Capital Investment Remains Robust

Japanese companies' capital investment has been progressing robustly. According to the latest *Financial Statements Statistics of Corporations by Industry* released by the Ministry of Finance, capital investment in the April–June quarter was up 12.8% year-on-year, the highest level in 11 years, also marking the seventh successive quarter of positive growth. Among GDP statistics, the quarter-on-quarter percentage change in capital investment in real terms also recorded its seventh successive quarter of positive growth. Meanwhile the assessment regarding capital investment in the Cabinet Office's latest *Monthly Economic Report* was likewise revised upward from "increasing moderately," where it had been since December last year, to "increasing." After slumping badly in the aftermath of the global financial crisis of 2008, Japanese companies' capital investment has slowly regained its vigor in tandem with improvements in the business environment through the correction of the strong yen and the reduction in corporate tax, among other developments, mitigating the previous "sextuple whammy."

The problem is whether or not this investment has been making an adequate contribution to the "virtuous economic cycle" advocated by Abenomics. When capital investment is implemented it leads in most cases to the placement of orders for machinery and equipment of some kind, but it is sure to give rise to different effects on subsequent economic activity, depending upon the purpose of the investment, for example whether it is for increasing production, for replacing outmoded equipment, or for rationalization and labor-saving.

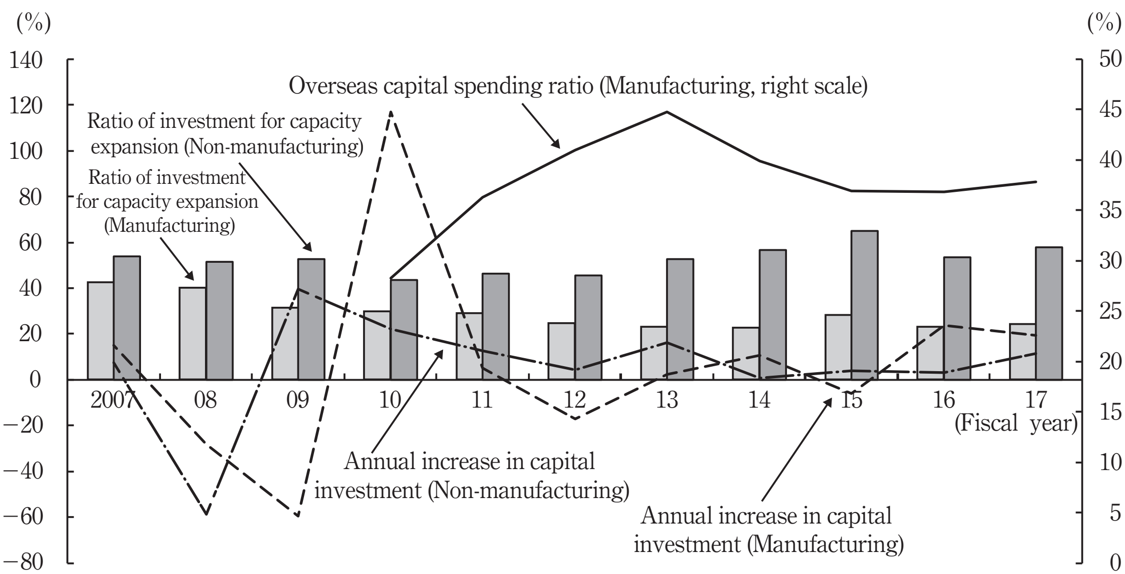
On this subject, the *Survey on Planned Capital Spending* conducted annually by the Development Bank of Japan provides a useful reference. The figure on the next page contains time-series data—separately for manufacturing and non-manufacturing—for the ratio of investment for "capacity expansion," which is considered to be the purpose of Japanese companies' capital investment that has a bigger impact on post-investment factors such as production and employment. This shows that, whereas in recent years the non-manufacturing sector has been assigning between 50% to nearly 60% of capital investment to capacity expansion, in the manufacturing sector the ratio has declined to between 20% and 30%, which is almost the same level as investment for "maintenance and repair."

With regard to capacity expansion in the non-manufacturing sector, prominent examples include the injection of capital by the transportation industry for the speeding-up and enhancement of safety measures in railway services and into logistics facilities, and a host of construction plans in the real estate industry for large complex facilities and international business centers. Although it is true that the huge amounts of all of these investments have been quick to attract attention, from the perspective of having a positive effect on economic activity it is hoped that in the manufacturing sector the ratio of investment for capacity expansion will also be increased somewhat.

The fact is, however, that for some time past the eyes of the manufacturing sector have been directed overseas. The above-mentioned survey by the Development Bank of Japan demonstrates this through the "overseas capital spending ratio," which shows the extent to which the Japanese manufacturing sector's capital investment is directed overseas. From this it can be seen that over the past few years the ratio has fallen to below 40%, probably attributable in part to moves to bring investment back to Japan that began in tandem with the economic recovery. Looking back further, however, reflecting the sequence of events during which investment overseas increased from the time of the global financial crisis of 2008, in fiscal 2013 the ratio rose to 44.8%, meaning almost half of total capital investment was directed overseas (see Figure). What is even more noteworthy is that the motives for investment overseas have differed from those for domestic investment, with investment for capacity expansion accounting for an overwhelmingly high ratio: in fiscal 2017, "capacity expansion" was cited as the number-one purpose of investment by 57% of companies, followed by a mere 16% citing "maintenance and repair" as their primary purpose.

When taking investment decisions it is natural for companies to give importance to investment efficiency. Therefore, even though manufacturers' investments for capacity expansion have flowed overseas, if they have judged that to be the route that offers the prospect of higher returns , then other people should keep their opinions to themselves. However, signs of a recovery of investment for capacity expansion in Japan have been emerging recently, and given its contribution to the virtuous economic cycle it is to be hoped that the flow will be made bigger. Meanwhile, the Abe cabinet has been reshuffled, and discussion on the fiscal 2019 tax reform has begun, among other initiatives. The issue of preferential treatment for companies' capital investment is also likely to be tabled again, and it would be desirable for the agenda to include consideration of measures such as this that would add momentum to the aforesaid moves to bring investment back to Japan.

Capital investment:
Rates of increase, ratios of overseas spending, and investment purposes



Note: Overseas capital spending ratio (Manufacturing)=Consolidated overseas capital investment / (Consolidated domestic capital investment+Consolidated overseas capital investment)×100
Sources: *Financial Statements Statistics of Corporations by Industry* by Ministry of Finance, *Survey on Planned Capital Spending* by Development Bank of Japan