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In Abe We Trust as Japan Inc. Buybacks Climb to Eight-Year High
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July 16 (Bloomberg) -- Eight months into the biggest equity rally in three decades, Japanese executives are gaining faith in the nation's recovery as they reward shareholders with stock buybacks and pledge to increase capital spending.

Topix companies bought 1.78 trillion yen ($17.8 billion) of their own shares in the half ended June 30, the most since 2005, according to data compiled by Bloomberg. With companies from Orix Corp. to Toyota Motor Corp. to Nissin Foods Holdings Ltd.
holding a record 115 trillion yen, plans for capital projects are rising at the fastest rate in seven years.

While investors realized last November that Japan's economy was starting to rebound, sending the Topix up 66 percent, corporate leaders have been slower to respond to Prime Minister Shinzo Abe's spending and reform policies. It was only in June that optimists among large manufacturers outnumbered pessimists for the first time in two years, according to Japan's quarterly Tankan index. Bears say companies are only dumping cash because inflationary policies will erode their savings.

"Abe is helping to change the trend of how companies spend their money," Taku Arai, Japanese equities investment manager at Schroder Investment Management (Japan) Ltd., whose British parent overseas 236.5 billion pounds ($357.2 billion), said in an interview in Tokyo. "Japan's managerial ranks are starting to think more about shareholder returns."

Japanese stocks advanced last week, with the Topix index of 1,711 companies adding 1.1 percent to 1,201.99, as exporters rose amid optimism a weakening yen will boost overseas earnings.
Even after sliding 5.8 percent from its 2013 peak on May 22, the measure is still the best-performing major equity benchmark in the world, having risen 40 percent this year.

Historic Rebound

The Topix has gained more than 500 points since closing at its lowest level in almost 29 years last June, boosted by Abe's pledge to double the money supply and end two decades of deflation. About 196 trillion yen was added to share values as analysts pushed forecasts for 2013 earnings growth to 57 percent and the Bank of Japan said the economy is starting to recover.

"Abe and his reflationary policies are working to get companies moving," said Masaru Hamasaki, a senior strategist at Tokyo-based Sumitomo Mitsui Asset Management Co., which oversees about $111 billion. "It's been a while since the policies started, and while there are many complaints about it, it is starting to work."

Topix companies bought back 1.78 trillion yen worth of shares in the six months ended June 30, or 0.66 percent of the gauge's market value, according to data compiled by Bloomberg.
That's the highest level since 2005, when companies spent 3.06 trillion yen on repurchases.

Buyback Estimates

Share repurchases in Japan may double to 3.8 trillion yen in year ending March 2014, funded by higher earnings and cash balances, Goldman Sachs Group Inc. said in an April 24 report.
Shareholder demands for the return of cash will rise in coming quarters as inflation picks up, Goldman Sachs analysts Hiromi Suzuki, Kathy Matsui, Kazunori Tatebe and Tsumugi Akiba wrote.

Fujikura Ltd., the cable manufacturer based in Tokyo, rallied the most in more than a year on Feb. 27, when it announced a plan to buy back more than 3 billion yen. It completed the repurchase in April. Nidec Corp., the world's biggest maker of hard-disk drive motors, has advanced 34 percent since saying in January it will spend up to 20 billion yen on its stock.

Returning Cash

Dividends will rise 8.7 percent this year, according to estimates based on criteria such as options prices, comparisons with competitors and management statements compiled by Bloomberg. Payout ratios, or the cost of dividends relative to earnings, for the Topix are 39.4 percent, higher than the Hang Seng Index's 34.5 percent and S&P 500's 36.3 percent, according to data compiled by Bloomberg.

At 1.66 percent, the Topix's dividend yield, or payout as a percentage of share price, is more than twice the return offered by Japan's 10-year government bond. It compares with the 2.06 percent paid by the S&P 500, which is about 80 percent of the yield on the U.S. government's 10-year notes.

Japan Tobacco Inc., Asia's biggest listed cigarette maker, raised its annual dividend by 35 percent to 92 yen this year. It will rise another 8.7 percent by 2016, according to Bloomberg forecasts. Astella Pharma Inc., based in Tokyo, will boost its dividend every year through 2017 to 150 yen, according to company and Bloomberg forecasts.

"The windfalls of Abenomics -- more cash flow from a weaker currency and better growth -- are being reinvested for future growth and to reward current shareholders," Jesper Koll, head of Japan strategy at JPMorgan Chase & Co. in Tokyo, said in an interview. "The change in mindset is absolutely enormous."

Spending Plans

After cutting capital spending for three years starting in 2008, CEOs plan to boost it again. Japan's largest companies will increase outlays for plant and equipment by 5.5 percent in 2013, according to the Tankan quarterly survey released by the central bank on July 1. The change from the first quarter, when executives saw investments reduced by 2 percent, was the biggest swing to a positive expectation since 2006, data compiled by Bloomberg show.

Capital expenditures expanded by 19 percent last year among Topix constituents, data from earnings statements compiled by Bloomberg show. Machine orders surged 16.5 percent in May from a year earlier, the biggest jump since 2011. Economists had estimated a 3.3 percent increase.

Quarterly Retreat

In the first full quarter of Abe's tenure, capital spending excluding software fell 5.2 percent from a year earlier, according to a report from the Ministry of Finance released June 3. Spending by Japan's biggest companies dropped 4.9 percent in January-March, the biggest decline since the quarter after the March 2011 earthquake.

That may signal that while corporations are concerned an exit from deflation will erode the value of their cash, they still don't want to spend to improve or expand their businesses.

Consumer goods makers from brewer Kirin Holdings Co. to Ajinomoto Co., a food and food-additives producer, are skeptical Abe will be able to reignite a domestic economy where more than
25 percent of the population is over 65 years old.

About a third of Ajinomoto's capital expenditure in the two years to March 31 was in its overseas food products segment, more than twice what it spent domestically. The company is focusing its efforts on Southeast Asia, Masatoshi Ito, its president, said in June.

'Hasn't Recovered'

"Household consumption hasn't recovered yet," Kirin President Senji Miyake said June 13 on the sidelines of a consumer goods executives forum in Tokyo. "Overseas business, rather than domestic, will definitely be our growth trigger."

Kirin spent $12 billion over the past five years on acquisitions abroad, versus less than 500 million yen at home, according to data on announced deals compiled by Bloomberg.

"Capital expenditure is increasing but if you look at their cash flow, their cash flow is obviously much larger,"
said Ayako Sera, a strategist at Sumitomo Mitsui Trust Bank Ltd., which manages the equivalent of $163 billion in corporate pensions. "There's no point keeping cash in inflation so they are looking to reduce it. But with Japan's long-term demographic problems, even with Abenomics, companies see real growth as difficult. That is why they are leaning toward share buybacks."

'Very Difficult'

The president of Japan's Government Pension Investment Fund, Takahiro Mitani, said the central bank's goal of reaching

2 percent inflation in two years is “very difficult.” It rarely got that high in past expansions, he said in a Tokyo interview June 21.

In the last five years of the 1980s, when Japan’s gross domestic product climbed from about $1.3 trillion to $3 trillion and the Nikkei 225 Stock Average peaked at almost 39,000, monthly readings for inflation averaged 1.2 percent, according to data compiled by Bloomberg. In the decade to May 2013, the average has been minus 0.1 percent, the data show, while the Nikkei 225 is still down about 63 percent from its 1989 high.

Abe’s forecast victory in an upper-house election on July 21 may strengthen his hand to push through deregulation to sustain a recovery that has so far been driven by monetary and fiscal stimulus.

The government is considering various tax reforms to promote capital investment including allowing companies to claim depreciation in a lump-sum, Economy Minister Akira Amari said July 1. Further tax incentives for capital expenditure may also be considered, Finance Minister Taro Aso said June 28.

Shopping Malls

Aeon Mall Co., an operator of shopping centers in Japan, plans to almost triple capital expenditure this fiscal year to 150 billion yen and open at least 20 new malls in Japan in the next two years, according to a July 5 company conference call.

Seven & I Holdings Co., the operator of 7-Eleven convenience stores, may more than double North American outlets, Chairman Toshifumi Suzuki said in a May 30 interview. Capital spending jumped 61 percent from a year ago in the three months ending May 31, Bloomberg data show.

Financial services company Orix reported capital expenditures increased 22 percent in the 12 months ended March 31, as it develops solar-power plants in Japan. Only Nippon Telegraph and Toyota spent more among Topix companies, according to data compiled by Bloomberg.

Nissin Foods, whose founder Momofuku Ando invented the instant noodle, aims to boost return on equity to 7.2 percent by fiscal 2016 from 6.4 percent in 2013 and spend as much as 50 billion yen on capital expenditure during the period, according to a mid-term plan announced on April 30.

“Japanese companies are both starting to invest in themselves again as well as being more shareholder friendly and returning more capital to shareholders,” Chris Konstantinos, director of international portfolio management at Riverfront Investment Group LLC in Richmond, Virginia, said in a July 10 phone interview. His firm, which oversees $3.8 billion, has been buying Japanese stocks this year. “It’s illustrative of a return of business confidence.”

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