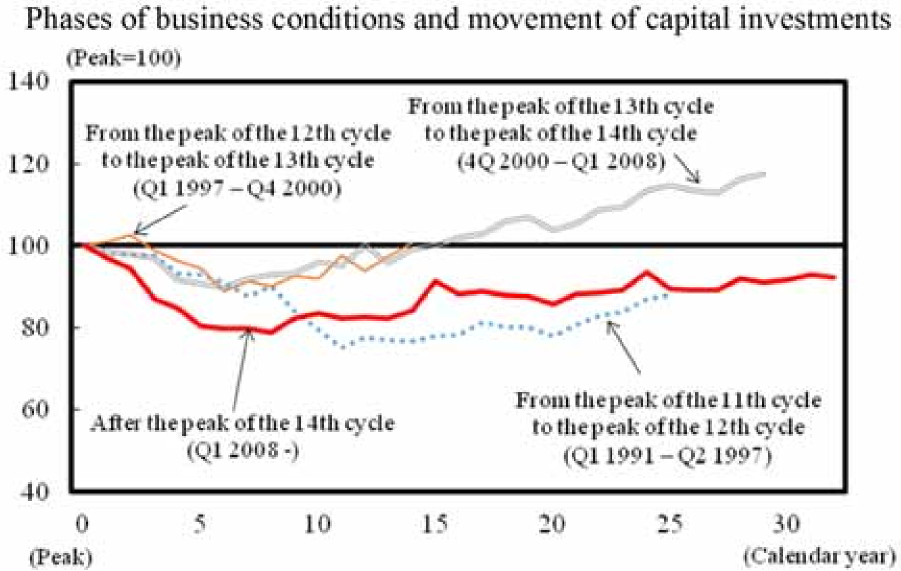
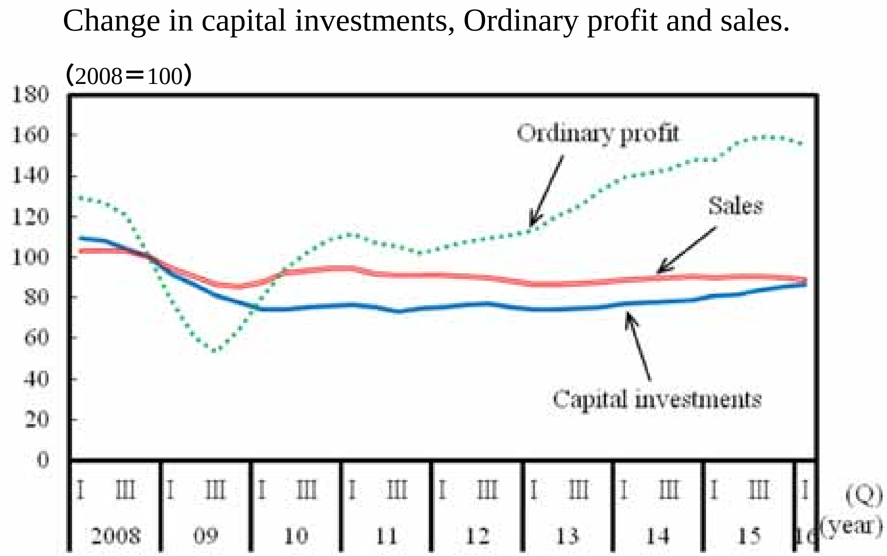
- It is essential that companies find investment opportunities and expand capital investments towards strengthening growth potentials.
- The pace of recovery in capital investments has been slower since the global financial crisis. Although corporate profits are at the highest level, especially since 2013, and a preferable investment environment has been realized, capital investments still lack strength. Growth in domestic demand and growth expectation is sluggish under the low birth rate and longevity, while the competitive environment surrounding companies has changed under globalization.

Figure 17 Phases of business conditions and movement of capital



(Note) Based on the System of National Accounts, Cabinet Office. Capital investment value at the peak of each business cycle is assumed to be 100 and changes up to the next peek of the business cycle are plotted.

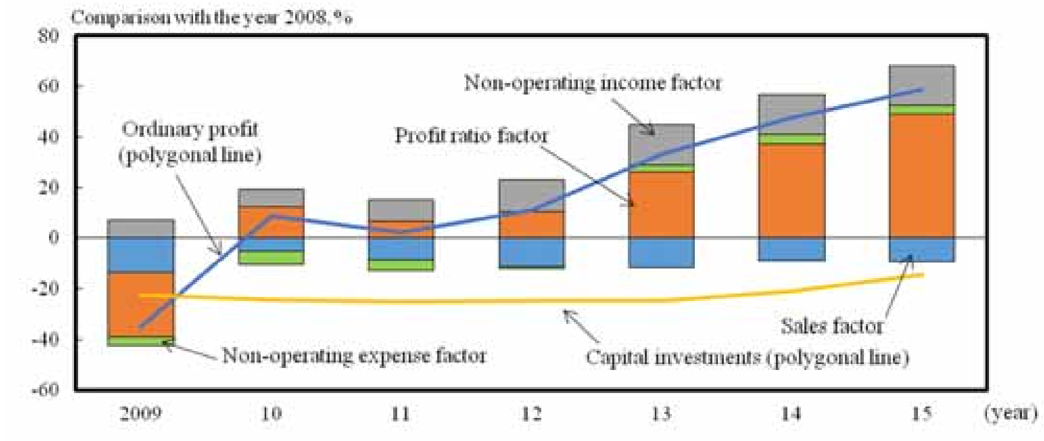
Figure 18 Relationship between corporate profits, sales and capital investments



(Note)1. Complied based on Financial Statements Statistics of Corporations by Industries Quarterly, Ministry of Finance. Values of overall sizes and industries.
Capital investments include software.
2. Changes in 4 four-quarters backward moving average

- Although profits have improved, it is mainly due to an increase in profit by cost reduction, yen depreciation and decrease in interest expenses, and has not necessarily solely reflected an increase in production and sales. Therefore, the improvement of profits did not lead to an increase in capital investments to the extent that had been expected.
- Sluggish growth expectation in companies also restrained capital investments. Weak growth in capital investments may cause a delay in strengthening growth potentials in the future and further sluggish growth expectation that leads to restraining capital investments. Therefore, steady implementation of growth strategy is important.

Figure 19 Movement of ordinary profit and its factors



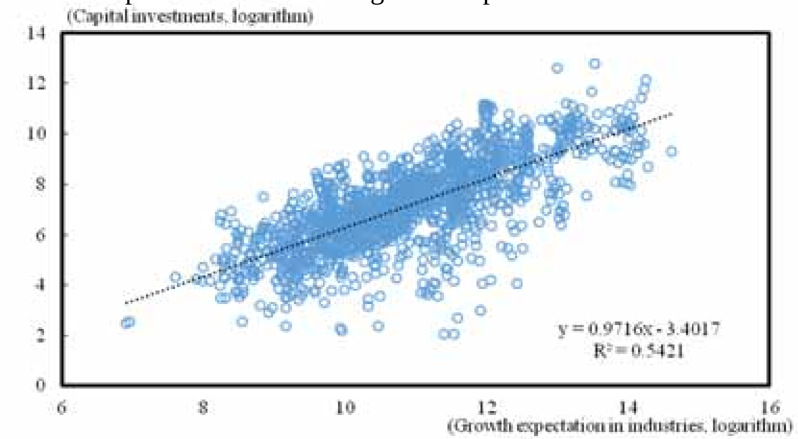
(Note)
1. Based on Financial Statements Statistics of Corporations by Industries Quarterly, Ministry of Finance. Financial services and insurance industries are excluded. Capital investments include software.
2. Factor-breakdown was conducted by breaking down ordinary profit as follows:

$$\text{Ordinary profit} = \underbrace{\text{sales}}_{\text{sales factor}} \times \underbrace{\text{operating profit / sales}}_{\text{profit ratio factor}} + \underbrace{\text{non-operating income}}_{\text{non-operating income factor}} - \underbrace{\text{non-operating expense}}_{\text{non-operating expense factor}}$$

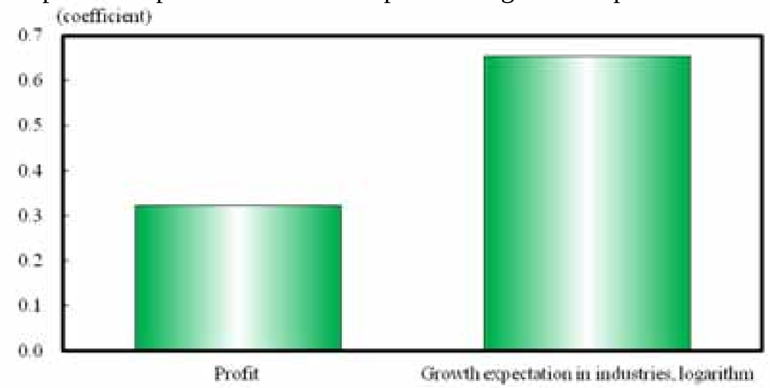
Non-operating income = interest income + other non-operating income e.g. interest income, dividend income and foreign exchange gain against deposit and loan.
Non-operating expense = interest expense + other non-operating expense e.g. interest expenses and foreign exchange loss against bonded debt.

Figure 20 Relationship between capital investments and growth expectation

Capital investments and growth expectation in industries



Impact on capital investments of profit and growth expectation in industries

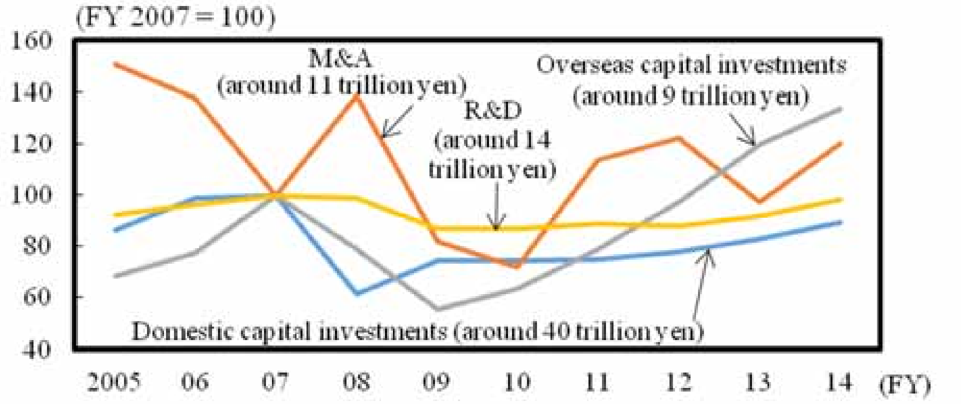


(Note)
1. Based on Questionnaire Concerning Corporation's Activities, the Cabinet Office and Nikkei NEEDS.
2. Growth expectation in industries is calculated by multiplying the results of sales in account settlement data of listed companies (non-consolidated basis) and 3-year forecast of nominal growth rates in industries (individual slip data of Questionnaire Concerning Corporation's Activities).
3. Estimation period: FY 2003 - FY 2014.
4. Estimation formula: log (capital investments) = -2.42＋0.32＊log (Ordinary profit) ＋0.65＊log (growth expectation in industries)
(value t: -9.42) (value t: 11.42) (value t: 18.43)
5. Ordinary profit is on a non-consolidated basis.

- While capital investments lack strength, certain trends in other investments, such as M&A, R&D, and overseas investments, can be seen among companies.
- These investments can lead to development of new needs and markets, as well as high added-value products and services, and are expected to enhance productivity and profitability and lead to development of growth potentials.

Figure 21 Spread of companies' investments

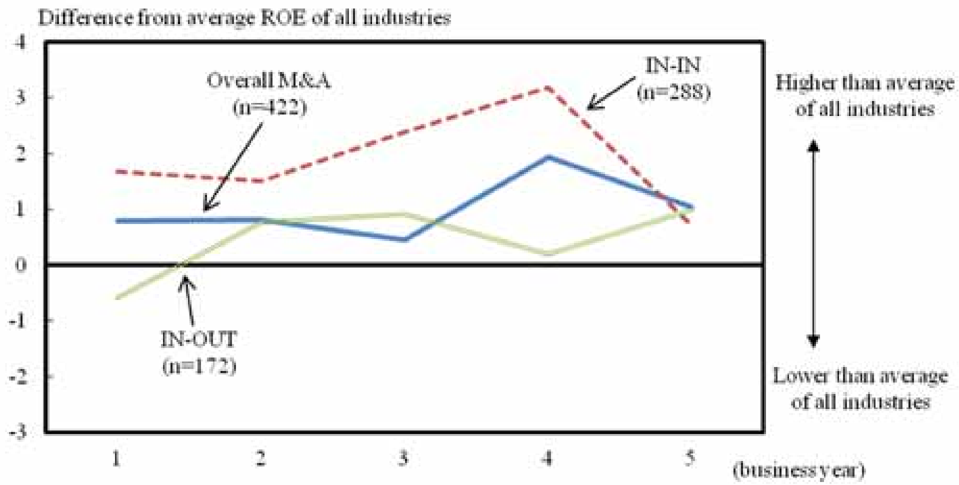
Changes in domestic/overseas capital investments, M&A and R&D



(Note)

1. Based on Financial Statements Statistics of Corporations by Industry, Annual Feature Edition of Financial Statements Statistics of Corporations by Industry, Ministry of Finance; Survey of Overseas Business Activities; Ministry of Economy, Trade and Industry; Survey on Science and Technology Research, Ministry of Public Management; and RECOF M&A Database, RECOF Corporation.
2. M&A is total amount of IN-IN and IN-OUT.
3. Within the parenthesis is an actual value of FY 2014.

Figure 22 Profitability of companies that carried out M&A

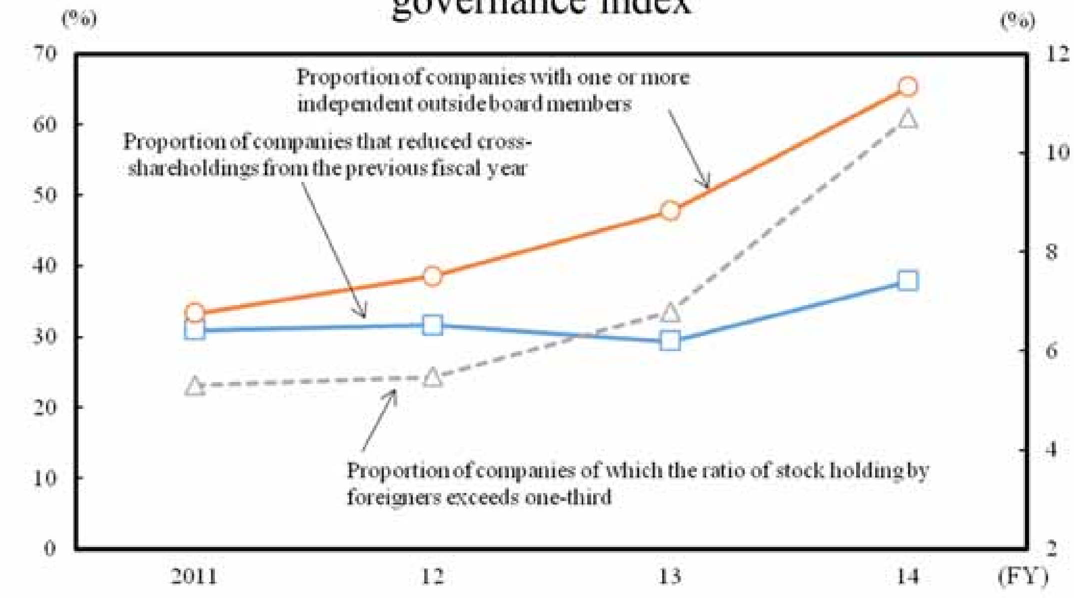


(Note)

1. Based on Nikkei NEEDS and RECOF M&A Database, RECOF Corporation.
2. Target companies are listed on the major section of Tokyo Stock Exchange, on a consolidated basis.
3. The difference from the average ROE of all industries after M&A announcement is calculated for companies that carried out M&A (IN-IN and IN-OUT) of over 10 billion JPY from 1999 to 2009 (422 companies; if a company carries out M&A over multiple years, each of them is counted). Changes on average of each period after the official announcement.
4. Difference from the average ROE of all industries is calculated as (ROE of target company) - (average ROE of the industry that the company belongs to).　Industrial classification is based on the name of industry of Tokyo Stock Exchange.
5. ROE = current net income before tax / (net assets - share options)

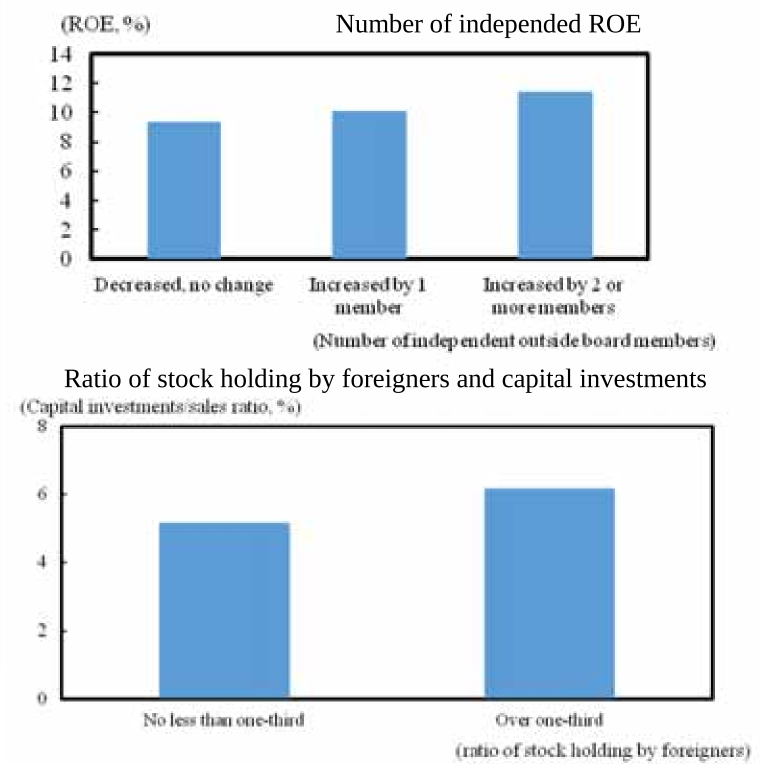
- While companies face the state of undergoing such changes as the low birth rate and longevity, it is important to enhance and instill a scheme for supporting more active management decisions to make the environment change a great opportunity for company growth.
- Companies that enhance their effort toward corporate governance may be able to develop their profitability and contribute to strengthening the growth potentials of the economy through more active investment behavior.

Figure 23 Movement of corporate governance index



(Note)
1. Based on Nikkei NEEDS and Bloomberg.
2. Listed companies on the major section of Tokyo Stock Exchange (1,223 companies; financial services and insurance industries are excluded) that can obtain the consolidated accounts data for FY 2011 and later and have no missing value.
3. Independent outside board members are outside board members who do not have any conflicts of interest with general shareholders. The ratio of stock holding by foreigners is the ratio of shareholding of foreign investors to issued shares.
Cross-shareholdings are so called crossholding stocks aimed at strengthening sales relationships, not net investment.

Figure 24 Relationship between ROE, capital investment and corporate governance index



(Note)
1. Compiled based on Nikkei NEEDS and Bloomberg.
2. Target companies are listed companies on the major section of Tokyo Stock Exchange (1,223 companies; financial services and insurance industries are excluded) that can obtain the consolidated accounts data for FY 2011 and later and have no missing values.
3. Number of independent outside board members consists of changes from FY 2011 to FY 2014.
ROE, Ratio of stock holding by foreigners and capital investments/sales ratio are averages between FY 2011 and FY 2014.
4. Regarding ROE, current net income before tax is used to remove the impact on profit of changes in effective corporate tax rate. Calculation formula is shown as follows:
ROE = current net income before tax / owned capital.
5. Capital investments/sales ratio = capital investments/sales.