to address the declining birth rate and aging population and to achieve continuous growth by any means. It will be necessary for the government to steadily implement effective policies that will lead to a drastic improvement in productivity by making use of the stability of both the current economic climate and their political base.

Chart 1: Nominal Capital Investment and Nominal Labour Productivity



Source: Cabinet Office, Japan Productivity Center, BTMU Economic Research Office

Chart 2: Ratio of the Percentage of Businesses who Forecast their Earnings and Investment to Rise Next Financial Year Across All Industries and Sizes



Source: Cabinet Office, BTMU Economic Research Office

2. Financial Markets

(1) Monetary Policy

In a speech given on 13th November, Governor Haruhiko Kuroda commented on the “reversal rate” saying, if the central bank lowered interest rates too far it will impair financial institutions’ intermediation function, so that the effects of monetary easing on the economy will reverse and become contractionary, which led markets to believe that this statement was paving the way for an exit strategy. Further to this point, at a press conference after the Monetary Policy Meeting on 20th-21st December, Mr Kuroda said that bringing up the reversal rate does not necessarily mean that monetary policy needs to be reviewed, dismissing this line of thinking. He also stated that the yield curve is having a suitable effect at present, which suggests the Bank of Japan (BoJ) will maintain its current policy until the trend of prices strengthens to a certain degree.

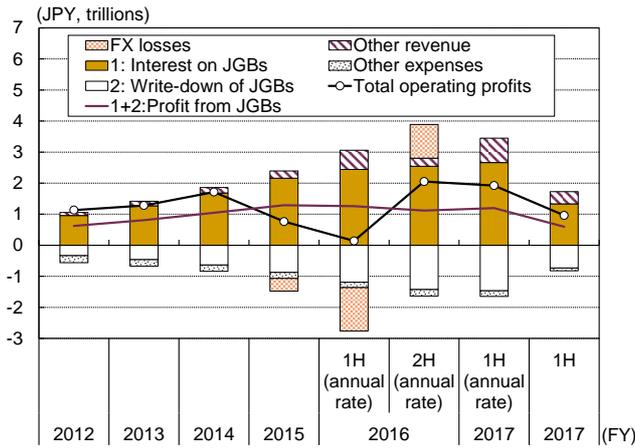
According to its Financial Statements for the First Half of Fiscal 2017 released on 28th November, the BoJ’s “interest and discounts on Japanese government bonds” (the profits of which are limited to JGBs – a large portion of the BoJ’s assets) remained relatively unchanged, despite the rising balance of JGBs held (Chart 3). This is because the “profits from JGBs” available from bonds held is rising, but the “write-down of JGBs”, which is loss incurred by purchasing JGBs at higher prices than their face value, is also rising. When interest rates are raised in the future, there will be a build-up of interest which has to be paid on the Complementary Deposit Facility, and it is thought that the longer current monetary easing continues, the larger the impact will be on the BoJ’s income and finances.

Recently, the BoJ has been testing the market’s reaction by using new phrases such as “reversal rate” with regards to the negative impact of monetary policy on the real economy, but it has not softened its stance that it is inappropriate to mention the effect of a rate hike on the BoJ’s income and finances at present. There are hopes that the BoJ will publicly disclose such information in order to avoid shaking the market when it starts its exit strategy.

(2) Long-Term Yields and Exchange Rate

At the Federal Open Market Committee on 12th-13th December, the US Fed raised the federal funds target rate from a range of 1.00%-1.25% to one of 1.25%-1.50%. As this rate hike was largely factored in beforehand, there was almost no impact on Japanese interest rates and currency exchange; the 10-year JGB yield remained in the vicinity of 0.05% and the JPY continued at around JPY112 to the USD (Chart 4). Looking forwards, unless the US increases the pace of its rate hikes or investors strengthen their risk-averse stance, the JPY/USD and the 10-year JGB yield will continue to see-saw.

Chart 3: Breakdown of the BoJ's Operating Profits



Source: Bank of Japan, BTMU Economic Research Office

Chart 4: JPY/USD and the 10-Year JGB Yield



Source: Bloomberg, BMTU Economic Research Office

(Translated by Elizabeth Foster)

MAIN ECONOMIC AND FINANCIAL INDICATORS (JAPAN)

1. Main Economic Indicators

As of Dec. 22, 2017

	Fiscal	Fiscal	2016		2017	2017				
	2015	2016	3Q	4Q	1Q	JUL	AUG	SEP	OCT	NOV
Real GDP Growth Rate <% changes from previous period at SA annual rate>	1.4	1.2	1.5 (1.5)	2.9 (1.6)	2.5 (2.1)	***	***	***	***	***
Index of All Industries Activity	0.9	0.6	-0.1 (0.8)	1.6 (2.5)	-0.2 (1.5)	-0.1 (2.0)	0.2 (1.7)	-0.5 (1.0)	0.3 (2.0)	
Industrial Production Index										
Production	-0.9	1.1	0.2 (3.8)	2.1 (5.8)	0.4 (4.2)	-0.8 (4.7)	2.0 (5.3)	-1.0 (2.6)	0.5 (5.9)	
Shipments	-1.1	0.8	-0.1 (3.7)	1.5 (5.2)	0.4 (3.7)	-0.7 (4.1)	1.8 (5.8)	-2.5 (1.5)	-0.4 (2.7)	
Inventory	1.1	-4.0	2.2 (-4.0)	-0.5 (-2.9)	-1.6 (-2.4)	-1.1 (-2.3)	-0.6 (-2.9)	0.0 (-2.4)	3.2 (2.0)	
Inventory/Shipments Ratio (2010=100)	114.9	112.9	111.5 [116.8]	112.5 [116.0]	110.7 [114.3]	113.3 [116.1]	108.6 [113.2]	110.3 [113.5]	114.2 [112.2]	108.0
Domestic Corporate Goods Price Index	-3.3	-2.3	1.6 (1.0)	0.4 (2.1)	0.5 (2.9)	0.3 (2.6)	0.0 (2.9)	0.3 (3.1)	0.3 (3.4)	0.4 (3.5)
Consumer Price Index(SA, total, excl.fresh foods)	0.0	-0.2	-0.1 (0.2)	0.6 (0.4)	0.0 (0.6)	0.0 (0.5)	0.1 (0.7)	0.0 (0.7)	0.2 (0.8)	
Index of Capacity Utilization (2010=100)	98.0	98.6	99.8 [96.1]	101.9 [96.3]	101.8 [98.0]	100.1 [97.2]	103.4 [99.2]	101.8 [97.6]	102.0 [98.7]	100.5
Machinery Orders(Private Demand, Excl.Electric Power and Ship building)	4.1	0.5	-1.4 (-1.0)	-4.7 (-1.0)	4.7 (-2.5)	8.0 (-7.5)	3.4 (4.4)	-8.1 (-3.5)	5.0 (2.3)	
Manufacturing	6.2	-4.6	-4.2 (-6.8)	3.7 (3.5)	8.2 (9.2)	2.9 (-1.8)	16.1 (14.7)	-5.1 (-14.8)	7.4 (26.0)	
Non-manufacturing Excl.Electric Power & Ship building	2.5	4.3	0.0 (3.1)	-9.9 (-4.5)	1.6 (-10.1)	4.8 (-12.3)	3.1 (-2.8)	-11.1 (-13.3)	1.1 (-13.9)	
Shipments of Capital Goods (Excl.Transport Equipment)	-2.2	1.5	-2.4 (3.1)	5.0 (6.6)	-0.2 (4.3)	-4.3 (1.5)	9.8 (10.1)	-6.1 (2.1)	1.6 (5.4)	
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)	97.5 (3.5)	100.2 (1.1)	95.6 (-2.4)	97.4 (-2.3)	94.2 (-2.0)	95.2 (-2.9)	93.3 (-4.8)	
Total floor	(2.1)	(4.1)	(3.3)	(1.0)	(-3.7)	(-3.2)	(-3.9)	(-3.9)	(-5.4)	
Sales at Retailers	0.8	-0.2								
Real Consumption Expenditures of Households over 2 persons (SA)	-1.2	-1.6	0.8 (-2.0)	1.0 (0.2)	-0.4 (0.0)	-1.9 (-0.2)	0.2 (0.6)	0.4 (-0.3)	-2.0 (0.0)	
Propensity to Consume (SA,%)	73.6	72.1	73.1 [72.6]	75.3 [72.8]	69.6 [70.7]	69.2 [70.0]	69.8 [70.7]	69.8 [71.6]	71.0 [71.1]	72.4
Overtime Hours Worked (All Industries, 5 employees or more)	-1.3	-0.7	1.5 (1.2)	-0.4 (0.9)	-0.2 (0.9)	-0.8 (0.6)	-0.2 (0.6)	1.8 (1.5)	-1.0 (0.7)	
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	112	131	130	134	123	133	136	
Ratio of Job Offers to Applicants (SA,Times)	1.23	1.39	1.44 [1.29]	1.49 [1.35]	1.52 [1.37]	1.52 [1.37]	1.52 [1.37]	1.52 [1.38]	1.55 [1.40]	1.41
Unemployment Rate (SA,%)	3.3	3.0	2.9	2.9	2.8	2.8	2.8	2.8	2.8	
Economy Watcher Survey (Judgment of the present condition D.I.%)	48.8	46.4	49.2 [45.6]	50.1 [42.6]	50.1 [45.2]	51.0 [45.1]	49.6 [45.6]	49.6 [44.8]	49.9 [46.2]	52.4 [48.6]
Bankruptcies (Number of cases)	8,684 (-9.0)	8,381 (-3.5)	2,079 (-3.0)	2,188 (2.8)	2,032 (-2.6)	714 (0.3)	639 (-12.0)	679 (4.6)	733 (7.3)	677 (-2.3)

(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 Dec. 22, 2017

	Fiscal	Fiscal	2016		2017	2017				
	2015	2016	3Q	4Q	1Q	JUL	AUG	SEP	OCT	NOV
Customs Clearance (Exports in Yen Terms)	-0.7	-3.5	(8.5)	(10.5)	(15.1)	(13.4)	(18.1)	(14.1)	(14.0)	(16.2)
Value	2.0	-5.8	(3.1)	(5.2)	(8.8)	(10.5)	(7.0)	(8.9)	(9.8)	(10.1)
Volumes	-2.7	2.4	(5.1)	(5.1)	(5.8)	(2.6)	(10.4)	(4.8)	(3.8)	(5.5)
Imports (In Yen terms)	-10.2	-10.2	(8.6)	(16.2)	(14.5)	(16.3)	(15.3)	(12.1)	(18.9)	(17.2)
Value	-8.4	-10.7	(6.2)	(10.8)	(12.5)	(12.6)	(12.6)	(12.4)	(15.2)	(14.2)
Volumes	-1.9	0.5	(2.2)	(4.9)	(1.8)	(3.2)	(2.4)	(-0.2)	(3.2)	(2.6)
Current Account (100 mil. yen)	178,618	203,818	59,697	45,622	69,717	23,200	23,804	22,712	21,764	
Goods (100 mil. yen)	3,296	57,726	10,961	9,493	17,375	5,666	3,187	8,522	4,302	
Services (100 mil. yen)	-13,527	-13,816	50	-2,834	-2,930	-2,373	202	-758	-334	
Financial Account (100 mil. yen)	238,492	249,299	52,424	44,237	48,142	8,542	19,230	20,371	-8,532	
Gold & Foreign Exchange Reserves (\$1mil.)	1,262,099	1,230,330	1,230,330	1,249,847	1,266,310	1,260,040	1,268,006	1,266,310	1,260,925	1,261,242
Exchange Rate (¥/\$)	120.13	108.37	113.60	111.06	111.01	112.44	109.91	110.68	112.96	112.92

3. Financial Market Indicators

	Fiscal	Fiscal	2016		2017	2017						
	2015	2016	3Q	4Q	1Q	JUL	AUG	SEP	OCT	NOV		
Uncollateralized Overnight Call Rates	0.063	-0.045	-0.042 [0.035]	-0.054 [-0.050]	-0.054 [-0.046]	-0.054 [-0.043]	-0.049 [-0.043]	-0.058 [-0.052]	-0.037 [-0.037]	-0.048 -0.049		
Euro Yen TIBOR (3 Months)	0.157	0.057	0.056 [0.122]	0.056 [0.060]	0.062 [0.057]	0.075 [0.058]	0.056 [0.058]	0.056 [0.056]	0.063 [0.056]	0.063 [0.056]		
Newly Issued Japanese Government Bonds Yields (10 Years)	-0.050	0.065	0.065 [-0.050]	0.075 [-0.230]	0.060 [-0.085]	0.075 [-0.195]	0.010 [-0.070]	0.060 [-0.085]	0.065 -0.050	0.035 [0.020]		
Average Contracted Interest Rates on Loans and Discounts(City Banks) (% changes from previous period)	0.924	0.847	0.847 (-0.006)	0.842 (-0.005)	0.831 (-0.011)	0.841 (-0.001)	0.839 (-0.002)	0.831 (-0.008)	0.834 (0.003)			
The Nikkei Stock Average (TSE 225 Issues)	16,759	18,909	18,909 [16,759]	20,033 [15,576]	20,356 [16,450]	19,925 [16,569]	19,646 [16,887]	20,356 [16,450]	22,012 [17,425]	22,725 [18,308]		
M2(Average)	(3.5)	(3.6)	(4.1)	(3.9)	(4.0)	(4.0)	(4.0)	(4.0)	(4.1)	(4.0)		
Broadly-defined Liquidity(Average)	(3.7)	(1.8)	(2.3)	(2.8)	(3.7)	(3.5)	(3.7)	(3.9)	(4.1)	(3.9)		
Principal Figures of Financial Institutions												
Loans and Discount (Average)	Banks & Shinkin		(2.4)	(2.4)	(2.8)	(3.1)	(3.1)	(3.3)	(3.2)	(2.9)	(2.8)	(2.7)
	Banks		(2.5)	(2.4)	(2.8)	(3.2)	(3.2)	(3.4)	(3.2)	(3.0)	(2.8)	(2.7)
	City Banks etc.		(1.2)	(1.2)	(2.0)	(2.8)	(2.8)	(3.2)	(2.8)	(2.3)	(2.0)	(1.8)
	Regional Banks		(3.7)	(3.5)	(3.6)	(3.7)	(3.7)	(3.7)	(3.8)	(3.7)	(3.6)	(3.7)
	Regional Banks II		(3.2)	(3.1)	(3.2)	(3.0)	(3.1)	(3.1)	(3.1)	(3.0)	(2.9)	(3.0)
Shinkin		(2.2)	(2.3)	(2.5)	(2.8)	(2.7)	(2.7)	(2.7)	(2.8)	(2.6)	(2.6)	
Deposits and CDs (Average)	Total(3 Business Condition)		(3.7)	(3.8)	(4.5)	(4.5)	(4.5)	(4.5)	(4.4)	(4.5)	(4.4)	(4.4)
	City Banks		(4.5)	(5.5)	(6.4)	(6.5)	(6.4)	(6.4)	(6.3)	(6.5)	(6.3)	(6.3)
	Regional Banks		(3.0)	(2.3)	(2.7)	(2.6)	(2.6)	(2.7)	(2.6)	(2.5)	(2.6)	(2.5)
	Regional Banks II		(2.5)	(2.1)	(2.4)	(2.3)	(2.3)	(2.3)	(2.3)	(2.2)	(2.2)	(2.2)

(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, Bank of Tokyo-Mitsubishi UFJ

Chief Manager, Yasuhiro Ishimaru Tel: +81-(0)3-3240-3204

Written by Tooru Kanahori <tooru_kanahori@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.