

Strong profits and a tight labour market will act as a tailwind for corporate investment and hiring

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1. The Real Economy

Corporations' sentiment for increasing capital investment and hiring has been improving. In the Annual Survey of Corporate Behavior published on 2nd March by the Cabinet Office, listed companies expect to increase capital investment by 4.8% over the next three years (average of FY2018 to FY2020, YoY), the highest growth since the global financial crisis. In addition, they expect to increase employees by 2.6% (average of FY2018 to FY2020, YoY), and the percentage of those expecting to increase full-time employees over the same period was 68.6% (average of FY2018 to FY2020, YoY), which were the highest levels of growth since records began (Chart 1). The result of a survey of corporations' stances on allocating profit in the Business Outlook Survey published on 11th March by the Cabinet Office also substantiates this improvement in business sentiment regarding capital investment and hiring. The weighting of areas related to improving corporations' financial standings, such as "retaining profits" and "reducing interest-bearing debt" is declining in terms of importance. On the other hand, it appears there is a marked increase in the weighting of areas related to an increase in expenditure, such as "capital investment", "hiring new employees" and "passing on profits to employees" (Chart 2).

The background of these results is a high level of corporate profits, supported by an economic recovery in Japan and overseas. The operating profits of non-financial corporations recorded a year-on-year increase for the sixth consecutive quarter at the end of last year. However, more important than this is the worsening labour shortage. The jobs-to-applicants ratio has reached historically high levels in recent years, but rather than merely being the result of economic cycles, these high levels are more closely associated with structural changes owing to the decline of the working-age population. At present, securing employees and investing in efficiency are urgent and long-term issues that are at a level which has never been seen before. This is resulting in strong expectations of investment and hiring, which continues despite short-term fluctuations in the economy.

Going forwards, it is very unlikely that corporate profits will be impervious to the impact from yen appreciation, which has been brought about by uncertainty surrounding the US' trade policies. However, there is a strong possibility that profits will remain at a high level due to the strength of the domestic and overseas economies. In addition, the tightening gap between labour supply and demand caused by structural factors is boosting investment in human resources and capital by corporations. Therefore, it seems that the virtuous economic cycle will not be interrupted easily.

Chart 1: Listed Companies' Expectations for Capital Investment and Hiring Over The Next 3 Years

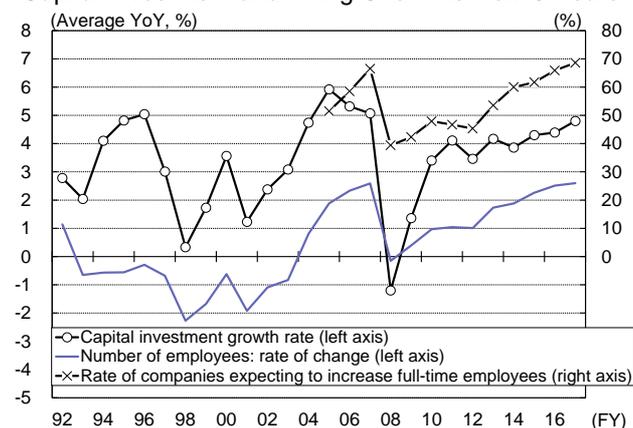
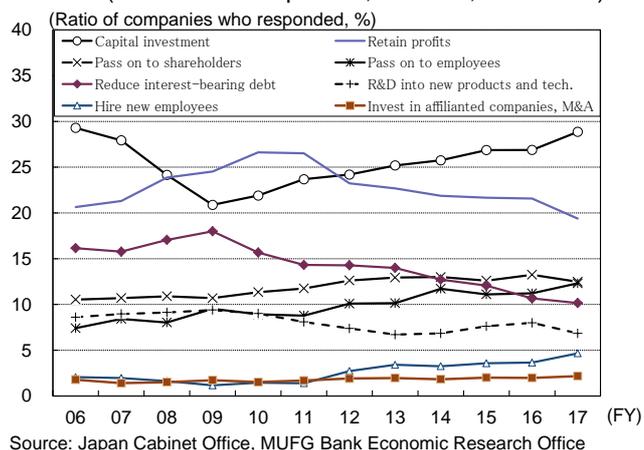


Chart 2: Corporations' Profit Allocation Each Financial Year (total of most important, all sizes, all sectors)



2. Monetary Policy and Financial Markets

On 16th March, parliament approved the nominations for the two deputy governors of the Bank of Japan (BoJ). Going forwards, policy management will be carried out under a new policy board as Masayoshi Amamiya and Masazumi Wakatabe were appointed as the two new deputies, and Haruhiko Kuroda was reappointed as governor. In his speech during a confirmation hearing at the lower house, Governor Kuroda reiterated his cautious stance towards a stimulus exit, saying “prices are still some distance from the 2% target, so discussing an exit right now would be incongruous” (Table 1). Likewise, at the press conference after the Monetary Policy Meeting on 9th March, he said “we are absolutely not considering changing the yield curve control and inflation-overshooting commitment components of the policy framework until the 2% target is reached”, emphasising that the BoJ will hold firm to achieving its price target and maintaining its current policy framework.

Turning to current prices, core CPI was 1.0% YoY in February, which is still some distance from 2%, suggesting that the current monetary policy framework will not change (Chart 3). However, there is significant upward pressure on prices from external factors such as energy prices, the weaker yen in 2017 and the rise in accommodation costs and travel costs around the Lunar New Year. As a result, core CPI exceeded 1% (YoY) for the first time since August 2014. In addition, the second round of annual labour negotiations resulted in a 2.17% increase in wages, falling below the 2015 wage hike of 2.36%, which was the highest in recent years. Nevertheless, a breakdown of the wage rise reveals the base salary of unions increased by 0.64%: roughly the same level as 2015 (0.65%). Looking ahead, this rise in wages is expected to spread, resulting in a gradual increase in the trend of prices.

At the press conference on 9th March, in response to the question, “if inflation expectations rise, logically speaking the easing effect would be unchanged and this is not an exit from monetary easing, even if the nominal target yield increases”, Governor Kuroda did not give much away and replied, “logically that does stand up, but we are not considering it at present”. Based on these points and assuming the degree of easing will not change, it is best to continue to allow for the possibility that the BoJ will fine tune its target rate, even before reaching their 2% price stability target.

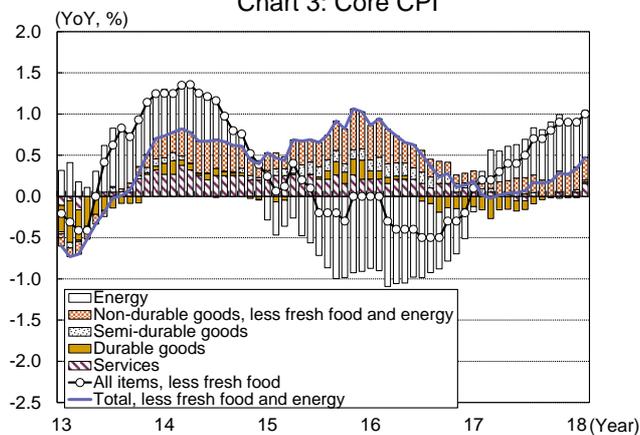
As investors became increasingly risk averse due to announcements by the US that it will set up extra tariffs on limit steel and aluminium imports and will impose sanctions on China, the 10-year Japanese government bond (JGB) yield fell to 0.02% and the JPY appreciated to JPY104 against the USD. Currently, concerns about a trade war between the US and China are fading, and JGBs and the JPY have started to return to their previous levels. However, it seems that they may fluctuate easily for the time being, depending on changes to each country’s trade policies.

Table 1: Statements Made by Governor Kuroda

	Comments
Policy management stance	<ul style="list-style-type: none"> The Bank can reach its targets by continuing to persist with powerful monetary easing. At a stage where the price stability target has not been attained, monetary easing will not be loosened or abandoned. It is not the case that we definitely will not change the current short-term policy rate and 10-year JGB yield target. If the economy loses momentum to achieve our price target, we would of course consider easing policy further. Currently, we are not thinking about ending negative interest rates.
Impact and side effects	<ul style="list-style-type: none"> Japan has overcome deflation as defined by a continual fall in prices. Currently, there has been no impact on financial intermediary functions, but there may be in the long term. I do not think that the Bank of Japan's finances are in a serious condition. Prices are still some distance from the 2% target, so discussing an exit right now would be incongruous.
Exit strategy	<ul style="list-style-type: none"> When monetary policy is normalised, the process will be very gradual and will take economic conditions into account. We are absolutely not considering changing the yield curve control and inflation overshooting commitment components of the policy framework until the 2% target is reached. (In response to the question, "if inflation expectations rise, logically speaking the easing effect would be unchanged and this is not an exit from monetary easing, even if the nominal target yield increases") logically that does stand up, but we are not considering it at present.

Source: Various news reports, MUFG Bank Economic Research Office

Chart 3: Core CPI



Note: Excludes the direct impact from the rise in consumption tax rate
 Source: Ministry of Internal Affairs and Communications, Bank of Japan, MUFG Bank Economic Research Office

(Translated by Elizabeth Foster)

MAIN ECONOMIC AND FINANCIAL INDICATORS (JAPAN)

1. Main Economic Indicators

As of Mar. 29, 2018

	Fiscal	Fiscal	2017			2017			2018	
	2015	2016	2Q	3Q	4Q	OCT	NOV	DEC	JAN	FEB
Real GDP Growth Rate <% changes from previous period at SA annual rate>	1.4	1.2	2.4 (1.5)	2.4 (1.9)	1.6 (2.0)	***	***	***	***	***
Index of All Industries Activity	0.9	0.6	1.6 (2.5)	-0.3 (1.5)	0.8 (1.9)	0.2 (1.8)	1.0 (1.9)	0.6 (1.9)	-1.8 (1.8)	
Industrial Production Index										
Production	-0.9	1.1	2.1 (5.8)	0.4 (4.2)	1.8 (4.6)	0.5 (5.9)	0.5 (3.6)	2.9 (4.4)	-6.8 (2.5)	
Shipments	-1.1	0.8	1.5 (5.2)	0.4 (3.7)	1.0 (3.0)	-0.4 (2.7)	2.3 (2.3)	2.9 (4.2)	-5.7 (2.0)	
Inventory	1.1	-4.0	-0.5 (-2.9)	-1.6 (-2.4)	2.1 (2.1)	3.2 (2.0)	-0.8 (3.0)	-0.3 (2.1)	-0.5 (1.4)	
Inventory/Shipments Ratio (2010=100)	114.9	112.9	112.5 [116.0]	110.7 [114.3]	111.9 [109.7]	114.2 [112.2]	111.1 [108.0]	110.5 [108.9]	114.2 [111.6]	[111.3]
Domestic Corporate Goods Price Index	-3.3	-2.4	0.5 (2.1)	0.4 (2.8)	0.9 (3.3)	0.4 (3.5)	0.4 (3.5)	0.2 (3.0)	0.3 (2.7)	0.0 (2.5)
Consumer Price Index(SA, total, excl.fresh foods)	0.0	-0.2	0.6 (0.4)	0.0 (0.6)	0.4 (0.9)	0.1 (0.8)	0.1 (0.9)	0.0 (0.9)	0.2 (0.9)	0.1 (1.0)
Index of Capacity Utilization (2010=100)	98.0	98.6	101.9 [96.3]	101.8 [98.0]	103.0 [100.1]	102.0 [98.7]	102.0 [100.5]	104.9 [101.1]	97.2 [98.3]	[101.4]
Machinery Orders(Private Demand, Excl.Electric Power and Ship building)	4.1	0.5	-3.4 (-1.0)	2.8 (-2.5)	0.3 (0.0)	2.7 (2.3)	5.5 (4.1)	-9.3 (-5.0)	8.2 (2.9)	
Manufacturing	6.2	-4.6	2.6 (3.5)	6.2 (9.2)	3.5 (13.3)	5.1 (26.0)	0.0 (14.2)	-8.5 (3.0)	9.9 (16.8)	
Non-manufacturing	2.5	4.3	-8.1 (-4.5)	0.0 (-10.1)	-2.1 (-9.7)	-0.7 (-13.9)	6.0 (-3.9)	-5.3 (-10.9)	4.4 (-7.0)	
Excl.Electric Power & Ship building										
Shipments of Capital Goods (Excl.Transport Equipment)	-2.2	1.5	5.0 (6.6)	-0.2 (4.3)	4.3 (7.1)	1.6 (5.4)	3.7 (5.6)	3.8 (9.9)	-5.2 (8.6)	
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)	98.7 (1.1)	95.4 (-2.4)	94.8 (-2.4)	94.5 (-4.8)	96.2 (-0.4)	93.6 (-2.1)	85.6 (-13.2)	
Total floor	(2.1)	(4.1)	(1.0)	(-3.7)	(-3.2)	(-5.4)	(-1.2)	(-2.9)	(-14.9)	
Sales at Retailers	0.8	-0.2								
Real Consumption Expenditures of Households over 2 persons (SA)	-1.2	-1.6	0.8 (0.2)	-0.4 (0.0)	-0.6 (0.5)	-1.2 (0.0)	1.4 (1.7)	-1.6 (-0.1)	2.8 (2.0)	
Propensity to Consume (SA,%)	73.6	72.1	74.6 [72.3]	70.3 [71.3]	71.3 [71.8]	71.2 [71.3]	71.7 [72.1]	70.9 [72.0]	74.5 [71.5]	[75.1]
Overtime Hours Worked (All Industries, 5 employees or more)	-1.3	-0.7	-0.4 (0.9)	-0.2 (0.9)	0.2 (1.2)	-1.0 (0.7)	0.6 (1.5)	-0.8 (1.5)	-1.4 (-2.0)	
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	131	130	133	136	135	129	131	
Ratio of Job Offers to Applicants (SA,Times)	1.23	1.39	1.49 [1.35]	1.52 [1.37]	1.57 [1.41]	1.55 [1.40]	1.56 [1.41]	1.59 [1.43]	1.59 [1.43]	[1.44]
Unemployment Rate (SA,%)	3.3	3.0	2.9	2.8	2.7	2.8	2.7	2.7	2.4	
Economy Watcher Survey (Judgment of the present condition D.I.%)	48.8	46.4	49.2 [41.4]	50.3 [45.5]	53.3 [49.8]	52.0 [48.3]	54.1 [50.5]	53.9 [50.7]	49.9 [49.4]	48.6 [48.8]
Bankruptcies (Number of cases)	8,684 (-9.0)	8,381 (-3.5)	2,188 (2.8)	2,032 (-2.6)	2,106 (1.0)	733 (7.3)	677 (-2.3)	696 (-2.0)	635 (5.0)	617 (-10.3)

(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 Mar. 29, 2018									
	Fiscal		2017			2017			2018	
	2015	2016	2Q	3Q	4Q	OCT	NOV	DEC	JAN	FEB
Customs Clearance (Exports in Yen Terms)	-0.7	-3.5	(10.5)	(15.1)	(13.0)	(14.0)	(16.2)	(9.4)	(12.3)	(1.8)
Value	2.0	-5.8	(5.2)	(8.8)	(8.1)	(9.8)	(10.1)	(4.6)	(2.7)	(4.0)
Volumes	-2.7	2.4	(5.1)	(5.8)	(4.6)	(3.8)	(5.5)	(4.5)	(9.3)	(-2.1)
Imports (In Yen terms)	-10.2	-10.2	(16.2)	(14.8)	(17.0)	(19.0)	(17.3)	(15.0)	(7.7)	(16.5)
Value	-8.4	-10.7	(10.8)	(12.8)	(12.7)	(15.3)	(14.3)	(8.6)	(5.0)	(4.4)
Volumes	-1.9	0.5	(4.9)	(1.8)	(3.9)	(3.2)	(2.6)	(5.9)	(2.6)	(11.7)
Current Account (100 mil. yen)	178,618	203,818	45,622	70,214	43,209	21,764	13,473	7,972	6,074	
Goods (100 mil. yen)	3,296	57,726	9,493	17,353	11,500	4,302	1,810	5,389	-6,666	
Services (100 mil. yen)	-13,527	-13,816	-2,834	-2,315	-1,962	-334	417	-2,045	-1,682	
Financial Account (100 mil. yen)	238,492	249,299	44,237	50,052	24,365	-8,532	14,046	18,851	12,072	
Gold & Foreign Exchange Reserves (\$1mil.)	1,262,099	1,230,330	1,249,847	1,266,310	1,264,283	1,260,925	1,261,242	1,264,283	1,268,535	1,261,749
Exchange Rate (¥/\$)	120.13	108.37	111.06	111.01	112.95	112.96	112.92	112.97	110.77	107.82

3. Financial Market Indicators

	Fiscal		2017			2017			2018			
	2015	2016	2Q	3Q	4Q	OCT	NOV	DEC	JAN	FEB		
Uncollateralized Overnight Call Rates	0.063	-0.045	-0.054 [-0.050]	-0.054 [-0.046]	-0.042 [-0.043]	-0.037 [-0.037]	-0.048 [-0.049]	-0.042 [-0.044]	-0.040 [-0.045]	-0.042 -0.038		
Euro Yen TIBOR (3 Months)	0.157	0.057	0.056 [0.060]	0.062 [0.057]	0.063 [0.056]	0.063 [0.056]	0.063 [0.056]	0.063 [0.056]	0.068 [0.056]	0.068 [0.056]		
Newly Issued Japanese Government Bonds Yields (10 Years)	-0.050	0.065	0.075 [-0.230]	0.060 [-0.085]	0.045 [0.040]	0.065 [-0.050]	0.035 [0.020]	0.045 [0.040]	0.080 0.085	0.045 [0.050]		
Average Contracted Interest Rates on Loans and Discounts(City Banks) (% changes from previous period)	0.924	0.847	0.842 (-0.005)	0.831 (-0.011)	0.828 (-0.003)	0.834 (0.003)	0.835 (0.001)	0.828 (-0.007)	0.827 (-0.001)			
The Nikkei Stock Average (TSE 225 Issues)	16,759	18,909	20,033 [15,576]	20,356 [16,450]	22,765 [19,114]	22,012 [17,425]	22,725 [18,308]	22,765 [19,114]	23,098 [19,041]	22,068 [19,119]		
M2(Average)	(3.5)	(3.6)	(3.9)	(4.0)	(3.9)	(4.1)	(4.0)	(3.6)	(3.4)	(3.3)		
Broadly-defined Liquidity(Average)	(3.7)	(1.8)	(2.8)	(3.7)	(3.8)	(4.1)	(3.9)	(3.5)	(3.3)	(3.1)		
Principal Figures of Financial Institutions												
Loans and Discount (Average)	Banks & Shinkin		(2.4)	(2.4)	(3.1)	(3.1)	(2.6)	(2.8)	(2.7)	(2.5)	(2.3)	(2.1)
	Banks		(2.5)	(2.4)	(3.2)	(3.2)	(2.6)	(2.8)	(2.7)	(2.4)	(2.3)	(2.1)
	City Banks etc.		(1.2)	(1.2)	(2.8)	(2.8)	(1.7)	(2.0)	(1.8)	(1.2)	(1.1)	(0.6)
	Regional Banks		(3.7)	(3.5)	(3.7)	(3.7)	(3.7)	(3.6)	(3.7)	(3.6)	(3.5)	(3.6)
	Regional Banks II		(3.2)	(3.1)	(3.0)	(3.1)	(3.0)	(2.9)	(3.0)	(3.0)	(2.8)	(2.8)
Deposits and CDs (Average)	Shinkin		(2.2)	(2.3)	(2.8)	(2.7)	(2.6)	(2.6)	(2.6)	(2.5)	(2.5)	
	Total(3 Business Condition)		(3.7)	(3.8)	(4.5)	(4.5)	(4.3)	(4.4)	(4.4)	(4.0)	(3.8)	(3.5)
	City Banks		(4.5)	(5.5)	(6.5)	(6.4)	(6.1)	(6.3)	(6.3)	(5.7)	(5.3)	(4.9)
	Regional Banks		(3.0)	(2.3)	(2.6)	(2.6)	(2.5)	(2.6)	(2.5)	(2.5)	(2.4)	(2.2)
Regional Banks II		(2.5)	(2.1)	(2.3)	(2.3)	(2.0)	(2.2)	(2.2)	(1.8)	(1.6)	(1.6)	

(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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