

## Corporations' forecasts for overseas demand grow more cautious

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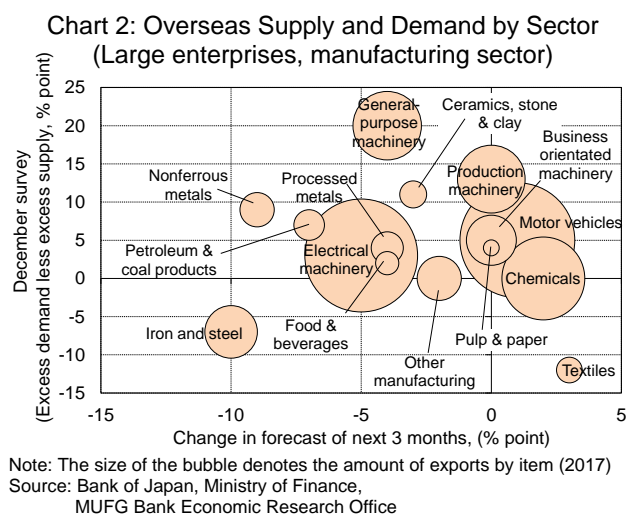
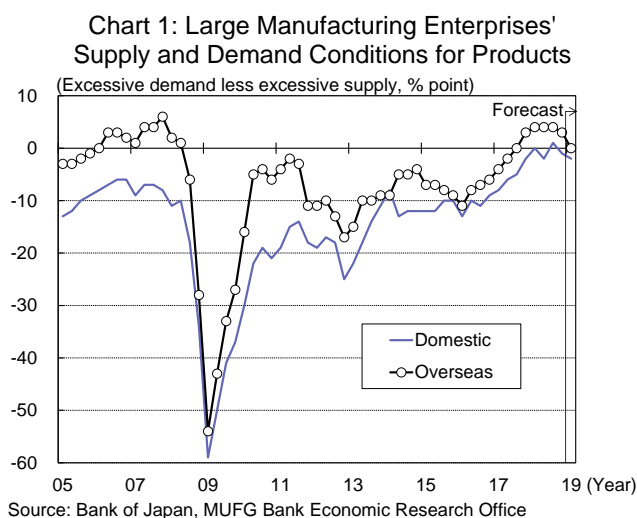
MUFG Bank, Ltd.  
A member of MUFG, a global financial group

(ORIGINAL JAPANESE VERSION RELEASED ON 26 DECEMBER 2018)

### 1. The Real Economy

Corporations are becoming more cautious when it comes to their forecast for the future business environment. According to the Bank of Japan's December Tankan survey which was published this month, the forecast of corporations' business sentiment for the next three months fell by 4% points compared with present conditions across both large manufacturing and non-manufacturing enterprises. Even though enterprises' judgement of current conditions is at a comparatively high level and they still have a forward-looking attitude towards investment, as seen by their strong planned fixed investment, the forecast of current profits for 2H was revised downwards and their judgement of business conditions is becoming more cautious. One of the reasons for this is a rise in personnel expenses due to the worsening labour shortage, and another significant factor, especially in the manufacturing sector, is an increase in enterprises' concerns that overseas demand will decline owing to the impact of trade friction between the US and China.

The diffusion index (DI) of large manufacturing enterprises' overseas supply and demand in the Bank of Japan's Tankan survey had risen since June 2016, but after three consecutive quarters at the same level since the start of 2018, it fell this time around in the December survey (Chart 1). In addition, the forecast has dropped by 3% points, a comparatively large fall, and although it is still at a high level, it shows that cautious views are increasing. However, a breakdown by industry reveals a mixed bag; the forecasts of more than half of all industries have grown more cautious, yet in the motor vehicle and chemical industries, which export on a large scale, the forecast is improving (Chart 2). In the December 2007 survey before the global financial crisis, the forecast also deteriorated by 3% points, but taking into consideration forecasts across all industries stayed the same or worsened at that time, the current phase is not a sign of a genuine adjustment. Rather, it appears that industries and corporations are at a stage where they are assessing the impact of the US-China trade friction. The US and China are currently in talks for 90 days while additional tariffs are postponed as agreed during the US-China summit at the start of December. As for the US-Japan trade agreement, full-fledged negotiations will start from the beginning of 2019. It seems the direction of negotiations will have a significant effect on the future of overseas demand and business sentiment and, as such, it will be important to keep an eye on it in future.



## 2. Prices and Financial Markets

### (1) Monetary Policy

The Bank of Japan (BoJ) decided to maintain its current monetary policy at its Monetary Policy Meeting on 19<sup>th</sup> and 20<sup>th</sup> December. One focal point this time was how the BoJ would assess the current increase in concerns about a slowdown of overseas economies and a softening of financial markets starting in the US. However, at a press conference, Governor Kuroda said “while it is necessary to pay sufficient attention to overseas risks, there’s no change to our baseline view on Japan’s economy and its outlook at present”, thereby maintaining his previous stance.

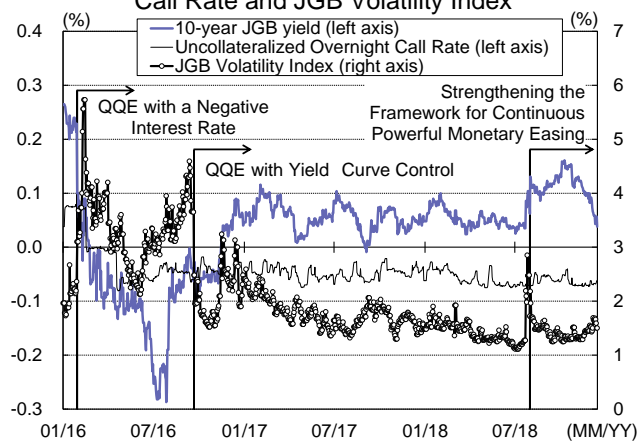
Meanwhile, the long-term JGB yield had been hovering at the top of its de facto range of movement (+0.2% to -0.2%) since the introduction of “Strengthening the Framework for Continuous Powerful Monetary Easing” (Strengthening the Framework) in July. However, it recently started to weaken alongside a sharp drop in yields overseas (Chart 3). Within its Strengthening the Framework, it is thought that the BoJ aims to tolerate a rise in Japanese long-term interest rates to their upper limit in line with strong foreign interest rates and to allow a certain degree of steepening of the yield curve in the case that long-term interest rates start to fluctuate more. In light of the accumulation of side effects impacting the function of financial intermediation owing to yield curve flattening and the difference between the degree of monetary easing in Japan and US/Europe, an increased tolerance for a rise in interest rates and a steepening of the yield curve appears to be the first step in the process of gradually normalising monetary policy. However, it also appears that the BoJ has had to start from the beginning again in terms of normalisation owing to the current decrease in foreign interest rates. Nevertheless, when asked about the trend of long-term interest rates, Governor Kuroda said “the recent moves are natural as Japanese yields are falling in line with declines in European and US long-term rates. I don’t think this is something problematic”. He added that “if yields are reflecting changes in economic, price and financial markets both domestically and overseas, this shows a rise in the functionality of the bond market”. It is thought that monetary policy normalisation is not an urgent political issue as entering into negative rates is also within

the BoJ's realm of acceptability, and it is likely that alterations on the management front will be central to normalisation for the time being.

## (2) Exchange Rates

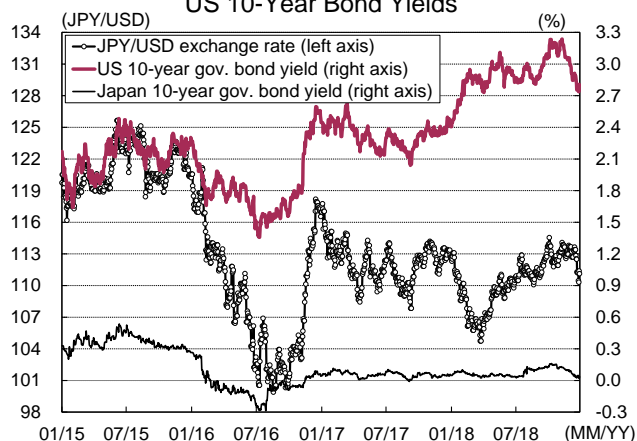
Since November, the JPY has generally remained at around JPY 113 to the USD. A subsequent rise in concerns about a slowdown of overseas economies and a weakening of global financial markets led to increased risk aversion, resulting in the JPY appreciating to around JPY 110 per USD at present (Chart 4). That being said, even if the JPY does fluctuate due to changes in the situation overseas, such as trade friction between the US and China, any sharp appreciation is expected to be avoided owing to the continued existence of the gap between Japanese and US interest rates.

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



Source: Bloomberg, MUFG Bank Economic Research Office

Chart 4: JPY/USD Exchange Rate and Japanese and US 10-Year Bond Yields



Source: Bloomberg, MUFG Bank Economic Research Office

(Translated by Elizabeth Foster)

## MAIN ECONOMIC AND FINANCIAL INDICATORS (JAPAN)

### 1. Main Economic Indicators

As of Dec. 26, 2018

|                                                                                                         | Fiscal                 | Fiscal                   | 2018                     |                          |                          | 2018                     |                        |                          |                        |                |
|---------------------------------------------------------------------------------------------------------|------------------------|--------------------------|--------------------------|--------------------------|--------------------------|--------------------------|------------------------|--------------------------|------------------------|----------------|
|                                                                                                         | 2016                   | 2017                     | 1Q                       | 2Q                       | 3Q                       | JUL                      | AUG                    | SEP                      | OCT                    | NOV            |
| Real GDP Growth Rate <% changes from previous period at SA annual rate>                                 | 0.9                    | 1.9                      | -1.3<br>(1.2)            | 2.8<br>(1.4)             | -2.5<br>(0.0)            | ***                      | ***                    | ***                      | ***                    | ***            |
| Index of All Industries Activity                                                                        | 0.6                    | 1.8                      | -0.5<br>(1.3)            | 0.9<br>(1.1)             | -0.8<br>(0.2)            | -0.1<br>(0.9)            | 0.4<br>(0.8)           | -1.0<br>(-1.2)           | 1.9<br>(2.3)           |                |
| Industrial Production Index                                                                             | 0.8                    | 2.9                      | -1.1<br>(1.8)            | 1.2<br>(1.2)             | -1.3<br>(-0.1)           | -0.4<br>(2.1)            | 0.3<br>(0.2)           | -0.4<br>(-2.5)           | 2.9<br>(4.2)           |                |
| Production                                                                                              |                        |                          |                          |                          |                          |                          |                        |                          |                        |                |
| Shipments                                                                                               | 0.6                    | 2.2                      | -1.3<br>(0.8)            | 2.1<br>(1.6)             | -1.9<br>(-0.5)           | -2.1<br>(0.9)            | 1.8<br>(0.6)           | -2.0<br>(-2.9)           | 3.5<br>(5.7)           |                |
| Inventory                                                                                               | -1.4                   | 5.2                      | 3.0<br>(5.2)             | -2.6<br>(2.4)            | 1.2<br>(3.5)             | 0.2<br>(3.2)             | -0.2<br>(2.8)          | 1.2<br>(3.5)             | -1.3<br>(-0.7)         |                |
| Inventory/Shipments Ratio<br>(2015=100)                                                                 | 100.7                  | 102.2                    | 106.6<br>[100.2]         | 104.1<br>[100.3]         | 104.6<br>[99.6]          | 105.8<br>[100.1]         | 102.7<br>[98.1]        | 105.2<br>[100.6]         | 104.7<br>[105.0]       | 101.5          |
| Domestic Corporate Goods Price Index                                                                    | -2.4                   | 2.7                      | 0.6<br>(2.5)             | 0.6<br>(2.4)             | 0.9<br>(3.0)             | 0.4<br>(3.0)             | 0.0<br>(3.0)           | 0.3<br>(3.0)             | 0.4<br>(3.0)           | -0.3<br>(2.3)  |
| Consumer Price Index(SA, total, excl.fresh foods)                                                       | -0.2                   | 0.7                      | -0.1<br>(0.9)            | 0.4<br>(0.7)             | 0.2<br>(0.9)             | 0.1<br>(0.8)             | 0.3<br>(0.9)           | 0.1<br>(1.0)             | 0.2<br>(1.0)           | 0.0<br>(0.9)   |
| Index of Capacity Utilization<br>(2015=100)                                                             | 99.2                   | 102.7                    | 101.9<br>[100.7]         | 103.2<br>[102.8]         | 101.4<br>[102.5]         | 100.3<br>[101.6]         | 102.7<br>[103.1]       | 101.2<br>[102.8]         | 105.2<br>[102.8]       | 103.4          |
| Machinery Orders(Private Demand,<br>Excl.Electric Power and Ship building)                              | 0.5                    | -0.8                     | 3.3<br>(0.2)             | 2.2<br>(8.0)             | 0.9<br>(4.8)             | 11.0<br>(13.9)           | 6.8<br>(12.6)          | -18.3<br>(-7.0)          | 7.6<br>(4.5)           |                |
| Manufacturing                                                                                           | -4.6                   | 9.2                      | 2.5<br>(10.6)            | 5.5<br>(17.8)            | -2.0<br>(8.5)            | 11.8<br>(21.2)           | 6.6<br>(13.9)          | -17.3<br>(-5.5)          | 12.3<br>(3.9)          |                |
| Non-manufacturing<br>Excl.Electric Power & Ship building                                                | 4.3                    | -7.8                     | 3.4<br>(-6.9)            | -0.4<br>(0.3)            | 3.5<br>(2.0)             | 10.9<br>(7.7)            | 6.0<br>(11.6)          | -17.1<br>(-8.0)          | 4.5<br>(5.1)           |                |
| Shipments of Capital Goods<br>(Excl.Transport Equipment)                                                | 0.3                    | 7.0                      | -0.7<br>(8.0)            | 0.7<br>(4.0)             | -1.5<br>(1.6)            | -0.2<br>(5.0)            | 3.6<br>(1.8)           | -2.0<br>(-1.3)           | 5.4<br>(7.2)           |                |
| 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<br>10,000 units at Annual Rate, SA<br>Total floor                                        | 97.4<br>(5.8)<br>(4.1) | 94.6<br>(-2.8)<br>(-3.7) | 89.2<br>(-8.0)<br>(-9.2) | 96.8<br>(-1.8)<br>(-3.6) | 95.3<br>(-0.2)<br>(-0.9) | 95.8<br>(-0.7)<br>(-1.6) | 95.7<br>(1.6)<br>(0.5) | 94.3<br>(-1.5)<br>(-1.6) | 95.0<br>(0.3)<br>(2.2) |                |
| Sales at Retailers                                                                                      | -0.2                   | 1.9                      |                          |                          |                          |                          |                        |                          |                        |                |
| Real Consumption Expenditures<br>of Households over 2 persons (SA)                                      | -1.6                   | 0.2                      | 1.1<br>(0.6)             | -1.4<br>(-1.3)           | 1.4<br>(1.0)             | -1.1<br>(0.4)            | 3.5<br>(2.8)           | -4.5<br>(-0.5)           | 1.8<br>(1.0)           |                |
| Propensity to Consume<br>(SA, %)                                                                        | 72.1                   | 71.7                     | 71.4<br>[73.0]           | 69.4<br>[74.6]           | 70.2<br>[70.3]           | 69.9<br>[70.3]           | 70.7<br>[70.3]         | 69.9<br>[70.3]           | 70.0<br>[71.2]         | 71.7           |
| Overtime Hours Worked<br>(All Industries, 5 employees or more)                                          | -0.7                   | 0.4                      | -1.1<br>(-1.2)           | 1.6<br>(0.6)             | -3.2<br>(-2.5)           | -3.1<br>(-1.8)           | -0.1<br>(-1.9)         | -0.6<br>(-3.6)           | 2.2<br>(-0.9)          |                |
| Total Cash Earnings (Regular Employees<br>Only; All Industries, 5 employees or more)                    | 0.4                    | 0.7                      |                          |                          |                          |                          |                        |                          |                        |                |
| Employment Index(Regular Employees Only;All Industries,<br>5 employees or more) (Change over the M/Q/Y) | 103                    | 105                      | 25                       | 6                        | -11                      | -11                      | -5                     | -16                      | -18                    |                |
| Ratio of Job Offers to Applicants<br>(SA, Times)                                                        | 1.39                   | 1.54                     | 1.59<br>[1.44]           | 1.60<br>[1.49]           | 1.63<br>[1.52]           | 1.63<br>[1.51]           | 1.63<br>[1.52]         | 1.64<br>[1.53]           | 1.62<br>[1.55]         | 1.56           |
| Unemployment Rate<br>(SA, %)                                                                            | 3.0                    | 2.7                      | 2.5                      | 2.4                      | 2.4                      | 2.5                      | 2.4                    | 2.3                      | 2.4                    |                |
| Economy Watcher Survey<br>(Judgment of the present condition D.I.%)                                     | 46.4                   | 50.5                     | 49.1<br>[48.7]           | 48.1<br>[49.2]           | 48.0<br>[50.3]           | 46.6<br>[49.9]           | 48.7<br>[50.0]         | 48.6<br>[51.1]           | 49.5<br>[52.0]         | 51.0<br>[54.1] |
| Bankruptcies (Number of cases)                                                                          | 8,381<br>(-3.5)        | 8,367<br>(-0.2)          | 2,041<br>(-1.8)          | 2,107<br>(-3.7)          | 2,017<br>(-0.7)          | 702<br>(-1.7)            | 694<br>(8.6)           | 621<br>(-8.5)            | 730<br>(-0.4)          | 718<br>(6.1)   |

(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. 26, 2018

|                                            | Fiscal    | Fiscal    | 2018      |           |           | 2018      |           |           |           |           |
|--------------------------------------------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|
|                                            | 2016      | 2017      | 1Q        | 2Q        | 3Q        | JUL       | AUG       | SEP       | OCT       | NOV       |
| Customs Clearance (Exports in Yen Terms)   | -3.5      | 10.8      | (4.9)     | (7.5)     | (2.9)     | (3.9)     | (6.6)     | (-1.3)    | (8.2)     | (0.1)     |
| Value                                      | -6.0      | 5.5       | (0.8)     | (1.8)     | (4.0)     | (3.0)     | (5.4)     | (3.7)     | (4.3)     | (2.1)     |
| Volumes                                    | 2.7       | 5.0       | (4.1)     | (5.6)     | (-1.1)    | (0.9)     | (1.1)     | (-4.9)    | (3.8)     | (-1.9)    |
| Imports (In Yen terms)                     | -10.2     | 13.7      | (7.5)     | (7.5)     | (12.4)    | (14.7)    | (15.5)    | (7.1)     | (19.9)    | (12.5)    |
| Value                                      | -10.0     | 8.8       | (3.6)     | (6.1)     | (10.3)    | (10.2)    | (10.5)    | (10.1)    | (8.7)     | (7.9)     |
| Volumes                                    | -0.2      | 4.4       | (3.7)     | (1.4)     | (1.9)     | (4.0)     | (4.5)     | (-2.7)    | (10.3)    | (4.2)     |
| Current Account (100 mil. yen)             | 210,188   | 218,127   | 58,821    | 49,775    | 56,698    | 20,097    | 18,384    | 18,216    | 13,099    |           |
| Goods (100 mil. yen)                       | 57,851    | 45,936    | 7,246     | 10,661    | 1,030     | -10       | -2,193    | 3,233     | -3,217    |           |
| Services (100 mil. yen)                    | -13,813   | -5,378    | 2,127     | -6,118    | -2,220    | -1,744    | -61       | -415      | -2,330    |           |
| Financial Account (100 mil. yen)           | 247,407   | 196,174   | 75,622    | 53,095    | 42,652    | -8,319    | 19,128    | 31,843    | 15,479    |           |
| Gold & Foreign Exchange Reserves (\$1mil.) | 1,230,330 | 1,268,287 | 1,268,287 | 1,258,748 | 1,259,673 | 1,256,276 | 1,259,305 | 1,259,673 | 1,252,873 | 1,258,264 |
| Exchange Rate (¥/\$)                       | 108.37    | 110.80    | 108.20    | 109.05    | 111.44    | 111.37    | 111.06    | 111.89    | 112.78    | 113.37    |

## 3. Financial Market Indicators

|                                                                                                             | Fiscal                      | Fiscal | 2018               |                    |                    | 2018               |                    |                    |                    |                    |        |        |
|-------------------------------------------------------------------------------------------------------------|-----------------------------|--------|--------------------|--------------------|--------------------|--------------------|--------------------|--------------------|--------------------|--------------------|--------|--------|
|                                                                                                             | 2016                        | 2017   | 1Q                 | 2Q                 | 3Q                 | JUL                | AUG                | SEP                | OCT                | NOV                |        |        |
| Uncollateralized Overnight Call Rates                                                                       | -0.045                      | -0.050 | -0.048<br>[-0.042] | -0.065<br>[-0.054] | -0.063<br>[-0.054] | -0.070<br>[-0.054] | -0.059<br>[-0.049] | -0.059<br>[-0.058] | -0.060<br>[-0.037] | -0.070<br>-0.048   |        |        |
| Euro Yen TIBOR<br>(3 Months)                                                                                | 0.057                       | 0.065  | 0.078<br>[0.056]   | 0.084<br>[0.056]   | 0.077<br>[0.062]   | 0.091<br>[0.075]   | 0.091<br>[0.056]   | 0.050<br>[0.056]   | 0.050<br>[0.063]   | 0.050<br>[0.063]   |        |        |
| Newly Issued Japanese Government Bonds Yields<br>(10 Years)                                                 | 0.065                       | 0.045  | 0.045<br>[0.065]   | 0.030<br>[0.075]   | 0.125<br>[0.060]   | 0.060<br>[0.075]   | 0.110<br>[0.010]   | 0.125<br>[0.060]   | 0.130<br>0.065     | 0.085<br>[0.035]   |        |        |
| Average Contracted Interest Rates<br>on Loans and Discounts(City Banks)<br>(% changes from previous period) | 0.847                       | 0.817  | 0.817<br>(-0.011)  | 0.789<br>(-0.028)  | 0.775<br>(-0.014)  | 0.788<br>(-0.001)  | 0.786<br>(-0.002)  | 0.775<br>(-0.011)  | 0.777<br>(0.002)   |                    |        |        |
| The Nikkei Stock Average<br>(TSE 225 Issues)                                                                | 18,909                      | 21,454 | 21,454<br>[18,909] | 22,305<br>[20,033] | 24,120<br>[20,356] | 22,554<br>[19,925] | 22,865<br>[19,646] | 24,120<br>[20,356] | 21,920<br>[22,012] | 22,351<br>[22,725] |        |        |
| M2(Average)                                                                                                 | (3.6)                       | (3.7)  | (3.2)              | (3.1)              | (2.9)              | (2.9)              | (2.9)              | (2.8)              | (2.7)              | (2.3)              |        |        |
| Broadly-defined Liquidity(Average)                                                                          | (1.9)                       | (3.1)  | (2.6)              | (2.5)              | (2.2)              | (2.2)              | (2.2)              | (2.2)              | (2.1)              | (1.8)              |        |        |
| Principal Figures of Financial Institutions                                                                 |                             |        |                    |                    |                    |                    |                    |                    |                    |                    |        |        |
| Loans and<br>Discount<br>(Average)                                                                          | Banks & Shinkin             |        | (2.4)              | (2.8)              | (2.1)              | (2.0)              | (2.2)              | (2.0)              | (2.2)              | (2.3)              | (2.2)  | (2.1)  |
|                                                                                                             | Banks                       |        | (2.4)              | (2.8)              | (2.1)              | (2.0)              | (2.2)              | (2.0)              | (2.2)              | (2.3)              | (2.2)  | (2.2)  |
|                                                                                                             | City Banks etc.             |        | (1.2)              | (2.0)              | (0.7)              | (0.5)              | (0.7)              | (0.3)              | (0.7)              | (1.1)              | (1.1)  | (0.9)  |
|                                                                                                             | Regional Banks              |        | (3.5)              | (3.6)              | (3.5)              | (4.1)              | (4.5)              | (4.5)              | (4.5)              | (4.3)              | (4.4)  |        |
|                                                                                                             | Regional Banks II           |        | (3.1)              | (3.0)              | (2.8)              | (0.6)              | (-0.5)             | (-0.5)             | (-0.5)             | (-0.8)             | (-0.8) |        |
| Shinkin                                                                                                     |                             | (2.3)  | (2.7)              | (2.5)              | (2.3)              | (2.2)              | (2.2)              | (2.2)              | (2.2)              | (2.1)              | (2.0)  |        |
| Deposits<br>and CDs<br>(Average)                                                                            | Total(3 Business Condition) |        | (3.8)              | (4.2)              | (3.5)              | (3.8)              | (3.7)              | (3.8)              | (3.7)              | (3.6)              | (3.4)  | (3.0)  |
|                                                                                                             | City Banks                  |        | (5.5)              | (5.9)              | (4.9)              | (5.2)              | (5.3)              | (5.4)              | (5.2)              | (5.2)              | (4.8)  | (4.3)  |
|                                                                                                             | Regional Banks              |        | (2.3)              | (2.5)              | (2.2)              | (2.8)              | (3.0)              | (3.0)              | (3.0)              | (2.9)              | (2.8)  | (2.5)  |
|                                                                                                             | Regional Banks II           |        | (2.1)              | (2.1)              | (1.6)              | (-0.2)             | (-1.3)             | (-1.2)             | (-1.3)             | (-1.4)             | (-1.7) | (-1.8) |

(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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